

Cornell Ruling Widens Circuit Court Split on ERISA Fiduciary Question

Appellate courts have different interpretation of prohibited transaction rules under the Employee Retirement Income Security Act, paving the way for a potential Supreme Court decision.

Reported by [NOAH ZUSS](#)

A recent appellate court ruling in favor of Cornell University—in a lawsuit alleging fiduciaries mismanaged the 403(b) retirement plans administered by the institution—positions the Supreme Court to eventually resolve deepened splits between U.S. appeals courts on prohibited transaction rules under the Employee Retirement Income Security Act.

In a November 14 decision, the [U.S. 2nd Circuit Court of Appeals](#) agreed with a lower court's decision in *Cunningham v. Cornell University* and affirmed the dismissal of many counts from a lawsuit against Cornell over the cost of recordkeeping fees. The 2nd Circuit's decision in *Cunningham* means plaintiffs in the region overseen by the 2nd Circuit—Connecticut, New York and Vermont—face a higher burden than those in other regions in retirement plan lawsuits.

“We conclude that the district court correctly dismissed Plaintiffs’ prohibited transactions claim and certain duty-of-prudence allegations for failure to state a claim and did not err in granting partial summary judgment to Defendants on the remaining duty-of-prudence claims,” wrote 2nd Circuit Chief Judge Debra Ann Livingston. “In so doing, we hold as a matter of first impression that to state a claim for a prohibited transaction pursuant, it is not enough to allege that a fiduciary caused the plan to compensate a service provider for its services; rather, the complaint must plausibly allege that the services were unnecessary or involved unreasonable compensation ..., thus supporting an inference of disloyalty.”

Decisions regarding ERISA prohibited transactions in cases heard in the 8th and 9th Circuits set different standards than the one set by the 2nd Circuit's decision, increasing the likelihood of the Supreme Court hearing an appeal to set nationwide precedent.

“We will be filing a motion for rehearing,” says Jerry Schlichter, founder and managing partner of Schlichter, Bogard & Denton, which represents the plaintiffs, via email.

The plaintiffs' appeal focused on the following points:

- The dismissal of their claim that Cornell entered into a “prohibited transaction” by paying the plans’ recordkeepers unreasonable compensation;
- The “parsing” of a single count alleging a breach of fiduciary duty into separate sub-claims at the motion-to-dismiss stage;
- The award of summary judgment against the plaintiffs for failure to show loss on their claim that the defendants breached their duty of prudence by failing to monitor and control recordkeeping costs; and
- The award of summary judgment to the defendants on the plaintiffs’ claims that Cornell breached its duty of prudence by failing to remove underperforming investment options and by offering higher-cost retail share classes of mutual funds, rather than lower-cost institutional shares.

The 2nd Circuit ruled for Cornell on each point, according to Livingston's decision.

“Because we agree with the ultimate disposition of each of these claims, we AFFIRM the district court’s judgment,” Livingston wrote. “As the judgment is affirmed, we dismiss the cross-appeals as moot. Because we affirm the district court’s judgment, we do not reach the issues related to the end date of the class period, and we dismiss Defendants’

conditional cross-appeals as moot.”

The retirement plan lawsuit is a tangle of procedural history. The case [initially was filed](#) in 2016 and decided in the U.S. District Court for the Southern District of New York. The original complaint alleged that participants in the Cornell University 403(b) plans were forced to pay excessive fees for investments, the plan included a large number of investment options and multiple recordkeepers, resulting in duplicative expenses for recordkeeping services

Cornell [agreed to pay \\$225,000 in 2020 to settle](#) a single claim that survived summary judgement.

Circuit Courts Split

Circuit courts have split on how to interpret the ERISA rule prohibiting transactions that permit goods or services between a benefit plan and a third party. In 2009, the [8th Circuit Court of Appeals ruled in favor](#) of a plaintiff-friendly approach in the case *Braden v. Wal-Mart Stores Inc.*

In that suit, the 8th Circuit decided that retirement plan investors can overcome a motion to dismiss by alleging that the plan provided goods or services to an interested party without having to show that the arrangement was overpriced or unreasonable.

In August, [the 9th Circuit arrived at its own ruling](#) on prohibited transaction claims. The decision reversed a lower court decision in a retirement plan lawsuit against the AT&T Services Inc. benefit plan committee that alleged the plan had not properly vetted and disclosed dealings with third-party service providers for its 401(k) plan.

In its analysis, the 9th Circuit ruled that ERISA’s “broad” and “unambiguous” prohibited transaction rules fulfill arm’s length service transactions between plans and their vendors. After review, the appeals court panel remanded all of the plaintiffs’ arguments back to the district court.

Several other circuit courts have also issued related decisions. Conflicting rulings from different appellate courts on the same legal issue is one factor the U.S. Supreme Court considers when deciding whether to review a case.

Whether the Supreme Court may step in is “anyone’s guess, even where there is a split in the circuits,” says Drew Oringer, partner in and general counsel at the Wagner Law Group, which is not involved in the litigation. “The Supreme Court has not historically shied away from taking ERISA cases, [and] the case would generally be one that the Court feels is worthy of taking. There’s also a concern that any given case may not have a sufficiently developed factual or legal record.”

In 2022, the Supreme Court [addressed ERISA matters](#) in *Hughes v. Northwestern*. The Supreme Court ruled that the act of determining whether petitioners state plausible claims against retirement plan fiduciaries for violations of ERISA’s duty of prudence demands a context-specific inspection of the fiduciaries’ continuing duty to monitor investments and to remove improper ones, as [articulated in a separate lawsuit heard](#) by the Supreme Court, *Tibble v. Edison*.

Representatives of Cornell did not respond to a request for comment on the *Cunningham v Cornell* ruling.

Tags

[403\(b\) plan](#), [defined contribution retirement plans](#), [Employee Retirement Income Security Act](#), [excessive fees](#), [fiduciary breach](#), [fiduciary duty](#), [nonprofit retirement plans](#), [prohibited](#), [prohibited transactions](#), [recordkeeping fees](#), [retirement plan lawsuit](#)

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