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Fifth Circuit Reverses Dismissal of 401(k) Fees Claims

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The Fifth Circuit recently reversed a district court's dismissal of claims that the fiduciaries of a 401(k) plan breached the duty of prudence under ERISA by offering participants retail share classes instead of cheaper institutional share classes, and causing the plan to pay allegedly excessive recordkeeping fees. The decision is notable for articulating the level of detail that may be sufficient in the Fifth Circuit for these kinds of claims to survive a motion to dismiss. The case is *Perkins v. United Surgical*, No. 23-10375, 2024 WL 1574342 (5th Cir. Apr. 11, 2024).

The District Court's Decision

The district court dismissed plaintiffs' claims, with prejudice, for failure to state a claim. (The district court also dismissed certain claims for lack of Article III standing, but plaintiffs did not appeal that ruling). On the share class claim, the district court held that the complaint failed to provide the context necessary to infer imprudence, because it did not expressly allege that retail share classes the Plan offered were identical in all ways except price to the cheaper institutional share classes that allegedly were available to the Plan. On the excessive recordkeeping fees claim, the court held that plaintiffs failed to allege context-specific facts supporting an inference of imprudence because they did not identify meaningful benchmarks or explain how the Plan's costs were high relative to the services offered by the Plan. The benchmarks that the court found to be insufficiently meaningful included the Brightscope/ICI study of industry averages, plans of different sizes, and fees of these other plans that were from different years and/or were calculated in materially different ways.

The Fifth Circuit's Decision on Share Class Claim

The Fifth Circuit reversed the dismissal of plaintiffs' claim that defendants' selection of retail share classes was imprudent, finding that defendants "failed to sufficiently refute the Plaintiffs' allegations." In so ruling, the Fifth Circuit rejected the district court's holding that plaintiffs had to provide more detail showing how retail and institutional share classes are alike. Notwithstanding the district court's contrary conclusion, the Fifth Circuit found that plaintiffs *had* established that the Plan's share classes were identical to institutional share classes except for cost, by alleging that the different share classes held identical investments and had the same manager. In so finding, the court credited plaintiffs' contention that the share classes would not be different in terms of potential returns, risk, services offered, or manager flexibility. The court also rejected defendants' argument that dismissal was warranted because plaintiffs failed to rebut the "obvious alternative explanation" for offering retail shares—unlike institutional shares, retail shares provide for revenue sharing that offsets plan recordkeeping expenses. Although the court acknowledged that reducing recordkeeping costs was a plausible explanation for defendants' conduct, it concluded that plan mismanagement was as well, and defendants' proposed explanation was undercut by allegations that the Plan's recordkeeping fees were excessive.

The Fifth Circuit's Decision on Recordkeeping Fees

The Fifth Circuit also reversed the district court's holding that the plaintiffs failed to state a claim in connection with excessive recordkeeping fees. Quoting a pleading standard recently articulated by the Seventh Circuit, the court found that, in order to state a plausible prudence claim based on excessive recordkeeping fees, plaintiffs must plead sufficient facts to render it plausible that defendants "incurred unreasonable recordkeeping fees and failed to take actions that would have reduced such fees." In holding that plaintiffs satisfied this standard, the court cited plaintiffs' allegations that: during the relevant period the plan paid about $83 per participant per year for recordkeeping services, but similarly-sized plans paid about $30 for services that, based on a review of codes used in Form 5500s, were similar to those received by the Plan. This holding contrasts with the district court's view that plaintiffs' benchmarks were not meaningful for evaluating the Plan because they had "major differences," such as size, and that plaintiffs failed to establish that the Plan's costs were excessive relative to the services received by the Plan. The Fifth Circuit also distinguished other decisions in which excessive recordkeeping fee claims were dismissed, reasoning that unlike plaintiffs here, plaintiffs in other cases either relied exclusively on industry-wide recordkeeping fee averages, or compared the plan at issue to plans that were dissimilar in size or received different services. The court also reasoned that plaintiffs' claim was supported by their allegation that defendants failed to take steps that may have reduced recordkeeping costs, such as regularly soliciting competitive recordkeeper bids.

Proskauer's Perspective

The Fifth Circuit's decision follows a well-established trend among circuit courts that makes it difficult for defendants to successfully move to dismiss share-class claims. (Indeed, the Fifth Circuit observed that six circuit courts have held that similar share class allegations should survive dismissal). The fact that plaintiffs alleged a viable claim for excessive recordkeeping fees made it even more difficult for defendants to dismiss this claim, because, in the court's view, it called into question whether revenue sharing—as opposed to imprudence—was a plausible explanation for selecting retail shares. But even if that were not the case, it is unclear whether the Fifth Circuit, like other appellate courts, would still have reversed dismissal In other cases, a revenue sharing defense may be more successful where a court takes judicial notice of documents that make it "obvious" rather than merely "plausible" that revenue sharing effectively made a plan's retail share classes cheaper than available institutional share classes.

With respect to the recordkeeping fee claim, the Fifth Circuit's requirement that plaintiffs plead that similarly-sized plans received similar services for lower fees is consistent with the standard set in other jurisdictions. However, the court appeared to require less specific pleadings with respect to such comparisons than courts require in other jurisdictions. For example, in *Matousek v. MidAmerican*, 51 F.4th 274 (8th Cir. 2022), the court conducted a more exacting comparison of services across plans and specifically identified fees associated with loans as a distinguishing service. Here, by contrast, the court accepted the assertion that fees associated with loans were negligible and therefore did not invalidate the plaintiffs' comparisons.

In short, the Fifth Circuit's ruling in *Perkins* reflects a continued trend among circuit courts toward articulating pleading standards that sound similar, but are applied differently.

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