

AUGUST 13, 2018

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In Closely Watched Mutual Funds Case, 8th Circuit Sets High Bar For Labeling Retirement Plan Investments ‘Imprudent’

Mutual Fund Challenges Must Allege Poor Performance Against Meaningful Benchmarks to Avoid Dismissal

In *Meiners v. Wells Fargo & Company*,¹ the U.S. Court of Appeals for the Eighth Circuit clarified the burden plaintiffs must meet to state a claim for breach of fiduciary duty under the Employee Retirement Income Security Act (“ERISA”) based on the inclusion of allegedly underperforming and expensive investment funds. Because plaintiffs often lack detailed information about the process plan fiduciaries followed to make investment choices, pleading a plausible claim that those fiduciaries have acted imprudently can pose a significant challenge. But the Eighth Circuit refused to water the pleading standard down to account for this reality in *Meiners*. Rather, the Eighth Circuit held that “[t]o show that ‘a prudent fiduciary in like circumstances’ would have selected a different fund based on the cost or performance of the selected fund, a plaintiff must provide a sound basis for comparison—a meaningful benchmark.”² As one of the first appellate decisions to tackle this thorny issue head on, litigants should expect *Meiners* to be cited as persuasive authority beyond the Eighth Circuit.

BACKGROUND

ERISA class action litigation challenging mutual fund fees and performance has been on the rise since the Supreme Court’s 2015 decision in *Tibble v. Edison International*,³ which confirmed that plan fiduciaries have a continuing duty to monitor investment options and remove imprudent ones. But *Tibble* also left open the question of what exactly is the scope of the fiduciary duty to monitor, and thus, what is



required to plead a viable claim that duty has been violated.⁴ *Meiners* at least partially answers that question.

In *Meiners*, a participant in Wells Fargo's 401(k) plan accused plan fiduciaries of favoring Wells Fargo's own target date funds as investment options, rather than offering cheaper and better performing alternatives, such as Vanguard target date funds.⁵ In particular, the plaintiff alleged that the Wells Fargo plan fiduciaries sought to maximize their own profits by generating fees and "seed" money for their underperforming funds.⁶

The district court dismissed the complaint because the plaintiff's comparison to Vanguard funds was insufficient to show that the performance and fees of the Wells Fargo funds rendered them imprudent investment choices.⁷ After reviewing fund prospectuses, the district court held that investors would expect the Wells Fargo and Vanguard funds to perform differently because they have different investment strategies (the Wells Fargo funds have a higher bond allocation).⁸ The district court also held that the plaintiff failed to establish cheaper Vanguard and Fidelity funds as reliable comparators, *i.e.*, ones that offer similar services or are of similar size.⁹ Finally, the district court found that the plaintiff did not show that the Wells Fargo funds are more expensive "compared to the market as a whole."¹⁰

THE EIGHTH CIRCUIT'S OPINION

The Eighth Circuit affirmed the district court's dismissal. The court acknowledged that plan participants have "different levels of knowledge regarding *what* investment choices a plan fiduciary made as compared to *how* a plan fiduciary made those choices."¹¹ But, because "ERISA plaintiffs typically have extensive information regarding the selected funds," they are expected to marshal that information and "provide a sound basis for comparison—a meaningful benchmark" by which to evaluate the cost or performance of the challenged funds.¹² And failure to do so equals failure to state a claim under the plausibility standard articulated by the Supreme Court in *Twombly* and *Iqbal*.¹³

As a result, the Eighth Circuit agreed with the district court that comparing an allegedly underperforming fund to one with a different investment strategy does not say anything about whether it was an imprudent choice.¹⁴ Nor is it enough to allege that "cheaper alternative investments with *some* similarities exist in the marketplace."¹⁵ Indeed, the Eighth Circuit made clear that its prior decision in *Braden v. Wal-Mart Stores Inc.*¹⁶ (which involved a comparison to cheaper share classes of the same funds) should not be read to support such a watered-down pleading standard.¹⁷ Finally, in considering whether the plaintiff's examples met the "meaningful benchmark" standard, the Eighth Circuit affirmed the district court's close analysis of fund prospectuses that were not attached to the complaint, finding that they were "necessarily embraced by the pleadings."¹⁸

The Eighth Circuit recognized in *Meiners* that the analytical rigor of its decision contradicted some earlier (unidentified) district court decisions supporting the plaintiff's position.¹⁹ Calling into question "the rationale of these cases," the Eighth Circuit explained that "the existence of a cheaper fund does not mean that a particular fund is too expensive *in the market generally* or that it is otherwise an imprudent choice. Any other conclusion would exempt ERISA plaintiffs both from pleading benchmarks for the funds and from pleading internal processes about selecting funds."²⁰ And because the plaintiff in *Meiners* had failed to plead a plausible claim of imprudence based on comparison of the Wells Fargo funds to meaningful benchmarks, the Eighth Circuit determined that it could not reasonably draw any inference that the plan fiduciaries had retained the challenged funds out of improper motives.²¹ Thus, even in so-called "proprietary fund" cases like *Meiners*, the Eighth Circuit held that ERISA plaintiffs are required "to pair allegations of self-interest with allegations of an imprudently chosen fund in order to survive a motion to dismiss."²² Without first establishing that a fund is an imprudent choice based on comparison to an analytically rigorous benchmark, a plaintiff is not entitled to discovery to test their conclusory allegations of unlawful motives and conduct.²³



KEY TAKEAWAYS

Following *Meiners*, ERISA plaintiffs alleging breaches of fiduciary duty based on fund fees and/or performance now have a clear burden to meet if they wish to avoid dismissal. Plaintiffs should not assume that their lack of access to information about the process that plan fiduciaries use to select and retain investment funds will entitle them to a relaxed pleading standard.

To the contrary, *Meiners* teaches that the identification of “meaningful benchmarks” by which to measure performance and fees will be required to state a plausible claim of fiduciary breach. Absent such benchmarks, “no inference can be reasonably drawn that the [plan fiduciaries] retained those funds . . . out of improper motives”²⁴—not even in so called “proprietary fund” cases.

While *Meiners* involved the employer’s own funds, nothing in the Eighth Circuit’s rationale limits it to that situation. In fact, the same week *Meiners* was decided, a federal district court in New York employed similar reasoning to rule in favor of New York University in a case involving allegedly excessive fees and underperformance.²⁵ In the NYU case, the court identified several additional factors to consider in determining appropriate benchmarks, including the fund’s cash holdings, domestic-foreign allocation, and passive versus active management.²⁶ Following *Meiners*, courts should demand specific allegations about these (and potentially more) factors before allowing ERISA breach of fiduciary duty claims to proceed to expensive and time-consuming discovery. A complaint lacking such analytical rigor should be dismissed for failure to state a claim.

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¹ Slip Op. No. 17-2397 (8th Cir. Aug. 3, 2018).

² *Meiners*, Slip Op. at 5.

³ 135 S. Ct. 1823 (2015).

⁴ *Tibble*, 135 S. Ct. at 1829.

⁵ *Meiners*, Slip Op. at 2.

⁶ *Id.* at 3.

⁷ *Meiners v. Wells Fargo & Co.*, 2017 WL 2303968, at *2-3 (D. Minn. May 25, 2017).

⁸ *Id.* at *3.

⁹ *Id.*

¹⁰ *Id.*

¹¹ *Meiners*, Slip Op. at 4 (emphasis original).

¹² *Id.* at 5.

¹³ *Id.* at 3 (citing *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 557 (2007); *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009)).

¹⁴ *Id.* at 5.

¹⁵ *Id.* at 6 (emphasis original).

¹⁶ 588 F.3d 585 (8th Cir. 2009).

¹⁷ *Meiners*, Slip Op. at 6-7

¹⁸ *Id.*

¹⁹ *Id.* at 7. The plaintiff on appeal had relied on *Gipson v. Wells Fargo & Co.*, 2009 WL 702004 (D. Minn. Mar. 13, 2009); *Wildman v. Am. Century Servs., LLC*, 237 F. Supp. 3d 902 (W.D. Mo. 2017); *Leber v. Citigroup, Inc.*, 2010 WL 935442 (S.D.N.Y. Mar. 16, 2010); *Urakhchin v. Allianz Asset Mgmt. of Am., L.P.*, 2016 WL 4507117 (C.D. Cal. Aug. 5, 2016); *Krueger v. Ameriprise Fin., Inc.*, 2012 WL 5873825 (D. Minn. Nov. 20, 2012); *Moreno v. Deutsche Bank Am. Holding Corp.*, 2016 WL 5957307 (S.D.N.Y. Oct. 13, 2016); *Lorenz v. Safeway, Inc.*, 2017 WL 952883 (N.D. Cal. Mar. 13, 2017); *Terraza v. Safeway, Inc.*, 2017 WL 952896 (N.D. Cal. Mar. 13, 2017); *McDonald v. Edward D. Jones & Co.*, 2017 WL 372101 (E.D. Mo. Jan. 26, 2017); and *Pledger v. Reliance Trust Co.*, 2017 WL 2624302 (N.D. Ga. Mar. 7, 2017).

²⁰ *Meiners*, Slip Op. at 7 (emphasis original).

²¹ *Id.*

²² *Id.* at 8.

²³ *Id.*

²⁴ *Id.* at 7.

²⁵ *Sacerdote v. New York Univ.*, 2018 WL 3629598 (S.D.N.Y. July 31, 2018).

²⁶ *Id.* at *28-30.