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2nd Circ. Shows How To Shut Down ERISA Self-Dealing Suits

By **Kellie Mejdrich**

Law360 (February 16, 2024, 5:12 PM EST) -- A recent Second Circuit decision affirming Goldman Sachs' win in a class action that took aim at proprietary funds in the bank's 401(k) plan provides an employer-side "road map" for staving off or defeating legal challenges to allegedly subpar in-house investment options, attorneys say.

A three-judge panel's nonprecedential summary order Wednesday affirmed a New York federal court's September 2022 decision granting The Goldman Sachs Group Inc. and the Goldman Sachs 401(k) Plan Retirement Committee summary judgment in the Employee Retirement Income Security Act suit.

Both plaintiff- and management-side benefits attorneys who spoke with Law360 after the decision agreed that the panel's opinion and the facts underlying the case underscore the importance of demonstrating a robust process for managing a 401(k) plan, particularly as class action litigation challenging retirement plan fees continues apace.

"What you have here is a very good road map for the defense bar" for how to prove a good retirement plan management process to the court, said Nancy Ross, a partner in Mayer Brown LLP's Chicago office and chair of the firm's ERISA litigation practice.

"There's a lot here that just reiterates what fiduciaries should be doing and how they can minimize their risk in operating plans," Ross said.

Charles Field, partner and chair of the financial services litigation practice at plaintiffs firm Sanford Heisler Sharp LLP, said he agreed that the case was a road map for fiduciaries "who want to prudently and loyally manage their funds."

How We Got Here

Attorneys agree that the case was among a wave of proposed class actions alleging that large employers breached their fiduciary duties under ERISA and violated restrictions against self-dealing by offering higher-fee, lower-performance in-house funds to employees.

Former Goldman employee Leonid Falberg first sued on behalf of a proposed class of employee 401(k) participants in October 2019, alleging that the bank breached its fiduciary duties under ERISA by giving preferential treatment to its own company-managed investment funds.

Falberg also alleged that the company's 2017 decision to remove the challenged funds from employees' 401(k) offering slate — managed by a subsidiary called Goldman Sachs Asset Management — only occurred "after a series of legal rulings against other financial services firms highlighted defendants' liability risk."

Goldman lost a motion to dismiss the case in July 2020, and a New York federal court certified a class of more than 29,000 participants in Goldman's employee 401(k) plan in February 2022. Before its decision to affirm summary judgment Wednesday, the Second Circuit rejected Goldman's bid to decertify the class in June 2022.

Management-side attorneys highlighted the importance of case law showing how to beat claims over in-house funds at the summary judgment stage given other lawsuits pending against employers nationwide.

"We think the plaintiffs bar tries to sue on every proprietary investment case that they can get their hands on," said Daniel Aronowitz, managing principal and owner of Euclid Fiduciary who sells fiduciary liability insurance and has been closely watching the Goldman case.

Aronowitz said the decision "does give plan sponsors more guidance as to how to demonstrate on the record that there is no conflict of interest." Still, Aronowitz said he doubted that the Goldman decision would "stop the plaintiff firms from suing on proprietary investment cases."

Decision Details

The Second Circuit panel said in its crisp nine-page order Wednesday that the New York federal court rightly granted summary judgment to Goldman on claims that the proprietary fund offerings breached a fiduciary duty of loyalty or prudence under ERISA.

The panel said the district court also properly shut down claims that Goldman engaged in prohibited transactions or failed to adequately monitor the plan with respect to the retention of proprietary funds managed by Goldman Sachs Asset Management. The panel said Goldman had also provided "evidence that defendants employed a robust process to manage potential conflicts of interest," including offering training for retirement plan committee members and hiring an independent investment consultant.

Several attorneys said a particularly notable portion of the appellate panel's decision came from its rejection of the class' contention that the lack of an investment policy statement, or IPS, was evidence of a faulty 401(k) management process.

The panel said Falberg had argued that Goldman's retirement plan committee wasn't able to properly scrutinize the in-house funds because the committee hadn't adopted an IPS, but he failed to point to any evidence for concluding that a prudent fiduciary would have necessarily adopted such a statement instead of "relying on another form of deliberative process for selecting and reviewing investments." And even without the statement, undisputed evidence in the record indicated the committee followed a "deliberative and rigorous process" when selecting and monitoring the plan's investments, the panel said.

It was a factor that Euclid Fiduciary's Aronowitz and other attorneys were watching as the case came up for argument in January, as they say most plans have an investment policy statement. Another reason the issue was on benefits attorneys' radar was because a plaintiff-side expert in the case — Marcia Wagner of The Wagner Law Group, a major firm that often represents employers — had faulted Goldman for the lack of an IPS when the case was at the district level.

Field, with Sanford Heisler, said he was "surprised" by the Second Circuit panel's holding regarding the policy statement.

"It's not required, but it seems to be something that you should do," he said, noting that the U.S. Department of Labor has said in guidance that an IPS is something the department considers evidence of a prudent process.

Scott Burnett Smith, founder and chair of Bradley Arant Boult Cummings LLP's appellate litigation practice group, said that even though the case was unpublished, he thought the panel's ruling was an "important" one.

Smith said the Goldman decision offered a "very muscular endorsement of the procedural view of these cases" by the appellate court, with the panel's opinion showing how a good process can protect an employer even if the funds being challenged were ultimately removed following underperformance.

"As long as the plan uses good procedures, and has good advisers, the second-guessing is going to fail," Smith said.

What's Next

Attorneys representing employers are already beginning to cite the Goldman decision in cases alleging 401(k)s were mismanaged because of an employer's conflicted in-house fund offerings.

For example, French investment bank Natixis Investment Managers LP and its retirement plan committee entered a notice of supplemental authority in Massachusetts federal court Thursday citing the Goldman decision in support of their motion for summary judgment in a class action targeting the company's in-house fund offerings. More than 1,200 Natixis workers won class certification in that case in May.

When asked about the nonprecedential nature of the Goldman decision, Mayer Brown's Ross said a summary opinion from the Second Circuit is generally an indication that the appellate court "feels like there's enough law on this already, that this case doesn't present any opportunity to clarify the law or make new law."

"So, the fact that this was a summary opinion suggests that the Second Circuit thought that the facts were very straightforward, and that the district court had enough evidence on summary judgment — so on the papers — to rule in favor of Goldman Sachs," Ross said.

Still, Mark Boyko, a plaintiff-side partner at Bailey Glasser LLP, pushed back on assertions from employer-side attorneys that the Goldman case is going to have an impact on litigation targeting in-house fund offerings.

"I don't know that it would have much impact on other proprietary fund cases where the fact pattern might be different ... the decision looks pretty closely tethered to the factual record in that case," Boyko said.

--Editing by Abbie Sarfo.
