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The Supreme Court Clarifies Low Pleading Bar for ERISA Excess Fee Cases

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On April 17, 2025, the U.S. Supreme Court issued a unanimous opinion that has the potential to make it more difficult for defendants to have excess fee cases for 401(k) or 403(b) plans dismissed at an early stage of litigation, before potentially costly and burdensome discovery processes begin.

In *Cunningham v. Cornell University*, 145 S. Ct. 1020 (2025), the Court found that plaintiffs do not have to plausibly allege that service provider fees paid by the plan are unreasonable; it is enough to allege that fiduciaries caused the plan to enter into a transaction for the payment of services, including one which is permitted under ERISA and necessary for the operation of the plan. While plaintiffs would still ultimately have to prove that service provider fees were unreasonable to prevail on excess fee claims, the *Cunningham* holding may make it more difficult for defendants to be granted a motion to dismiss because plausible allegations of unreasonable fees are not required at the pleadings stage.

The Court acknowledged that its decision has the potential to increase the costs and burdens of litigation for employers, but it pointed to several alternatives for lower courts to address "meritless" litigation. *Id.* at 1031-32. As the concurring opinion of Justice Alito (joined by Justices Thomas and Kavanaugh) noted, however, these alternatives have not been commonly used and will only ameliorate the repercussions of *Cunningham* to the extent that they are now adopted by lower courts—something that "remains to be seen." *Id.* at 1032, 1034 (Alito, J., concurring).

Thus, at present, *Cunningham* has the potential to increase litigation costs for employers sponsoring 401(k) or 403(b) plans. Further, because *Cunningham* increases the risk of sponsoring a plan, *Cunningham* may result in increased fiduciary liability premiums even for plans that are not the subject of excess fee litigation.

"Reasonable Compensation" Background

Fiduciaries of 401(k) plans and other ERISA-covered defined contribution plans have a duty to ensure that no more than reasonable expenses are paid for administering the plan. The reasonableness of plan expenses implicates both the general fiduciary duties under ERISA of acting prudently and exclusively in the interest of participants and paying only reasonable plan expenses, as well as the special prohibited transaction rules.

The prohibited transaction rules apply to most transactions involving a plan and "parties in interest" to

the plan, which include plan fiduciaries and other plan service providers, such as recordkeepers. Because recordkeepers are considered "parties in interest," a prohibited transaction results any time a fiduciary causes a plan to pay recordkeeping expenses. But there are a number of exemptions from the prohibited transaction rules, including Section 408(b)(2) of ERISA, which provides an exemption for services provided by a party in interest as long as (i) the services are necessary for plan operation (as recordkeeping services routinely are), and (ii) the plan pays the party in interest no more than "reasonable compensation" for the services provided (the "Reasonable Compensation Exemption"). Conceptually, both the fiduciary duties of prudence and the Reasonable Compensation Exemption are satisfied when no more than reasonable compensation is paid for necessary services provided to the plan.

Cuningham's Impact on Pleading Standards

To survive a motion to dismiss, plaintiffs must make plausible allegations in support of their claims. For plaintiffs to allege that fiduciaries breached their duties by causing a plan to pay excess fees under the general fiduciary duties of ERISA, they would have to make plausible allegations that the fees paid by the plan were excessive. Plaintiffs typically rely on fee information reported in disclosures to participants or as part of the plan's Form 5500 filings to support these claims.

The question addressed in *Cunningham* is whether plaintiffs would also need to make plausible allegations that fees were excessive as part of a prohibited transaction claim. The Court held that the Reasonable Compensation Exemption is an affirmative defense. Because the burden of proving an affirmative defense falls on the defendant, plaintiffs do not need to plead that the Reasonable Compensation Exemption was not met. As a result, plaintiffs have to allege only that a prohibited transaction occurred, which in the context of recordkeeping expenses means only that the plan paid expenses to the recordkeeper.

This ruling makes it more difficult for employers to secure dismissals. A motion to dismiss tests whether the plaintiff has made plausible allegations in support of its claims. Ordinarily affirmative defenses may not be raised on a motion to dismiss, although they may be raised if they clearly apply from the face of the pleading. *Boquist v. Courtney*, 32 F.4th 764 (9th Cir. 2022). If plaintiffs have to allege only that a plan paid service fees without having to plausibly allege that the fees paid were unreasonable, then plaintiffs may be able to survive a motion to dismiss and advance to the discovery phase without plausibly making any allegations that plan fees were in fact unreasonable (or that there was any imprudent action or omission of the plan fiduciaries). In his concurrence, Justice Alito noted that "getting by a motion to dismiss is often the whole ball game because of the cost of discovery. Defendants facing those costs often calculate that it is efficient to settle a case even though they are convinced that they would win if the litigation continued." *Id.* at 1033 (Alito, J., concurring).

Potential Alternatives for Mitigating Effects of _Cunningham_

The Court recognized that its holding has the potential to increase the costs of litigating excess fee

claims that lack merit. The Court pointed to four possible alternatives for limiting the decision's fallout, which otherwise will result in meritless cases advancing to discovery:

1. Defendants can assert the affirmative defense that the Reasonable Compensation Exemption applies in an answer, and the court can require plaintiffs to respond to it. If plaintiffs then do not plausibly allege that the exemption does not apply, the court can dismiss the action. Justice Alito's concurrence noted that while this does not appear to be a commonly used procedure, the Court has endorsed it in the past, and he encouraged lower courts to use this procedure to dismiss "insubstantial claims." *Id.* at 1033 (Alito, J., concurring).

2. Courts can dismiss the action on a standing basis if plaintiffs allege a prohibited transaction but fail to plausibly allege a concrete injury. The "standing" argument may potentially apply if a complaint only alleges a service provider contract without alleging that participants have been harmed by it. Accordingly, the plaintiffs may need to make some allegations of unreasonableness to survive a motion to dismiss. If plaintiffs allege that fees were unreasonable, this may facilitate defendants having the Reasonable Compensation Exemption defense considered in a motion to dismiss because the exemption would arguably be directly implicated on the face of the complaint.

- Note: Because the Supreme Court already recognized that participants in defined benefit pension plans ordinarily do not have standing because their benefits are usually not affected by investment performance or plan expenses, the ramifications of the *Cunningham*'s holding should not be expected to spill over to defined benefit plans except in rare circumstances.

3. If the Reasonable Compensation Exemption obviously applies, and plaintiff and counsel lack good faith basis to allege that it does not apply, the court may impose Rule 11 sanctions.

4. The court has discretion to allow for cost shifting (*e.g.*, attorneys' fees) if the defendants prevail in litigation.

The third alternative above seems unlikely to have a substantial impact in practice because the vast majority of service fee claims should get past a simple "good faith" standard. In turn, the fourth alternative seems likely to be hampered by existing standards for ERISA attorneys' fee awards that are harder for defendants to satisfy than for plaintiffs. In theory, the second alternative could have a real impact, but past decisions on standing in ERISA cases have been somewhat muddled, and so the second option's emergence as a meaningful shield for defendants may take some time. Therefore, the best near-term option for defendants appears to be that district courts, in a departure from traditional practice, follow the strong recommendation of the Alito concurrence (and the more moderate encouragement from the main opinion) to consider the Reasonable Compensation Exemption at the motion to dismiss stage (if it is plausibly asserted in the defendant's answer).

In addition to the alternatives recognized by the Court, the Department of Labor could possibly take steps to address the potential for meritless excess fee cases discouraging employers from continuing plans. Daniel Aronowitz, who has been nominated to lead the Department of Labor's Employee Benefits Security Administration, has unofficially (in his personal capacity and not on behalf of the agency) called for a higher pleading standard in ERISA cases to "weed out the many meritless cases being filed each month." (see: link).

However, the Department of Labor's ability to influence the course of fee litigation is limited by the Supreme Court's holding in *Loper Bright Enterprises v. Raimondo*, 603 U.S. 369 (2024), which found that courts should not defer to regulatory agencies in interpreting statutes simply because a statute is ambiguous. After *Loper Bright* courts cannot be expected to defer to the Department of Labor, but courts may still be persuaded by positions that the Department of Labor takes through regulatory actions or *amicus* (friend of the court) briefs. The Department of Labor could also recommend that Congress impose higher pleading standards through the legislative process to overturn the holding in *Cunningham*.

But without Congressional action, the consequences of *Cunningham* will depend on the extent to which lower courts apply the alternatives (and primarily the first and second alternatives) to resolve meritless excess fee cases promptly before defendants are subjected to the costs and burdens of the discovery process.