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Ruling addresses when a third-party acts as ERISA fiduciary

The 9th Circuit outlined the role that employers and others play as fiduciaries under ERISA, in order "to ensure that employees will not be left empty-handed."

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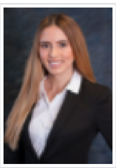

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Congress enacted the Employee Retirement Income Security Act of 1974 to protect employees from the then-rampant abuse of their employer-sponsored plans, including those plans that provide life, accident, disability, health and retirement benefits. To achieve its goals, ERISA establishes procedural protections and imposes fiduciary duties on various parties involved in a plan's administration. Once the relationship is established, an ERISA fiduciary must exercise discretion in accordance with a duty of care. Among other things, this duty of care requires that a fiduciary act in the sole interest of plan participants and beneficiaries, and prohibits self-dealing. If an ERISA fiduciary fails to meet these requirements, it may be liable for breach of those duties.

Generally, two types of fiduciaries exist under ERISA: named fiduciaries and unnamed fiduciaries, although ERISA makes no distinction between the two regarding liability for breach. *See* 29 U.S.C. Sections 1109, 1132(a); Glanton ex rel. *ALCOA Prescription Drug Plan v. AdvancePCS, Inc.*, 465 F.3d 1123, 1124 (9th Cir. 2006). An employer becomes a named fiduciary upon the formation of an ERISA plan, as identified in the primary plan document. In other circumstances, a party's conduct may give rise to a fiduciary relationship, sometimes referred to as a "claim" fiduciary. Such circumstances include the following: (1) if it exercises discretionary authority or control concerning the management or disposition of the plan's assets; (2) if it provides or has authority to provide compensated investment advice regarding the plan's assets; or (3) if it has discretionary authority or responsibility in the plan's administration. In assessing whether a party functions as an ERISA fiduciary, the scope of the inquiry is limited to the action which is the subject of the complaint. *See Pegram v. Herdrich*, 530 U.S. 211, 226 (2000).

In a recent decision, *Santomenno v. Transamerica Life Ins. Co.*, 2018 DJDAR 1713 (March 21, 2018), the 9th U.S. Circuit Court of Appeals addressed when a third-party administrator or service provider acts as an ERISA fiduciary. In the underlying case, the district court denied defendants' motion to dismiss because it found that Transamerica Life Insurance Company, the plan's service provider, functioned as a fiduciary when it negotiated and later collected its own administrative fees from the plan's funds. The 9th Circuit reversed the district court's order, finding that plaintiffs failed to state claims for relief because Transamerica's actions as alleged did not give rise to fiduciary liability.

Transamerica's relationship to the plan began when plaintiffs' employers negotiated with it to manage their retirement plans. The employers selected from various investment options, or bundles, provided by Transamerica and those bundles were then offered to employees. Transamerica serviced the pooled funds, tracked each employee's individual investment and performed other administrative tasks for the plan. The governing service agreement set Transamerica's compensation at a fixed percentage of the assets in each account, with a schedule of fees for each. Transamerica directly collected its own fees, daily, from the separate accounts. The managers of the primary investment vehicles likewise charged fees and, through a separate arrangement, Transamerica also collected payments from them.

Plaintiffs filed suit, alleging that Transamerica violated ERISA by charging certain fees, collecting revenue-sharing payments, failing to invest in the lowest-priced share class and negotiating lower fees without passing the savings on to plaintiffs. Transamerica moved to dismiss, claiming it did not function as a fiduciary concerning the terms of its own compensation. The district court denied the motion and certified three classes of plaintiffs based on the alleged violations. Transamerica appealed.

On appeal, the 9th Circuit outlined the role that employers and others play as fiduciaries under ERISA, in order "to ensure that employees will not be left empty-handed." In assessing Transamerica's alleged breaches, the court divided the action subject of the complaint into "pre-administration" claims, before Transamerica began servicing the plan, and "administration" claims, after Transamerica began servicing the plan. For those pre-administration breaches, the court found that Transamerica did not function as a fiduciary. Per the court, Transamerica did not exercise discretionary control or provide investment advice when it negotiated its own prospective fees and compiled a list of investment options. At that stage, the employers, and not Transamerica, retained the discretion to decide whether to accept the terms as offered by the service provider.

After Transamerica began servicing the plan, plaintiffs claimed that Transamerica violated its duty not to engage self-dealing by receiving revenue-sharing payments from investment managers and withdrawing its own fees from the plan's funds. The court summarily dismissed the first contention on the basis that the revenue-sharing arrangements were fully disclosed pre-administration and the payments did not come from plan assets. As to the withdrawal of its own fees from the separate accounts, the 9th Circuit found that Transamerica did not act as a fiduciary in merely accepting previously bargained-for and fixed compensation. Relying on trust principles and similar rulings in the 3rd and 6th Circuits, the court reasoned that such contractually-fixed payments were an exercise of control only in the "hollowest sense" and thus did not give rise to fiduciary liability.

The 9th Circuit's ruling in *Santomenno* does not significantly alter the landscape of ERISA's law on fiduciaries. As the court made clear, its holding "is narrow." The court simply found that, when a service provider collects definitively calculable and nondiscretionary fees out of plan funds, in strict adherence with governing contractual terms, it does not breach its fiduciary duty. As the court discussed, had plaintiffs alleged that Transamerica exercised its discretion to change its fees, to withdraw more than entitled, to charge fees based on self-reported hours, or to withdraw expenses, then it would be a "different case." *Cf. IT Corp. v. Gen. Am. Life Ins. Co.*, 107 F.3d 1415, 1417-18 (9th Cir. 1997) (finding that a service provider who "had checkwriting authority" to "pay all claims which it has determined to be payable under the agreement" was an ERISA fiduciary). But, because the complaint made no such assertions, plaintiffs' claims were insufficient. Despite this ruling, breach of fiduciary duty claims will continue to play an ever more important role in ERISA litigation, particularly given that some recent developments in the law expand the situations under which a breach of fiduciary duty claim under ERISA may be asserted.

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