THE WAGNER LAW GROUP

A PROFESSIONAL CORPORATION

ERISA Litigation Update

ERISA, Employee Benefits and Executive Compensation Law

March 2010

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In this issue of our newsletter, we explore the litigation spawned by the Hecker v. Deere lawsuit and review the major cases that have recently settled.

Best regards,
Marcia Wagner

Deere and Its Offspring

Hecker v. Deere

When last examined, the dismissal of plaintiffs' claims in Hecker v. Deere had been affirmed in a landmark opinion by the Seventh Circuit Court of Appeals. The plaintiffs had argued that Deere, which sponsored a 401(k) plan for its employees, had committed a fiduciary breach by providing plan investment options with excessive and unreasonable fees and that these fees had not been adequately disclosed to plan participants. In February 2009, the appellate court affirmed dismissal of these claims by the district court, and in June 2009 it denied a petition for rehearing, at which time it took the opportunity to issue an addendum to its original opinion that some thought narrowed the scope of the defendants' victory. On January 19, 2010, the U.S. Supreme Court declined to review the case, so for the moment, Deere stands as precedent which must be followed in the Seventh Circuit (Illinois, Indiana and Wisconsin) and which may be followed by courts elsewhere.

Loomis v. Exelon

Loomis v. Exelon Corp., 2009 WL 4667092 (N.D. Ill., Dec. 9, 2009) is an example of an excessive fee case that closely followed Deere and resulted in dismissal. Plaintiffs' claims alleged excessive fees and nondisclosure of revenue sharing and were, therefore, similar to the claims made in Deere. Exelon's plan offered nineteen retail and wholesale investment funds with fees from 0.03% to 0.96%, whereas the range of fees in Deere's 25 funds was slightly higher. While the Loomis plaintiffs argued that the funds were more expensive than they needed to be and that no additional services were rendered to the plan in exchange for the additional expense, the court noted that there was no allegation that the funds were unsound

The Wagner Law Group News

We have had a few articles published during the past two months and have been quoted as well. I am delighted to announce that an outstanding attorney, John Sohn, has joined the Firm. During the next two months we have a number of speeches. Please let me know if we can speak to your organization.

Marcia Wagner

Managing Director

The Wagner Law Group

A Professional Corporation

Specializing in ERISA, Employee Benefits and Executive Compensation Law

Upcoming Speeches in April & May

Marcia will be speaking at the **ASPPA Benefits Council of New England** on Avoiding Conflicts of Interest as You Grow Your Business. (April 6th)

She will be talking at **Eaton Vance** on on Benchmarking Services. (April 8th & April 29th)

The **New England Employee Benefits Council's** conference, Helping Retirement Plan Participants Reach their Goal, is the setting for

or reckless. As a result, the court held that the case was "indistinguishable" from Deere and warranted dismissal.

Braden v. Wal-Mart

Two weeks before the Loomis case was decided, the neighboring Eighth Circuit Court of Appeals took a decidedly different tack.   In Braden v. Wal-Mart Stores, Inc., 2009 WL 4062105 (8th Cir., Nov. 25, 2009) the famous retailer was charged with breaching its duties of prudence and loyalty by selecting retail class mutual funds as plan investment options. These funds were generally more expensive than institutional class funds and the plaintiffs' complaint compared the plan's investment options with less expensive funds available in the marketplace. However, in October 2008, the district court held that this was not sufficient to allow the action to move forward, because there were no factual allegations that Wal-Mart had failed to investigate the funds or that the fund selection process was otherwise flawed. The district court reasoned that the mere existence of less expensive funds did not mean that the actual selection of more expensive funds was a breach of fiduciary duty. The court also dismissed claims that Wal-Mart had committed prohibited transactions involving revenue sharing, since revenue sharing is not inherently illegal or unreasonable. Finally, the district court dismissed the claim that Wal-Mart had failed to provide participants with complete and accurate information, since there was no duty to disclose revenue sharing and the information the plaintiffs sought was not material.

On November 25, 2009, the Eighth Circuit Court of Appeals vacated the district court's judgment and remanded the Wal-Mart case to the lower court for further proceedings. Generally, the appeals court faulted the lower court for imposing on the plaintiffs an overly rigorous standard of pleading. It concluded that the district court had drawn too many inferences in favor of the defendants and incorrectly placed on the plaintiffs the burden of rebutting possible lawful explanations as to why higher-cost mutual funds had been selected as plan investment options.

The Eighth Circuit held that the complaint's allegations, read as a whole, plausibly stated a claim that Wal-Mart's selection process for plan investment options was flawed. These allegations included assertions that: (1) a plan the size of the Wal-Mart plan (one million participants and nearly $10 billion in assets) had the ability to obtain institutional class shares, but, instead, offered its participants higher-cost retail shares; (2) the majority of Wal-Mart plan funds charged 12b-1 fees; (3) the more expensive funds were retained even though they did not meet their performance benchmarks; and (4) funds made revenue sharing payments to the plan trustee, not for trustee services, but to be included in the investment line-up.

The Eighth Circuit distinguished Deere on the ground that the plan in Deere provided access to over 2,500 mutual funds through a brokerage window, making it untenable to suggest that all of such investment options had excessive expense ratios. In contrast, the Wal-Mart plan offered a far narrower range of investments, making it more plausible that the Wal-Mart plan was imprudently managed.

On the disclosure issue, the Eighth Circuit held that plan fiduciaries are required to furnish plan participants with material information that could adversely affect the participants' interests in the plan and that a reasonable person could find that such material information includes the fact that plan funds charged higher fees than comparable funds to which an employer, such as Wal-Mart, had access.

As to the plaintiffs' prohibited transaction claim involving the receipt of undisclosed amounts of revenue sharing funds by the plan trustee, the Eighth Circuit held that that the complaint alleged sufficient facts to declare an arrangement amounting to the provision of services to a another presentation by Marcia. (April 16th)

At the **ING 401(k) Mid-Market Conference**, Marcia will talk about benchmarking for 401(k) plans. (April 21st)

Marcia will be speaking at an **Oppenheimer Funds** conference on Evolving Best Practice emerging from ERISA litigation. (April 26th)

The **Internal Revenue Service** has tapped Marcia to be a panelist at a Continuing Professional Education seminar. (May 18th)

Since 2007 Marcia has served on the **Internal Revenue Service Advisory Committee on Tax Exempt and Government Entities** and is the 2010 Chair of the Employee Plans Section of the Advisory Council, which provides advice and consultation to the IRS on pension matters. In 2010 the consultation is on favorable letters and qualified plans. In 2009 the focus was on international pension tax laws and in 2008 plan compliance.

John Sohn Joins Firm as Senior Associate

John J. Sohn has joined the firm as a Senior Associate. Sohn, who graduated from Harvard Law School in 1994, has had a 15-year career exclusively in employee benefits and

plan by a party in interest, and that this shifted the burden to Wal-Mart to show that no more than reasonable compensation was paid. The court observed that the trust agreement between Wal-Mart and the trustee required that the amount of revenue sharing be kept secret and that, in view of their monopoly on information, the defendants were in the best position to demonstrate the absence of self-dealing.

The Wal-Mart decision had an immediate effect. Thus, the plaintiffs in the Second Circuit case of Taylor v. United Technologies, 2009 WL 4255159 (2nd Cir., 2009) whose appeal of a lower court dismissal had been denied on December 1, 2009, petitioned for a rehearing by the Second Circuit in light of Wal-Mart which had not been considered in the United Technologies decision. In the Wal-Mart case itself, the defendants' petition for rehearing was denied on January 5, 2010.

George v. Kraft Foods

George v. Kraft Foods Global, Inc. 2010 WL 331695 (N.D. Ill. Jan. 27, 2010) is a case in which the defendants successfully relied on Deere to obtain summary judgment. However, equally important, it shows the benefits of engaging in a prudent decision making process. This case is referred to as Kraft I to distinguish it from a similar but separate lawsuit (Kraft II).

The claims in Kraft I were similar to those of other 401(k) fee cases, i.e., various plan administrative and investment bodies and their individual members had breached their fiduciary duties by (i) structuring the company stock funds as unitized funds, (ii) paying excessive recordkeeping fees, (iii) failing to properly account for float retained by the trustee, and (iv) failing to adequately disclose plan fees and expenses.

The plaintiffs argued that the cash in the unitized company stock funds reduced investment returns and that such funds unfairly imposed the transactional costs incurred by frequent traders on all participants. However, the court concluded that the defendants' internal discussions showed that they had properly considered the pros (e.g., the ability to trade without delay) and cons of offering the stock as unitized funds and that these discussions were evidence of fiduciary prudence.

The court also observed that participants had the ability to select at least seven investment alternatives other than the company stock funds. Based on Deere, it ruled that, in the absence of evidence that an investment alternative is "unsound or reckless, the provision of a large number of investment alternatives, with disclosures allowing participants to make an informed decision as to their investment choices, would preclude a finding that defendants breached their fiduciary duties."

The Kraft I plaintiffs also argued that the defendants were responsible for allowing the plan to pay $28 million in excessive recordkeeping fees and were deficient in failing to request an RFP when deciding to renew the plan's recordkeeping arrangement with Hewitt. The court also rejected this argument, concluding that an RFP is not always necessary, particularly when the defendants had used consultants to benchmark Hewitt's fees and services. Once again focusing on the defendants' procedure, the court found that "based on the number of times they reviewed and renegotiated their contract with Hewitt and their utilization of various standard industry methods to determine the reasonableness of Hewitt's fees," there was no triable issue as to whether defendants used a reasonable decision-making process in making their contracts with Hewitt.

As to the claim that recordkeeping fees were inadequately disclosed, the court, again resorting to Deere, concluded that the critical information was the total fee charged by an investment option and that the quarterly reporting of investment option expense ratios, in which compensation law.

John will continue his work designing employee benefit plans, negotiating with the IRS on qualified retirement plans and representing clients in audits with the IRS, DOL and PBGC.

"John's extensive experience in ERISA and his work with the governing agencies gives The Wagner Law Group even more in-depth expertise to bring to our clients," says Marcia Wagner.

John is also responsible for all aspects of ERISA Title I investment matters, including prohibited transaction exemptions, trading, custody, registered investment advisers and retirement platforms.

Articles & Quotes

PlanSponsor.com quoted Marcia regarding the DOL's rule for providing investment advice to participants in the March 13th on-line issue.

Russell Gaudreau's white paper, Executive Retirement Benefits in the Non-Profit Sector, appeared in BNA's Executive Compensation Library on the Web on March 8th. Crain's New York Business printed the white paper in their February 23rd on-line issue.

Dow Jones News Service quoted Marcia in the article Practice Management: New Rules Likely to Shake Up IRA Advice in the March 3rd on-line issue.

Marcia and Senior Associate John Sohn wrote an article, Best Practices Evolving from 401(k) Fee Litigation, which appeared in the February issue of 401(k) Advisor.

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recordkeeping fees were embedded, was sufficient for this purpose. Further recordkeeping fees were disclosed on the Plan's Form 5500. Thus, the defendants' fiduciary duties with regard to disclosing recordkeeping fees had been satisfied.

Finally, the Kraft I plaintiffs argued that the defendants had not obtained enough information about the trustee's (State Street Bank & Trust) float program to make an informed decision about State Street's compensation, as required by Department of Labor guidance. The court, however, concluded that the defendants had acquired adequate information about the float from State Street's invoices which indicated the circumstances in which float would be earned and retained as compensation, when float periods would begin and end, and the nature of the interest rate that would be applied to determine the float. While the invoices did not show float amounts, this was furnished by annual reports. Further, there had been at least one meeting with State Street to discuss float. Thus, defendants had not breached their fiduciary duty by allowing State Street to receive part of its compensation as float.

A Season for Settlement

Caterpillar Settlement

In Martin v. Caterpillar, No. 07-cv-1009 (C.D. Ill.), the plaintiffs' claims were typical of 401(k) fee litigation in that they alleged a breach of fiduciary duty arising from investment options with excessive and unreasonable fees and the failure to make adequate disclosures to plan participants. In addition, the plaintiffs alleged self-dealing arising from the plans' offering investment options that were advised by a wholly-owned Caterpillar subsidiary. The court had previously upheld the viability of the central complaint that the defendants had charged excessive fees, although it agreed with the defendants and the court in Deere that ERISA does not require plan fiduciaries to disclose revenue sharing.

On November 5, 2009, the Caterpillar parties announced a $16.5 million settlement of the case without the admission of any wrongdoing by the defendants. The net proceeds of the settlement (after deduction of attorneys' fees, expenses and settlement administration) will be allocated to the accounts of participants and former participants based on the length of time that a participant maintained an account in one of the Caterpillar plans. Distributions to the class will begin after the court grants final approval of the settlement and all appeal rights have been exhausted.

As part of the Caterpillar settlement, the parties agreed that during a two-year settlement period, Evercore Trust Company, an independent fiduciary, will monitor the Caterpillar plans. Further, during this period, retail mutual funds will not be included as core investment options under the plans. The use of retail mutual funds, which generally have a higher fee structure than wholesale funds, separate accounts and collective trusts, is a common complaint in 401(k) fee cases. The Caterpillar settlement, once again, raises the question of whether plan sponsors should be using such funds if other investment options are available.

During the two-year settlement period, Caterpillar must also increase and enhance communications with employees about 401(k) investment options and associated fees and continue to limit its cash holdings in the company stock fund investment option. Caterpillar will undertake a request for proposal to select or retain the plans' recordkeeper. Further, if service contracts come up for renewal, Caterpillar will undertake requests for proposal.

An independent fiduciary must review and approve the settlement on behalf of the affected executive compensation and employment practice.

Established in 1996, The Wagner Law Group has 15 attorneys engaged exclusively in employee benefits law. The firm is among the largest ERISA boutiques in the country. Our practice is national in scope, with clients in more than 30 states and several foreign countries.

Services We Provide for Our Clients

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- Welfare Benefit Plans
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- Administrative Representation

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plans. Some wondered whether the settlement would encourage further 401(k) fee litigation while motivating some plan sponsors to settle their own cases. The early answer seems to be in the affirmative.

Hartford Settlement

Hartford Life Insurance Company has thrown in the towel in its long-running dispute with a group of disaffected plan trustees over allegations that Hartford had received certain payments from mutual funds that were actually made in exchange for offering the funds as investment options under Hartford's variable annuity contracts, rather than for Hartford's rendering of administrative services. The trustee plaintiffs claimed that this was a breach of fiduciary duty, as well as a prohibited transaction. In April 2006, the district court had denied the defendants' motion for summary judgment, holding that there were triable issues of fact on whether Hartford was an ERISA fiduciary by virtue of its authority, whether or not exercised, to eliminate and substitute underlying investment options, or, alternatively, based on revenue sharing payments that might be plan assets. More recently, in November 2009, the court had granted plaintiffs' motion for class certification.

Under the terms of the settlement, Hartford will deposit $13,775,000 in a fund to be divided among the 401(k) plans that used Hartford as a service provider from November 14, 2003 through the date the settlement is approved. An additional $300,000 will be paid for administrative costs in effectuating the settlement.

Hartford is also required to make a number of changes to its business practices relating to the allegations made by the plaintiffs. Accordingly, under the settlement, Hartford will eliminate language in its plan documents that restricts the type of property in which plan assets may be invested and will not enforce such language as a means of restricting the selection of investment options from the overall menu. In addition, Hartford will not enforce language in its annuity contracts or funding agreements that would otherwise allow it to invest assets in short-term money market instruments, cash or cash equivalents and will revise such contracts and agreements to clarify that Hartford does not have the right to substitute other investment options for those chosen by a plan, except in certain narrow circumstances, such as the unavailability of the option. The Hartford settlement further provides that all dividends and capital gains distributions on the shares of any mutual fund will be paid as additional shares of that fund, if available, and that Hartford will disclose such fact, as well as provide for customer instruction on the issue.

On the issue of revenue sharing, the Hartford settlement provides that new and existing customers will receive disclosure documents explaining that all of the mutual fund investment options on the Hartford overall menu make revenue sharing payments to Hartford or its affiliates. Further, Hartford must make available a list of all investment options offered to each particular plan, as well as the revenue sharing rate for such options, the published expense ratio for each option, an estimate of the dollar amount of revenue sharing per plan, an explanation of how the estimate was calculated, a narrative description of the revenue sharing and certain fees broken out by participant.

The foregoing changes are to be implemented within 60 days of the settlement's effective date.

Other Settlements

Other recently negotiated resolutions of private litigation include final approval of a $35 million settlement on January 29, 2010 in In Re Marsh Litigation, S.D.N.Y., No. 04 Civ. 8157 (CM), a stock drop case brought by employees of Marsh McLennan Companies stemming from the New

York Attorney General's charges in 2004 that Marsh had defrauded clients by steering business to select third-party insurance providers in order to maximize Marsh's receipt of contingent commissions from those providers. The Attorney General's action resulted in an $850 million settlement and generated substantial negative publicity, causing the value of Marsh's stock to decline by 38%. Nevertheless, the judge presiding over the employee lawsuit noted that settlement by the employees was justified, in part, by the fact that very few stock drop cases have gone to trial and that those that have been tried resulted in employer victories.

On December 1, 2009, the plaintiffs in Hochstadt v. Boston Scientific Corp., 08 Civ. No 12139 filed a motion for approval of an $8.2 million settlement of fiduciary breach claims in a stock drop case involving the company stock fund that was offered as an investment option in that company's 401(k) plan.

Even though they do not shed much light on the standards of legal culpability, we would be remiss not to mention the various settlements that State Street Bank & Trust Company has entered into with regard to losses experienced by retirement plan investors exposure to subprime-mortgage backed securities. On February 4, 2010, a $313 million settlement was reached with the SEC and Massachusetts regulators. The gist of the SEC's complaint was that "State Street led investors to believe that their investments were more diversified than a typical money market portfolio, when instead they were invested almost entirely in subprime investments that ultimately caused hundreds of millions of dollars in losses." Moreover, State Street selectively disclosed information about the problem to specific investors, including internal advisory groups that used the information to redeem their clients' investments in the fund, leaving the money market fund with largely illiquid holdings, causing it to be unable to pay less well-informed investors. The settlement money will go to pay a civil penalty of $50 million and to establish a fund for the benefit of harmed investors.

The State Street settlement with the SEC was said to be in addition to nearly $350 million that the bank had previously agreed to pay to settle private claims. It appears that this contributed to the relative leniency of its treatment by the regulators. Presumably, such private claims included an $89.75 million settlement on behalf of retirement plans of the Massachusetts-based Merrimack Mutual Fire Insurance Company and New York-based Unisystems, Inc. that was announced on September 21, 2009 in the US District Court for the Southern District of New York. Recovery was said to be about 58% of the losses caused by State Street's mismanagement.