

# Unanimous Supreme Court Overturns Court of Appeals in Northwestern University 403(b) Plans Excessive Fee Case

by Suzanne E. Meeker on January 25, 2022

The United States Supreme Court has agreed with participants in two 403(b) plans sponsored by Northwestern University that their lawsuit, alleging that plan recordkeeping and investment fees were excessive, should not have been dismissed. On January 24, 2022, the Court sent *Hughes v. Northwestern University* (Jan. 24, 2022) back to the United States Court of Appeals for the Seventh Circuit for a “context-specific” determination of whether the participants plausibly alleged that plan fiduciaries breached their duty of prudence under ERISA. The Court’s unanimous decision came just seven weeks after oral argument.

The background to the Supreme Court’s decision is described in our earlier post on the case, found [here](#). Briefly, the lawsuit involves claims that Northwestern breached its duty of prudence in several ways, resulting in excessive recordkeeping fees being charged to some participant accounts, excessive investment fees being charged for some investment options, and too many investment options being offered overall. The District Court dismissed the complaint for failing to plausibly allege a breach of fiduciary duty, and the Court of Appeals upheld the dismissal.

The Court of Appeals refused to second-guess Northwestern’s decision-making as to the selection of (multiple) recordkeepers and the resulting structure of recordkeeping fees, noting that the recordkeeper selection affected the plans’ ability to offer popular and well-performing TIAA annuity products. Regarding investment fees, the Court focused on the wide array of investment options and participants’ ability to choose many of the types of funds the complaint described as preferable choices. Thus, the Court concluded that Northwestern “cannot be faulted for leaving choice to the people who have the most interest in the outcome.”

The Supreme Court, however, ruled that the Court of Appeals “erred in relying on the participants’ ultimate choice over their investments to excuse allegedly imprudent decisions” by the plan fiduciaries. Applying principles enunciated in its 2015 decision in *Tibble v. Edison Int’l* and 2014 decision in *Fifth Third Bancorp v. Dudenhoeffer*, the Supreme Court said that ERISA requires plan fiduciaries to “to conduct their own independent investigation to determine which investments may be prudently included,” and to remove imprudent investments within a reasonable period of time. The fact that the Northwestern plans allowed participants to direct the investment of their accounts and some investment options matched the participants’ preferences for low-cost recordkeeping and low expense ratios did not alter this duty. Notably, the opinion at least

suggests that in some circumstances offering a large number of options may itself violate the duty of prudence if, for example, the menu can be shown to result in participant confusion and poor choices.

Ultimately, the Supreme Court found that the Court of Appeals' repeated reliance on participants' investment choice required reconsideration of the motion to dismiss in its entirety. In this regard, the Supreme Court also quoted *Dudenhoeffer* to emphasize that fiduciary prudence is dependent on prevailing circumstances, so that the appropriate analysis of the motion to dismiss must be context-specific. The opinion ends with the observation that, at times, "the circumstances facing an ERISA fiduciary will implicate difficult tradeoffs, and courts must give due regard to the range of reasonable judgments a fiduciary may make based on her experience and expertise." This observation should provide some comfort to plan fiduciaries that the Supreme Court acknowledges the pressures of dealing with legacy investment funds and the practical challenges involved with moving away from the TIAA recordkeeping platform.

The Supreme Court's decision means that participants in Northwestern's 403(b) plans will have another day in court. For fiduciaries of retirement plans generally, the decision underscores the importance of good plan governance, including multiple elements: an established process for ongoing evaluation of the prudence of each plan investment option, for taking action within a reasonable time if an option becomes imprudent, and for documenting both the ongoing evaluation and the reasons for any action taken. The Supreme Court's emphasis on circumstances and context for assessing fiduciary decisions provides reassurance that perfection is not required, but also shows why a contemporaneous record of fiduciary decisions may be critical.

Please contact a member of Verrill's [Employee Benefits & Executive Compensation Group](#) if you have any questions about the implications of the *Northwestern* decision and your retirement plans' fiduciary governance.



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