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BENEFITS & COMPENSATION UPDATE

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Supreme Court Decision Offers Guidance on 401(k) Plan Fiduciaries' Duty of Prudence With Respect to Plan Investments

The Supreme Court recently issued its unanimous decision in *Hughes v. Northwestern University*, a case concerning whether fiduciaries of Northwestern University's defined contribution retirement plan breached their duty of prudence by failing to adequately monitor plan investments. The Supreme Court reiterated that plan fiduciaries have an ongoing duty to monitor plan investments and held that offering participants a wide array of investment options does not itself excuse the inclusion of allegedly imprudent choices in the plan's investment lineup. This decision is a reminder to 401(k) plan fiduciaries of the importance of (i) regularly reviewing each option in a plan's investment lineup and (ii) adopting formal policies and benchmarks for evaluating plan investments and terminating imprudent ones.

Background on 401(k) Plan Fiduciaries' Duty of Prudence with Respect to Plan Investments

Under ERISA, plan fiduciaries must act prudently when selecting and monitoring plan investments. In this regard, it is good practice for fiduciaries to retain professional investment advisors to assist them in carrying out their duties.

In the context of a defined contribution plan where participants choose how to invest their funds among various options selected by the plan's administrator, the element of participant choice does not relieve fiduciaries from their responsibility (i) to establish governance procedures and performance benchmarks and standards for selecting, evaluating and, if necessary, removing options from the plan's investment lineup and (ii) to ensure the reasonableness of administrative and investment fees associated with the investment options provided for under the plan. Fiduciaries must also provide participants with a range of investment options that allows participants to make choices tailored to their individual return objectives and risk tolerance. However, the composition of the plan's menu of investments should not be so complex that the plan's participants have difficulty navigating those options.

Plaintiff's Claims and Lower-Court Decisions

Plaintiffs alleged that the fiduciaries of Northwestern University's retirement plan breached their fiduciary duty of prudence by including in the plan's investment lineup funds with management and administrative fees higher than those of nearly identical alternatives. In dismissing the plaintiffs' claims, both the district court's and appellate court's rulings relied on the fact that participants could have invested in the low-fee funds included in the plan's extensive investment offerings. Because participants ultimately chose how to direct their investments, the lower courts reasoned, the plaintiffs could have availed themselves of the plan's various low-fee options and were therefore not harmed by the inclusion of allegedly imprudent funds in the plan's lineup.

The Supreme Court's Holdings

The Supreme Court rejected the lower courts' conclusion that the plaintiffs' control over how to direct their investments barred their fiduciary breach claims as a matter of law. Instead, the Supreme Court instructed the Seventh Circuit to evaluate the plaintiffs' claims in light of the principles the Supreme Court articulated in its 2015 decision *Tibble v. Edison International*. In that case, which also involved allegations that fiduciaries had included imprudent investments among a defined contribution plan's investment options, the Supreme Court held that ERISA's duty of prudence requires fiduciaries to regularly review plan investments and timely remove imprudent ones from the plan's roster. In other words, the duty of prudence requires more than offering plan participants a broad array of investment options, as fiduciaries must also monitor and evaluate each such option on an ongoing basis and take appropriate action with respect to imprudent investments in the plan's lineup.

The Supreme Court also instructed lower courts to take a "context specific" approach when evaluating allegations that fiduciaries breached their duty of prudence. The decision concludes that "[a]t times, the circumstances facing an ERISA fiduciary will implicate difficult tradeoffs, and courts must give due regard to the range of reasonable judgments a fiduciary may make based on her experience and expertise."

Key Takeaways for Fiduciaries

The decision in *Hughes v. Northwestern University* reiterates the importance of following good fiduciary practices with respect to plan investments. Fiduciaries should regularly review and monitor plan investments, including associated fees, in accordance with their plan's established protocols and procedures. In this regard, fiduciaries should ensure that benchmarks and standards for evaluating investments and fees are formalized in their plan's investment policy statement and/or other applicable governance documents. Moreover, such regular review should be adequately documented in the plan's records in order to demonstrate that fiduciaries are prudently monitoring plan investments.

If you have any questions or would like any assistance with respect to your 401(k) plan's procedures and protocols governing the investment options under the plan, please contact:

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