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WHAT IS THE CORRECT STANDARD OF PRUDENCE IN EMPLOYER STOCK CASES?

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I. INTRODUCTION

A decade after the collapse of Enron and WorldCom, the headlines were flooded with the collapse of companies like Bear Stearns and Lehman Brothers due to the subprime mortgage crisis.[1] After this latest economic crisis, the continued investment in common stock via a retirement plan may be considered risky for purposes of achieving a suitable retirement; however, this is not necessarily true. Common stock can arguably be a prudent investment within the overall investment portfolio of a retirement plan. In reality, common stock often fluctuates in value, so a drop in the stock price over a period of time should not be the basis of a lawsuit claiming the stock was an imprudent investment. Many prudent investors purchase stock that fluctuates, but becomes profitable in the long run.[2] As the great investor Warren Buffet

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1. Carrick Mollenkamp, Susanne Craig, Serena NG, & Aaron Lucchetti, *Lehman Files for Bankruptcy, Merrill Sold, AIG Seeks Cash*, WALL ST. J. (Sept. 16, 2008), http://online.wsj.com/article/SB122145492097035549.html.

2. *Table: Returns of Corporate DC Plans with Large Investments in Company Stock*, PENSION AND INVESTMENTS (July 12, 2010), http://www.pionline.com/article/20100712/chart01/100709908. Company stock returns of corporate defined contribution plans with large investments in company stock vs. the S & P 500. Total returns through June 30, 2010; returns for periods of more than one year annualized.

once said, "In the 20th century, the United States endured two world wars and other traumatic and expensive military conflicts; the Depression; a dozen or so recessions and financial panics; oil shocks; a flu epidemic; and the resignation of a disgraced president. Yet the Dow rose from 66 to 11,497."[3] Accordingly, investment in common stock can be judged on a uniform basis in accordance with a well-crafted retirement portfolio and can ultimately be deemed a prudent investment.

Yet, with the stock market crisis of 2008, many companies that provide pension plans with an option to invest in employer stock have been the subject of lawsuits claiming violations of the fiduciary provisions under the Employee Retirement Income Security Act of 1974 ("ERISA"). Many cases have involved companies on the verge of bankruptcy, causing employer stock to become worthless.[4] Nonetheless, even after a decade of the billion-dollar losses in retirement savings by participants in the more publicized cases of the Enron, WorldCom and Global Crossing, participants are still investing a considerable percentage of their retirement account balances in employer stock today.[5]

Over the years, given the subprime mortgage crisis, scandals such as those involving Enron and Bernie Madoff, the unprecedented government bailout, and the international economic crises, many participants in 401(k) plans have seen the value of their account balances drop dramatically in their

Company	1-year return	3-year return	5-year return	10-year return
General Electric	26.25%	-24.37%	-12.73%	-9.43%
Caterpillar	87.58%	-5.59%	7.42%	16.46%
Target	26.29%	-6.95%	-0.88%	6.37%
Occidental Petroleum	19.25%	11.94%	16.89%	24.97%
Coca-Cola	7.78%	1.56%	6.75%	1.01%
Johnson & Johnson	7.45%	1.65%	0.84%	3.73%
CSX	46.12%	5.24%	20.26%	18.65%
Praxair	9.21%	3.85%	12.34%	16.95%
McDonald's	18.57%	12.97%	22.46%	9.44%
S & P 500 Index	14.43%	-9.79%	-0.79%	-1.59%

3. Warren Buffett, *Buy American. I am.*, N.Y. TIMES (Oct. 17, 2008), *available at* http://www.nytimes.com/2008/10/17/opinion/17buffett.html?pagewanted=print.

4. Christopher Farrell, *The Problem with Pension Plans*, BUS. WK. ONLINE (Jan. 11, 2002), http://www.businessweek.com/bwdaily/dnflash/jan2002/nf20020111_3044.htm.

5. Bruce Meyerson, *All Business: 401(k) Savers Should Heed Lessons of Enron*, COLUMBIAN (VANCOUVER, WA) (June 12, 2004), *available at* www.westlaw.com (accessed by searching for 2004 WLNR 11543921).

investments in employer stock. In this regard, the individuals and entities responsible for the administration of 401(k) plans, and frequently the members of the companies' board of directors, have been sued by 401(k) participants under ERISA for breach of fiduciary duty. Usually the class action complaints allege that the plan's investment in employer stock was imprudent and/or that certain misrepresentations or omissions were made about the company's financials that precluded participants from making informed decisions about their investment in employer stock.[6]

In cases involving employer-directed contributions, as well as cases involving participant-directed contributions, the allegations of many of these cases sound very much like matters that would be alleged as violations of federal securities laws but for the fact that the plaintiffs are participants in a plan governed by ERISA. In fact, many of the same plaintiffs have brought suits alleging securities law violations in addition to bringing ERISA lawsuits.

A bright line rule has not yet developed as to liability in these stock drop cases. In fact, to date, very few of these cases have been fully litigated.[7] Motions to dismiss have been granted[8] or denied,[9]

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6. The disclosure claims are beyond the scope of this Article. *See* Jeffrey Mamorsky & Jose Jara, *Subprime Mortgage Crisis Impacts ERISA Plan Investment in Employer Stock*, 24 J. COMP. & BENEFITS 2, 5 (2008) (discussing disclosure obligations).

7. Landgraff v. Columbia/HCA Healthcare Corp. of Am., 2000 WL 33726564, at *19 (M.D. Tenn. 2000) ("[i]n summary, the Court finds that the plaintiffs have not established that a reasonable fiduciary would have determined that the investment of the [Plan] assets in Columbia/HCA stock was imprudent, thereby rebutting the presumption of reasonableness afforded to defendants' actions."); DiFelice v. U.S. Airways, Inc., 436 F. Supp. 2d 756, 786 (E.D. Vir. 2006) (finding that the defendant fiduciaries met their duties of procedural prudence because of the existence of the SPD and its myriad of disclosures and warnings regarding the company stock fund, regular meetings regarding the sustainability of the company stock fund, appointment of an independent fiduciary, and good faith belief in the legitimacy of the U.S. Airways restructuring plan to stave off bankruptcy); Nelson v. Hoodwall, 512 F.3d 347, 350 (7th Cir. 2008) ("With or without the [*Moench*] presumption . . . it is clear that the defendants here all viewed continued investments in IPALCO and AES as an appropriate and suitable investment option . . . ."); Brieger v. Tellabs, Inc., 629 F. Supp. 2d 848, 863-64 (N.D. Ill. 2009) (deferring to a fiduciary's good faith investigation and reasonable belief in the soundness of investment decisions).

8. *In re* Lehman Brothers Secs. and ERISA Litig., 683 F. Supp. 2d 294, 301-02 (S.D.N.Y. 2010) (dismissing complaint because the committee members could not have known of an imminent corporate collapse or other dire situation); *In re* Williams Cos. ERISA Litig., 271 F. Supp. 2d 1328, 1338 (N.D. Okla. 2003) (dismissing claims against board members for not correcting inaccurate disclosures and failing to monitor the benefits committee, which continued plan investments in company stock); *In re* Sprint Corp. ERISA Litig., 388 F. Supp. 2d 1207, 1229-30 (D. Kan. 2004) (granting directors motion to dismiss certain ERISA claims including prudent investment and inadequate disclosures); Crowley *ex rel.* Corning, Inc. Inv. Plan v. Corning,

motions for summary judgment have been granted or denied,[10] and a large number of settlements have been reached.[11] Over the past decade, these settlements have totaled over $1 billion.[12] Yet, despite these risks and uncertainties, many employers still offer employees the opportunity to invest in the employer's common

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Inc., 2004 WL 763873, at *4 (W.D.N.Y. 2004) (dismissing the case and finding that company and board members are not fiduciaries under ERISA).

9. Dann v. Lincoln National Corp., 708 F. Supp. 2d 481 (E.D. Penn. 2010) (denying defendants' motion to dismiss because "[w]ith the present interest in the etiology of the financial crisis, it would be irresponsible to cut off discovery into the allegations in the Amended Complaint at this stage of the litigation."); Hill v. BellSouth Corp., 313 F. Supp. 2d 1361, 1365 (N.D. Ga. 2004) (noting defendants' motion to dismiss was denied); *In re* Elec. Data Sys. Corp. ERISA Litig., 305 F. Supp. 2d 658, 668-69 (E.D. Tex. 2004) (determining that board of directors had fiduciary status under ERISA because they had authority to appoint other fiduciaries and rejected the defendants' arguments that the "ESOP presumption" bars plaintiffs' claim); *In re* CMS Energy ERISA Litig., 312 F. Supp. 2d 898, 907-08 (E.D. Mich. 2004) (granting defendant's motion to dismiss based because the directors and officers could not have breached their fiduciary duties for failing to amend the plans to eliminate the employer stock investments, but also finding that the individual directors and officers could have breached their ERISA fiduciary duties by failing to take other actions to protect the value of participants' plan assets depending on the "responsibilities actually assumed by them"); Kling v. Fidelity Mgmt. Trust Co., 323 F. Supp. 2d 132, 150 (D. Mass. 2004) (denying defendants' motion to dismiss); Rankin v. Rots, 278 F. Supp. 2d 853, 879 (E.D. Mich. 2003) (denying defendants' motion to dismiss because the plaintiffs adequately alleged fiduciary status of board members); Pa. Fed'n v. Norfolk S. Corp. Thoroughbred Ret. Inv. Plan, 2004 WL 228685, at *7 (E.D. Pa. 2004) (refusing to apply the ESOP presumption at the 12(b)(6) motion stage, but noting that the plaintiff must overcome this presumption at summary judgment or trial stage).

10. Stanford v. Foamex, 2011 U.S. Dist. LEXIS 112283 (E.D. Penn. Sept. 30, 2011) (granting defendants' summary judgment motion in part and denying it in part); George v. Kraft Foods, 2011 U.S. Dist. LEXIS 76473 (N.D. Ill. July 14, 2011) (same); McGabe v. Capital Mercury Apparel, 752 F. Supp. 2d 396 (S.D. N.Y. 2010) (granting defendants' motion for summary judgment).

11. *In re* Hartford Fin. Servs., 2010 WL 135186, at *1 (D. Conn. 2010) (noting $1.925 million for stock drop claim arising from the credit crisis); Stanford v. Foamex L.P., 263 F.R.D. 156, 160 (E.D. Pa. 2009) (noting $3.6 million in claim arising out of the liquidation of employer stock); *In re* YRC Worldwide, Inc. ERISA Litig., 2011 WL 1303367, at *2 (D. Kan. 2011) (noting $6.5 million settlement of stock drop claim); Taylor v. ANB Bancshares, Inc., 682 F. Supp. 2d 970, 972 (W.D. Ark. 2009) (noting $2 million to resolve ESOP claims arising from unsafe and unsound business practices); *In re* MCI/WorldCom, Inc. ERISA Litig., 2004 WL 2338151, at *2-3 (N.D. Cal. 2004) (noting settlement announced in July 2004: $51 million from company and insurers; $4 million from former director and CEO); *In re* Global Crossing Secs. and ERISA Litig., 225 F.R.D. 436, 443 (S.D.N.Y. 2004) (noting $79 million settlement reached in March 2004); *In re Lucent* Techs., Inc. *ERISA Litig., 327 F.Supp.2d 426, 430* (D.N.J. 2003) (noting $69 million settlement reached in late 2003); Kolar v. Rite Aid Corp., 2003 WL 1257272, at *1-2 (E.D. Pa. 2003) (noting settlement estimated at $67.7 million).

12. David K. Randall, *Danger in Your 401(k)*, FORBES, Aug. 30, 2010, at 48.

stock.[13]

There are a large number of ERISA class action lawsuits claiming fiduciary breaches relating to the administration of employee individual account plans ("EIAPs"), typically alleging that fiduciaries should have minimized losses by liquidating the employer stock in the retirement plan to avoid the effects of the bear market. The alleged facts in these cases rely on the drop in value of the employer's stock coupled with allegations regarding the employer's plan design. The expensive litigation involving employer stock lawsuits is ever-growing while the general public thirsts to assign blame for the financial crisis facing the country's retirement plans.

But in actuality, employee retirement savings plan investments in employer stock further a congressional objective of encouraging employee ownership. In furtherance of this public policy, courts examining fiduciary breach claims involving employer stock in retirement savings plans have repeatedly held that plaintiffs must allege a "precipitous decline" in the price of the stock before such suits can go forward. Thus, if no such allegation exists, a suit cannot proceed. Such a burden helps to prevent litigation over normal short-term trends in the fluctuation of the market.

At times, the price of the stock actually fluctuates higher during litigation, and sometimes substantially higher by the time of trial than at the beginning of the class period. The burden to demonstrate a "precipitous decline" filters out the prematurely-panicked plaintiffs with ill-conceived allegations that portray their retirement savings plan investments in stock as the functional equivalent of investments in Enron or WorldCom. In those companies' well-publicized litigations, the courts held that the plan sponsors' imminent financial collapse may be a sufficient reason to require plan fiduciaries to take extraordinary measures to override plan terms and discontinue investments in employer stock.

To rebut allegations of a "precipitous decline," a defendant can focus on factors that show financial stability and profitability, such as paying consistent dividends to shareholders. ERISA is designed to accomplish many worthwhile objectives, but the regulation of "purely corporate behavior is not one of them."[14] ERISA should not be construed to afford plaintiffs a method of

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13. *Id.* (stating that "58% of large-company defined contribution pension plans . . . offer employees a choice of receiving contributions in cash or company stock of equal value," and that aside from offering the stock, certain companies actually have participants' accounts heavily invested in common stock: Coca-Cola 51%; McDonald's 45%; Caterpillar 44%, General Electric 42%).

14. Akers v. Palmer, 71 F.3d 226, 229 (6th Cir. 1995).

challenging purely corporate behavior that has no legally-cognizable impact on a plan, or on the long-term retirement savings investments held therein.

The question that arises is whether the fiduciaries' actions are entitled to a presumption of prudence as set forth in *Moench v. Robertson*.[15] This Article examines the recent cases involving suits for breach of fiduciary duty under ERISA for the continued investment in employer stock. There is no current uniform standard of review and many cases have yet to go to trial. However, given the trend of increasingly substantial litigation costs and the need to review the overall performance of a retirement investment only with a "precipitous decline," clearly the proper standard courts should use to analyze employer stock cases in ERISA litigation is a fiduciary presumption of prudence, as fluctuations in the market will likely always occur.

This Article proposes a uniform standard to apply in the context of employer stock investments in retirement plans. Part II discusses the background of ERISA, the types of retirement plans, and the identity and respective duties of fiduciaries. Part III explains the modern portfolio theory and its shortcomings. Part IV addresses the investment in employer stock in defined contribution plans and the presumption of prudence. Finally, Part V presents the conflicts among the circuit courts and sets forth the correct standard of prudence that the Supreme Court should adopt to have some uniformity in this particular area of ERISA jurisprudence.

II. BACKGROUND - ERISA

Employees' retirement accounts are protected by the statute known as ERISA. Its origins are derived from the Studebaker Co. bankruptcy in December 1963, which left many workers without retirement savings and led to many years of legislative study. Congress passed ERISA in 1974 with the intent of establishing "minimum standards of fiduciary conduct for Trustees, Administrators and others dealing with retirement plans . . . and to improve the equitable character and soundness of private pension plans."[16]

ERISA is a complicated statute to navigate, as the Second Circuit once eloquently stated "[i]n truth, ERISA is a veritable Sargasso Sea of obfuscation."[17] Crucial to an ERISA analysis is the determination of the status of the parties involved. Particularly, fiduciaries must be located and their ERISA-mandated duties

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15. Moench v. Robertson, 62 F.3d 553, 568 (3d Cir. 1995).

16. H.R. REP. NO. 93-533, at 16 (1974), *reprinted in* 1974 U.S.C.C.A.N. 4639, 4655.

17. Travelers Ins. Co. v. Cuomo, 14 F. 3d 708, 717 (2d. Cir. 1993).

must be applied to them. Then the actions performed by these fiduciaries must be analyzed to determine which are "settlor" in nature. As will be discussed later in greater detail, settlor actions are actions individuals partake in their corporate capacity, and not fiduciary capacity. Acting in a settlor capacity is a defense to liability.

A. *Defined Contribution Plans*

Pension plans[18] are plans or arrangements that, by their terms or operations, either provide for retirement income or defer income until the termination of employment or beyond. Pension plans that are Code-qualified are funded and generally have an established accompanying trust.

There are many types of pension plans. The traditional plan, also known as a "defined benefit plan," is a pension plan that provides a definite formula with which the amount of a participant's pension benefit is determined. In a defined benefit plan, the employer bears the investment risk, as its contributions are actuarially determined each year based on the benefit formula and factors such as the compensation, age, and service of participants, as well as the fund's investment performance.

More popular today and more important to the issue of investments in employer stock are plans known as "defined contribution plans" ("DC Plans"). These pension plans provide an individual account for each participant, whereby a participant's benefit is determined by the value of his or her account. Thus, the participant bears the investment risk. Each participant's account is based on the amount of contributions allocated to the account plus any income, expense, and investment gain or loss credited to or charged against the account. Money purchase, profit sharing, stock bonus, 401(k), and employee stock ownership plans ("ESOPs") are all forms of DC Plans. Defined as eligible individual account plans, they are statutorily termed as follows: "(i) a profit-sharing, stock bonus, thrift, or savings plan, or (ii) an employee stock ownership plan," which "explicitly provides for acquisition and holding of qualifying employer securities."[19] "Qualifying employer securities" are stock issued by an employer of employees covered by the plan.[20]

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18. In general, qualified plans enjoy certain tax advantages under the Internal Revenue Code (the "Code") including (a) from the company's perspective, immediate tax deductions for employer contributions to the plan; (b) from the employees' perspective, tax deferral on such contributions and the earnings on such contributions; and (c) from the perspective of the trust holding the contributions, tax exemption on the earnings. I.R.C. § 401(a)(28)(A) (2012).

19. 29 U.S.C. §§ 1107(d)(3)(A)-(B).

20. 29 U.S.C. §§ 1107(d)(5)(A) and (d)(1).

A special type of EIAP designed to serve as an employer stock bonus plan is known as an Employee Stock Ownership Plan.[21] ESOPs are intended to reward and motivate employees by making them stakeholders in the success of the company that employs them, typically through stock-matching contributions. By linking employee compensation to the actual performance of the company, productivity and general worker utility is generally perceived as enhanced.[22] ESOPs mandatorily include employer stock as an option in a retirement investment portfolio.

To qualify as an ESOP, the plan must be "designed to invest primarily in employer stock."[23] This requirement has not yet been interpreted by the IRS or the courts. The phrase implies that in order for the plan, or a portion thereof, to qualify as an ESOP, it must invest or hold the major portion of its plan assets in employer securities. However, there are no bright line quantitative tests to apply.[24]

Plans named in the employer stock drop cases typically involve individual account plans under ERISA section 3(34),[25]

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21. 29 U.S.C. § 1107(d)(6).

22. Donovan v. Cunningham, 716 F.2d 1455, 1458 (5th Cir. 1983) (explaining that ESOPs are employee benefit plans in which the employees invest in securities issued by the employer).

23. DOL Advisory Opinion, No. 83-6 (Jan. 24, 1983) (declining to establish a fixed, quantitative standard for the "primarily invested" requirement, but emphasizing that the applicable requirements are flexible and vary according to the facts and circumstances of each case).

24. *Id.* Furthermore, in terms of diversification, the Tax Reform Act of 1986 amended the Code to permit participants who have attained at least age fifty five with at least ten years of plan participation to elect to "diversify" their ESOP account in non-employer securities. Under Code section 401(a)(28)(A), each such "qualified participant" must be given the opportunity to direct the plan as to the investment of at least twenty five percent of his or her employer stock account for five years and on the sixth year the participant must be provided with the option to direct at least fifty percent of his or her employer stock account. I.R.C. § 401(a)(28)(A) (2012). This requirement is met if the qualified participant is able to elect to have the portion of his or her account subject to the diversification election either be distributed to him or her or be invested among at least three investment options other than employer securities. *Id.*

While it is clear that the statutorily mandated age fifty five and ten years of participation diversification election can be broadened to a degree without a plan failing to continue to qualify as an ESOP, it is unclear how far such diversification election can be extended. Arguably as long as a plan is "designed" to primarily invest in employer securities at least initially, subsequent participant diversification elections are irrelevant if at least more than half of the ESOP portion remains invested in employer stock. However, we cannot predict the extent of participant elections nor whether the IRS would view the proposed unrestricted diversification provision which provides for momentary investment in employer stock as being mere form over substance inconsistent with the "designed to primarily invest in employer securities" requirement.

25. ERISA section 3(34) defines an "individual account plan" as "a pension

which are often described as defined contribution plans. As the name suggests, investments in such plans are given preferential treatment under Code section 401(k). Moreover, these plans are designed to encourage employees to save for their retirement and "other long-term goals." Generally, these plans permit employees to defer a percentage of their salary on a pre-tax basis. Some plans also provide employer-matching contributions for up to 6 percent of a participant's compensation from the employer. In addition, sometimes the plan sponsor may make additional discretionary contributions to participants' accounts. But unlike traditional defined benefit pension plans, participants bear the investment risk in defined contribution savings plans.[26]

Participants may invest their contributions and their plan sponsor's matching and additional contributions in several different places, including in the plan sponsor's employer stock fund ("Stock Fund").[27] Certain plans allow up to one hundred percent of its assets to be invested in the Stock Fund. In accordance with ERISA, participants are given detailed information about each investment option and they alone decide how to invest their retirement money. Sometimes there are restrictions on the participants' ability to transfer their money in and out of a Stock Fund. Moreover, some plans require its fiduciaries to invest in a Stock Fund only upon the participants' direction.

In the aftermath of the Enron debacle, Congress attempted to prevent the losses that occurred in retirement plans by passing the

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plan which provides for an individual account for each participant and for benefits based solely upon the amount contributed to the participant's account, and any income, expenses, gains and losses." 29 U.S.C. § 1002(34) (2008).

26. *See* Bash v. Firstmark Std. Life Ins. Co., 861 F.2d 159, 163 (7th Cir. 1988) (asserting that to impose liability upon plan fiduciaries for account losses in a defined contribution/individual account plan would give participants "the best of both worlds" resulting in "an inequity of the heads I win, tails you lose variety that neither the ERISA statute nor the . . . plan documents perpetrate"); *see also* Wright v. Oregon Metallurgical Corp., 360 F.3d 1090, 1097 n.2 (9th Cir. 2004) ("Unlike traditional pension plans governed by ERISA, EIAPs . . . are not intended to guarantee retirement benefits and indeed, by their very nature, 'place employee retirement assets at much greater risk than does the typical diversified ERISA plan.'") (quoting Martin v. Feilen, 965 F.2d 660, 664 (8th Cir. 1992)); *In re* Unisys Sav. Plan Litig., 1997 WL 732473, at *25 n.30 (E.D. Pa. Nov. 24, 1997) (noting that the participants in a defined contribution plan, not the employer, assume the risk of loss for their investments); D. Fischel & J. H. Langbein, *ERISA's Fundamental Contradiction: The Exclusive Benefit Rule*, 55 U. CHI. L. REV. 1105, 1112-13 (1988) ("Defined contribution and defined benefit plans allocate investment risk oppositely. Under a defined contribution plan, the employee bears the burden of disappointing results and pockets the gains from good results.").

27. Pension Protection Act of 2006, Pub. L. No. 109-280, 120 Stat. 780 (2006).

Pension Protection Act of 2006 ("PPA").[28] The PPA mandates that contribution plans offering publicly traded employer stock allow participants and beneficiaries to divest themselves of employer stock either immediately, with respect to employee contributions, or after three years, with respect to employer contributions.[29] Furthermore, under PPA regulations, there is a 10 percent cap on investment in employer stock.[30] However, this attempted congressional fix has not been able to lessen the number of employer-stock lawsuits that have been filed.

B. Elements of an ERISA Breach of Fiduciary Duty Claim

"[I]n every case charging breach of ERISA fiduciary duty, . . . the threshold question is not whether the actions of some person employed to provide services under a plan adversely affected a plan beneficiary's interest, but whether that person was acting as a fiduciary (that is, was performing a fiduciary function) when taking the action subject to complaint."[31] Before determining whether there has been a breach of a duty, an actual duty as a fiduciary must be established. Sometimes the question as to who is a fiduciary is not clear. For example, it has been held that an officer acting on behalf of a corporate fiduciary is not a fiduciary unless it can be shown that the officer has individual discretion regarding plan administration.[32] On the other hand, some courts have held that, to the extent a person performs a fiduciary function on behalf of a corporate fiduciary, that person is a fiduciary.[33]

Section 409(a) of ERISA specifically provides for liability of individual fiduciaries that breach their duties:

> Any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this subchapter shall be personally liable to make good to such plan any losses to the plan resulting from each such breach, and to restore to such plan many profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, and shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary.[34]

Thus, under ERISA sections 404 and 409, to plead a breach of

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28. *Id.*
29. *Id.* at §§ 901(a) and (b).
30. *Id.* at § 1.401.
31. Pegram v. Herdrich, 530 U.S. 211, 226 (2000).
32. Confer v. Custom Eng'g Co., 952 F.2d 34, 36 (3d Cir. 1991).
33. Kayes v. Pac. Lumber Co., 51 F.3d 1449, 1460 (9th Cir. 1995); Musmeci v. Schwegmann Giant Supermarkets, Inc., 332 F.3d 339, 351 (5th Cir. 2003).
34. 29 U.S.C. § 1109(a).

fiduciary duty, a plaintiff must allege that (1) the defendants are plan fiduciaries; (2) the defendants breached their fiduciary duties; and (3) the breach caused harm to the plaintiff.[35]

1. *Standing*

To have standing to sue under ERISA, a plaintiff must be "a participant, beneficiary, or fiduciary" of a plan.[36] A "participant" is defined as "any employee or former employee of an employer . . . who is or may become eligible to receive a benefit of any type from an employee benefit plan which covers employees of such employer."[37] In order to establish that he or she is eligible or may become eligible for benefits, a claimant must have a colorable claim that (1) he or she will prevail in a suit for benefits, or that (2) eligibility requirements will be fulfilled in the future.[38] Applying these provisions and principles, some courts have found that class members who were former participants in a plan lack standing.[39] Other courts have held that plaintiffs who were participants in a plan at the time of the alleged breaches do have standing under ERISA.[40] The weight of authority seems to favor finding standing for plaintiffs who were former plan participants.

ERISA sections 502(a)(2) and 502(a)(3) provide that plan participants may seek relief on behalf of the plan as a whole and may seek equitable relief as to fiduciaries.[41] Therefore, in some ERISA cases, defendants have sought to dismiss participants' claims for lack of standing, arguing that what plaintiffs in these cases truly seek is monetary relief for plan participants in their individual capacity.[42] However, the Supreme Court has ruled that former participants may bring suit under ERISA 502(a)(2) to

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35. Jenkins v. Yager, 444 F.3d 916, 924 (7th Cir. 2006).

36. 29 U.S.C. § 1132(a).

37. 29 U.S.C. § 1002(7).

38. Firestone Tire & Rubber Co. v. Bruch, 480 U.S. 101, 117-18 (1989).

39. *See, e.g.*, Renton v. Kaiser Found. Health Plan, Inc., 2001 WL 1218773, at *5 (W.D. Wash. 2001) ("Under the plain language of ERISA's civil enforcement provisions, class members who are former, but not current participants in a . . . plan lack standing to bring the claims alleged in the complaint.").

40. *See, e.g., Rots*, 220 F.R.D. at 519-20 (E.D. Mich. 2004) ("Rankin was a participant in the Kmart plan during the time when the alleged breaches of fiduciary duty occurred. She was paid her vested benefit when the Kmart store she was employed at closed. To find that she lacks standing would permit Kmart to exclude potential class members by simply paying them their vested benefits. ERISA should not be interpreted to circumvent a plaintiff's recovery in this manner."); Vartanian v. Monsanto, 14 F.3d 697, 702 (1st Cir. 1994) (finding that ERISA's legislative history indicated that the Plaintiff did have standing).

41. 29 U.S.C. § 1132 (2008).

42. *See, e.g., In re* AEP ERISA Litig., 327 F.Supp.2d 812, 818 (S.D. Ohio 2004) (refusing to dismiss plaintiffs' claims for lack of standing).

redress harm to an individual participant's account.[43]

2. *The ERISA Fiduciaries*

a. ERISA-Defined Fiduciary

Congress intended retirement plans to be safeguarded by fiduciaries, and defined "fiduciary" under ERISA as follows:

> [A] person is a fiduciary with respect to a plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan.[44]

Thus, "[f]iduciary status is not an all or nothing concept . . . . [A] court must ask whether a person is a fiduciary with respect to the particular activity in question."[45]

b. De Facto Fiduciary

ERISA requires that every benefit plan document designate a "named fiduciary" who has the authority to control and manage the operations of the plan.[46] A "named fiduciary" is defined as:

> [A] fiduciary who is named in the plan instrument, or who, pursuant to a procedure specified in the plan, is identified as a fiduciary (A) by a person who is an employer or employee organization with respect to the plan or (B) by such an employer and such an employee organization acting jointly.[47]

In the first instance, it is the named fiduciary who has fiduciary responsibility to the plan. However, others acting in a fiduciary capacity to the plan may also be fiduciaries under ERISA, regardless of the named fiduciary designation.

The Supreme Court has held that fiduciary status is based on a functional test that focuses on a person's actions or authority,

43. LaRue v. DeWolff, Boberg & Assocs., Inc., 552 U.S. 248, 266 (2008).

44. 29 U.S.C. § 1002(21)(A) (2008); *see also* Beddall v. State St. Bank and Trust Co., 137 F.3d 12, 18 (1st Cir. 1998) (discussing the factors a court relies on to determine the existence of a fiduciary relationship); Kling v. Fidelity Mgmt. Trust Co., 323 F. Supp. 2d 132, 139 (D. Mass. 2004) (hereinafter *Kling III*) (discussing the application of the definition of a fiduciary provided in 18 U.S.C § 1002(21)(A) with respect to a particular activity).

45. Maniance v. Commerce Bank of Kansas City, 40 F.3d 264, 267 (8th Cir. 1994).

46. 29 U.S.C. § 1102(a)(1).

47. *Id.* at (a)(2).

not on his or her formal designation.[48] Therefore, under ERISA, anyone – irrespective of the person's formal title or designation – may become a fiduciary if he or she exercises or has any discretionary authority or control over plan administration or assets. Integral to ERISA fiduciary status is the level of "discretion" exercised over the plan as it relates to the investment and disposition of the plan assets.[49] Importantly, a person may qualify as an ERISA fiduciary with regard to discretion over certain matters, but not others.[50] An individual's specific function in overseeing plan assets is the determinative factor in the threshold fiduciary analysis, particularly as it relates to the control, disposition, and administration of plan assets.[51]

Lawsuits claiming breaches of fiduciary duty must first prove, as a threshold matter, that the defendant was acting in a fiduciary manner "when taking the action subject to complaint."[52] If not, ERISA fiduciary obligations are inapplicable and the individual is considered merely a settlor under the statute. The U.S. Department of Labor ("DOL") has clarified that settlor activities are traditionally related to the establishment, design, amendment, and termination of plans, rather than functional discretionary control over them as a going concern.[53]

Furthermore, this exercise of discretionary authority or control is to be contrasted with a person who "performs purely ministerial functions for an employee benefit plan within a framework of rules and procedures made by other persons." Such a person is "not a fiduciary because he does not have discretionary authority regarding administration of the plan or management of the plan assets."[54] Because of this functional test, the determination of one's fiduciary status is fact intensive.[55]

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48. Mertens v. Hewitt Assocs., 508 U.S. 248, 262 (1993).

49. *In re* Citigroup ERISA Litig., 662 F.3d 128, 140 (2d Cir. 2011).

50. *Id.*

51. Hecker v. Deere & Co., 556 F.3d 575, 583 (7th Cir. 2009).

52. Harris Trust & Sav. Bank v. John Hancock Mut. Life Ins. Co., 302 F.3d 18, 28 (2d Cir. 2002).

53. Field Assistance Bulletin 2002-2, Memorandum From Robert J. Doyle, Dir. Of Regulations and Interpretations, U.S. Dept. of Labor, to Virginia C. Smith, Dir. of Enforcement, Regional Directors, U.S. Dept. of Labor (Nov. 4, 2002) *available at* http://www.dol.gov/ebsa/regs/fab_2002-2.html.

54. Kuper v. Quantum Chem. Corp., 838 F. Supp. 342, 347 (S.D. Ohio 1993) (citing Flacche v. Sun Life Assurance Co. of Canada, 958 F.2d 730, 734 (6th Cir. 1992)).

55. Bell v. Exec. Comm. of the United Food & Commercial Workers Pension Plan for Emps., 191 F. Supp. 2d 10, 15 (D.D.C. 2000); *see also In re* Fruehauf Trailer Corp., 250 B.R. 168, 204-05 (D. Del. 2000) (noting that merely alleging a fiduciary relationship would be insufficient under Fed. R. of Civ. P. 12(b)(6)); Penn. Fed'n v. Norfolk S. Corp., 2004 WL 228685, at *11 (E.D. Pa. 2004) ("Determining a party's fiduciary status under ERISA is a highly fact intensive inquiry that cannot be properly decided on a motion to

Even so, the Supreme Court has held that fiduciary status is to be "construed liberally."[56] A person need not have exclusive or final decision-making authority to be a fiduciary – he or she only has to have some discretionary authority or control.[57] Some courts, using a literal reading of the statute, have determined that to the extent one exercises any control over the assets of a plan, it is not necessary that such exercise be "discretionary."[58]

The power to appoint/remove plan fiduciaries is itself a fiduciary function.[59] Thus, if one's fiduciary function is to appoint plan administrators or other plan fiduciaries, he or she will generally be found to have a duty to monitor such appointees under ERISA.[60]

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dismiss."); LaLonde v. Textron, Inc., 270 F. Supp. 2d 272, 285 (D.R.I. 2003), *aff'd in part and vacated in part*, 369 F.3d 1 (1st Cir. 2004) (refusing to rule on the fiduciary status of defendants on motion to dismiss because it was too fact specific of an inquiry).

56. *Mertens*, 508 U.S. at 262; John Hancock Mut. Life Ins. v. Harris Trust & Sav. Bank, 510 U.S. 86, 96 (1993); *see also* Am. Fed. of Unions Local 102 Health & Welfare Fund v. Equitable Life Assurance Soc'y, 841 F.2d 658, 662 (5th Cir. 1988) (giving the term "fiduciary" a liberal construction).

57. *Firestone*, 489 U.S. at 113 (1989) (noting that ERISA "does not characterize a fiduciary as one who exercises entirely discretionary authority or control. Rather, one is a fiduciary to the extent he exercises any discretionary authority or control.").

58. *See In re* Enron Corp. Secs., Derivative & ERISA Litig., 284 F. Supp. 2d 511, 544-45 (S.D. Tex. 2003) (describing the cases that have made the distinction between discretionary control over the administration of the plan and any control over the assets of the plan).

59. Keach v. U.S. Trust Co., N.A., 313 F. Supp. 2d 818, 864 (C.D. Ill. 2004); Coyne & Delany Co. v. Selman, 98 F.3d 1457, 1465 (4th Cir. 1996) ("[T]he power . . . to appoint, retain and remove plan fiduciaries constitutes 'discretionary authority' over the management or administration of a plan. . ."); Hickman v. Tosco Corp., 840 F.2d 564, 566 (8th Cir. 1988); Mehling v. N.Y. Life Ins. Co., 163 F. Supp. 2d 502, 509-10 (E.D. Pa. 2001); Newton v. Van Otterloo, 756 F.Supp. 1121, 1132 (N.D. Ind. 1989); Liss v. Smith, 991 F.Supp. 278, 310-311 (S.D.N.Y. 1998) ("It is by now well-established that the power to appoint plan trustees confers fiduciary status.").

60. Martin v. Feilen, 965 F.2d 660, 669-70 (8th Cir. 1992) (stating that corporate directors' power to appoint an ESOP trustee includes a duty to monitor the trustee); *Enron*, 284 F. Supp. 2d at 511; *Elec. Data Sys.*, 305 F. Supp. 2d at 671 ("Although the Court accepts the duty to monitor's existence, the Court makes no holding regarding the duty's scope. . . . The Court simply holds that some duty to monitor does exist and that Plaintiffs have sufficiently pled a possible cause of action sufficient to allow them access to discovery."); *Sears*, 2004 WL 407007, at * 7 ("Under ERISA guidelines, a fiduciary who delegates responsibility or appoints other fiduciaries has a duty to monitor those delegates."); *In re* Xcel Energy, 312 F. Supp. 2d 1165, 1176 (D. Minn. 2004) ("Implicit in the fiduciary duties attaching to persons empowered to appoint and remove plan fiduciaries is the duty to monitor appointees."). *But see* Beauchem v. Rockford Prods., 2003 WL 1562561, at *2 (N.D. Ill. 2004) (holding that appointment power did not necessarily require duty to monitor); *Williams Cos.*, 271 F. Supp. 2d at 1339 (maintaining that a board's fiduciary responsibility is limited to the appointment act itself); *Corning*, 234 F. Supp.

c. Limitation of Fiduciary Status: Defining "Settlor"

A person is generally a fiduciary only with respect to those aspects of the plan over which he or she exercises discretionary authority and control.[61] An individual who only has discretionary authority or control to appoint plan administrators will only be a fiduciary with respect to those actions.[62] Moreover, directors whose only fiduciary authority is to appoint plan administrators may not be liable for the actions of the fiduciary it appoints.[63]

ERISA's reach is narrow: the statute regulates only the administration of benefits plans, and participants cannot invoke the statute's fiduciary standards to challenge activities related to the running of the business.[64] Although individuals may serve as a fiduciary while in the plan sponsor's employ, only their fiduciary conduct can be challenged under ERISA. This principle, known as the "two hats" doctrine, means that when individuals act in a

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2d at 229 (W.D.N.Y. 2002) (same).

61. 29 C.F.R. § 2509.75-8 (determining that liability of fiduciaries is limited to particular fiduciary functions performed); *Beddall*, 137 F.3d at 18 ("Fiduciary status is not an all or nothing proposition."); Drug Stores Co. Emp. Profit Sharing Trust v. Corrigan, 883 F.2d 345, 352 (5th Cir. 1989); Bannistor v. Ullman, 287 F.3d 394, 401 (5th Cir. 2002).

62. *Williams Cos.*, 271 F. Supp. 2d at 1339; *Corning*, 234 F. Supp. 2d at 229 (dismissing board members because the "only power the Board had under the plan was to appoint, retain or remove members of the Committee;" the board could not be liable for fiduciary breaches with respect to alleged investment-related breaches); *Sprint*, 2004 WL 1179371, at *17; *In re* WorldCom, Inc. ERISA Litig., 283 F. Supp. 2d 745, 760-61 (S.D.N.Y. 2003); Batchelor v. Oak Hill Med. Grp., 870 F.2d 1446, 1449 (9th Cir. 1989) (stating that physicians operating clinics could only be subject to ERISA fiduciary duties concerning selection and retention of plan administrators); Leigh v. Engle, 727 F.2d 113, 133-35 (7th Cir. 1984) (asserting that parties with power to select and retain plan administrators were fiduciaries for the purpose of making such selections); Indep. Ass'n of Publishers Emps., Inc. v. Dow Jones & Co., 671 F. Supp. 1365, 1367 (S.D.N.Y. 1987) (stating that an employer, who retained power to appoint, renew, or remove members of advisory committee, had fiduciary duties under ERISA only with respect to such acts); *cf.* Chicago Bd. Option Exch. Inc., v. Conn. Gen. Life Ins. Co., 713 F.2d 254, 259 (7th Cir. 1983) (determining that a company with power to amend annuity contract was fiduciary only with regard to amending that contract).

63. *Kuper*, 838 F. Supp. at 347 (granting summary judgment and dismissing board members because their fiduciary duties were limited to the board's "appoint and remove" powers and because there was no showing that the board influenced the investment decisions of the committee it appointed or knew of any wrongdoing by the committee) *aff'd sub nom.*, Kuper v. Iovenko, 66 F.3d 1447 (6th Cir. 1995).

64. Husvar v. Rapoport, 337 F.3d 603, 609 (6th Cir. 2003) (finding that defendants' mismanagement of the company so as to result in a dramatic decrease in the value of the [employer's] stock," which "happened to devalue the ESOP funded with such stock," did not state ERISA claims because "[a] claim that the company directors did not operate the business itself in conformity with sound business practices does not . . . implicate the protections afforded by ERISA.").

corporate capacity, ERISA's fiduciary rules do not apply to their actions even if they also serve as ERISA fiduciaries.[65] Therefore, to state a claim for breach of fiduciary duty, plaintiffs must allege that each defendant acted as a fiduciary when they purportedly misrepresented or withheld material information to participants.[66]

Under the "two hats" doctrine, an individual, such as a corporate director, may function in both fiduciary and corporate/non-fiduciary capacities, but not at the same time.[67] When acting in a fiduciary capacity, the fiduciary must act exclusively for the benefit of plan participants. Yet, employers have significant leeway to adjust the plan without incurring fiduciary duties.[68] Thus, it becomes difficult for a plaintiff to show a link between a defendant's discretionary control and the breach causing the plaintiff's harm.

The "two hats" doctrine has also been defined as follows:

> [W]here an administrator of a plan decides matters required in plan administration or involving obligations imposed upon the administrator by the plan, the fiduciary duties imposed by ERISA attach. Where, however, employees conduct business and make business decisions not regulated by ERISA, no fiduciary duties apply. And, when employers wear "two hats" as employers and as administrators . . . they assume fiduciary status "only when and to the extent" that they function in their capacity as plan administrators, not when they conduct business that is not regulated by ERISA.[69]

Furthermore when those with "two hats" make a decision concerning the design of a plan, this decision is not subject to ERISA's fiduciary duties, but the decision makers will be subject to such duties when the decision concerns the plan's

65. *Pegram*, 530 U.S. at 225-26; 29 U.S.C. § 1002(21)(A) (2008) (stating that ERISA Section 3(21)(A) provides that a person is a fiduciary "only 'to the extent' the [person] acts in such a capacity in relation to a plan."); Amato v. Western Union Int'l, 773 F.2d 1402, 1416-17 (2d Cir. 1985) ("ERISA permits employers to wear 'two hats,' and . . . they assume fiduciary status 'only when and to the extent' that they function in their capacity as plan administrators, not when they conduct business that is not regulated by ERISA.").

66. 29 U.S.C. § 1002(21)(A) (2008) (stating that section 3(34) of ERISA provides that "a person is a fiduciary with respect to the plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets"); Sasso v. Cervoni, 985 F.2d 49, 50 (2d Cir. 1993) ("[A]n individual cannot be liable as an ERISA fiduciary solely by virtue of her position as a corporate officer, shareholder or manager.").

67. Varity Corp. v. Howe, 516 U.S. 489, 506-07 (1996); Siskind v. Sperry Ret. Prog., 47 F.3d 498, 505 (2d Cir. 1995); *Akers*, 71 F.3d at 230.

68. *Sasso*, 985 F.2d at 50.

69. Payonk v. HMW Indus., Inc., 883 F.2d 221, 225 (3d Cir. 1989).

administration.[70] The Third Circuit has applied an expansive conception of "design," so that many plan-related decisions simply do not implicate ERISA fiduciary duties.[71] Thus, employers have the power to amend, merge, or even terminate plans entirely without triggering such duties.[72]

Some cases require that fiduciaries have discretionary control. For example, the First Circuit has stated that:

> The key determinant of whether a person qualifies as a functional fiduciary is whether that person exercises discretionary authority in respect to, or meaningful control over, an ERISA plan, its administration, or its assets. . . . We make two points that inform the application of this rule. First, the mere exercise or physical control or the performance of mechanical administrative tasks generally is insufficient to confer fiduciary status. Second, fiduciary status is not an all or nothing proposition; the statutory language indicates that a person is a plan fiduciary only "to the extent" that he possesses or exercises the requisite discretion and control. Because one's fiduciary responsibility under ERISA is directly and solely attributable to his possession or exercise of discretionary authority, fiduciary liability arises in specific increments correlated to the vesting or performance of particular fiduciary functions in service of the plan, not in broad, general terms.[73]

A Massachusetts case emphasizes that, to maintain a cause of action for a breach of fiduciary duty, the plaintiff "must plead first that the defendant was a fiduciary with respect to [the relevant plan] and that he or she breached a duty to that Plan that related to matters within his or her discretion or control."[74]

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70. *See, e.g.*, Hlinka v. Bethlehem Steel Corp., 863 F.2d 279, 282-285 (3d Cir. 1989) ("ERISA is not a direction to employers as to what benefits to grant their employees. Rather, ERISA is concerned with the administration of an established plan and its elements. . . . The design of this plan was unquestionably not violative of ERISA because [the employer] in drafting the plan was acting as an employer and not a fiduciary."); *see also* Nazay v. Miller, 949 F.3d 1323, 1329-31 (3d Cir. 1991) (asserting that employers occupy, under certain circumstances, two hats under ERISA's mandates).

71. Walling v. Brady, 125 F.3d 114, 119-20 (3d Cir. 1997).

72. *See, e.g.*, *id.* (noting that "amending, altering, terminating, or otherwise redesigning the plan itself" are functions considered "not fiduciary"); *see also* Jackson v. Truck Drivers' Union Local 42 Health & Welfare Fund, 933 F. Supp. 1124, 1142-43 (D. Mass. 1996) (citing Curtis-Wright Corp. v. Schoonejongen, 514 U.S. 73, 78 (1995), and referring to Am. Flint Glass Workers Union v. Beaumont Glass Co., 62 F.3d 574, 579 (3d Cir. 1995) (concerning pension plan)) ("'Employers or other plan sponsors are generally free under ERISA, for any reason at any time, to adopt, modify, or terminate welfare plans'").

73. *Beddall*, 137 F.3d at 18.

74. Stein v. Smith, 270 F. Supp. 2d 157, 166 (D. Mass. 2003); *see also Kling III*, 291 F. Supp. 2d at 3 (D. Mass. 2003) (asserting that "discretion is the *sine qua non* of fiduciary duty").

However, some courts have determined that while discretionary control over management or plan administration is needed to make one a fiduciary, any sort of control over a plan's assets is sufficient. This difference springs from the ERISA definition of "fiduciary," which states that one is a fiduciary to the extent that one "exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets," or "has any discretionary authority or discretionary responsibility in the administration of such plan."[75]

On numerous occasions, the Supreme Court has held that an employer acts as a plan settlor, and not a fiduciary. Examples of settlor functions include establishing, designing, amending, or terminating an ERISA plan.[76]

The Seventh Circuit has also acknowledged that an employer may design a pension plan with features of its choosing.[77] More recently, that court has emphasized the definition of a settlor by stating that inclusion of particular "investment vehicles in [a] plan . . . bears more resemblance to the basic structuring of a plan than to its day-to-day management . . . . We therefore question whether [the company's] decision to [designate particular investments] . . . is even a decision within [the company's] fiduciary responsibilities."[78]

d. Directors and Officers as Fiduciaries

Directors and officers ("D & Os") have been held to be ERISA fiduciaries, to the extent that they have or exercise discretionary authority or control over the administration or assets of a plan.[79] Typically, D & Os only have the authority to appoint and remove others who perform the administrative functions of the plan. In such cases, D & Os can be ERISA fiduciaries with respect to such appointments.[80]

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75. 29 U.S.C. § 1002(21)(A)(i) and (iii) (2008).

76. *See, e.g.*, Hughes Aircraft Co. v. Jacobson, 525 U.S. 432, 444 (1999) (noting that activities related to the formation and design rather than management of the plans are settlor functions); Lockheed Corp. v. Spink, 517 U.S. 882, 890 (1996)(same); *Curtiss-Wright Corp.*, 514 U.S. at 78 (same); *Pegram*, 530 U.S. at 226 (same); Beck v. PACE, Int'l Union, 551 U.S. 96, 102-110 (2007) (same).

77. *See* McNab v. Gen. Motors Corp., 162 F.3d 959, 961 (7th Cir. 1998) (concluding that the employer is free to choose the features of its plan so long as those choices are not arbitrary or capricious).

78. Hecker v. Deere & Co., 556 F.3d 575, 586 (7th Cir. 2009), *pet. for reh'g and reh'g en banc denied*, 569 F.3d 708 (7th Cir. 2009) and *cert. denied*, 130 S. Ct. 1141 (2010).

79. *Beddall*, 137 F.3d at 18.

80. Leigh v. Engle, 727 F.2d 113, 133-34 (7th Cir. 1984); *Corning*, 234 F. Supp. 2d at 229; Beam v. HSBC Bank USA, 2003 WL 22087589, at *2-3 (W.D.N.Y. 2003); *Enron*, 284 F. Supp. 2d at 511; *Rankin*, 278 F. Supp. 2d at

A regulation from the Department of Labor also provides that D & Os are ERISA fiduciaries to the extent that they have responsibility for the selection and retention of other plan fiduciaries.[81] With respect to directors, this regulation states:

> Members of the board of directors of an employer which maintains an employee benefit plan will be fiduciaries only to the extent that they have responsibility for the functions described in section 3(21)(A) of the Act. For example, the board of directors may be responsible for the selection and retention of plan fiduciaries. In such a case, members of the board of directors exercise "discretionary authority or discretionary control respecting management of such plan" and are, therefore, fiduciaries with respect to the plan. However, their responsibility, and, consequently, their liability, is limited to the selection and retention of fiduciaries (apart from co-fiduciary liability arising under circumstances described in section 405(a) of the Act). In addition, if the directors are made named fiduciaries of the plan, their liability may be limited pursuant to a procedure provided for in the plan instrument for the allocation of fiduciary responsibilities among named fiduciaries or for the designation of persons other than named fiduciaries to carry out fiduciary responsibilities, as provided in section 405(c)(2). The Internal Revenue Service notes that it would reach the same answer to this question under section 4975(e)(3) of the Internal Revenue Code of 1954.[82]

Certain courts have held that D & Os are not ERISA fiduciaries in the absence of express individual authority for plan administration:

> [W]hen an ERISA plan names a corporation as fiduciary within the meaning of section 3(21)(A)(iii), the officers who exercise discretion on behalf of that corporation are not fiduciaries within the meaning of section 3(21)(A)(iii), unless it can be shown that these officers have individual discretionary roles as to plan administration. For example, if the plan designates an officer as plan administrator or if, pursuant to 29 U.S.C. § 105(c)(1)(B), the corporation delegates some of its fiduciary responsibilities to an officer, then the designated individual would be a fiduciary under Section 3(21)(A)(iii).[83]

In *Confer v. Custom Engineering Company*, the plan document named the corporation, rather than an individual or committee, as the named fiduciary of the plan. D & Os have

857; *Stein*, 270 F. Supp. 2d at 162; *Keach*, 313 F. Supp. 2d at 864; *Sears*, 2004 WL 407007, at *3; *Williams Cos.*, 271 F. Supp. 2d at 1328.

81. 29 C.F.R. 2509.75-8 (2008).

82. *Id.*

83. *Confer*, 952 F.2d at 37.

sought to use *Confer* to support the broad proposition that they cannot be fiduciaries under ERISA unless specifically designated to act in such role.[84]

In *Eyler v. Commissioner of Internal Revenue*,[85] an ESOP valuation case, the plan named the company as fiduciary. However, the court determined that the board members were fiduciaries because the company acted through the board. The court did not analyze how, under the *Confer* theory, the board members were given discretionary control over the plan in their individual rather than corporate capacity.[86]

The weight of authority seems to favor a rejection of a bright-line rule shielding D & Os from ERISA fiduciary liability unless they are fiduciaries in a personal, rather than a corporate, capacity. One district court, in *Bell v. Executive Committee of the United Food and Commercial Workers Pension Plan for Employees*,[87] recognized the "widespread disagreement among courts" over the *Confer* reasoning and concluded:

> While the courts have considered this issue in a variety of ways, in all the rulings, in accordance with 29 U.S.C. 1002(21)(A) and *Mertens*, the facts of the case affect whether an individual is found to be a fiduciary under the statute. Under the cases cited by the parties, there is no per se rule against holding an individual employed by the corporate fiduciary as an ERISA fiduciary, but

84. *See Stein*, 270 F. Supp. 2d at 168 (noting that the plan in *Confer* named the corporation as fiduciary whereas the plan in *Stein* named an administrative committee as fiduciary); *Enron*, 284 F. Supp. 2d at 552-53 (same); *Bell*, 191 F. Supp. 2d at 10 (same); *In re* CMS Energy ERISA Litig., 312 F. Supp. 2d 898, 902 (E.D. Mich. 2004). Some courts have agreed with the reasoning of *Confer*. In *Torre v. Federated Mut. Ins. Co.*, 854 F. Supp. 790, 813 (D. Kan. 1994), the court determined that one cannot be a "de facto" plan administrator. The court noted that the individual defendant (who was not a director of the company) had the authority to grant or deny claims for benefits and negotiate settlements of benefit disputes and therefore exercised some discretion over plan administration, but the court determined that he was not an ERISA fiduciary. The court cited *Confer* for the proposition that when the plan names the corporation as a fiduciary, employees of the corporation acting "within the procedural framework established by the corporate fiduciary" are not ERISA fiduciaries. Other courts have rejected *Confer*. *Enron* rejected a per se rule of non-liability for D & Os acting on behalf of the corporation and instead made a functional, fact-specific inquiry to assess "the extent of responsibility and control exercised by the individual with respect to the Plan" to determine if a corporate employee, and thus also the corporation, has exercised sufficient discretionary authority and control to be deemed an ERISA fiduciary and thus personally liable for a fiduciary breach. The *Enron* court described how other courts have rejected an interpretation of *Confer* that could shield D & Os from fiduciary liability under ERISA. *Enron*, 284 F. Supp. 2d at 552-53.

85. Eyler v. Comm'r, 88 F.3d 445, 460 (7th Cir. 2005)

86. *Id.*

87. *Bell*, 191 F. Supp. 2d at 15.

rather it is a factual determination involving an assessment of the extent of responsibility and control exercised by the individual with respect to the Plan. It seems that more likely than not that courts outside *Confer* would reject its rationale and determine that D & Os could be ERISA fiduciaries if they have or exercise discretionary authority or control over the administration or assets of the plan, regardless of whether they are acting in an individual or corporate capacity.[88]

C. ERISA Fiduciary Duties

ERISA fiduciaries are bound by a prudent standard of care inclusive of four intertwining obligations of plan stewardship: exclusive purpose (the duty of loyalty), prudence (the duty of care), the duty to diversify plan assets, and the duty to follow the terms of the plan.[89] Note that, as mentioned previously, there is a qualified exemption from the prudent person standard for "employer securities."[90]

Because of congressional preference for EIAP and ESOP plans, the fiduciary standards governing such plan assets are relaxed. Notably, EIAP fiduciaries are not bound by the duty to diversify. Fiduciaries are not deemed to act imprudently by not diversifying the assets of an EIAP but are still required to act prudently in overseeing the plan assets.[91]

In determining the standard of care required, the Second, Third, Fifth, Sixth, Ninth, and Eleventh Circuit have adopted the *Moench* presumption, derived from the Third Circuit case, *Moench v. Robertson*.[92] This watershed case held that a fiduciary meets his duties by virtue of investing the plan assets in employer stock and, in such cases, the burden shifts to the plaintiff to prove that the fiduciary abused his discretion by investing in employer securities.[93]

1. Exclusive Purpose

ERISA's exclusive purpose rule, a subsection of ERISA section 404(a), 29 U.S.C. § 1104(a),[94] requires that fiduciaries must act for the exclusive purpose of providing plan benefits. This "exclusive

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88. *Id.*
89. 29 U.S.C. § 1104(a) (2008).
90. 29 U.S.C. § 1107(d)(3)(B) (2008).
91. 29 U.S.C. § 1104(a)(2) (2008).
92. *Moench*, 62 F.3d at 568.
93. *Citigroup*, 662 F.3d at 137.
94. ERISA section 404(a)(1)(A) provides, in pertinent part that "a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and . . . for the exclusive purpose of (i) providing benefits to participants and their beneficiaries; and (ii) defraying reasonable expenses of administering the plan." 29 U.S.C. § 1104(a).

benefit" rule embodies the common law duty of loyalty. It limits the use of plan assets (i) to pay plan benefits; and (ii) to pay plan expenses that are reasonable and relate only to plan activities.[95] This rule is expanded by the ERISA bar against "prohibited transactions," which, in substance, codifies a generic list of potential conflict of interest situations.[96]

ERISA expressly recognizes that employees of the plan sponsor may serve as plan fiduciaries.[97] Unlike fiduciaries under the common law of trusts, ERISA fiduciaries are expressly permitted to work for the plan sponsor and as mentioned above, thereby wear "two hats."[98] Under ERISA, a fiduciary's resignation and the appointment of an independent fiduciary is required only when an ERISA fiduciary "cannot ignore its self-interest" in making a fiduciary decision.[99] In other words, courts have mandated resignation or removal of fiduciaries only when particular conflicts arise that are qualitatively different from the types of conflicts inherent when the plan fiduciary is the employer or its employees.[100] As the Western District of New York explained:

> [I]n *Donovan* the officers/trustees of the target company had an additional, significant interest of their own in the context of the outcome of the [takeover attempt that would oust their] corporate control.... Here, in contrast, the conflicting interests the defendants had to face – their interest as corporate officers to keep the company afloat and the interest as fiduciaries to keep the Plan fully funded — were of the nature that is inherent in the officers' assumption of dual capacity.[101]

Similarly, plaintiffs tend to allege that inherent conflicts are present whenever plan sponsor employees serve as fiduciaries to a plan that holds employer stock. Indeed, officers and employees of a company, as well as plan participants who invest in employer stock, almost always benefit when the price of employer stock

95. *Id.*

96. *See* Erschick v. United Mo. Bank of Kan. City, N.A., 948 F.2d 660, 671 (10th Cir. 1991) ("[t]he court will not create a . . . conflict of interest where Congress and precedent have not indicated one.").

97. *See* 29 U.S.C. § 1108(c)(3) ("Nothing in section 1106 of this title shall be construed to prohibit any fiduciary from . . . serving as a fiduciary in addition to being an officer, employee, agent, or other representative of a party in interest.").

98. *See Pegram*, 530 U.S. at 225 ("Under ERISA a fiduciary may have financial interests adverse to beneficiaries.").

99. Crowhurst v. Cal. Inst. of Tech., 1999 WL 1027033, at *17 (C.D. Cal. 1999).

100. *See, e.g.*, Donovan v. Bierwirth, 680 F.2d 263, 268-69 (2d Cir. 1982) (noting that plan trustees increased plan holdings of company stock in response to hostile tender offer).

101. Ches v. Archer, 827 F. Supp. 159, 170 (W.D.N.Y. 1993).

rises. ERISA permits, and indeed encourages, investment in employer stock. Thus, there can be no violation of the exclusive purpose rule where fiduciaries followed the express terms of the plan, and those terms comport with ERISA.[102] As the District of Columbia Circuit held, in affirming dismissal of a similar claim:

> [Plaintiffs] argue that the fiduciaries were subject to a conflict because they sought to continue ownership of U.S. News by its employees. But that interest was not some "outside" concern; rather, by the terms of the Plan, it was an interest that Plan beneficiaries shared, inseparable from their interests in the Plan itself.[103]

While a dual hat is not sufficient to prove a breach of fiduciary duty, many courts have imposed the duty to disclose material information to participants as part of the exclusive purpose rule, but this is a developing and controversial area of the law.[104] Although a fiduciary duty to disclose is not specifically enumerated in the statutory disclosure requirements, many courts find an affirmative duty to disclose material facts to plan participants under the general ERISA fiduciary provisions. Courts

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102. *See WorldCom*, 263 F. Supp. 2d at 768 ("Plaintiffs' allegations that [an alleged fiduciary defendant's] holding of WorldCom stock and participation in its compensation program created a conflict of interest are insufficient by themselves to state a claim under ERISA."); *Wright*, 360 F.3d at 1100 (affirming dismissal of plaintiffs' exclusive purpose claim where defendants "complied with the Plan's lawful terms and were under no legal obligation to deviate from those terms"); McElroy v. Smithkline Beecham Health & Welfare Benefits Trust Plan for U.S. Emps., 340 F.3d 139, 142 (3d Cir. 2003) ("The plan administrator's duty to administer a plan for the sole benefit of its participants is qualified by his obligation to interpret a plan consistent with the documents and instruments governing the plan."); Bennett v. Conrail Matched Sav. Plan Admin. Comm., 168 F.3d 671, 677 (3d Cir. 1999) ("While ERISA provides that a fiduciary must act '(A) for the exclusive purpose of: (i) providing benefits to participants and their beneficiaries;' . . . ERISA does no more than protect the benefits which are due to an employee under a plan.").
Stated somewhat differently, the exclusive purpose rule does not impose a duty on fiduciaries to maximize financial gains for participants in derogation of the terms of a plan. *E.g.*, Collins v. Pension & Inv. Comm., 144 F.3d 1279, 1282 (9th Cir. 1998) (noting that duty to act for the "exclusive purpose" of providing benefits does not "create an exclusive duty to maximize pecuniary benefits" to participants; administrators must "act in accordance with [the] plan document"); Foltz v. U.S. News & World Report, Inc., 865 F.2d 364, 372 (D.C. Cir. 1989) (ruling the plan must be administered according to its terms and not according to whether particular interpretation would provide greater "pecuniary value" to participants; if plan is designed to hold employer stock, fiduciaries may take into account the nonpecuniary benefits afforded by employee-ownership stake in the company); Dzinglski v. Weirton Steel Corp., 875 F.2d 1075, 1078-80 (4th Cir. 1989) (noting that whether fiduciary has acted solely in the interest of the participants and beneficiaries is "not to be judged in a vacuum but under the terms of the plan").

103. *Foltz*, 865 F.2d at 374.

104. *Enron*, 284 F. Supp. 2d at 555.

that have recognized this duty have generally done so based on the fiduciary duty of loyalty set forth in 29 U.S.C. § 1104(a).

The Supreme Court has held that an ERISA fiduciary has a duty not to mislead participants.[105] In *Varity Corporation v. Howe*, the employer/plan sponsor distributed materials and called a meeting where it persuaded employees to transfer voluntarily to a new subsidiary by intentionally misrepresenting that the subsidiary was financially stable and that their employee benefits would be secure.[106]

Other courts have required that a fiduciary who knows certain material facts must affirmatively disclose them to participants.[107] This duty to affirmatively disclose includes the duty to provide all material information.[108] Information is considered "material" if it would induce reasonable reliance on the information by the participant,[109] or if there is a substantial likelihood that it would mislead a reasonable employee in making an adequately informed decision.[110]

2. *Duty of Prudence*

The "prudent man" rule with regard to funds entrusted to a fiduciary is derived from the 1830 case, *Harvard College v. Amory*.[111] Pursuant to *Harvard College*, a trustee's duty consists of:

> . . . conduct[ing] himself faithfully[,] . . . excercis[ing] . . . a sound discretion[,] observ[ing] how men of prudence, discretion and

105. *Varity*, 516 U.S. at 489.

106. *Id.*

107. Glaziers and Glassworkers Union Local 252 Annuity Fund v. Newbridge Secs., 93 F.3d 1171, 1180 (3d Cir. 1996); Bins v. Exxon Co. USA, 189 F.3d 929 (9th Cir. 1999) ("We believe that once an ERISA fiduciary has material information relevant to a plan participant or beneficiary, it must provide that information whether or not it is asked a question."); Ervast v. Flexible Prods. Co., 346 F.3d 1007, 1015 (11th Cir. 2003); Krohn v. Huron Mem'l Hosp., 173 F.3d 542, 550 (6th Cir. 1999); Bixler v. Cent. Penn. Teamsters Health & Welfare Fund, 12 F.3d 1292, 1301 (3d Cir. 1993).

108. Griggs v. E.E. Dupont de Nemours & Co., 237 F.3d 371, 381 (4th Cir. 2001); Schmidt v. Sheet Metal Workers' Nat'l Pension Fund, 128 F.3d 541, 550 (7th Cir. 1997) ("A plan fiduciary may violate its duties . . . either by affirmatively misleading plan participants about the operations of the plan, or by remaining silent in circumstances where silence could be misleading.").

109. *See* Ballone v. Eastman Kodak Co., 109 F.2d 117, 121 (2d Cir. 1997) (finding that the change to an ERISA plan is only one factor in the inquiry).

110. *See* James v. Pirelli Armstrong Tire Corp., 305 F.3d 439, 450 (6th Cir. 2002); *Unisys*, 74 F.3d at 442 (noting that, in the ERISA context, a misrepresentation is material if there is "a substantial likelihood that it would have misled a reasonable participant in making an adequately informed decision about whether to place or maintain monies" in a particular investment option).

111. Harvard Coll. v. Amory, 26 Mass. 446, 461 (1830).

> intelligence manage their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, [and] considering the probable income, as well as the probable safety of the capital to be invested.[112]

Under ERISA, a fiduciary must act with the "care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in like capacity and familiar with such matters would use in the conduct of an enterprise of like character with like aims."[113] Courts have held that "the test of prudence – the Prudent [Person] Rule – is one of conduct . . . not whether his investment succeeded or failed."[114] Thus, the prudence standard considers what a hypothetical prudent fiduciary would do under comparable circumstances.[115] With respect to employee benefit plan investments, courts have interpreted the prudence requirement with the "prudent expert" standard – i.e., the fiduciary must act "as a prudent investment manager under the modern portfolio theory."[116] While no one, including fiduciaries, can predict exactly which investments will out-perform others, prudence requirements may be met by a process that requires investments to be examined for appropriate factors such as the risk of loss, the opportunity for return, diversification, liquidity, current return, and projected return.[117]

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112. *See* BEVIS LONGSTRETH, MODERN INVESTMENT MANAGEMENT AND THE PRUDENT MAN RULE 3 (1986) (discussing the origins of the prudent man rule).

113. 29 U.S.C. § 1104(a)(1)(B) (2008).

114. *See* Smith v. Sydnor, 2000 WL 33687953, at *16 (E.D. Va. 2000) (determining that the Prudent Person Rule analyzes a fiduciary's actions in selecting a particular investment); *Keach*, 419 F.3d at 638 (explaining that ERISA's duty of care obligation "requires prudence, not prescience").

115. Pfeil v. State St. Bank & Trust Co., 671 F.3d 585, 591 (6th Cir. 2012). The ERISA duty of care further includes procedural prudence — a fiduciary's prudent investigation and evaluation of a course of action is just as important as the action taken. *See* Fink v. Nat'l Sav. & Trust Co., 772 F.2d 951, 965 (D.C. Cir. 1985) (determining that "[a] fiduciary's independent investigation of the merits of a particular investment is at the heart of the prudent person standard."); Donovan v. Bierwirth, 538 F. Supp. 463, 470 (E.D.N.Y. 1981) (stating that courts routinely consider a fiduciary's independent investigations when determining whether or not the fiduciary complied with the prudence requirement).

116. *Enron*, 284 F. Supp. 2d at 547.

117. *See* Laborers Nat'l Pension Fund v. N. Trust Quantitative Advisors, Inc., 173 F.3d 313, 317–18 (5th Cir. 1999) (listing the requirements that a fiduciary must comply with in order to satisfy the modern portfolio theory). "[T]he fiduciary must act as though he were a reasonably prudent businessperson with the interests of all the beneficiaries at heart." *Jenkins*, 444 F.3d at 924. However, prudence has its limits. In Rogers v. Baxter Int'l, Inc., 521 F.3d 702, 705–06 (7th Cir. 2008), the plaintiffs alleged that the pension fiduciaries should never have allowed them to invest in Baxter's stock because it was overpriced. However, the Seventh Circuit concluded that "pension fiduciaries [do not] have a duty to outsmart the stock market." *Id.* at

Under the modern portfolio theory, fiduciaries are required to give appropriate consideration to all relevant or material attributes of an investment, as well as the surrounding facts and circumstances.[118] An investment that is reasonably designed as part of an overall plan portfolio to further the purposes and objectives of a plan should not be deemed to be imprudent simply because the investment, standing alone, would have a relatively high degree of risk.[119] In addition, under ERISA investing in employer stock is not considered imprudent without meeting the burden of establishing a "precipitous decline."[120]

However, this does not simply mean that a plan investment should be deemed prudent solely by reason of the aggregate risk and return characteristics of the plan's portfolio.[121] Rather, a fiduciary must give "appropriate consideration" to those facts and circumstances that the fiduciary knows or should know are relevant to the investment involved, including the role the investment plays in the plan's investment portfolio.[122]

3. *Duty for Diversification*

A fiduciary must diversify the investments of the plan "so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so."[123] There are three situations in which the duty to diversify assets is limited: (1) it is clearly prudent not to do so, (2) when ownership of employer stock is a principal purpose of the plan (i.e., the plan is an ESOP), and (3) when participants' direct the investment of their own accounts.[124]

ERISA does not establish actual percentage limits for plan investments.[125] In determining whether assets are diversified, fiduciaries should examine factors such as "(i) the amount of plan assets; (ii) the cash flow needs of the plan; and (iii) the composition of the plan's investment portfolio as a whole."[126] Note that EIAPs

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118. *Laborers Nat'l Pension Fund*, 173 F.3d at 317–18.

119. *See id.* at 316 (determining that an investment was not imprudent simply because when it was viewed in isolation from the portfolio, it resulted in a $4.2 million loss, when the portfolio, considered as a whole, resulted in a $18 million gain).

120. *See* Quan v. Computer Sci. Corp., 623 F.3d 870, 882 (9th Cir. 2010) (outlining the factors that plaintiffs need to prove in order to successfully overcome the presumption that an investment was prudent).

121. *See generally Laborers Nat'l. Pension Fund*, 173 F.3d at 317–18 (providing multiple factors to consider when determining whether an investor acted with appropriate consideration, and thus, was prudent).

122. *Id.*

123. 29 U.S.C. § 1104(a)(1)(C) (2008).

124. *Xcel*, 312 F. Supp. 2d at 1175–76.

125. *Wright*, 360 F.3d at 1094.

126. Howard Pianko, *Elements of ERISA Litigation – Ps, Bs and Other*

are exempt from the diversification requirement.[127]

Congress in enacting ERISA, desired to promote employee ownership.[128] Specifically, ERISA expressly exempts pension plan fiduciaries overseeing company stock plans, like ESOPs or company stock investment options (401(k)), from any duty to diversify such investments.[129] "In the case of an eligible individual account plan [like an ESOP or 401(k)], the diversification requirement . . . and the prudence requirement (only to the extent that it requires diversification) is not violated by acquisition or holding of . . . qualifying employer securities."[130]

In view of this congressional policy choice, most courts have applied a presumption of prudence, first adopted by the Third Circuit in *Moench*.[131] Under the *Moench* presumption, a fiduciary is entitled to a presumption that his decision to invest in the employer's securities was prudent.[132] To defeat the presumption, a plaintiff must show that "owing to circumstances not known to the settlor and not anticipated by him [the making of such investment] would defeat or substantially impair the accomplishment of the purposes of the trust."[133]

4. Duty to Follow the Terms of the Plan

ERISA expressly commands fiduciaries to discharge their duty "in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with [ERISA]."[134] In other words a fiduciary's adherence to an ERISA controlled plan "cannot constitute a breach of its fiduciary duties."[135]

When plan documents require assets to be invested in

Players, 526 PLI/TAX 197, 219 (2002).

127. *Wright*, 360 F.3d at 1094.

128. Chao v. Hall Holding Co., Inc., 285 F.3d 415, 425 (6th Cir. 2002).

129. Peabody v. Davis, 636 F.3d 368, 374 (7th Cir. 2011).

130. 29 U.S.C. § 1104(a)(2)(2008); *see* Steinman v. Hicks, 352 F.3d 1101, 1103 (7th Cir. 2003) ("Congress, believing employees' ownership of their employer's stock a worthy goal, has encouraged the creation of ESOPs both by giving tax breaks and by waiving the duty ordinarily imposed on trustees by modern trust law (including ERISA . . .) to diversify the assets of a pension plan.").

131. *Moench*, 62 F.3d at 571.

132. *Id.*

133. *Id.*

134. 29 U.S.C. § 1104(a)(1)(D).

135. *Harris*, 302 F.3d at 29; *see also Wright*, 360 F.3d at 1100 ("ERISA requires fiduciaries to comply with a plan as written unless it is inconsistent with ERISA."); White v. Sundstrand Corp., 256 F.3d 580, 583 (7th Cir. 2001) ("The employer's fiduciary duty, as plan administrator, is to implement faithfully the provisions of the plan as written."); Sedlack v. Braswell Servs. Grp., 134 F.3d 219, 225 (4th Cir. 1998) ("[A]dherence to an ERISA controlled plan is not a breach of fiduciary duty.").

employer stock, courts have recognized the conflict between the duty to comply with the terms of the plan and the duty to diversify investments or act prudently.[136] Courts have typically resolved this conflict by holding that in certain circumstances, the fiduciary must ignore the terms of the plan regarding investments if the investments are not prudent.[137] However, where the plan requires that all assets, not just the majority of assets as in *Moench*, be invested in employer stock, at least one court has determined that the terms of the plan must be followed and that fiduciaries would not be liable for doing so.[138]

III. FIDUCIARY RESPONSIBILITIES AND PRUDENT PORTFOLIO MANAGEMENT

A. *The Prudent Portfolio Manager Standard*

ERISA fiduciaries must meet a standard of prudence in connection to their investment decisions. Specifically, ERISA fiduciaries are required by statute to act:

> With the care, skill, prudence and diligence under the circumstances then prevailing that a prudent man acting in like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims; and . . . by diversifying the investments of the plan so as to minimize the risk of large losses unless, under the circumstances, it is clearly prudent not to do so.[139]

The application of the ERISA prudent person standard to a plan fiduciary drives to the heart of the legislation. Nonetheless, on its face, the exact meaning of "prudence" for fiduciaries is patently ambiguous. Fiduciaries are bound to differ on projections, risk assessments, and preferred portfolio construction of different asset classes.[140]

In response to such uncertainties related to the prudent person standard and investment decision making, the DOL has issued specific regulations that create a framework for ERISA fiduciaries to follow. Notably, in 2000, the DOL embraced a quantitative portfolio management strategy known as Modern

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136. *See generally Moench*, 62 F.3d at 569 (conceding that a conflict exists when a fiduciary is alleged to have violated ERISA by continuing to invest in an employer's stock).

137. *See generally id.*; *In re* Ikon Office Solutions, Inc. Secs. Litig., 86 F. Supp. 2d 481, 500 (E.D. Pa. 2000) (finding that fiduciaries do not always need to adhere to the plan).

138. Nelson v. IPALCO Enterprises, Inc., 2003 WL 402253, at *8–9 (S.D. Ind. 2003).

139. 29 U.S.C. § 1104(a) (2008).

140. *See generally In re* Ford Motor Co. ERISA Litig., 590 F. Supp. 2d 883, 895 (E.D. Mich. 2008) (indicating that there are circumstances in which reasonable fiduciaries could differ).

Portfolio Theory ("MPT") through a regulatory safe harbor for ERISA fiduciaries.[141] MPT, in its most general of terms, looks to produce an "optimal" portfolio through carefully crafted formulas intended to enhance portfolio diversification.[142] The safe harbor provides that a fiduciary satisfies ERISA's prudence provision if the fiduciary:

> (i) has given appropriate consideration to those facts and circumstances that, given the scope of such fiduciary's investment duties, the fiduciary knows or should know are relevant to the particular investment or investment course of action involved, including the role the investment or investment course of action plays in that portion of the plan's investment portfolio with respect to which the fiduciary has investment duties; and (ii) has acted accordingly.[143]

Integral to the DOL's guidance is the meaning of "appropriate consideration." Appropriate consideration or, alternatively, procedural due diligence means:

> A determination by the fiduciary that the particular investment or investment course of action is reasonably designed, as part of the portfolio (or, where applicable, that portion of the plan portfolio with

141. 29 C.F.R. § 2550.404a-1(b)(1) (2000); *see also Jenkins*, 444 F.3d 916, 925 (7th Cir. 2006) (finding that the trustee's initial selection of the plan's investment funds was consistent with the strategy of finding "long-term, conservative and reliable investments that would do well during market fluctuations[]" and that the trustee did not breach his fiduciary duty to monitor or alter investments when the funds lost value because he regularly consulted with a financial advisor regarding the funds' performance, and "investment losses are not proof that an investor violated his duty of care"). When evaluating prudence by continuing to invest in employer stock, employees' overall retirement packages should also be taken into account. This is consistent with the modern portfolio theory. Howell v. Motorola, Inc., 633 F.3d 552, 566 (7th Cir. 2011) (holding that "[t]he decision of the Plan fiduciaries . . . to continue offering - as *one* option - the Motorola Stock Fund must be evaluated against that backdrop); Summers v. State St. Bank & Trust Co., 453 F.3d 404, 411 (7th Cir. 2006) (concluding that "it is the riskiness of one's portfolio, not of a particular asset in the portfolio, that is important to the risk-averse investor."); *see also Nelson*, 480 F. Supp. 2d at 1102 (S.D. Ind. 2007) (finding that fiduciaries did not imprudently fail to close or divest company stock fund where participants could choose among an array of investments); *Steinman*, 252 F. Supp. 2d at 758 (C.D. Ill. 2003) (determining that the lack of diversification was not imprudent since diversification ran counter to purpose of ESOP, and stock in acquiring company represented only portion of plan participants' overall holdings, which also included conventional defined benefit plan); Hill v. The Tribune Co., 2006 WL 2861016, at *14 (N.D. Ill. 2006), (noting that "investment risk . . . is the key consideration, including whether the participants' retirement funds are almost entirely invested in the company's stock or there are other assets besides the company's stock").

142. Harry Markowitz, *Portfolio Selection*, 7 J. OF FIN. 77-91 (1952).

143. *Id.*

respect to which the fiduciary has investment duties), to further the purposes of the plan, taking into consideration the risk of loss and the opportunity for gain (or other return) associated with the investment or investment course of action.[144]

On the micro-portfolio level, the DOL emphasizes that fiduciaries adopt core MPT principles relating to suggested portfolio diversification and quantitative risk management. Fiduciary consideration of the following factors is recommended: (a) the composition of the portfolio with regard to diversification; (b) the liquidity and current return of the portfolio relative to the anticipated cash flow requirements of the plan; and (c) the projected return of the portfolio relative to the funding objectives of the plan.[145]

However, there is a conflict among the circuits as to what the modern portfolio theory really means. The Seventh and Fifth Circuits and several district courts have held that MPT applies to the plan's portfolio as a whole.[146] However, the Fourth and the D.C. Circuits have ruled that MPT alone is not enough and that prudence of the plan's investment must be judged in isolation.[147]

On the other hand, the Fourth Circuit stated that it "cannot espouse one particular economic theory over another."[148] Thus, the modern portfolio theory is a good start in analyzing a plan's investments. But clearly, MPT views investments in the aggregate. Further protection to fiduciaries may be provided by following the MPT and meeting some additional criteria discussed later in this Article.

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144. *Id.*

145. 29 C.F.R. § 2550.404a-1(b)(2)(ii) (2012).

146. *Leigh*, 858 F.2d at 368 (stating that in determining whether the fiduciaries acted prudently in creating a diversified portfolio, "it makes sense for courts to look at the whole portfolio to determine the investment strategy's success"); *Laborers Nat'l Pension Fund*, 173 F.3d at 322 (finding that the district court erroneously judged the challenged investment in isolation instead of according to the modern portfolio theory required by ERISA policy as expressed by the Secretary's regulations); *Unisys*, 1997 WL 732473, at *3 (E.D. Pa 1997) ("The proper inquiry into whether any harm has been suffered by participants looks to the performance of the portfolio in the aggregate . . .").

147. Modern Portfolio theory, "[s]tanding alone, cannot provide a defense to the claimed breach of the 'prudent man' duties. . . . 'Under ERISA, the prudence of investments or classes of investments offered by a plan must be judged individually.'" *DiFelice*, 497 F.3d at 424. "[O]ur circuit has stated that 'to make prudent investments, the fiduciary has a duty to [research and analyze] the merits of a particular investment.'" *Fink*, 772 F.2d at 951.

148. Masters Mates & Pilots Pension Plan v. USX Corp., 900 F. 2d 727, 740 (4th Cir. 1990) ("We cannot discern the approval of only one theory of valuation in the statutory scheme. Neither can we espouse one particular economic theory over another.").

B. A More Extensive Definition of Modern Portfolio Theory

In 1952, economist Harry M. Markowitz changed the theory and practice of investment management by publishing his groundbreaking article "Portfolio Selection."[149] Markowitz designed new quantitative formulas to effectively manage portfolio risk of loss while at the same time enhancing possible returns for investors.[150]

In order to accomplish such ends, Markowitz emphasized that diversification of the portfolio on the whole was required. Previously, investment analysts examined portfolio performance on a security-by-security basis. "[Portfolio] diversification is both observed and sensible," Markowitz explained.[151] Markowitz based MPT on the statistical concepts of covariance and correlations. Covariance measures the relationship between two risky securities. For example, a high covariance indicates that two security prices move up or down in a similar manner. A low or negative covariance indicates that the securities have a lesser probability of generating similar returns based upon various market forces.[152]

Correlation is another method used to determine how two securities are related. In addition to providing the level of positive or negative relation, correlation also provides a numerical value, which precisely determines the likelihood that assets will move together in performance based upon previous investment returns.[153] The basis of MPT is that portfolios should be composed of assets with low correlation and covariance values.[154] Markowitz hypothesized that low correlations and covariance results would produce "efficient" portfolios where the assets would effectively balance each other out.

Markowitz did not believe in diversification simply for its premise, but rather, for smart diversification based upon correlation and covariance algorithms that produced precise measurements of projected future asset performance. Markowitz's MPT algorithms could be adjusted based upon the level of desired investor risk.[155] Through MPT, Markowitz revolutionized the quantification of portfolio risk and returns. The "goal of portfolio selection is the construction of portfolios that maximize expected returns consistent with individually acceptable levels of risk,"

149. Frank J. Fabozzi, Harry M. Markowitz, Peter N. Kolm, and Francis Gupta, *Portfolio Selection*, THE THEORY AND PRACTICE OF INVESTMENT MANAGEMENT, 45-78 (Frank J. Fabozzi & Harry M. Markowitz, eds., 2d ed.).
150. *Id.*
151. *Id.* at 77.
152. *Id.* at 80-81.
153. *Id.*
154. *Id.* at 89.
155. *Id.*

Markowitz noted.[156]

Theoretically, MPT leads to the construction of portfolios that have the greatest expected return for a given level of risk. Markowitz termed this concept the "efficient portfolio."[157] Yet, in practice this is quite an arduous task. Portfolios must be constructed quantitatively by measuring covariance and correlation trends among a gigantic number of possible equity and debt securities. For example, "for a portfolio of just 50 securities, there are 1,224 covariances that must be measured. For 100 securities, there are 4,950."[158]

Subsequent to these calculations, MPT calls for finding the "optimal portfolio" on an "efficiency frontier." Markowitz defined the "efficiency frontier" as the portfolio with the greatest expected return based upon the preferred level of risk or "standard deviation" value.[159] According to Markowitz, rational portfolio managers would choose the optimal portfolio based upon an investor's desired risk tolerance.[160]

Optimal portfolios are selected by fiduciaries without regard to factors existing outside the portfolio calculations, such as market risk, long-term liquidity, and other systemic concerns.[161] The fiduciary duty of procedural due diligence mandates, in part, that fiduciaries select a portfolio of investments that are optimally diversified without regard for other macro-economic forces. A 1994 DOL Interpretive ERISA bulletin clarified that "fiduciaries may never subordinate the economic interests of the plan to unrelated objectives, and may not select investments on the basis of any factor outside the economic interest of the plan except in very limited circumstances.[162]

Rather than taking actual, existing market variables into account, MPT makes a series of quantitative macro-economic assumptions, such as (1) investors are rational; (2) market information is symmetric, available, and cost free; (3) markets are only temporarily inefficient; and (4) returns follow a normal bell-

156. *Id.* at 45.
157. *Id.* at 60-61.
158. *Id.*
159. *Id.* at 63.
160. *Id.*
161. James P. Hawley, *Corporate Governance, Risk Analysis, and the Financial Crisis: Did Universal Owners Contribute to the Crisis*, CORPORATE GOVERNANCE FAILURES, THE ROLE OF INSTITUTIONAL INVESTORS IN THE GLOBAL FINANCIAL CRISIS 110 (James P. Hawley, Shyam J. Kamath & Andrew T. Williams, eds., 2011).
162. U.S. Dept. of Labor, *Interpretive Bulletin Relating to Investing in Economically Targeted Investments*, 73 Fed. Reg. 61, 735 (October 17, 2009); U.S. Dept. of Labor Advisory Opinion No. 2007–07A (Dec. 21, 2007) and Advisory Opinion No. 2008–05A (June 27, 2008).

curve distribution.[163]

C. *Criticisms of Modern Portfolio Theory and Alternative Strategies*

When markets are liquid and operate efficiently, MPT has the capacity to produce "optimal" portfolios and, accordingly, discharge the DOL's fiduciary obligations of "prudence." However, with the credit crisis in the rearview mirror, there is now growing belief among economists that MPT might not be the most appropriate theory for fiduciary portfolio management.

In a recent article entitled *Reclaiming Fiduciary Duty Balance*, authors James Hawley, Keith Johnson, and Ed Waitzer wrote that an "adjustment" to MPT is "likely" to occur based upon proven shortcomings with the investment philosophy.[164] The authors primarily rest their argument on four premises: (1) the growth of exotic synthetic financial instruments has led to the mispricing of market credit, liquidity, and operational risk; (2) major institutional investor adoption of MPT has produced returns that are extrinsically linked, resulting in investment "herding" and market inefficiency; (3) MPT's sweeping unrealistic assumptions regarding investor risk aversion are not always appropriate; and (4) that MPT neglects to consider the potential extraordinary impact of systemic risk on the liquidity of a given investment portfolio.[165]

Certainly, the widespread adoption of speculative synthetic derivative products and their inclusion in plan asset portfolios creates inefficiencies in Markowitz's MPT. It is far more difficult to craft accurate correlations between synthetic derivative assets than it is to gauge how two equity securities or generic corporate bonds will move in price against each other. Synthetic security returns are strongly affected by latent and uncertain future market risk.[166]

When market risk becomes uncertain, MPT correlations may tend to skewer from projected price movement. As a result, MPT efficiency trees then become unrealistic projections of the greatest possible return for fiduciary portfolios. Moreover, as previously noted, MPT narrowly confines its risk scope to a single portfolio. It does not consider potential market effects of cumulative fiduciary adoption.[167] The potential "herding" effect among large institutional plans results in the implementation of identical investment strategies and undermines the predictive power of

163. James Hawley, Keith Johnson, and Ed Waitzer, *Reclaiming Fiduciary Duty Balance*, 4 ROTMAN INT'L J. PENSION MGMT. 4-5 (2011).
164. *Id.* at 5.
165. *Id.*
166. *Id.*
167. *Id.* at 110.

MPT.[168]

MPT also relies upon the efficient market hypothesis ("EMH"). EMH assumes that market information is readily available and used rationally by market participants to create a daily market price.[169] The MPT presumption is that markets are stable and only temporarily inefficient.[170] Yet, the credit crisis proved that over reliance upon MPT and the EMH be damaging for asset managers because these model distributions failed to account for "fat tail" stress scenarios. "Fat tail" events are economic scenarios that are severe and potentially cataclysmic. During the credit crisis, for instance, market saturation of speculation and default insurance resulted in extreme volatility that the MPT model was unable to predict. In short, MPT did not account for the variable of systemic risk.[171]

Recently, new investment management paradigms have emerged that seek to address the perceived one-size-fits-all nature of MPT investing and the inability to account for "fat tail" distributions.[172] For example, leading economists at the EDHEC Business School and Risk Institute advocate for the construction of a "customized liability hedging portfolio" ("LHP") and a "performance seeking approach" ("PSP").[173] The sole purpose of the LHP would be to "hedge away as effectively as possible the impact of unexpected changes in risk factors" and provide investors with an optimal risk-return trade off.[174]

In February 2012, Harvard University Senior Research Fellow Steve Lydenberg in his research paper, *Reason, Rationality and Fiduciary Duty*[175] also has addressed various purported inadequacies of MPT. Lydenberg echoed the "herding" criticism of MPT by explaining that "Modern Portfolio Theory has directed fiduciaries to act rationally — that is, in the sole financial interests of their funds — downplaying the effects of their investments on others."[176]

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168. *Id.*

169. *Id.* at 111.

170. *Id.*

171. *Id.*at 111-12.

172. Noël Amenc, Felix Goltz, Lionel Martellini, and Vincent Milhau, *Asset Allocation and Portfolio Construction*, *THE THEORY AND PRACTICE OF INVESTMENT MANAGEMENT* 159-202 (Frank J. Fabozzi & Harry M. Markowitz, eds., 2d ed. 2011).

173. *Id.* at 160.

174. *Id.*

175. Investor Responsibility Research Ctr., *IRRC Inst. Announces Two $10,000 Awards for Best Research on Post-Modern Portfolio Theory* (Feb. 21, 2012), http://www.irrcinstitute.org/pdf/IRRC-Award-Winners_Feb-21-2012.pdf.

176. Steve Lydenberg, *Reason, Rationality and Fiduciary Duty, INITIATIVE FOR RESPONSIBLE INVESTMENT AT HARVARD UNIVERSITY* 2 (Jan. 2012), http://hausercenter.org/iri/wp-content/uploads/2010/05/Reason-Rationality-and-Fiduciary-Duty.pdf.

Lydenberg concluded that fiduciary decisions based upon mathematical formulas, without subjective reason only exacerbates the potentiality of "fat tails" and systemic risk. He explained that "[a]s increasing numbers of passive index investors enter the markets they encourage a blind 'herding' behavior that exacerbates the bubbles and bursts created by the speculators who are increasingly left to set prices in the markets."[177]

Rather than clinging to MPT quantitative rationality, the importance of fiduciary reasonability and a "conception of prudence characterized by wisdom, discretion and intelligence" is what should drive fiduciary decisions, according to Lydenberg.[178] In his award-winning research paper, he criticizes fiduciary reliance upon mathematical algorithms and formulas that fail to take into account market uncertainty. Academic economists with a mathematical bent, rather than legal scholars or financial professionals, laid the groundwork for MPT, substituting risk control at a portfolio level for specific, judgment-based security selection as the basis for prudent investment.[179]

In looking towards the future, Lydenberg examined three new corporate governance paradigms that are intended to supplement arguable inadequacies of MPT selection:

> (1) *the universal owner approach, i.e.*, concern about the effect of [fiduciary] investments on the whole economy [increases returns for plan assets because investments will not perform unless the macro economy performs].
>
> (2) *the sustainable or responsible investment approach, i.e.*, concern about the effect of [fiduciary] investments on the quality of the environment and society in which their current and future beneficiaries live [is vital to maintain long-term positive returns].
>
> (3) *the broad-based-norms approach, i.e.*, concern that [fiduciary] investments be consistent with certain universally recognized norms and standards that are associated with [corporate] governance [are integral to consistent portfolio returns].[180]

Lydenberg writes that, in practical application, these three paradigms have been implemented in various institutional measures. For instance, the "universal approach" was adopted in recent decisions by the California Public Employees Retirement System to invest $800 million in infrastructure projects, by TIAA-CREF to invest $50 million with Good Energies Inc., and by J.P. Morgan, The Bill & Melinda Gates Foundation, The Gatsby Charitable Foundation, and The Rockefeller Foundation to invest cooperatively $25 million in an African Agricultural Capital Fund

177. *Id.* at 23.
178. *Id.* at 2.
179. *Id.* at 7.
180. *Id.* at 11.

managed by Pearl Capital Partners.[181]

The sustainable approach was accepted by institutional European funds such as the Norway Government Pension, when in 2011 they eliminated from their portfolio "nine companies involved in creating severe environmental damage and 17 companies involved in the production of tobacco products."[182] Lydenberg also notes that the U.K. pension fund managers Universities Superannuation Scheme, the Hermes Fund Managers, and the Dutch pension fund managers APG and PGGM are among the investors in the Access to Medicines Index, which ranks pharmaceutical companies on their efforts to provide access to medicine to impoverished communities.[183]

Finally, Lydenberg noted that SNS Asset Management, a Dutch based asset manager, has adopted the "broad-based approach" and financial services company SNS REAAL, with over €50 billion under management, employs a number of social and environmental principles in its fundamental investment policies including an emphasis on "human rights, child and forced labor, controversial weapons systems, and environmental contamination."[184]

Apart from enhancing fiduciary consideration of governance and corporate social responsibility, Lydenberg emphasized that fiduciaries should embrace known economic convention when making investment decisions. This requires the opposite of deference to quantitative MPT models. Indeed, to combat uncertainty and systemic risk, Lydenberg contended that fiduciaries should rely upon their own wisdom from known "conventions," in other words, practical common sense.[185] Lydenberg advocated that a range of factors beyond narrow financial criteria should supplement fiduciary investment decision making, including the "sustainability of society" and the "stability of financial markets"[186] – in essence, combining MPT rationality with a humanistic risk management standard.

D. Where Do We Go from Here?

Stand-alone fiduciary reliance upon MPT is a good start, but adding protection would entail tweaking the investment philosophy to the current economic climate. As stated above, ERISA § 404 fiduciary requirements mandate appropriate diversification and minimization of large portfolio losses. MPT is a safe risk adverse means to invest plan asset funds. However, in

181. *Id.* at 12.
182. *Id.* at 15.
183. *Id.* at 15-16.
184. *Id.* at 16.
185. *Id.* at 32.
186. *Id.* at 33.

implementation, analyzing the current economic environment would further assist in minimizing plan losses.

While the previously prudent fiduciary had good reason to rely on MPT, financial times have changed. The current trend is towards rational quantitative adjustments to MPT. For example, the EDEC method calls for a hedged portfolio to account for potentially bad investments and market risks. Moreover, supplementation of MPT with notions of social responsibility, governance, and accepted economic and societal conventions is also gaining popularity, especially in European circles. Taking the foregoing into account, the DOL MPT safe harbor is ripe for modification to assist and provide guidance to fiduciaries in meeting their duties under ERISA.

IV. DEFINED CONTRIBUTION PLAN INVESTMENTS IN EMPLOYER STOCK

A. *Employer Stock Jurisprudence Created from Trial Court Decisions*

As mentioned previously, most cases involving allegations of breach of fiduciary duty under ERISA for maintaining employer stock have been adjudicated in the motion to dismiss and summary judgment stages, and thereafter have usually settled. Thus, only a handful of employee stock fiduciary cases have gone to trial. While the factual scenarios may be different, these cases generally favor a presumption of prudence for the employer fiduciary, or at least a high burden of proof to support an allegation that the fiduciary breached his duties in continuing to invest in employer stock.

In the first case that went to trial, *Landgraff v. Columbia/HCA*, a Tennessee district court addressed whether the defendant fiduciaries were both procedurally and substantively prudent.[187] The company at issue, Columbia/HCA, was a health care management firm, which owned and operated approximately 300 hospitals throughout the United States.[188] Former employees and participants in the company's ESOP known as the Stock Bonus Plan ("SBP"), Landgraff and Magarian, sued claiming that the defendant fiduciaries were not procedurally or substantively prudent in overseeing the SBP, which qualified as an EIAP as defined under 29 U.S.C. § 1107 (d)(3)(A).[189]

In *Columbia/HCA*, the plaintiffs were participants in a stock bonus plan and 401(k) plan that invested in employer stock, and the value of their plan accounts decreased as a result of federal

187. *Columbia/HCA Healthcare Corp., 2000 WL 33726564, at *19.*
188. *Id.* at *1.
189. *Id.* at *1-2.

government investigations of the company's Medicare billing practices. [190] After discussing the committee meetings and the committee's continued determination that the employer stock was still a prudent plan investment, the court determined there was no breach of fiduciary duty because the plaintiffs did not establish that a reasonable fiduciary would have determined that the investment of the plan assets in Columbia/HCA stock was imprudent, thereby rebutting the presumption of reasonableness afforded to defendants' actions.[191] The court noted that based on the facts, "an inquiry into the fundamentals of the company would not have revealed to a reasonable fiduciary that the investment at issue was improvident."[192] In addition, the court found that the company itself was not liable based on an alleged failure to monitor and remove the committee members.[193]

However, despite adopting the *Moench* presumption as the appropriate standard of review, the court found the defendant fiduciaries to be procedurally imprudent.[194] Essentially, this determination was made because under the plain language of the SBP "investment guidelines" the defendant fiduciaries were required to consider whether "at certain times additional assets may be added to the portfolio to dampen the volatility of Employer Common Stock without severely damaging the Employee's ability to participate in the growth of the Employer Common Stock."[195] The defendant fiduciaries did not consider these stated diversification requirements, and as a result, the court ruled they failed to meet their procedural requirement of prudence.[196]

Nonetheless, the court held that the plaintiffs could not establish substantive imprudence.[197] The court ruled that there was no casual link between the procedural deficiency and the harm suffered by the plan because the company's financials were strong, according to internal and external reports.[198] Two years later, the Sixth Circuit likewise found no substantive breach of fiduciary duty in portfolio investments based upon the facts presented.[199]

In *DiFelice v. U.S. Airways*, the ERISA allegations stemmed from the U.S. Airways bankruptcy, specifically involving the company's many diversified portfolio funds as well as a U.S.

190. *Id.* at *1.
191. *Id.* at *19.
192. *Id.* at *16.
193. *Id.* at *19.
194. *Id.* at *14.
195. *Id.* at *3.
196. *Id.* at *13.
197. *Id.* at *19.
198. *Id.* at *14-17.
199. Landgraff v. Columbia, 30 Fed. App'x. 366, 372 (6th Cir. 2002).

Airways Company stock fund.[200] In affirming the lower court's holding that there was no breach of the fiduciary duty of procedural or substantive prudence, the Fourth Circuit emphasized that the plaintiffs had an "almost unlimited ability to allocate their investments" because of the diversity of 401(k) plan options offered to them.[201] In fact, since U.S. Airways offered such a diverse plethora of 401(k) plan investment options, the court noted, "in this way, the onus was on the participants to manage their investments."[202]

The plan did impose certain restrictions on the participants' ability to invest in the company stock fund.[203] For example, "matched" contributions provided by U.S. Airways were not permitted to be invested in the company stock fund.[204] A participant who removed his or her investment from the company stock fund could not reinvest in the fund until thirty calendar days later.[205] Moreover, U.S. Airways provided a Summary Plan Document ("SPD"), which provided general information and descriptions of investment options, as well as important warnings regarding the company stock fund including a clear disclaimer that U.S. Airways could not guarantee its performance.[206]

In its review of the facts presented, the Fourth Circuit held that the defendant fiduciaries met their duties of procedural prudence because of the existence of the SPD and its myriad of disclosures and warnings regarding the company stock fund, regular meetings regarding the sustainability of the company stock fund, appointment of an independent fiduciary, and good faith belief in the legitimacy of the U.S. Airways restructuring plan to stave off bankruptcy.[207]

With regard to the impact of an independent fiduciary's appointment on procedural prudence the court indicated that "although appointment of an independent fiduciary does not 'whitewash' a prior fiduciary's actions, timely appointment of an independent fiduciary, prompted by concerns about the continued prudence of holding company stock under an ERISA plan, does provide some evidence of 'procedural' prudence and proper monitoring during the relevant period."[208]

Fiduciary prudence was met in *U.S. Airways* because those fiduciaries were active, engaged, and advised participants of their

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200. *DiFelice*, 497 F.3d at 413-15.
201. *Id.* at 414.
202. *Id.* at 414-15.
203. *Id.* at 414 n.1.
204. *Id.*
205. *Id.*
206. *Id.* at 415.
207. *Id.* at 421.
208. *Id.*

options without ignoring plan mandates or any other 401(k) diversification requirements. The fiduciaries reasonably believed at the time that their restructuring program would work and that the company stock was a viable investment for the airline company's employees.[209] The Fourth Circuit did not discuss the applicability of the *Moench* presumption in this case.

The Seventh Circuit addressed similar prudence issues in the case *Nelson v. Hodowal*.[210] Indianapolis Power and Light Company ("IPALCO") employees brought an action arising out of a precipitous drop in the company's stock – from $49.60 to $4.11 in a matter of months – after IPALCO merged with AES Corporation in 2001.[211] IPALCO maintained a defined benefit 401(k) plan and a defined contribution plan.[212] The defined benefit plan held a diversified portfolio and the defined contribution plan initially included only company stock where the employer matched these contributions up to four percent of an employee's annual salary.[213] Upon consummation of the merger IPALCO shares were sold to AES and the defined contribution plan participants received AES stock.[214] The pension committee believed at the time of the merger that the AES deal held better long-term options for IPALCO plan participants.[215]

From the plan's inception, IPALCO hired Merrill Lynch, Pierce, Fenner & Smith, Inc., to advise the participants about appropriate plan investments.[216] The record indicated that Merrill Lynch emphasized to the participants the benefits of diversification and, subsequent to the merger, it widely distributed literature advising participants of their new options with appropriate disclosures and warnings.[217] Nonetheless, the plaintiffs alleged that the fiduciaries should have predicted the extreme decline in stock and, thus, were neither procedurally nor substantively prudent in exercising their obligations.[218]

While the IPALCO-defined contribution plan required the pension committee to maintain IPALCO stock as an option, the district court held that "a number of court decisions have recognized at least a possibility that, under sufficiently dire circumstances, ERISA fiduciaries' duty of prudence may require them to act contrary to the terms of the plan and sell employer

209. *Id.* at 422.
210. *Nelson*, 512 F.3d at 347.
211. *Id.* at 348.
212. *Id.* at 347.
213. *Id.*
214. *Nelson*, 480 F. Supp. 2d at 1064.
215. *Id.* at 1077.
216. *Nelson*, 512 F.3d at 348.
217. *Nelson*, 480 F. Supp. 2d at 1103.
218. *Hodowall*, 512 F.3d at 349.

stock."[219] Moreover, the fact that the condition of both the IPALCO and AES stocks were "reasonably healthy . . . weigh[ed] heavily against a finding of breach of fiduciary duty."[220] In holding that the *Moench* presumption was applicable, the district court stated:

With or without the [*Moench*] presumption . . . it is clear that the defendants here all viewed continued investments in IPALCO and AES as an appropriate and suitable investment option for the thrift plan participants. The Defendants had reasonable grounds for that view after going through the process that led the IPALCO board to approve the AES Share exchange.[221]

Specifically, the district court relied upon the IPALCO pension committee and board of directors' diligent research into the health of AES and its long-term viability.[222] The IPALCO board was substantively and procedurally prudent because it took many steps to ensure, in its own good faith, that the merger with AES was in the best interest of the plan participants and the company as a whole.[223] There was "no non-public information indicating that AES stock was likely to decline in value."[224] Further, the district court asserted that even if the defendant fiduciaries were found to be procedurally deficient, this "would not have resulted in the removal of IPALCO/AES as investment options," i.e., the causation necessary for a showing of a breach of substantive prudence.[225] Indeed, on review in the Seventh Circuit, the court affirmed this holding without modification or criticism.[226]

Like *U.S. Airways*, the IPALCO case demonstrates that application of the *Moench* presumption is inconsequential so long as the defendant fiduciaries make good faith reasonable decisions that they believe at the time are in the best interests of the plan participants. Courts assume a deferential analysis and are reluctant to be critical of decisions they believe may be imprudent with the added benefit of hindsight.

Finally, the most recently tried employer stock case, *Brieger v. Tellabs, Inc.*, is yet another example of a court deferring to a fiduciary's good faith investigation and reasonable belief in the soundness of investment decisions.[227] Tellabs was a telecommunications company that provided two retirement plans: a savings plan and profit sharing plan.[228] "An employee could elect to make contributions to the savings portion of the plan, which

219. *Nelson*, 480 F. Supp. 2d at 1097.
220. *Id.*
221. *Id.* at 1099.
222. *Id.* at 1099-1100.
223. *Id.*
224. *Id.*
225. *Id.*
226. *Nelson*, 512 F.3d at 351.
227. *Brieger*, 629 F. Supp. 2d at 852.
228. *Id.*

Tellabs matched in an amount up to three percent of the employee's income."[229] Each individual employee had the authority to allocate his or her investments among eleven or twelve different investment choices.[230] One fund consisted solely of Tellabs stock.[231] "The Tellabs stock fund was the only single-security investment offered to the plan participants."[232]

In an effort to provide investment education, Tellabs employees were warned about holding company stock, had access to extensive information about how the company was performing, other investment disclosures, and quarterly statements.[233] Indeed, employees had access to a Tellabs intranet website that contained numerous news articles about the company, a daily update of its stock price, and links to websites where participants could review and alter their investment choices in the plan.[234]

At issue in the case was the prudence of the defendant fiduciaries in failing to remove Tellabs stock as an investment option during the class period when the value dropped from $63.19 to $6.58 per share. The plaintiffs argued that the plan documents did not require the defendant fiduciaries to offer Tellabs stock as an investment option.[235]

As a preliminary matter, the district court found that while the plan "granted defendants the power to evaluate and terminate 'Funds,' it specifically stated that a Fund comprised of Tellabs stock was required to be maintained and offered to Plan participants."[236] The court held that the plaintiff could not prove that the defendant was procedurally and substantively imprudent in failing to remove Tellabs as an investment option because of market conditions. The court reasoned that the Tellabs fiduciaries did not have to hold formal discussions regarding the utility of retaining the company stock as an investment option to satisfy procedural requirements. Furthermore, even if the plaintiffs could show procedural imprudence, the court indicated "a reasonably prudent individual in similar circumstances who undertook such an examination would not have sold the plan's Tellabs stock or removed it as an investment option. The fact that the stock price dropped significantly during the class period is not, on its own, conclusive."[237] Like the aforementioned cases, the court instructed that instead of basing imprudence claims on dips in the stock price

229. *Id.*
230. *Id.*
231. *Id.*
232. *Id.*
233. *Id.* at 853.
234. *Id.*
235. *Id.* at 855.
236. *Id.* at 861.
237. *Id.* at 862-63.

or troubled company claims, it is imperative to remove hindsight from the analysis and simply determine what "reasonably prudent fiduciaries would have done based on the information available at the time."[238] Critical to the court's decision was that the defendant fiduciaries presented "ample evidence" that Tellabs's business prospects in the short term and long term would recover.[239]

Like in *IPALCO* and *U.S. Airways*, the defendant fiduciaries had good reason to believe that their decision-making in periods of market turmoil would not require dilution of the plans investments. Clearly, the aforementioned cases illustrate that whether the *Moench* presumption is applied or not, ERISA plaintiffs must demonstrate some form of scienter evidence among defendant fiduciaries that they knew their investment decisions were not in the best interests of the plan, or alternatively, as in *Columbia/HCA,* that they ignored plan mandates of diversification or other equally as important requirements.

In conclusion, in the stock drop cases that have gone to trial, the courts have refused to impute the benefit of hindsight and crystal ball predictions when reviewing the prudence of the defendant fiduciaries. Instead, such fiduciary prudence is weighed based on the information available during the respective class period.[240] Such costly litigation, in light the fiduciaries' heavy burden, further supports the need to afford fiduciaries with a presumption of prudence.

B. *The Presumption of Prudence Standard*

1. *Evolution of the Presumption in Employer Stock Cases*

In the earlier stock drop cases, courts generally recognized claims for breach of fiduciary duty for continued investment in employer stock of decreasing value. However, courts seemed reluctant to apply fiduciary liability to board members absent an active role in the plan administration.

In *Eaves v. Penn*,[241] the court determined that a cause of action for investing an ESOP in employer stock that declined in

238. *Id.* at 863.

239. *Id.* at 864.

240. *See Kuper*, 852 F. Supp. at 1399 ("By enacting ERISA with specific exemptions for ESOPs, Congress signaled its conviction that ESOP investment in employer stock is a desirable practice that should be encouraged. This Court will not assume that Congress thereby intended to foist upon ESOP fiduciaries the additional duty of clairvoyance."); Kirschbaum v. Reliant Energy, Inc., 526 F.3d 243, 256 (5th Cir. 2008) ("A fiduciary cannot be placed in the untenable position of having to predict the future of the company stock's performance."); *DiFelice*, 497 F.3d 410, 424 (4th Cir. 2007) ("whether a fiduciary's actions are prudent cannot be measured in hindsight").

241. Eaves v. Penn, 587 F.2d 453, 460 (10th Cir. 1978).

value was valid.[242] However, the director that was liable was also the plan trustee and the decline in value was partially due to his transaction with the ESOP and his "mismanagement of the company."[243] The facts showed that he was using the plan for his own benefit, i.e., he was using his role as trustee to acquire all the legal title to the company's stock and control of the company.[244] The director's first defense was that, as director, he was not a "fiduciary." The court rejected this because he was also the plan trustee and it was clear he was exercising discretionary control over the plan. Next, the director argued that, as trustee, he was bound by the terms of the plan to invest in the company's stock. The court rejected this reasoning based on the statutory language and said that there was no such exception to the "exclusive benefit" and "prudent man" requirements of ERISA 404(a)(1)).[245]

The plaintiffs in *Fink v. National Savings and Trust Company*[246] also brought an action against the plan trustees for investing too much of the plan's assets in employer stock.[247] Apparently, the company amended the terms of the plan and trust to require that all assets be invested in company stock.[248] The plan borrowed funds to purchase employer stock and used company contributions to make loan payments.[249] When the company experienced a "serious downturn due to the loss of their largest customer," the company could not make contributions to the plan and the plan could therefore not make payments on the note or pay benefits when due.[250] Although the plaintiffs claimed that the trustees breached their fiduciary duties by "acquiring and retaining" employer stock, the primary issues related to the prudence of the plan's leverage transaction rather than the value of the stock itself.[251] The court determined that the plaintiffs' claims were not time barred and remanded the case.[252]

In *Canale v. Yegan*,[253] the defendants were D & Os and also "plan administrators," although there is little discussion in the case of what administrative functions the defendants had as plan administrators. The plaintiffs alleged that the defendants engaged in misbehavior, mismanagement of companies, and fraudulent concealment of facts, which resulted in a decline in the value of the

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242. *Id.*
243. *Id.* at 456.
244. *Id.* at 458.
245. *Id.* at 460.
246. *Fink*, 772 F.2d at 955.
247. *Id.* at 956.
248. *Id.* at 954.
249. *Id.*
250. *Id.*
251. *Id.* at 956.
252. *Id.* at 958.
253. Canale v. Yegan, 782 F. Supp. 963, 966 (D.N.J. 1992).

company's stock.[254] After noting the special status of an ESOP and its primary investment in employer securities, the court concluded that the plaintiffs stated a valid "failure to diversify plan asset" claim under ERISA:

> [U]nder these circumstances, where plaintiffs have alleged that the value of the plan's investment was impaired by the plan fiduciaries' own fraudulent and illegal acts, allegations of failure to diversify plan assets invested in an ESOP can state a claim under ERISA. . . . [T]he basis for this ERISA action is not the perpetration of the fraud on Integrity's shareholders itself, but the fact that, knowing the Plan's investment had been impaired by their own fraudulent acts, defendants, acting as fiduciaries, failed to take any steps to protect the Plan's assets from dissipation.[255]

In *Kuper v. Quantum Chemical Corporation*,[256] the court granted summary judgment for the company and board members in an ERISA breach of fiduciary duty lawsuit where the value of the stock declined during an eighteen-month period before the plan assets were transferred to a new plan.[257] Although the court recognized that board members could be fiduciaries under ERISA if they have the power to appoint plan administrators, it determined that the plaintiffs in that case "failed to come forward with specific facts showing that that there [was] a genuine issue as to whether the defendants were fiduciaries in pertinent respects."[258] The court found that the company and the board were not named fiduciaries under the plan and did not, under the terms of the plan, have discretionary authority over the management, administration, or assets of the plan.[259] Although the plaintiffs claimed they had a "reasonable suspicion" that the board influenced the committee's decisions, the court held that the plaintiffs failed to articulate specific facts to support that contention.[260] Therefore, since the plaintiffs did not allege that the company and its board breached a duty with respect to the appointment and removal of plan administrators, and did not allege that the company or board knew of any wrongdoing by the plan administrators, summary judgment was appropriate.[261] Thus, only one of these early employer stock drop cases denied board members' motions for summary judgment.[262]

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254. *Id.*
255. *Id.* at 968.
256. *Kuper*, 838 F. Supp. 342, 344.
257. *Id.*
258. *Id.* at 348.
259. *Id.*
260. *Id.*
261. *Id.*
262. McKinnon v. Cairns, 698 F. Supp. 852, 860 (W.D. Okla. 1988) ("While plaintiffs do not allege any discretionary authority or responsibility of [the

2. *The Presumption of Prudence as Applied to EIAPs*

At the same time, to encourage employee ownership through pension plans and to give workers a long-term stake in the enterprise for which they labor,[263] Congress expressly allows EIAP fiduciaries to concentrate the plan's holdings in employer securities, by exempting such plans from the diversification requirement and from the prudence requirement, insofar as it encompasses duties related to diversification.[264] Congress intended ERISA to balance the protection of employee benefits against creating a system "so complex that administrative costs, or litigation expenses, unduly discouraged employers from offering [pension] benefit plans in the first place."[265] In the context of EIAPs, "Congress has expressed a strong preference for plan investment in the employer's stock, although this preference may be in tension with ERISA's general fiduciary duties."[266]

In determining whether a fiduciary acted prudently in continuing to offer company stock as an investment option, "[t]he focus of the inquiry is how the fiduciary acted, not whether his investments succeeded or failed."[267] A fiduciary's conduct must be

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individual directors] in the administration of the plans, this allegation can be inferred from the Complaint. The question whether all or any of these defendants exercised such control sufficient to establish them as ERISA fiduciaries is a factual one, and will be borne out through evidence, or the lack thereof, presented following discovery.")

263. *Foltz*, 865 F.2d at 373 (explaining that "ERISA . . . specifically favors" capital structures involving "long-term employee ownership").

264. *See Kirschbaum*, 526 F.3d at 249 ("ERISA exempts an EIAP from the duty to diversify with regard to the purchase or holding of company stock."); *Steinman*, 352 F.3d at 1103 ("Congress, believing employees' ownership of their employer's stock a worthy goal, has encouraged the creation of ESOPs both by giving tax breaks and by waiving the duty ordinarily imposed on trustees by modern trust law (including ERISA . . .) to diversify the assets of a pension plan."). As one court reasoned:

> If there is no duty to diversify ESOP plan assets under the statute, it logically follows that there can be no claim for breach of fiduciary duty arising out of a failure to diversify, or in other words, arising out of allowing the plan to become heavily weighted in company stock.

In re McKesson HBOC, Inc. ERISA Litig., 2002 WL 31431588, at *5 (N.D. Cal. 2002).

Despite the risks inherent in concentrating plan assets in any one security, the express statutory exemption of the diversification duty in relation to an employer's stock holdings precludes recovery. *Kirschbaum*, 526 F.3d at 249; *see In re* Dell, Inc. ERISA Litig., 563 F. Supp. 2d 681, 687 (W.D. Tex. 2008) (dismissing diversification claim because "EIAP fiduciaries do not have a duty to diversify and do not act imprudently by not diversifying the assets of an EIAP.").

265. *Kirschbaum*, 526 F.3d at 253.

266. *Id.*

267. *Id.*

evaluated "in light of the character and aims of the particular type of plan he serves."[268] For pension plans invested in company stock, the court should consider the "long-term horizon of retirement investing" as well as the "favored status Congress has granted to employee stock investments in their own companies."[269]

Attempting to strike the proper balance between these competing interests, the Third Circuit adopted an abuse of discretion standard of review for assessing fiduciary prudence in the context of ESOPs or other EIAPs.[270] An EIAP fiduciary who invests the assets in employer stock is entitled to a presumption that it acted consistently with ERISA in making that decision."[271] The *Moench* standard has been expressly adopted by the Second, Fifth, Sixth, Ninth and Eleventh Circuits. Certain districts courts have also applied the presumption in circuits not expressly adopting it.[272] The latest circuit to adopt the *Moench* presumption stated that by not affording the fiduciaries this presumption of prudence, it would "force ESOP fiduciaries to choose between the devil and the deep blue sea."[273]

In *Moench*, the Third Circuit concluded that an ESOP fiduciary is entitled to a presumption that his decision to invest in the employer's securities was prudent and that a plaintiff may

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268. *Id.* at 253-54.

269. *Id.* at 254.

270. *See Moench*, 62 F.3d at 571 (discussing ESOPs); Edgar v. Avaya, Inc., 503 F.3d 340, 347 (3d Cir. 2007) (extending *Moench* to EIAPs).

271. *Moench*, 62 F.3d at 571. In that case, the court developed a "prudence presumption" that a fiduciary "who invests the assets in employer stock is entitled to a presumption that it acted consistently with ERISA by virtue of that decision. *Id.* However, the plaintiff may overcome that presumption by establishing that the fiduciary abused its discretion by investing in employer securities." *Id.* To rebut the prudence presumption, a plaintiff must establish that continued investment in employer stock would "defeat or substantially impair the accomplishment of the purposes of the trust." *Id.*

272. *Lalonde*, 369 F.3d at 6; Bunch v. W.R. Grace & Co., 555 F.3d 1, 5 (1st Cir. 2009); *Stein*, 270 F. Supp. 2d at 168; Kennet v. State St. Corp., 694 F. Supp. 2d 283, 299 (D. Mass. 2008); Coffin v. Bowater, Inc., 385 F. Supp. 2d 38, 47 (D. Maine 2005); *DiFelice*, 497 F.3d at 417; *Duke*, 281 F. Supp. 2d at 795; *In re* Wachovia Corp. ERISA Litig., 2010 WL 3081359, at *8-12 (W.D.N.C. 2010); *In re* Constellation Energy Grp., Inc., 738 F. Supp. 2d 602, 614 (D. Md. 2010); Pugh v. Tribune, 521 F.3d 686, 696 (7th Cir. 2008); *Steinman*, 252 F. Supp. 2d at 758; Harzewski v. Guidant, 489 F.3d 799, 810 (7th Cir. 2007); *Summers*, 453 F.3d at 412; Howell v. Motorola, 633 F.3d 552, 571 (7th Cir. 2011); Armstrong v. LaSalle Bank, 446 F.3d 728, 740 (7th Cir. 2006); *Brieger*, 629 F. Supp. 2d at 872; Peabody v. Davis, 636 F.3d 368, 385 (7th Cir. 2011); *Nelson*, 480 F. Supp. 2d at 1072 (S.D. Ind. 2007); In re Harley-Davidson, Inc. Secs. Litig., 660 F. Supp. 2d 953, 967 (E.D. Wis. 2009); *Sears*, 2004 WL 407007, at *3; Brown v. Medtronic, 628 F.3d 451, 459 (8th Cir. 2010); *Xcel*, 312 F. Supp. 2d at 1180; Morrison v. Moneygrams Interns, Inc., 607 F. Supp. 2d 1033, 1045 (D. Minn. 2009); Crocker v. KV Pharms., 782 F. Supp. 2d 760, 780 (E.D. Mo. 2010).

273. Lanfear v. Home Depot, 2012 WL 1580614, at *10 (11th Cir. 2012).

rebut the presumption only by showing that "owing to circumstances not known to the settlor and not anticipated by him [that the making of such investment] would defeat or substantially impair the accomplishment of the purposes of the trust."[274]

The strength of the presumption depends on other factors, such as the amount of discretion given to the fiduciary under the terms of the plan or any conflicts of interests the fiduciary may have.[275] The Second Circuit in *Citigroup* also adopted this sliding scale, stating that "[a] fiduciary's failure to divest from company stock is less likely to constitute an abuse of discretion if the plan's terms require - rather than merely permit - investment in Company stock."[276]

Given the presumption of prudence to which ERISA fiduciaries are entitled, plaintiffs must plead facts sufficient to show what "circumstances not known to the settlor and not anticipated by him" should have caused the EIAP fiduciary to determine that employer stock was not a prudent investment.[277] In other words, plaintiffs must, at a minimum, allege what caused stock to become an imprudent investment.[278]

For example, in *Kirschbaum v. Reliant Energy, Inc.*, the plaintiff alleged that the stock became an imprudent investment when the fiduciaries obtained adverse information about improper trading by a few employees and the stock dropped in value by forty percent.[279] However, the *Kirschbaum* court found that these allegations were insufficient to overcome the presumption of prudence.[280]

Thus, *Kirschbaum* demonstrates that the *Moench* presumption may be overcome only where the employer's financial

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274. *Moench*, 62 F.3d at 571 (quoting RESTATEMENT (SECOND) OF TRUSTS § 227 cmt. g (1959)); *see Dell*, 563 F. Supp. 2d at 691-93 (stating that the *Moench* presumption of prudence applies regardless of whether the "plan requires, encourages, or permits investment [in employer stock] so long as the investment is an EIAP or ESOP" and may be applied at the motion to dismiss stage).

275. *Quan*, 623 F.3d at 883; *Kirschbaum*, 526 F.3d at 255.

276. *Citigroup*, 662 F.3d at 137.

277. *Dell*, 563 F. Supp. 2d at 693.

278. *Kirschbaum*, 526 F.3d at 253-55.

279. *Id.* at 255.

280. *Id.*; *see also Wright*, 360 F.3d at 1098 (noting the ill-fated merger, reverse stock split, and seventy five percent drop in stock price were insufficient to rebut the *Moench* presumption of prudence); *Kuper*, 66 F.3d at 1459 (noting the company-wide financial woes and eighty percent drop in stock price were insufficient); *In re* Avon Prods., Inc., Secs. Litig., 2009 WL 884687, at *1 (S.D.N.Y. 2009) (noting that the twenty four percent drop in stock price and declining sales were insufficient); *McKesson*, 391 F. Supp. 2d at 830-33 (declining to apply *Moench*, but concluding widespread accounting violations, restated revenues for three years, and seventy five percent drop in stock price were insufficient to rebut presumption).

circumstances are so dismal that continued investment in employer stock would impress upon participants extraordinary risks – risks that go beyond what Congress contemplated when it endorsed in ERISA long-term investments in employer securities through the creation of EIAPs.[281]

3. *"Precipitous Decline" and "on the Brink of Collapse"*

Moench and its progeny stand for the proposition that an EIAP's fiduciaries must sell employer securities in contravention of plan terms only "where a company's financial situation is seriously deteriorating and there is a genuine risk of insider self-dealing."[282] Plaintiffs must allege facts showing gravely dire

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281. *Wright*, 360 F.3d at 1098 (affirming grant of 12(b)(6) motion and holding that the presumption of prudence "may be overcome when a precipitous decline in the employer's stock is combined with evidence that the company is on the brink of collapse or undergoing serious mismanagement"). The Third Circuit in *Moench* addressed claims brought against the fiduciaries of a plan sponsored by a bank that failed and went into bankruptcy. *Moench*, 62 F.3d at 572. The plan's fiduciaries were members of the sponsoring bank's board of directors, and in the year preceding the bankruptcy, had inside, non-public "knowledge of [the company's] impending collapse" by virtue of being privy to the fact that federal bank examiners had found "violations of law and regulation . . . across a number of areas in the [company's] subsidiary banks," and had found "unsafe and unsound credit practices," a "rapid deterioration in the quality of the loan portfolio," and other harbingers of imminent disaster. *Id.* Despite this intimate knowledge of an expected rapid deterioration in the fundamentals of the company and a downward trend in the price of the securities, the plan fiduciaries continued investing plan assets in employer stock while the collapse of the company appeared increasingly imminent. *Id.* Given both the quantum and content of the information then known to the fiduciaries, the Third Circuit remanded the case to allow plaintiffs to pursue their claim that the fiduciaries "properly could effectuate the purposes of the trust only by deviating from the trust's direction." *Id.*; *see also Duke*, 281 F. Supp. 2d at 795 (applying *Moench/Kuper* construct, plaintiffs' prudence claims fail as a matter of law because Duke Energy was "a viable, strong company with substantial assets . . . far from impending collapse and not in dire circumstances").

282. Many courts have applied the "impending collapse"/imminent bankruptcy standard. *See, e.g., Moench*, 62 F.3d at 572 ("impending collapse"); *Howell*, 633 F.3d at 569 (affirming summary judgment on claim that fiduciaries breached their duties by offering Motorola stock without evidence of imminent collapse); *Summers*, 453 F.3d at 408-11 (affirming motion to dismiss on claim that fiduciary imprudently failed to divest employer stock when share price dropped precipitously and CEO warned that company was at risk for bankruptcy); *Kuper*, 66 F.3d at 1460 (finding that presumption was not overcome despite eighty percent decline in stock value, mounting debt, a major plant fire halting production, and the CEO's sale of all of his company stock holdings); *Brieger*, 629 F. Supp. 2d at 863 (ruling that plan required the offering of employer stock fund but declining to decide applicability of prudence presumption because plaintiffs' claims failed under any standard; stock was a sound investment, despite drop in price from $63 to $6.48 over class period).

circumstances that would suggest an abuse of discretion by fiduciaries in deeming the company stock an appropriate long-term investment for the plan.[283] A complaint "should allege facts, not mere conclusions, to demonstrate that the circumstances . . . were such that it was an abuse of discretion for the plan fiduciaries to follow the [plan's] directions and allow company contributions to be made in the form of company stock."[284]

Other courts have permitted lawsuits to proceed in spite of the ESOP presumption because "presumptions are evidentiary standards that should not be applied to motions to dismiss."[285] In its survey of the presumption, a district court noted, however, that some courts have in fact used the ESOP presumption to grant motions to dismiss, but found that there was "ample authority to the contrary."[286]

Most of the employer stock cases are not yet at the point where the merits have been analyzed by the courts. Therefore, it is difficult to determine whether future courts will follow or distinguish the earlier stock drop cases described above, especially because more recent cases have expanded the earlier stock drop cases by applying the ESOP exception.

For example, in *In re Duke Energy ERISA Litigation*, the court granted the defendants' motion to dismiss for failure to state a claim and determined that the fiduciaries' decision to remain invested in the employer's stock after a press release detailed questionable "round trip" energy trades was reasonable.[287] The court applied the presumption to the investment of matching contribution in company stock and permitting employees to direct the investment of employee contributions in company stock.[288] The court cited earlier employer stock cases, which stated that a claim for breach of fiduciary duty in the circumstances of continued investment of an ESOP in company stock was a "narrow exception." "Decreasing stock prices, such as the 80% drop in value in *Kuper*, did not meet this narrow exception, whereas a 'precipitous decline' in stock price, 'combined with evidence that the ESOP fiduciaries knew the sponsoring company was being seriously mismanaged and facing impending collapse might.'"[289] The *Duke* court held:

283. EIAP investments in employer stock must be scrutinized for their suitability over the long term. *Wright*, 360 F.3d at 1099 (recognizing that beneficial effects of corporate actions "could likewise be generated years into the future").

284. *McKesson*, 2002 WL 31431588, at *5.

285. *Xcel*, 312 F. Supp. 2d at 1180.

286. *Sprint*, 388 F. Supp. 2d at 1223.

287. *See Duke*, 281 F. Supp. 2d at 795 (granting defendants' motion to dismiss).

288. *Id.*

289. *Id.* at 793.

> Nowhere do Plaintiffs explain why Duke Energy stock was 'unduly risky' . . . . Plaintiffs also make vague allegations of 'lack of internal controls' and some 'underreporting of profits,' but nowhere do Plaintiffs allege that Duke Energy was anything other than a viable, strong company with substantial assets. In fact, the materials Plaintiffs incorporate into their Complaint or upon which this court can take judicial notice demonstrate that Duke Energy is a solid, viable company, far from 'impending collapse,' and not in 'dire circumstances.' Under the circumstances, the court must hold that Plaintiffs' 'prudence claim' fails as a matter of law.[290]

In *Crowley v. Corning, Inc.*,[291] the court dismissed claims against the administrative committee because the plaintiffs "made only conclusory allegations insufficient to show that following the ESOP portions of the Plan was imprudent under the circumstances."[292] Distinguishing *Stein v. Smith*,[293] the *Crowley* court stated that plaintiffs did not allege that "Corning had any problems that could subject it to collapse, let alone that any fiduciary knew, or should have known, of such problems."[294]

In *Wright v. Oregon Metallurgical Corporation*, the court granted plan-administrator defendants' motion to dismiss the breach of fiduciary duty claim related to continued investment of ESOP in employer stock.[295] Applying the presumption of prudence, the court held that fluctuations in the stock price absent "unusual circumstances" are not enough to rebut the reasonableness presumption.[296] The financial information revealed that the stock was at all times a viable concern that continued to pay dividends to investors even though it did not meet analysts' expectations. Various economic factors affected its stock prices, including depressed stainless steel prices and weaker demand for its products. The stock was not in such dire circumstances that defendants' decision to hold it in compliance with the plan's requirement could have given rise to a claim for breach of fiduciary duty.[297]

In *LaLonde v. Textron, Inc.*, the district court, citing the *Moench* line of cases, granted the defendants' motion to dismiss

290. *Id.* at 794-95.
291. *Corning*, 234 F. Supp. 2d at 228.
292. *Id.* at 230. "In order to plead such a claim, however, it is fitting to require plaintiffs to allege underlying facts that demonstrate that the fiduciaries abused their discretion in continuing to hold such a high percentage of company stock." *McKesson*, 2002 WL 31431588, at *6.
293. *Stein*, 270 F. Supp. 2d at 166.
294. *Corning*, 2004 WL 763873, at *9.
295. *Wright*, 222 F. Supp. 2d at 1228.
296. *Id.* at 1229.
297. *Id.* at 1234.

the breach of fiduciary duty claim.[298] However, the First Circuit vacated this decision[299] and criticized the district court for setting a "hard-and-fast rule" in the standard it applied to the presumption.[300] Rather, the First Circuit noted that:

> Because the important and complex issue of law implicated by plaintiffs' claim is neither mature nor uniform, we believe that we would run a very high risk of error were we to lay down a hard-and-fast rule (or to endorse the district court's rule) based only on the statute's text and history, the sparse pleadings, and the few discordant judicial decisions discussing the issue we face.[301]

The court also stated that the district court failed to consider plaintiffs' allegations that Textron artificially inflated its stock price by concealing business problems, which were the later subject of federal securities lawsuits.[302]

V. TEEING UP THE ISSUE IN ERISA STOCK DROP CASES FOR THE SUPREME COURT

There is significant chaos in the courts with respect to the presumption of prudence. It is true that:

> [Courts] do not pick our rules of law full-blossomed from the trees. Every judge consulting his own experience must be conscious of times when a free exercise of will, directed of set purpose to the furtherance of the common good, determined the form and tendency of a rule which at that moment took its origin in one creative act.[303]

Although the Pension Protection Act attempted to provide a legislative fix to the problem of investment in employer stock, it does not appear to have completely remedied all employer stock issues. It is therefore time for the issue on the presumption of prudence to be settled by the Supreme Court. As noted earlier, six circuit courts have adopted the *Moench* presumption. However, there is still much disagreement as to when it applies and what it entails. The first issue is to determine to which stage the presumption applies. Does it apply at the motion to dismiss stage or is it an evidentiary standard to apply at the summary judgment stage? Further, there is disagreement with regard to what is required to rebut or overcome the presumption. Courts all over the country are espousing divergent views on these issues.

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298. *LaLonde*, 270 F. Supp. 2d at 277.
299. *LaLonde*, 369 F.3d at 6.
300. *Id.* at 6.
301. *Id.*
302. *Id.*
303. BENJAMIN NATHAN CARDOZO, A.L. SAINER, AND ROBERT F. WAGNER, LAW IS JUSTICE: NOTABLE OPINIONS OF MR. JUSTICE CARDOZO 428 (The Lawbook Exchange, Ltd. ed., 1999).

Issues involved in the fifty six Supreme Court ERISA decisions have included ERISA preemption, application of the abuse of discretion standard afforded to fiduciaries who have discretion over the plan, and the prudent person standard, although not in the context of plan investments. None of the cases have involved the interpretation of the ERISA prudence section in connection with plan investments and what standard should apply.

A. *The Presumption of Prudence Should Apply and at the Pleading Stage*

In the latest round of circuit court holdings regarding the application of the *Moench* presumption, the hat tips in favor of defendants.[304] Recent victories for defendants have taken place in the Second and Eleventh Circuits.[305] However, there are circuits that have not formally adopted the presumption and there is a clear conflict with the Sixth Circuit about the stage to which the presumption applies.

1. *Fiduciaries Are Entitled to Deference Under* Firestone

Plaintiffs have argued that the *Moench* presumption has no statutory basis in ERISA.[306] However, the Supreme Court has interpreted ERISA and granted fiduciaries deference in benefit determination cases, beginning with *Firestone Tire & Rubber Co. v. Bruch*.[307] *Firestone* states that fiduciary deference not only applies to benefit cases, but also to cases where fiduciaries have discretion "to construe the terms of the plan."[308] While these cases do not involve the investments of pension plan assets, let alone the ability to invest in the employer's common stock via a defined contribution plan specifically, the language in *Firestone* should nevertheless apply to plan fiduciaries investing in employer stock.

Under *Firestone*, a de novo standard applies "unless the benefit plan gives the fiduciary discretionary authority to construe the terms of the plan," in which case the standard of review is for abuse of discretion.[309] This deferential treatment has subsequently been upheld by the Supreme Court in *Conkright v. Frommert*.[310]

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304. *Lanfear*, 2012 WL 1580614 (11th Cir. 2012).
305. *Citigroup*, 662 F.3d at 137.
306. Herman v. Nationsbank Trust Co., 126 F.3d 1354, 1371 (11th Cir. 1997) (stating that following an ESOP plan provision regarding tendering shares should not be reviewed for merely abuse of discretion).
307. *Firestone*, 489 U.S. at 115.
308. *Id.*
309. *Id.*
310. Conkright v. Frommert, 130 S. Ct. 1640, 1660 (2010) (instructing the district court to apply a deferential standard of review to the plan administrator's interpretation of the plan on remand).

The Supreme Court has explained the ERISA considerations and concerns for an abuse of discretion standard:

> Congress enacted ERISA to ensure that employees would receive the benefits they had earned, but Congress did not require employers to establish benefit plans in the first place. We have therefore recognized that ERISA represents a "'careful balancing' between ensuring fair and prompt enforcement of rights under the plan and the encouragement of the creation of such plans." Congress sought to "create a system that is [not] so complex that administrative costs, or litigation expenses, unduly discourage employers from offering [ERISA] plans in the first place." ERISA "induc[es] employers to offer benefits by assuring a predictable set of liabilities, under uniform standards of primary conduct and a uniform regime of ultimate remedial orders and awards when a violation has occurred."[311]

This, along with ERISA's exception from diversification of employer stock and the case law adopting it, supports the presumption of prudence.[312] Accordingly, the presumption should be applied.

Presumptions have long been relied upon in other areas of law. They are created out of "considerations of fairness, public policy, and probability, as well as judicial economy."[313] One of the most common presumptions is the business judgment rule, which provides that courts "will not interfere with internal management and substitute its judgment for that of D & Os to enjoin or set aside the transaction or to surcharge the D & Os for any resulting loss."[314] The test is met when "there is no showing of bad faith, negligence, or gross abuse of discretion."[315]

Even the dissent in *Citigroup* believed that a deferential standard should apply in the corporate context, just not to ERISA plan fiduciaries.[316] However, the dissent in that case did not delve into the ERISA policy considerations that the Supreme Court has established as mentioned above. Thus, the presumption of prudence should be adopted by the Supreme Court.

2. *Plausibility - The Heightened Pleading Standard*

Once it is established that the presumption should apply, it then becomes necessary to determine the stage in the litigation to

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311. *Id.* at 1648-1649.
312. *Quan*, 623 F.3d at 882.
313. Basic v. Levinson, 485 U.S. 224, 246-247 (1988).
314. HARRY G. HENN AND JOHN R. ALEXANDER, LAWS OF CORPORATIONS 661 (West Publishing, 3d ed. 1983).
315. *Id.* at 663.
316. *Citigroup*, 662 F.3d at 149-50.

which the presumption applies. In *Pfeil v. State Street*[317] the Sixth Circuit clearly pronounced the distinction between its standard and that of the Second Circuit's as set forth in *Citigroup*.[318] The *Pfeil* court held that the *Moench* presumption is an evidentiary standard, not a pleading requirement.

By contrast, the *Citigroup* court stated that the "presumption is not an evidentiary presumption; it is a standard of review applied to the decision made by an ERISA fiduciary." This is the same approach also taken by the Third[319] and Eleventh Circuits.[320]

The Sixth Circuit acknowledged that it adopted the *Moench* presumption in so far as fiduciaries of ESOPs or EIAPs with employer stock operate under two hats and therefore should be granted an abuse of discretion standard of review.[321] That presumption, however, does not apply at the pleading stage. The court recognized "that many district courts in this Circuit have confronted the issue and reached conflicting decisions."[322] Notably, the *Kuper* court espoused the presumption as an "evidentiary presumption, and not a pleading requirement,"[323] as it was decided on a fully developed evidentiary record. It further citied the Supreme Court case *Swierkiewicz v. Sorema*.[324]

However, all of the cases cited by the Sixth Circuit were decided prior to adoption of the pleading requirements espoused in *Twombly* and *Iqbal*. *Sorema*, for example, required only that the plaintiff give the defendant some notice of the plaintiff's claims and the grounds for it.[325] In support of its holding, the Supreme Court relied on the liberal pleading standard articulated in *Conley v. Gibson*. Under *Conley*, a motion to dismiss would be granted

317. *Pfeil*, 671 F.3d at 591-95.

318. *Citigroup*, 662 F.3d at 139 ("Where plaintiffs do not allege facts sufficient to establish that a plan fiduciary has abused his discretion, there is no reason not to grant a motion to dismiss.").

319. *Edgar*, 503 F.3d at 349 (holding that the *Moench* presumption applies at the motion to dismiss stage because there is "no reason to allow [the] case to proceed to discovery when, even if the allegations [were] proven true, [the plaintiff could not] establish that the defendants abused their discretion.").

320. *Lanfear*, 2012 WL 1580614, at *10 (applying the *Moench* presumption at the motion to dismiss stage).

321. *Pfiel*, 671 F.3d at 597

322. *Id.* (noting that "[a]t least fourteen district courts in this Circuit have addressed this issue . . ." and have "overwhelmingly declined to apply the presumption of prudence" when considering a motion to dismiss); Dudenhoeffer v. Fifth Third Bancorp, 757 F. Supp. 2d 753, 758-59 (S.D. Ohio 2010) (holding that the *Moench* presumption applied at the pleadings stage in light of *Twombly* and *Iqbal*).

323. *Pfiel*, 671 F.3d at 599.

324. Swierkiewicz v. Sorema, N.A., 534 U.S. 506, 510 (holding that a plaintiff was not required to plead all the *prima facie* elements of the *McDonnell Douglas* evidentiary framework in order to survive a motion to dismiss).

325. *Id.*

only if the plaintiff fails to prove facts supporting the claim entitling the plaintiff to relief.[326] But, keeping with the theme of this Article, the *Conley* standard of pleading has since been put into "retirement" by the Supreme Court in *Twombly*.[327]

On the other hand, the Second Circuit in *Citigroup* found that "the presumption is not an evidentiary presumption; it is a standard of review applied to the decision made by an ERISA fiduciary."[328] The court followed the plausibility standard set forth in *Twombly* and *Iqbal*: the complaint must contain sufficient factual matter, accepted as true, to state a claim for relief that is plausible.[329] Even the Seventh Circuit, which has not formally adopted the presumption, has recognized that under *Twombly*, more is required than just labels and conclusions. Specifically, the court stated "[a] conclusory statement that all defendants should have known specific facts about a company is generally insufficient to state a claim; it must be alleged that each defendant was in a position to know or learn of the information."[330]

As discussed previously, the *Moench* presumption is to plan fiduciaries what the business judgment rule is to D & Os, and Delaware Courts have required that the plaintiffs overcome the business judgment rule at the motion to dismiss stage.[331] While the Federal Courts were slow to follow,[332] they now apply the business judgment rule at the motion to dismiss stage as well.[333] Thus, the *Moench* presumption for plan fiduciaries should also apply at the motion to dismiss stage.

326. Conley v. Gibson, 355 U.S. 41, 47 (1957).

327. Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 563 (2007).

328. *Citigroup*, 662 F.3d at 129.

329. *Id.* at 141; *Twombly*, 550 U.S. at 556-57 (holding that plaintiffs must allege facts sufficient to suggest their claims are plausible as against other theories explaining the alleged conduct); Ashcroft v. Iqbal, 556 U.S. 662, 679 (2009) (stating that *Twombly*'s heightened pleading standard applies to all claims pled under the Federal Rules of Civil Procedure).

330. *Pugh*, 521 F.3d at 695.

331. J.P. Morgan Chase & Co. v. S'holder Litig., 906 A.2d 808, 824 (Del. Ch. 2005).

332. Fleet Nat'l Bank v. Bayle, 2005 WL 2455673, at *16 (E.D. Pa. 2005) (applying business judgment rule at motion to dismiss stage).

333. Robotic Vision Sys., Inc., 374 B.R. 36, 48-49 (2007) ("In asserting breach of fiduciary duty claims, it should have been obvious . . . that the business judgment rule would be implicated. For that reason, the [plaintiff] was required to plead that he can overcome the presumption created by the business judgment rule in order to survive a motion to dismiss under Fed. R. Civ. P. 12(b)(6)."); Desimone v. Barrows, 924 A.2d 908, 929 (Del. Ch. 2007) (acknowledging that the Supreme Court "has now embraced the pleading principle that Delaware courts have long applied . . ."); Dixon v. ATI Ladish LLC, 667 F.3d 891, 894 (7th Cir. 2012).

B. *The Proper Standard for Rebutting the Presumption*

Plaintiffs need not necessarily prove that a company is "on the brink of bankruptcy" in order to rebut the fiduciary presumption, but they must demonstrate more than possible fraud or corporate wrongdoing.[334] "Mere fluctuations, even those that trend downward significantly, [were] insufficient to establish the requisite imprudence to rebut the *Moench* presumption."[335]

Courts have focused on developing the proper method for plaintiffs to rebut the *Moench* presumption in order to preserve the true purpose of ERISA. Indeed, the Second Circuit recently explained in *Citigroup* that an overreaching irrefutable presumption, "would leave employees' retirement savings that are invested in [employer stock] without any protection at all – a result that Congress sought to avoid in enacting ERISA."[336] Accordingly, courts allow plaintiffs to rebut the presumption by showing that it was an "abuse of discretion" to allow continued investment in employer stock while the employer was in "a 'dire situation' that was objectively unforeseeable by the settlor," and that the fiduciary "knew or should have known" about the dire situation.[337]

In deciphering when a fiduciary has an affirmative obligation to override the EIAP or ESOP plan terms, the *Moench* court held that this responsibility exists where "owing to circumstances not known to the [plan] settlor and not anticipated by him, maintaining the investment in company stock would defeat or substantially impair the accomplishment of the purposes of the [plan]."[338] In applying this standard, the *Citigroup* court held that it would not be pragmatic for settlor administrators to intend for fiduciaries to divest the plan of EIAP or ESOP investments at the first sign of trouble, but rather only in cases where the situation is "dire."[339] In cases where reasonable fiduciaries may disagree regarding overriding a plan's EIAP or ESOP investment mandate, the court affirmed that fiduciaries should be presumptively shielded and only responsible in the most "dire" of situations.[340]

The *Citigroup* court explained that, in order to rebut the presumption of reasonableness, the plaintiff might not necessarily have pled the company's impending collapse, but must allege a dire situation. The court held that the plaintiffs failed to allege facts "sufficient to show that the defendants either know or should have known that Citigroup was in the sort of dire situation that

334. *Edgar*, 503 F.3d at 348-49.
335. *Id.* at 349.
336. *Id.*
337. *Id.* at 348.
338. *Moench*, 62 F.3d at 568.
339. *Citigroup*, 662 F.3d at 140.
340. *Id.*

required them to override Plan terms in order to limit participants' investments in Citigroup stock."[341] The court further added that even if the fiduciaries had investigated the company's exposure to the subprime mortgage market, the dire situation the company was in was not foreseeable.[342]

The Sixth Circuit clearly stated that it was not adopting a rebuttal presumption requiring a dire situation or that the company be on the brink of collapse. "The rebuttal standard adopted in this Circuit, and one which we are bound to follow, requires a plaintiff to prove that 'a prudent fiduciary acting under similar circumstances would have made a different investment decision.'"[343] The court reasoned that this sets out an abuse of discretion standard forcing plaintiffs to carry a demanding burden, while at the same time providing the "flexibility to address the unique circumstances that might give rise to a breach-of-duty claim against an ESOP fiduciary, whether the company is one with small capitalization or a corporation 'too big to fail.'"[344] The court concluded that "the better course is to permit the lower courts to consider the presumption in the context of a fuller evidentiary record rather than just the pleadings and their exhibits.[345] The Sixth Circuit stands alone on this issue, that the proper rebuttable standard that of a dire situation.

VI. CONCLUSION

In the end, while the MPT is still considered a viable investment theory, it may require some tweaking to account for the current economic environment. Although no particular investment theory may be considered better than another, plan fiduciaries should at least consider some type of investment theory in viewing the plan's investment portfolio and how employer securities add value to the mix.

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341. *Id.* at 141. An example of a dire situation can be found in *Peabody v. Davis*, where the court held that "a widely known and permanent change in the regulatory environment had undermined [the company's] core business model," and accordingly, investing in the company's stock became imprudent. Peabody v. Davis, 636 F.3d 368, 375 (7th Cir. 2011). The idea that a "regulatory" change could eviscerate a company's stated business model and purpose was central to the Seventh Circuit's holding that this was a "dire" situation. *Id.* In declining to address the applicability of the *Moench* presumption, the *Peabody* court stressed that the SEC's decimalization rule was so devastating to the defendant company's profit margins from 2001 to 2003 that no prudent fiduciary could continue an investment in this stock during that time. *Id.* From 2001 to 2003 the company's profit margin had declined by approximately 70-80%. *Id.*

342. *Id.*

343. *Pfiel*, 671 F.3d at 599.

344. *Id.*

345. *Id.* at 600.

In connection with litigation, the ERISA employer stock cases have grappled with the apparent conflict in the use of the *Moench* presumption at the motion to dismiss stage as well as whether plaintiffs must plead an "impending collapse" of the company to overcome the presumption. Courts should apply the presumption at the motion to dismiss stage as well as require plaintiffs to show "impending collapse" to overcome the *Moench* presumption. While questions as to the application of the *Moench* presumption to EIAP plans have not been solidified, the issues of investment choice and company information available to the employees, as well as whether company investment is mandated under the plan are strong considerations. However, what is clear is that the courts need to review the fiduciary's duties and the "dire circumstances" based on the information available at the time of the alleged breach, not on hindsight. Accordingly, having this uniform standard of prudence applied early in the litigation would certainly filter out meritless cases, resulting in freeing plan fiduciaries and D & Os from needless litigation and loosening courts' dockets.