No. 17-3244

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

JENNIFER SWEDA, BENJAMIN A. WIGGINS, ROBERT L. YOUNG, FAITH PICKERING, PUSHKAR SOHONI, AND REBECCA N. TONER, individually and as representatives of a class of similarly situated persons of the University of Pennsylvania Matching Plan,

Plaintiffs-Appellants,

v.

THE UNIVERSITY OF PENNSYLVANIA, INVESTMENT COMMITTEE, AND JACK HEUER,

Defendants-Appellees.

Appeal from the United States District Court for the
Eastern District of Pennsylvania
The Honorable Gene E.K. Pratter
No. 2:16-cv-04329-GEKP

REPLY BRIEF OF APPELLANTS

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INTRODUCTION

If the factual allegations in Plaintiffs' 117-page, 236-paragraph Amended Complaint are accepted as true, the defendant-fiduciaries of the $3.8 billion University of Pennsylvania Matching Plan (Plan) wasted Penn employees' retirement savings on wholly unnecessary fees and poorly performing investments that enriched the Plan's recordkeepers. Specifically, Defendants:

- provided higher-cost "retail" class shares of 58 of the Plan's investment options instead of "institutional" class shares of the *same* funds which were *identical* in all respects except that they charged much lower fees;
- retained two recordkeepers (TIAA and Vanguard) and allowed them to collect uncapped revenue sharing payments in an amount *six times* greater than the market rate for their services; and
- retained two investment options affiliated with TIAA (CREF Stock Account and TIAA Real Estate Account) that a prudent fiduciary would have removed years earlier based on the funds' long record of abysmal performance.

This conduct caused Penn employees and retirees to lose over $26 million due to excessive fees (A85 ¶120), and many millions more in performance losses (A119 ¶172, A123–24 ¶178).

As fiduciaries, Defendants were required to act solely in the interest of the

Plan's participants and "'with the care, skill, prudence, and diligence' that a prudent person 'acting in a like capacity and familiar with such matters' would use." *Tibble v. Edison Int'l (Tibble III)*,

135 S.Ct. 1823, 1829 (2015)(quoting 29 U.S.C. §1104(a)(1)). Background principles of trust law, which inform those duties, confirm Defendants' obligations to control costs and to monitor and remove imprudent investments. Plaintiffs' allegations that Defendants provided dozens of retail-class shares when the *same* investments were available at lower-cost, failed to control administrative costs, and retained severely underperforming investments that a prudent review process would have removed—all of which served to benefit the Plan's recordkeepers at participants' expense—are more than adequate to raise a reasonable inference that Defendants failed to satisfy their fiduciary obligations.

In response to these allegations, Defendants contend that ERISA affords them fiduciary discretion to forego identical lower-cost shares of the Plan's funds, to allow recordkeeper to collect unlimited compensation, and to retain imprudent investments regardless of performance. Relying on *Renfro v. Unisys Corp.*, 671 F.3d 314 (3d Cir. 2011), Defendants assert that a defined contribution fiduciary's duties are limited to providing a range of choices with fees comparable to the plan in that case. In Defendants' view, as long as the investment menu as a whole provides choices, it is immaterial that the fiduciaries overpaid for dozens of

individual funds within that menu.

Nothing in *Renfro* or ERISA supports Defendants' proposed limitation on a fiduciary's duties. Although Defendants strain to fit Plaintiffs' claims within the *Renfro* framework, that case involved fundamentally different issues, and held only that a complaint containing sparse factual allegations "directed exclusively to the fee structure" of retail mutual funds failed to raise a plausible inference of imprudence. 671 F.3d at 327. The court did not address the prudence of providing more expensive versions of the *same* funds. The Court also did not address a fiduciary's duties to monitor the reasonableness of recordkeeping compensation paid through revenue sharing, to monitor investment performance, and to avoid prohibited transactions which favor a service provider at participants' expense, all of which are at issue here.

The facts alleged in the Amended Complaint establish plausible grounds for relief. Defendants' arguments to the contrary should be rejected.

ARGUMENT

I. Plaintiffs allege plausible breaches of fiduciary duties.

A fiduciary breach claim is plausible if the factual allegations, considered as a whole, allow the court to infer "that the process was flawed." *Renfro*, 671 F.3d at 327 (quoting *Braden v. Wal-Mart Stores, Inc.*, 588 F.3d 585, 596 (8th Cir. 2009));[1]

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[1] Defendants assert in passing that *Renfro* additionally requires Plaintiffs to show

see Pla. Br. 36–37. As described by Judge Diane Wood, author of the *Hecker* opinion that this Court followed in *Renfro*:[2] "No heightened pleading standard applies" to these claims; "it is enough to provide the context necessary to show a plausible claim for relief." *Allen v. GreatBanc Tr. Co.*, 835 F.3d 670, 674 (7th Cir. 2016). A plaintiff meets that standard "as long as the facts alleged tell a plausible story." *Id.* at 678. "All the plaintiff must do is to plead the breach of a fiduciary duty, such as prudence, and to explain how this was accomplished." *Id.* at 679.

The facts alleged tell a plausible story in which Defendants allowed the Plan's recordkeepers—TIAA and Vanguard—to influence the Plan's investment lineup in a manner that enriched those entities at the expense of the Plan's participants. The recordkeepers persuaded Defendants to limit the Plan to the recordkeepers' proprietary investment options, to include the higher-cost retail-class shares of those funds, and to lock the Plan into options regardless of performance, all of which provided the recordkeepers a larger stream of fee revenues while reducing the Plan's assets by millions of dollars. Moreover, similarly situated fiduciaries of prudently managed plans—particularly multi-billion dollar defined contribution

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"that the fiduciary made a decision that no prudent fiduciary would have made." Def. Br. 17. Because the alleged facts plausibly show a flawed process causing losses to the Plan, the burden shifts to *Defendants* to prove that a prudent fiduciary would have made the same decision. *See, e.g.*, *Tatum v. RJR Pension Inv. Comm.*, 761 F.3d 346, 362–64 (4th Cir. 2014), *cert denied*, 135 S.Ct. 2887 (2015).

[2] *See Hecker v. Deere & Co.*, 556 F.3d 575 (7th Cir. 2009), cited in *Renfro*, 671 F.3d at 326.

plans—would have leveraged the Plan's size to obtain the lowest-cost share classes of mutual funds; investigated and monitored whether the recordkeeper's compensation was competitive with the market; and eliminated investments that consistently underperformed year after year. These facts, if accepted as true, raise a plausible inference that Defendants had a flawed process for monitoring the Plan's fees and investments, resulting in millions of dollars of Plan losses.

Defendants assert that because *Renfro* involved a plan with a similar number of investment options and range of fees, any claimed breach is necessarily implausible. Defendants misunderstand their duties under ERISA and misinterpret *Renfro*.

A. Plaintiffs plausibly allege that Defendants caused the Plan to pay excessive investment management fees (Count V).

1. *Tibble* establishes the framework for determining the scope of Defendants' duty regarding mutual fund share classes.

In 2011, this Court announced a standard for evaluating claims "challenging the overall composition of a [defined contribution] plan's mix and range of investment options[.]" *Renfro*, 671 F.3d at 327. Four years later, the Supreme Court reviewed a claim presenting the distinct issue presented here—the prudence of providing "higher priced retail-class mutual funds as Plan investments when materially identical lower priced institutional-class" shares of the same mutual funds were available—and held that it was error for the lower courts to reject such

a claim "without considering the role of the fiduciary's duty of prudence under trust law." *Tibble III*, 135 S.Ct. at 1826–27.

Defendants nevertheless insist that *Tibble III* is merely a statute of limitations decision that has no relevance to Plaintiffs' share-class claim, because the Court ultimately declined to resolve the parties' factual dispute regarding "the scope of [the defendants'] fiduciary duty" to review the mutual funds at issue. Def. Br. 29–30 (quoting *Tibble III*, 135 S.Ct. at 1829). The Supreme Court's instruction for *how* to determine the scope of the duty, however, was unambiguous: by "considering the role of the fiduciary's duty of prudence under trust law" and "recognizing the importance of analogous trust law." *Tibble III*, 135 S.Ct. at 1827, 1829; Pla. Br. 28. That instruction applies to Plaintiffs' share-class claim here. A85–96 ¶¶121–31; *see* Pla. Br. 27–28, 37–40.

2. *Renfro* did not address a similar share-class claim.

The Court need not decide whether *Tibble III* "call[s] *Renfro*'s current viability into question" (Def. Br. 29), because *Renfro* is readily distinguishable. *See* Pla. Br. 34–36. Defendants' assertion that the claim in *Renfro* "was no different from the retail-vs.-institutional argument" here is contradicted by the record. *See* Def. Br. 24. In contrast to the fund-specific comparisons here (A88–96 ¶128), the *Renfro* complaint contained only a bare reference to the availability of "less expensive institutional share classes," without identifying a single alternative share class or

the difference in fees compared to a specific fund in the plan. A329. Indeed, the same defense lawyers argued in *Renfro* that the pleading was inadequate because it "failed entirely to allege with any specificity that institutional classes of the same funds offered as retail funds were available to the Plan and not selected." *See* Br. for Appellees Unisys Corp. et al., at 55 & n.45, *Renfro*, 671 F.3d 314 (3d Cir. 2010)(No. 10-2447) ("*Renfro* Unisys Br."). Given this Court's finding that the *Renfro* plaintiffs' "factual allegations" were "directed exclusively to the fee structure and [were] limited to contentions that Unisys should have paid per-participant fees," 671 F.3d at 327, the Court evidently discarded the share-class allegation as a "conclusory statement[]" rather than a "well-pled factual allegation[]," *see id*. at 320; *cf.* Def. Br. 19, 24.

Tellingly, Defendants point not to the *Renfro* complaint (A312–51), but to an appellate brief. Def. Br. 24. But as the same lawyers argued in urging this Court to disregard such outside facts, it is "axiomatic that the complaint may not be amended by the briefs in opposition to a motion to dismiss." *Renfro* Unisys Br. 33–38 (quoting *Pennsylvania ex rel v. Zimmerman v. PepsiCo*, 836 F.2d 173, 181 (3d Cir.1988)). Nothing in *Renfro* suggests the Court considered this "allegation." Even assuming the Court considered that theory, the scope of the breach is not comparable to the claim here. Only three of the *Renfro* plan's 67 mutual funds had lower-cost share classes available, which would have provided a 0.03% fee

reduction for what were already the cheapest funds (0.10%). *See* Def. Br. 23; *Renfro*, 671 F.3d at 318. Here, *58* of the mutual funds in the Plan since 2010 had lower-cost share classes available, many of which charged fees *multiples* higher than the identical institutional-class versions. A88–96 ¶¶128–29. The facts here thus raise a much stronger, more plausible, inference of a flawed process.

Defendants further contend that Plaintiffs' allegations are "indistinguishable" because the *Renfro* plaintiffs alleged that the plan's funds charged excessive fees "as compared to *other*, less expensive, investment options *not* included in the plan." Def. Br. 19 (quoting *Renfro*, 671 F.3d at 319)(emphasis added); *see also Renfro*, 671 F3d at 325–26 (allegation that defendants should have used "other types of investments" such as commingled pools); A329. But Plaintiffs' share-class allegations do not pertain to *other* options not included in the Plan—they pertain to lower-cost shares of the *same* mutual funds Defendants had "already selected." *See Tibble v. Edison Int'l (Tibble IV)*, 843 F.3d 1187, 1198 (9th Cir. 2016)(en banc).

Although Defendants (at 30) criticize *Tibble IV* for not addressing "the analyses of *Hecker*, *Loomis*, or *Renfro*," that proves Plaintiffs' point: the Ninth Circuit had no reason to address those cases because they are inapposite. They involved *per se* challenges to using "retail" mutual funds instead of unspecified "institutional" vehicles, not the type of share-class claim remanded from the

Supreme Court and which is at issue here. *See* Pla. Br. 42–43.[3] The court's earlier panel opinion, *Tibble v. Edison International (Tibble II)*, 729 F.3d 1110 (9th Cir. 2013), in fact followed *Renfro* in rejecting a claim that it was "categorically imprudent" to provide a range of 40 retail mutual funds instead of "separate accounts" or "commingled pools," *id*. at 1134–35, yet held that for three specific funds within that group for which the plan could have obtained identical institutional shares, the fiduciaries imprudently provided the higher-cost retail-class shares, *id.* at 1137–39.

Defendants inaccurately portray *Tibble* as turning on the fact that the employer benefited from the retail-class shares, which paid a greater amount of revenue sharing and thus reduced the employer's bills from the recordkeeper. Def. Br. 29–30. In fact, the trial court found "no evidence" that the investment committee's decision to "invest in the retail share classes" was designed to "capture more revenue sharing" for the employer or to "put the interests of [the employer] in offsetting the record-keeping costs to Hewitt Associates above the interests of the Plan participants in paying lower fees." *Tibble v. Edison Int'l (Tibble I)*, No. 07-

[3] *See Renfro*, 671 F.3d at 326; *Loomis v. Exelon Corp*., 658 F.3d 667, 671–72 (7th Cir. 2011)(comparing "retail" mutual funds to non-mutual fund "Institutional trusts" and "commingled pools"); *Hecker v. Deere & Co*., 556 F.3d 575, 586 (7th Cir.)(rejecting claim based on possibility that "other funds" were less expensive), *supplemented*, 569 F.3d 708, 711 (7th Cir. 2009)(plaintiffs challenged decision "to accept 'retail' fees" instead of "negotiat[ing] *presumptively* lower 'wholesale' fees")(emphasis added).

5359, 2010 U.S.Dist.LEXIS 69119, *22–25, *65–66, *70–75 (C.D.Cal. July 8, 2010), *aff'd*, 729 F.3d 1110 (9th Cir. 2013). Their decision to invest in retail shares for three of the plan's funds was nevertheless *imprudent*, because if they had conducted a "thorough investigation" they "would have realized that the institutional share classes offered the exact same investment at a lower cost," and "would have known that investment in the retail share classes would cost the Plan participants wholly unnecessary fees." *Id*. at *82–83 (citing, *inter alia*, *In re Unisys Sav. Plan Litig. (Unisys I)*, 74 F.3d 420, 436 (3d Cir. 1996)); Pla. Br. 26–27.

After a second trial on remand from the Supreme Court regarding 17 additional funds initially selected outside the limitations period, the district court held that a "hypothetical prudent fiduciary" would not have made the same decision, again concluding that "[b]ecause the institutional share classes are otherwise *identical* to the retail share classes, but with lower fees, a prudent fiduciary would know immediately that a switch is necessary." *Tibble v. Edison Int'l (Tibble V)*, No. 07-5359, 2017 U.S.Dist.LEXIS 130806, *25–27, *38–40 (C.D.Cal. Aug. 16, 2017).

Tibble thus undermines Defendants' theory that "excessive fee allegations generally must be accompanied by a lack of sufficient alternative options, plausible allegations of wrongdoing, or both" (Def. Br. 29), which would reduce the duty of *prudence* to a formulaic requirement of providing a large number of investment options. *Cf. Hecker*, 569 F.3d at 711 (fiduciary cannot "insulate itself from liability

by the simple expedient of including a very large number of investment alternatives in its portfolio and then shifting to the participants the responsibility for choosing among them."); *DiFelice v. U.S. Airways, Inc.*, 497 F.3d 410, 413 (4th Cir. 2007)("A fiduciary cannot free himself from his duty to act as a prudent man simply by arguing that other funds" are available). "Because the content of the duty of prudence turns on 'the circumstances . . . prevailing' at the time the fiduciary acts, §1104(a)(1)(B)," there is no basis for the bright-line rule Defendants propose. *See Fifth Third Bancorp v. Dudenhoeffer*, 134 S. Ct. 2459, 2471 (2014); *see also Roth v. Sawyer-Cleator Lumber Co.*, 16 F.3d 915, 920 (8th Cir. 1994)("There is no formula, however, for determining whether an ERISA fiduciary's conduct was reasonable, so the court should take into account all relevant circumstances.").

3. *Renfro* does not preclude claims that particular investment options charged excessive fees.

Renfro described its holding not in terms of broad application regarding all fee-related issues in defined contribution plans, but as a standard for evaluating claims "challenging the overall composition of a plan's mix and range of investment options[.]" 671 F.3d at 327. The "factual allegations" were "directed exclusively to the fee structure and [were] limited to contentions that Unisys should have paid per-participant fees rather than fees based on a percentage of assets in the plan." 671 F.3d at 327. Those allegations follow in their entirety:

> 41. Per the Trust Agreement, the Plan was obligated, through its participant accounts, to pay Fidelity for these investment management and administrative services.
>
> 42. Rather than prudently limiting the payment by the Plan for these services based on an agreed fixed amount or an amount based on the numbers of participants in the Plan, the amount of payment by the Plan to Fidelity for these services was based on a percentage of the total assets in the Plan.
>
> 43. However, many of the services provided by Fidelity to the Plan, including administrative services, did not and do not vary with the amount of assets in the Plan. That is, it costs the same to administer a participant account holding $100,000.00 as it does an account holding $10,000.00 or only $1,000.00.

A324; *see Renfro*, 671 F.3d at 326 n.7 (citing ¶¶42–43). In light of the plan's mix and range of options, such "general allegations" of imprudence did not raise a plausible inference "that the process was flawed." *Renfro*, 671 F.3d at 327–28 (quoting *Braden*, 588 F.3d at 596).

Defendants interpret *Renfro* as effectively holding that any plan with a range of fees consistent with "the *Renfro* range" has reasonable fees as a matter of law, both as to the Plan as a whole and every fund within the Plan. Def. Br. 21–22.[4] In light

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[4] Instead of endorsing *Renfro*, which involved a tax code §401(k) plan, Defendants' *amici* contend that a different fiduciary standard should apply to §403(b) fiduciaries. Am. Council Br. 14–18. The historical differences cited by *amici* have "largely eroded" over time. A52 ¶52; A13–16. "[T]he same standard of prudence applies to all ERISA fiduciaries." *Fifth Third Bancorp v. Dudenhoeffer*, 134 S.Ct. 2459, 2467–71 (2014)(emphasis added). All retirement plans have the same "character and aims" and "exclusive purpose." *Id.* at 2468. Just as excessive fees "significantly reduce the value" of a defined contribution account in a 401(k) plan, the same is true in a 403(b) plan. *Tibble*, 135 S.Ct. at 1826.

of the context, a claim which challenged the "mix and range" of options in the plan as a whole, the better reading is that the Court held that "the *range* of expense ratios offered was reasonable, not that a fiduciary's decision to include an investment option that has an expense ratio within that range is always reasonable as a matter of law." *Terraza v. Safeway Inc.*, 241 F.Supp.3d 1057, 1079 (N.D. Cal. 2017). Indeed, Defendants themselves insist elsewhere that cost is not dispositive. Def. Br. 35; TIAA Br. 26; *cf. Terraza*, 241 F.Supp.3d at 1078.

Although Defendants acknowledge the Court's statement that the plaintiffs in *Renfro* did not challenge the prudence of including any "particular" option, they speculate that the Court intended to distinguish an excessive fees claim from a claim that an investment was "inherently flawed" because of risk. Def. Br. 22–23, 31–32. Defendants fail to explain why a claim that an option was imprudently *risky* should be actionable, while a claim that an option was imprudently *costly* is not. In both cases, the imprudent option harms participants' retirement savings. *See Tibble III*, 135 S.Ct. at 1826 (expenses can "significantly reduce the value of an account in a defined-contribution plan."). *Tibble* itself involved a claim that "individual investment options" (Def. Br. 23) charged excessive fees, and held that a "plaintiff may allege that a fiduciary breached the duty of prudence by failing to properly monitor investments and remove imprudent *ones*." 135 S.Ct. at 1829 (emphasis added).

That is not to say that identifying a lone "sub-optimality in an investment menu" would necessarily raise an inference of a flawed process. *See* Def. Br. 38, 40; Chamber Br. 23–28. But that is not this case. Defendants provided *58* mutual funds in retail-class shares when the same investment was readily available at a significantly lower cost if Defendants had conducted a minimal investigation. Pla. Br. 39–40; A34 ¶3, A46–47 ¶37, A85–A96 ¶¶121–29. Doing so caused the Plan to lose millions of dollars, with no offsetting benefit. Selecting the higher-cost shares to defray the Plan's administrative costs (Def. Br. 21) was not a *lawful* explanation for Defendants' conduct,[5] because the resulting revenue sharing payments from the retail-class shares resulted in recordkeeping fees up to *six times* higher than the market rate for the same service. Pla. Br. 43–45; *infra*, I.B. While Defendants further dispute whether they could have obtained waivers of minimum investment requirements for *every* fund at issue (Def. Br. 39), that is simply a fact dispute. The well-pled facts—corroborated by the trial evidence in *Tibble*—show that the Plan easily could have obtained any necessary waivers upon request. Pla. Br. 12, 39,

[5] Defendants' *amici* contend that *Twombly*'s general pleading standard requires ERISA plaintiffs to rule out all "rational" explanations for a fiduciary's decision. Chamber Br. 2, 5, 15–23, n.12 (discussing *Bell Atl. Corp v. Twombly*, 550 U.S. 544 (2007)). The need to rule out "rational" business strategy in *Twombly* "turned largely" on established principles of *antitrust* law. *In re Ins. Brokerage Antitrust Litig.*, 618 F.3d 300, 320 n.18, 321, 341 n.42, 361 (3d Cir. 2010)(citations omitted). *Twombly* "does not require as a general matter that the plaintiff plead facts supporting an inference of defendant's liability more compelling than the opposing inference." *Id*. at 341 n.42; *see* Pla. Br. 37.

41–42; A86–A87 ¶¶124–27 (requirements "are routinely waived").

4. Neither ERISA nor trust law afford Defendants discretion to incur unreasonable expenses or to retain imprudent investments.

Defendants' fiduciary duty under ERISA, as informed by the law of trusts, incorporates a duty "to properly monitor investments and remove imprudent ones." *Tibble III*, 135 S.Ct. at 1828–29. The trust law authorities confirm that Defendants' monitoring duty applies to the fees of the Plan's investments. *See Tibble IV*, 843 F.3d at 1197–98; Pla. Br. 28–29. "[C]ost-conscious management is fundamental to prudence" in selecting and monitoring investments. *Tibble IV*, 843 F.3d at 1197–98 (quoting RESTATEMENT (THIRD) OF TRUSTS §90, cmt. b). "Wasting beneficiaries' money is imprudent." *Id*. at 1198 (quoting Unif. Prudent Investor Act §7).

Although Defendants suggest that these standards do not translate to the defined contribution setting (Def. Br. 34), that is wrong. The Restatement specifically notes that mutual fund expenses "require special attention by a trustee." RESTATEMENT (THIRD) OF TRUSTS §90, cmt. m. Because differences in mutual fund expenses "can be significant, it is important for trustees to make careful overall cost comparisons, particularly among similar products of a specific type being considered for a trust portfolio." *Id*.

Defendants do not dispute that investment expenses are important to the prudence inquiry, but argue that ERISA and trust law afford fiduciaries

"discretion" not to prioritize expenses "*above all else*." Def. Br. 2, 13, 34, 35 (emphasis added); Chamber Br. 12–14. Plaintiffs have not alleged that Defendants were required to provide "the cheapest possible fund" without regard to other factors. *See* Def. Br. 27–28;[6] Chamber Br. 13; TIAA Br. 26 (quoting *Hecker*, 556 F.3d at 586). As to different share classes of the *same* fund, however, cost *is* the only difference, meaning the institutional-class shares are guaranteed to provide a higher return. A49–50 ¶45, A66 ¶77, A96 ¶130. In these circumstances, it is highly plausible that cost would be the dispositive factor. *See Tibble IV*, 843 F.3d at 1198; *Tatum v. RJR Pension Inv. Comm. (Tatum II)*, 855 F.3d 553, 566 (4th Cir. 2017) ("[F]iduciaries . . . ordinarily have a duty to seek . . . the lowest level of risk *and cost* for a particular level of expected return — or, inversely, the highest return for a given level of risk and cost.")(quoting RESTATEMENT (THIRD) OF TRUSTS §90 cmt. f(1))(Am. Law Inst. 2007)(emphasis added).

Further, this Court has recognized that the "discretionary" nature of fiduciary functions does not create a relaxed standard of conduct. *In re Unisys Sav. Plan*

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[6] Defendants further mischaracterize the Amended Complaint as alleging "that the Plan should not have offered actively managed mutual funds but instead only a handful of passively managed index funds." Def. Br. 27 n.4. In fact, Plaintiffs merely allege, consistent with ERISA's requirements, that a fiduciary should *weigh* the higher costs associated with actively managed funds against "the likelihood of increased return from such strategies." A51 ¶47 (quoting RESTATEMENT (THIRD) OF TRUSTS ch. 17, intro. note; *id.* § 90 cmt. h(2)). Here, Defendants provided multiple actively managed funds in the same style, which creates a "shadow index"—*i.e.*, paying active management prices for index fund returns. A140 ¶216.

Litig. (Unisys II), 173 F.3d 145, 154 (3d Cir. 1999). Thus, because Defendants had a duty to be cost-conscious and to monitor each of the Plan's investments, fiduciary discretion was not a license to ignore those duties.

Defendants' final trust law argument, that anyone who invests in an imprudent fund consents to Defendants' breach, makes little sense. Def. Br. 35–37. Had Defendants informed participants that the same funds were available at significantly lower cost that Defendants failed to obtain, no one would have agreed to continue having their account balance reduced by unnecessary fees.

B. Plaintiffs allege a plausible breach of fiduciary duty based on excessive administrative fees (Count III).

Defendants' duties included an obligation to monitor the Plan's recordkeeping expenses, particularly assessing whether the revenue sharing compensation paid to TIAA and Vanguard was reasonable and competitive. *See Tussey v. ABB, Inc.*, 746 F.3d 327, 336 (8th Cir. 2014); Pla. Br. 43–46.

Although Defendants contend that *Renfro* rejected a similar revenue sharing claim, they are mistaken. Defendants rely on the *Renfro* plaintiffs' assertion that the "fee compensation on the *mutual funds*" should have been "calculated on a per-participant basis" rather than "as a percentage of the total assets in the funds." Def. Br. 19 (quoting *Renfro*, 671 F.3d at 326)(emphasis added); *see also Renfro*, 671 F.3d at 326 (this allegation was within the "rubric" of the claim that Unisys should have provided "other mutual funds" and "other types of investments"). That was

the same issue addressed in *Loomis*, 658 F.3d at 672; Def. Br. 27. Plaintiffs have not alleged that the Plan's mutual funds should not charge their expense ratios as a percentage of assets. Rather, Plaintiffs contend that Defendants were required to monitor the total amount of the revenue sharing payments to the recordkeepers. *See* Pla. Br. 48–49.

Defendants also cite a portion of the *Renfro* plaintiffs' appellate brief discussing revenue sharing. Def. Br. 25. But this Court did not address that issue, finding it waived. *Renfro*, 671 F.3d at 326 n.7. While Defendants contend that *Renfro* involved a general "revenue sharing" claim separate from the waived claim as to Fidelity's "internal distribution" of "fee revenues," that is wrong. *See* Br. for Appellees Fidelity Corp. et al., at 52, *Renfro*, 671 F.3d 314 (3d Cir. 2010)(No. 10-2447)(arguing for waiver because complaint made "no allegations whatsoever about 'revenue sharing.'"). *All* of the mutual funds in the *Renfro* plan were affiliated with Fidelity. 671 F.3d at 318. By definition, then, any sharing of fee revenues was "internal" revenue sharing among Fidelity affiliates. Thus, *Renfro* did not address a fiduciary's duty to monitor a recordkeeper's revenue sharing compensation. Defendants' failure to cite any pertinent authority supporting dismissal is reason alone to reverse.

Although Defendants seek to distinguish *Tussey* on the ground that the employer indirectly benefited from the excess revenue sharing, the basis for the

decision was not so limited. Def. Br. 29. The finding of breach was also based on three other "specific failings." *Tussey*, 746 F.3d at 336. The fiduciaries failed to: "(1) calculate the amount the Plan was paying Fidelity for recordkeeping through revenue sharing, (2) determine whether Fidelity's pricing was competitive, [and] (3) adequately leverage the Plan's size to reduce fees." *Id.* Each of those factors applies here. And while the court indeed noted that revenue sharing is a "common" practice, the more salient points are the court's holdings that: (1) a failure to "monitor and control recordkeeping fees" paid through revenue sharing is a breach of fiduciary duty; (2) providing "a wide 'range of investment options from which participants could select low-priced funds" is not a defense to such a claim; and (3) fiduciary breach claims are "inevitably fact intensive." *Id*.

Defendants misleadingly suggest (at 32) that the reversal of summary judgment in *George v. Kraft Foods Global, Inc*., 641 F.3d 786 (7th Cir. 2011), was somehow based on the purportedly "restricted menu" of investments. In fact, the two were unrelated. The evidence showed that the fiduciaries' failure to solicit competitive bids periodically caused the plan to overpay for recordkeeping, which required reversal of summary judgment. *Id*. at 798–99. The allegations here similarly show that Defendants' failure to obtain bids contributed to the excessive fees. A48 ¶41, A56–57 ¶60, A78–79 ¶103, A81–82 ¶¶112, A84 ¶114. Defendants' assumption that hiring a different recordkeeper would require changing the mix of investments

overlooks that an "open architecture" model provides *greater* flexibility to customize the investment lineup. A63 ¶71, A38 ¶86.[7] But whether Defendants ultimately decided to *replace* the existing service provider is beside the point—the bidding process *itself* allows the fiduciary to gauge the market and to negotiate lower fees with the incumbent. A78–79 ¶103.[8]

C. Plaintiffs allege a plausible breach of fiduciary duty regarding the imprudent CREF Stock Account and TIAA Real Estate Account (Counts I, V).

Because "the most basic of ERISA's investment fiduciary duties, [is] the duty to conduct an independent investigation into the merits of a particular investment," *Unisys I*, 74 F.3d at 435, allegations plausibly showing that the fiduciary failed to conduct such an investigation on an ongoing basis raise an inference that the process was flawed, *Renfro*, 671 F.3d at 327; *see George*, 641 F.3d at 796 (fiduciary must "balance the relevant factors and make a reasoned decision as to the preferred course of action"); *cf*. Def. Br. 41.

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[7] The schools to which Defendants compare the Plan's fees (Def. Br. 33, A252), have much smaller assets. D.Ct. Doc. 36 at 24 n.20; A60 ¶63.

[8] Defendants' *amicus* TIAA challenges Plaintiffs' allegations as "incorrect" and not "accurate," asking the Court to instead rely upon TIAA's marketing materials and opinions about the purported "distinctive value" and "high quality" of its services. TIAA Br. 1–2, 4, 6, 17–22, 27. This is improper. *Byers v. Intuit, Inc.*, 600 F.3d 286, 291 (3d Cir. 2010); *Victaulic Co. v. Tieman*, 499 F.3d 227, 236 (3d Cir. 2007)(courts should be "wary of finding judicially noticeable facts" on corporate websites). TIAA's credibility is also undermined by recent events. Gretchen Morgenson, *TIAA Receives N.Y. Subpoena on Sales Practices*, N.Y. TIMES (Nov. 9, 2017), https://www.nytimes.com/2017/11/09/business/tiaa-subpoena.html.

Plaintiffs show that by the beginning of the class period in 2010, and continuing throughout, the CREF Stock Account and TIAA Real Estate Account both severely underperformed relevant benchmarks, yet Defendants retained them in the Plan without investigation despite a prominent investment consultant recommending that clients terminate CREF Stock investments. Pla. Br. 15–16, 49–52; *see In re Unisys Sav. Plan Litig.*, 74 F.3d 420, 436 (3d Cir. 1996)(reversing summary judgment where evidence included "that at least one reputable consultant had strongly recommended against investments in Executive Life annuity contracts").

Defendants merely dispute whether the funds, in fact, underperformed, and the proper benchmarks to measure performance. Those factual issues cannot be resolved at this stage. *Flora v. Cty. of Luzerne*, 776 F.3d 169, 175 (3d Cir. 2015)("[I]nsofar as there is a factual dispute, the court may not resolve it."); *see Moreno v. Deutsche Bank Ams. Holding Corp.*, No. 15-9936, 2016 U.S.Dist.LEXIS 142601, *18 (S.D.N.Y. Oct. 13, 2016).

The purported "true benchmark" (Def. Br. 42) for CREF Stock is not a judicially noticeable fact. *Cf*. Fed.R.Evid. 201(b). The prospectuses cited by Defendants are not relevant to prove their truth, *Oran v. Stafford*, 226 F.3d 275, 289 (3d Cir. 2000), and are contrary to the Russell 3000 benchmark Defendants and TIAA repeatedly disclosed to participants. A112–14 ¶¶163–64, A141 ¶218,

A219, A290. In another similar case, TIAA's corporate representative testified that TIAA "believe[s] [the Russell 3000 is] the best benchmark" for CREF Stock. *Sacerdote v. New York University*, No. 16-cv-6284, ECF 252 at 129 n.660.

Defendants contend the "locked in" arrangement was permissible because removing CREF Stock would have required giving up the TIAA Traditional Annuity.[9] Plaintiffs, allege, however, that even if a prudent fiduciary would have stopped short of removing it, at a minimum CREF Stock should have been closed to new investments. A109 ¶154, A142 ¶220.

As to Defendants' contention that the Vanguard REIT Index mutual fund is not a proper benchmark for the TIAA Real Estate Account annuity, Defendants themselves used the S&P 500 index as the benchmark. A222. This is also not an annuity and *is not even a real estate fund*.

The imprudence of these options was not a matter of "hindsight" as Defendants assert (Def. Br. 44)—the consistent underperformance record existed well *before* the limitations period (A115 ¶167, A120 ¶175), meaning the imprudence of these options would have been apparent from an appropriate investigation based on the information available to Defendants at that time.[10]

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[9] Defendants (at 17, 43), mistakenly rely on *Amgen Inc. v. Harris*, 136 S.Ct. 758 (2016)(per curiam), which "announced a pleading standard for breach of fiduciary duty involving insider information and employer stocks," which are not at issue here. *Tatum II*, 855 F.3d at 560 n.5.

[10] In *Ellis v. Fid. Mgmt. Tr. Co.*, 883 F.3d 1 (1st Cir. 2018), the plaintiff relied on

D. Allowing Plaintiffs to pursue a remedy for excessive fees and imprudent investments supports ERISA's purposes.

Permitting plan participants to enforce ERISA's fiduciary duties furthers Congress's stated purpose of "protect[ing] . . . the interests of participants in employee benefit plans and their fiduciaries, . . . by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and by providing appropriate remedies, sanctions, and *ready access to the Federal courts*." 29 U.S.C. §1001(b)(emphasis added). The Secretary of Labor "depends in part on private litigation to ensure compliance with the statute." *Braden*, 588 F.3d at 597 n.8.

Reversing the dismissal of these claims would not, as Defendants and their *amici* speculate (Def. Br. 37–38, Chamber Br. 6–7), discourage "employers from offering . . . benefit plans in the first place." *Varity Corp. v. Howe*, 516 U.S. 489, 497 (1996). Enforcing ERISA's long-standing statutory duties cannot possibly pose any significant risk to the availability of retirement plans. Moreover, neither Defendants nor their *amici* offer any evidence that litigation challenging the prudence of investment options offered by ERISA plans has caused employers to abandon or decline to establish those plans.

Defendants' alarmist fears of "class action lawyers" demanding "extortionate

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hindsight in that it criticized the fiduciary "for shying away from asset-backed securities in the wake of the 2007-2008 market collapse," *id*. at 10.

settlements" based on a single "sub-optimality" ignores the practical context of ERISA litigation. There is simply no incentive for ERISA plaintiffs to waste "time and resources" pursuing claims over some triviality. *See Allen*, 835 F.3d at 677. In any event, this case does not present some mere technical violation. The Plan and its participants suffered significant losses in retirement savings, which could and should have been avoided. While Defendants and their *amici* request heightened pleading standards that would render ERISA's fiduciary duties virtually unenforceable, Plaintiffs request only that the Court apply the plausibility standard, which mandates that the district court be reversed.

II. Plaintiffs plausibly allege prohibited transactions (Counts II, IV, VI).

Defendants misapprehend ERISA's prohibited transaction provisions. A prohibited transaction claim does not merely "repackage" a fiduciary breach claim. *See Allen*, 835 F.3d at 675–76. Defendants' reliance on *Krauter* is misplaced for the same reason their reliance on *Renfro* is misplaced. *See Krauter v. Siemens Corp.*, No. 17-1662, 2018 U.S. App. LEXIS 3741 (3d Cir. Feb. 16, 2018). Krauter's complaint lacked "specific factual allegations," *id.* *12 n.36; Plaintiffs provide them in droves.

Defendants' limitations argument, which is limited to Count II (Def. Br. 45, A133 (¶ 193)), overlooks that Penn continues to maintain the "lock in" arrangement to date. Under *Tibble*, Defendants have an ongoing duty to avoid

prohibited transactions. Applying the six-year period requires "considering the contours" of the violation, "recognizing the importance of analogous trust law." *Tibble III*, 135 S.Ct. at 1829. Section 1106(a)(1) prohibits transactions between a plan a "party in interest," which "Congress defined . . . to encompass those entities that a fiduciary might be included to favor at the expense of the plan's beneficiaries," including a plan's service providers. *Harris Tr. & Sav. Bank v. Salomon Smith Barney Inc.*, 530 U.S. 238, 250 (2000). Under analogous trust law, the duty not to favor such third parties at the expense of beneficiaries is encompassed within the "general duty of loyalty," which "continues 'throughout the administration of the trust.'" *In re Northrop Grumman Corp. ERISA Litig.*, No. 06-6213, 2015 U.S.Dist.LEXIS 176822, *105–06 (C.D.Cal. Nov. 24, 2015)(quoting G. Bogert & A. Hess, The Law of Trusts and Trustees §543 (3d ed. 2015)). Accordingly, just as the Supreme Court in *Tibble* recognized a continuing duty to remove imprudent investments, Defendants had a continuing duty to discontinue prohibited transactions. *Id.* at *105.

Regarding the Plan's recordkeeping services (Count IV), Defendants mistakenly rely on *Hecker*, which did not address §1106(a). *Hecker*'s "plan asset" analysis dealt only with whether a mutual fund adviser that decides how much of the mutual fund's fees to share with a recordkeeper is a plan fiduciary. 556 F.3d at 584; *cf.* Def. Br. 46. Further, the statute applies to "direct *or indirect*" transfers of

plan assets. 29 U.S.C. §1106(A)(1)(emphasis added). When a plan invests in a mutual fund, the plan's assets include the *shares* of the mutual fund, but not the underlying *assets* of the mutual fund. 29 U.S.C. §1101. Revenue sharing is an "indirect" payment from the Plan (*see* A261), which reduces the value of the Plan's shares, and hence the value of the Plan's assets.

Although Penn claims (at 46 n.8) that the Plan's mutual funds and investment options are exempt from party in interest status under 29 U.S.C. §1002(21)(B), that provides only that the plan's investment of "money or other property in "money or other property" in a mutual fund "shall not *by itself* cause" the mutual fund to be deemed to be a party in interest. 29 U.S.C. §1002(21)(B)(emphasis added). The exemption says nothing about a mutual fund that furnishes "services" to a plan. 29 U.S.C. §1106(a)(1)(C).

While Defendants (at 46) criticize Plaintiffs for having a "far-fetched" view that §1106(a) covers service provider contracts, that and is exactly what the statute provides: "Congress saw fit in ERISA to create some bright-line rules, on which plaintiffs are entitled to rely." *Allen*, 835 F.3d at 676; Pla. Br. 54. Defendants' reading of §1106(a)(1)(C) as restricting only a *plan* from providing services, but not the other way around, is at odds with the view of the Department of Labor,[11]

[11] Reasonable Contract or Arrangement Under Section 408(b)(2)—Fee Disclosure, 77 Fed.Reg. 5632, 5632 (Feb. 3, 2012)("[A] service relationship between a plan and a service provider" constitutes a prohibited transaction, subject

plain language of the statute, and legislative history. If Congress wanted to make the §1106(a)(1)(C) prohibition one-sided, it could have prohibited "services *to*" a party-in-interest (instead of "between"), as it did in prohibiting "transfer to" a party-in-interest in §1106(a)(1)(D).

As Defendants concede, ERISA's exemptions from prohibited transactions are affirmative defenses. Def. Br. 48 n.9. The Amended Complaint negates any possible exemptions for the same reasons it plausibly alleges excessive fees. A133 ¶¶4, 112–20; 199–201; 29 U.S.C. §1108(b)(2); Pla. Br. 54–55.

CONCLUSION

The Court should vacate the district court's dismissal of Plaintiffs' claims.

May 3, 2018

Respectfully submitted,

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to exemptions); 29 C.F.R. §2550.408b-2.

CERTIFICATE OF COMPLIANCE

1. I certify that this brief complies with the type-volume limitation set forth in Fed.R.App.P. 32(a)(7)(B) because this brief contains 6,465 words, excluding the parts of the brief exempted by Fed.R.App.P. 32(f).

2. I certify that this brief complies with the typeface requirements of Fed.R.App.P. 32(a)(5) and the type style requirements of Fed.R.App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft Office Word 2010 Times New Roman 14 point font.

3. **L.A.R. 31.1(c) Certification**: The text of the electronic version of this brief is identical to the text in the paper copies of this brief. A virus detection program (Trend Micro Antivirus version 9.0 Service Pack 1 Build 3147) has been run on the file of this brief and no virus was detected.

s/ Jerome J. Schlichter
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May 3, 2018

CERTIFICATE OF SERVICE

I hereby certify that, on this date, I caused the foregoing Brief to be electronically filed with the Clerk of the Court for the United States Court of Appeals for the Third Circuit by using the CM/ECF system. I certify that service will be accomplished by the CM/ECF system, which will send notice to all users registered with CM/ECF.

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