FIRST CIRCUIT UPHOLDS FIDELITY'S FLOAT INTEREST PRACTICES

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A group of six retirement plan participants and one plan administrator filed a lawsuit on behalf of eight 401(k) plans against Fidelity Management Trust Company and its affiliates (Fidelity) for dealing with plan assets in breach of Fidelity's fiduciary duties under the Employee Retirement Income Security Act of 1974 (ERISA). In connection with plan withdrawals requested by plan participants, the plaintiffs in the case alleged Fidelity, in acting as an intermediary in the withdrawal process, improperly retained and benefited from interest earned on cash generated by the liquidation of plan investments (so-called "float" interest), and therefore breached the ERISA fiduciary duty of loyalty and the ERISA prohibition against self-dealing. Funds generated by the liquidation of mutual fund investments earned interest while they were temporarily held in an overnight account that was owned and controlled by Fidelity before those funds (without any of the interest earned overnight) were transferred back to an account for disbursement to the participant. And, if the participant requested a payout via check (instead of an electronic disbursement), the principal in the disbursement account would accrue interest until the check was cashed.

The suing participants did not claim any direct, personal stake in the "float" interest, and did not contend that the payouts they received were less than the amount to which they were entitled from the plans. The plaintiffs maintained, however, that the "float" interest nonetheless was required by ERISA to be credited to the plans, and could not be retained for the benefit of Fidelity or the investment funds from which funds were withdrawn. The plaintiffs argued that the "float" interest should inure to the benefit of all plan participants.

A federal district court dismissed the lawsuit for failure to state a claim on which relief could be granted (see April 2015 edition of *Employee Benefits Developments*), and the plaintiffs appealed the district court decision to the Court of Appeals for the First Circuit. The First Circuit affirmed the district court's decision and, in so doing, ruled that there was no basis for concluding that Fidelity's practice with respect to "float" interest violated ERISA's duty of loyalty or the prohibition on self-dealing.

The crux of the plaintiff's argument was that cash generated from the redemption of the plans' mutual fund shares, under ordinary property rights, was a plan asset because the mutual fund shares, immediately before the redemption, were plan

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assets. And, if the cash proceeds of the redemption are plan assets, then the interest earned on that cash also must be plan assets.

The First Circuit disagreed. The First Circuit ruled that because the cash proceeds of the redemption did not go, and were never intended to go, back to the plan, those proceeds never became plan assets. The First Circuit determined that Fidelity should be more properly viewed as "an agent charged with transferring the cash [directly] from the fund to participant outside the plan, not to the plan itself." In reaching its decision, the court noted that the agreements between Fidelity and the plans expressly provided for direct distribution by Fidelity to a participant, and did not offer any indication that the plans were "meant to exercise, or receive a benefit under, ordinary property rights in the traveling cash." Because the First Circuit ultimately rejected the plaintiff's assertion that the cash should be treated as a plan asset, there was no basis for fiduciary breach claims under ERISA. *In re Fidelity ERISA Float Litig.* (1st Cir. 2016)