

# LESSONS FOR 401(k) PLANS FROM THE UNIVERSITY 403(B) CASES

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## MODERATOR:

**Donald Wellington**, *Reed Smith*, Los Angeles CA

## PRESENTERS:

**Blake MacKay**, *Alston & Bird*, Atlanta GA

**Sara Pikofsky**, *Steptoe & Johnson*, Washington D.C.

**Robert Rachal**, *Holifield · Janich · Rachal · Ferrera*, New Orleans LA

# Program Overview

- Overview and background 403(b) plans:
  - Historical origins and development
  - Some similarities and differences to 401(k) plans
- 401(k) lessons from 403(b) litigation:
  - *Sacerdote v NYU* trial – focus on process
  - *U Penn, Northwestern, and Washington U* – favorable plan facts that may result in case dismissal
- Emerging claims and issues:
  - *Cassell v Vanderbilt* – participant data and service provider marketing
  - *Munro v USC* – arbitration agreements

# Overview & Background 403(b) Plans

# 403(b) Plan Basics

- **What is it?**
  - A 403(b) plan is a retirement plan where contributions are eligible for tax-deferred treatment
- **Who can have one?**
  - Public educational organizations or 501(c)(3) non-profits
- **Also known as...**
  - “Tax-sheltered annuity Plans;” “Tax-deferred annuity Plans;” or “Annuity Contracts”
- **Types of Investments:**
  - Annuity contracts (fixed or variable) through insurance companies (403(b)(1))
  - Custodial account made up of mutual funds (403(b)(7))
  - Retirement income account for church employees (403(b)(9))

# Historical Origins and Development

- **1958:** Section 403(b) added to the Internal Revenue Code.
- **1961:** Section 403(b) extended to cover public education employees
- **1974:** Section 403(b)(7) added to permit mutual funds to be available investment options
- **1982:** Section 403(b) expanded to cover retirement income accounts (Section 403(b)(9)) for employees of church organizations.
- **1986:** Additional restrictions and rules added to make 403(b) plans more similar to 401(k) plans
- **2007:** 403(b) regulations issued requiring written plan document

# 403(b) Similarities and Differences to 401(k) Plans

- Types of investments (Annuities, etc.)
  - 1918: Carnegie Foundation established the Teachers Insurance and Annuity Association, now known as TIAA.
- Multiple Record-keepers
- Number of investment options
- Historical cost of various investment options
- Universal Availability requirements for elective deferrals
- Special rules on “catch-up” contributions and service transfer among employer organizations
- Potential donor conflicts, e.g. NYU case

# **Lessons for 401(k) Plans from 403(b) Litigation**

# *Sacerdote v NYU* Trial – Focus on Process

- *Sacerdote v NYU* went to trial. Judgment for defendants being challenged on appeal and because of alleged judicial conflict.
- Prudent process – use of RFPs helped defeat claim paid too much for recordkeepers.
- Prudent process – showed actively monitored under-performing funds.
- Prudent process – investment advisor Cammack gave sound investment advice.
  - But found certain committee members did not understand fiduciary role.
  - Need for fiduciary training and careful selection of committee members.



# Favorable Plan Facts That May Lead to Dismissal

- *U Penn, Northwestern, and Washington U* all had case dismissed. Exception not rule, and cases will be challenged on appeal.
- But some takeaways on facts and practices that help:
  - Providing broad mix of funds, including low-cost index funds.
  - Logical reasons to allow multiple recordkeepers, bundling of funds and recordkeepers
  - Fulsome disclosures of fees and risks.
  - Facts showing monitoring of funds and expenses:
    - Changing recordkeepers, switching to flat fee or imposing caps
    - Eliminating funds that persistently underperform

# Emerging Claims and Issues

# *Vanderbilt and Use of Participant Data*

- *Cassell v Vanderbilt* – Plaintiffs recently added claim that plan fiduciaries allowed service provider TIAA CREF to improperly access participant data for marketing purposes.
  - Claim data was plan asset that fiduciaries did not protect from misuse by TIAA CREF.
  - Also claimed fiduciaries failed to get value for this data.
- Claim allowed to go forth as a class claim, but no decision yet on the merits.
  - Case recently stayed for a mediation.

# Vanderbilt and Use of Participant Data

- Is participant data a “plan asset”?
  - How does it fit within “ordinary notions of property rights”?
  - Is it something fiduciary can use at expense of plan participants?
  - Do economic realities of modern economy (e.g., data driving multi-billion value of Facebook, Google *et al.*) impact this analysis?
  - If it’s a plan asset, what does this mean for fiduciary duties and prohibited transactions?
- What are plans and advisors doing here?
  - Vanderbilt complaint claimed that other plans enforce clear limits on use of this data.

# *USC and Arbitration Agreements*

- Supreme Court has been very pro enforcement of arbitration agreements. Important practical effect is that defendants often use them to bar class actions/class exposures.
- *Munro v USC* – held employment agreement to arbitrate not apply to claim brought on behalf of the plan under ERISA § 502(a)(2).
  - Cert petition filed with Supreme Court.
- Legal issues – include, can you require claims on behalf of the plan to be arbitrated?
- Practical issues – what ERISA claims (if any) do you want subject to arbitration?