

## Publications

# A Growing Trend: Fiduciary Secures Trial Victory in Excessive Fee Litigation

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## Introduction

On August 22, 2024, the Central District of California found in favor of the defendants after a bench trial on breach of fiduciary duty claims related to the monitoring of recordkeeping expenses and selection of investments in *In re: Prime Healthcare ERISA Litigation*. *Prime Healthcare* involved claims that the fiduciaries of the Prime Healthcare Services, Inc. 401(k) Plan (the “Plan”), a multiple employer plan with sixty-eight different participating employers, caused the Plan to pay excessive recordkeeping fees and retain underperforming investments. This decision is another example of district courts across the country rejecting excessive recordkeeping fee and imprudent investment claims after trial. It also provides a notable rejection of the testimony from certain experts that the plaintiffs’ bar has used in recent years to support these types of claims. On September 23, 2024, plaintiffs filed a notice of appeal to the Ninth Circuit Court of Appeals.

## Background

In *Prime Healthcare*, the plaintiffs asserted three fiduciary breach claims that have become common in the ERISA litigation space. *First*, the plaintiffs alleged that the defendants failed to prudently monitor six funds in the Plan lineup, including the Active Suite of the Fidelity Freedom Funds (the “Challenged Funds”). In support of this claim, the plaintiffs argued, among other things, that the body responsible for administering the Plan (the “Committee”), (1) failed to adhere strictly to the Plan’s investment policy statement (“IPS”), (2) reflexively deferred to the recommendations of its investment advisor without sufficient independent review, and (3) lacked proper training regarding its fiduciary duties.

*Second*, the plaintiffs contended that the defendants failed to prudently monitor the recordkeeping expenses paid to the Plan’s recordkeeper (the “Recordkeeper”), which

caused the Plan to pay excessive recordkeeping fees. In particular, the plaintiffs asserted that the Committee failed to conduct a request for proposal (“RFP”) process during the relevant period, which the plaintiffs claimed is a necessary requirement of a prudent monitoring process.

*Third*, the plaintiffs claimed that the defendants failed to appropriately monitor and switch to lower-cost share classes of investments in the Plan lineup, causing participants to pay excessive investment-management fees. The plaintiffs’ main argument in support of this claim was that the Committee switched the Plan from a revenue-sharing based recordkeeping fee model to a zero-revenue sharing fee structure in 2019, which caused a transition to institutional share classes for the Plan’s investments that had a higher expense-ratio than the non-institutional share classes. This change, according to the plaintiffs, caused participants to pay more for the same investments.

At trial, the plaintiffs presented testimony from two experts. As to the Committee’s process, the defendants offered testimony from one expert.

## Rejection of Plaintiff’s Experts

In its decision, the Court first reviewed the testimony from the experts and determined that it would afford “little to no weight” to the opinions offered by the plaintiffs’ experts. With respect to the plaintiffs’ first expert, the Court found that while she was generally qualified to opine on “industry practice among benefit committees,” her testimony in this case “was conclusory, internally inconsistent, and not credible in its factual assumptions and characterization of evidence.” Notably, the Court found that her testimony, among other things, was replete with generic, conclusory “*ipse dixit*” opinions without any supporting explanation; disregarded countervailing evidence without providing a basis for doing so; and was internally inconsistent. Regarding plaintiffs’ second expert, the Court similarly afforded his opinions “little to no weight” because of, among other things, his “minimal relevant industry experience” and the “conclusory, *ipse dixit* nature” of his opinions. Notably, the Court also found that he misunderstood ERISA’s requirements, as he believed ERISA required fiduciaries to pursue the “best possible course of action at every turn,” an opinion that is at odds with the process-based nature of ERISA’s duty of prudence.

The Court’s opinions regarding the plaintiffs’ experts stand in stark contrast to its conclusion that the defendants’ expert’s testimony was “highly probative.” In reaching this conclusion, the Court noted that the defendants’ expert “has broad, longstanding, and substantial experience in the retirement-benefits industry” that includes providing “consulting services to thousands of retirement plans,” including those with as many as 50,000 participants and \$10 billion in assets under management. This experience led the Court to find the testimony provided by the defendants’ expert to be highly probative of common industry practice when it comes to managing the investments, recordkeeping fees, and share classes of a plan “similar in size and nature to that of” the Plan.

## Rejection of Plaintiff’s Claims

The Court also wholly rejected the plaintiffs’ theories regarding the defendants’ alleged imprudence, finding that the defendants used a “prudent process” to monitor the plan’s investments and recordkeeping fees.

In assessing the defendants’ process related to the Challenged Funds, the Court noted that the defendants—through the Committee—followed an established process for selecting, monitoring, and removing investment options, guided by the Plan’s IPS. In particular, the IPS directed the Committee to consider (1) fees, (2) style consistency, (3) volatility and diversification, (4) performance, and (5) management and organization, when determining which funds to add to the Plan. In terms of monitoring, the IPS directed the Committee to use “a comprehensive Scoring System proprietary to the Investment Consultant/Advisor” that included eight quantitative metrics, such as performance versus peer groups on a three- and five-year basis, and two qualitative metrics, such as the strength and experience of the fund’s management team. Finally, while the IPS did not contain any hard-and-fast rules on fund removal, it directed the defendants to remove a fund “after noncompliance with the IPS has been established, or appears likely.”

The Court found that the defendants followed the IPS’s guidelines with respect to the Challenged Funds. In doing so, the Court rejected the plaintiffs’ argument that the defendants’ “reflexively deferred” to the investment advisor for monitoring the Plan’s investments. Instead, the Court found that the Committee meeting minutes showed that the defendants actively engaged with the investment advisor’s advice and conducted meaningful discussions regarding investment performance.

Finally, the Court found that the Committee received regular fiduciary training as part of its quarterly meetings, with updates provided by advisors. The Court also agreed with the defendants’ expert’s testimony that this training aligned with industry standards and included specific fiduciary-duty updates based on external developments in the industry. Overall, because the defendants prudently

monitored the Challenged Funds, appropriately monitored and relied upon the investment advisor's expertise, and received regular and proper fiduciary training, the Court ruled in the defendants' favor on plaintiffs' claim related to the Challenged Funds.

Similarly, the Court also found that the defendants, through the Committee, "reasonably informed" themselves of "the market for recordkeeping services" by directing its advisors to conduct one request for information and three vendor benchmarks during the relevant period. In reaching this conclusion, the Court rejected the plaintiffs' contention that plan fiduciaries only prudently monitor a plan's recordkeeping fees if they conduct an RFP process. The Court based this finding, in part, on the defendants' expert's testimony that RFPs "are not industry standard," as evidenced by the fact that only a small percentage of plans use RFPs, while the majority rely on benchmarking studies similar to those employed by the defendants. As a corollary to this finding, the Court also rejected an allegation plaintiffs often raise in excessive recordkeeping fee claims—that the defendants failed to ensure that the Plan's fees remained reasonable despite the growth in the Plan's asset levels. Overall, because the Court concluded that the defendants' use of a request for information and vendor-fee benchmarks, which relied on the investment advisor's expertise in assessing fees, was prudent, it ruled in defendants' favor on plaintiffs' recordkeeping fee claim.

Finally, the Court rejected the plaintiffs' claim that the defendants reflexively switched to a zero-revenue sharing recordkeeping fee structure without considering whether this change inadvertently increased net effective expenses due to higher-cost share classes. The Court specifically noted that evidence in the record showed that the Committee "closely monitored" the share classes of the Plan's investments, including emails showing that Committee members discussed share classes with its advisors on numerous occasions. Moreover, the evidence also demonstrated that the Committee directed its advisors—after the change to a zero-revenue sharing fee model—to work with fund managers to see if the Plan could obtain lower-cost share classes of various funds in the Plan lineup. Because of this, the Court ruled in the defendants' favor on the plaintiffs' claim related to the share classes of investments in the Plan.

## Key Takeaways

*Prime Healthcare* represents another significant defense victory in excessive fee and imprudent investment litigation. In recent years, defendants have fared well in defending against these types of claims at trial—including in cases such as *Nunez v. B. Braun Medical, Inc.*, *Mattson v. Milliman, Inc.*, *Vellali v. Yale University*, *Lauderdale v. NFP Retirement, Inc.*, and *Mills v. Molina Healthcare, Inc.*—and *Prime Healthcare* is another example in this growing trend. In line with the Supreme Court's guidance in *Hughes v. Northwestern University*, district courts in these cases are placing greater emphasis on the fiduciary process employed in reaching a decision. This trend also highlights that courts are becoming skeptical of the expert testimony proffered by plaintiffs in support of these threadbare lawsuits, rejecting even qualified opinions if they promote an outcome-based, rather than process-based, view of fiduciary duties.

*Prime Healthcare* demonstrates that litigating through summary judgment and trial is a viable strategy when a plan has a thoughtful decision-making process. Plan sponsors who can present evidence of a thorough process and prudent monitoring—like those seen in *B. Braun*, *Milliman*, and *Prime Healthcare*—may consider pursuing litigation rather than settling.