VOL. 44, NO. 4 SPRING 2019

Employee Relations
LAW JOURNAL

Employee Benefits

Sacerdote v. NYU: Lessons for Plan Fiduciaries

Mark E. Bokert and Alan Hahn

Over the last few years lawsuits have been filed against approximately 20 university retirement plans. Typically, the lawsuits allege that plan fiduciaries breached their duties by offering poorly performing funds and allowing their plans to pay excessive fees. Defendants include:

- Brown University;
- Columbia University;
- Cornell University;
- Duke University;
- Emory University;

Mark E. Bokert is a partner and co-chairs the Benefits & Compensation Practice Group of Davis & Gilbert LLP. His practice encompasses nearly all aspects of executive compensation and employee benefits, including matters related to equity plans, deferred compensation plans, phantom equity plans, qualified retirement plans, and welfare plans. Mr. Bokert may be contacted at *mbokert@dglaw.com*.

Alan Hahn is a partner and co-chairs the Benefits & Compensation Practice Group of Davis & Gilbert LLP. His practice is devoted to advising clients of all sizes, including in the design and implementation of a wide variety of creative, unique, and tax-effective employee benefit plans and programs. Mr. Hahn may be contacted at *ahahn@dglaw.com*.

- Georgetown University;
- George Washington University;
- The Johns-Hopkins University;
- Massachusetts Institute of Technology;
- Northwestern University;
- New York University (NYU);
- Princeton University;
- University of Chicago;
- University of Pennsylvania;
- University of Southern California;
- University of Rochester;
- Vanderbilt University;
- Washington University; and
- Yale University.

Among these lawsuits, one of the first major decisions was *Sacerdote v. NYU*[1] (referred to herein as the NYU case) which offers several important lessons for plan committees regarding their fiduciary duties under ERISA.

ERISA Fiduciary Duties

As explained by the court in the NYU case, ERISA imposes twin duties of prudence and loyalty on fiduciaries of retirement plans. The duty of loyalty requires fiduciaries to act "solely in the interest of the participants and beneficiaries," and "for the exclusive purpose of providing benefits to participants and their beneficiaries; and defraying reasonable expenses of administering the plan."[2] The duty of prudence requires a fiduciary to act "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims."[3]

To evaluate whether the "prudent person" standard is satisfied, a court must ask whether "the individual trustees, at the time they engaged in the challenged transactions, employed the appropriate methods to investigate the merits of the investment and to structure the investment."[4] The prudence of a fiduciary is measured against an objective standard, and their own "lack of familiarity with investments is no excuse" for failing to act with the care, skill, prudence and diligence required under the circumstances then prevailing.[5]

A fiduciary breaches its duty of prudence when it fails to employ "the appropriate methods" in making investment decisions.[6] Pursuant to ERISA regulations, a fiduciary's compliance with the prudent-man standard requires that the fiduciary give "appropriate consideration" to whether an investment "is reasonably designed, as part of the portfolio . . . to further the purposes of the plan, taking into consideration the risk of loss and the opportunity for gain (or other return) associated with the investment."[7] Fiduciaries should consider the prudence of each investment as it relates to the portfolio as a whole, rather than in isolation. Accordingly, courts must look "not only to [a fiduciary's] investigation procedures, but also to the methods used to carry out those procedures as well as the thoroughness of their analysis of the data collected in that investigation."[8]

Moreover, fiduciaries have a continuing duty to monitor investments and remove imprudent ones. This means that a fiduciary "cannot assume" that investments that were prudent at one time "will remain so indefinitely."[9] Rather, the fiduciary "must 'systematic[ally] conside[r] all the investments of the trust at regular intervals' to ensure that they are appropriate."[10] In short, a fiduciary who ignores changed circumstances that increase the risk of loss is imprudent.'"[11]

A fiduciary also has the responsibility of ensuring that fees paid to recordkeepers are not excessive relative to services rendered.[12] A prudence claim based on excessive fees must be supported by facts that take the particular circumstances into account.[13] ERISA does not dictate "any particular course of action" with regards to fees, but it does require a "fiduciary . . . to exercise care prudently and with diligence under the circumstances then prevailing."[14]

Sacerdote v. NYU

In the NYU case, plaintiffs asserted that the NYU Retirement Plan Committee (the Committee) breached its duty of prudence with regard to two NYU retirement plans: the New York University Retirement Plan for Members of the Faculty, Professional Research Staff and Administration and the New York University School of Medicine Retirement Plan for Members of the Faculty, Professional Research Staff and Administration (together, the Plans). Plaintiffs' first claim was that the Committee imprudently managed the selection and monitoring of recordkeeping vendors resulting in excessively high fees. According to plaintiffs, the Committee could have reduced such fees by "consolidating" its use of two recordkeepers into one, and also by negotiating a lower overall rate. Plaintiffs also argued that the Committee failed to prudently manage a request-for-proposal (RFP) process relating to recordkeeping vendors.

Plaintiffs' second claim was that the Committee acted imprudently by failing to remove the TIAA Real Estate Account and the CREF Stock Account as investment options (thereby continuing to allow plaintiffs to invest in such funds). Plaintiffs asserted that the Committee used confusing and inappropriate financial benchmarks to review their performance and that these funds objectively underperformed, resulting in significant losses.

After carefully reviewing the record, the court found that the evidence showed that while there were some compliance deficiencies—including that several members displayed a concerning lack of knowledge about their plans—plaintiffs had not proven that the Committee acted imprudently or that the Plans suffered losses as a result. Accordingly, NYU was exonerated on all counts. The case offers several important lessons for Plan fiduciaries.

Process Matters

The first important lesson of the NYU case is that a plan committee must conduct its business according to a prudent process. In the NYU case, the court thoroughly examined the Committee's process and found it to be sufficient. Had the Committee's process not been sound, the court would likely have cast a more skeptical eye on specific decisions made by the Committee. Hallmarks of a prudent process include holding meetings on a quarterly basis, retaining an investment advisor and ERISA counsel, and having an investment policy statement and committee charter. The investment advisor should prepare a written report which evaluates the performance of each of the plan's investment funds and the report should be distributed to committee members prior to each meeting so that committee members have sufficient time to review the report. Minutes that are drafted by ERISA counsel should reflect the decisions made by the committee and the reasons behind those decisions.

Be a Good Committee Member

In the NYU case, committee members were called to testify and their knowledge of plan matters was tested. Accordingly, the second important lesson of the NYU case is that committee members should ensure that they are knowledgeable about their plan's investments and have at least a basic understanding of their plan's terms, such as plan provisions that relate to eligibility and vesting and the types of contributions that are allowed. Committee members should attend committee meetings on a regular basis and be thoughtful and involved while attending those meetings.

Interestingly, in the NYU case, some members of the Committee were not knowledgeable, thoughtful, or involved. For example, one of the co-chairs of the Committee viewed her role as primarily concerned with scheduling, paper movement, and logistics; she displayed a surprising lack of in-depth knowledge concerning the financial aspects of managing a multi-billion-dollar pension portfolio and a lack of true appreciation for the significance of her role as a fiduciary. Another Committee member was similarly unfamiliar with basic concepts relating to the Plans, such as who fulfilled the role of the plan administrator. When asked about her inability to remember Plan details, she responded that she has a "big job" in the human resources department and that her role on the Committee is one of many responsibilities she has, which suggested that she did not view herself as having adequate time to serve effectively on the Committee. Another Committee member who was also a co-chair, testified that she did not know whether NYU was a large plan relative to others in the United States and she could not recall a particular investment fund even though it was discussed at multiple meetings and was on the "watch list" during her tenure. Another Committee member testified that he did not even know whether he was, at the time of trial, still a member of the Committee—and thus whether he bore a fiduciary responsibility to thousands of NYU participants.

It appears, however, that several members of the Committee were "good" committee members—i.e., they were knowledgeable and heavily involved in plan matters and Committee decisions. Therefore, the court said that "[w]hile the court finds the level of involvement and seriousness with which several committee members treated their fiduciary duty troubling, it does not find that this rose to a level of failure to fulfill fiduciary obligations." Best practice dictates, however, that all committee members strive to be "good" members.

Use Independent Judgment

The third important lesson is that a committee should not blindly follow its investment advisor's advice. It must use independent judgment. Independent judgment is demonstrated by asking the investment advisor questions and probing the reasons for its advice. This is not to say a committee should deviate routinely from its investment advisor's advice. To the contrary, in the vast majority of situations, it will be prudent to follow the investment advisor's advice. In addition, committees often vote unanimously in favor of their advisor's recommended course of action. But if circumstances call for it, such as when a committee is offered a choice between several very similar investment funds, a committee member should not be afraid to cast a dissenting vote as it will clearly demonstrate the use of independent judgment.

Consider RFPs

The final takeaway is that, unless a committee routinely obtains rate reductions from in its third-party administrator, the committee should periodically issue an RFP for their plan. Issuing an RFP approximately once every five years is a good rule of thumb. In the NYU case, the Committee issued one RFP in 2009 and the next one in 2016. Plaintiffs argued that RFPs should have been issued more frequently. The court, however, held that more frequent RFPs were not necessary because NYU's recordkeeping fees consistently decreased as NYU obtained rate reductions. Also, the court correctly noted that RFPs are not required under ERISA but they can be an example of an action taken to ensure fees are appropriate.

Conclusion

The NYU case demonstrates that a committee's overall conduct contributes to its ability to successfully defend a lawsuit based on a breach of fiduciary duty. The first lesson of the NYU case is that plan committees should conduct their business according to a prudent process. Other lessons are that committee members should be knowledgeable, thoughtful and involved and use independent judgment. Finally, to evaluate their plan's administrative fees and services, a committee should issue an RFP from time to time. A committee should work with its ERISA counsel to develop these and other prudent practices.

Notes

1. Sacerdote v. N.Y. Univ., 16-cv-6284 (SDNY July 31, 2018).

2. ERISA § 404(a)(1)(A).

3. ERISA § 404(a)(1)(B).

4. Katsaros v. Cody, 744 F.2d 270, 279 (2d Cir. 1984) (quoting Donovan v. Mazzola, 716 F.2d 1226, 1232 (9th Cir. 1983), cert. denied, 464 U.S. 1040 (1984).

5. *Katsaros*, 744 F.2d at 279.

6. *Katsaros*, 744 F.2d at 279 (quoting *Mazzola*, 716 F.2d at 1232).

7. 29 C.F.R. § 2550.404a–1(b)(2)(i)).

8. Chao v. Tr. Fund Advisors, No. Civ. A. 02-559, 2004 WL 444029, at *3 (D.D.C. Jan. 20, 2004).

9. A. Hess, G. Bogert & G. Bogert, Law of Trusts and Trustees (Bogert 3d) § 684, pp. 145-146 (3d ed. 2009)).

10. Bogert 3d § 684.

11. Armstrong v. LaSalle Bank Nat'l Ass'n, 446 F.3d 728, 734 (7th Cir. 2006).

12. Young v. Gen. Motors Inv. Mgmt. Corp., 325 Fed. App'x 31 (2d Cir. 2009).

13. *Id.*

14. Chao v. Merino, 452 F.3d 174, 182 (2d Cir. 2006) (internal quotation omitted).

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