Employee Benefits Newsletter
Winter 2022

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# Target Date Fund Litigation Intensifies

With the explosive rise in excessive fee litigation against retirement plans and their fiduciaries, the threat of a lawsuit is a realistic one for most mid-sized and large retirement plans. Recently, however, some of the litigation involving the selection of "do-it-for-me" investment products such as target date funds and managed accounts has become increasingly complex. The takeaway from this litigation is that plan fiduciaries cannot merely look at fees for these products. They must also evaluate the history and track record of these products, the process for selection of underlying investments, and whether these products have been adopted by other plan fiduciaries or whether their plan is becoming a "guinea pig" for a novel and untested investment.

## Northern Trust

Over the last two years, plan sponsors have faced costly litigation over the Northern Trust Focus Funds; this litigation demonstrates the need to review target date funds to ensure that plan fiduciaries are not adopting an untested product. Although the litigation included allegations related to fees, a significant part of the litigation focused on the fact that the plan sponsors adopted the funds when they had less than five years of performance data available. Subsequently, the funds underperformed 75%-90% of their peers. The plan fiduciaries also failed to take into account the relatively low adoption rates of the Northern Trust investments. One plan fiduciary implicated in these cases settled for $13.75 million in 2021, while the other lawsuits are ongoing.

## Wells Fargo

Recent litigation against Wells Fargo also emphasizes the need to review both novel target date fund products and the nature of the underlying investments especially carefully. In April, Wells Fargo agreed to pay a $32.5 million settlement in connection with offering a proprietary target date fund product in its own plan. The lawsuit alleged that Wells Fargo mapped nearly $5 billion in participant assets to its own untested target date fund product as a means of "seeding" the product for marketing it to other plans. While proprietary funds in target date funds themselves are common and generally not problematic per se, plan fiduciaries should pay special attention to the use of proprietary products in newer product offerings.

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### NFP flexPATH

In recent years, vendors have expanded their offerings of custom target date products. While these products should be considered and offer some advantages compared to traditional target date funds, plan fiduciaries must review them carefully. In particular, the flexPATH litigation focuses on the “novel and untested” management style of the flexPATH product, as well as the selection process for the fund manager and the expertise of that manager. The litigation also raises the issue of unreasonable investment expenses that benefit NFP.

### BlackRock

Finally, plaintiffs have filed at least nine lawsuits in July and August targeting passively managed BlackRock target date funds. These lawsuits, in contrast to the previous wave of lawsuits alleging that plan fiduciaries should have selected low-cost, passively-managed investments, allege that the plan fiduciaries who selected the BlackRock funds chased low fees at the expense of higher-performance investments. The complaints also allege that the plan fiduciaries in question should have selected target date funds with a “through” retirement glidepath, rather than a “to” retirement glidepath like that utilized by the BlackRock funds.

Although much of the litigation described above is ongoing, there are a few takeaways for plan fiduciaries. Merely reviewing fees and performance is not sufficient for target date funds. Plan fiduciaries should also be careful to evaluate new products in the target date fund marketplace and pay special attention to the utilization of proprietary funds in target date funds. While plan fiduciaries may want to consider custom target date fund products that are available to them, these products require special due diligence with respect to manager selection and methodology, fees, and utilization of proprietary products.

If you have questions about the trends in ERISA litigation or want more information about how to mitigate your litigation risks, please reach out to a member of the Kutak Rock Employee Benefits and Executive Compensation practice group.