Plan Sponsor Quarterly Update

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What's New: A Look at the Pentegra Suit

You've likely heard the headline— a recent jury trial awarded more than $38 million to retirement plan participants in a suit involving unreasonable plan fees. There are a lot of angles floating around as well. Is this about 3(16) fiduciaries? MEPs? Plan fees in general? Does this change how plan sponsors evaluate fees? This article will walk through some underlying themes in *Khan v. Board of Directors of Pentegra Defined Contribution Plan et al.* to help provide clarity moving forward.

Some legal background. This is jury finding. This is notable for at least a few reasons:

- ERISA cases generally go before a judge only— going before a jury *and* making it all the way to a jury verdict is extremely rare.

- Jury verdicts are different from court rulings. Juries are finders of fact. They are tasked with determining which facts are true and applying those to existing law. This means that jury verdicts do not generally establish legal precedent in the way that court rulings do—that is, jury verdicts are binding only on the specific fact pattern they decide.

- This case has not yet been appealed. In jury verdicts, any resulting precedent will generally come from appellate court holdings. We do not have those yet.

So: while this verdict can be instructive in terms of best practices, it has not yet established new law.

What exactly did the case allege? The complaint is centered on fiduciary duty and associated prohibited transactions. The counts alleged were as follows: (1) breach of fiduciary duty related to excess administrative fees, (2) prohibited transactions including self-dealing, (3) breach of fiduciary duties related to unreasonable investment management fees, and (4) failure to monitor fiduciaries.

What do we do with this? While the case's underlying facts do include a MEP and 3(16) fiduciaries, there are no explicit allegations that would apply only in the MEP space or only to 3(16) fiduciaries. The allegations were much more broad and, to many practitioners, confirmed existing bedrock principles of ERISA: fees must be reasonable and fiduciary processes should be prudent and well-documented.

- *Excess fees*: The allegations here, which were argued to the jury, were centered on the fact that the plan sponsor did not engage in prudent process under ERISA and that the resulting plan administration fees were unreasonable. Pertinent for our purposes, in arguing breach of fiduciary duty, the complaint alleged that (1) the plan sponsor failed to conduct an RFP to look at competitive pricing and (2) Pentegra raised prices while industry prices were declining and without providing any additional services to support those increased fees. The jury agreed and found that such practices resulted in unreasonable fees. This does not mean that fees cannot be changed—this means that fees must be reasonable. Best practice here remains the same. Fees must be reasonable and plan sponsors must follow prudent processes to retain and oversee plan providers.

- *Self-dealing*: Importantly, Pentegra served as recordkeeper and "contract administrator" while also causing the plan to invest in Pentegra collective instrument trusts. Best practice here is similarly unchanged: any advice or action from an advisor or fiduciary to invest plan assets in that advisor or fiduciary's own funds should be met with extreme skepticism. Again, prudent process is key under ERISA.

- *Fiduciary duty to monitor*: An important note for plan sponsors: you cannot wholly delegate your fiduciary duties under ERISA. Even when certain duties are delegated, the plan sponsor always maintains—at minimum—an ongoing fiduciary duty to monitor service providers.

This suit is a great reminder for all plan sponsors and service providers to revisit fiduciary standards and ensure their actions are aligned with best practices under ERISA. Reasonableness, prudent process, and good documentation are key.

Best Practices:
Recent Legislative Trends

This quarter, we bring you an overview of key litigation updates, examining how new rulings and ongoing legal battles can impact your clients.

- **Importance of good documentation** (*Wallace v. Oakwood Healthcare, Inc.*, 954 F.3d 879, Sixth Circuit Court of Appeals, 2020): Here, a plaintiff brought suit without exhausting a plan's claims procedures—and the case was permitted to move forward! The court found that the employer's plan document did not contain claims procedures or the requirement that the claims process be exhausted before a participant files suit. The SPD, similarly, did not clearly state the claims procedure exhaustion requirements. Therefore, though the plan administrator provided notice of the exhaustion requirement in its initial claim denial, the court held that the plan documents' lack of written claims procedures and lack of a written claims exhaustion requirement meant that the participant could bring suit immediately.

  Though this case occurred in the health and welfare plan context, the same reasoning would likely apply to all ERISA-covered plans. As a plan sponsor, you should routinely review all plan documents and SPDs to ensure that they are complete, consistent, and updated timely. Plan sponsors should ensure that claims procedures are well-documented, and that they include claims exhaustion provisions.

- **Accuracy in communication** (*Sullivan-Mestecky v. Verizon Communications Inc.*, 961 F.3d 91, Second Circuit Court of Appeals, 2020): Here, a benefits plan provided life insurance in an amount equal to one year's salary. A participant was told repeatedly by a plan representative, however, that her life insurance benefit would be in an amount equal to *twelve* times her salary. The participant died, and the beneficiary brought suit alleging that she was entitled to this greater amount. Verizon, the plan sponsor, attempted to counter by asserting that both the plan document and SPD were clear and, therefore, that the misstatements should not prevail. The court, perhaps surprisingly, did not find that argument determinative. Instead, it held that Verizon may have breached its fiduciary duty of prudence by failing to provide the participant (via the communications of its representatives) with complete and accurate information about her benefits.

  The takeaway: clear plan documents and SPDs are good but may not always be enough. Plan sponsors should remember that actions by vendors may result in fiduciary breaches that are imputed to them.

- **Forfeiture litigation**: There are a number of pending forfeiture litigation matters across the country. These suits generally target plans that permit plan sponsors to choose how forfeitures will be allocated. The general allegations in each follow a similar pattern: (1) deciding how to use forfeitures is a fiduciary decision (2) using forfeitures to offset company contributions is a fiduciary breach as (3) the plan sponsor should have allocated forfeitures to participant accounts instead. While these allegations are similar in these suits, it is important to remember that these are just allegations—that is, they are just arguments that plaintiffs are bringing. A court has not yet ruled on the merits of these claims.

  You may have heard of these suits and have some worries. Though there are no rulings yet, best practices for plan sponsors could include: (1) reviewing the plan document for a list of permissible uses of forfeitures, (2) consider amending the plan to "hard wire" in an order of preference and ensure forfeiture decisions are settlor in nature, and (3) spending down the forfeiture account no later than the year after any forfeiture arises.

- **Heads up**: Though not in litigation yet, a tip to avoid potential future suits: in the DOL's recent expansion of its Voluntary Fiduciary Correction Program, the Department announced that it considers it a *fiduciary duty* for plan sponsors to review plan contributions and loan repayments **at least every 180 days** to ensure all such payments have been made to the plan. This means that checking only at year-end for missing or late contributions is no longer sufficient.

Hot Topic:
DOL Releases New Annual Funding Notice Guidance

Last month, the DOL released Field Assistance Bulletin 2025-02, which provides guidance regarding changes to the annual funding notice ("AFN") requirements of ERISA Section 101(f), as expanded under the SECURE 2.0 Act of 2022 ("SECURE 2.0"). The Field Assistance Bulletin was drafted as a series of questions and answers and included two model notices: (1) Appendix 1 for single-employer plans and (2) Appendix 2 for multiemployer plans.

The Field Assistance Bulletin provides a few key takeaways:

1. **Average return on assets**: Under SECURE 2.0, AFNs must provide the plan's "average return on assets" for the notice year. The Field Assistance Bulletin provides two possible methods of calculating this figure but also notes that other methods may be sufficient.

2. **New metric**: While prior AFNs disclosed a plan's funding level using the plan's "funding target attainment percentage," SECURE 2.0 requires a new metric—instead, it requires that the AFN provide the plan's "percentage of plan liabilities funded." The Field Assistance Bulletin provides that plans may use reasonable estimates for the year-end metric for the notice year. This means, for example, that a plan may use reasonable estimates for the 2025 year-end liabilities in the 2025 AFN. However, estimates are not permitted for the metric for the prior two years—for these, the metric should match the figure disclosed on the corresponding Form 5500 for those years.

3. **Demographic information**: Under SECURE 2.0, AFNs must also include participant and beneficiary totals as of the last day of the notice year and the two prior years. The Field Assistance Bulletin clarified that, as with the new metric above, plans may use a reasonable estimate for the year-end figures of the notice year. For the prior two years, however, estimates are not permitted.

The best practice for plan sponsors will be to follow the model notices included in the Field Assistance Bulletin. Frustratingly, given the timing of the guidance's release, the DOL provides that it will hold plans to this new requirement for the 2024 notice year. If an AFN has been sent out for 2024 that does not comply with the Field Assistance Bulletin, it is worth sending a new notice that meets all new requirements.

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