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It’s Unanimous: The Fiduciary Duty to Monitor Has Teeth

MAY 18, 2015| PUBLICATIONS

The United States Supreme Court gave considerable comfort to defined contribution plan participants – and their lawyers – who sue plan fiduciaries for failing to keep track of plan investment options. In a unanimous decision handed down on May 18, 2015, the Court held in Tibble v. Edison International that ERISA fiduciaries have a “continuing duty” to monitor investment options, and that plan participants have six years from the date of an alleged violation of that duty to file a lawsuit against the plan’s fiduciaries. This ruling significantly undercuts the utility of a statute of limitations defense that had been successfully deployed by plan fiduciaries in previous cases, and creates fertile ground for more litigation.

The *Tibble* Case. The dispute before the Supreme Court began in 2007, when participants and beneficiaries of a 401(k) plan sponsored by Edison International sued the plan’s fiduciaries to recover losses they allegedly suffered as a result of the fiduciaries’ conduct. The participants and beneficiaries claimed that the fiduciaries violated their duties under ERISA with respect to six mutual funds; three that were added to the plan in 1999, and three others that were added in 2002. They argued that the fiduciaries acted imprudently by offering those six retail-class mutual funds when identical, lower-priced institutional-class funds were available. The more expensive funds reduced the net investment returns the participants and beneficiaries were able to obtain.

ERISA requires a breach of fiduciary duty claim to be filed no more than six years after the date of the last action constituting the breach, or in the case of an omission, the latest date on which the fiduciary could have cured the breach or violation. The district court and the Ninth Circuit Court of Appeals held that the *Tibble* plaintiffs did not file their claims with respect to the funds added in 1999 within that six-year period. And because the plaintiffs did not prove that circumstances had changed enough within the six-year period after those funds were added to require the fiduciaries to review the funds, the lower courts found that the plaintiffs’ claims were barred by the statute of limitations. (Those courts concluded that the plaintiffs’ claims with respect to the funds added in 2002 were both timely and valid, holding that the fiduciaries breached the duty of prudence by offering the higher-cost funds.) The Supreme Court agreed to consider the case last fall.

During the briefing process, the litigants attempted in various ways to recharacterize the issues they were asking the Supreme Court Justices to resolve. By the time of oral argument, however, all of the parties agreed that ERISA’s duty of prudence includes a continuing duty to monitor investments and remove imprudent ones. They disagreed about *when* that duty arises, and what it entails.

The fiduciaries argued that the duty to monitor is triggered only if there is a significant change in the circumstances surrounding an investment which would require a prudent fiduciary to conduct a renewed, in-depth review of it. Under this theory, if there is no significant change in circumstances within six years after a fund is initially added to a plan, ERISA’s statute of limitations bars any challenge to it. Although the fiduciaries convinced the Ninth Circuit to adopt this standard, the Supreme Court unanimously rejected it.

According to the opinion written by Justice Breyer for the Supreme Court, the Ninth Circuit erred in applying a statutory bar to all fiduciary breach claims arising out of the duty to monitor because it did not consider the nature of that duty. The Court noted that the duty to monitor, like most fiduciary duties under ERISA, is derived from the common law of trusts. Under trust law, fiduciaries have a “continuing duty to monitor trust investments and remove imprudent ones.” This duty “exists separate and apart from the [fiduciaries’] duty to exercise prudence in selecting investments at the outset.”

The Supreme Court held that as long as plan participants and beneficiaries file a claim alleging a violation of the

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continuing duty to monitor within six years of the alleged violation, it satisfies ERISA's six-year statute of limitations. It is then up to the court to determine whether any review and monitoring activities in which the fiduciaries engaged were sufficient to satisfy their duty, in light of the circumstances. Thus, the *Tibble* decision effectively creates a "rolling" six-year period within which claims may be filed.

The parties to the *Tibble* case also disagreed with respect to the scope of the duty to monitor, and the Supreme Court punted on this issue, as well, remanding the case back to the lower courts to determine what kind of investment review and monitoring is sufficient. Under the Court's analysis, however, this question is separate and distinct from the statute of limitations issue. If plan participants or beneficiaries adequately allege that the plan's fiduciaries violated the duty to monitor as of a certain date, and if they file suit within six years of that date, the suit will be timely. The court then must grapple with whether the monitoring process the fiduciaries used (if any) was sufficient.

Lessons for Plan Fiduciaries. Although the *Tibble* decision leaves much more to be decided by subsequent cases, the Supreme Court gave some helpful hints to plan fiduciaries and ERISA litigants.

First, during oral arguments in this case the Justices expressed skepticism about the prudence of using retail-class mutual funds as plan investment options when lower cost, institutional-class funds are available. Though the Justices' comments are not binding precedent, they likely predict how the Court would rule if this issue comes before it.

Second, the Court's analysis makes it less likely that fiduciaries will be able to have duty-to-monitor claims dismissed on statute of limitations grounds before substantial discovery takes place. In addressing the statute of limitations issue, the Court disaggregated the *timeliness* of the alleged failure or omission from the *substance* of the alleged failure or omission. The former bar is now fairly easy for plaintiffs to jump; so long as suit is filed within six years of the alleged failure or omission, it is timely. The latter issue is one the courts must analyze in light of the circumstances and context. This will make it easier for plaintiffs to survive a motion to dismiss, which ultimately will make litigation more time consuming and costly.

Third, the precise scope of the duty to monitor is now fertile ground for additional litigation. The Supreme Court expressed no view on the contours of this duty, except to say that the timing and nature of a fiduciary's review is contingent on the circumstances. Notably, the *Tibble* opinion borrows heavily from sources that interpret the common law of trusts. Those sources will likely be carefully reviewed and often cited by ERISA litigants as they attempt to create precedent in this area.

Finally, the Court's ruling gives hints to plan fiduciaries who are wondering what a "prudent" monitoring process looks like. Justice Breyer notes that trustees of common-law trusts must "*systematically* consider all the investments of the trust at *regular intervals*." From this language we can conclude that fiduciaries should (i) monitor investment funds on a regular basis (e.g., quarterly or twice annually) using (ii) a *systematic process* (such as guidelines set forth in an investment policy statement).

In another section of its opinion, the Court describes the monitoring process as one that should be "reasonable and appropriate to the *particular investments, courses of action, and strategies involved*." Thus, the process and information required in order to review certain investment options might be different from the process and information necessary to review others. A more thorough review might be required for the plan's default investment fund, or a fund in which a significant portion of the plan's assets are held, or a fund that is inherently more risky or time-sensitive (*e.g.*, hedge funds, commodity funds, and those that are especially sensitive to interest rate fluctuations).

The *Tibble* decision may also provide some guidance on another common fiduciary dilemma: What to do with an underperforming investment option. Investment fiduciaries frequently debate whether it is more prudent to eliminate an underperforming fund entirely or to "freeze" the fund to new participants while allowing current participants to maintain their investment. Again citing to trust law, Justice Breyer's opinion in *Tibble* declares that "a fiduciary *normally* has a continuing duty of some kind to monitor investments and *remove imprudent ones*" within a reasonable time. Although this language is merely "dicta" (*i.e.*, it is not necessary for the Court's ruling and thus is not binding precedent), it supports the notion that, in most cases, ERISA fiduciaries should completely remove investment funds they deem to be imprudent from the plan's lineup.

By making it more difficult for ERISA fiduciaries to prevail on a statute of limitations defense early in a case, the *Tibble* decision makes it likely that litigation involving investment funds and other fiduciary decisions that affect plan assets will continue. Lower courts will gradually shape the confines of the duty to monitor as this litigation progresses. For plan fiduciaries, this means that standards of conduct and best practices will evolve, making it even more important to engage in regular and systematic fiduciary training and education.