No. 18-1165

In the Supreme Court of the United States

RETIREMENT PLANS COMMITTEE OF IBM, ET AL.,
Petitioners,

v.

LARRY W. JANDER, ET AL.,
Respondents.

On Writ of Certiorari to the United States
Court of Appeals for the Second Circuit

BRIEF OF AMICI CURIAE AMERICAN ASSOCIATION FOR JUSTICE AND PUBLIC JUSTICE IN SUPPORT OF RESPONDENTS

BRUCE STERN
President
AMERICAN ASSOCIATION
FOR JUSTICE
777 6th Street, NW
Suite 200
Washington, DC 20001
(202) 944-2810
bruce.stern@justice.org

LEAH M. NICHOLLS
PUBLIC JUSTICE, P.C.
1620 L Street NW, Suite 630
Washington, DC 20036
(202) 797-8600
LNicholls@publicjustice.net

MATTHEW W.H. WESSLER
Counsel of Record
GREGORY A. BECK
GUPTA WESSLER PLLC
1900 L Street, NW
Suite 312
Washington, DC 20036
(202) 888-1741
matt@guptawessler.com

Counsel for Amici Curiae

October 1, 2019

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

INTEREST OF AMICI CURIAE[1]

The American Association for Justice ("AAJ") is a national, voluntary bar association established in 1946 to strengthen the civil justice system, preserve the right to trial by jury, and protect access to the courts for those who have been wrongfully injured. With members in the United States, Canada, and abroad, AAJ is the world's largest plaintiff trial bar. AAJ's members primarily represent plaintiffs in personal injury actions, employment rights cases, consumer cases, and other civil actions, including ERISA actions. Throughout its more than seventy-year history, AAJ has served as a leading advocate for the right of all Americans to seek legal recourse for wrongful conduct.

Public Justice is a national public interest law firm dedicated to pursuing justice for the victims of corporate and governmental abuses. Public Justice specializes in precedent-setting and socially significant cases designed to advance consumers' and victims' rights, civil rights and civil liberties, occupational health and workers' rights, the preservation and improvement of the civil justice system, and the protection of the poor and powerless. This case is of particular interest to Public Justice because it concerns the pleading requirements that workers must satisfy to use the civil justice system to enforce their federal statutory rights; unjustifiably stringent pleading standards interfere with workers' ability to get into court to hold ERISA fiduciaries liable for breaches of their duties.

---

[1] This brief was not authored in whole or in part by counsel for a party and no one other than amici curiae and their counsel made a monetary contribution to the preparation or submission of this brief. All parties have consented to the filing of this brief; letters of consent have been lodged with the Clerk.

AAJ and Public Justice agree, for the reasons set forth in the respondents' brief, that this Court should apply *Fifth Third Bancorp v. Dudenhoeffer*, 573 U.S. 409 (2014), to affirm the Second Circuit's decision below., AAJ and Public Justice file this brief to urge that the Court, in doing so, use caution in setting forth the boundaries of the rules set forth in *Dudenhoeffer*. Lower courts have already expanded those rules well beyond the circumstances that originally justified them. The Court should take this opportunity to cabin *Dudenhoeffer* before it becomes a general standard applicable in almost all ERISA cases.

INTRODUCTION AND SUMMARY OF ARGUMENT

A fiduciary's duties of prudence and loyalty under ERISA are the highest known to law. In *Dudenhoeffer*, this Court held that those duties apply with full force to fiduciaries of employee stock ownership plans (ESOPs). 573 U.S. 409. The Court declined to adopt a presumption of prudence for such fiduciaries. Nor did it require new pleading standards for claims in ESOP cases. All the Court did was identify considerations relevant to the plausibility of a claim under the particular circumstances of that case, where the plaintiffs alleged that ESOP fiduciaries breached their duty of prudence by overvaluing a publicly traded stock.

Since *Dudenhoeffer* was decided, however, lower courts have applied it in contexts far afield from those original circumstances, where application of the "context-specific" considerations this Court identified no longer makes sense. Taken together, these cases extend *Dudenhoeffer* not only to most allegations of imprudence regarding publicly traded stock, but even to non-public stock as well. Left unchecked, the lower courts are likely to continue inching *Dudenhoeffer* toward a general rule requiring allegations of "special circumstances" in nearly every ESOP case. In doing so, they will effectively bring back the presumption of prudence that *Dudenhoeffer* rejected.

This Court should take this opportunity to rein in these lower courts by reiterating the limits of its holding in *Dudenhoeffer*. In particular, the Court should clarify that *Dudenhoeffer* has no application to claims involving investments that are not available in a public market. In addition, it should limit *Dudenhoeffer*'s scope to allegations that fiduciaries breached their duty of prudence by over- or underpaying for stock. The Court, in other words, should make clear that *Dudenhoeffer* applies only in those circumstances that rendered its holding relevant in the first place.

ARGUMENT

I. ERISA's stringent fiduciary duties are limited by the considerations in *Dudenhoeffer* only in the specific circumstances where this Court held those considerations relevant.

ERISA's overriding purpose is "to protect beneficiaries of employee benefit plans." *Slupinski v. First Unum Life Ins. Co.*, 554 F.3d 38, 47 (2d Cir. 2009). Congress's concern was "the mismanagement of funds accumulated to finance employee benefits and the failure to pay employees benefits from accumulated funds." *Mass. v. Morash*, 490 U.S. 107, 115 (1989). The "inadequacy" of existing management standards, it found, was a threat to "the soundness and stability of plans." 29 U.S.C. § 1001(a). Congress thus imposed safeguards intended to "insure against the possibility that the employee's expectation of the benefit would be defeated through poor management." *Morash*, 490 U.S. at 115.

To that end, the law "imposes high standards of fiduciary duty upon those responsible for administering an ERISA plan and investing and disposing of its assets." *Martin v. Feilen*, 965 F.2d 660, 664 (8th Cir. 1992). Those standards include the duty of loyalty and the duty of prudence, which requires that fiduciaries act "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use." 29 U.S.C. § 1104(a)(1)(B). Courts have characterized these fiduciary duties as "the highest known to the law." *Donovan v. Bierwirth*, 680 F.2d 263, 272 n.8 (2d Cir. 1982); *see also Jones v. Am. Gen. Life & Acc. Ins. Co.*, 370 F.3d 1065, 1071 (11th Cir. 2004).

In *Dudenhoeffer*, this Court held that the duty of prudence applies equally to the fiduciary of an employee stock ownership plan (ESOP)—that is, a plan that invests primarily in an employer's stock. 573 U.S. at 412. The Court declined to recognize a "presumption of prudence" for ESOP fiduciaries, holding that—although the statute exempts them from a duty to diversify beyond the employer's stock—they are otherwise "subject to the same duty of prudence that applies to ERISA fiduciaries in general." *Id.* The Court also declined to impose a "heightened pleading standard" to ESOP cases. *Allen v. GreatBanc Tr. Co.*, 835 F.3d 670, 674 (7th Cir. 2016). Instead, it required plaintiffs to plead only "the context necessary to show a plausible claim for relief." *Id.*

Dudenhoeffer also identified some "considerations" bearing on the plausibility of the specific claims there—that ESOP fiduciaries had breached their duty of prudence by overvaluing a publicly traded stock. 573 U.S. at 426. The Court did not, however, adopt those considerations as general rules for ESOP cases. Rather, it emphasized that whether a complaint states a plausible claim for breach of the duty of prudence "will necessarily be context specific," turning "on 'the circumstances … prevailing' at the time the fiduciary acts." *Id.* at 425 (quoting 29 U.S.C. § 1104(a)(1)(B)). Rather than imposing a per se rule, *Dudenhoeffer* therefore requires "careful, context-sensitive scrutiny of a complaint's allegations." *Id.*

II. This Court should expressly limit *Dudenhoeffer* to allegations involving publicly traded companies.

Although *Dudenhoeffer* involved investments in a publicly traded stock, courts have also applied its reasoning to investments in non-public companies. *See, e.g.*, *Hill v. Hill Bros. Constr. Co., Inc.*, 2016 WL 1252983, at *4 (N.D. Miss. 2016). Those cases misapply *Dudenhoeffer*'s reasoning and badly undermine settled standards of fiduciary duty under ERISA. This Court should take this opportunity to make clear that they are wrongly decided.

A. *Dudenhoeffer* held that, "[t]o state a claim for breach of the duty of prudence on the basis of inside information, a plaintiff must plausibly allege an alternative action that the defendant could have taken that would have been consistent with the securities laws and that a prudent fiduciary in the same circumstances would not have viewed as more likely to harm the fund than to help it." 573 U.S. at 428. As the Court explained, trading (or refraining from trading) on such information could violate the federal securities laws, and the duty of prudence "does not require a fiduciary to break the law." *Id.* at 428. Moreover, there is a risk that "the market might take" a decision to stop purchases of the company's stock "as a sign that insider fiduciaries viewed the employer's stock as a bad investment" and thus that such a decision "would do more harm than good to the fund by causing a drop in the stock price and a concomitant drop in the value of the stock already held by the fund." *Id.* at 430.

Although *Dudenhoeffer* was talking about public stock, lower courts have applied its "alternative action" test to stock in companies that are not public. *See, e.g.*, *Hill*, 2016 WL 1252983. The district court in *Hill*, for example, dismissed the plaintiffs' claim that fiduciaries had overpaid for private stock—the price of which was set by a neutral third party rather than a public market—because the plaintiffs failed to allege an "alternative action" under *Dudenhoeffer*. *Id.* at *9. Other courts have followed suit. *See Vespa v. Singler-Ernster, Inc.*, 2016 WL 6637710, at *2 (N.D. Cal. 2016); *Fish v. GreatBanc Trust Co.*, 2016 WL 5923448, at *53 n.24 (N.D. Ill. 2016).

Those decisions, however, make no sense. The securities laws do not apply to a company that is privately held. *See Allen*, 835 F.3d at 679 (noting that "the need to protect fiduciaries from running up against insider trading law … has no application to the private stock context"). Thus, no purpose would be served by requiring plaintiffs to allege an alternative action "consistent with the securities laws." *Dudenhoeffer,* 573 U.S. at 428. And when a stock is not publicly traded, there is no risk of a market reaction causing a drop in stock price. There is thus also no need for an allegation that the alternative action would not have been "more likely to harm the fund than to help it." *Id.*

The court in *Hill* acknowledged that "none of the situations outlined by [*Dudenhoeffer*] are relevant for closely held corporations." 2016 WL 1252983 at *5. It concluded, however, that this Court did "not necessarily preclude the application of the alternative action pleading standard" in such a case. *Id.* at *5. Although there was no "potential for conflict" with the securities laws, the court held that "a potential for conflict did exist due to the alleged fiduciaries' role as directors and/or officers" of the company. *Id.* at *6. The existence of those "dual loyalties," it concluded, required the plaintiffs to allege an alternative action that the fiduciaries could have taken that would not have conflicted with their duties until either role. *Id.*

Petitioners, and their amici, urge this Court to embrace essentially that same understanding. In their view, affirming the Second Circuit's decision would "eviscerate" a fiduciary's ability to wear "two hats" and "alternate between corporate and fiduciary roles." Amicus Br. of Securities Industry, at 14; *see also* IBM Br. at 26–27. They see the Second Circuit's decision to allow the claims to move past the pleading stage as tantamount to a "rule" requiring "fiduciaries to act always in their fiduciary capacity" and never in their corporate capacity. Amicus Br. Securities Industry at 14. And they suggest that the risks of allowing a case like this one to proceed "will naturally prompt employers to drop" ESOPs. *Id.* at 26. As a result, they urge the Court to impose such a high pleading bar so as to foreclose breach claims against ESOP fiduciaries. *See id.* at 25.

That approach, however, sets all the wrong incentives. When ESOP fiduciaries are also company insiders, "the potential for disloyal self-dealing and the risk to the beneficiaries from undiversified investing are inherently great." *Martin*, 965 F.2d at 670–71. Fiduciaries with such dual loyalties thus face a "risk of liability" unless they "obtain[] the impartial guidance of a disinterested outside advisor to the plan" when making investment decisions. If they do not obtain such guidance, courts subject their decisions to careful scrutiny to ensure that they fulfilled their fiduciary duties "with the utmost care and fairness." *Id.* at 670. Requiring plaintiffs to allege an alternative action consistent with both roles, however, would allow fiduciaries to hide behind their dual loyalties, leaving them with no incentive to seek impartial advice. Rather than subjecting their decisions to careful scrutiny, a fiduciary's conflicts would allow them to escape liability altogether.

Decisions like *Hill* are possible because this Court in *Dudenhoeffer* never expressly "specified that the 'alternative action' standard is to be applied to ESOPs of publicly-traded entities only." *Hill*, 2016 WL 1252983 at *5. The Court should therefore make that express statement in this case.

B. *Dudenhoeffer* also held that, "where a stock is publicly traded, allegations that a fiduciary should have recognized from publicly available information alone that the market was over- or undervaluing the stock are implausible as a general rule, at least in the absence of special circumstances." 573 U.S. at 426. That is because fiduciaries have "little hope of outperforming the market based solely on their analysis of publicly available information." *Id.* A fiduciary is thus usually "not imprudent to assume that a major stock market provides the best estimate of the value of the stocks traded on it that is available to him." *Id.* at 427.

By its plain terms, that "special circumstances" test is confined to cases "where a stock is publicly traded." *Id.* at 426. Like the "alternative action" requirement, however, the rule has been extended beyond its logical foundations. In *Allen v. Greatbanc Trust Co.*, the district court relied on *Dudenhoeffer* in dismissing the plaintiffs' claim that ESOP fiduciaries overpaid for stock in a privately held company. 2015 WL 5821772, at *3 (N.D. Ill. 2015). Although the court recognized that *Dudenhoeffer* involved "publicly traded stock," it nevertheless held that the plaintiffs were required to allege "special circumstances" showing that reliance on the stock's assessed value was imprudent. *Id.* That requirement was necessary, the court wrote, to protect fiduciaries from "discovery costs" every time "the value of an asset declines." *Id.*

The district court's extension of *Dudenhoeffer* in *Allen* is, again, nonsensical. *Dudenhoeffer*'s holding that fiduciaries "may, as a general matter, … prudently rely on the market price" of a security, 573 U.S. at 427, works only because "the market price of shares traded on well-developed markets reflects all publicly available information." *Basic Inc. v. Levinson*, 485 U.S. 224, 246 (1988). The price of a nonpublic company, in contrast, is not set by the market. *See Coburn v. Evercore Tr. Co., N.A.*, 844 F.3d 965, 970 n.1 (D.C. Cir. 2016). Thus, it is "plausible that a fiduciary could act imprudently by not acting on publicly available information because there is less assurance that that information has already been incorporated into the security price." *Id.*

Ultimately, the Seventh Circuit reversed the decision in *Allen*. Private stock, the court wrote, has "no market price," and thus there is "no reason to apply any 'special circumstances' rule." *Allen*, 835 F.3d at 679. Nevertheless, this Court should reiterate that the rule in *Dudenhoeffer* is limited to publicly traded stock to ensure that future courts do not repeat the mistake of the district court in *Allen*.

III. The Court should also limit *Dudenhoeffer* to allegations that a fiduciary over- or undervalued an investment.

Dudenhoeffer applied its "special circumstances" test in the context of claims that an ESOP's stock was inflated in value, and its reasoning makes sense only in the context of such claims. There are many possible ERISA claims, however, that do not involve allegations of "over- or undervaluing" a stock. 573 U.S. at 426. Lower courts have already applied *Dudenhoeffer* in some of those contexts. This Court should make clear that they are wrong to do so.

A. *Dudenhoeffer* recognized that it usually "is not imprudent" for a fiduciary "to assume that a major stock market … provides the best estimate of the value of the stocks traded on it that is available to him." *Id.* at 427. The decision thus forecloses claims that a fiduciary violated the duty of prudence by failing to beat the stock market, at least in the absence of special circumstances. *See id.* But there are other ways that investments can be imprudent that do not involve the failure to second-guess the market. In particular, the claim that a stock is excessively risky does not depend on an allegation that the stock is overpriced. Even assuming that the price of a risky stock is efficient, the stock may still be an imprudent investment for a retirement plan.

Why is that so? It is true that, all else being equal, the market will value risky stocks at a lower price. But price also incorporates potential reward, meaning that the price of a very risky stock will be higher if the potential return is also high. *See Tatum v. RJR Pension Inv. Comm.*, 855 F.3d 553, 565 n.10 (4th Cir. 2017). A claim that such a stock is excessively risky does not require second-guessing market price. The market may be willing to gamble on a small chance of a large payout, but that does not make it a prudent investment strategy for a fund on which employees depend for their financial security. *Summers v. State Street Bank & Trust Co.*, 453 F.3d 404, 409 (7th Cir. 2006).

An investment may also be imprudently risky if it is excessively volatile. *See DiFelice v. U.S. Airways*, Inc., 497 F.3d 410, 424 (4th Cir. 2007). Again, such a claim does not require second-guessing the market. A stock that wildly fluctuates in value may reflect the best valuation based on public information available at any given time. But a fund that invested in such a stock would face the risk that a sudden downturn could render the plan's assets unavailable. Even assuming that it is efficiently priced, such a stock therefore may not be a prudent investment choice.

Moreover, prudent fiduciaries do not consider just price when choosing an investment, but also "the character and aim of the particular plan and decision at issue and the circumstances prevailing at the time." *Bussian v. RJR Nabisco, Inc.*, 223 F.3d 286, 299 (5th Cir. 2000). For a plan with beneficiaries near retirement age, a highly risky investment may be especially imprudent because, in the event that the stock loses money, there will be little time for it to recover. *See GIW Indus., Inc. v. Trevor, Stewart, Burton & Jacobsen, Inc.*, 895 F.2d 729, 732 (11th Cir. 1990) (upholding a duty-of-prudence claim based not on the fiduciary's "investment strategy from the vantage point of hindsight," but on failure to consider "the anticipated needs of the fund").[2]

---

[2] ESOP fiduciaries are exempt from the duty to diversify plan investments "so as to minimize the risk of large losses." *Dudenhoeffer*, 573 U.S. at 417 (2014). Some courts, however, have applied the "special circumstances" test to fiduciaries of non-ESOP plans, who are not exempt from the diversification requirement. *See Usenko v. MEMC LLC*, 926 F.3d 468, 474–75 (8th Cir. 2019). At least in those cases, prudence also requires consideration of a risky investment's role "within the overall plan portfolio." *Tatum v. RJR Pension Inv. Comm.*, 761 F.3d 346, 370 (4th Cir. 2014). In some circumstances, investing "in a risky security as part of a diversified portfolio" can be "an appropriate means to increase return while minimizing risk." *DiFelice*, 497 F.3d at 423. But it would probably not be prudent to (continued …)

Courts, however, have applied the "special circumstances" test to such claims anyway, reasoning that, in an efficient market, a stock's price will have already incorporated information bearing on its risk. In *Rinehart v. Lehman Bros. Holdings Inc.*, for example, the court dismissed claims that the fiduciaries had breached their duty of prudence based on the "excessive risk" of their investments. 817 F.3d 56, 65–66 (2d Cir. 2016). The "purported distinction between claims involving 'excessive risk' and claims involving 'market value,'" the court wrote, "is illusory." *Id.* at 66; *see also Coburn*, 844 F.3d at 971; *Pfeil v. State Street Bank and Trust Co.*, 806 F.3d 377, 386 (6th Cir. 2015).

To limit these kinds of excessive-riskiness claims to "special circumstances" would, in ordinary cases, let fiduciaries off the hook for gambling away the assets of beneficiaries with risky investments. That would defeat ERISA's core purpose of preventing the "possibility that the employee's expectation of the benefit would be defeated through poor management." *Morash*, 490 U.S. at 115. Indeed, the Second Circuit has held that "special circumstances" are required not just for allegations of excessive risk, but for "*all* allegations of imprudence based upon public information." *Rinehart*, 817 F.3d at 66. If that were true, it would mean that there is no such thing as an imprudent public stock.

The lower courts have squarely blamed *Dudenhoeffer* for those results, claiming that the decision "foreclose[d] breach of prudence claims based on public information irrespective of whether such claims are characterized as based on alleged overvaluation or alleged riskiness of a

---

invest *all* of a plan's resources in such a stock, even assuming that the stock price accurately reflects the investment's risks.

stock." *Id.*; *see also Coburn*, 844 F.3d at 971 (stating that the court has "no license to deviate" from *Dudenhoeffer*'s holding). This Court should make clear that *Dudenhoeffer* requires no such thing.

B. Another example of claims where requiring "special circumstances" makes little sense are claims based on a fiduciary's failure to adequately investigate or monitor an investment. Courts have recognized that "[w]hether an ERISA fiduciary has acted prudently requires consideration of both the substantive reasonableness of the fiduciary's actions and the procedures by which the fiduciary made its decision." *Fish v. GreatBanc Tr. Co.*, 749 F.3d 671, 680 (7th Cir. 2014). *Dudenhoeffer*, which involved "an ESOP fiduciary's *decision* to buy or hold the employer's stock," was about substantive reasonableness. 573 U.S. at 412. But the duty of prudence depends "not only on the merits of a transaction, but also on the thoroughness of the investigation into the merits of that transaction." *DiFelice*, 497 F.3d at 418.

To demonstrate procedural prudence, fiduciaries must "engage[] in a reasoned decision-making process" and use "appropriate methods to investigate the merits of the investment and to structure the investment." *Tatum*, 761 F.3d at 356. And after an investment decision has been made, they must continue to "monitor the prudence of their investment decisions to ensure that they remain in the best interest of plan participants." *Id.* at 358. As this Court recognized in *Tibble v. Edison Int'l*, the duty of prudence thus requires a fiduciary "to conduct a regular review of its investment with the nature and timing of the review contingent on the circumstances." 135 S. Ct. 1823, 1827–28 (2015). And that requirement "exists separate and apart from the trustee's duty to exercise prudence in selecting investments at the outset." *Id.* at 1828.

In *Usenko v. MEMC LLC*, the Eighth Circuit affirmed dismissal of a failure-to-monitor claim under *Dudenhoeffer*'s "special circumstances" test, holding that it amounted to a claim that the fiduciaries "failed to 'outperform the market.'" 926 F.3d at 474–75 (quoting *Dudenhoeffer*, 573 U.S. at 427). But that is nonsense. The allegation that a fiduciary failed to adequately investigate an investment does not require the fiduciary to have made the "decision that in the light of hindsight proves best." *Tatum*, 761 F.3d at 369. All that is required is a "reasoned decision-making process." *Id.* A "fiduciary need not be prescient about future stock-value movements" to use "the procedures that a prudent fiduciary would use." *Allen*, 835 F.3d at 679.

For that reason, the D.C. Circuit in *Coburn v. Evercore Trust Co.* suggested that *Dudenhoeffer*'s "special circumstances" test is inapplicable to a failure-to-monitor claim under *Tibble*. 844 F.3d at 970. As explained by a concurrence in that case, "*Dudenhoeffer* involves the substance of investment decisions, while *Tibble* has to do with a fiduciary's obligation to monitor those decisions." *Id.* at 977 (Edwards, J., concurring). The theories thus "embrace distinct, albeit not mutually exclusive, causes of action for violations of a fiduciary's duty." *Id.*; *see also Brannen v. First Citizens Bankshares Inc.*, 2016 WL 4499458, at *6 (S.D. Ga. 2016) (holding that *Dudenhoeffer* did not apply to a case alleging that a Defendant … fail[ed] to conduct an investigation into the prudence of continuing to hold an investment").

*   *   *

There are many other possible ERISA claims relevant to ESOPs that do not involve allegations of "over- or undervaluing the stock" and to which *Dudenhoeffer*'s reasoning should not apply. To allow the lower courts to require "special circumstances" in almost any ESOP case would be to effectively bring back the presumption of prudence that *Dudenhoeffer* rejected. This Court should take this opportunity to firmly reject that result.

CONCLUSION

This Court should affirm the Second Circuit's decision below. In doing so, it should clarify that its holding in *Dudenhoeffer* is limited to the particular circumstances of that case.

Respectfully submitted,

MATTHEW W.H. WESSLER
Counsel of Record
GREGORY A. BECK
GUPTA WESSLER PLLC
1900 L Street, NW Suite 312
Washington, DC 20036
(202) 888-1741
matt@guptawessler.com

BRUCE STERN
President
AMERICAN ASSOCIATION
FOR JUSTICE
777 6th Street, NW Suite 200
Washington, DC 20001

LEAH M. NICHOLLS
PUBLIC JUSTICE, P.C.
1620 L Street NW, Suite 630
Washington, DC 20036

Counsel for Amici Curiae

October 1, 2019