

MEMO# 31621

February 21, 2019

ICI Files Amicus Brief in 401(k) Fee Case Urging Supreme Court to Rule on Burden Shifting Issue

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February 21, 2019 TO: ICI Members
Pension Committee

Pension Operations Advisory Committee SUBJECTS: Pension RE: ICI Files Amicus Brief in 401(k) Fee Case Urging Supreme Court to Rule on Burden Shifting Issue

ICI recently filed the attached amicus brief in *Putnam Investments, LLC v. Brotherston*,^[1] urging the US Supreme Court to grant certiorari and reverse the First Circuit's decision in the case. The case is the first to go to trial of several class-action lawsuits filed against mutual fund families and focused on the inclusion of proprietary fund products in the 401(k) plans they sponsor for their employees.

At issue in this appeal is whether the plaintiffs bear the burden of proving that a fiduciary breach caused losses to the plan or whether the defendant has the burden of *dis*-proving that a fiduciary breach caused losses to the plan. A related second issue is whether plaintiffs can demonstrate losses simply by comparing the returns and fees of the plan's actual investment options to a hypothetical index-fund-only lineup.

Background

The plaintiffs (former Putnam employees) alleged that Putnam breached its fiduciary duty by including proprietary fund products in its 401(k) plan.^[2] In addition to claiming that Putnam's decision-making was inadequate regarding the investments offered, plaintiffs calculated a loss to the plan, determined by comparing the investment returns and fees of the Putnam funds offered in the plan against a hypothetical lineup of only index funds.

On appeal of the district court's dismissal of the case,^[3] the First Circuit held that plaintiffs' comparison of the plan's fund lineup against index funds was sufficient to show there was a loss to the plan.^[4] It then ruled that "once an ERISA plaintiff has shown a breach of fiduciary duty and loss to the plan, the burden shifts to the fiduciary to prove that such loss was not caused by its breach." The court opined that its decision would not increase plan fiduciaries' burden because a fiduciary "can easily insulate itself" by selecting index funds instead of actively managed funds (i.e., the First Circuit would have fiduciaries offer *only* index funds to avoid litigation). In applying this burden-shifting approach, the First Circuit

deepens an existing circuit split.[\[5\]](#)

Amicus Brief

In January, Putnam filed a petition for certiorari, requesting that the US Supreme Court consider two issues:

- 1) Whether an ERISA plaintiff bears the burden of proving that “losses to the plan result[ed] from” a fiduciary breach, or whether ERISA defendants bear the burden of *dis*-proving loss causation.
- 2) Whether evidence that a plan’s actual investment options did not perform as well as a set of index funds, selected by the plaintiffs with the benefit of hindsight, suffices as a matter of law to establish “losses to the plan.”

ICI’s amicus brief supports Putnam’s request, urging the Supreme Court to resolve both issues and highlighting the importance to the retirement plan community. The brief explains that when selecting a plan’s investment lineup, fiduciaries typically make available a wide range of options because participants’ needs vary significantly. The First Circuit’s ruling disregards the nuances of constructing an investment lineup that serves the best interests of a broad array of plan participants. Its ruling will adversely skew fiduciaries’ selection decisions, increasing fiduciaries’ incentive to limit the menu of investment options, based on the greater litigation risk posed by burden-shifting.

ICI’s brief also explains that allowing plaintiffs to prove a loss solely by comparison to an index-fund-only hypothetical ignores the differences between actively managed investments and index funds as well as their differing benefits for participants. Because of these substantial differences and benefits, actively managed funds and index funds are not suitable as simple comparators for determining loss causation.

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[Attachment](#)

endnotes

[\[1\]](#) *Putnam Inv., LLC v. Brotherston*, U.S., No. 18-926; appealed from *Brotherston v. Putnam Inv., LLC*, No. 17-1711 (1st Cir. 2018).

[\[2\]](#) Although plaintiffs criticize the fact that Putnam made proprietary funds available in the plan, it is important to note that plaintiffs had a wide menu of options from which to choose, including index funds. Putnam’s 401(k) investment menu included nearly all of the open-end mutual funds managed by Putnam that were generally made available to other employers’ retirement plans, as well as passively managed index CITs managed by a Putnam affiliate and a brokerage window through which participants could invest in thousands of unaffiliated funds.

[\[3\]](#) The district court held that plaintiffs failed to identify any specific circumstance in which Putnam and its 401(k) plan put their own interests ahead of plan participants and failed to show that Putnam’s actions resulted in losses to the plan. The First Circuit vacated the district court decision (in part) and remanded the case back to district court, instructing the

lower court to reconsider the case by applying the First Circuit's rules on burden shifting and loss causation.

[4] ICI also filed an amicus brief at the circuit court level. See ICI Memorandum No. 31059, dated January 29, 2018. Available at https://www.ici.org/my_ici/memorandum/memo31059.

[5] The First Circuit joins the Fourth, Fifth, and Eighth Circuits in applying this burden-shifting rule in an action under ERISA seeking monetary relief for breach of fiduciary duty. The Second, Sixth, Seventh, Ninth, Tenth, and Eleventh Circuits apply the ordinary default rule in which the plaintiff bears the burden of proving loss causation.

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