

Court Dismisses Excessive Fee Charge - When Parties are Considered Fiduciaries

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A U.S. Court of Appeals has denied a 401(k) plan sponsor's effort to recover funds from its administrator based on an accusation that it had charged participants "excessive" fees. The court, in *McCaffree Financial Corp. v. Principal Life Insurance Company*, rejected the plaintiff's arguments.

Just the Facts

McCaffree and Principal entered into a contract in which Principal provided investment options and associated services to McCaffree employees participating in McCaffree's retirement plan. The contract assessed administrative fees at two levels: 1) for separate accounts containing Principal's own mutual funds, and 2) the administrative charges embedded in the mutual funds themselves.

Five years after entering into this contract, McCaffree filed a class-action lawsuit against Principal. According to McCaffree's theory, because each Principal mutual fund charged its own layer of fees, the additional separate account fees were unnecessary and excessive. The trial court dismissed the claim, finding that Principal wasn't acting as a fiduciary when it negotiated fees with McCaffree.

Fiduciary Status Criteria

The outcome of the case hinged on whether Principal was indeed a fiduciary with respect to the issues raised in the case. Under ERISA, for an entity that's not explicitly named as a fiduciary to hold that status, courts consider the extent to which a party:

- Exercises any discretionary authority or control over the management of the plan and its assets,
- Offers investment advice for a fee to the plan or its assets, and
- Has discretionary authority over plan administration.

Courts assessing ERISA claims must determine whether a person was acting as a fiduciary when taking the action subject to the complaint. In other words, there must be "a nexus between the alleged basis for fiduciary responsibility and the wrongdoing alleged in the complaint." Thus, McCaffree had to prove that Principal had been acting in a fiduciary capacity when it established the fee structure.

Arm's Length Agreement

Perhaps the biggest shortcoming in McCaffree's case is that it had agreed to Principal's clearly described fee structure when McCaffree signed its contract with Principal five years earlier. "A service provider's adherence to its agreement with a plan administrator does not implicate any fiduciary duty where the parties negotiated and agreed to the terms of that agreement in an arm's length bargaining process," the court held.

Under the service agreement, Principal maintained discretionary authority to increase separate account management fees and adjust amounts charged to participants. McCaffree cited that power as evidence that Principal had fiduciary status. The court disagreed, finding that McCaffree failed to plead any connection between this discretion and the complaint's excessive fee allegations.

Careful Scrutiny

With this decision, three U.S. Courts of Appeals have held that adherence to a properly negotiated agreement doesn't implicate a service provider's fiduciary duty. Thus, plan sponsors must carefully scrutinize fee structures during contract negotiations, a responsibility they should already be taking seriously.

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