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Aon Quarterly Update

Retirement Legal Consulting & Compliance

In this Issue

Editor's Note

by Susan Motter

The country's midterm elections and the approaching holiday season signal we are nearing the close of 2022. As our readers approach the year end, we bring you the latest on the hottest benefit areas that may be of interest, particularly those areas which may require attention before year end or shortly thereafter.

In a bit of a surprise during late summer when regulatory activity is typically slow, the Securities and Exchange Commission issued final regulations implementing certain new pay versus performance (PVP) disclosures in proxy statements. As companies with calendar fiscal years will be first required to make these PVP disclosures in proxies to be issued in early 2023, we open this edition of the *Quarterly Update* with reporting on the new PVP disclosure rules.

Many of our readers have been anticipating year-end 2022 amendments to their retirement plans for certain required and discretionary changes for the SECURE Act, Miners Act, and CARES Act. As the Internal Revenue Service has recently announced extensions of most of the amendment deadlines, we report on these deadline extensions as well as include a link to Aon's much-favored year-end guidance related to retirement plans.

One evolving, hot area of interest to plan fiduciaries of defined contribution (DC) plans is the possibility of investment of plan assets in cryptocurrency. In March 2022, the Department of Labor (DOL) issued subregulatory guidance to plan fiduciaries interested in adding a cryptocurrency option to their DC plans. This edition of the *Quarterly Update* reports on the latest developments on this front—including reaction to the guidance and the recently filed lawsuit challenging the DOL's position on cryptocurrency.

On the regulatory front, we include an article regarding the DOL's proposed amendment to the Prohibited Transaction Class Exemption 84-14, also known as the exemption for qualified professional asset managers (QPAM Exemption). This article is intended to help our readers understand how the QPAM Exemption and the proposed amendment may affect their plans' compliance strategy, investment practices, and procedures.

Our readers have come to trust that we will report the latest on the excessive fee litigation cases involving retirement plans. We include two articles highlighting two interesting cases—one case regarding the possible emergence of a consensus among the circuit courts of appeals in the aftermath of the Supreme Court decision in *Hughes v. Northwestern Univ*. The other case involves allegations that DC plan fiduciaries breached their fiduciary duties when they permitted the DC plan to offer pricier retail shares of mutual funds when those same mutual funds were available as less expensive institutional shares.

The final litigation update we provide in this edition of the *Quarterly Update* relates to the success of Johnson & Johnson (J&J) plan fiduciaries in obtaining a dismissal of a stock-drop complaint involving employee stock ownership subaccounts currently offered in three of J&J's 401(k) plans. We highlight this case as it illustrates the impact of the new enhanced pleading requirements for stock-drop cases after the Supreme Court decision in *Fifth Third Bancorp v. Dudenhoeffer*. The *Dudenhoeffer* case was particularly instructive in that it provided guidance to the lower federal courts to strictly enforce the enhanced pleading requirements for stock-drop complaints.

If you have any questions or need any assistance with the topics covered, please contact the author of the article or Tom Meagher, our practice leader.

Living by Proxy: New SEC Pay Versus Performance Disclosures

by Eric Keener and Lee Nunn

On August 25, 2022, the Securities and Exchange Commission (SEC) issued final regulations implementing new pay versus performance (PVP) disclosures mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act that was enacted in July 2010. These new regulations will require SEC registrants to disclose information in their annual proxy statements regarding the relationship between executive compensation actually paid and the registrant's financial performance.

Proposed PVP regulations were initially issued for public comment in April 2015. The comment period was reopened in January 2022 to request feedback on certain changes to the original proposal. The final regulations, which incorporate comments received by the SEC on the original and revised proposals, are effective for fiscal years ending on or after December 16, 2022. For companies with calendar fiscal years, this means that the new PVP disclosures will first be required in the proxy statement to be issued in early 2023.

The new rules generally require a tabular disclosure of specific executive compensation and financial performance measures for the five most recently completed fiscal years. However, a transition rule allows disclosure for the most recent three fiscal years in the year of implementation, the most recent four fiscal years in the following year, and the most recent five fiscal years thereafter. Executives covered by the new PVP disclosures are the Principal Executive Officers (PEOs) and other Named Executive Officers (NEOs) currently included in the proxy Summary Compensation Table (SCT) and related disclosures.

A new PVP table must disclose executive compensation separately for each PEO, and as an average for all other NEOs. The table does not identify the PEOs or the other NEOs, and these individuals can change from year to year. There may be more than one PEO in a single year. Two measures of compensation must be shown in the table: the amounts reported in the SCT and a measure of compensation "actually paid" that reflects certain adjustments to the amounts reported in the SCT. These adjustments are discussed further below.

Registrants will be required to:

- Report total shareholder return (TSR) for the registrant and the companies in its selected peer group, net income, and a financial performance measure chosen by the registrant as most important for linking compensation actually paid to the registrant's performance for the fiscal year;
- Describe the relationship between executive compensation actually paid and each performance measure;
- Describe the relationship between the registrant's TSR and the TSR of its selected peer group; and
- Provide a list of three to seven financial performance measures that the registrant determines are most important for linking executive compensation actually paid to the registrant's performance.

Scaled disclosure requirements apply for smaller reporting companies.

In determining compensation "actually paid" to an executive for the new PVP disclosures, compensation reported in the SCT that is attributable to pension benefits and equity awards must be adjusted as follows:

- For pension benefits, the SCT includes any aggregate increase in the present value of an executive's accrued benefit under qualified and nonqualified pension plans. The new PVP disclosures subtract these amounts and add in the executive's service cost, and any new prior service cost, as calculated under U.S. Accounting Standards Codification Topic (ASC) 715-30 for the fiscal year.
- For equity awards, the SCT includes the fair value of any equity awards granted during the fiscal year, measured as of the grant date. The new PVP disclosures replace this amount with the fair value as of the end of the fiscal year of any grants made during the year, plus the year-to-year change in the fair value of any prior grants, until the vesting date.

These adjustments will require employers to obtain additional information from their actuaries and equity valuation service providers, beyond the information already provided for the SCT.

The final regulations allow registrants to provide supplemental disclosures, provided that they are clearly labeled as such, are not misleading, and do not obscure the required disclosures. These supplemental disclosures are not mandatory. However, some registrants may want to consider including additional information to help explain the differences between the SCT and the new PVP disclosures, since these differences may be confusing to investors. In addition, it may be helpful to clarify that the amounts reported as compensation "actually paid" for pension benefits and equity awards generally do not represent cash compensation received by the executive.

For example, suppose a registrant has a frozen pension plan and the registrant's PEO has an accrued benefit in the plan. The registrant would report a positive pension compensation amount in the SCT in any year when the present value of the PEO's benefit increases (due to changes in discount rates or other actuarial assumptions). However, the change in present value would not represent cash compensation to the PEO. The pension amount reported as "actual compensation" in the PVP table would be zero, equal to the PEO's service cost under ASC 715-30. Investors may require additional information to better understand these differences.

The new PVP regulations make important changes to the executive compensation disclosures included in the annual proxy statement. SEC registrants should discuss these changes with their actuarial and executive compensation consultants to understand the impact of these rules, ensure that they have the information needed for the current fiscal year and prior fiscal years to implement the rules, and consider additional supplemental disclosures that may be helpful to investors.

A Look Ahead: What's in Store for Plan Amendments?

by Linda M. Lee and Susan Motter

With the rapidly approaching holiday season and the end of the year soon to be fast upon us, it is time for plan sponsors and fiduciaries to review deadlines and consider strategies to mitigate risks and to simplify plan administration.

SECURE Act, Miners Act, and CARES Act Amendments

The deadlines to adopt amendments for the SECURE Act, Miners Act, and CARES Act have generally been extended to December 31, 2025 for nongovernmental qualified retirement and certain 403(b) plans. Governmental plans, certain other 403(b) plans, and plans covering collectively bargained employees may have delayed adoption dates. Specifically, IRS Notices 2022-33 and 2022-45 extend the deadlines to adopt amendments reflecting certain optional and required changes under the SECURE Act, Miners Act, and CARES Act. The extended deadlines depend on the type of plan subject to amendment as we note below:

Type of Plan	Extended Deadline for Plan Amendments
Nongovernmental Qualified Plan	December 31, 2025
Governmental Qualified Plan	Legislative Session-Related Deadline[1]
403(b) Plan Not Maintained by a Public School	December 31, 2025
403(b) Plan Maintained by a Public School	Legislative Session-Related Deadline[1]
Governmental 457(b) Plan	The later of: (i) Legislative Session-Related Deadline;[1] or (ii) if applicable, the first day of the first plan year beginning more than 180 days after the date of notification by the IRS that the plan was administered in a manner inconsistent with the requirements of Section 457(b) of the Internal Revenue Code
Tax-Exempt Organization 457(b) Plan	December 31, 2022 (or, if later, the end of the plan year beginning in 2022)[2]

[1] Legislative Session-Related Deadline means 90 days after the close of the third regular legislative session of the legislative body with the authority to amend the plan that begins after December 31, 2023.

[2] Neither IRS Notices 2022-33 nor 2022-45 address the extension of amendment deadlines for tax-exempt 457(b) plans. Therefore, these plans generally remain subject to the year-end 2022 deadline.

It is noteworthy that although the time to amend a plan may have been extended, plans are required to be operated presently in accordance with applicable statutory changes. Many plan sponsors may find it advisable to amend their plans during the remainder of 2022 so that the plan terms are consistent with plan administration.

What's Next?

Aon has published a detailed **Year-End Amendment Guidance** that summarizes certain recent developments for required and discretionary plan amendments for tax-qualified defined benefit, defined contribution, and other retirement plans, along with some strategies to mitigate plan sponsor and fiduciary risks. We encourage plan sponsors to use this summary to evaluate, in consultation with their retirement plan advisers, how their tax-qualified retirement plans are impacted. Please contact any member of Aon's Retirement Legal Consulting & Compliance practice for assistance with such a review.

Cryptocurrency Funds: Should 401(k) Plans Consider?

by Tom Meagher

Whenever a new investment hits the market, investors (including 401(k) plan participants) are keenly interested in evaluating the product and considering it for their individual portfolios.

With the arrival of cryptocurrency investment funds, there has been a rising level of interest among investment providers and defined contribution (DC) plan participants in the product. Most recently, the providers of cryptocurrency investment funds have begun to approach DC plan sponsors to offer the funds as a new investment option. For example, at least one service provider has partnered with a digital currency exchange platform to offer a cryptocurrency fund within a self-directed brokerage window. The offering allows participants to transfer up to 5% of their account balance directly into more than 50 different cryptocurrencies. Not surprisingly, with all of the attention being given to cryptocurrency investment funds, other service providers and plan sponsors are considering adding such an investment to their plan offerings.

With the popularity of cryptocurrency investing continuing to grow and interest peaking among plan sponsors, the investment itself has raised alarms with the Department of Labor (DOL).

On March 10, 2022, the DOL issued guidance in their Compliance Assistance Release No. 2022-01. This guidance warned plan fiduciaries that if they are considering adding a cryptocurrency option to a DC plan, they must be prepared to demonstrate that they are acting solely in the financial interests of plan participants and that they are adhering to their duty of prudence and loyalty. The DOL guidance went on to note that the DOL had "serious concerns" about the prudence of a fiduciary's decision to expose plan participants to direct investments in cryptocurrencies, or other products whose value is tied to cryptocurrencies. The DOL further noted that, in its view, these investments present significant risks and challenges to participants' retirement accounts due to lack of education and possible fraud, theft, and loss due to volatility. In raising concerns with cryptocurrency investing, the DOL indicated that the assets themselves are not held in a traditional trust or custodial account and are not readily valued or available to pay benefits and plan expenses. Rather, they generally exist as lines of computer code in a digital wallet. Moreover, the DOL expressed concerns with how best to value cryptocurrencies and the impact such volatility would have on participants' retirement accounts.

As part of this guidance, the DOL noted that it expects to conduct an "investigative program" aimed at plans that offer participant investments in cryptocurrencies and related products. The DOL further noted that it would take appropriate action to protect the interests of plan participants and beneficiaries with respect to these investments.

As you might imagine, the DOL "guidance" was not well received by investment fund managers and others looking to access the substantial assets being held in DC plans. In June 2022, one provider, ForUsAll, Inc., filed a lawsuit against the DOL claiming that the DOL breached its statutory authority by threatening "an investigative program" aimed at plan sponsors and fiduciaries that offer cryptocurrency investments through their core plan line-up or self-directed brokerage accounts. The complaint went on to allege that the DOL violated the Administrative Procedures Act by effectively enacting a prohibition on cryptocurrency investments without following the formal rulemaking process (e.g., providing for a notice of proposed rulemaking and a comment period for interested parties). In responding to the lawsuit, the DOL noted that the March 2022 guidance was not necessarily final guidance, the DOL contemplated further agency action, and the guidance was issued more as an "interpretive rule," that would not be subject to the notice-and-comment requirements in the Administrative Procedures Act.

While the DOL guidance does not create new regulations nor does it have any binding effect on plan sponsors or fiduciaries, it does put fiduciaries on notice as to the DOL's view of the investment product. Thus, plan fiduciaries considering a cryptocurrency investment product for their plan should proceed with extreme caution and anticipate developing a strong record to support why such product is prudent and in the best interests of plan participants.

Aon consultants are available to discuss how cryptocurrency and/or the DOL guidance may impact your plan and the risk to plan fiduciaries. We will continue to monitor developments in this evolving area.

DOL Proposes Amendments to QPAM Exemption

by Elizabeth Groenewegen and Mark Manning

In late July, the Department of Labor's (DOL's) Employee Benefits Security Administration proposed an amendment to the Prohibited Transaction Class Exemption 84-14, also known as the exemption for qualified professional asset managers (QPAM Exemption).

The QPAM Exemption presently allows investment managers to engage in certain otherwise prohibited transactions with parties in interest (as defined in the Employee Retirement Income Security Act of 1974 (ERISA)) and disqualified persons (as defined in the Internal Revenue Code (Code)). Many major investment managers serve as QPAMs, and they will need to evaluate the proposed changes should they become final.

The QPAM Exemption allows qualified investment managers to enter into transactions such as loans and extensions of credit, leases, and services between the plan it serves and a party in interest to that plan. Ordinarily, Section 406 of ERISA (and Section 4975 of the Code) would prohibit such transactions and impose sanctions for violations. Congress enacted these prohibitions to protect plans, their participants and beneficiaries, and IRA owners from the risk of abuse that might arise when plans and IRAs engage in transactions with closely connected parties. Recognizing that blanket prohibitions could hamper legitimate functions, Congress also provided the DOL with authority to make exceptions. The DOL exercised this authority in 1984 in promulgating the QPAM Exemption.

In order to qualify for the current QPAM Exemption under present law, the entity must comply with the following:

- The entity must be a bank, a savings and loan, or an insurance company with equity capital or net worth in excess of $1 million, or be a registered investment advisor under the Investment Advisers Act of 1940 with assets under management in excess of $85 million and equity in excess of $1 million;
- The entity must acknowledge its fiduciary status to the client in writing;
- The entity must not have been previously convicted of a felony in the last 10 years affecting trust management (which includes not only the organization, but also subsidiaries, certain other related entities, and their individual employees);
- Transaction counterparties may not be an entity with authority to appoint the QPAM;
- Transaction counterparties may not be (or be related to) the QPAM; and
- Collectively, the value of assets attributable to the client's plan and its sponsor(s) cannot exceed 20% of the entity's total assets under management.

The proposed amendments to the QPAM Exemption include several requirements that an investment manager would need to comply with when seeking a QPAM Exemption. The proposed amendments include:

- Requiring a one-time notice to the DOL that the entity is relying upon the QPAM Exemption;
- Adjusting for inflation the minimum dollar thresholds for assets under management and equity (and providing for indexing prospectively):
  - For investment advisors, assets under management would increase from $85 million to $135.87 million;
  - Equity capital would increase from $1 million to $2.4 million; and
  - For banks, insurance companies, and savings and loans, equity capital would increase from $1 million to $2.72 million;
- Requiring up-front terms in a written management agreement that apply to allow the relationship to be unwound and for indemnification in the event of ineligibility;

- Updating the list of crimes to explicitly include foreign crimes that are substantially equivalent to the listed crimes in the U.S.;
- Expanding the circumstances that may lead to ineligibility to include a new category of “Prohibited Misconduct”;
- Providing a one-year winding-down period to help plans and IRAs avoid or minimize possible negative impacts of terminating or switching QPAMs or adjusting asset management arrangements when a QPAM becomes ineligible;
- Providing clarifying updates regarding a QPAM’s independent authority over investment decisions; and
- Adding a new recordkeeping requirement that QPAMs maintain records for at least six years to substantiate that the exemption was met.

The initial comment period was set to expire on September 26, 2022; however, the DOL extended the comment period to October 11, 2022. Additionally, the DOL will hold a public hearing on the proposed amendment beginning on November 17, 2022, and then intends to re-open the comment period afterward for about 14 additional days.

Aon Investments USA Inc. and Aon’s Retirement Legal Consulting & Compliance consultants are available to assist with understanding how the QPAM Exemption and the proposed amendments may affect your plan’s compliance strategy, practices, and procedures.

Please see the applicable Disclosures and Disclaimers on page **14**.

New Court Decision Reflects Possible Post-*Hughes* Emerging Consensus

by Hitz Burton

On August 29, 2022, the Seventh Circuit Court of Appeals ruled in favor of a plan sponsor’s motion to dismiss in *Albert v. Oshkosh Corp*. Plaintiff, Andrew Albert, a participant in the Oshkosh Corporation and Affiliates Tax Deferred Investment Plan (Oshkosh 401(k) plan) between January 2018 and April 2020, raised various fiduciary breach and prohibited transaction claims against Oshkosh and plan fiduciaries under the Employee Retirement Income Security Act of 1974 (ERISA). The allegations included claims regarding excessive recordkeeping fees paid to Fidelity Management Trust Company (Fidelity), excessive investment advisor fees paid to Strategic Advisors, Inc., a Fidelity subsidiary, and the use of expensive actively managed investment funds when lower-cost actively managed funds were readily available, among other claims.

Each of these three claims, and certain other related claims, were rejected by the Seventh Circuit because the plaintiff failed to provide a specific context on which each allegation was based. For example, where Albert alleged that the expense ratios for the actively managed funds offered in the Oshkosh 401(k) plan were “too high,” he provided no suitable benchmark for the court to consider when evaluating those costs. Similarly, when the plaintiff alleged that the Oshkosh 401(k) plan paid investment advisory fees that were too expensive, Albert provided no basis for comparison and merely relied on a statement that the plan fiduciaries had not completed a formal request for a proposal process covering investment advisory services in years.

The *Oshkosh* decision also reflects the Seventh Circuit’s first evaluation of excessive fee and fiduciary breach claims since the decision of the U.S. Supreme Court in *Hughes v. Northwestern Univ*. As you may recall, and as we previously discussed in the **Second Quarter 2022** issue of our *Quarterly Update*, in *Hughes*, the Supreme Court rejected the Seventh Circuit’s prior reasoning that the mere offering of lower-cost mutual funds as a designated investment alternative exempted fiduciaries from prudently evaluating why other higher-cost mutual funds were still offered. *Hughes* further noted that the Seventh Circuit’s reasoning was inconsistent with the Supreme Court’s decision in *Tibble v. Edison Int’l* that ERISA fiduciaries have an ongoing duty to monitor and remove imprudent plan investments. (Please see the article, “U.S. Supreme Court to Evaluate Limitation Periods Under ERISA; Will Not Review Revenue Sharing Litigation” in the **First Quarter 2015** issue of our *Quarterly Update*.)

In its *Hughes* decision, the Supreme Court articulated a need for plaintiffs to present allegations reflecting context-specific claims. Allegations of a plan charging excessive annual recordkeeping fees without more, for example, is not typically sufficient without consideration of the complete set of services provided to the plan for those fees.

The *Oshkosh* decision is perhaps most significant because the decision is in line with a recent Sixth Circuit Court of Appeals decision in *Smith v. Commonspirit Health* (excessive fee case with allegations regarding the cost of various actively managed investment funds). Taken together, and with certain other recent U.S. district court decisions interpreting *Hughes*, the *Oshkosh* and *Commonspirit Health* decisions suggest the emergence of a possible post-*Hughes* consensus among the federal courts of appeal that the pleading standard for plaintiffs in future excessive fee litigation will be substantial and will require more than mere allegations that fees standing alone are excessive.

In a possible sign that plaintiffs' attorneys are arriving at the same determination and following approximately 15 years of extremely active excessive fee litigation involving larger 401(k) and other defined contribution (DC) plans, there has been a recent uptick in proposed class action complaints filed against large DC plans offering lower-cost target-date funds focused on investment performance rather than expense ratios, revenue sharing, or other cost-related items.

Plan sponsors interested in developing the best possible fiduciary record regarding the selection of mutual funds or other designated investment alternatives offered in their 401(k) or other DC plans, on both a cost-and-performance basis and in light of ongoing litigation risks, should contact Aon's Retirement Legal Consulting & Compliance consultants for additional advice on how best to bolster their current fiduciary processes and develop an appropriate record to support the decisions made.

Don't Buy Retail When Plan Can Buy Institutional

by Dan Schwallie

The recent decision by the Sixth Circuit Court of Appeals in *Forman v. TriHealth, Inc*. reversed the district court's dismissal—for failure to state a claim—of class-action plaintiffs' complaint that a plan sponsor acted imprudently under the fiduciary requirements of the Employee Retirement Income Security Act of 1974. The court's decision considered the context-sensitive inquiry required to survive a motion to dismiss a complaint alleging a breach of fiduciary duty due to selecting plan investments with fees higher than available alternatives. Note that a decision of the Sixth Circuit directly impacts federal district courts in the states of Kentucky, Michigan, Ohio, and Tennessee.

The court distinguished the plaintiffs' allegations of higher fees from other allegations comparing, directly or indirectly—fees for actively managed funds versus passively managed funds, funds offering different investment strategies and objectives, or funds and providers offering different services or features. The plaintiffs' complaint at issue in the appeal to the court was that the defendant violated the duty of prudence by offering the plaintiffs pricier retail shares of mutual funds when those same investment management companies offered less expensive institutional shares of the same funds to other retirement plans. Plaintiffs further claimed that the retail and institutional shares of these mutual funds were exactly the same except for costs, that the institutional funds were all less expensive than their retail counterparts, and that both retail and institutional versions were subject to the same restrictions concerning deposits and withdrawals.

The court stated that, "Even if a prudent investor might make available a wide range of valid investment decisions in a given year, only an imprudent financier would offer a more expensive share when he could offer a functionally identical share for less." The court held that the plaintiffs plausibly alleged their claim that the plan sponsor offered them more expensive mutual fund shares when shares with the same investment strategy, management team, and investments were available to the plan at lower costs. Thus, the court reversed the district court's grant of defendants' motion to dismiss that claim.

The *TriHealth* case illustrates the importance of having policies and procedures in place while continually monitoring and evaluating plan investments and associated fees. Aon consultants are available to assist plan sponsors in evaluating their investment policies and procedures.

Plan Sponsor Wins Dismissal of Stock-Drop Allegations

by Hitz Burton

On September 7, 2022, in *Perrone v. Johnson & Johnson*, the Third Circuit Court of Appeals granted Johnson & Johnson's (J&J's) motion to dismiss a stock-drop complaint involving employee stock ownership (ESOP) subaccounts currently offered in three separate J&J sponsored 401(k) plans (J&J Plans).

This lawsuit arose from earlier product liability and related securities litigation involving J&J's talc-based products. Specifically, Perrone and the other plaintiffs argued that J&J and various plan fiduciaries violated their duty of prudence under the Employee Retirement Income Security Act of 1974 (ERISA) when they permitted the J&J Plans to continue to purchase and allocate investments in employer stock in the J&J Plans. The plaintiffs alleged that, alternatively, J&J should have been contributing cash to the ESOP subaccounts when they knew or should have known that such continued stock purchases were imprudent in light of J&J's exposure to damages arising from various products liability and related securities litigation.

Prior to 2014 such continued share purchases by an ESOP would likely have been presumed to be prudent by a federal court. The Supreme Court, however, eliminated this prior long-standing presumption of prudence in *Fifth Third Bancorp v. Dudenhoeffer* finding the presumption inconsistent with the ERISA fiduciary duties of prudence and loyalty. To avoid frivolous and other unnecessary litigation against ERISA plans and fiduciaries, however, the Court replaced this presumption with instructions to the lower federal courts to strictly enforce enhanced pleading requirements for stock-drop complaints. For additional information on *Dudenhoeffer*, please see the **First Quarter 2015** and **Third Quarter 2015** issues of our *Quarterly Update*.

Under these enhanced pleading standards, allegations based on general economic theories without specific additional context are not sufficient. In *Perrone*, for example, the Third Circuit found that it is not sufficient for plaintiffs to allege that plan fiduciaries violated ERISA by taking specific actions (e.g., continuing the share purchases by the ESOP subaccounts) unless they can also plausibly articulate a viable alternative course of action. The plaintiffs would have to demonstrate that the alternative course of action would not violate federal securities or other applicable law and that a prudent fiduciary could not have concluded that those alternative steps would have likely done more harm than good.

Following the decision in *Dudenhoeffer*, and as we have previously noted in prior *Quarterly Update* articles, the outcomes for most plan sponsors and fiduciaries in such stock-drop litigation since 2014, absent specifically damaging facts, has generally been favorable. The decision in *Perrone* confirms that general trend with the Third Circuit decision joining similar results in the Fifth, Sixth, and Eighth Circuit Courts of Appeal. While the general trend since *Dudenhoeffer* has been favorable to plan sponsors and their ERISA fiduciaries, plaintiff allegations can survive motions to dismiss if the court determines that earlier disclosure would not have done more harm than good to the stock price. (See the article, "Supreme Court Agrees to Hear IBM Stock Case" in the **Third Quarter 2019** issue of our *Quarterly Update*.)

Plan sponsors and ERISA fiduciaries who wish to more fully understand how to develop the best possible fiduciary record for ESOPs and employer stock funds should contact Aon's Retirement Legal Consulting & Compliance consultants for additional advice on how best to bolster their current fiduciary processes.

Quarterly Roundup of Other New Developments

by Sandy Combs, Teresa Kruse, Mark Manning, and Jan Raines

Know When to Hold 'Em

Market volatility has certainly been a consistent theme in 2022. If you are old enough to remember Kenny Rogers, you probably remember the lines from his song "The Gambler" that "You've got to know when to hold 'em, know when to fold 'em, know when to walk away, and know when to run." That is true for the game of poker and has been all too true for participants in retirement plans during all the recent volatility. During times such as this, participants in defined contribution (DC) plans are generally advised to stay calm and not make too many changes that are typically made in hindsight since retirement investing is for the long term and not the short term. Easy to say, a little more difficult to practice when markets are so turbulent and generally on a downward trend.

Alight Solutions recently reported[1] that for the month of May, trading activity was above normal with trading inflows concentrated heavily in stable value/money market funds (87%) and outflows concentrated heavily in target-date funds and large-cap U.S. equity funds (65%). In contrast, the month of April did not reflect any above-normal trading activity. This could be a signal that participants are becoming a little more rattled by the ongoing volatility—especially when other economic indicators, primarily inflation, continue to offer bad news. Considering such news, plan sponsors invariably begin to consider whether to provide some form of communication to participants regarding market volatility and thoughts on dealing with turbulent markets. For plan sponsors considering such a communication, Aon encourages them to request participant activity from the plan's recordkeeper and review the activity for their participant base to determine if a communication is in order. While employers do not want provide investment advice to their employees, sometimes a communication as to the importance of diversification[2] in a turbulent market may prove quite helpful to employees. Just as the song lyric suggests, timely actions are based on "knowing" which is the real tricky part in the game of poker just as investing is for participants in DC plans.

Managing Managed Accounts

In the current environment, many DC plan sponsors are looking for ways to enhance the participant investment experience by offering personalized investment services. The result has been a greater focus on managed accounts—the ability for participants to receive, and pay for, professional management of their retirement plan portfolio. For plan fiduciaries and committees, this managed account service comes with additional responsibility for them to review the managed account offering just as they would any other investment offering in the plan. Are the services and fees offered reasonable based on the current market?

Recently, a case was filed against Dover Corporation, the company's compensation committee, and benefits committee as fiduciaries of its DC plan alleging that the plan fiduciaries breached their fiduciary duties due to excessive recordkeeping and managed account fees. This lawsuit is particularly interesting as it heavily cites the recent Supreme Court decision, *Hughes v. Northwestern Univ.*, to support the allegations in the lawsuit (see the **Fourth Quarter 2021** and **Second Quarter 2022** issues of our *Quarterly Updates*). While the lawsuit does not name the two plan recordkeepers or managed account provider as defendants, the plaintiffs allege that the plan fiduciaries retained the managed account service provider, Financial Engines (now known as "Edelman Financial Engines" after the merger with Edelman Financial Services), through the plan's recordkeeper (Wells Fargo) which promoted the provider over other providers since Wells Fargo had a revenue incentive to do so.

The lawsuit further alleges the plan fiduciaries breached their duty of prudence by not monitoring and evaluating the plan's managed account fees or having a system in place for doing so, not monitoring the process by which the managed account service provider was evaluated, and ultimately not negotiating managed account fees or replacing the managed account provider with another provider with lesser cost. As demonstrated by the *Dover* lawsuit, the challenge for plan sponsors and their fiduciaries is that many times the provider of managed account services is dependent upon the recordkeeper providing services for the plan. What are plan sponsors and fiduciaries to do?

As the managed account option has become more popular, plan sponsors have increased leverage. Plan fiduciaries are reminded to have a process (and actually follow that process) to review all recordkeeping fees—including managed account fees. Other factors to consider include: (i) whether there is a choice of managed account providers with the current recordkeeper; (ii) whether the sponsor can contract independently with a managed account provider; (iii) what percentage of managed account fees is the recordkeeper retaining (or receiving); and (iv) whether the fees associated with the managed account provider are negotiable. For the responsible fiduciaries, these are questions that should be asked and evaluated on a regular basis to ensure that the duty of prudence is being fulfilled. *Gosse v. Dover Corp., No. 1:22-cv-04254 (N.D. Ill. Aug. 11, 2022*).

[1] Alight Solutions, *Alight Solutions 401(k) Index™: May 2022 Observations*, May 2022

[2] Diversification does not ensure a profit, nor does it protect against loss of principal. Diversification among investment options and asset classes may help to reduce overall volatility.

State-Sponsored Retirement Programs

A March 2022 working paper[3] by the Pension Research Council notes that almost half of all workers in the United States are not covered by an employer-sponsored retirement program. This lack of savings opportunity, coupled with no federal mandate for employers to offer a savings program, has led states to create their own requirements to help ensure retirement readiness.

Over 46 states have looked at adding these types of programs, with 16 states and two cities signing state- or city-sponsored retirement programs into law. The states with active retirement programs include California, Connecticut, Illinois, Maryland, Massachusetts, Oregon, and Washington. States that have passed legislation and are in the process of implementing programs include Colorado, Delaware, Maine, New Jersey, New Mexico, Vermont, and Virginia. The states of Hawaii and New York and the cities of New York and Seattle have passed legislation; however, implementation is not currently scheduled.

State- and city-sponsored programs generally offer an automatic IRA program or a marketplace allowing for multiple retirement options. Several of these programs are mandated for employers that do not currently sponsor a retirement program for their employees.

Businesses with employees in states that have active mandatory retirement programs are generally exempted from those state programs if an employer-sponsored retirement program is currently offered. Businesses offering such a program are encouraged to review the state laws to determine whether action is required to opt out of the state program, and whether preemption under the Employee Retirement Income Security Act of 1974 (ERISA) may apply.

Department of Labor (DOL) Gets Sued: The Never-Ending Saga of the Fiduciary Rules

During the Trump administration, the DOL reinstated its five-part test (originally issued in 1975) and thereafter, on December 18, 2020, issued Prohibited Transaction Exemption 2020-02 (PTE 2020-02) related to whether a financial institution or investment professional is considered a fiduciary for providing "investment advice" (see the **Fourth Quarter 2020** and **Second Quarter 2022** issues of our *Quarterly Updates*). In April 2021, the DOL under the Biden administration issued a set of Frequently Asked Questions (FAQs) to provide guidance with respect to PTE 2020-02 and information on the DOL's next steps in its regulation of investment advice. Since the issuance of the FAQs, two trade groups separately sued the DOL in February 2022. The first suit brought by the American Securities Association alleges that the FAQs did not go through the statutorily prescribed notice-and-comment process, as with other regulation changes. In June 2022, the DOL moved to dismiss the case for a number of procedural reasons (e.g., plaintiff's failure to specify an injury resulting from the two FAQs identified in the lawsuit) but also argued that the FAQs interpreted the five-part test and PTE 2020-02 and didn't change prior regulations or the definition of "fiduciary" under ERISA. *Am. Sec. Ass'n. v. U.S. Dep't of Labor, No. 8:22-cv-00330 (M.D. Fla. complaint filed Feb. 9, 2022).*

The second suit brought by the Federation of Americans for Consumer Choice, Inc. seeks to vacate the 64-page preamble that accompanied PTE 2020-02 when it was issued. The plaintiffs allege that this interpretative preamble is inconsistent with the Fifth Circuit Court of Appeals 2018 ruling in the *Chamber of Commerce* case which vacated the 2016 iteration of the fiduciary rule regarding investment advice. Specifically, the plaintiffs allege that the preamble has the same core problem as the rule vacated in 2018—the DOL is impermissibly attempting to rewrite and expand the definition of a fiduciary through the interpretive guidance provided in the preamble. In September 2022, the DOL moved to dismiss this case based on procedural grounds including a lack of jurisdiction and the plaintiffs' failure to establish an injury resulting from the interpretive preamble. *Fed'n of Americans for Consumer Choice, Inc. v. U.S. Dep't. of Labor, No. 3:22-cv-00243 (N.D. Tex. complaint filed Feb. 2, 2022)*.

As the courts have yet to rule on the motions to dismiss, Aon will continue to follow these cases and will report on the findings as they become available. In the meantime, plan fiduciaries should ensure that their recordkeeping partners or other advisers working with participants are following the DOL guidance. Aon's Defined Contribution Plan and Retirement Legal Consulting & Compliance consultants are available to assist with reviewing the advisers' policies, procedures, and actual practices to confirm they are in compliance with the DOL guidance.

Fiduciary Follies

Aon Investments USA Inc. offers fiduciary training sessions for retirement plan committees to help them become fully familiar with their fiduciary obligations. Within the context of our training, we note that there is little risk in being a good fiduciary; rather, the risk lies in being a bad fiduciary. Below is an example of yet another situation where being a bad fiduciary just isn't worth the risk!

After conducting an investigation, on August 30, 2022, the DOL sued InterArch and its plan fiduciaries, Shirley Hill (President, CEO, and sole owner of InterArch who also had responsibility for plan administration and as the sole plan trustee) and Vernon Hill (Shirley's banker husband who had provided investment advice as well as also had authority and control over plan assets). In the lawsuit, the DOL alleged that InterArch and the Hills invested as much as 70% of the company's profit sharing plan assets in the stock of London-based Metro Bank, PLC, a bank which Vernon co-founded, had a financial stake in, and where Vernon was the chairman, and at least 13% of the plan's assets

[3] John Sabelhous, *The Current State of U.S. Workplace Retirement Plan Coverage* (Pension Research Council, The Wharton School, University of Pennsylvania, Working Paper No. PRC WP2022-07, 2022)

in Republic First Bancorp, Inc. (d/b/a Republic Bank), where Vernon was a senior leader. The lawsuit alleged the defendants failed to diversify the plan's holdings, even as the share prices of both Metro Bank and Republic Bank fluctuated significantly.

As the complaint noted, it was only in June 2020 as the defendants were preparing to, and did, terminate the plan that the defendants sold the plan's shares in Metro Bank, and the defendants never sold the plan's Republic Bank stock. Rather than acting in the participants' best interests, as required by ERISA, the Hills are alleged to have been looking out for themselves and at the very least as having entered into a prohibited transaction. On September 23, 2022, the court entered a consent order and judgment under which the defendants agreed to not contest the allegations made by the DOL in its complaint and pay plan participants $1.8 million in settlement of claims that their breach of fiduciary duties caused financial losses to the accounts of participants and $184,000 in civil penalties to the DOL. *U.S. Dep't of Labor v. Interarch, Inc., No. 1:22-cv-05289 (D.N.J. complaint filed Aug. 30, 2022)*.

The settlement of the DOL lawsuit nearly coincides with the settlement of the 2020 class action suit by plan participants against InterArch and the Hills for the nearly identical allegations made by the DOL in its lawsuit. In response to the lawsuit, the defendants (specifically Mr. Hill) tried to assert that the losses were due to the COVID-19 pandemic; however, the pandemic outbreak did not begin to affect capital markets until February or March 2020, and the majority of the losses occurred prior to 2020. On September 26, 2022, the class action lawsuit settled for a total of $1.5 million ($950,000 of which was associated with a prior settlement amount), which will be allocated to the participants following payment of court costs and attorney fees. *McCann v. Hill, No. 1:20-cv-06435 (D.N.J. complaint filed May 27, 2020)*.

While the two cases offer interesting and somewhat absorbing allegations and illustrate a number of plan fiduciary issues, the cases do serve as a great reminder to plan fiduciaries: know your fiduciary duties and responsibilities and act accordingly. If you would like to schedule fiduciary training for your committee or your executives, please contact your Aon consultant.

New Retirement Plan Cases

When it rains, it pours. That is certainly the case since the last quarter, as at least 26 new cases were filed with at least 11 of those cases filed involving certain BlackRock Inc. target-date funds (TDFs). The BlackRock cases are interesting because the allegation is not focused on excessive fees but rather on underperformance resulting, allegedly, from plan fiduciaries choosing a lower-cost TDF series over better-performing TDF series even though investment management fees may have been higher. Although the list of recently filed cases is only illustrative, it is intended to provide a summary of the types of claims being alleged against plan fiduciaries and their committees. Fund performance cases this quarter, all involving BlackRock, were filed against Advance Publications, Inc.; Booz Allen Hamilton Inc.; Capital One Financial Corp.; CMFG Life Insurance Co.; Cisco Systems, Inc.; Citigroup, Inc.; Genworth Financial Inc.; March & McLennan Cos. Inc.; Microsoft Corp.; Stanley Black & Decker, Inc.; and Wintrust Financial Corp. Excessive fee cases this quarter were brought against Cook Group Inc.; Dover Corp.; Gerdau Ameristeel U.S. Inc.; Janus Henderson U.S. Inc.; Kellogg Co.; Laboratory Corp. Of American Holdings; Marmon Holdings Inc.; MITRE Corp.; North Memorial Health; Northeastern Univ.; Swiss Re American Holding Co.; and TTEC Services Corp. In addition, cases were filed against Coal Exclusive Co. (operational failure); Colgate-Palmolive Co. (data security); and Seyfarth Shaw LLP (benefit payment).

Aon will continue to track these cases, and others, as they develop.

Retirement Plan Litigation Update

Retirement plan litigation has been prevalent over the past decade impacting corporate plan sponsors, financial institutions that are also plan sponsors, and universities sponsoring 403(b) plans, among others. DC plan cases generally fall into the following three areas: inappropriate or imprudent investment choices; excessive fees; and self-dealing. Recently, several cases involving corporations, universities, and other institutions have been dismissed (in full or in part) or settled, including cases involving L Brands, Inc. (settled for $2.75M); Commonspirit Health (also known as Catholic Health Initiatives) (dismissed); Costco Wholesale Corp. (settled for $5.1M and other remedies); Nextep, Inc. (settled for $1.1M and other remedies); and Rush University Medical Center (settled for $2.95M).

Plan sponsors seeking to reduce their litigation risk use a variety of strategies including improving their fiduciary process for plan governance, increasing the number of passive funds in their plans, and implementing better fee transparency. To the extent helpful, Aon has a team that can review your plan governance as it applies to plan fees, investments, and decision-making processes.

Please see the applicable Disclosures and Disclaimers on page **14**.

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About Aon

Aon plc (NYSE:AON) is a leading global professional services firm providing a broad range of risk, retirement, and health solutions. Our 50,000 colleagues in 120 countries empower results for clients by using proprietary data and analytics to deliver insights that reduce volatility and improve performance.