# Hanigan, et al vs. Bechtel

## Cross-selling Managed Account Services

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On May 24, 2024, a class action complaint was filed in the Eastern District Court of Virginia by Debra Hanigan, et al ("Plaintiff") against Bechtel Global Corporation and the Bechtel Trust & Thrift Plan Committee ("Defendants") for a breach of fiduciary duty of prudence by requiring Plan participants to pay excessive administrative fees to be defaulted into the Plan's managed account program.

### FIDUCIARY OBLIGATION

ERISA's fiduciary standards expect employers to (1) establish a prudent process for selecting service providers and reviewing investments [*fiduciary duty of due care*]; (2) ensure that fees paid to service providers are reasonable in light of the level and quality of services provided [*control plan expenses*]; and (3) monitor service providers and investments once selected to make sure they continue to be prudent choices. [*duty to monitor service providers and investments*]

### CLAIM SUMMARY

Plaintiff was automatically defaulted at various times without her consent or instructions into the Plan managed account program, now called the Empower PMP (sub-advised by Financial Engines), which in turn invested her in the International Equity Index Fund, U.S. Small Cap/Mid Cap Equity Index Fund, S&P 500 Index Fund, Bond Fund, Long Duration Bond Index Fund, U.S. Bond Index Fund, and Money Market Fund. As a part of the default process, no additional personalized information was provided by Plaintiff such as demographic or financial background.

Qualified default investment alternatives ("QDIAs") are a legal form of automatic enrollment plan under ERISA. QDIAs allow plan fiduciaries, in the absence of investment direction from the participant, to automatically invest their assets in a default fund or portfolio.

Although the QDIA rule[1] "does not require a plan fiduciary to undertake an evaluation as to which of the QDIAs provided for in the regulation is the most prudent for a participant or the plan," the rule "does not provide relief from the general fiduciary rules applicable to the selection and monitoring of a particular qualified default investment alternative or from any liability that results from a failure to satisfy these duties, including liability for any resulting losses."

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[1] Final Rule, 72 Fed. Reg. 60452, 60453 (Oct. 24, 2007)

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A. MANAGED ACCOUNT

1. MULTI-ASSET PORTFOLIO - Managed accounts (MAs) are a discretionary portfolio management service for a fee that makes investment decisions for the participant within the confines of a plan and its fund options. Most plan participants are expected to receive a Target Date Fund (TDF)-like experience with MAs[2]. According to the 2018 Cerulli Report[3], the top three managed account providers are Fidelity, Financial Engine, and Morningstar
2. PERSONALIZATION - Participants are responsible for proactively entering data that is key to personalization of MAs and engagement is required for a participant to have any chance at receiving any value from portfolio management with MAs. Yet, Empower's MA service did not result in any material personalization for Bechtel Plan participants to warrant any additional fees.
3. UNCLEAR VALUE - MA portfolios are (a) often meaningfully more expensive and not meaningfully more effectively diversified than TDFs and (b) there is no meaningful difference in the level or the personalization of the diversification. According to the 2018 Alight Solutions report[4], TDFs outperformed MAs in median, upside and downside cases.
4. LACK OF FEE TRANSPARENCY – MA fees often account for a significant portion of administrative fees and the portion of fee paid tot eh recordkeeper is often not transparently disclosed[5].
5. FINANCIAL INCENTIVE – Fidelity is one of the largest Mas providers. A study of Form 5500 from 2014 through 2022 reveals that by the end of 2014, Fidelity had 686 recordkeeping plans that had adopted its MAs, but by the end of 2022 if has grown 288% to 2,659 plans adopted MAs at the same time total number of Fidelity clients only grew 38%. The study shows Fidelity revenue grew roughly twice as fast among plans using the MAs compared to those not using the MAs. Through MA offering to participants, recordkeepers collects fees through various structures and is economically incented to have MAs utilized. Revenue received is often 50% or more of participant fees.
6. EMPOWER SPECIFIC – Frome 2016 to 2021, among a consistent set of Empower's recordkeeping clients with more than $500M in assets, those clients that used Empower's MA service generated on average almost fice times as much revenue per participant than those did not us its MA service.

B. SELECTION PROCESS - Under the minimum standard of care for prudent plan fiduciaries, based on the information available prior to and throughout the Class Period (May 24, 2018, through the date of judgment), no rational plan fiduciary having conducted

[2] Aon, Are Managed Accounts More Efficient Than Target Date Funds? (2020)
[3] The Cerulli Report, U.S. Retirement Markets 2018
[4] Alight Solutions, 2018 Professional Investment Assistance Report: The Impact of Managed Accounts and Target Date Funds in Defined Contribution Plans 2007-2016.
[5] Aon, Can You Truly Evaluate Managed Accounts Through Marketing's Rose-Colored Glasses? (2019)

even a cursory analysis could have concluded that it was prudent to utilize an MA service as the QDIA for the Plan.

MA providers are willing to accept lower fees for plans that offer the MA service as the QDIA (as compared to those plans that do not designate the MA as the QDIA) since more total revenue is generated for MA providers when the MA is the QDIA. Given the excessive fees that Defendants agreed to have a large segment of its Plan participants pay for MA services by establishing the Empower managed account as the QDIA, it can be inferred that Defendants did not follow a prudent fiduciary process in selecting the Empower managed account program as the Plan QDIA during the Class Period, thereby causing Bechtel Plan participants to lose tens of millions of dollars in retirement monies during the Class Period.

C. CONTROLLING PLAN EXPENSES

77. A plan fiduciary must monitor the total administrative fees, including QDIA managed account compensation, it pays to the Plan recordkeeper by regularly conducting an independent evaluation of those fees to ensure that such administrative fees are reasonable and remove the recordkeeper and/or change the QDIA if those fees are unreasonable.

During the Class Period, Defendants failed to consider other QDIA alternatives to the Empower managed account program, including TDFs that most plans use as QDIAs, in order to avoid having Plan participants pay excessive and unreasonable administrative fees.

From the years 2018 through 2022, based upon information provided in Participant Fee Disclosures, Financial Statements, and/or in participant quarterly account statements, the Plan paid an effective average annual rate of $320 per participant for administrative fees (including bundled recordkeeping and administrative ("RKA") fee and QDIA Managed Account Compensation).

**Bundled Recordkeeping and Administration Fees**
**Plus QDIA Managed Account Compensation (Bundled RKA+MA)**

| | 2018 | 2019 | 2020 | 2021 | 2022 | *Average* |
|---|---|---|---|---|---|---|
| **Participants** | 16,598 | 16,570 | 16,170 | 15,509 | 15,508 | ***16,071*** |
| **Est. Bundled RKA+MA Fees** | $4,944,765 | $5,255,804 | $5,313,466 | $5,392,174 | $4,803,813 | ***$5,142,004*** |
| **Est. Bundled RKA+MA Per Participant** | $298 | $317 | $329 | $348 | $310 | ***$320*** |
| **Bundled RKA Fees** | $476,695 | $475,890 | $464,402 | $372,216 | $372,192 | ***$432,279*** |
| **Bundled RKA Fees Per PP** | $28.72 | $28.72 | $28.72 | $24 | $24 | ***$27*** |
| **Est. Losses** | $4,468,070 | $4,779,914 | $4,849,064 | $5,019,958 | $4,431,621 | ***$4,709,725*** |
| **Est. Losses Per PP** | $269 | $288 | $300 | $324 | $286 | ***$293*** |
| ***Excessive Fee Multiple*** | *1037%* | *1104%* | *1144%* | *1449%* | *1291%* | *1190%* |

The Bechtel Plan's recordkeeping rate was between $24/pp and $29/pp during the relevant Class Period, but the use of the Empower managed account as the Plan QDIA generated an additional $298/pp to $348/pp for Empower and Financial Engines during the Class Period. By using the Empower managed account program instead as the QDIA, the Plan cost its participants (when accounting for compounding percentages) a total, cumulative amount in excess of $23,555,043.

**Bundled Recordkeeping and Administration Fees**
**Plus QDIA Managed Account Compensation (Bundled RKA+MA)**

| | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|
| RKA Direct Compensation | $4,944,765 | $5,255,804 | $5,313,466 | $5,392,174 | $4,803,813 |
| Est. Conservative RKA Indirect Compensatio | $0 | $0 | $0 | $0 | $0 |
| Est. Conservative Administrative Credit to I | $0 | $0 | $0 | $0 | $0 |
| Est. Conservative Bundled RKA Fees | $4,944,765 | $5,255,804 | $5,313,466 | $5,392,174 | $4,803,813 |
| | | | | | |
| Reasonable Bundled RKA Fees | $476,695 | $475,890 | $464,402 | $372,216 | $372,192 |
| | | | | | |
| Est. Conservative Bundled RKA Losses | $4,468,070 | $4,779,914 | $4,849,064 | $5,019,958 | $4,431,621 |
| Compounding Percentage (Plan Return) | | 19.37% | 13.47% | 10.54% | -17.09% |
| Est. Conservative Cumulative Bundled RKA Losses | $4,468,070 | $10,113,309 | $16,324,151 | $23,064,261 | $23,555,043 |

ERISA FIDUCIARY

A. WHO IS A FIDUCIARY - ERISA's three-pronged functional "fiduciary" definition[6] states that "a person is a fiduciary with respect to a plan to the extent:
   1. he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets,
   2. he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or
   3. he has any discretionary authority or discretionary responsibility in the administration of such plan.

B. THE SOLE INTEREST & EXCLUSIVE PURPOSE - An ERISA fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and for the exclusive purpose of providing benefits to participants and their beneficiaries and defraying reasonable expenses of administering the plan.

C. THE PRUDENT PERSON RULE - A fiduciary also must act prudently "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use."[7]

[6] 29 U.S.C. § 1002(21)(A)
[7] 29 U.S.C. § 1104(a)(1)(B)

## ALLEGATIONS

A. BREACH DUTY OF PRUDENCE

1. Defendants failed to: ensure that the Plan's administrative fees (including QDIA managed account compensation) were objectively reasonable, defray reasonable expenses of administering the Plan, and act with the care, skill, diligence, and prudence required by ERISA.
2. Defendants had a continuing duty to regularly monitor and evaluate the Plan's recordkeeper, Empower, to make sure they were providing the administrative services at reasonable costs, given the highly competitive market surrounding administrative services and the enormous bargaining power the Plan had to negotiate the best fees, and replace the imprudent managed account QDIA with a prudent TDF QDIA.
3. Defendants breached its duty to Plan participants, by failing to employ a prudent process and by failing to evaluate the cost of the Plan's administrative services, include the managed account QDIA, critically or objectively in comparison to other QDIA options available to the Plan.
4. Defendants' failure to discharge its duties with respect to the Plan with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would have used in the conduct of an enterprise of like character and with like aims, breaching its duties under 29 U.S.C. § 1104(a)(1)(B).

B. FAILURE TO ADEQUATELY MONITOROTHER ERISA FIDUCIARIES

Defendants Bechtel and Board had a duty to monitor those individuals responsible for administrative fees and the Plan's QDIA and the related fees on the Plan Committee to ensure that they were adequately performing their fiduciary obligations, and to take prompt and effective action to protect the Plan in the event that these individuals were not fulfilling those duties.

Defendants Bechtel and Board breached their duty to monitor by, among other things:

1. Failing to monitor and evaluate the performance of individuals responsible for administrative fees and the Plan's QDIA on the Plan Committee or have a system in place for doing so, standing idly by as the Plan suffered significant losses in the form of objectively unreasonably administrative fees;
2. Failing to monitor the process by which the Plan's recordkeeper, Empower, was evaluated and failing to investigate the availability of more reasonably priced QDIA alternatives with Empower; and
3. Failing to remove individuals responsible for administrative fees and the Plan's QDIA on the Plan Committee whose performance was inadequate in that these individuals continued to pay the same administrative fees (including QDIA Managed account compensation) over numerous years even though the contracted price was imprudent and excessively costly, given the lack of value associated with the Empower Managed account programs.

## OBSERVATIONS

The increasing prevalence of financial technology in the retirement plan recordkeeping industry is making managed account solutions more widely available. Managed account services typically charge an asset-based account fee ("MA Fee") to make the personalized investment portfolios available to enrolled participants. This MA Fee is assessed on top of the underlying investment fund fees. Further, to make managed account solutions available, the recordkeeper needs to provide fintech access, and related services; thus an added recordkeeping fee is charged. MA Fee is typically scalable. This means the higher the amount of assets being managed, the lower the asset-based fee. As such, by making a managed account solution the QDIA default investment solution, the asset-based fee is typically reduced due to the expected asset volume. The combination of the layered fees is typically more to significantly more than a target date fund default option

The value to a managed account solution is personalization. Typically, the known census data of a participant on a recordkeeping platform are incorporated. Thereafter, the participant would add more personalized data so that a complete picture is taken into consideration when optimizing an investment portfolio for the participant. Then, on an ongoing basis, the participant is to continue to add or revise the data set so that the managed account solution can be responsive and dynamically adjust the personalized portfolio in real time.

Behavioral finance and actual enrollment experience have repeatedly and consistently found that defaulted participants (i.e., those participants unwilling or unable to make investment decisions) tend to be disengaged from the investment management process and as such do not engage with the managed account service. Under this reality, the complete personalization benefit is not realized. The Complaint makes the point that a lower to much lower cost target date fund would deliver equal, and in some cases better, overall outcome than a managed account starved of ongoing participant engagement.

The Allegations in this Complaint against the Defendants are centered around fiduciary prudence and a lack of fiduciary process when managing the plan assets. Moreover, they failed to demonstrate meeting their duty of ongoing monitoring of service providers and the managed account solution itself. Finally, the Complaint makes the point that the Defendants also failed to control Plan expenses and to make certain that not only the cost of the managed account solution is "reasonable" but also all recordkeeping and administration expenses are as well.

The purpose of this summary is to lay out the Plaintiffs' basic case and to examine if (1) there are any issues that a plan sponsor or a plan advisor/consultant should be concerned about regarding underlying allegations and claims; and (2) there is validity that this case sets a new path in future litigations along similar fact pattern pertaining to the use of managed account service in QDIA and what are the fiduciary process in monitoring service providers, their value and controlling plan expenses.