No. 23-1007

IN THE

Supreme Court of the United States

CASEY CUNNINGHAM, ET AL.,

Petitioners,

v.

CORNELL UNIVERSITY, ET AL.,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF OF QUINN CURTIS, ET AL, AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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INTEREST OF *AMICUS CURIAE*[1]

Amici are law professors with particular interest and scholarly research in the fields of securities and mutual fund regulation, corporate governance, and protections afforded to investors. *Amici* submit this brief because, in their view, the Second Circuit improperly borrowed a plead standard from *Jones v. Harris Assoc. L.P.*, 559 U.S. 335 (2010), which arose under the Investment Company Act (the "ICA"), when determining the pleading requirements of plan participants in their claims arising under the Employee Retirement Income Security Act of 1974 ("ERISA").

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SUMMARY OF ARGUMENT

The ICA does not expressly require that fees be "reasonable" and, indeed, Congress rejected such a standard when it passed that statute. Therefore, a plaintiff raising a claim under the ICA based on a fee being too high can only create an inference of a violation at the pleadings stage if it is "so disproportionately large that [it] could not have been the product of arm's-length bargaining." *Jones v. Harris Assoc. L.P.*, 559 U.S. 335, 346 (2010).

In contrast, Congress imposes a requirement that fees be "reasonable" under ERISA's general fiduciary duties, expressed in ERISA § 404(a)(1)(A)(ii), 29 U.S.C. § 1104(a)(1)(A)(ii), and further dictates that where a transaction is otherwise expressly prohibited by ERISA § 406, 29 U.S.C. § 1106, a defendant fiduciary may, in certain situations, be able to avoid liability by proving an affirmative defense that requires it — the defendant fiduciary — demonstrate that the fee pay by the plan was reasonable. 29 U.S.C. § 1108(b)(2)(A). As a matter of statutory law and policy, the Second Circuit should not have borrowed the ICA's pleading standard from *Jones v. Harris Associates L.P.,* because the statutes are expressly distinct on this point and also because doing so undermines the rights ERISA was intended to protect.

ARGUMENT

Nearly 100 million workers and retirees have over $11 trillion saved in employer-sponsored defined contribution retirement plans.[2] In most of

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[2] EMP. BENEFIT RSCH. INST., *Workplace Retirement Plans: By the Numbers* 1 (Jan. 19, 2023), https://www.ebri.org/docs/default-source/by-the-numbers/ebri_rsrc_facts-and-figures_011923.pdf?sfvrsn=9b6b392f_8 ("There were 85.3 million private-sector

these plans, employers and their agents select the service provider for the plan's recordkeeping, administrative and other services and select a small menu of investment options plan participants can use within their retirement plan.[3] This is an important function as the offering of imprudent investments to plan participants "would place an unreasonable burden on unsophisticated plan participants who do not have the resources to pre-screen investment alternatives." *Hecker v. Deere & Co.*, 569 F.3d 708, 711 (7th Cir. 2009); see also *Hughes v. Nw. Univ.*, 595 U.S. 170, 176 (2022) ("plan fiduciaries are required to conduct their own independent evaluation to determine which investments may be prudently included in the plan's menu of options."). This Court has consistently held that ERISA imposes a requirement that plan sponsors avoid burdening their plans with excessive fees, whether those fees are for recordkeeping and administrative services or charged by the individual investment options selected by the fiduciaries for the plans. *Hughes*, 595 U.S. at 173–176; *Tibble v. Edison Int'l*, 575 U.S. 523, 530–31 (2015); 29 U.S.C. § 1104(a)(1)(A)

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workers who were active participants in a DC plan in 2020.").]; *Release: Quarterly Retirement Market Data*, INV. CO. INST. (Sept. 19, 2024), https://perma.cc/PZZ6-T3UQ.

[3] There are over 7,000 mutual funds available to US investors, *Number of Mutual Funds in the United States from 1997 to 2023*, STATISTICA (Oct. 7, 2024), https://perma.cc/5WYY-GCR2, and employers and their agents can also select from a large number of institutional investment products available to mid-sized and large plans. On average, these thousands of funds are narrowed by the employer or their agents to 20–30 options for the Plan participant. Sarah Holden, Steven Bass & Craig Copeland, *Changes in 401(k) Plan Asset Allocation Among Consistent Participants, 2016–2020*, EBRI ISSUE BRIEF, Oct. 20, 2023, at 10 n.13, https://perma.cc/2CVY-98LM.

(fiduciaries may only burden the plan with "reasonable expenses").

The cases cited above concerned alleged violations of a fiduciary's duties of prudence under ERISA § 404(a), 29 U.S.C. § 1004(a). However, ERISA also expressly prohibits "certain types of transactions" under ERISA § 406, 29 U.S.C. § 1106, "that had been used in the past to benefit other parties at the expense of the plans' participants and beneficiaries." *Reich v. Compton*, 57 F.3d 270, 275 (3d Cir. 1995); *see also*, *Cunningham v. Cornell*, 86 F.4th 961, 978 (2d Cir. 2023). "[T]he point of imposing *per se* liability for ERISA § 406 prohibited transactions is that they are violations even when they are not necessarily a material departure from ordinary standards of care." *McMaken v. GreatBanc Tr. Co.*, No. 17-4983, 2019 WL 1468157, *4 (N.D. Ill. April 3, 2019). As the courts below noted, a fiduciary can avoid liability for a prohibited transaction under ERISA§ 406 by proving that the plan paid "no more than reasonable compensation." *Cunningham*, 86 F.4th at 973.

The current case presents the question of what is required of a plaintiff, if anything, to make a prima facie case sufficient to shift the burden of proof to the defendant about whether "no more than reasonable compensation" was paid. 29 U.S.C. § 1108(b)(2)(A). We take no position on the precise allegations that a plaintiff must make, nor whether a plaintiff must make any allegation at all, to disprove the affirmative defense. Rather, we, as scholars of investment law, write to draw attention to the lower court's error in relying on a wholly inapplicable legal standard that, if adopted, would significantly undermine the welfare of retirement investors and degrade the quality of retirement plans, leading to lower performance and reduced savings at retirement.

I. The lower court erred in relying on cases interpreting the Investment Company Act because, unlike ERISA, the ICA does not require fees to be "reasonable".

The Court below relied on *Jones v. Harris Assocs. L.P.* for an inapplicable standard that a high fee can only create an inference of a violation at the pleadings stage if it is "so disproportionately large that it bears no reasonable relationship to the services rendered". *Cunningham*, 86 F.4th at 977–79 ("[h]ere, Plaintiffs have failed to allege any facts… that would suggest the fees were so disproportionately large that they could not have been the product of arm's-length bargaining.") (quoting *Jones v. Harris Assocs. L.P.*, 559 U.S. 335, 346 (2010)). However, *Jones* is not a case grounded in ERISA § 1108(b)(2)(A) at all, indeed it is not an ERISA case. Rather, *Jones* arose out of an alleged violation of the Investment Company Act ("ICA"). 15 U.S.C. § 80a-35(b).

The lower court's comparison is inapt because the "fiduciary duties" under the ICA are fundamentally different from both ERISA's fiduciary duties under ERISA's general standard of care found in 29 U.S.C. § 1104(a) and Defendants' burden of proving its affirmative defense to *per se* prohibited transactions under ERISA. 29 U.S.C. §§ 1106 and 1108(b)(2)(A).

Jones itself recognizes the point:

> The 'fiduciary duty' standard contained in § 36(b) represented a delicate compromise. Prior to the adoption of the 1970 amendments, shareholders challenging investment adviser fees under state law were required to meet common-law standards of corporate waste, under which an unreasonable or unfair fee might be

> approved unless the court deemed it 'unconscionable' or 'shocking,' and security holders challenging adviser fees under the Investment Company Act itself had been required to prove gross abuse of trust. Aiming to give shareholders a stronger remedy, the SEC proposed a provision that would have empowered the Commission to bring actions to challenge a fee that was not 'reasonable' … Industry representatives, however, objected to this proposal, fearing that it 'might in essence provide the Commission with ratemaking authority.'
>
> The provision that was ultimately enacted adopted a different method of testing management compensation, that was more favorable to shareholders than the previously available remedies but that *did not permit a compensation agreement to be reviewed in court for reasonableness.* This is the fiduciary duty standard in § 36(b).

Jones, 559 U.S. at 340–41 (cleaned up and emphasis added). *See also id*. at 352 ("Congress rejected a 'reasonableness' requirement").

Unlike the ICA, ERISA *does* impose a reasonableness requirement on such fees, both with respect to "expenses of administering the plan" (29 U.S.C. § 1103(c)(1), § 1104(a)(1)(A)(ii)) and as "compensation" of plan service providers (29 U.S.C. § 1108(b)(2)). ERISA's duties to ensure fees are no more than "reasonable" are more demanding than the Investment Company Act's fiduciary duties, which do not mention the level of fees at all and for which Congress expressly rejected imposing an analogous reasonableness requirement.

The two statutes are expressly different in the one way the lower court relied on them to be the same.

This Court need look no further than its own decision in *Tibble v. Edison Int'l* to understand the distinction. In *Tibble*, the fiduciaries selected mutual funds priced at presumptively market rates, yet the plan's participants brought a cause of action alleging breaches of fiduciary duty because the same investments were available at lower cost to large institutional investors, like the Edison plan. *Tibble*, 575 at 525–26. Following a dismissal below, this Court remanded the claims and found the participants could state claims for the fees of such mutual funds being excessive. The participants ultimately prevailed even though the fees set by the plans' investments were normal market rates presumptively set by arms-length negotiations. *Tibble v. Edison Int'l*, 2017 WL 3523737, No. 07-5359 (C.D. Cal. Aug. 16, 2017).

This Court's approach in *Tibble* and *Hughes* cannot be squared with the idea that fees create liability only when they "are so disproportionately large they could not have been the product of arm's length bargaining." Instead, the emphasis under 29 U.S.C. § 1104 is on prudence and reasonableness and the affirmative defense on which this case rests specifically requires a defendant to prove fees were no more than reasonable, rather than establish compliance with *Jones'* far less stringent standard.

II. The Court erred in relying on cases interpreting the ICA because the ICA and ERISA operate within fundamentally different contexts.

The ICA, interpreted in *Jones v. Harris Associates*, operates in a profoundly different context than ERISA

retirement plans, one in which investors are far better positioned to protect themselves. The clearest way to think about the distinction is that the ICA is akin to a usury or anti-price-gouging statute, designed to operate in those rare instances where a normally free and fair marketplace may result, nevertheless, in unfair or unjust outcomes. In contrast, ERISA is an extension to trust law, operating in a situation where the participant has no ability to change recordkeepers or administrators, limited ability to change investment options, and is presumed not to have the sophistication necessary to do so.

15 U.S.C. § 80a-35(b) was adopted by Congress in response to concerns that the mutual fund industry as a whole was overpriced at a time when the market was far smaller and less competitive than it is today. Today, mutual fund investors have thousands of low-cost options. This is not to say that every fund everywhere is fairly priced, but the reality is that outside of the retirement plan context investors dissatisfied with the cost of their fund can simply invest elsewhere and have no shortage of good options. These circumstances have motivated courts to give a narrow reading to the fiduciary protections of the ICA in order to avoid the perception of rate-setting. However, unlike the ICA's background in corporate law, ERISA's trust law fiduciary standards require "something stricter than the morals of the marketplace." *Meinhard v. Salmon*, 249 N.Y. 458, 464 (1928). Indeed, the *Jones* standard is so stringent, it has all but rendered 36(b) a dead letter, with no plaintiffs successfully prosecuting claims.

Investors in retirement plans have only the choice their employers provide. Only the prudence of the employer protects them from excessive recordkeeping

fees. For this reason, it makes sense that ERISA imposes a reasonableness standard to fees that the ICA does not, particularly in the context of prohibited transactions under 29 U.S.C. § 1106. The strength of the fiduciary duty with respect to recordkeeping and investment management fees is critical to plan participants in a way that simply does not apply to retail investors outside of defined contribution and other ERISA plans. Applying *Jones* in the context of retirement plans imports a standard from a fiercely competitive market with thousands of options and applies it a plan menu in which employees may have few, if any, choices and the promised benefit of a prudent expert looking out for them. The lower court erred in finding ERISA's reasonableness requirement analogous context to 36(b) because investors cannot protect themselves by choosing other options and the text of the ICA and ERISA are expressly different on this point.

CONCLUSION

The judgment of the Court of Appeals should be reversed.

Respectfully submitted,

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