No. 16-56418

IN THE

United States Court Of Appeals

FOR THE NINTH CIRCUIT

TRANSAMERICA LIFE INSURANCE COMPANY, an Iowa corporation; TRANSAMERICA INVESTMENT MANAGEMENT, LLC, a Delaware limited liability company; and TRANSAMERICA ASSET MANAGEMENT, INC., a Florida corporation
Defendants-Appellants,

v.

JACLYN SANTOMENNO; KAREN POLEY and BARBARA POLEY, all individually and on behalf of all others similarly situated,
Plaintiffs-Appellees

Appeal from a Decision of the United States District Court for the Central District of California, Case No. 2:12-cv-02782-DDP (MANX); Honorable Dean D. Pregerson, District Judge

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INTRODUCTION

A fundamental purpose of the Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1001 *et seq.* ("ERISA") is to protect retirement savers from the perils of conflicts of interest. At its core, this case is about an ERISA fiduciary who committed a series of per se violations of statutory prohibitions intended to prevent self-dealing and other conflicts of interest, and who used its fiduciary powers to charge, and to allow its affiliates to charge, excessive fees on retirement plan assets causing significant harm to retirement savers.

The district court's ruling, that Plaintiffs plausibly alleged that the Transamerica Life Insurance Company ("TLIC") is a fiduciary to participants in the ERISA plans in the certified classes, ER191-205, should be affirmed. TLIC is an entity that exercises discretion over plan management, has authority and control over the disposition and management of plan assets, and has discretion over plan administration. TLIC sets and extracts its own fees from plan assets, and it controls the investment lineup. TLIC thus qualifies as a functional fiduciary under 29 U.S.C. § 1002(21)(A).

Arguing that it is not a fiduciary, Defendants-Appellants ("Defendants") focus primarily on the district court's discussion of TLIC's conduct prior to its retention, wrongly suggesting that this was the entirety of the district court's analysis. Appellants' Opening Brief ("Br") at 1-3, 20, 24-31. According to TLIC, it has no fiduciary responsibilities when it negotiates its retention. Regardless, as the district court held, it is TLIC's conduct *after* it signed the contracts it wrote—and thus became a fiduciary by retaining numerous fiduciary powers—that implicates TLIC's responsibilities under ERISA. That plan sponsors signed TLIC's standard contracts cannot insulate TLIC from that liability. *See infra* Section I. Although plan sponsors also have fiduciary duties, Br. 3; Br. 15; Br. 25, the conduct of the plan sponsors that signed TLIC's form contracts is irrelevant. Ultimately, it was *TLIC* who retained powers that make it a fiduciary and who engaged in the misconduct which injured plan participants.

Defendants invoke a false dichotomy between what they label an "independent plan fiduciary" and a "service provider." *See, e.g.*, Br. 1. By "independent plan fiduciary," Defendants seem to refer to the concept of a "named fiduciary," which is the fiduciary required to be named in

every plan instrument who must have "authority to control and manage the operation and administration of the plan." *See* 29 U.S.C. § 1102. Defendants ignore three fundamental principles under ERISA: (1) notwithstanding whether an entity is "named" a fiduciary in a plan's instrument, an unnamed service provider can indisputably be a "fiduciary" pursuant to ERISA's functional definition, *see id.* § 1002(21)(A); (2) *all* fiduciaries, whether named or *de facto*, must be "independent," *i.e.*, they must act "solely in the interest" of plan participants and beneficiaries, *id.* § 1104(a)(1); and (3) plans may have multiple fiduciaries.

TLIC is not just a vendor, nor is it merely "help[ing]" the plans out. Br. 1. Rather, TLIC is in control of a massive pool of the ERISA-protected plan assets of thousands of retirement savings plans. Indeed, as of December 31, 2010, TLIC was operating approximately 15,500 401(k) plans through its group annuity product and was managing approximately $19.5 billion in ERISA plan assets. ER185. TLIC was a fiduciary with respect to these plan assets.

When Congress enacted ERISA, it imposed a duty on ERISA fiduciaries to refrain from engaging in certain transactions that are

defined by statute as *per se* tainted by conflicts of interest, called "prohibited transactions." 29 U.S.C. § 1106(b)(1). The district court properly concluded that Plaintiffs plausibly alleged that TLIC has and continues to use its fiduciary powers to commit proscribed acts of self-dealing and other conflicted transactions, in violation of 29 U.S.C. § 1106(b), and to charge the Plaintiffs' retirement plans excessive fees in violation of 29 U.S.C. § 1104(a). ER205-216. The district court also properly upheld claims that TLIC committed self-dealing and otherwise conflicted prohibited transactions, in violation of § 1106(b), when it paid its affiliates, Transamerica Investment Management ("TIM") and Transamerica Asset Management ("TAM"), fees from plan assets which TLIC held in its separate account investment options, and that TLIC violated its fiduciary duties under § 1104(a) by allowing TIM and TAM to charge excessive fees.

The district court, applying this Court's precedent with respect to fiduciary status and the substance of Plaintiffs' claims, correctly exercised its discretion in certifying two classes with respect to these claims. ER62-102. Because common legal and factual questions predominate, these rulings too should be affirmed.

In addition to being wrong about the questions of law before this Court, TLIC and its amici are incorrect when they claim that this lawsuit threatens TLIC's viability and would disrupt the industry. Br. 29-31. As discussed *infra* Section V, there are other remedies available to TLIC that could be easily and inexpensively implemented and would fulfill Congress's desire to protect retirement investors and allow TLIC to conform its conduct to ERISA. If Plaintiffs prevail on the merits of the certified classes' claims, neither TLIC nor the entire retirement plan services industry will be destroyed.

ISSUES PRESENTED

1. Does a service provider qualify as an ERISA fiduciary under 29 U.S.C. § 1002(21)(A) with regard to ERISA restrictions on self-dealing and fees in circumstances in which it (a) sets and/or extracts its fees from plan assets that it controls; or (b) has discretion to do so; or (c) exercises discretion to do so?

2. Did TLIC, an ERISA fiduciary, plausibly engage in prohibited transactions within the meaning of 29 U.S.C. § 1106(b)(1), which prohibits fiduciary self-dealing, when TLIC paid fees to itself from plan assets?

3. Does 29 U.S.C. § 1108(b)(8) provide an exemption from a 29 U.S.C. § 1106(b) self-dealing prohibited transaction and, if so, does that exemption apply to allegations that a fiduciary repeatedly and unlawfully extracts fees from plan assets?

4. Did the district court abuse its discretion in concluding that the TIM and TAM Class satisfied the requirements of Fed. R. Civ. P. 23(b)(3) with respect to Plaintiffs' excessive fee claims?

STATEMENT OF THE CASE

I. Factual Background.

A. The Parties.

TLIC sells retirement investment products and services to small- and medium-sized 401(k) retirement plans. ER63. Plaintiffs are or were participants in retirement plans offered by TLIC. Karen and Barbara Poley are participants in the QualCare Alliance Networks Inc., Retirement Plan (the "QualCare Plan") and, prior to December 2010, Jaclyn Santomenno was a participant in the Gain Capital Group, LLC 401(k) Plan (the "Gain Plan"). ER186. As participants in these plans, Plaintiffs acquired interests in separate account "investment options" sold and managed by TLIC, and were then charged the investment fees at issue in this case.

B. TLIC's Products, Contracts, and Fees.

TLIC's investment products, along with investment management, expense monitoring, and administrative services, are provided to 401(k) plans pursuant to two separate contracts. ER185; ER319-334; ER338-366; ER367-392. Under an "Application and Agreement for Services," TLIC offers recordkeeping, administrative, and other plan-level services. Under a form "Group Annuity Contract" ("GAC"), which is the focus of this case, TLIC provides investment options and investment management to the 401(k) plans at issue. ER338-366; ER367-392.

Once a sponsor signs a GAC, plan assets are transferred into TLIC's "Separate Accounts." Each "Separate Account," is an "investment choice … established by TLIC." ER175. Most of these TLIC Separate Account investment choices are pass-through vehicles that invest in an underlying mutual fund or, less often, are directly advised by a TLIC affiliate with no underlying mutual fund. ER186-187. TLIC charges an investment management and administrative fee ("IM/Admin Fee") for "managing and administering the assets in the separate accounts." SR161. While all of the Separate Accounts are TLIC Separate Accounts, ER 175; ER186, many of the mutual funds

underlying TLIC's Separate Accounts are advised by third parties. ER186. Some Separate Accounts, however, are directly advised by TAM; others hold mutual funds managed by TIM (collectively, the "Affiliated Separate Accounts"). SR211-212; ER187; Br. 7 n.1. The Separate Accounts underperform the performance of the underlying funds because of TLIC's additional fees. SR193-194; SR18-19.

Each Separate Account charges investors a fee calculated as a percentage of the assets invested in that account. ER187. These fees are a combination of the advisory fee charged by the underlying mutual fund or investment advisor *plus* TLIC's "IM/Admin Fee." ER187. Because the IM/Admin Fee challenged here is specific to the Separate Account, every participant that invests in that particular Separate Account investment choice is charged the same percentage fee; the fees, as the Court observed, are not plan specific. ER119. TLIC promises that these IM/Admin Fees are used for "managing and administering the assets in the separate accounts," SR161, but TLIC exercises discretion to use these fees for other, plan-level purposes. SR195; SR216; Br. 6-7.

Plan participants also pay recordkeeping charges, and a Contract Asset Charge (which TLIC refers to as the "CAC"), which can be very

large over the life of a plan, ER354;[1] the CAC is used to defray, among other costs, brokerage commissions to agents who sell the TLIC product, marketing costs and sales costs. ER67.

As an internal TLIC study found, TLIC had "[h]igh fees relative to competition." SR164. For example, a retirement saver can acquire the Vanguard Total Stock Market Index Fund (Investor Class) and pay a fee of .18%, or 18 basis points, if he or she is not part of the TLIC program. TLIC offers this Vanguard fund as part of a TLIC Separate Account, called the "Transamerica Vanguard Total Stock Market Index Ret Opt," and charges an additional fee of .75% for a total cost of .93% or 93 basis points. ER188.

Several of the Separate Accounts are directly advised by TAM or contain mutual funds advised by TIM. ER186-187. Plaintiffs contend that, although TIM and TAM offer substantially identical services to investors outside of retirement plans, they charge the Separate Accounts significantly greater fees than they charge others. ER98. Like TLIC's IM/Admin Fee, the fees paid to TIM and TAM are uniform.

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[1] For a small plan less than $75,000, the CAC is 2% annually. ER354.

C. TLIC's Role as a Fiduciary in the Misconduct Alleged.

It is undisputed that TLIC controls the disposition and management of plan assets invested in its Separate Accounts and that it has discretion over those accounts. *See, e.g.,* ER64; ER175 ("TLIC investment choices with names ending in 'Ret Opt' … correspond to investment choices for which Transamerica retains investment discretion over the assets.").[2] TLIC retains the power to withdraw its IM/Admin Fee and its affiliates' fees from the Separate Accounts and actually does so. ER65. The GAC provides that:

> [f]or each Separate Account … , an Investment Management Charge *may* be withdrawn daily and will belong to us.

ER350; ER379 (emphasis added). The GAC further provides that "[t]he applicable Administrative Charge for each Investment Account … is calculated and withdrawn daily and will belong to us." ER350; ER379.

The GAC affords TLIC the unfettered right to alter the amount of its IM/Admin Fees. ER187; ER350-51; ER379-80. Specifically, the GAC states that TLIC "reserve[s] the right to change" the IM/Admin Fees "upon advance written notice to the Contractholder of at least 30 days." ER351; ER380. If a plan wishes to contract with another provider as a

[2] The case involves TLIC's Ret Opt investment options.

consequence of the changes, it is not realistic to do so within 30 days and without significant expense and disruption.[3]

The GAC also affords to TLIC the right to add or delete Separate Account investment options upon six months' notice to the plans or with "less notice than is otherwise required by the terms of the contract." ER365; *see also* SR231; *see, e.g.,* ER342; ER350; ER371; ER379. In addition to its power under the GAC, through Transamerica Investment Monitor, TLIC "may also completely close an investment choice outside of the general time guidelines … at the discretion of the [TLIC] investment committee." SR22.

II. Procedural Background.

Plaintiffs' complaint alleged violations of ERISA and the Investment Advisors Act. The Court dismissed Plaintiffs' claim brought under the Investment Advisors Act, which alleged that TLIC failed to register as an investment advisor, but declined to dismiss Plaintiffs'

[3] While the reasonableness of TLIC's IM/Admin Fee is not before this Court, TLIC's claim that it needs seven years to recoup the expenses it incurs when it adds a plan to its platform is misleading, because the largest portion of these expenses are sales commissions which TLIC pays to agents. These expenses are defrayed by the Contract Asset Charge paid by plan participants. SR205-210; SR213.

ERISA claim. In response to TLIC's motion to dismiss, Plaintiffs argued that they plausibly pleaded that TLIC was an ERISA fiduciary for all prohibited transaction and excessive fee claims under 29 U.S.C. § 1002(21)(A). The district court, in an opinion issued on February 19, 2013, agreed. ER191-206.

Plaintiffs thereafter moved for class certification. In its August 28, 2015 ruling, the district court denied this motion, but reaffirmed its prior holdings as to the basis for TLIC's fiduciary status. ER123-130; ER152. Plaintiffs then renewed their motion for class certification. TLIC did not, in its brief, advance any new arguments in response to Plaintiffs' fiduciary status argument and the district court, on March 14, 2016, granted Plaintiffs' second motion to certify two classes. In so doing, the Court reasoned that by using powers that are alleged to make TLIC a fiduciary over fees to decide what fees to withdraw, and to actually withdraw them from plan assets repeatedly, it may be shown on a class-wide basis that TLIC committed non-exempt self-dealing prohibited transactions under 29 U.S.C. § 1106(b)(1).

The certified TLIC Prohibited Transaction Class, alleges that TLIC engaged in prohibited transactions under 29 U.S.C. § 1106(b)(1)

(self-dealing) by paying its own IM/Admin Fees from plan assets in its control. The certified TIM and TAM Class seeks to prosecute two claims. The first claim is that TLIC committed prohibited transactions under 29 U.S.C. §§ 1106(b)(1) and (2) (self-dealing and acting on behalf of, or representing a party, whose interests are adverse to the plan[4]) by allowing plan assets to be invested in Separate Accounts that were managed for a fee by TLIC affiliates (TIM and TAM) and extracting fees from plan assets under TLIC's control. The second claim is that TLIC breached (1) its duty of loyalty, to act "solely in the interest of participants and beneficiaries," 29 U.S.C. § 1104(a)(1)(A); (2) its duty to defray only reasonable expenses, 29 U.S.C. §§ 1104(a)(1)(A)(ii); and (3) its duty of prudence, 29 U.S.C. § 1104(a)(1)(B), by allowing its affiliates, TIM and TAM, to charge excessive fees on plan assets invested in the Affiliated Separate Accounts. ER98.

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[4] Although the Court certified the TIM and TAM Class's claims that TLIC committed a prohibited transaction with respect to TIM and TAM's fees by acting on behalf of a party whose interest is adverse to the Plaintiffs' plans, 29 U.S.C. § 1106(b)(2), Defendants do not challenge this aspect of class certification.

STANDARD OF REVIEW

The three legal questions—(i) whether Plaintiffs adequately pleaded that TLIC was a fiduciary, (ii) whether TLIC's alleged conduct constitutes prohibited transactions, and (iii) whether TLIC's alleged conduct does not fall within statutory exceptions to the prohibited transaction provisions—are reviewed de novo by this Court. *California Ironworkers Field Pension Trust v. Loomis Sayles & Co.*, 259 F.3d 1036, 1042 (9th Cir. 2001). The district court's class certification rulings are reviewed for abuse of discretion. *Pulaski & Middleman, LLC v. Google, Inc.*, 802 F.3d 979, 984 (9th Cir. 2015).

SUMMARY OF ARGUMENT

First, Plaintiffs plausibly pleaded that TLIC is a fiduciary and this is an issue common to the classes. In 29 U.S.C. § 1002(21)(A), Congress defined an ERISA fiduciary in functional terms as an entity (1) that exercises discretion over plan management; or (2) that exercises any authority or control over plan assets; or (3) that has discretionary authority or responsibility over plan administration.

With regard to Plaintiffs' and the certified classes' prohibited transaction claims, TLIC was a fiduciary because it had "authority and control" over plan assets, "exercised discretion" over plan management,

and "had discretion" over plan administration when it paid its fee and the fees of TIM and TAM from Separate Accounts. TLIC was also a fiduciary because it exercised discretion to use part of the investment management fee to pay plan-level costs. 29 U.S.C. § 1002(21)(A)(i), (iii).

Further, TLIC was a fiduciary when it charged—and when it allowed TIM and TAM to charge—excessive fees using powers it retained under the GAC. In addition to exercising "authority or control" over management or disposition of plan assets, 29 U.S.C. § 1002(21)(A)(i), TLIC was an ERISA fiduciary because it "had discretion" to reduce fees on all Separate Accounts and on the investment options managed by its affiliates, and it had the discretion to remove the excessively priced TIM and TAM investment options from the investment menu. In addition, TLIC was an ERISA fiduciary because it "exercised discretion" when it monitored fund expenses but elected to continue to offer excessively priced funds to the plans. TLIC was thus an ERISA fiduciary under 29 U.S.C. § 1002(21)(A)(i) and (iii).

While Defendants' brief addresses TLIC's fiduciary status in the context of Plaintiffs' excessive fee claims, that brief largely fails to address the bases upon which Plaintiffs maintain that TLIC functioned

as an ERISA fiduciary when it committed ERISA prohibited transactions.

TLIC argues that it is free to commit prohibited transactions and to charge excessive fees because its conduct was authorized by a contract negotiated between it and plan sponsors before it became a fiduciary. As the district court found and this Court has held, those negotiations cannot "get TLIC off the hook," ER207, from complying with statutory obligations owed to plan participants as a consequence of TLIC's subsequent assumption of fiduciary functions. Nor does TLIC's claim that a plan sponsor, also a fiduciary, failed in its duty to constrain TLIC's misconduct immunize TLIC. The cases upon which TLIC relies are distinguishable and are inconsistent with Ninth Circuit jurisprudence.

Second, TLIC committed prohibited transactions under 29 U.S.C § 1106(b)(1): (1) It engaged in self-dealing when it withdrew its fees from the Separate Accounts; and (2) it engaged in self-dealing when it withdrew funds from Separate Accounts to pay the fee of its affiliates, TIM and TAM. By paying fees to itself from plan assets, TLIC violated § 1106(b)(1) even if those withdrawals were contractually authorized or

approved by a plan sponsor. *Barboza v. Cal. Ass'n of Prof'l Firefighters*, 799 F.3d 1257 (9th Cir. 2015), *cert. denied*, 125 S. Ct. 1171 (2016). And if the Court were to find, as TLIC argues, that it was required to both set its fees and pay them to itself in order to have committed a prohibited transaction, Plaintiffs have plausibly pleaded that TLIC does so.

Third, the exception to which TLIC alludes in its brief, set forth in 29 U.S.C. § 1108(b)(8), is irrelevant to a claim brought under § 1106(b), and the facts alleged here make this exception inapplicable in any event.

Fourth, common issues predominate with regard to the investment management fees charged by TIM and TAM, which are much higher than the fees TIM and TAM charge third parties for the same services. The fees of these affiliates are no different than the fees charged by any other advisor who provides management services to a fund underlying a Separate Account. TLIC has failed to make any showing that the fees of TIM and TAM subsidize other plan costs.

Finally, TLIC's claim that the obligation to conform its conduct to ERISA will impair its business, be disruptive, and injure retirement

plans is inaccurate and, even if it were accurate, should be addressed by Congress. TLIC could inexpensively remedy the conduct that underlies Plaintiffs' prohibited transaction claim by ceasing to function as a fiduciary with respect to its fees or by exposing its fee payment requests to outside scrutiny by a separate entity acting on behalf of the Separate Accounts and tasked with monitoring withdrawals to prevent use of plan assets for improper purposes.

ARGUMENT

I. Plaintiffs Plausibly Pleaded that TLIC is a Fiduciary with Regard to the Misconduct Which Forms the Basis of Plaintiffs' Claims.

TLIC, not the plan-side fiduciaries, is the party responsible for the misconduct Plaintiffs alleged. TLIC attempts to avoid its responsibility by urging that its conduct, even if wrongful, was authorized by the GAC, a form contract signed by plan sponsors, or that the responsible party is the plan sponsor. However, it is TLIC's exercise of authority and control, as well as TLIC's possession and exercise of discretion, as those terms are used in 29 U.S.C. § 1002(21)(A)(i) and (iii), that make TLIC a fiduciary.

TLIC's brief minimizes the facts that make TLIC a fiduciary: (1) its "authority and control" over TLIC's Separate Accounts; (2) its

possession of discretion to change (*i.e.*, raise) its own fees; (3) its "exercise of discretion" to pay itself and TIM and TAM fees from those accounts; (4) its "exercise of discretion" to divert funds intended for investment management to pay plan-level costs; (5) its possession of discretion to remove (or retain) excessively priced funds, including those of TIM and TAM, from the plan menus; (6) its possession of discretion to change (*i.e.*, lower) its fees and those of TIM and TAM; and (7) its exercise of discretion to retain high priced investments on the investment menu notwithstanding its monitoring obligations. Plaintiffs plausibly pleaded that these powers make TLIC a fiduciary under the functional test set forth in 29 U.S.C. § 1002(21)(A)(i) and (iii); and they all implicate common issues such that TLIC's fiduciary status can be adjudicated in a class action. The terms of the GAC and the role of the plan sponsors do not, and under the law, cannot absolve TLIC of its fiduciary responsibilities.

Further, the question of whether ERISA's fiduciary status test actually has been met here is not before the Court, because no trial has

occurred.[5] And the relevant legal questions—as well as the factual questions that will resolve them—are common to the certified classes.[6]

A. ERISA's Fiduciary Definition Must Be Broadly Construed.

ERISA requires an employee benefit plan to designate one or more named fiduciaries who are granted authority to manage a retirement plan. 29 U.S.C. § 1102(a)(1). In addition, ERISA provides that others who exercise control or authority or exercise or have discretion are "functional fiduciaries" defined in pertinent part as follows:

> [A] person is a fiduciary with respect to a plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan *or* exercises any authority or control respecting management or disposition of its assets, … *or* (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan.

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[5] Fiduciary status "is essentially a factual conclusion." *Steen v. John Hancock Mut. Life Ins. Co.*, 106 F.3d 904, 913-14 (9th Cir. 1997) (citing *Thomas, Head & Greisen Emps. Trust v. Buster*, 24 F.3d 1114, 1116 (9th Cir. 1994)).

[6] TLIC's assertion, Br. 39 n.7, that the classes must be "decertified because plaintiffs are not class members" ignores that under ERISA, Plaintiffs may bring their claims in a representative capacity, on behalf of the plans for losses to the plans. 29 U.S.C. § 1132(a)(2); 29 U.S.C. § 1109. In any event, this hyper-technical objection may be easily resolved by a slight change in the class definitions to certify "all participants in the plans" rather than "all plans," which can be accomplished on remand and should not be decided by this Court in the first instance.

29 U.S.C. § 1002(21)(A) (emphasis added).

Three clauses of this provision are relevant here—the two bases for fiduciary status in subsection (i), along with the basis set forth in subsection (iii). Under the first clause of subsection (i), a service provider may be an ERISA fiduciary by exercising discretionary authority or discretionary control with regard to the management of a plan. Under the second clause of subsection (i), a service provider may be an ERISA fiduciary by exercising "any authority or control" over management or disposition of plan assets. Under this second clause, discretion has no role in assessing whether a service provider qualifies as a fiduciary. *Trs. of S. Cal. Bakery Drivers Sec. Fund v. Middleton*, 474 F.3d 642, 646 (9th Cir. 2007); *Bd. of Trs. of Bricklayers & Allied Craftsmen Local 6 of New Jersey Welfare Fund v. Wettlin Assocs., Inc.*, 237 F.3d 270, 273 (3d Cir. 2001); *IT Corp. v. Gen. Am. Life Ins. Co.*, 107 F.3d 1415, 1421 (9th Cir. 1997) ("'Any' control over disposition of plan money makes the person who has the control a fiduciary."); *id.* ("The right to write checks on plan funds is 'authority or control respecting management or disposition of its assets.'"). Further, this power has nothing to do with actually writing the checks and speaks

simply of the defendant's "authority under the plan to do so." *Id.*; *Briscoe v. Fine*, 444 F.3d 478, 490-91 (6th Cir. 2006). The Department of Labor has agreed with this interpretation.[7]

Fiduciary status predicated upon discretion is addressed in two subsections of 29 U.S.C. § 1002(21)(A): subsections (i) and (iii). As noted above, a service provider is a fiduciary under the first clause of subsection (i) if it "*exercises*" discretionary authority or control over plan management. Alternatively, a service provider is a fiduciary under subsection (iii) if it merely "*has*" discretionary authority or responsibility over plan administration. Thus, a service provider with discretion over plan administration is a fiduciary irrespective of whether that discretion is "exercised." *Bouboulis v. Transp. Workers Union of Am.*, 442 F.3d 55, 63-64 (2d Cir. 2006) ("Local 100 should thus

[7] Br. of the Sec'y of Labor as Amicus Curiae in Supp. of Pl.-Appellant Urging Reversal and Remand, *Leimkuehler v. Am. United Life Ins. Co.*, No. 12-1081, 2012 WL 3066710, at *18-19, 26-27 (7th Cir. June 1, 2012); Corrected Br. of the Sec'y of Labor, Thomas E. Perez, as Amicus Curiae in Supp. of Pls.-Appellants and Requesting Reversal, *Santomenno v. John Hancock Life Ins. Co.*, No. 13-3467, 2014 WL 2553787, at *14-19 & n.3 (3d Cir. May 28, 2014); Br. of the Sec'y of Labor as Amicus Curiae in Supp. of Pl.-Appellants and Requesting Reversal, *McCaffree Fin. Corp. v. Principal Life Ins. Co.*, No. 15-1007, 2015 WL 1824627, at *12-28 (8th Cir. Apr. 8, 2015).

be considered a fiduciary under subsection three … , even if, as the district court found, there is no evidence that Local 100 actually exercised this authority in a manner that would qualify under subsection one."); *Healthcare Strategies, Inc. v. ING Life Ins. & Annuity Co.*, 961 F. Supp. 2d 393, 401 (D. Conn. 2013) (subsection (iii) "makes possession of authority, not its exercise, the key determinant of fiduciary status").

In determining whether a service provider is a fiduciary under one or more of the grounds set forth in 29 U.S.C. § 1002(21)(A), the Supreme Court has recognized that "[t]o help fulfill ERISA's broadly protective purposes, Congress commodiously imposed fiduciary standards on persons whose actions affect the amount of benefits retirement plan participants will receive." *John Hancock Mut. Life Ins. Co. v. Harris Tr. & Sav. Bank*, 510 U.S. 86, 96 (1993). Therefore, the several alternative grounds for imposition of fiduciary responsibilities set forth in the statute must be broadly construed. *Kayes v. Pac. Lumber Co.*, 51 F.3d 1449, 1461 (9th Cir. 1995), *cert. denied*, 516 U.S. 914 (1995).

B. The District Court Correctly Found that Plaintiffs Plausibly Pleaded that TLIC Acted as an ERISA Fiduciary When It Committed Prohibited Transactions by Paying Itself and TIM and TAM Fees from Plan Assets in TLIC's Separate Accounts.

1. TLIC Exercises Authority and Control Over Management and Disposition of Plan Assets in Insurance Company Separate Accounts.

TLIC's Separate Accounts contain plan assets. *John Hancock Mut. Life Ins. Co.,* 510 U.S. at 101 n.12 ("separate account assets [fall] within the definition of 'plan assets'"); *see also* 29 C.F.R. § 2510.3-101(h)(1)(iii) (assets in insurer's separate account are plan assets); DOL Advisory Opinion ("DOL Op.") 05-22A, 2005 WL 3751637 (Dec. 7, 2005) ("Under this regulation, once a plan acquires or holds an interest in a pooled separate account, all of the assets of the separate account become plan assets.") (citing 29 CFR § 2510.3-101(h)(1)(iii))). *See* 29 C.F.R. § 2550.401c-1(d)(2)(c):

> [A]n insurer is subject to ERISA's fiduciary responsibility provisions with respect to the assets of a separate account …. ERISA requires insurers, in administering separate account assets, to act solely in the interest of the plan's participants and beneficiaries; prohibits self-dealing and conflicts of interest; and requires insurers to adhere to a prudent standard of care.

See also H.R. Conf. Rep. 93-1280 (1974), *reprinted in* 1974 U.S.C.C.A.N. 5038, 5077.

TLIC's form GAC provides that:

> For each Separate Account … an Investment Management Charge **may** be withdrawn daily and will belong to us.

ER350; ER379 (emphasis added). It also provides that the administrative portion of the fee will be "withdrawn" from the Separate Account. *Id*.

Thus, when TLIC removed its fees and those of TIM and TAM from the plan assets invested in the TLIC Separate Accounts, ER350, it was exercising "authority and control" over plan assets and their management, and thus was a fiduciary under the second clause of 29 U.S.C. § 1002(21)(A)(i).

None of the cases cited by Defendants address self-dealing prohibited transaction claims like those here, nor do they address the second clause of 29 U.S.C. § 1002(21)(A)(i) as applied by this Court.[8]

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[8] Plaintiffs argued that TLIC was an ERISA fiduciary under the second prong of 29 U.S.C. § 1002(21)(A)(i) (nondiscretionary control and authority) in each brief they submitted. *See* excerpts from Plaintiffs' briefs on their motion to dismiss, SR41; SR42-45, first motion for class certification, SR24-25, and second motion for class certification, addressed to Plaintiffs' Prohibited Transaction claims, SR2-9. Defendants did not address this argument in their response to Plaintiffs' second motion for class certification and do not address it before this Court.

2. TLIC Exercises and Has Discretion over the Management and Administration of the Plans' Separate Accounts.

TLIC was a fiduciary for a second reason. TLIC "exercised" its discretion to withdraw its investment management fees and those of TIM and TAM from the Separate Accounts. Not only did it withdraw those fees, but it exercised its discretion to determine its fees and devote much of the IM/Admin Fee, intended for investment management, to defray plan-level costs. *See supra* p. 7. On these two bases, TLIC is a fiduciary under the first clause of 29 U.S.C. § 1002(21)(A)(i).

A third reason TLIC is a fiduciary is that it "had" discretion, and thus qualifies as a fiduciary under 29 U.S.C. § 1002(21)(A)(iii). Under that provision, a service provider is a fiduciary if it has discretion irrespective of whether that discretion is exercised. *Yeseta v. Baima*, 837 F.2d 380, 384-85 (9th Cir. 1988) (failure to exercise discretionary authority or responsibility does not negate fiduciary status); *IT Corp.*, 107 F.3d at 1420-21. Because the GAC affords TLIC discretion as to the method of the payment of its fees as well as discretion with respect to

the amount of those fees, which TLIC could unilaterally *raise*, TLIC is a fiduciary for purposes of Plaintiffs' prohibited transaction claims.

Therefore, under both prongs of 29 U.S.C. § 1002(21(A)(i) and under 29 U.S.C. § 1002(21)(A)(iii), TLIC "was acting as a fiduciary (that is, was performing a fiduciary function) when taking the action subject to complaint," *Pegram v. Herdrich*, 530 U.S. 211, 226 (2000), *i.e.*, withdrawing funds from Separate Accounts.

C. The District Court Correctly Found that Plaintiffs Plausibly Pleaded TLIC Was an ERISA Fiduciary with Regard to Plaintiffs' Excessive Fee Claims in Connection with the Fees of TLIC, TIM, and TAM.

TLIC's brief largely focuses on its fiduciary status in connection with Plaintiffs' claims that it charged and that it allowed TIM and TAM to charge excessive fees. TLIC was a fiduciary under 29 U.S.C. § 1002(21)(A)(iii) in connection with Plaintiffs' excessive fee claims because, after it was appointed, it "had discretion" to set and *lower* its fees or to eliminate excessively priced investment options from the investment menu. In addition, it was an ERISA fiduciary under 29 U.S.C. § 1002(21)(A)(i) because it "exercised" discretionary authority or control when it used part of the IM/Admin Fees to pay plan-level costs,

and when, after undertaking to monitor the expenses of investment options, chose to retain high priced options on the investment menu.[9]

1. TLIC "Has" Discretion.

First, under subsection (iii) of the statutory definition, one can be a fiduciary if he or she "has" discretion. *Yeseta*, 837 F.2d at 384-85; *Concha v. London*, 62 F.3d 1493, 1502 (9th Cir. 1995) ("defendants were given and accepted discretion to manage the Plan" which was "precisely the kind of discretionary control … that *Yeseta* requires"); *IT Corp.*, 107 F.3d at 1420-21.

As the district court determined in its order denying TLIC's motion to dismiss:

> TLIC could lower its fees at any time, without any approval apparently required from the employer. In such a scenario, TLIC has discretion over its fees because it has the power to modify them without approval.

ER199. In its order denying Plaintiffs' initial motion for class certification, the district court expanded upon this rationale:

[9] The law has long-ago dispensed with artificial distinctions between feasance and nonfeasance. George G. Bogert *et al.*, The Law of Trusts and Trustees § 591 (Sept. 2016 Update) ("Nonfeasance where there is a duty to act ought to be regarded as the equivalent of misfeasance."). And the law is clear that failure to act when one has the power to do so can violate ERISA. *Tibble v. Edison Int'l,* 135 S. Ct. 1823, 1828 (2015).

> [TLIC] did charge fees, and when it did so, it was within its discretion to adjust the fee to reasonably reflect its expenses and/or market conditions (subject to 30 days' notice). Thus, every time it charged fees, TLIC was acting with discretionary authority to set the level of those fees.

ER129.

Because TLIC "had discretion" to alter investment option fees, TLIC was a fiduciary with regard to the magnitude of those fees. *See Glass Dimensions, Inc. v. State Street Bank & Trust Co.,* 931 F. Supp. 2d 296, 306 (D. Mass. 2013); *Charters v. John Hancock Life Ins. Co.*, 583 F. Supp. 2d 189, 198 (D. Mass. 2008) (because service provider could change fees on three months' notice, that "discretion was sufficient to make [provider] an ERISA fiduciary with respect to its fees").

Second, TLIC was a fiduciary because it "had discretion" to alter the investment menu available for the Plans' and the participants' investment. *See Healthcare Strategies, Inc. v. ING Life Ins. & Annuity Co.,* 961 F. Supp. 2d 393, 400 (D. Conn. 2013) ("Various courts … have reasoned that the contractual right to substitute mutual funds in retirement plans can confer fiduciary status on service providers, regardless of whether they ever actually substitute funds."); *Haddock v. Nationwide Fin. Servs., Inc.*, 262 F.R.D. 97, 108 (D. Conn. 2009),

vacated on other grounds, 460 F. App'x 26 (2d Cir. 2012); *Charters v. John Hancock Life Ins. Co.*, 534 F. Supp. 2d 168, 171-73 (D. Mass. 2007); *Haddock v. Nationwide Fin. Servs., Inc.*, 419 F. Supp. 2d. 156, 164-68 (D. Conn. 2006). Since TLIC had the discretion to remove expensive TIM and TAM investment options from the investment menu, including those of TIM and TAM, it was an ERISA fiduciary under 29 U.S.C. § 1002(21)(A)(iii).

2. TLIC "Exercises" Discretion.

First, TLIC was an ERISA fiduciary under 29 U.S.C. § 1002(21)(A)(i) because it exercised discretion to divert money from the 75 basis point IM/Admin Fee that ostensibly was collected for investment management, and used that money to defray plan-level costs. *See supra* p. 7. No contract provision allows or contemplates this diversion.

Second, it exercised its discretion to keep high priced funds on the menu when it undertook to monitor fees and expenses. In *Tibble v. Edison International,* 135 S. Ct. 1823, 1828 (2015), the Supreme Court reasoned that an ERISA fiduciary

> has a continuing duty to monitor trust investments and remove imprudent ones. This continuing duty exists

separate and apart from the trustee's duty to exercise prudence in selecting investments at the outset.

After the GAC is signed, TLIC promises to monitor the "Fees & Expenses," of each investment choice, and if it fails to meet TLIC's "stringent criteria," TLIC will remove the investment choice from the plan's line-up. SR22. Notwithstanding its obligations and the undertaking to monitor expenses, TLIC exercised its discretion by concluding that its fees and those of TIM and TAM, although excessive, should remain on the investment menu because they met TLIC's "stringent criteria." ER163-164.

Therefore, TLIC was a fiduciary with regard to all excessive fee claims.

D. Neither the GAC nor TLIC's Negotiations with Plan Sponsors Can Absolve TLIC of Its Fiduciary Responsibilities.

1. The GAC Cannot Authorize TLIC to Commit Future ERISA Violations.

TLIC maintains that, if the plans were injured, TLIC is nonetheless immune from liability because the GAC allows TLIC to self-deal and charge excessive fees. Therefore, according to Defendants, TLIC need not comply with ERISA's requirements when it later becomes a fiduciary. TLIC errs for several reasons.

First, 29 U.S.C. § 1110(a) provides:

> Except as provided in sections 1105(b)(1) and 1105(d) of this title, any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part shall be void as against public policy.

See also Cent. States v. Cent. Transp., Inc., 472 U.S. 559, 568 (1985) ("trust documents cannot excuse trustees from their duties under ERISA"); *Kayes*, 51 F.3d at 1460 (a fiduciary cannot by agreement relieve itself of fiduciary responsibilities). Once TLIC became a fiduciary, it was required to comply with ERISA irrespective of whether its misconduct may or may not have been permitted by the GAC.

Second, TLIC's negotiations with plan sponsors could not authorize future ERISA violations that injure plan participants who were not parties to those negotiations. *See IT Corp*, 107 F.3d at 1418. There, a service provider argued that it could not be held liable for a breach of fiduciary duty because the contract it negotiated with the employer-plan-sponsor exonerated it from any fiduciary responsibilities. In rejecting this argument, this Court stated:

> First, a contract exonerating an ERISA fiduciary from fiduciary responsibilities is void as a matter of law. Second, a fiduciary's contract with an employer cannot get it off the hook with the employees who participate in the ERISA plan.

Id.

As the district court determined, the negotiations between TLIC and the plan sponsors were not true arm's length negotiations:

> It appears to the court that TLIC and the employer are not bargaining for TLIC to provide services and for the employer to pay a fee, but instead for TLIC to provide services and for a fee to be assessed on the employees' retirement accounts. If this is true, it is not a traditional arm's length negotiation where the parties are adverse and pursuing independent interests; instead, the parties are collaborating to manage the employees' 401(k) plans.

ER197-198.

Third, nothing about the negotiations authorized TLIC to (1) withdraw fees for itself and TIM and TAM from Separate Accounts without review by another fiduciary, or (2) to use those fees to defray plan-level costs. SR195; SR216; Br. 6-7.

Fourth, if TLIC were absolved of responsibility because it was not a fiduciary when it negotiated the GAC, its promise to monitor fees, SR22; ER163, and to assist plan sponsors as a co-fiduciary, ER154; ER166; ER168; ER175, would be illusory. The goal of ERISA, to protect employee retirement assets, would be frustrated.

Thus, the district court ruled, as this Court did in *IT Corp.*, that TLIC could not, in the GAC, immunize itself from liability for its conduct once it became a fiduciary:

> The contract can immunize the future fiduciary TLIC from fiduciary breach no more than it can immunize the employer. To hold otherwise would allow fiduciaries to contract themselves out of their duties, so long as it was done prior to the assumption of those duties.

ER196.

2. The Conduct of Plan Sponsors is Irrelevant.

In a related argument, TLIC maintains that the plans should look to plan sponsors who signed the GAC. The possible liability of plan sponsors has nothing whatever to do with TLIC's responsibility. *Kanawi v. Bechtel Corp.*, 590 F. Supp. 2d 1213, 1225 (N.D. Cal. 2008) (ERISA service provider "cannot hide behind the [plan sponsor's] oversight to shield itself from possible liability over its own actions .... Accordingly, FIA was a fiduciary ...."); *IT Corp.*, 107 F.3d at 1418 (sponsors' conduct cannot get fiduciary "off the hook" for its responsibilities to plan). What matters are the powers *TLIC* had. Plans typically have several different fiduciaries that perform different functions and thus an entity need not have absolute discretion to qualify as a fiduciary. *See, e.g., Blatt v.*

Marshall & Lassman, 812 F.2d 810, 812 (2d Cir. 1987); *United States v. Glick*, 142 F.3d 520, 527-28 (2d Cir. 1998).

TLIC argues that sponsors retained the ability to reject any changes which TLIC might make in its fees or the composition of the investment menu by terminating their participation. Therefore, according to TLIC, it could not be a fiduciary merely because it could alter fees or the investment menu. Br. 32. TLIC errs for three reasons. First, a plan sponsor cannot reject these changes. *See* ER177 at n.16 (Transamerica may close an investment choice "outside of the general time guidelines … [f]or other reasons at the discretion of the investment committee.") Second, even were a plan to elect to discontinue its relationship with TLIC, that process is cumbersome and time consuming. Third, as the district court found:

> In making this argument, TLIC conflates an ability to change the fees with the consequences of changing the fees …. In such a scenario, TLIC has discretion over its fees because it has the power to modify them without approval; whether the employer chooses to terminate the contract or not is immaterial to determining whether TLIC has the discretion to change the fees.

ER199.

3. TLIC's Reliance on Out of Circuit Cases is Misplaced.

Finally, TLIC relies upon decisions of other Courts of Appeals that, according to TLIC, stand for the proposition that a service provider has no fiduciary responsibility to plan participants when negotiating its fees and the manner in which those fees will be paid. Br. 27-28. However, those decisions are inconsistent with this Court's decision in *IT Corp.*, 107 F.3d 1415, and are distinguishable. As a threshold matter, not a single one of these cases involve a fiduciary who exercises "authority and control" over plan assets and who exercises discretion to divert funds intended for one purpose, investment management of the Separate Account, to another, to defray plan-level costs. The cases upon which TLIC relies are, in other respects distinguishable.

For instance, in *Renfro* v. *Unisys Corp.*, 671 F.3d 314 (3d Cir. 2011), the Third Circuit rejected a claim of ERISA fiduciary status based upon plaintiff's assertion that a directed trustee could veto proposed changes to the investment lineup. The Court held that the "veto power" was insufficient to confer fiduciary status because "Fidelity had no contractual authority to control the mix … of investment options

. . . .” *Id.* at 323. Here, TLIC (who is not a directed trustee) does, as the district court determined, have the authority to control that mix.

In another Third Circuit decision, rejected by the district court here, *Santomenno v. John Hancock Life Ins.* 768 F.3d 284, 297 (3d Cir. 2014), the court concluded that in the absence of the exercise of discretion, the defendant was not a fiduciary. The *Santomenno* court, however, ruled that any argument under subsection (iii) of 29 U.S.C. § 1002(21)(A) (one who “has discretion” is a fiduciary) had been “waived,” *id.* at 300, because plaintiffs argued fiduciary status only under “the first prong” of 29 U.S.C. § 1002(21)(A)(i). The 9th Circuit has construed subsection (iii) to confer fiduciary status in circumstances such as this, *i.e.*, where the putative fiduciary “had” discretion. *Yeseta,* 837 F.2d 380. Moreover, the Supreme Court in *Tibble*, 135 S. Ct. 1823, held that a fiduciary’s failure to act can be the basis of a fiduciary violation.

Leimkuehler v. American United Life Insurance Co., 713 F.3d 905 (7th Cir. 2013), relied upon by the amici but not TLIC, is similarly limited: it did not address subsection (iii) at all. Further, unlike in *Leimkuehler*, which presented a general challenge to a service

provider's receipt of payments from mutual fund companies and a provider's share class selection, Plaintiffs here allege mismanagement of the Separate Account attributable to improper withdrawals of the "IM/Admin Fee"—*i.e.*, TLIC's "handling" of Separate Accounts. *Cf. Leimkuehler*, 713 F.3d at 913 (no challenge to direct fees paid by participants). Also, in that case, there was no contention that the putative fiduciary misused its authority over the separate account, which is what Plaintiffs contend here.

In *McCaffree Financial Corp. v. Principal Life Insurance Co.,* 811 F.3d 998 (8th Cir. 2016), the court found that no fiduciary status applied to initial fund selection and, as pleaded, the plaintiffs' claims with regard to investment advice (none of which is at issue here). Further, no prohibited transaction claims were the subject of the opinion. The Court did however find that fiduciary status was not conferred by the ability to alter fees. That decision is incorrect and inconsistent with the overwhelming weight of authority. Moreover, the court there noted that plaintiffs did *not* allege that the putative fiduciary passed "through unreasonable or fabricated expenses," but used the separate account only to pay those "expenses which 'must be

paid' to operate the accounts." *Id.* at 1004 n.3. Here, Plaintiffs allege diversion of IM/Admin Fees from the Separate Accounts, which TLIC had promised to use for investment management, but instead diverted to plan-level costs. *See infra* Section V.

TLIC also claims that *Hecker v. Deere & Co.*, 556 F.3d 575 (7th Cir. 2009) absolves it of liability. Br. 27. However, *Hecker* distinguished its holding from *Haddock*, *see supra* pp. 29-30, because, as here and in *Haddock*, the service provider had the "authority to delete and substitute mutual funds from the plan without seeking approval," *Hecker*, 556 F.3d at 584, which is the basis upon which Plaintiffs here seek to impose fiduciary status with regard to their excessive fee claim. Moreover, neither *Hecker* nor *Renfro* involves insurance company separate accounts.

In this Circuit, *see supra* pp. 20-31, and in other Circuits, the retention of control and authority or the retention of discretion make a service provider a fiduciary. *F.H. Krear & Co. v. Nineteen Named Trustees*, 810 F.2d 1250, 1259 (2d Cir. 1987) ("[A]fter a person has entered into an agreement with an ERISA-covered plan, the agreement may give it such control over factors that determine the amount of its

compensation that the person thereby becomes an ERISA fiduciary with respect to that compensation."); *Ed Miniat, Inc. v. Globe Life Ins. Grp., Inc.*, 805 F.2d 732, 737 (7th Cir. 1986); *see also Healthcare Strategies, Inc.*, 961 F. Supp. 2d at 401 (holding that reasoning of *Leimkuehler* "is of limited value … because the Seventh Circuit only analyzed whether the contractual right to substitute funds implicated fiduciary status under subsection one … rather than subsection three, which makes possession of authority, not its exercise, the key determinant of fiduciary status").

Thus, once a service provider becomes a fiduciary, it must act in accordance with ERISA and no contract can immunize it from fiduciary liability. 29 U.S.C. § 1103.

II. Section 1106(b)(1)'s Per Se Prohibition on Fiduciary Self-Dealing Precludes a Fiduciary Like TLIC from Extracting Its Fees from Plan Assets.

ERISA's fiduciary obligations are the "highest known to the law." *Donovan v. Bierwirth*, 680 F.2d 263, 272 n.8 (2d Cir. 1982). The "crucible of congressional concern" in enacting ERISA "was misuse and mismanagement of plan assets" by plan fiduciaries. *Mass. Mut. Life Ins. Co. v. Russell*, 473 U.S. 134, 140 n.8 (1985). "One facet of plan misuse

particularly troubling to Congress was self-dealing by fiduciaries." *Nat'l Sec. Sys., Inc. v. Iola*, 700 F.3d 65, 96 (3d Cir. 2012).

To ensure that fiduciaries did not misuse plan assets, Congress included in ERISA the fiduciary duty of loyalty, which requires that a fiduciary act "solely in the interest of the participants and beneficiaries" of a plan and for the "exclusive purpose" of providing benefits and paying expenses. ERISA § 404(a)(1)(A), 29 U.S.C. § 1104(a)(1)(A); *see also* Daniel Fischel & John H. Langbein, *ERISA's Fundamental Contradiction: The Exclusive Benefit Rule*, 55 U. Chi. L. Rev. 1105, 1110-15 (1988).

Congress "supplement[ed]" this general duty of loyalty by enacting 29 U.S.C. § 1106, which "categorically bar[s] certain transactions deemed 'likely to injure the pension plan.'" *Harris Trust & Sav. Bank v. Salomon Smith Barney, Inc.*, 530 U.S. 238, 241 (2000) (citation omitted). The transactions described in 29 U.S.C. § 1106 are "per se ERISA violation[s]," that constitute statutory violations "even in the absence of bad faith, or in the presence of a fair and reasonable transaction." *Patelco Credit Union v. Sahni*, 262 F.3d 897, 911 (9th Cir. 2001) (quoting *Gilliam v. Edwards*, 492 F. Supp. 1255, 1263 (D.N.J.

1980)). In other words, Congress enacted a "blanket prohibition of certain acts" that can be "easily applied, in order to facilitate Congress's remedial interest in protecting employee benefit plans." *Id.*

One of the acts that is strictly prohibited is self-dealing by a fiduciary. Specifically, 29 U.S.C. § 1106(b)(1) provides that a fiduciary shall not "deal with the assets of the plan in his own interest or for his own account." In light of Congress's overriding concern with the protection of plan participants and beneficiaries, the protections provided by this subsection must be construed "broadly." *Acosta v. Pac. Enters.*, 950 F.2d 611, 620 (9th Cir. 1992); *see also Reich v. Compton*, 57 F.3d 270, 288 (3d Cir. 1995) (29 U.S.C. § 1106 is to be broadly construed).

A. This Court's Recent Decision in *Barboza*, Which is Controlling Authority, Holds That a Fiduciary's Payments to Itself out of Plan Assets Constitutes a Per Se Violation of Section 1106(b)(1).

Plaintiffs' prohibited transaction claims based on TLIC's payment of its own fees out of plan assets is controlled by this Court's recent decision in *Barboza v. California Association of Professional Firefighters*, 799 F.3d 1257. There, the named fiduciary under an employee welfare benefit plan employed a service provider, CAISI, to

act as the plan's administrator. *Id.* at 1263. The employee's contributions into the plan were deposited into a checking account controlled by CAISI. *Id.* In addition to paying benefits to eligible participants from the account, CAISI also, as in this case, paid its own service fees directly out of this account. *Id.* The payment was authorized by CAISI's administrative services agreement with the plan sponsor. *Id.* at 1270 n.5.

The Court concluded that CAISI's practice of paying its own fees and expenses from the plan assets held in the plan checking account constituted a per se violation of ERISA's prohibition against self-dealing under § 1106(b). 799 F.3d at 1270. In the course of its discussion, this Court explained:

> Because fiduciary self-dealing under 29 U.S.C. § 1106(b)(1) is a per se violation of ERISA, it is irrelevant that CAISI was authorized to pay its own fees and expenses from Plan assets pursuant to its administrative services agreement with [the plan sponsor].

Id. at 1270 n.5.[10] Thus, *Barboza* holds that, even if the service provider-fiduciary's fees are authorized by its agreement with the plan sponsor

[10] The Court further rejected CAISI's argument that its fees were exempted from ERISA's prohibition on self-dealing by 29 U.S.C. § 1108(c)(2), which permits "reasonable compensation for services

(though also TLIC in fact determined the *amount* of its fees, *see supra* pp. 10-11, 28-30), and even if those fees were reasonable (though Plaintiffs contend they were not, *see infra* Section V), the payment of those fees out of plan assets constitutes a per se violation of 29 U.S.C. § 1106(b)(1). *See id.* at 1270 ("Here, CAISI is a fiduciary that paid its own fees from Plan assets, and thus engaged in prohibited transactions under 29 U.S.C. § 1106(b)(1).").

TLIC does not even mention *Barboza* until the ninth page of its discussion of Plaintiffs' prohibited transaction claim. Br. 47. At that point, TLIC does not attempt to distinguish *Barboza* based on anything stated in the opinion but instead relies upon statements in the briefs submitted in that appeal. Br. 48. Moreover, the "facts" that TLIC purports to glean from those briefs are inconsistent with the facts found by the district court in *Barboza,* which stated that the plan sponsor and fiduciary service provider "negotiated and mutually agreed upon [the fiduciary's] fees, rather than [the fiduciary] determining them unilaterally." *Barboza v. Cal. Ass'n of Prof'l Firefighters*, No. 08-02569,

rendered." *See infra* Section III.B (addressing exemptions from ERISA's prohibited transaction provisions).

2011 WL 285022, at *9 (E.D. Cal. Jan. 25, 2011). This Court explained that *as a matter of law*, it is "irrelevant that [the fiduciary service provider] was authorized to pay its own fees and expenses from Plan assets" because "fiduciary self-dealing under 29 U.S.C. § 1106(b)(1) is a per se violation of ERISA." *Barboza*, 799 F.3d at 1270 n.5. Therefore, this Court should reject TLIC's attempt to distinguish *Barboza* based on facts that are not set forth in the opinion.

Defendants cite to *Wright v. Oregon Metallurgical Corp.*, 360 F.3d 1090 (9th Cir. 2004), arguing that this case supports their position. *Wright* is inapposite because, *inter alia*, in that case, there was no "transaction" and the defendant was not a fiduciary. *Acosta* is also distinguishable because that case involved a fiduciary who took no action (to use a list of plan participants) which differs from this case in which a fiduciary paid itself from plan assets. 950 F.2d at 621.

Plaintiffs have alleged, SR127-128; SR130-131, and the evidence will demonstrate that TLIC engaged in precisely the sort of self-dealing that *Barboza* prohibits. As discussed *supra* pp. 24-25, assets within each Separate Account are "plan assets." TLIC, a fiduciary, collects its IM/Admin Fees by withdrawing prorated amounts daily from the assets

of each separate account. *See* ER350 (IM/Admin Fees "withdrawn daily"); ER357-361 (listing fees); *accord* ER379, ER385-389. In addition, TLIC had discretion to do so and exercised that discretion. *See* 29 U.S.C. § 1002(21)(A)(i) and (iii). *See also supra* at 26-27. TLIC, a fiduciary, "paid its own fees from Plan assets, and thus engaged in a prohibited transaction under 29 U.S.C. § 1106(b)(1)." *Barboza,* 799 F.3d at 1270; *accord Teets v. Great-West Life & Annuity Ins. Co.*, 315 F.R.D. 362, 373 (D. Colo. 2016).

B. TLIC's Attempts to Avoid These Per Se Violations Fail.

1. Common Law Trust Principles Do Not Authorize TLIC's Misconduct.

Defendants argue that "principles of trust law" permit a fiduciary to "withdraw its compensation from the trust's assets in accordance with the trust document." Br. 43-44. Although ERISA's fiduciary duties are derived from the common law of trust, the common law of trusts is only a "'starting point' for analysis" and "must give way if it is inconsistent with 'the language of the statute, its structure, or its purposes.'" *Hughes Aircraft Co. v. Jacobson*, 525 U.S. 432, 447 (1999) (citation omitted).

Congress enacted the prohibited transaction rules in order to "supplement[]" general fiduciary duties in "respon[se] to deficiencies in prior law regulating transactions by plan fiduciaries." *Harris Trust*, 530 U.S. at 241; *Varity Corp. v. Howe*, 516 U.S. 489, 496 (1996) (Congress enacted ERISA because of inadequacies in the common law of trusts). ERISA imposes stricter limitations than trust law and it is the language of the statute that ultimately controls. *Kayes*, 51 F.3d at 1461 (""The legislative history is replete with indications of congressional concern to assure adequate protection for the interests of plan participants and beneficiaries beyond that available under conventional trust law.""); *C.I.R. v. Keystone Consol. Indus., Inc.*, 508 U.S. 152, 160 (1993) ("Before ERISA's enactment in 1974, the measure that governed a transaction between a pension plan and its sponsor was the customary arm's-length standard of conduct. This provided an open door for abuses….").

2. TLIC's Focus On "Causation" Is Misplaced.

TLIC, relying on a misreading of the statutory text and a distinguishable Department of Labor regulation, contends that the district court failed to focus on whether it "*caused* the challenged

transaction through an exercise of fiduciary discretion." Br. 41, 44-46 (emphasis added). Contrary to Defendants' textual argument, liability under the plain language of 29 U.S.C. § 1106(b) is predicated upon a fiduciary's dealing directly with plan assets, not upon *causing* some *other* misconduct. *Id.* § 1106(b)(1) ("A fiduciary with respect to a plan shall not … deal with the assets of the plan in his own interest or for his own account …."). Unlike § 1106(a), which addresses transactions where a fiduciary "*cause*[*s*] the *plan* to engage in" transactions with other parties in interest, the plain language of § 1106(b) omits any causation requirement and instead describes direct transactions between the fiduciary and the plan. *See Loughrin v. United States*, 134 S. Ct. 2384, 2390 (2014) ("[W]hen 'congress includes particular language in one section of a statute but omits it in another'—let alone in the very next provision—this Court 'presume[s]' that Congress intended a difference in meaning.") (citation omitted). It is the direct action of the fiduciary dealing with plan assets—and not some *other* plan misconduct *caused* by the fiduciary—that constitutes the prohibited transaction within the meaning of § 1106(b). Thus, as the district court correctly concluded, § 1106(b) does not contain any

requirement to "cause" some separate transaction as in § 1106(a). *See, e.g.*, ER85-86.

What defendants refer to as "causation" is the uncontroversial principle that a service provider can be liable for a fiduciary breach only if it "was acting as a fiduciary (that is, was performing a fiduciary function) when taking the action subject to complaint." *Pegram v. Herdrich*, 530 U.S. at 226. The district court found this to be the case:

> TLIC used the "authority, control [and] responsibility" that made it a fiduciary to pay itself out of the plan assets over which it exercises that authority, control, and responsibility, which is a per se prohibited transaction.

ER38.

The Department of Labor regulation upon which TLIC relies describes § 1106(b)'s prohibition on self-dealing as applying to instances where a fiduciary "use[s] the authority, control, or responsibility which makes such person a fiduciary to cause a plan to pay an additional fee to such fiduciary." Br. 44 (quoting 29 C.F.R. § 2550.408b-2(e)(1)). Defendants emphasize the use of the words "use" and "cause," but these words simply refer to the basic concept under ERISA that there must be a nexus between a fiduciary breach and breaching party's fiduciary

status. When a fiduciary uses its control or authority over plan assets to extract its own fees from plan assets, that nexus exists.

Defendants also cite an example in a Department of Labor regulation that explained that a service providing fiduciary has not engaged in self-dealing in violation of section § 1106(b)(1) where a plan's employer approves the service provider's proposal to perform a service for an additional fee. Br. 45-46 (citing 29 C.F.R. § 2550.408b-2(f) (Example 1)). But this example does not address a situation where, as here and in *Barboza*, the service provider had control over plan assets in separate accounts and extracted its fee directly from the plan assets under its control.

Notably, the very regulation upon which Defendants rely explains that

> because the authority, control or responsibility which makes a person a fiduciary may be exercised 'in effect' as well as in form, mere approval of the transaction by a second fiduciary [here, a plan sponsor] does not mean that the first fiduciary has not used any of the authority, control or responsibility which makes such person a fiduciary to cause the plan to pay the first fiduciary an additional fee for a service.

29 C.F.R. § 2550.408b-2(e)(2).

Contrary to Defendants' contentions, the fact that "each independent plan fiduciary" signed the form GAC does not mean that those other fiduciaries—and not TLIC—"caused the investment transactions that resulted in the payment of fees to TLIC." Br. 46. This argument erroneously assumes that the only "transactions" that matter are the initial contractual arrangements between TLIC and the plan sponsors. But this Court has routinely held that fee payments themselves are relevant "transactions" for a claim under § 1106(b), *see, e.g.*, *Barboza*, 799 F.3d at 1269–70; *Patelco*, 262 F.3d at 909–12, and they occur each time TLIC *extracts its own fees* from the Separate Accounts, over which TLIC exercises control. Moreover, as discussed above, the plan sponsor in *Barboza* had signed a contract with the insurer that authorized the insurer to pay its own fees from plan assets, and this Court correctly found that fee extractions were prohibited transactions. 799 F.3d 1279 & n.5.

TLIC also argues that, even if a fiduciary has control over plan assets and uses such control to extract its fees from those plan assets, it does not "cause" the fees to be extracted through an exercise in fiduciary authority if the *amount* of the fees was contractually pre-determined.

See Br. 40, 47-49. However, as discussed *supra* pp. 42-26, this argument cannot be reconciled with *Barboza*.

3. Even if *Barboza* Required that a Fiduciary Have Discretion Over the Amount of Its Fees, Common Facts Demonstrate that TLIC Possessed Such Discretion.

Even if, as Defendants contend, a fiduciary that extracts its fees from plan assets under its control has exercised fiduciary authority—and thus "caused" its self-dealing—*only if* the fiduciary also had authority to determine the *amount* of its fees, *see* Br. 47-49, this is precisely what TLIC does. The GAC explicitly provides that TLIC "reserve[s] the right to change" the IM/Admin Fees "upon advance written notice to the Contractholder of at least 30 days." ER351. *Accord* ER357; ER380; ER385.

Although Defendants appear to deny that this language actually gave TLIC the authority to change its fees, *see, e.g.*, Br. 41, 47-49, this is a merits question that is indisputably common to the certified classes and capable of generating a common answer. Defendants do not dispute that TLIC used uniform GAC contracts and that the GAC contracts for each of the plans within the class contained the same provision giving TLIC the unilateral discretion to raise its IM/Admin Fees upon 30 days

advanced notice. ER351; ER357; ER380; ER385. Defendants cannot dispute that the IM/Admin Fees are set at the Separate Account level, and thus any changes to fees charged on any given Separate Account would apply uniformly to all plans offering that Separate Account. And because 1106(b)(1) provides a per se prohibition, plan-level questions of reasonableness in light of other plan-level fees are irrelevant.

Defendants also argue that TLIC did not "choose its own fees"—*i.e.*, did not exercise its fiduciary discretion to set its fees—because the amount the fees it decided to withdraw on an ongoing basis was consistent with the amount initially included in the schedule of fees attached to the GAC. Br. 41. The *decision* to maintain a constant fee, rather than to increase or decrease the fee, is itself an exercise of discretion, which occurs anew when TLIC decides to withdraw its fees from the Separate Accounts. As the district court explained,

> The power of free decision comprises not only the power to act but the power not to act. A person without discretionary authority has no choice with respect to acting or not acting; she is required either to act or to refrain from acting, depending on the circumstances. A person with discretionary authority, in contrast, may act or not act, as she deems best. But she exercises her discretion no less in choosing not to act than in choosing to act.

ER205.

Indeed, a fiduciary with ongoing discretionary authority has a duty to regularly reevaluate its decisions; it cannot assume it is permissible to stay the course merely because an original decision was permissible. *Tibble*, 135 S. Ct. at 1828. TLIC decided to pay itself, and "when it did so, it was within its discretion to adjust the fee to reasonably reflect its expenses and/or market conditions (subject to 30 days' notice)." ER129.

TLIC further exercises discretion over its fees by charging 75 basis points in IM/Admin Fees on each Separate Account and then deciding to use part of those fees for purposes other than the management or administration of the Separate Accounts. Specifically, although TLIC represented to the plan sponsors annually that "Investment Management and Administrative Charge Expenses [are] for managing and administering the assets in the separate accounts," SR161, TLIC's own expert explained that the "IM and Admin Fees…[do] not…simply … cover the specific services associated with the Separate Accounts to which they apply…." SR195. Rather, as TLIC elsewhere explained, the "IM/Admin fees subsidize other services …." SR216; SR215 ("Revenues from particular fees are not earmarked to specific services ….").

Accordingly, the facts alleged, as supported by the terms of the GAC—which are common to the class—demonstrate that TLIC had and exercised discretion and control over the amount of its own fees and withdrew those fees from plan assets in separate accounts. These are prohibited transactions.

III. TLIC's Prohibited Transactions Are Not Subject to the Exemption Found in Section 1108(b)(8).

A. Section 1108(b)(8)'s "Reasonable Compensation" Exemption Applies Only to Section 1106(a) Prohibited Transactions, Which Are Not at Issue Here.

TLIC's reliance on ERISA section 408(b)(8), 29 U.S.C. § 1108(b)(8), which provides a limited exemption from certain prohibited transactions for "reasonable compensation," is misplaced. *See* Br. 52-57. This Court has held that § 1108 exemptions apply only to § 1106(a) violations not to § 1106(b) violations. *Patelco*, 262 F.3d at 911 (concluding that the "reasonable compensation" provision in 1108(b)(2) "does not apply to fiduciary self-dealing" as prohibited by ERISA 1106(b)). As explained in *Patelco*:

> 29 U.S.C. § 1106(a) prohibits fiduciaries from causing the plan to engage in specified transactions with parties in interest "[e]xcept as provided in section 1108 of this title." But 29 U.S.C. § 1106(b), which prohibits fiduciary self-dealing, *makes no mention of the exceptions in § 1108.*

262 F.3d at 910 (emphasis added). *See also Hi-Lex Controls, Inc. v. Blue Cross Blue Shield of Mich.*, 751 F.3d 740, 750 (6th Cir. 2014) ("[T]he majority of courts that have examined this statutory interpretation issue have held that § 1108 applies only to transactions under § 1106(a), not § 1106(b)."). In *Barboza* this court concluded, in addressing an analogous exemption for "reasonable compensation" in 29 U.S.C. § 1108(c)(2), that

> while a plan may pay a fiduciary "reasonable compensation for services rendered" under 29 U.S.C. § 1108, the fiduciary may not engage in self-dealing under 29 U.S.C. § 1106(b) by paying itself from plan funds. Such conduct constitutes a per se violation of § 1106(b).

797 F.3d at 1269 (citation omitted).

The district court correctly concluded "that the reasoning behind" this Court's "conclusion in *Barboza* and *Patelco* applies with equal force to other potential exemptions in § 1108," such that an exemption listed in § 1108 will not apply to self-dealing and other violations of section 1106(b) unless the exemption "explicit[ly] nam[es] … 1106(b) – like occurred for cross trading in (b)(19)…." ER93 n.4.

Defendants cite footnotes in two DOL advisory opinions that stated that "if all conditions of the exemption are met, section 408(b)(8)

will provide relief from sections 406(a)(1)(A), 406(a)(1)(D), 406(b)(1) and 406(b)(2)." DOL Adv. Op. No. 96-15A, 1996 WL 453859, at *3 n.3 (Aug. 7, 1996); DOL Adv. Op. No. 05-09A, 2005 WL 1208696, at *5 n.2 (May 11, 2005); Br. 53.

The statutory construction reflected in these opinions is not entitled to judicial deference under *Chevron, U.S.A. v. NRDC, Inc.*, 467 U.S. 837, 843 (1984), because it was not arrived at through "a formal adjudication or notice-and-comment rulemaking," *Christensen v. Harris Cnty.*, 529 U.S. 576, 587 (2000), and was not intended to be binding on third parties, *United States v. Mead Corp.*, 533 U.S. 218, 233 (2001); *Patelco*, 262 F.3d at 908 (DOL advisory opinion "is not binding") (citing ERISA Procedure 76-1, § 10). Certainly the DOL cannot, in responding to individual inquires, overrule contrary Ninth Circuit case law.

Moreover, the DOL has made clear through notice and comment rulemaking that, at least where a specific exemption in § 1108 does not explicitly apply to § 1106(b) violations, fiduciary self-dealing in violation of § 1106(b) is "not exempt" under an § 1108 exemption. 29 C.F.R. § 2550.408b-2(e)(1) (if conduct violates § 1106(b), "such an act

constitutes a separate transaction which is not exempt under section 408(b)(2) of the Act").

B. Even if the Section 1108(b)(8) Exemption Generally Applied to Section1106(b) Violations, By Its Plain Terms, This Exemption Does Not Apply to a Fiduciary's Repeated Decisions to Extract Its Own Fees from Plan Assets.

By its plain terms, the § 1108 (b)(8) exemption for "reasonable compensation" applies only to transactions between a plan and a "pooled investment fund," not to a transaction between a plan and a *fiduciary*. In addition, according to 29 U.S.C. § 1108(b)(8)(A), the transaction must involve the "sale or purchase of an interest in the fund." This provision has nothing whatsoever to do with TLIC's repeated and unilateral extraction of its fees.

The transaction challenged here is not a transaction between the plan and the Separate Accounts. Rather, the challenged transactions occur every time TLIC, a fiduciary, extracts *its fees* from the plan assets in the Separate Accounts. As the district court explained, "[t]he transaction Plaintiffs challenge is not 'a sale or purchase in the fund' but instead the act of TLIC taking its own fees out of the plan assets over which TLIC exercises fiduciary management." ER89.

In addition, Defendants' contrary argument, Br. 54, is based on the false premise that TLIC did not exercise any discretion or control over the amount of or extraction of its fees from plan assets. As addressed *supra* Sections I.A-C, this argument is both factually and legally flawed. Because TLIC's exercise of control and discretion was necessary to effect each extraction of fees, the relevant transactions are not the initial investments by plans into the Separate Accounts but instead TLIC's repeated decisions to extract its own fees from the Separate Accounts.

Defendants misconstrue an excerpt from the legislative history. Br. 55. The House Conference Committee Report Defendants rely upon stated that an otherwise prohibited transaction was permissible so long as "no more than reasonable compensation may be paid by the plan in the purchase (or sale) and no more than reasonable compensation may be paid by the plan for investment management by the pooled fund." H.R. Rep. No. 93-1280, pt. 1, at 316 (1974), *reprinted in* 1974 U.S.C.C.A.N. 5038, 5096. But as the district court explained, Defendants read "paid by the plan" to mean "paid by the plan by the fiduciary taking the reasonable compensation out of the plan's assets

over which it exercises fiduciary control." ER45. This provision suggests only that Congress intended to permit a fiduciary to be paid a reasonable fee in connection with investment management of a pooled fund. Nothing suggests Congress wanted to permit a fiduciary to *unilaterally extract* its compensation directly from assets under its control, and certainly nothing suggests that Congress wanted to permit such self-dealing where the fiduciary also had retained *discretion over the amount of its fees*. For this same reason, Defendants' reliance, Br. 55-56, on DOL Advisory Opinions is misplaced.

Ultimately, nothing in § 1108(b)(8) (or the legislative history or the regulatory materials) suggests that a fiduciary may claim this exemption to shield its use of its fiduciary authority to repeatedly extract its own fees from plan assets *following* a covered sale or purchase. Absent a specific exemption from § 1106 for such practices, TLIC's practice of paying itself from plan assets violates § 1106(b)(1)'s prohibition of fiduciary self-dealing.

IV. The TIM/TAM Class Was Properly Certified.

The district court certified a class of plans that invested in the Affiliated Separate Accounts that in turn invested in underlying mutual

funds managed by TLIC's affiliate, TAM, or are directly advised by TLIC's affiliate, TIM. Although this class was certified with respect to two claims—(1) that TLIC committed prohibited transactions under both § 1106(b)(1) and (b)(2); and (2) that TLIC breached its fiduciary duties of loyalty and prudence by allowing TIM and TAM to charge excessive fees on plan assets invested in the Affiliated Separate Accounts, ER68; ER77; ER95-97—Defendants do not challenge the district court's certification of the TIM/TAM class with respect to the § 1106 prohibited transaction claims. *See* Br. 57-61.

While Defendants do challenge the certification of this class with respect to the excessive fee claims, *id.*, they fail to show that the district court *abused its discretion* in concluding the common questions predominate within the meaning of Fed. R. Civ. P. 23(b)(3)—and their assertions are based on a misuse of the term "due process."

Defendants' argument appears to be that the Court cannot assess the excessiveness of the fees charged by TIM and TAM without assessing the reasonableness of the total fees collected by TIM, TAM, *and* TLIC on the Separate Accounts. Br. 58-59. But this argument misconstrues Plaintiffs' claims. The claim is not that *TLIC's* fees are

excessive, but rather that the fees charged by TIM and TAM—distinct entities who provide services comparable to those provided by advisors to all underlying mutual funds—were excessive in light of the services *these entities* provided. SR167-170; SR171-172. Specifically, although TIM and TAM offer substantially identical services to other investors to whom TLIC owes no fiduciary duty, TIM and TAM charge the Affiliated Separate Accounts substantially higher fees than they charge others. *Id.* "TLIC's bundled service arrangement," Br. 58, has *nothing* to do with whether TIM and TAM charged excessive fees for the services TIM and TAM provided in their role as advisors to underlying investment vehicles.

The "facts" that Defendants cite in support of their bundling defense consist of (a) pages in their briefing that do not cite evidence indicating that TIM and TAM's fees and services were bundled with TLIC's fees and services, *see* Br. 58-59 (citing ER396-97; ER60-61), and (b) a declaration that addresses TLIC's fees, but not TIM's or TAM's fees, Br. 59 (citing ER257). Defendants cannot credibly contend that these citations establish that the district court abused its discretion.

If, during the course of future proceedings in the district court, Defendants submit evidence indicating that that TLIC's, TIM's, and TAM's fees and services are bundled and must be considered collectively, and assuming *arguendo* such facts would cause individual issues to predominate, Defendants can move to decertify the class. However, on the record before it on the motion for class certification, the district court reasonably concluded that resolving the TIM and TAM excessive fee claims will not require any plan-level analysis of the reasonableness of all fees charged collectively by TLIC, TIM, and TAM. And because TIM and TAM provide identical services to each underlying investment, the reasonableness of these fees can be evaluated based on facts common to the class.

V. TLIC's and Its Amici's Policy Arguments Are Flawed and Misplaced.

In several portions of their brief, TLIC and the amici contend that, were Plaintiffs to prevail at trial, "it would be especially disruptive to small employers," Br. 30, the market is already competitive, and compliance with ERISA "would wreak havoc" because "[t]he investment industry broadly relies on asset-based fee arrangements." Br. 49-50.

Those arguments are irrelevant, unsupported in the record, and inconsistent with ERISA.

TLIC's arguments are irrelevant because in *John Hancock Mut. Life Ins. Co.*, 510 U.S. at 110, the Supreme Court responded to the very same arguments of insurance companies: that to hold them to fiduciary standards with regard to their separate accounts would be disruptive and costly. As to these concerns, the Court said:

> we cannot give them dispositive weight. The insurers' views have been presented to Congress and that body can adjust the statute.

Id.

TLIC's concern that holding it to fiduciary standards would be disruptive is irrelevant for another reason: it had promised to perform as a fiduciary. The Plaintiffs' plans are marketed by TLIC as part of its "Partner Series III Transamerica Master Retirement Plan Program," (formerly known as the "Director Series III"). SR36; ER157. In its Partnership III Series product brochure, TLIC provides the following acknowledgment of its fiduciary status:

> For the Retirement Options, Transamerica Life Insurance Company ("TLIC") has discretionary authority over the Investment Objectives, which makes TLIC a co-fiduciary regarding:

* * *

> Monitoring of portfolio managers and/or underlying investments
>
> Retaining/changing … the underlying investments

ER166. *See also* SR37.

In that same brochure, TLIC agrees that it has fiduciary responsibilities over the Ret Opt Separate Accounts here in issue:

> TLIC acknowledges it is a "fiduciary" within the meaning of [ERISA] with respect to the "Ret Opt" separate accounts and "Ret Opt" sub-accounts as described below.[11]

ER175. *See also* SR38. TLIC's Rule 30(b)(6) witness confirmed that after the GAC is signed, "we [TLIC] have discretionary capabilities over those particular funds" and provided the "fiduciary service …." SR178.

As the district court noted, TLIC admitted in briefing that it has "fiduciary responsibility for the separate accounts" and "limited fiduciary responsibilities for monitoring the investment performance."

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[11] TLIC's Separate Accounts, each of which holds a different investment option, fall into two broad categories, which it calls "Ret Opts" (Retirement Options) and "Inv Opts" (Investment Options). TLIC charges an IM/Admin Fee on each Ret Opt but does not charge an IM/Admin Fee on any Inv Opt. The certified classes consist of 401(k) retirement plans invested in the Ret Opt Separate Accounts.

ER195. Therefore, the district court's ruling that TLIC may be a fiduciary cannot have any disruptive effect.

Moreover, there is no support in the record for TLIC's arguments that it would sustain financial difficulties were it compelled to comply with ERISA. For instance, TLIC argues that holding it to fiduciary responsibilities would impair the viability of its retirement business. Br. 29-30. The only factual foundation cited by TLIC for this assertion are self-serving statements by TLIC's own employees that it takes seven years to recoup the expenses which it charges to add a plan to its platform. *See* ER269; ER285-287. These assertions are not germane to disposition of a motion to dismiss or a motion for class certification. Further, TLIC's expenses far exceed those of competitors, all of whom seem to continue in business. According to TLIC's own expert, in 2009, the *median* "Total Fees [charged by TLIC among plans in the Proposed Class] vary with plan size" from 1.75% for plans with over $1 billion in assets to 6.15% for plans with less than $50 million in assets. SR198; SR199-200.

In contrast, an annual study prepared by Deloitte and the Investment Company Institute—relied upon by TLIC's own expert in

his initial report, *see* SR196-197; SR201, as well as Plaintiffs' expert in his rebuttal report, SR181-184—found that in 2009 the "Median All in Fee," for plans with over $500 million in assets was .41% and for plans with $10 million to $50 million in assets was .78%. Deloitte, Defined Contribution / 401(k) Fee Study 19 (2009), https://www.ici.org/pdf/rpt_09_dc_401k_fee_study.pdf. This means that TLIC's fees, depending on the size of a plan, are either double, or more than ten times, the industry average.

ERISA should not be construed to sacrifice the interests of retirement savers for the benefit of insurance companies. The fiduciary standards and prohibited transaction provisions serve a laudable purpose for small and medium sized employers. Plan sponsors lack the sophistication, resources, and incentive to police the Separate Accounts which serve the universe of all TLIC plans.[12] Therefore, plan

[12] For example, a report by the Government Accountability Office ("GAO") concerning the impact of conflicts of interest and hidden fees on participants of retirement savings plans found that more than one-third of plan sponsors responding to a survey by an industry group "either did not know the fees being charged to participants or mistakenly thought no fees were charged at all" and that many plan sponsors were unaware of conflicts of interest "which could result in higher fees that can lower investment returns for participants." Gov't Accountability Office, GAO-09-503T, Private Pensions: Conflicts of

participants are largely unprotected from self-dealing at the Separate Account level.

TLIC can be protected by implementing one of several inexpensive remedies. First, TLIC could surrender the discretion and control over fees that makes it a fiduciary. Neither "efficiencies" nor "industry practice" justify an arrangement that creates such substantial opportunity and temptation for fiduciary service providers to abuse their discretion and control. *See generally Donovan v. Cunningham*, 716 F.2d 1455, 1464-65 (5th Cir. 1983) ("The object of Section 406 was to make illegal per se the types of transactions that experience had shown to entail a high potential for abuse"); *Cf. N.L.R.B. v. Amax Coal Co., a Div. of Amax*, 453 U.S. 322, 329-30 (1981) ("'uncompromising rigidity'" in enforcing loyalty duties is required). Alternatively, the Separate Accounts could be held or controlled by others. Third, an outside fiduciary, appointed to protect the interest of the Separate Accounts, could evaluate, approve and pay TLIC's fees.

Interest Can Affect Defined Benefit and Defined Contribution Plans 7-9 (2009), *available at* http://www.gao.gov/new.items/d09503t.pdf.

TLIC's self-dealing has great consequences, which explains in part why it is a fiduciary and illustrates the danger of self-dealing. Thus, while the GACs state that TLIC uses the IM/Admin Fee of 75 basis points is to pay costs associated with "managing and administering the assets in the separate accounts," SR161, that is not accurate. TLIC and its expert acknowledge that the IM/Admin Fees extracted from the Separate Accounts are used to subsidize other services and thus are used for purposes other than managing and administering the Separate Accounts. SR195; SR216; Br. 6-7. *See also* Br. 58, 60.

This creates several problems. First, as Plaintiffs' expert, Ethan Kra, Ph.D., notes, the contention that IM/Admin Fees are used to subsidize other services:

> is itself incompatible with TLIC's fiduciary duties and is troublesome. The IM/Admin fee is for investment management services. If this function is performed well, participants flourish. The CAC covers very different costs, including commissions to business brokers.

SR228. The use of IM/Admin Fees to defray costs unrelated to the separate account violates a fiduciary's "core obligation" to refrain from misleading participants. *Matthews v. Chevron Corp.*, 362 F. 3d 1172, 1180 (9th Cir. 2004).

Second, insofar as TLIC claims some plans do not become profitable for seven years, the shortfall must be covered by the IM/Admin Fees of other plans. *Donovan v. Mazzola*, 716 F.2d 1226, 1238 (9th Cir. 1983), *cert. denied,* 464 U.S. 1040 (1984) ("If there is a single member who participates in only one of the plans, his plan must be administered without regard to the interests of any other plan.").

Third, these subsidies may be used to pay inappropriate costs rather than costs of "administering the plan." 29 U.S.C. § 1104(a)(1)(A)(ii). Clearly, a plan sponsor who benefits from such a subsidy has no incentive to confirm that the IM/Admin Fees are withdrawn for an appropriate purpose. Likewise, to the extent that these funds are used to pay the CAC, IM/Admin Fees are actually being used to pay sales and brokerage commissions, for the benefit of TLIC, not for the benefit of plan participants.

In any event, resolution of these issues is not necessary to resolve this appeal. Plaintiffs' claims and the facts upon which they are based are common to the class and should be adjudicated, on the merits, in the court below, where the facts can be tried.

CONCLUSION

The orders of the district court should be affirmed.

RESPECTFULLY SUBMITTED this 5th day of April, 2017.

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CERTIFICATE OF SERVICE

I hereby certify that I electronically filed the foregoing with the Clerk of the Court for the United States Court of Appeals for the Ninth Circuit by using the appellate CM/ECF system on April 5, 2017.

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