



## Fiduciary Update | May 2022

### **DOL Weighs In on Cryptocurrencies in 401(k) Plans: Be Very Careful ... and Audits Are Coming**

The U.S. Department of Labor (DOL) issued a Compliance Assistance Release in March cautioning 401(k) plan fiduciaries “to exercise extreme care” before they consider adding a cryptocurrency option to a plan’s investment menu. The release included the DOL’s view that, “When plan fiduciaries, charged with the duties of prudence and loyalty, choose to include a cryptocurrency option on a 401(k) plan’s menu, they effectively tell the plan’s participants that knowledgeable investment experts have approved the cryptocurrency option as a prudent option for plan participants.” Although focused on cryptocurrency, the release also references a wide range of digital assets. Importantly, the release is not a formal regulation with the force of law, but it does make clear the DOL’s negative view of cryptocurrencies and other digital assets.

Although the release was directed primarily to 401(k) plan fiduciaries, it referenced defined contribution plans more broadly and can be anticipated to apply to all plans offering participant-directed investments, including 403(b) plans. The DOL also addressed the possible availability of cryptocurrencies in self-directed brokerage windows, which is addressed below.

Specific issues the DOL called out, which fiduciaries should consider if evaluating cryptocurrencies, include:

- They are “highly speculative” and have been “subject to extreme price volatility.” Extreme volatility can have a “devastating impact” on plan participants.
- It is harder for participants to make informed investment decisions about cryptocurrencies than

other investments. It can be “extraordinarily” difficult for even expert investors to separate the facts from the hype about cryptocurrencies.

- Cryptocurrencies are not held in the same way as other investments, presenting a variety of potential issues.
- There is not a commonly accepted approach to how cryptocurrencies are valued. Also, cryptocurrency market intermediaries are not subject to the same reporting and data integrity requirements as more traditional investments.
- The regulatory environment for cryptocurrencies is evolving, and some market participants may be operating outside the regulatory framework. Additionally, cryptocurrencies have reportedly been used in a variety of illegal activities, which could result in limitations on the use of specific offerings.

In an unusual step, following this cautionary list of issues, the DOL also notes that it expects to conduct an investigative program “aimed” at plans that offer participant investments in cryptocurrencies and related products. Any plan fiduciaries considering the addition of cryptocurrencies may want to consider involving legal counsel.

### **Self-Directed Brokerage Accounts: DOL Cryptocurrency Release Opens Door to Examining What Is Offered Through the Account**

At the end of its Compliance Assistance Release on digital currencies, discussed above, the DOL added a further caution to plan fiduciaries whose plans offer self-directed brokerage accounts. A self-directed brokerage account option permits a participant to use a brokerage account as one of their 401(k) plan investment options. Using the brokerage account, they can invest 401(k) plan assets in anything available in the brokerage account.

In the release, the DOL said that fiduciaries whose plans permit self-directed brokerage accounts should expect to be questioned on how they have “squared” their responsibility for plan oversight with the DOL’s serious concerns about cryptocurrency. This seems to open a new area of evaluation by the DOL into what is available through self-directed brokerage accounts.

There is a fiduciary responsibility to select the self-directed brokerage offering and monitor that it is functioning properly and without issues. However, until now it has been generally understood that there is not a fiduciary responsibility to monitor the specific investments offered through the brokerage account. The release seems to lay that responsibility at plan fiduciaries’ feet with respect to cryptocurrencies. It also raises the possibility that other investments available through a self-directed brokerage program may be challenged.

Fiduciaries whose plans offer a self-directed brokerage option should evaluate whether their brokerage account includes cryptocurrencies or other digital assets the DOL is challenging.

### **Pension Actuarial Equivalence Lawsuits Update**

At least 14 lawsuits have been filed alleging that pension plans paid improperly low benefits to some pensioners and their survivors by using incorrect actuarial assumptions. Generally, these cases allege that outdated mortality assumptions or interest rates were used to calculate joint and survivor or early retirement benefits, resulting in understated benefits, violating ERISA's rules.

It has been reported that half of these cases have been resolved. Only two monetary settlements have been reported: one for approximately \$59 million, where the claim was for approximately \$150 million, and the other for \$2.8 million. Motions to dismiss in two of the remaining cases were recently issued and came to opposite conclusions.

In *Belknap v. Partners Healthcare System, Inc.* (D. Mass. 2022), an early retirement (age 62) joint and survivor benefit was calculated using a mortality table from 1951 and an interest rate of 7.5 percent—as prescribed by the plan. In the same plan, for standard single life annuities, up-to-date assumptions including the 2000 mortality table and market-based interest rates (likely 3.7 percent) are used. The suit alleges that, if the early retirement was calculated using the current mortality table and an appropriate interest rate, the monthly difference to the participant would be \$33.48, with a present value of \$5,840. The judge evaluated the law and did not find a requirement that reasonable actuarial assumptions be used. Rather, he found that the plan's dictated assumptions should be used and dismissed the case. An appeal has been filed.

In *Urlab v. CITGO Petroleum Corp.* (ND Ill. 2022), an early retirement (age 62) joint and survivor benefit was calculated using 1971 mortality tables and an interest rate of 8 percent. The plan sponsor argued that the applicable law does not require the use of reasonable actuarial assumptions. The judge rejected this argument, saying, “[I]t cannot possibly be the case that ERISA's actuarial equivalence requirements allow the use of unreasonable mortality assumptions.” For this and other reasons, the motion to dismiss was denied and the case will proceed.

There have been no full trials of these cases, and a pattern of outcomes cannot be discerned from the settlements and motion to dismiss rulings at this time. However, outcome of the appeal in *Belknap* may be informative.

## **Fee Litigation Update**

The flow continues of new cases, decisions, and settlements alleging fiduciary breaches through the overpayment of fees and the retention of underperforming investments in 401(k) and 403(b) plans. A sound process for periodically assessing the reasonableness of fees and expenses and monitoring documents is essential to the defense of these cases. Following is a sampling of this quarter's developments, including appellate court reversal of two cases that had been dismissed in favor of plan fiduciaries and a new suit against fiduciaries of a plan with only \$70 million in assets. Fiduciaries of smaller plans cannot assume that they will not be targeted.

Following is a summary of recent developments:

- **New Case Filed Against Smaller Plan**—Most plans that have been sued alleging overpayment of recordkeeping fees and investment expenses have had approximately \$1 billion in assets or more. A plan with only \$70 million has recently been sued in a case making nearly identical allegations to those in the larger plan cases and requesting class action status. *Aquino v. 99 Cents Only Stores, LLC* (C.D. Cal. 2022)
- **Dismissed Cases Reinstated**—We previously reported on *Davis v. Salesforce.com, Inc.* and *Kong v. Trader Joe's Co.*, both of which were dismissed because the complaints did not include sufficient allegations. Each dismissal was reversed by a separate panel of the U.S. Court of Appeals for the Ninth Circuit. In both instances, the court of appeals found the allegations in the complaints to be sufficient for the case to proceed. *Davis v. Salesforce.com, Inc.* (9<sup>th</sup> Cir. 2022), *Kong v. Trader Joe's Co.* (9<sup>th</sup> Cir. 2022).

#### **New Cases with Mixed Dismissal Results:**

- Case was initially dismissed and survives dismissal after an amended complaint was filed. *Johnson v. PNC Financial Services Group* (D. N.C. 2022).
- After plaintiffs were given the opportunity to file an amended complaint, the new complaint was found to be insufficient and dismissed with prejudice. This means that the case is finished and cannot be refiled. *Matney v. Barrick Gold of North America, Inc.* (D. Utah 2022)
- New case dismissed with leave to file an amended complaint in 28 days. *Perkins v. United Surgical Partners International, Inc.* (N.D. Tex. 2022)
- New case survives motion to dismiss. *Cunningham v. USI Insurance Services, LLC* (S.D. N.Y. 2022)

#### **Fiduciary Breach in Evasive and Incomplete Participant Communications**

Sean Smarra was a participant in the Boilermaker-Blacksmith National Pension Trust, the defined benefit pension plan for Boilermakers union members. He worked as a boilermaker until he was permanently disabled at age 42. Under the Boilermakers pension plan, a fully disabled plan participant is eligible to begin receiving lifetime pension benefits. The plan was amended in January 2017 to substantially reduce the amount of disability benefits based on the participant's age when requesting benefits if they are not yet age 55. To qualify for an unreduced disability pension benefit, plan participants were required to apply for benefits by August 14, 2017.

When he was age 45, in March 2017, Smarra contacted Stacy Higgins at the pension plan's administration firm to ask about his disability retirement benefit. Although he did not say he wanted to begin receiving retirement benefits immediately, Higgins understood his intention to retire soon. Indeed, she mailed him a pension retirement packet the next day. However, she did not inform Smarra that the plan had been amended and that he would receive a reduced benefit if he did not submit his retirement papers by August 14. Because Smarra was only 45, his benefit reduction would be approximately 60 percent.

Higgins was aware of the plan change and the deadline to receive unreduced benefits. However, she and other employees at the pension administrator were affirmatively instructed to not raise or discuss upcoming changes with participants who contacted them. They were also instructed to not respond to participant questions on the subject.

When Smarra applied for benefits later in 2017, he was informed that his benefit would be \$1,393 per month, rather than the \$3,804 he was quoted about a year earlier. Disappointed that his lifetime monthly benefit had been reduced by more than 60 percent, he sued.

The judge observed that fiduciary responsibilities under ERISA “encompass not only a negative duty not to misinform, but also an affirmative duty to inform when the [fiduciary] knows that that silence might be harmful.” The Boilermakers argued that Higgins, as a staff person, was not acting in a fiduciary capacity. The judge disagreed, noting that Boilermakers as the plan fiduciary is responsible for Higgins’s failure to provide Smarra the information he needed to protect his benefits.

Finding that a trial would be unnecessary, the judge entered summary judgment in favor of Smarra. *Smarra v. Boilermaker-Blacksmith National Pension Trust* (W.D. Penn. 2022). The case is now on appeal.

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