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Supreme Court Clarifies ERISA Fiduciary's Duty of Prudence

On January 24, 2022, the Supreme Court held in *Hughes* v. *Northwestern University* that a context-specific inquiry is required to determine whether a retirement plan fiduciary violated ERISA's duty of prudence. The Court reiterated that a fiduciary has the continuing duty to monitor investments and that merely providing investors with a range of investment choices does not excuse the fiduciary's allegedly imprudent decisions.

Background

Under the Employee Retirement Income Security Act of 1974 (ERISA), a fiduciary is subject to a duty of prudence. A fiduciary must discharge its duty "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in alike capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims." 29 U.S.C. § 1104(a)(1)(B). The duty of prudence includes a duty to regularly review and monitor investments. *See Tibble* v. *Edison International*, 575 U.S. 523, 528, 530 (2015).

In *Hughes*, several current and former employees of Northwestern University sued the university, its Retirement Investment Committee, and individual officials, alleging that they breached the statutory duty of prudence in administering the university retirement plans. The relevant plans allowed individual participants to choose how to invest their funds, provided that they select from the menu of options selected by the plan administrators. The employees alleged that the plan administrators acted imprudently by failing to monitor and control recordkeeping fees, offering certain "retail" class investments when materially identical "institutional" class investments were available for lower prices, and presenting too many investment options such that investors were likely to be confused.

The district court granted the plan administrators' motion to dismiss for failure to state a claim and denied leave to amend, and the Seventh Circuit affirmed on appeal. The Supreme Court granted review.

The Supreme Court's Decision

In a unanimous opinion written by Justice Sotomayor, the Supreme Court held that the Seventh Circuit erred in its analysis of the statutory duty of prudence, remanding the case to the panel for further consideration. Justice Barrett did not take part in the decision.

The Court's decision relied on *Tibble*'s articulation of the fiduciary's continuing duty—derived from the common law of trusts—to "monitor investments and remove imprudent ones." In *Tibble*, the Court held that a fiduciary's allegedly imprudent *retention* of an investment can trigger ERISA's limitations period, because a fiduciary is required to "conduct a regular review" of investments. This duty to monitor plan investments, according to the Court, is similarly implicated by the employees' allegations that the plan administrators here acted imprudently through some combination of retaining record-keepers that charged excessive fees; offering too many investment options and thereby causing participant confusion; and neglecting to provide cheaper alternative investments.

The Court concluded that the Seventh Circuit erred in its "exclusive focus" on investor choice and its "categorical rule" that imprudence is not a concern where the plans offered a broad menu of options, including the employees' preferred types of lowcost investments. Rather, even when investors can choose their investments, "plan fiduciaries are required to conduct their own independent evaluation to determine which investments may be prudently included in the plan's menu of options," and to remove imprudent investments within a reasonable time.

The Court remanded the case to the Seventh Circuit for further consideration of the employees' claims, instructing that the appropriate inquiry is "context-specific" and turns on the circumstances prevailing at the time of the fiduciary acts.

Implications

The decision in *Hughes* makes clear that merely providing investors with a broad menu of investment options does not excuse a fiduciary's allegedly imprudent decisions. A retirement plan that includes prudent investment options alongside imprudent options may be insufficient because a fiduciary has the duty to protect investors by continually monitoring and removing those imprudent investments. This duty is not discharged simply because investors have the choice to select their own investments.

But beyond that narrow reaffirmation and application of *Tibble*, the Court did not provide additional guidance on many issues that were hotly contested in the briefing and argument. The Court did not flesh out the factual contours of the duty of prudence or address the district court's factual finding that certain of the plan administrators' decisions were prudent. Nor did the Court directly address questions regarding the proper pleading standard for fiduciary imprudence or discuss what factual allegations would be sufficient to allow the employees' claims to survive a motion to dismiss. The decision thus leaves open to fiduciaries to explain the investment options provided, including those that may charge higher fees. The decision also leaves untouched precedents that analyze whether the fiduciaries engaged in a reasonable process rather than focusing on the results. In remanding to the Seventh Circuit, the Court acknowledged that certain circumstances will "implicate difficult tradeoffs," and that a fiduciary may face a "range of reasonable judgments" depending on context. Specific factual contours will likely be shaped in future litigation in the lower courts.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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