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Will Increased 401k Fee Scrutiny Trump DOL's New Fiduciary Rule?

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With the advent of new fee disclosure rules and the fallout from class action lawsuits, 401k plan sponsors appear to have become more serious about the potential liability of breaching their fiduciary duty. Was there a "straw that broke the camel's back" that caused plan sponsors to take their fiduciary duty more seriously? Could increase in attention reduce the impact of the DOL's new Fiduciary Rule?

Several recent events appear to have prompted more intense scrutiny on 401k fees. "I'd say plan sponsors started to notice it in late 2014-early 2015," says Gary Watts, Vice President at Alamo Capital in Walnut Creek, California. "It was prompted by news of lawsuits and judgements against large and well-known employers."

Indeed, the earliest warning signals occurred a decade ago. Bob Ward, Chief Revenue Officer at Vertical Management Systems in Pasadena, California, says, "Plan sponsors started noticing the liability associated with failing to scrutinize fees at the end of 2006, when St. Louis law firm Schlichter Bogard & Denton began filing claims against major plan sponsors on behalf of participants for breach of fiduciary duty around excessive fees."

The press may have given greater attention to the liability exposure produced by conflict-of-interest fees. This likely gave those plan sponsors not already attuned to these risks an impetus to start paying attention. "Many of our client plan sponsors have been scrutinizing (and negotiating) fees for a long time as they have been aware of their fiduciary duties and responsibilities," says Benjamin L. Grosz, a benefits and tax attorney at Ivins, Phillips & Barker in Washington, DC. "The wave of recent litigation, settlements, and headlines have certainly enhanced plan sponsor awareness of potential legal liability and risk."

Ward says the "several class action court cases filed in late 2006 and early 2007 shined a spotlight on the fiduciary responsibility to scrutinize fees. High-profile in nature, these cases settled over the past few years, largely in favor of the

plaintiffs: Abbott v. Lockheed Martin Corp ($62M awarded to plaintiffs), Beesley v. International Paper Company ($30M), and Spano v. Boeing ($57M)."

But, was there a particular case that stood out above the rest. "I would say the Tussy v. ABB, Inc, case was probably the watershed moment because it involved practices that do not appear to be uncommon (and the types of decisions that must be made by all qualified plan fiduciaries), significant dollar amounts, and it was a court decision as opposed to a settlement," says John C. Hughes, an ERISA attorney with the Boise, Idaho based law firm The ERISA Law Group, P.A. "The case involved issues and provides guidance on the monitoring and assessment of recordkeeping fees, as well as investment fund selection. The defendant fiduciaries were found to have breach their duties in these regards."

Grosz cites this and another case. He says, "Two of the more significant court decisions, as far as causing increased plan sponsor awareness are the Tussey v. ABB and Tibble v. Edison cases."

Many feel the highly publicized Tibble case was the straw that broke the camel's back. Watts, says "The Tibble case (Tibble v. Edison International) caused plan sponsors to take their fiduciary responsibility seriously. It was one of 13 class-action suits filed in the past eight years, but it's the one that made it to the U.S. Supreme Court and is the one usually mentioned."

The biggest takeaway from Tibble is that "fiduciary means forever." "Tibble v. Edison is probably most responsible for setting the 'tipping point' in terms of ERISA compliance," says Thomas P. Coté, Senior Vice President – Retirement Plan Solutions at San Rafael, CA based EQIS. "It establishes the fact that a Statute of Limitations must be regarded in a dynamic rather than static manner and that a plan fiduciary has an on-going responsibility to monitor and ensure that the owners of the assets, i.e. the employees/participants, are at all times properly served by the plan's service providers. In terms of the relevance and magnitude of the Supreme Court's decision, when was the last time this standing court voted in unanimity?"

For some, it wasn't one single case but the cumulative impact of all the cases as well as the cases to come. "From my experience it wasn't one case that tipped the tide of action, rather it was the cumulative effect of the large number of suits and the broad range of topics from excess fees to fund selection and the larger 'fiduciary duties'," says Murray Carter, Executive VP – Wealth Management at CSG Capital Partners of Janney Montgomery Scott in Washington DC. "Of recent concern is proposed class action of Anthem Inc. workers whose plan uses Vanguard and whom is routinely cited as the 'low cost fund' alternative."

It's not only the largess of these cases, but the breaking down of what has been considered an unquestionable axiom regarding fees. "The Lockheed Martin settlement of $62 million was a wakeup call for plan sponsors and boards of directors," says Douglas G Prince, CEO of ProCourse Fiduciary Advisors, LLC in Carmel, Indiana. "We have had a number of client Board of Directors ask about what is being done with the 401k plan fees. The newly filed Anthem claim will be interesting because if focuses on mostly Vanguard funds. This suit suggests Anthem should have used another fund instead of the one they used in various categories, and that it should have used a stable value fund instead of a money market."

It has been the convergence of these high profile class action suits with the recent DOL Fee Disclosure regulations that has elevated the focus on fees. "The advent of the Department of Labor's fee disclosure rules forced many plan sponsors to ask questions about what it all meant," says Carter. "While the participant reporting is still largely ignored, the plan sponsor reporting has helped to generate necessary dialogue and thus education."

Specifically, "408(b)(2) and 404(a)(5) are two regulations that increased fee awareness by requiring the disclosure of plan-related fees and participant-level fees," says Ward. "These regulatory actions have led to more scrutiny around all fees and increased demand for full transparency to all stakeholders."

But, by themselves, these DOL initiatives seemed to fail to prod many plan sponsors as expected. "The ERISA 408(b)(2) regulation that prompted service providers to issues a fee disclosure and the ERISA 404(a)(5) regulation that requires plan sponsors to send a fee and expense summary to participants each year were the two important pieces of regulatory action in recent years," says Prince. "From our experience, both participants and plan sponsors are 'papered' to death and maybe these notices do not have the desired impact that regulators envisioned."

While it has legitimate consequences, Fee Disclosure, for a variety of reasons, appears to be a paper tiger. Watts says, "As it stands now, plans could lose their tax-advantaged status, participants could face additional taxes, and well as possible

civil liability for the plan sponsor. So I'd say the regulatory pieces are in place but plan sponsors have to believe the rules have teeth."

While the DOL continues to do its best to enforce its own rule, it is the class action attorneys who have made the strongest statement in the area of enforcement. "As mentioned earlier, there have been some significant monetary settlements that could be damaging not only to the reputation of a company, but could have dire consequences to a firm's long term stability and profitability," says Coté. "Judging from daily industry news, there seems to be a growing trend towards more of these fiduciary cases emerging. As these cases evolve to include smaller plans and regional advisory firms, there should be an even greater focus by both service providers and plan sponsors towards fee awareness and best practice standards to comply with the Department of Labor and the Employee Benefits Security Administration."

Part of the issue is, without a viable template from the DOL, unless the plan sponsor can afford dedicated staff, interpreting the meaning of the fees being disclosed can be elusive. "Unfortunately, while most plans sponsors are more aware that there are fees associated with their plan the knowledge and understanding is still lacking," says Carter. "The larger plans have sophisticated teams who are generally on top of things. Unfortunately, the bulk of plans sponsors still don't know what to do with the information and/or how to use the data. I find that when I'm pointing out the obvious flaws in their fee/pricing structure that most plan sponsors are generally surprised and don't know why it was never fully explained to them before.'

"Most plan sponsors and fiduciaries still do not recognize the existence of this potential liability, or the magnitude," says Hughes. "There certainly has been an uptick in recognition of fiduciary liability and responsibility in recent years. I believe it was primarily the result of the ERISA 404(a)(5) regulations and the 408(b)(2) regulations, which in turn not only actually increased the responsibility of plan fiduciaries because they then had additional actions to take in order to fulfill their duties and comply with the new regulations, but the issuance of those regulations also shined a light on fiduciary issues overall. This generated commentary and discussion within the industry on the overall topic of fiduciary responsibilities and liabilities, and in particular, the responsibility of fiduciaries to understand the fees they are paying and to ensure those fees are reasonable."

Prince says, "The fee and expense regulation under 408(b)(2) helped get plan sponsors focused on fees, but not very much. The number of notices that plan sponsors (and participants) receive has numbed their senses about the whole notice. A more important impetus for plan sponsors paying attention to fees is the lawsuits that have been filed and the resulting press coverage about these suits. At the end of the day, the ones that got plan sponsors thinking about fees are attorneys and advisers. We still have prospective clients that contact us because their attorney told them to have us look at their fees."

While Fee Disclosure in itself has not produced the desired effect, it has, together with class action suits, galvanized the attention of the retirement plan industry on 401k fees. "Ever since the Department of Labor's more stringent fee disclosure regulations went into effect in 2012, the 401k industry has been well aware that there could be the possibility of significant financial and censure consequences for non-compliance," says Coté. "Fast forward to 2016 and we have now witnessed the reality of those consequences with several highly visible court cases: Abbott v. Lockheed Martin; Haddock v. Nationwide; Bilewicz v. FMR LLC; and the most famous to date: Tibble v. Edison in which the highest court in our nation, the Supreme Court of the United States, ruled 9-0 to reverse an earlier lower court decision that had been rendered in favor of the defendant, Edison International. The Abbott v. Lockheed monetary settlement at around $62MM is the largest to date and punctuates just how damaging lack of proper fiduciary oversight can be."

Is this increased scrutiny enough to make the DOL's new Fiduciary Rule moot? "The increase in awareness has led to an increase in compliance, and to a decrease in actions that might be alleged to be fiduciary breaches," says Hughes. "Overall, as a result of this increased recognition, many fiduciaries are doing a better job. The new Fiduciary Rule does not affect those parties who are already fiduciaries; it is more focused on expanding and identifying the fiduciary role of others, particularly investment providers. Potentially, there is an argument that given that existing fiduciaries have a keener awareness and are doing a better job, the new rules are unnecessary. However, I do not believe that the rule is focused on those parties; thus, the rationale behind the rule remains valid. Plans are paying less in investment-related fees on account of the 404(a)(5) and 408(b)(2) regulations, but I also do not believe that such would justify an argument that the fiduciary rules are unnecessary (which is not to say that rules might not be better focused)."

Interested in learning more about this and other important topics confronting 401k fiduciaries? Explore Mr. Carosa's book 401(k) Fiduciary Solutions *and discover how to solve those hidden traps that often pop up in 401k plans.*

Mr. Carosa is available for keynote speaking engagements, especially in venues located in the Northeast, MidAtantic and Midwestern regions of the United States and in the Toronto region of Canada. His new book Hey! What's My Number? – How to Increase the Odds You Will Retire in Comfort is available from your favorite bookstore.

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