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Trader Joe's $1.2 Million Reminder About Fiduciary Oversight

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Trader Joe's may be known for its cult favorite snacks, like their dark chocolate peanut butter cups, but a recent federal court decision serves up a less appealing item: a judgment of $1.2 Million caused by the failure to prudently monitor 401(k) plan recordkeeping fees.

In *Stephan v Trader Joe's Co.,* the U.S. District Court for the District of Massachusetts agreed with plaintiffs (who, surprisingly, included board members in their complaint), holding that fiduciaries of the Trader Joe's 401(k) Plan breached their fiduciary duties under the Employee Retirement Income Securities Act of 1974 ("ERISA") by failing to adequately monitor and negotiate recordkeeping fees. However, the Trader Joe's Co. successfully defended claims involving investment performance and the use of plan forfeitures. This decision followed a bench trial, (actual trials are rare in ERISA fiduciary litigation), and Trader Joe's, on October 28th filed a Notice of Appeal to the U.S. First Circuit Court of Appeals.

Recordkeeping Fees: Don't Forget to Compare Prices

In the decision, the court found that Trader Joe's defendants breached their fiduciary duty of prudence by failing to adequately monitor and evaluate the reasonableness of the 401(k) plan fees. Central to the court's findings was the fiduciaries' failure to conduct a request for proposal ("RFP") or request for information ("RFI"), or otherwise meaningfully negotiate fees with its longtime recordkeeper, Capital Group.

Capital Group charged $48 per participant annually before voluntarily offering to reduce its fees to $40 per participant in 2021. The court cited that voluntary and significant reduction in fees against the fiduciaries as evidence that a prudent fiduciary review process could have secured the lower rate years earlier. The absence of competitive bidding, evidence of any fee reduction negotiations, and a documented process for evaluating the continued reasonableness of the arrangement supported the court's finding of a fiduciary breach.

This failure proved costly. The court awarded a surcharge of $715,265 plus approximately $472,000 in prejudgment interest, bringing the total to $1.2 million. It is quite likely that the amount awarded was far less than the total attorneys' fees expended, which is a reminder that a good fiduciary insurance policy is critical to mitigating the risks plan fiduciaries face as they navigate ERISA's requirements.

Although ERISA does not require fiduciaries to conduct an RFP on a prescribed schedule or select the lowest-cost provider; the decision reinforces that fiduciaries must actively monitor service provider arrangements and demonstrate a prudent process for evaluating fees. Simply maintaining a longstanding relationship with a recordkeeper because a plan sponsor is satisfied with its service, without documentation of meaningful negotiations or oversight, is not enough.

Investment performance: Not Every Underperformer Needs to Be Replaced

The plaintiffs also challenged the plan's retention of the American Funds Growth Fund of America, alleging its performance warranted removal. Here, Trader Joe's prevailed because it demonstrated that it had used a prudent process, including reviewing fund performance against benchmarks and placing it on a "watch list" when its performance fell below its peers.

Forfeitures: Follow the Recipe

Trader Joe's also prevailed on a claim challenging its use of forfeiture to reduce future company contribution rather than pay plan administrative expenses.

The court found that the plan document expressly permitted this use of forfeitures and assigned responsibility for allocating those funds to the company rather than to the investment committee. The committee's responsibility was to ensure that forfeitures were applied consistently with the plan's terms, which the court found it had done. The forfeited amounts also remained plan assets and were ultimately allocated to participant accounts.

Viewed in the context of the ongoing litigation challenging similar forfeitures practice, the decision does not mean that every use of forfeitures to offset employer contributions is permissible. It does, however, reinforce the importance of clear plan provisions, properly allocated responsibilities, and compliance with the plan documents.

Keep Fiduciary Oversight on the List

Perhaps the most important reminder from Trader Joe's is that fiduciary prudence is about process, and not just the outcome. While Trader Joe's successfully defended its investment monitoring practice by demonstrating a comprehensive review process, its recordkeeping fee oversight fell short.

For Plans who have maintained a longstanding relationship with the same recordkeeper, particularly those who have not recently evaluated or documented their evaluation of their fees and services, now may be a good time to consider conducting a review or conducting a request for proposal ("RFP"). Even if a change in recordkeeper is not necessary, an RFP can help fiduciaries assess and document competitive pricing, evaluate available services, and most importantly demonstrate and document a prudent process for determining whether their current recordkeeping arrangement remains appropriate.

The forfeiture ruling also provides a timely reminder for plan sponsors to review their plan documents and administrative practices. Plan sponsors should confirm that their forfeiture provisions clearly identify permissible uses and that the forfeitures are actually being applied in accordance with those provisions and applicable law.

In sum, this decision reinforces the importance of regularly reviewing plan performance and fees, documenting fiduciary decisions, and ensuring that responsibilities are clearly assigned and conducted. A well-documented process can be just as important as the decisions themselves.

If you have questions about your retirement plan's fiduciary responsibilities, recordkeeping arrangements, or forfeiture provisions, please contact your Boutwell Fay attorney for assistance.

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