ERISA Fiduciaries Must Continuously Monitor 401(k) Investment Choices

Insights
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Introduction

The U.S. Supreme Court has held unanimously that a plan fiduciary has a continuing duty to monitor investments offered under a 401(k) plan, a duty that is separate and apart from the duty to exercise prudence in selecting investments in the first place. The Court overturned a decision by the U.S. Court of Appeals for the 9^{th} Circuit, which held that a claim for breach of fiduciary duty with respect to a fund selection was time barred unless made within six years of the date the fund was originally selected for inclusion in the plan. *Tibble v. Edison International*

The decision confirms that employers have a continuing duty to monitor the investments offered through their 401(k) plans and the fees attached to them. The Supreme Court declined to comment on what type of review a fiduciary must undertake to satisfy ERISA's "prudent man" requirement, remanding the case to the 9^{th} Circuit for further proceeding consistent with the Court's analysis. This decision opens the door for additional litigation against plan sponsors who have failed to monitor investments on an ongoing basis.

Background

Edison International owns subsidiaries that generate and distribute electric power, and invest in energy services and technologies. Beginning in 1999, the company offered some retail-class mutual funds as part of its 401(k) plan, even though otherwise identical institutional-class funds that charged lower fees could have been offered. In 2007, Glenn Tibble and other employees sued the company under ERISA, claiming the company's failure to offer identical funds with lower fees was a breach of its duty to manage the plan prudently for the exclusive benefit of its participants. The employees argued that by offering the higher cost funds, the company committed a "continuing violation" of ERISA.

In affirming a district court ruling, the 9^{th} Circuit found that ERISA's statute of limitation bars claims filed more than six years after the date a fund is first offered under a plan and that there is no "continuing violation" theory under ERISA. The court of appeals held that the selection of an investment for inclusion started the six-year period and "only a significant change in circumstances" could give rise to a new breach of fiduciary duty.

Legal Analysis

In this case, the Supreme Court held that ERISA's fiduciary duty is derived from the common law of trusts, which creates a continuing duty – separate and apart from the duty to exercise prudence in selecting investments in the first place – to monitor funds and remove imprudent investments. ERISA's six-year statute of limitation had become a roadblock for participants challenging investment decisions, because many funds remain in a retirement plan's fund line-up for years after their initial selection. Three federal circuit courts had held that plan fiduciaries are not liable for investments selected before this six-year window.

The disagreement between the parties focused on the scope of the duty to monitor. But the Court declined to determine the scope required in these circumstances, recognizing only that under trust law, "a fiduciary is required to conduct a regular review of its investment with the nature and timing of the review contingent on the circumstances." The case is remanded back to the 9th Circuit to determine if the company breached its fiduciary duty given the particular facts of the case.

Significance For Employers

For employers who maintain 401(k) plans, this decision confirms that there is a duty to monitor the investment funds offered under a 401(k) plan and the fees associated with those funds. If not previously undertaken, employers should review their practices with respect to selecting, monitoring, and removing funds offered under 401(k) plans.

It's important to ensure that the funds being offered to participants have been reviewed for the level of fees charged to the fund, the performance of the funds against their appropriate benchmarks, and the fiduciary's adherence to the plan's investment policy statement. With tougher Labor Department scrutiny on fees paid by 401(k) plan participants, it is more important than ever that employers maintain an active and sophisticated benefits committee to oversee the selection and monitoring of investments for their plans.

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