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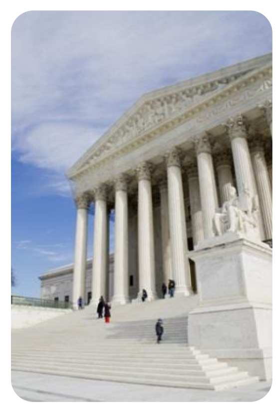
Supreme Court to Consider Statute of Limitations and Scope of Duty to Monitor Investments in ERISA Fiduciary Breach Case

At the urging of the US solicitor general, on October 2 the Supreme Court agreed to hear arguments in a case on how ERISA's statute of limitations provisions apply to fiduciary breaches related to the retention of imprudent investments.

Background



ERISA requires plan fiduciaries to prudently administer employee benefit plans in accordance with the plan terms, and do so for the exclusive benefit of participants and beneficiaries. ERISA's "Limitation on Actions" provision under section 413 states that when suing a fiduciary for a breach or violation, if the plaintiff had no actual knowledge of a breach and there was no fraud or concealment, legal action must be brought within six years from the date of the last action that constituted a part of the breach (or in the case of an omission, within six years from the latest date on which the fiduciary could have cured the breach). However, if the plaintiff had actual knowledge of the breach, legal action must be brought sooner — within three years of obtaining such knowledge. If fraud or concealment was involved, plaintiffs only need to bring an action within six years of the date they learned of the breach.

A Brief Overview of the Case

In *Tibble v. Edison*, the plan fiduciaries included certain retail-class mutual fund shares in their defined contribution plan's investment menu when otherwise identical institutional-class mutual fund shares were available at a lower cost. Though three of the six retail-class funds that were challenged by the plaintiffs were initially selected within the six-year limitation period before the suit was brought, the other three were initially selected more than six years earlier.

For the three funds initially selected during the six-year limitation period, the district court found that the plan's fiduciaries breached their duty to participants and beneficiaries by offering the retail-class funds without investigating the possibility of using institutional-class funds. However, for the three funds initially selected before the six-year limitation period, the district court found that there was no breach of fiduciary duty since the initial decision to use retail-class shares was time barred by the statute of limitations. And with regard to the on-going duty to monitor the plan's investments, there was no subsequent "triggering event" that required the fiduciaries to re-examine their decision to offer the higher cost shares.

The US Court of Appeals for the Ninth Circuit agreed with the district court, finding that the initial designation of an investment for inclusion in the plan's menu started the six-year limitations period, and that the retention of the retail-class funds thereafter was neither an omission nor "a continuing violation" that would allow a claim to be filed six years from the last date the fund was offered under the plan.

The plaintiffs petitioned the Supreme Court to hear the case. The Court asked the US solicitor general for its opinion, and the solicitor general recommended that the Court review the statute of limitations issue. Despite the arguments of the defense, who filed a supplemental brief in opposition, the Court has agreed to review the statute of limitations issue.

US Solicitor General: View Statute of Limitations in Light of Trust Law and Continuing Duty to Monitor Investments

The US solicitor general submitted a "friend of the court" brief to the Supreme Court, urging the court to hear an appeal on the statute of limitations issue to resolve a circuit split among US Circuit Courts of Appeal.

The solicitor general argued that a fiduciary's duty with regard to investments does not end when an investment is initially selected, and that a fiduciary must also periodically monitor the performance and fees of plan investments — investigating alternative investment options and removing funds that charge excessive fees. The brief further stated that such monitoring must be undertaken routinely to ensure prudence — even if no external event arises that prompts such a review.

In its view, the Court of Appeals failed to consider that ERISA expressly authorizes suits for both affirmative acts and omissions, and that a failure to remove an investment within the limitation period is an omission for which a plaintiff can bring suit to recover losses that were incurred within the limitation period. Accordingly, the solicitor general concluded that the plaintiffs should have had at least six years from the latest date the fiduciary could have cured the breach resulting from the retention of "imprudent" investments (i.e., the higher cost retail-class shares in this case).

Furthermore, the solicitor general said that under trust law on which ERISA is based, fiduciaries have a continuing duty to review investments through the life of the trusteeship and to sell imprudent trust investments. The question is not whether there is a "continuing violation," but rather whether there is a "continuing duty" of prudence.

Anatomy of a "Circuit Split"

As with any federal circuit split, appeals courts in different circuits have come down on opposite sides of an issue involving federal law. The following is a summary of the federal appeals court cases cited by the solicitor general as supporting arguments on each side of the statute of limitations case at hand.

Cases Supporting the Defense. In 2013, the Fourth Circuit decided in *David v. Alphin* that the statute of limitations barred a claim that Bank of America's 401(k) plan fiduciaries failed to remove or replace imprudent funds, reasoning that in the absence of a material change in circumstances after the initial selection, such a claim was really a challenge to the initial selection of funds (for which the statute of limitations had expired). In 2014, the Eleventh Circuit cited the David v. Alphin case (among others) in deciding *Fuller v. Suntrust Banks, Inc.*, which similarly held that a failure to replace certain allegedly imprudent funds was "not a distinct, cognizable breach from the alleged breach that occurred at selection."

Cases Supporting the Plaintiffs. By contrast, the appeals court cases cited by the solicitor general as holding that fiduciaries can be held liable for breaching their duty to monitor investments did not directly address the statute of limitations for claims on the selection of 401(k) plan investments. In a 1977 case, *Morrissey v. Curran*, the Second Circuit held that a plan fiduciary was liable for keeping an imprudent investment that was first selected before ERISA was enacted because retaining that investment became an ongoing breach of the duty of prudence under ERISA once ERISA became effective. The solicitor general's brief acknowledged that the court's decision in *Morrissey v. Curran* was not really about the statute of limitations. Instead, the Morrissey case centered on whether a federal court had ERISA subject matter jurisdiction over an ongoing fiduciary breach that resulted from investment decisions (and misappropriations of plan funds) that initially occurred prior to ERISA's enactment. In 1992, the Seventh Circuit's decision in *Martin v. Consultants & Administrators, Inc.* held that a health and welfare plan fiduciary's renewal of an imprudent service provider contract was not barred by the statute of limitations, finding that "a past violation should not be held to preclude a suit for a repeated and continued violation."

In Closing

We expect that the Supreme Court's decision (likely to be announced in June 2015) will help clarify the standards of prudence applicable to all participant-directed 401(k) plans under ERISA, and that the decision has the potential to influence the conduct of plan fiduciaries for years to come.

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