# Navigating Fee Benchmarking in a Litigious Era

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## The Importance of Fiduciary Duties

In today's litigious environment, sponsors of 401(k) and 403(b) plans face increased scrutiny regarding the fees associated with their retirement plans. Ensuring fees are reasonable is not only a fiduciary duty under the Employee Retirement Income Security Act (ERISA), but also a safeguard against potential lawsuits alleging excessive fees. Recent legal actions highlight the importance of diligent fee benchmarking and overall plan management.

Plan Sponsors are tasked with adhering to five fiduciary duties under ERISA, but notably a committee's process and documentation is more critical than the actual outcome of fiduciary decisions. The key to managing ERISA fiduciary duties is to establish and follow prudent plan governance practices. This fiduciary trail underscores the way recommendations, managers and the reasonableness of decisions made by the committee are evaluated. Implementing these practices and procedures helps ensure proper handling of plan assets and prudent decision making, demonstrating that fiduciary obligations are met. An advisor can also be a valuable resource by providing fiduciary education, helping Plan Sponsors understand their responsibilities and developing a fiduciary calendar.

The five key fiduciary duties under ERISA are:

- Duty of Loyalty: Fiduciaries must act solely in the interest of plan participants and beneficiaries, avoiding conflicts of interest and ensuring that their actions benefit the plan.
- Duty of Prudence: Fiduciaries are required to act with care, skill, prudence and diligence. This includes making informed decisions and seeking expert advice when necessary.
- Duty to Diversify: Fiduciaries must diversify plan investments to allow participants to manage risks.
- Duty to Follow Plan Documents: Fiduciaries must operate the plan in accordance with the governing documents and instruments, as long as they comply with ERISA. This includes adhering to the plan's terms and ensuring that all actions are consistent with the plan's provisions.

- Duty to Avoid Prohibited Transactions: Fiduciaries must avoid engaging in transactions that are expressly prohibited by ERISA, such as self-dealing or transactions that benefit parties related to the fiduciary. This duty helps prevent misuse of plan assets and helps ensures ethical management.

## Key Documents for Fiduciary Oversight

Operational documents are critical to ensuring the fiduciary oversight process is documented in a structured way. More Plan Sponsors today keep a collection of key documents to help ensure continuity of the committee and understanding of fiduciary responsibilities. These key documents for fiduciary oversight include:

- Committee Charter: Outlines the role of the committee and operational structure.
- Investment Policy Statement: Outlines a plan's decision-making process for investment management.
- Corporate Bylaws: Establishes authorized signatories on behalf of the corporation.
- Investment Committee Minutes: Documents actions and decisions made by the committee.

## Litigation Trends and Lessons Learned

The litigious environment for ERISA fiduciary breaches has become increasingly active, as evidenced by the numerous cases involving Plan Sponsors like Edison International[1], Juniper Networks[2], Estee Lauder[3] and others. These cases highlight common allegations such as excessive fees, imprudent investment options and failure to monitor plan investments. Courts have shown a willingness to allow these claims to proceed, emphasizing the importance of fiduciary plan management and the need for Plan Sponsors to act in the best interest of participants. Settlements in many cases, such as those involving American Century Services[4] and Banner Health[5], emphasize the financial risks associated with litigation.

Recent cases like Qualcomm, Inc.[6] and BAE Systems[7] have shifted the focus from investment management and recordkeeping fees to prohibited transaction claims, alleging improper use of forfeiture assets. The IRS proposed regulations for plans subject to vesting, identifying proper use of forfeiture accounts. Forfeitures cannot be returned to the Plan Sponsor. They can be used for one of the following plan purposes:

- Reduce employer contributions
- Pay reasonable plan expenses
- Allocate as an additional employer contribution

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[1] Tibble v. Edison Int'l, 575 U.S. 523 | Casetext Search + Citator
[2] Reichert v. Juniper Networks, Inc., 21-cv-06213-JD | Casetext Search + Citator
[3] Berman v. Estee Lauder Inc. et al (4:19-cv-06489), California Northern District Court
[4] Wildman v. American Century Services, LLC, et al. - Analysis Group
[5] Banner Health ERISA Litigation Reaches Mixed Ruling | PLANSPONSOR
[6] Perez-Cruet v. Qualcomm Incorporated et al 3:2023cv01890 | U.S. District Court for the Southern District of California | Justia
[7] Naylor v. BAE Systems, Inc. 1:2024cv00536 | U.S. District Court for the Eastern District of Virginia | Justia

Although forfeitures could be used for one of the above-mentioned purposes, it is important for Plan Sponsors to use the forfeitures in a manner consistent with the plan document. Most plan documents adhere to the IRS's mandatory deadline for forfeiture amounts to be used by the end of the plan year following the year the forfeiture occurred. It is important for Plan Sponsors to review their plan documents to determine the vesting schedule and how the forfeitures may be applied. Also, Plan Sponsors should have a process of monitoring the forfeitures balance on at least an annual basis.

Additionally, Plan Sponsors should focus their attention on regularly reviewing and monitoring investment options and to help ensure fees are reasonable. By maintaining thorough documentation and adhering to ERISA requirements, Plan Sponsors can better defend against potential litigation and fulfill their fiduciary responsibilities. Incorporating fee benchmarking into the fiduciary process is the best way to help ensure fees are reasonable.

## Understanding the Importance of Fee Benchmarking

Fee benchmarking is the process of comparing your plan's fees against industry standards and/or similar plans to evaluate their reasonableness. This practice is essential for several key reasons. First, ERISA mandates that plan fiduciaries act prudently and solely in the interest of plan participants, which includes ensuring that fees paid for plan services are necessary and reasonable. Second, there is the risk of litigation. As mentioned previously, there has been a notable increase in lawsuits alleging that Plan Sponsors allowed participants to be charged excessive fees. Further, fees can significantly impact participant outcomes by eroding retirement savings over time, thereby affecting their financial security. By conducting regular fee benchmarking, Plan Sponsors can better fulfill their fiduciary duties, mitigate litigation risks and enhance the financial well-being of plan participants.

There is a difference between open market bidding and benchmarking as it relates to what plaintiffs are looking out for. Open market bidding, also known as a request for proposal (RFP), solicits bids from various vendors to secure the best price and terms for the services provided. Plan Sponsors should consider conducting a recordkeeper RFP every three to seven years or more frequently if necessary due to unexpected changes to service and/or provider dissatisfaction. Fee benchmarking, on the other hand, involves comparing investment management, recordkeeping and other related fees against peers. Benchmarking should be conducted annually to assess the competitiveness of fees, investment options and to keep up with the latest fee trends as plans and markets evolve. Plaintiffs will examine the Plan Sponsor's process for evaluating recordkeeping services and how often fees were benchmarked to determine reasonableness.

## Key Components to Benchmark

When conducting fee benchmarking analysis, consider the following components:

- Administrative Fees: Costs associated with plan management, including recordkeeping, compliance, etc.

- Investment Fees: Expenses related to managing the investment options offered within the plan, such as mutual fund expense ratios.
- Individual Service Fees: Charges for optional services utilized by participants, like loan processing, transactional or financial planning.

To navigate fee benchmarking effectively, Plan Sponsors should start by gathering comprehensive data on all fees associated with their plan, including direct fees and indirect fees such as revenue sharing arrangements. It would be prudent to engage independent experts or an advisor to conduct a thorough fee analysis and provide recommendations that can further enhance the benchmarking process. Utilizing reliable benchmarking tools, such as industry surveys or databases, is crucial for comparing plan fees against those of similar plans. It is important to document the entire process meticulously, including data sources, comparisons made and decisions reached, to demonstrate fiduciary due diligence. Potential results of a benchmarking exercise could include a renegotiation of contracts with service provider, a transition to an alternative provider to help ensure cost-effectiveness or modification of fee structure.

## Current Fee Trends

There are many fee trends to consider as a Plan Sponsor today. Fee compression has helped reduced costs for participants even in open architecture pricing models. These pricing models can become even more compressed with the utilization of proprietary investment options and services. When selecting a recordkeeper, it is imperative to consider the provider with the best solutions and services for employees. Then, thoroughly evaluate the fees in open architecture and proprietary models to determine which one is reasonable and a good fit for plan participants.

Other fee trends include fee leveling. More Plan Sponsors today are deciding to eliminate the revenue sharing built into investment management. Plan Sponsors also now consider a debiting and crediting approach as well as a zero-revenue sharing approach. These approaches have garnered attention as some Plan Sponsors believe they are the most equitable for participants.

There has also been increased utilization of Collective Investment Trusts (CITs). CITs are pooled investment vehicles, similar to mutual funds but managed by a bank or trust company. Currently, CITs are available to 401(k) qualified retirement plans. Since the SECURE 2.0 Act of 2022 was amended to allow 403(b) plans to invest in CITs, the government is working to amend the securities law attached to the Expanding Access to Capital Act of 2023 thereby potentially allowing 403(b) plans access to these same investments.

The Retirement Fairness for Charities and Educational Institutions Act has been reintroduced in the Senate, aiming to allow 403(b) plans to include CITs as part of their investment menu options. This legislation is supported by the American Retirement Association (ARA), which emphasizes that CITs can boost retirement savings for employees at hospitals, universities and other nonprofit organizations. CITs typically have lower fees than mutual funds due to their exemption from SEC registration requirements and lower administration, marketing and distribution costs. The bill's passage would provide 403(b) plan participants with access to the same lower-cost investments available to 401(k) plan participants[8].

Plan Sponsors should consider the potential fee savings and improved investment options that CITs can offer, especially as legislative changes continue to progress. Evaluating the cost savings and benefits of CITs can help Plan Sponsors make informed decisions that enhance the value of their retirement plan offerings.

## Proactive Steps for Plan Sponsors

As a Plan Sponsor, proactively managing and benchmarking your plan's fees is essential to fulfilling your fiduciary responsibilities and safeguarding against litigation. Initiate a comprehensive fee review to assess all fees associated with your plan and identify potential areas for cost savings. Engage with service providers to discuss fee structures and seek opportunities for renegotiation or enhanced services. Consult with ERISA experts to help ensure compliance and implement best practices. By taking these proactive measures, you can enhance the value of your retirement plan offerings and protect your organization from potential legal challenges.

Fiducient Advisors supports plan fiduciaries in overseeing plan fees via our *Fiduciary Governance Calendar*. Each year, Fiducient Advisors conducts a comprehensive review of plan fees and benchmarking using The Institutional Consultant's Plan Survey. Fiducient Advisors is dedicated to helping Plan Sponsors maintain a robust, well-documented Fiduciary Trail of their processes.

Navigating the complexities of fee benchmarking and fiduciary duties in a litigious environment requires diligence, discipline and proactive management. By adhering to best practices and leveraging expert advice, Plan Sponsors can help ensure they fulfill their fiduciary responsibilities and provide optimal value to plan participants. Please contact the professionals at Fiducient Advisors for additional information on fee benchmarking and governance services.

[8] CITs in 403(b)s Bill Reintroduced in the Senate | PSCA

## About the Author

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Paige services institutional clients by providing counsel and guidance on fund menu design, manager selection, vendor due diligence, investment policy statements and performance monitoring. She joined Fiduciary Investment Advisors, LLC in 2015, which combined with Fiducient Advisors in 2020. She earned her MBA with a concentration in Finance from the University of Connecticut and a BA at Fairfield University. Paige serves as Chairwoman of the Salvation Army's Greater Hartford Advisory Board and is also a member of the Retirement Advisor Council. Her personal interests include traveling and staying active.