Employee Relations LAW JOURNAL

Electronically reprinted from Spring 2016

Employee Benefits

The Trouble Caused by *Tibble*: Supreme Court Case Requires Enhanced Monitoring of Plan Investments

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In Tibble et al. v. Edison International et al., *the U.S. Supreme Court held that a plan fiduciary has a continuing duty to monitor plan investments and, therefore, plan participants have six years to bring a lawsuit from the date of the last breach based on ERISA's statute of limitation. This column discusses the ruling and its implications.*

The United States Supreme Court held in *Tibble et al. v. Edison International et al.*[1] that a plan fiduciary has a continuing duty to monitor plan investments, and, therefore, plan participants have six years to bring a lawsuit from the date of the last breach based on ERISA's statute of limitation. The trouble with this ruling is that if the duty to monitor is continuously breached because a plan fiduciary fails to monitor prudently, the statute of limitations will never run and participants will never lose their ability to bring a lawsuit. The impact of *Tibble* is significant and should cause fiduciaries to immediately enhance their monitoring techniques and engage in best practices to avoid potential lawsuits.

Tibble v. Edison

In 2007, several participants in the 401(k) savings plan sponsored by Edison International commenced a legal action against the plan's fiduciaries seeking equitable relief and damages for losses. The participants alleged that the defendants had breached their fiduciary duties by adding three mutual funds to the Plan in 1999 and three other mutual funds to the Plan in 2002. The gravamen of the complaint was that defendants breached their duty of prudence by offering six higher priced mutual funds when virtually identical lower priced mutual funds were available at exactly the same time.

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The Employee Retirement Income Security Act of 1974, as amended (ERISA), contains a "statute of limitations" that provides:

> No action may be commenced under this subchapter with respect to a fiduciary's breach of any responsibility, duty, or obligation under this part, or with respect to a violation of this part, after the earlier of—
>
> (1) six years after
>
> (A) the date of the last action which constituted a part of the breach or violation, or
>
> (B) in the case of an omission the latest date on which the fiduciary could have cured the breach or violation, or
>
> (2) three years after the earliest date on which the plaintiff had actual knowledge of the breach or violation;
>
> except that in the case of fraud or concealment, such action may be commenced not later than six years after the date of discovery of such breach or violation.[2]

In other words, in relevant part, ERISA provides that a lawsuit claiming a breach of fiduciary duty is timely if it is filed no more than six years after the date of the last action that constituted a part of the breach or violation.

The district court held that pursuant to ERISA's statute of limitations, the claims that defendants acted imprudently with regard to the three mutual funds that were added in 1999 were untimely because the mutual funds were added more than six years before the complaint was filed in 2007.[3] The case was appealed to the Ninth Circuit that ultimately agreed with the district court.[4] The Ninth Circuit indicated that the plaintiffs' claims would have been timely if they could establish a change in circumstances that might trigger an obligation to review and change the mutual fund investments within the six-year statute of limitations. However, as plaintiffs did not establish a "change in circumstances," the Ninth Circuit upheld the district court's decision that the plaintiffs' claim was time-barred by the statute of limitations.

The Supreme Court vacated and remanded the Ninth Circuit's decision, finding that it failed to consider the "nature of the fiduciary duty" that was being breached. The Court further stated that the Ninth Circuit did not properly address trust law, which includes a duty to monitor the investments of a trust and remove imprudent investments. Noting that ERISA is "derived from the common law of trusts," the Court found that fiduciaries of plans governed by ERISA also have a continuing duty to monitor the prudence of plan investments. The Court further explained that the duty to monitor is separate and distinct from a "trustee's duty to exercise prudence in selecting investments at the outset." The Court held, therefore, that a participant in an ERISA-covered plan may properly claim that plan fiduciaries breached their duties by failing to adequately monitor plan investments and, accordingly, such a claim would not be time-barred by ERISA as long as the alleged monitoring failure occurred within six years of the commencement of the lawsuit.

The Court held, therefore, that a participant in an ERISA-covered plan may properly claim that plan fiduciaries breached their duties by failing to adequately monitor plan investments.

The Court did not address the parameters or details of a fiduciary's duty to monitor plan investments. The Court did, however, remand the case to the Ninth Circuit to flesh out the details of the duty to monitor and to reconsider the participants' claims that plan fiduciaries breached this duty within the relevant six-year period. It is hoped that the Ninth Circuit will address certain important issues on remand. Among them are (i) how frequently a fiduciary must review the prudence of an investment fund, and (ii) whether a fiduciary is required to apply the same level of scrutiny when monitoring an investment as when initially selecting the investment for inclusion in the plan.

Impact of Tibble

The Supreme Court's decision in *Tibble* has removed a major impediment that blocked plan participants from filing a lawsuit relating to an improperly monitored plan investment where the initial decision to add that investment occurred beyond ERISA's six-year statute of limitations. In other words, although the selection of an investment fund for an ERISA plan would generally be insulated from claims of fiduciary breach after six years, the failure to properly monitor an investment fund once selected would still be exposed to claims for six years from the date of such monitoring failure. Furthermore, if there is a continuing monitoring failure, participants would never lose their ability to sue. Because an increase in failure-to-monitor claims is expected, plan fiduciaries should seek immediately to enhance their monitoring techniques and establish best practices for monitoring their plan investments.

Monitoring Plan Investments

In the *Tibble* case, the Supreme Court commented that a fiduciary must "systematic[ally] conside[r] all the investments of the trust at regular intervals." Thus, as an initial matter, Plan fiduciaries will want to make sure that their approach to monitoring plan investments is "systematic" and "regular." A systematic and regular approach to monitoring would call for the adoption of procedures for the periodic monitoring of plan investments, closely adhering to those procedures, and then documenting the implementation of those procedures. Set forth below are recommendations for the implementation and content of such procedures.

Retain ERISA Counsel

The first thing a committee should do to ensure compliance with its duty to monitor, as well as its other fiduciary duties, is to hire an ERISA counsel who has first-rate expertise in fiduciary matters. The committee's ERISA counsel should quarterback the committee's compliance endeavors, attend each committee meeting, advise on fiduciary issues, and draft minutes. There are many reasons why a committee should have ERISA counsel. First, ERISA's central fiduciary duty is the duty to act prudently, that is, "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims." Thus, the duty of prudence requires committees to act like prudent *experts*. Because most committees are not experts in ERISA fiduciary law, they need to hire expert ERISA counsel. Hiring solely an investment advisor is not enough. Investment advisors are expert in evaluating plan investments and, while they may have some legal knowledge, they are not lawyers and, thus, are not experts in the legal field.

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Second, it is inarguable that the best person to draft minutes of committee meetings is ERISA counsel. The person who drafts the minutes should have a thorough and up-to-date understanding of what plaintiff lawyers are alleging and how judges analyze fiduciary issues. The minutes need to be drafted to nullify all potential avenues of attack but cannot be so specific that they could serve as a potential source of liability. Third, the *Tibble* case illustrates the need for a committee to have ERISA counsel. The case was all about an investment advisor and a committee adding investment funds that were too expensive. Had ERISA counsel been in the room at the time of the decision, we are confident that he or she would have asked whether lower priced share classes were available. Finally, the environment in which plan fiduciaries operate is both adversarial and complex, and fiduciaries are personally liable for damages caused by fiduciary breaches. Thus, from a practical perspective, it is simply a matter of common sense to hire ERISA counsel to advise and protect the plan committee.

Retain an Investment Advisor

Once an ERISA counsel is retained, they will be able to advise on prudent procedures for selecting an investment advisor. An investment advisor is essential for assisting the committee with, among many other things, the selection and monitoring of plan investments. A prudent process for hiring an investment advisor would include evaluating several investment advisors on the basis of certain characteristics, including the following:

- Business structure of the candidate;
- Size of staff;
- Identification of individual who will handle the plan's account;
- Education;
- Professional certifications;
- Relevant training;
- Relevant experience;
- Fees and expenses;
- Performance record;
- References;
- Professional registrations, if applicable;
- Technical capabilities;
- Financial condition and capitalization;

- Insurance/bonding;
- Enforcement actions/litigation; and
- Termination by other clients and the reasons.[5]

Establish Systematic Monitoring Procedures

To comply with their fiduciaries duties, plan fiduciaries must have a prudent process for monitoring plan investments. When evaluating investment decisions made by plan fiduciaries, courts will only look at the process, and not the results of the decision, to determine whether fiduciary duties have been breached. Courts do not expect fiduciaries to have a crystal ball or be able to see into the future. Thus, while decisions made by plan fiduciaries should be well-reasoned, the results of the decisions do not have to be "correct." However, the process for monitoring plan investments must be prudent and diligently followed. As long as fiduciaries have engaged in a prudent process with respect to monitoring investments, they ought to have a strong defense to any lawsuit.

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The hallmark of a prudent, systematic monitoring process is to have a written "to do" list of items that need to be accomplished each time plan fiduciaries meet to evaluate their plan's investments. Best practice is for plan fiduciaries to meet quarterly to monitor their plan's investments. Each time the fiduciaries meet, it is recommended that they address the items listed below (to the extent applicable). These items should be included in the plan's investment policy statement or in a separate document (such as the minutes) that is adopted and ratified by the committee.

- Review the quarterly report prepared by the investment advisor to evaluate the performance of investment funds over relevant time periods, including performance over quarter, year-to-date, and three-, five-, and 10-year periods. As illustrated by *Tibble*, the systematic review should apply to all plan investment funds, regardless of whether they were added recently or decades ago. The quarterly report prepared by the investment advisor should include a quantitative and qualitative analysis of the investment funds. For example, the report should show the performance of the investment funds relative to benchmark and peer group, but also provide information as to whether there have been any management changes within the fund.

- Review whether institutional share classes are available for the plan's investment funds. Given the Supreme Court's decision in *Tibble,* it is imperative to ask this question each quarter. It should be noted that if an institutional share class is available, but the plan is ineligible for it because the fails to have a minimum level of assets invested in the fund, fiduciary duties would require the plan committee to ask the fund manager to make an exception on behalf of the plan. Moreover just because there is lower fee share class available does not mean that fiduciaries should automatically switch to that share class. Other factors, including revenue sharing that the plan investments might generate, should also be considered. If higher fee share classes are needed to support revenue sharing, it should not be considered an automatic breach of fiduciary duty to fail to move from such share class to the lower fee share class. However, in order to protect itself, the committee must go through a prudent process for determining that revenue sharing is the prudent method for compensating the plan's third party administrator. This process must be carefully documented in the committee's minutes.

- Evaluate the investment funds to determine if they represent all the desired asset classes and if there has been "style drift" since the funds were last evaluated.

- Review recent changes in the law with ERISA counsel, including court cases and government pronouncements. For example, the Securities and Exchange Commission recently changed the rules for money market funds.[6] Under the new rules, institutional money markets will have a floating NAV. In addition, institutional and retail money market funds may implement liquidation fees and redemption gates in times of high financial stress. Plan fiduciaries will want to evaluate their plan's money market fund and determine whether switching to a money market fund that is unaffected by the rule changes (e.g., a government money market fund) is warranted.

- More and more money is flowing into target date funds as a result of target date funds being the qualified default investment alternative for most plans. Accordingly, plan committees should take care to evaluate their target date funds on a quarterly basis. The fee structure of the target date fund family (as well as the underlying investment funds) should be confirmed and the performance of each target date fund versus appropriate indexes should be noted. Also, any change in plan demographics that might affect the appropriateness of the target date funds for the plan should be noted and evaluated.

Plan committees should take care to evaluate their target date funds on a quarterly basis.

- Review all fees that are directly or indirectly paid by the plan and make sure the fees are reasonable. This exercise may be performed annually or semi-annually instead of quarterly. Such fees include fund expense ratios, service provider fees, fees directly charged to participant accounts, and revenue sharing received by the plan's third party administrator.

Conclusion

In *Tibble*, the Supreme Court found that fiduciaries of plans governed by ERISA have a continuing duty to monitor the prudence of plan investments. If there is a breach of this duty, plan participants may wage a potentially successful lawsuit within six years of the breach. However, if the breach is continuing, plan participants never will lose their right to sue on that breach. Thus, plan fiduciaries should immediately enhance their monitoring techniques to prevent lawsuits based on past or future breaches.

Notes

1. No. 13-550, 575 U.S. ___ (2015).
2. ERISA § 413.
3. 639 F.Supp.2d 1074 (C.D. Ca., 2009).
4. 711 F.3d 1061 (9th Cir. 2013), *as amended by* 729 F.3d 1110 (9th Cir. 2013).
5. United States Department of Labor, Report of the Working Group on Guidance and Selecting and Monitoring Service Providers, November 13, 1996.
6. Securities and Exchange Commission, Release No. 33-9616, July 23, 2014.