Federal Court Dismisses "Excessive Fee" Claims Against Plan's Service Provider: McCaffree Financial Corporation v. Principal Life Insurance Company

01.20.2016

The U. S. Court of Appeals for the Eighth Circuit has affirmed the dismissal of a retirement plan?s claims against a company with whom the plan had contracted to provide the plan?s investment options. The holding in *McCaffree Financial Corporation v. Principal Life Insurance Company,* No. 15-1007 (8th Cir. January 8, 2016), found that the defendant service provider was not a fiduciary for the services at issue, and thus had no fiduciary liability for allegedly excessive fees charged to the plan?s participants.

Background. McCaffree Financial Corporation (?McCaffree?) sponsored a retirement plan for its employees, and, as the plan administrator, contracted with Principal Life Insurance Company (?Principal?) in 2009 to provide investment options and related services to the plan participants. Principal was paid by the participants for management fees and operating expenses. The management fees were calculated as a percentage of the assets in each individual account, subject to a cap. Principal could adjust the fee for any such account annually, subject to thirty days? notice. Principal could charge for the operating expenses only the amount necessary to maintain the separate accounts; expenses that Principal incurred were passed through to the participants. All of these charges were in addition to any fees charged by any mutual fund in which an account had invested. In the 2009 contract, Principal listed sixty-three funds as an initial ?investment menu?; McCaffree alleged that Principal ?winnowed? this list and ultimately chose twenty-nine funds for the participants? investment options.

Five years after entering the contract, McCaffree filed this lawsuit as a class action on behalf of its plan participants, alleging that Principal charged the participants ?grossly excessive management and other fees? in breach of Principal?s duties as a fiduciary of the plan under ERISA section 404(a).

The federal district court granted Principal?s motion to dismiss the case on the grounds that McCaffree had agreed to the charges in the 2009 contract, Principal was not an ERISA fiduciary at the time the parties agreed upon the allegedly excessive fees, and any subsequent fiduciary duty Principal might owe the participants had an insufficient nexus with the excessive fees alleged in the complaint.

McCaffree appealed to the Eight Circuit.

The Court?s Ruling. In a pithy opinion, the Eighth Circuit affirmed the dismissal, citing several reasons why McCaffree?s complaint failed to state a claim against Principal.

The parties did not dispute that the plan did not name Principal as a fiduciary. McCaffree therefore had to plead facts showing that Principal functioned as fiduciary when taking the actions McCaffree complained of, namely, setting or charging the allegedly excessive fees. This required McCaffree to plead facts showing that Principal exercised discretionary authority or control over the management or administration of the plan and its assets within the meaning of ERISA section 3(21)(A), at least to the extent of setting or charging the fees.

The court held first that Principal?s selection of sixty-three funds for the initial investment menu in the 2009 contract was not a fiduciary act. Following other circuits, the Eighth Circuit held that Principal?s adherence to its agreement with McCaffree did not implicate any fiduciary duty where the agreement resulted from an arm?s-length negotiation. Furthermore, selecting the twenty-nine funds from that larger menu, the ?winnowing process,? did not show a basis to allege a fiduciary breach by Principal, for McCaffree failed to show that the act of selecting the smaller menu was connected to the allegedly excessive fees. Nothing in the complaint showed that only some of the funds on the initial menu had excessive fees or that Principal used its contractual selection authority to choose only ?excessive fee? funds for the shorter menu ultimately offered to the participants.

McCaffree also failed to plead that Principal?s exercise of its contractual authority to increase the management fees annually, subject to a cap, resulted in the allegedly excessive fees, or that Principal?s passing through of operating expenses implicated any fiduciary duty of Principal?s to ensure that such expenses were reasonable. The complaint did not show, for example, that Principal passed through fees in excess of the expenses it actually incurred, and the 2009 contract did permit the pass-through of the expenses incurred.

The court also rejected McCaffree?s assertion that Principal was a fiduciary because it offered the participants investment advice giving rise to a fiduciary duty under ERISA section 404(a). Again, the court found that McCaffree offered no facts to show Principal?s actions as an investment manager were connected to or caused the excessive fees alleged in the complaint.

Finally, the court rejected McCaffree?s argument that Principal did not fully disclose a layer of management fees underlying the Principal mutual funds offered to the plan. Nothing in the complaint showed those fees were excessive, and they were not connected to the additional separate account fees said to be excessive.

In short, Principal?s exercise of the terms of its 2009 contract with McCaffree did not implicate any of its fiduciary duties, and McCaffree showed no connection between an exercise of fiduciary duty and the allegedly excessive fees charged to participants.

The Significant Lessons. The *McCaffree* opinion is a straightforward application of case precedents construing ERISA?s fiduciary duties and liabilities, demonstrates that ERISA fiduciary status is not an

?all or nothing? proposition, and underscores the crucial importance of showing the causal nexus ? especially for claims against plan service providers - between the defendant?s conduct and the alleged injury to the plan and its participants. That lesson is useful not only for ?excessive fee" cases like *McCaffree*, but also for other cases alleging the breach of ERISA fiduciary duties.

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