Q & A

The Debate over Plan Participant Data as ERISA Plan Assets

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Jeff Mandell, editor of the 401(k) Advisor, interviews Thomas E. Clark, Jr., to discuss the debate over whether plan participant data is an ERISA plan asset, a hot topic in the latest ERISA fiduciary breach lawsuits.

Q An issue developing out of ERISA fiduciary breach litigation centers around the fiduciary duties owed regarding the protection of plan participant data. Can you tell us about this?

A ERISA fiduciaries have always had an obligation to protect the assets of plan participants held in trusts of retirement plans. With the proliferation of website access to retirement plan information along with the increasing use of websites for basic plan interactions such as changing deferral allocations or requesting distributions, questions began to arise about how ERISA's fiduciary duties interacted with the protection of participants from data or privacy breaches. For example, if a plan recordkeeper was hacked and participant data stolen, would this be a violation of ERISA's fiduciary duties or would it instead fall to other more general federal or state laws to define roles and responsibilities. Shortly after this debate began, the law firm Schlichter, Bogard, and Denton, known for mechanizing excessive fee lawsuits against large billion-dollar 401(k) plan, filed its first lawsuit alleging that participant data in general was a plan asset and therefore protection of participant data involved ERISA's fiduciary duties.

Q Did that original lawsuit involve privacy breaches?

A No. The original lawsuit alleging that plan participant data is a plan asset instead centered around the common practice of allowing plan service providers to have access to participant data in order to allow them the opportunity to "cross-sell" or offer additional products and services to plan participants outside of the retirement plan. The basic premise, and motive behind the original lawsuit, was to allege that the fees received by the plan's recordkeepers were excessive because the plan's fiduciaries should not have given the participant data to the recordkeeper and allow them the opportunity to make additional revenue.

Q Has the Department of Labor ever addressed this issue?

A Not directly. There is no statute, regulation, or subregulatory guidance stating that plan participant data is a

plan asset. Additionally, no court in the United States agreed with the position.

Q But what about settlement agreements that have prohibited cross selling by the recordkeepers?

A Settlement agreements amount to nothing more than private contracts between the parties of the agreement. They have no precedential authority over any other party. However, the settlement agreements, along with the bringing of additional lawsuits alleging the same theory, have created something of a firestorm in the industry.

Q Have courts ruled against the theory?

A Yes. The judge in *Divane v. Northwestern University* in the Northern District of Illinois stated the following in rejecting the theory: "To begin with, it is in no way imprudent for defendants to allow [the recordkeeper]…to have access to each participant's contact information, their choice of investments, their employment status, their age and their proximity to retirement. [The recordkeeper] needed that information in order to serve as record keeper… Plaintiff has…cited a single case in which a court has held that releasing confidential information or allowing someone to use confidential information constitutes a breach of fiduciary duty under ERISA. This Court will not be the first, particularly in light of Congress's hope that litigation would not discourage employers from offering plans and in light of the principle that breach of fiduciary duty remedies inure to the plans."

Q What subsequently happened in *Divane*? And have there been other lawsuits?

A The plaintiffs in the case appealed to the Seventh Circuit Court of Appeals and their appeal was entirely rejected on other grounds, with the judges not directly addressing the issue of participant data as a plan asset. Furthermore, there have been lawsuits independent of *Divane*.

Q Are there allegations that any recordkeeper sells participant data to any other party?

A Not that I am aware of. Nor am I aware of that outside of any court allegations.

Q Doesn't the Department of Labor have a regulation that defined plan assets?

A Absolutely yes. Finalized in the 1990's, the plan asset regulation is an important one in the ERISA fiduciary world because whether or not you are a fiduciary often involves whether your conduct or actions involved plan assets, so it is very important to understand how the regulation is drafted.

Q Does the plan asset regulation address participant data?

A No, it does not. Instead, the plan asset regulation focuses on tangible assets that can be held in trust like securities, bonds, and the like.

Q How are defendant plan sponsors responding to these allegations?

A The arguments are too numerous for our interview to address all of them, so I will address a few. In one argument, defendants take the position that the complaints alleging breaches don't allege that any of the plan participants acting as plaintiffs in the lawsuits were harmed in any way. For example, the lawsuits do not provide any factual allegation that a plaintiff was sold a product by a recordkeeper affiliate that harmed them. This is important because there is a legal doctrine called standing. Plaintiffs in a lawsuit must have "standing" to bring the claim or said another way, they must show that they themselves allegedly suffered the injury they allege the defendant caused. The issues of standing and ERISA are influx right now with a major decision by the Supreme Court this year involving defined benefit plans that may have consequences over defined contribution plans. Second, defendants have argued that

In another argument, defendants point out that plan participant data cannot be a plan asset because if it was, a plan participant themselves would be a plan fiduciary when they provide their own data to someone else. It is well understood that a participant does not have a right to distribute their own assets from a retirement plan because those assets are held in trust by a fiduciary. Only the fiduciary can approve a distribution (presumably after receiving a request from a participant) and the approval of the distribution is itself a fiduciary act governed by ERISA. It is well understood that a plan participant cannot only provide their own personal data to anyone they choose, they can also log onto their retirement plan website and download every notice, form, participant statement, and fee disclosure associated with their account, that would them provide the same data that the plaintiffs in these cases are alleging is a plan asset. As we know, participants do this every day and it has never been a problem. As such, it demonstrates that the plaintiffs alleging these theories have quite an uphill battle to convince the court they are right.

Q Are there any unintended consequences of the theory that plan participant data is a plan asset?

A Yes. If in fact plan participant data is a plan asset and theoretically could be quantified and given a value, service providers are free to be paid from plan assets as long as there is an applicable prohibited transaction exemption such as 408(b)(2). Consequently, an ERISA fiduciary could be sued if they refuse to let a recordkeeper use the data in order to lower the overall recordkeeping fees from the plan. Or in another situation, an ERISA fiduciary could be sued for selecting a recordkeeper that doesn't cross sell because the fees paid would be excessive compared to a recordkeeper who could make additional revenue not from the plan through cross selling.

Q What should fiduciaries be doing now while these lawsuits wind their way through court?

A First, ERISA fiduciaries should review their service agreements with their plan recordkeepers. In most agreements, the use of plan participant data is addressed in the agreement and the agreement reads that the ERISA fiduciary is approving the recordkeeper's use. As of the current state of the law, this is sound and prudent, especially if such a term is included after a traditional recordkeeper search is done and the ERISA fiduciary determines that the fees are reasonable. ERISA fiduciaries should make sure that they understand how and if participant data is used by the recordkeepers responding to the search. Second, if an ERISA fiduciary decides they do not want to allow their plan's recordkeeper to use participant data, they should explicitly get that in writing as part of the service agreement. This is regularly seen in practice, especially by the largest plan sponsors who often have robust custom communications programs with their participants and want complete control over what is received.

Q How do you see the litigation resolving?

A While on any day it is possible to get a judge to agree with your argument, even if it is in the minority, I think the plaintiffs in these cases face an uphill battle fighting against the weight of there being no new explicit statutory statement, regulatory statement, or subregulatory statement on the issue in their favor. Along with the absurdities that would result like participants becoming fiduciaries over their own data, judges, like the one in *Divane*, are likely to take the position that such a drastic change in fiduciary duties is better left to Congress or the Department of Labor to decide.

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