No. 12-751

In the Supreme Court of the United States

FIFTH THIRD BANCORP, ET AL., PETITIONERS

v.

JOHN DUDENHOEFFER, ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES
AS AMICUS CURIAE SUPPORTING RESPONDENTS

M. PATRICIA SMITH
Solicitor of Labor
G. WILLIAM SCOTT
Acting Associate Solicitor
ELIZABETH HOPKINS
Counsel for Appellate and Special Litigation
THOMAS TSO
Attorney
Department of Labor
Washington, D.C. 20210

DONALD B. VERRILLI, JR.
Solicitor General
Counsel of Record
EDWIN S. KNEEDLER
Deputy Solicitor General
JOHN F. BASH
Assistant to the Solicitor General

Department of Justice
Washington, D.C. 20530-0001
SupremeCtBriefs@usdoj.gov
(202) 514-2217

QUESTION PRESENTED

The Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, 88 Stat. 829, imposes duties on plan fiduciaries, including a duty to administer the plan prudently. 29 U.S.C. 1104(a)(1). The question presented is:

Whether, to state a claim that a fiduciary of an employee stock ownership plan violated the duty of prudence by continuing to invest plan assets in the employer's stock, a plaintiff must rebut a presumption that the fiduciary acted prudently by alleging that the employer faced imminent financial peril.

TABLE OF CONTENTS

Page

Interest of the United States 1
Statement 1
Summary of argument 7
Argument:
A. The text and purposes of ERISA do not support a nearly insurmountable presumption that an ESOP fiduciary acted prudently in continuing to invest plan assets in employer stock 9
1. Fiduciaries of all ERISA plans are subject to the "prudent person" standard of care in making investment decisions 10
2. ESOP fiduciaries are subject to the same standard of prudence as other ERISA fiduciaries and therefore are not entitled to any special presumption that they acted prudently 15
3. Petitioners' policy rationales do not justify a presumption of prudence 26
4. No reason exists to apply a presumption of prudence at the summary-judgment or trial stages either 31
B. Respondents stated a claim for breach of ERISA's duty of prudence 33
Conclusion 35
Statutory appendix 1a

TABLE OF AUTHORITIES

Cases:

Ashcroft v. *Iqbal*, 556 U.S. 662 (2009) 34
Central States, Se. & Sw. Areas Pension Fund v. *Central Transp., Inc.*, 472 U.S. 559 (1985) 12

Cases—Continued: Page

Curtiss-Wright Corp. v. *Schoonejongen*, 514 U.S. 73 (1995) 12

Fink v. *National Sav. & Trust Co.*, 772 F.2d 951 (D.C. Cir. 1985) 13

Firestone Tire & Rubber Co. v. *Bruch*, 489 U.S. 101 (1989) 25

Howell v. *Motorola, Inc.*, 633 F.3d 552 (7th Cir.), cert. denied, 132 S. Ct. 96 (2011) 15

LaRue v. *DeWolff, Boberg & Assocs., Inc.*, 552 U.S. 248 (2008) 3

Martin v. *Feilen*, 965 F.2d 660 (8th Cir. 1992), cert. denied, 506 U.S. 1054 (1993) 32

Massachusetts Mut. Life Ins. Co. v. *Russell*, 473 U.S. 134 (1985) 10

McDonnell Douglas Corp. v. *Green*, 411 U.S. 792 (1973) 32

Mead Corp. v. *Tilley*, 490 U.S. 714 (1989) 26

Metropolitan Life Ins. Co. v. *Glenn*, 554 U.S. 105 (2008) 25

Moench v. *Robertson*, 62 F.3d 553 (3d Cir. 1995), cert. denied, 516 U.S. 1115 (1996) 17

Pension Benefit Guar. Corp. v. *Morgan Stanley Inv. Mgmt. Inc.*, 712 F.3d 705 (2d Cir. 2013) 13, 14

Pfeil v. *State St. Bank & Trust Co.*, 671 F.3d 585 (6th Cir.), cert. denied, 133 S. Ct. 758 (2012) 31

Rinehart v. *Akers*, 722 F.3d 137 (2d Cir. 2013), petition for cert. pending, No. 13-830 (filed Jan. 8, 2014) 17

Smith v. *United States*, 133 S. Ct. 714 (2013) 32

United States Dep't of Justice v. *Landano*, 508 U.S. 165 (1993) 32

Varity Corp. v. *Howe*, 516 U.S. 489 (1996) 10, 11

Statutes, regulations and rules: Page

Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, 88 Stat. 829 1
§ 404(a)(1)(A), 88 Stat. 877 (29 U.S.C. 1104(a)(1)(A)) 19
§ 404(a)(2), 88 Stat. 877 (29 U.S.C. 1104(a)(2)) 19
§ 407(b)(1), 88 Stat. 880 (29 U.S.C. 1107(b)(1)) 19
29 U.S.C. 1001(a) 12, 20
29 U.S.C. 1001(b) 2
29 U.S.C. 1002(13) 1
29 U.S.C. 1002(18) 14
29 U.S.C. 1002(34) 2
29 U.S.C. 1021(i)(2)(C)(i) 28
29 U.S.C. 1021(i)(7)(B)(i) 28
29 U.S.C. 1102(a)(1) 2
29 U.S.C. 1103(a) 2
29 U.S.C. 1104 .... 12, 14, 15, 17
29 U.S.C. 1104(a) 2
29 U.S.C. 1104(a)(1) 28
29 U.S.C. 1104(a)(1)(A) 19, 21, 24
29 U.S.C. 1104(a)(1)(A)(i) 8
29 U.S.C. 1104(a)(1)(A)(ii) 8
29 U.S.C. 1104(a)(1)(B) 2, 6, 7, 10, 18, 23
29 U.S.C. 1104(a)(1)(C) 2
29 U.S.C. 1104(a)(1)(D) 7, 12, 17, 24, 25
29 U.S.C. 1104(a)(2) 2, 3, 16
29 U.S.C. 1104(c)(1)(A) 14
29 U.S.C. 1106-1108 22
29 U.S.C. 1106(a) 3
29 U.S.C. 1107 3
29 U.S.C. 1107(a)(2) 3

Statutes, regulations and rules—Continued: Page

29 U.S.C. 1107(b)(1) 3
29 U.S.C. 1107(d)(3)(A)(i) 3
29 U.S.C. 1107(d)(3)(A)(ii) 3
29 U.S.C. 1107(d)(5)(A) 3
29 U.S.C. 1107(d)(6)(A) 3
29 U.S.C. 1108(e) 3
29 U.S.C. 1110(a) 7, 12, 17
29 U.S.C. 1132(a)(2) 2
29 U.S.C. 1132(a)(3) 2
29 U.S.C. 1135 1
29 U.S.C. 1136(b) 1
Pension Protection Act of 2006, Pub. L. No. 109-280, 120 Stat. 780 20
Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67 109 Stat. 737 27
Tax Reform Act of 1976, Pub. L. No. 94-455, § 803(h), 90 Stat. 1590 (26 U.S.C. 4975 note) 21
Tax Reform Act of 1986, Pub. L. No. 99-514, § 1175(a)(1), 100 Stat. 2518-2519 .... 20, 23
26 U.S.C. 401(a)(28) 20
15 U.S.C. 77q(a) 28
15 U.S.C. 78j(b) 28
17 C.F.R. 240.10b-5 28
29 C.F.R.:
Section 2509.08-01 20
Section 2550.404c-1 15
Section 2550.407d-6(a)(4) 4

Miscellaneous: Page

George Gleason Bogert et al.:

The Law of Trusts and Trustees (rev. 2d ed. 1993) 11, 12

The Law of Trusts and Trustees (3d ed. 2000) 11, 13

Final Regulations Regarding Participant Directed Individual Account Plans (ERISA Section 404(c) Plans) 57 Fed. Reg. (Oct. 13, 1992):

p. 46,906 15

p. 46,924 15

H.R. Conf. Rep. No. 1280, 93d Cong., 2d Sess. (1974) 19, 22, 23, 31

H.R. Rep. No. 533, 93d Cong., 1st Sess. (1973) 13, 24

Restatement (Second) of Trusts (1959) 11, 13

S. Conf. Rep. No. 1236, 94th Cong., 2d Sess. (1976) 22

S. Rep. No. 127, 93d Cong., 1st Sess. (1973) 12, 13, 24

Austin Wakeman Scott, *The Law of Trusts* (3d ed. 1967):

Vol. 2 .... 11, 31

Vol. 3 .... 11, 12, 13

Staff of the Senate Special Comm. on Aging, 101st Cong., 2d Sess., *Developments in Aging: 1989 Volume 1* (Comm. Print 1990) 23

In the Supreme Court of the United States

No. 12-751

FIFTH THIRD BANCORP, ET AL., PETITIONERS

v.

JOHN DUDENHOEFFER, ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES
AS AMICUS CURIAE SUPPORTING RESPONDENTS

INTEREST OF THE UNITED STATES

This case concerns the scope of a fiduciary duty imposed on pension plan fiduciaries by the Employee Retirement Income Security Act of 1974 (ERISA), Pub. L. No. 93-406, 88 Stat. 829, which the Secretary of Labor has primary authority for administering. 29 U.S.C. 1002(13), 1135, 1136(b). At the Court's invitation, the United States filed a brief as amicus curiae at the petition stage of this case.

STATEMENT

1. ERISA is designed to "protect * * * the interests of participants in employee benefit plans and their beneficiaries * * * by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and by providing for appropriate remedies, sanctions, and ready access to

the Federal courts." 29 U.S.C. 1001(b). The statute requires every plan to be established and maintained pursuant to a written instrument and to have named fiduciaries who have authority to control and manage the administration of the plan and its assets. 29 U.S.C. 1102(a)(1), 1103(a).

Fiduciaries of ERISA plans are subject to duties of loyalty and care. See 29 U.S.C. 1104(a). The statute provides that a fiduciary must "discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries" of the plan, and "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 in the conduct of an enterprise of a like character and with like aims." 29 U.S.C. 1104(a)(1)(B). In addition, for most ERISA plans, the 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." 29 U.S.C. 1104(a)(1)(C). Plan participants and their beneficiaries may seek judicial redress against a fiduciary for violations of the plan or the statute, including breaches of ERISA's fiduciary duties. 29 U.S.C. 1132(a)(2) and (3).

ERISA sets forth limited exceptions to its statutory duties for fiduciaries who administer "eligible individual account plans." See 29 U.S.C. 1104(a)(2). An individual account plan (more commonly known as a "defined-contribution plan") is "a pension 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); see

LaRue v. *DeWolff, Boberg & Assocs., Inc.*, 552 U.S. 248, 250 n.1 (2008). Such plans often give each participant the discretion to select from a range of investment options chosen by the plan fiduciaries. ERISA defines an "eligible" individual account plan to include any individual account plan that is a "profit-sharing, stock bonus, thrift, or savings plan," or "an employee stock ownership plan [ESOP]." 29 U.S.C. 1107(d)(3)(A)(i) and (ii). An ESOP is in turn defined as an individual account plan that "is designed to invest primarily in qualifying employer securities" and meets certain other requirements. 29 U.S.C. 1107(d)(6)(A). An employer's common stock is one type of "qualifying employer security." 29 U.S.C. 1107(d)(5)(A).

For a plan fiduciary who administers an eligible individual account plan, "the diversification requirement * * * and the prudence requirement (only to the extent that it requires diversification)" are "not violated by acquisition or holding of * * * qualifying employer securities." 29 U.S.C. 1104(a)(2). In addition, eligible individual account plans are not subject to the ordinary requirement that no more than 10% of plan assets be invested in employer stock. 29 U.S.C. 1107(a)(2) and (b)(1). ERISA also exempts such plans from rules that would otherwise prohibit a fiduciary from purchasing stock for a plan from the employer. 29 U.S.C. 1106(a), 1107, 1108(e).

2. Petitioner Fifth Third Bancorp (Fifth Third) is a large financial-services company that sponsors an individual-account retirement plan for its employees called the Fifth Third Bancorp Master Profit Sharing Plan (Plan). Under the Plan, employees make voluntary contributions from their earnings, which they can

direct into any of various investment options. See Pet. App. 30; J.A. 576-577. One of those options is the Fifth Third Stock Fund (Fund), an ESOP required to be "invested primarily in shares of common stock of Fifth Third Bancorp." J.A. 350.[1] Fifth Third makes matching contributions of up to 4% of each employee's pre-tax compensation. J.A. 349, 574-577. Participants may then transfer those contributions to another investment option. J.A. 576.

The Plan generally grants Fifth Third's Pension and Profit Sharing Committee, whose members are made up of company officials and employees, "the discretionary authority and fiduciary duty to determine the investment funds to be made available" to participants, but provides that "in all events, the Fifth Third Stock Fund * * * shall be an investment option." J.A. 289, 735. The Plan requires the Committee to "monitor[] [the] investment funds to determine the continued prudence of offering such funds" and to "change the investment funds available if and when it deems it prudent to do so." J.A. 735.

Respondents, two former participants in the Plan, filed putative class actions against Fifth Third, its Chief Executive Officer, the Committee, and other individual Fifth Third officers who allegedly acted as fiduciaries of the Plan. J.A. 24-30. Respondents sued on behalf of all participants whose plan accounts were invested in Fifth Third stock between July 19, 2007 and September 21, 2009. J.A. 15, 19-20. According to the complaint, petitioners knew or should have known

---

[1] Under Department of Labor regulations, "[a]n ESOP may form a portion of a plan the balance of which includes a qualified pension, profit-sharing, or stock bonus plan which is not an ESOP." 29 C.F.R. 2550.407d-6(a)(4).

that the company's stock was excessively risky because of the company's exposure to high-risk subprime mortgages and that its price was artificially inflated because the company's financial statements were inaccurate. J.A. 98. Noting that the price of Fifth Third stock had declined by 74% following public disclosure of the company's actual financial condition, respondents attributed a loss of tens of millions of dollars in the value of the Plan to petitioners' alleged failure "to protect the Plan and its participants and beneficiaries from the risks of the Company's reckless and improper conduct." J.A. 37.

Respondents alleged that petitioners breached ERISA's duty of prudence by continuing to offer the Fund as an investment option and to invest plan assets in the Fund, and by failing to divest plan assets from the Fund. J.A. 104. They also alleged that petitioners "breached their duties of loyalty and prudence by failing to provide complete and accurate information to Plan participants and beneficiaries" about the company's financial condition. *Ibid.* Because of that, the complaint continued, "participants in the Plan could not appreciate the true risks presented by investments in the Company's stock and therefore could not make informed decisions regarding their investments in the Plan." J.A. 105.

3. The district court granted petitioners' motion to dismiss the complaint for failure to state a claim upon which relief could be granted. Pet. App. 28-52. The court believed that it was required to presume at the motion-to-dismiss stage that petitioners' decision to continue investing in Fifth Third stock was prudent and that respondents could rebut that presumption only by plausibly alleging that Fifth Third had been in

a "dire financial predicament" during the relevant period. *Id.* at 39-45. The court concluded that respondents' allegations did not meet that standard because "Fifth Third remained a viable company throughout the [relevant] period." *Id.* at 45.

4. The court of appeals reversed. Pet. App. 1-25. It explained that, under circuit precedent, "[a] fiduciary's decision to remain invested in employer securities is presumed to be reasonable." *Id.* at 10-11 (citation omitted). But it held that the "presumption is not a[] * * * pleading requirement" and therefore does not apply at the motion-to-dismiss stage. *Id.* at 11-12. The court went on to explain that to rebut the presumption where it applies, a plaintiff must "prove that a prudent fiduciary acting under similar circumstances would have made a different investment decision." *Id.* at 12 (citation and internal quotation marks omitted). That "unembellished standard," the court held, "closely tracks the statutory language of [29 U.S.C. 1104(a)(1)(B)]," which "imposes identical standards of prudence and loyalty on *all* fiduciaries, including ESOP fiduciaries." Pet. App. 12-13.

The court of appeals concluded that respondents' allegations that petitioners knew that Fifth Third stock was an imprudent investment but continued to invest plan assets in the Fund were sufficient to state a claim. Pet. App. 15.[2]

---

[2] In December 2013, the Securities and Exchange Commission instituted administrative proceedings against Fifth Third relating to the company's "failure to record substantial losses during the [2008] financial crisis by not properly accounting for a portion of its commercial real estate loan portfolio." *In re Fifth Third Bancorp.* 2 (Dec. 4, 2013), http://www.sec.gov/litigation/admin/2013/33-

SUMMARY OF ARGUMENT

A. ERISA does not require a court to conclusively presume that, absent "rare and extraordinary circumstances" (Pet. Br. 34), an ESOP fiduciary acted prudently in continuing to invest plan assets in employer stock. Rather, the same basic standard of prudence that protects all ERISA plans governs ESOP fiduciaries.

1. ERISA incorporates the "prudent person" standard from trust law. 29 U.S.C. 1104(a)(1)(B). Under that standard, a fiduciary in charge of a plan's investment decisions must conduct an adequate investigation of investment options and make reasonable choices based on that investigation. ERISA departs from trust law, however, in that an employer may not dispense with the duty of prudence by requiring the plan to make imprudent investments. 29 U.S.C. 1104(a)(1)(D), 1110(a). The prudent-person standard for investment decisions applies to all ERISA plans, including defined-contribution plans in which the fiduciary selects a menu of investment options (such as an ESOP) for participants.

2. No textual basis exists to depart from ERISA's prudent-person standard for an ESOP by presuming that its fiduciary's investment decisions are prudent absent "rare and extraordinary circumstances," such as the "impending collapse" of the employer. Pet. Br. 24, 34. Although ERISA exempts ESOP fiduciaries from the duty to diversify plan investments, the statute expressly preserves the basic duty of prudence in all other respects. Petitioners have pointed to nothing in the text of ERISA, its trust-law underpinnings, or

---

9490.pdf. As part of a settlement of that matter, Fifth Third agreed to pay a civil penalty of $6.5 million. See *id.* at 1-2, 10.

its foundational purpose of providing security for retirement benefits that supports a virtually insurmountable presumption that an ESOP fiduciary acted prudently in continuing to invest plan assets in employer stock, even if the fiduciary knew or should have known that the stock was materially overvalued due to the misconduct of corporate officers. Although the duty of prudence looks to how a reasonable fiduciary would manage a plan with "like aims," ERISA provides that an ESOP, like any other plan, must be administered with the "exclusive purpose" of "providing benefits to participants and their beneficiaries" (and defraying administrative expenses). 29 U.S.C. 1104(a)(1)(A)(i) and (ii). That statutory mandate does not permit a fiduciary to subordinate the interest in protecting the value of employees' retirement savings to other interests, such as raising capital for the company and building employee ownership in it.

3. Petitioners' policy arguments do not support a judicially created presumption of prudence that lacks support in ERISA's text. A presumption is not necessary to protect fiduciaries from liability for mere drops in stock price. If that is all that is alleged, a claim should ordinarily be dismissed. Any further concern about unduly burdensome class-action litigation should be addressed by Congress. Nor is a presumption of prudence required to avoid a conflict with the securities laws. Although an ESOP fiduciary who is also a corporate officer with material inside information may have a more limited range of options to ensure compliance with her ERISA duties, she always has the option of ceasing purchases or disclosing information to the market that would prevent the stock price from being artificially inflated. Any conflict,

moreover, can be avoided by appointing an independent entity, such as a financial institution, as the investment fiduciary of the ESOP.

4. The court of appeals erred in imposing a presumption of prudence at the factfinding stage. Particularly given that plaintiffs already bear the burden of proof and that plan fiduciaries have better access to information about the investigation they undertook and what they knew about the value of the employer's stock, it would be anomalous and inequitable to impose a heightened burden of proof in this context.

B. Respondents' complaint stated a claim for breach of the duty of prudence. Respondents plausibly alleged that petitioners knew, or would have known had they undertaken an adequate investigation, that Fifth Third stock was materially overvalued because of the bank's public misrepresentations about its mortgage portfolio and financial health, but continued to invest employees' retirement savings in the Fund and to offer it as an investment option.

ARGUMENT

A. The Text And Purposes Of ERISA Do Not Support A Nearly Insurmountable Presumption That An ESOP Fiduciary Acted Prudently In Continuing To Invest Plan Assets In Employer Stock

Petitioners contend that to succeed on a claim that an ESOP fiduciary acted imprudently in continuing to make an ESOP available as an investment option and to invest plan assets in employer stock, a plaintiff must overcome a "presumption of prudence" by plausibly pleading that "rare and extraordinary circumstances" existed during the challenged period of investment, "such as a serious threat to the employer's viability." Pet. Br. 16, 34. That standard has no basis

in ERISA's text, purposes, or trust-law underpinnings and should be rejected.[3]

1. Fiduciaries of all ERISA plans are subject to the "prudent person" standard of care in making investment decisions

a. ERISA imposes a duty of prudence on all plan fiduciaries. The statute provides that a "fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—(A) for the exclusive purpose of * * * providing benefits to participants and their beneficiaries * * * ; [and] (B) 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 in the conduct of an enterprise of a like character and with like aims." 29 U.S.C. 1104(a)(1)(B). Those standards govern "fiduciaries' investment decisions and disposition of assets." *Massachusetts Mut. Life Ins. Co.* v. *Russell*, 473 U.S. 134, 143 n.10 (1985).

Congress modeled ERISA's duty of prudence on the "prudent man" standard developed in the common law of trusts, see *Varity Corp.* v. *Howe*, 516 U.S. 489, 497 (1996), which in similar terms provides that "[i]n his management of the trust, the trustee is required to

---

[3] In its invitation brief, the United States explained that petitioners' question presented "is closely bound up with the question whether a presumption of prudence applies at all, and that question is logically antecedent to any questions concerning when such a presumption applies and what is necessary to rebut it." U.S. Br. 19. Although the Court declined the government's suggestion to reformulate the question "[t]o ensure adequate briefing" on that preliminary issue, *ibid.*, petitioners have thoroughly addressed it. See Pet. Br. 21-44 & n.7.

manifest the care, skill, prudence, and diligence of an ordinarily prudent man engaged in similar business affairs and with objectives similar to those of the trust in question." George Gleason Bogert et al., *The Law of Trusts and Trustees* § 541, at 167 (rev. 2d ed. 1993) (*Bogert* (2d ed.)); see Restatement (Second) of Trusts § 174, at 379 (1959); 2 Austin Wakeman Scott, *The Law of Trusts* § 174, at 1408 (3d ed. 1967) (*Scott*). At common law, the prudent-person standard imposed particular requirements on a trustee's investment decisions. See Restatement § 227(a), at 529; 3 *Scott* § 227, at 1805-1806. The principal obligation of the trustee was to "make[] an investigation as to the safety of [an] investment and the probable income to be derived therefrom," and then to make a reasonable investment decision based on that investigation. Restatement § 227 cmt. b, at 530. In addition, "a reasonably prudent trustee always would have considered diversifying his investments." George Gleason Bogert et al., *The Law of Trusts & Trustees* § 612, at 22 (3d ed. 2000) (*Bogert* (3d ed.)). The trustee also had an ongoing duty to monitor investments in the trust portfolio, and "if a particular asset in the trust portfolio [became] improper as a trust investment," the trustee was required to "act promptly to sell or convert the asset to avoid or minimize the risk of loss and personal liability." *Id.* § 612, at 19.

By incorporating the common-law standard into ERISA, Congress intended those basic requirements to apply to ERISA fiduciaries. But as this Court has observed, Congress also "expect[ed] that the courts w[ould] interpret th[e] prudent man rule * * * bearing in mind the special nature and purpose of employee benefit plans." *Varity Corp.*, 516 U.S. at 497

(first set of brackets in original). Accordingly, courts applying the duty of prudence in specific cases must take into account that ERISA plans are retirement-savings programs that are vital to "the continued well-being and security of millions of employees and their dependents." 29 U.S.C. 1001(a).

ERISA's duty of prudence operates differently from the trust-law duty of prudence in at least one significant respect. Under the common law, it was "generally recognized that the settlor can reduce or waive the prudent man standard of care by specific language in the trust instrument." *Bogert* (2d ed.) § 541, at 172; see *id.* § 542, at 187; 3 *Scott* § 227.14, at 1845-1848. But as this Court has explained, "trust documents cannot excuse trustees from their duties under ERISA." *Central States, Se. & Sw. Areas Pension Fund* v. *Central Transp., Inc.*, 472 U.S. 559, 568 (1985); cf. *Curtiss-Wright Corp.* v. *Schoonejongen*, 514 U.S. 73, 82 (1995). ERISA provides that a fiduciary is required to follow plan terms only "insofar as [plan] documents and instruments are consistent" with the other provisions of the statute, including its fiduciary duties. 29 U.S.C. 1104(a)(1)(D). Furthermore, "any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any * * * [fiduciary] duty" is "void as against public policy." 29 U.S.C. 1110(a).

ERISA fiduciaries, therefore, must follow plan terms, including investment guidelines, only if they are not "inconsistent with the fiduciary principles of [Section 1104]." S. Rep. No. 127, 93d Cong., 1st Sess. 30 (1973) (Senate Report). Indeed, Congress included express fiduciary duties in the statute itself in part because "the trust law in many states [had been] in-

terpreted" to relieve a fiduciary from liability for investment decisions "if the settlor specifie[d] that the trustee shall be allowed to make investments which might otherwise be considered imprudent." *Id.* at 29; see also H.R. Rep. No. 533, 93d Cong., 1st Sess. 12 (1973) (House Report) (same).

b. At common law, a court reviewing a trustee's investment decisions "endeavor[ed] to place itself in the position of the trustee at the time he made the investment and not to charge him with knowledge of what has happened since the investment." *Bogert* (3d ed.) § 612, at 60; see 3 *Scott* § 227, at 1807. The court would consider whether the trustee complied with his obligations "to investigate and evaluate investments, and to invest prudently." *Fink* v. *National Sav. & Trust Co.*, 772 F.2d 951, 962 (D.C. Cir. 1985) (Scalia, J., concurring in part and dissenting in part). In the typical case, "the extent of the trustee's investigation and evaluation [was] * * * the focus of inquiry," because "the determination of whether an investment was objectively imprudent [was] made on the basis of what the trustee knew *or should have known*; and the latter necessarily involve[d] consideration of what facts would have come to his attention if he had fully complied with his duty to investigate and evaluate." *Ibid.*; see Restatement § 227 cmt. b; 3 *Scott* § 227.1, at 1809.

In the ERISA context, therefore, to state a claim based on losses resulting from imprudent plan investments, a plaintiff typically must plausibly allege facts showing that the fiduciaries knew that an investment was imprudent or would have known that it was imprudent if they had undertaken an adequate investigation. See *Pension Benefit Guar. Corp.* v.

Morgan Stanley Inv. Mgmt. Inc., 712 F.3d 705, 718 (2d Cir. 2013). Absent such allegations, a plaintiff generally will not be able to state a claim for breach of the duty of prudence based on the fiduciaries' investment decisions and offering of investment options, even if the investments turned out to be unprofitable. See *id.* at 716. Thus, when a plaintiff suing an ERISA fiduciary for breach of the duty of prudence alleges only that a publicly traded security was experiencing a decline in price at the time that the fiduciary bought it for the plan, a court should ordinarily dismiss the claim on the pleadings. See *id.* at 722; cf. 29 U.S.C. 1002(18) (providing that "'adequate consideration' * * * in the case of a security for which there is a generally recognized market" is the price at which that security is trading). We would expect that to be particularly so with respect to investment in employer securities under an ESOP, because the exemption from ERISA's diversification requirement (and the toleration of greater risk as a result) means that a fiduciary may maintain or increase plan investments in employer stock even during a volatile period if the fiduciary does not know or have reason to know that the market price materially overstates the stock's value.

c. The prudent-person standard in Section 1104 applies to defined-contribution plans as well as defined-benefit plans. Some defined-contribution plans give participants discretion in choosing investments, and Section 1104(c)(1)(A) exempts fiduciaries of such plans from liability for investment-related losses caused by participant choices. But even for such a

"Section 404(c) plan,"[4] the Secretary has established in notice-and-comment rulemaking that the "act of limiting or designating investment options which are intended to constitute all or part of the investment universe of an ERISA 404(c) plan is a fiduciary function." *Final Regulation Regarding Participant Directed Individual Account Plans (ERISA Section 404(c) Plans)*, 57 Fed. Reg. 46,906, 46,924 n.27 (1992). Accordingly, "the plan fiduciary has a fiduciary obligation to prudently select such vehicles, as well as a residual fiduciary obligation to periodically evaluate the performance of such vehicles to determine, based on that evaluation, whether the vehicles should continue to be available as participant investment options." *Id.* at 46,924 n.27. That interpretation of the statute is reasonable and therefore entitled to deference. See *Howell* v. *Motorola, Inc.*, 633 F.3d 552, 567 (7th Cir.), cert. denied, 132 S. Ct. 96 (2011).

2. ESOP fiduciaries are subject to the same standard of prudence as other ERISA fiduciaries and therefore are not entitled to any special presumption that they acted prudently

ERISA's text and purposes do not support the virtually insurmountable presumption, urged by petitioners, that an ESOP fiduciary acted prudently in continuing to invest plan assets in the employer's stock or to offer it as an investment option.

a. The same prudent-person standard applicable to fiduciaries of ERISA plans generally applies to fiduciaries of ESOPs. Section 1104 sets forth specific ex-

---

[4] It is not clear from the record whether the plan at issue here meets the requirements of a Section 404(c) plan. See 29 C.F.R. 2550.404c-1.

emptions for fiduciaries of eligible individual account plans, including ESOPs, but does not exempt them from the basic duty of prudence: "In the case of an eligible individual account plan * * * , the diversification requirement of paragraph (1)(C) and the prudence requirement (*only to the extent that it requires diversification*) of paragraph (1)(B) is not violated by acquisition or holding of * * * qualifying employer securities." 29 U.S.C. 1104(a)(2) (emphasis added).

The straightforward meaning of that provision is that the same basic duty of prudence applicable to ERISA plans generally governs the investment choices of fiduciaries of ESOPs and other eligible individual account plans. The exemptions relieve those fiduciaries *only* of the specific requirement that a plan's investment portfolio be sufficiently diversified to minimize risk. By otherwise preserving the duty of prudence for ESOPs, Congress clearly expressed its intent that the same general standard of prudence is to govern ESOP fiduciaries as other ERISA fiduciaries. That standard does not permit courts to apply any special presumption that an ESOP fiduciary acted prudently, much less a standard of review that shields a fiduciary from liability so long as the employer did not face "rare and extraordinary circumstances" on the level of "a collapse [that] would leave employees with no meaningful ownership interest in their employer." Pet. Br. 16-17, 34.

The courts of appeals that have adopted such a presumption of prudence appear to have viewed any allegation that an ESOP fiduciary acted imprudently by continuing to invest in employer stock as logically indistinguishable from a claim that the fiduciary failed

to diversify plan assets. See Pet. Br. 7 (discussing *Moench* v. *Robertson*, 62 F.3d 553, 570 (3d Cir. 1995), cert. denied, 516 U.S. 1115 (1996)). That view is mistaken. The diversification exemption merely absolves ESOP fiduciaries from the ordinary obligation to reduce risk by spreading plan assets among multiple prudent investments. It does not permit them to concentrate plan assets in an *imprudent* investment, such as employer securities the fiduciary knows or should know are materially overvalued.

Some courts of appeals have also thought a presumption of prudence is warranted to resolve a perceived tension between a plan's requirement that the fiduciary invest plan assets in employer stock and ERISA's duty to invest plan assets prudently. See Pet. Br. 8 (citing *Moench*, 62 F.3d at 571-572). ERISA itself, however, resolves any such tension. As discussed above (see pp. 12-13, *supra*), a fiduciary is required to follow the terms of the plan only if it is consistent with Section 1104's fiduciary duties. 29 U.S.C. 1104(a)(1)(D). Just as a plan could not authorize a fiduciary to violate the statutory duty of loyalty, a plan cannot relax the duty of prudence. 29 U.S.C. 1110(a). Although that limitation represents a departure from the common law of trusts, it reflects ERISA's special protection for the security of employees' promised retirement benefits.

ERISA thus obligates the fiduciary of a plan that includes an ESOP option to depart from the plan's requirements if the initial investment options are no longer prudent. In fact, some ESOPs make that requirement explicit by requiring continued investment in employer stock only in conformity with ERISA's fiduciary duties. See *Rinehart* v. *Akers*, 722 F.3d 137,

145 (2d Cir. 2013) (discussing plan giving fiduciary power "to eliminate or curtail investments in [employer] [s]tock . . . *if and to the extent that* the [fiduciary] determines that such action is required in order to comply with the fiduciary duties rules" of ERISA), petition for cert. pending, No. 13-830 (filed Jan. 8, 2014) (citation omitted); cf. J.A. 387 (providing that Fifth Third's Committee must follow plan terms only "insofar as such documents and instruments are consistent with the provisions of title I of ERISA").

Accordingly, ERISA does not place ESOP fiduciaries in an "untenable position" (Pet. Br. 40) in deciding whether to follow a plan requirement to continue investing in employer stock. The duty of any ESOP fiduciary is to continue investing only if it is prudent to do so. As explained above, that standard assures fiduciaries wide latitude to make reasonable determinations in conditions of market uncertainty. For that reason, fiduciaries' decisions to continue investment in employer securities that have been declining in price, made after an adequate investigation into the soundness of the investment, should almost uniformly be upheld. See pp. 13-14, *supra*. But the prudent-person standard does not shield fiduciaries from liability when they knew, or would have known had they undertaken an adequate investigation, that the employer stock was materially overvalued.

b. Petitioners also contend (Br. 25-34) that a "robust presumption of prudence" that can be overcome only in "rare and extraordinary circumstances" follows from the statutory requirement that a fiduciary exercise the level of care that a prudent person would exercise for "an enterprise of a like character and with like aims," 29 U.S.C. 1104(a)(1)(B). That language,

however, does not support the virtually insurmountable barrier to relief that petitioners propose. The premise of petitioners' argument—that the exclusive "purpose of an ESOP is to foster employee ownership through investment in employer securities" (Br. 30), irrespective of whether those securities are materially overvalued—is fundamentally mistaken. Rather, ERISA makes clear that the exclusive "aim" of an ESOP, as of any pension plan, is to provide employee retirement benefits.

i. Like any other ERISA pension plan, an ESOP is a vehicle for retirement savings. That is clear on the face of the statute. As originally enacted, ERISA included the targeted exemptions from diversification requirements designed to enable employers to set up ESOPs. See ERISA §§ 404(a)(2), 407(b)(1), 88 Stat. 877, 880. Yet Congress did not see fit to exempt ESOPs from the requirement that fiduciaries administer plans "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)(1)(A) (emphasis added); see ERISA § 404(a)(1)(A), 88 Stat. 877; see also H.R. Conf. Rep. No. 1280, 93d Cong., 2d Sess. 302-303 (1974) (Conference Report). The statute nowhere permits an ESOP fiduciary to manage a plan with the objective of advancing any other goal, such as raising capital for the company and building employee equity in it.

It would therefore be at odds with the statutory text to elevate an unwritten objective of "foster[ing] employee ownership" (Pet. Br. 30) over ERISA's explicit command to operate plans with the exclusive goal of safeguarding retirement benefits—a goal that

advances Congress's overarching purpose of ensuring "the continued well-being and security of millions of employees and their dependents." 29 U.S.C. 1001(a). As the Secretary has explained in interpretive guidance, "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 [specified] circumstances." 29 C.F.R. 2509.08-01.

Congress, moreover, has taken steps since the enactment of ERISA to improve the reliability of ESOPs as retirement vehicles. In the Tax Reform Act of 1986, Pub. L. No. 99-514, § 1175(a)(1), 100 Stat. 2518-2519, Congress required employers to allow the partial diversification of ESOPs for older workers to protect their retirement savings. See 26 U.S.C. 401(a)(28). And as petitioners acknowledge only in a footnote, the Pension Protection Act of 2006, Pub. L. No. 109-280, 120 Stat. 780, "requires certain [ESOPs] to provide participants with the right to diversify their investments." Pet. Br. 36 n.14. Those statutory provisions reflect Congress's continued understanding that an ESOP, like any ERISA plan, serves primarily as a retirement-savings vehicle.

Some believe that by building employee equity in a company, ESOPs give employees a sense of ownership in their employer, which may have salutary effects on the efficiency and cohesiveness of the workforce. See ESOP Ass'n Amicus Br. 24. And by encouraging employees to invest their earnings in the company, ESOPs help employers raise capital. See Chamber of Commerce Amicus Br. 6. But Congress sought to advance those objectives through the ESOP-specific exemptions set forth in the text of the statute, as well

as certain tax benefits to facilitate the formation of ESOPs. Congress did not permit fiduciaries appointed to administer ESOPs, once they are established, to make investment decisions on the basis of the fiduciaries' perception or assessment of such generalized policy considerations. Instead, Congress applied to ESOPs, as to other plans, the requirement that the plan be administered for the "exclusive purpose" of "providing benefits to participants and their beneficiaries" and defraying administrative expenses. 29 U.S.C. 1104(a)(1)(A). An investment decision that subordinates that interest to other goals violates the duties of both prudence *and* loyalty.

ii. No other provision of ERISA supports petitioners' view that a fiduciary must administer an ESOP with the principal aim of raising capital for and building employee ownership in their company without regard to the effect of that investment on their retirement savings. Petitioners principally rely (Br. 6, 18, 21, 26, 38, 40) on a mere expression of congressional intent in a subsection of a complex tax statute enacted two years after ERISA in which Congress cautioned against "regulations and rulings which treat employee stock ownership plans as conventional retirement plans." Tax Reform Act of 1976, Pub. L. No. 94-455, § 803(h), 90 Stat. 1583, 1590 (reprinted at 26 U.S.C. 4975 note). The cited subsection does not suggest that a fiduciary administering an ESOP may subordinate the statutory objective of providing retirement benefits to the goal of building employee ownership in the company (much less do so at all costs), nor does it discuss the proper interpretation and enforcement of ERISA's fiduciary duties more generally. The expression of intent was instead di-

rected at specific provisions of proposed regulations relating to ESOP loans, stock options, voting rights, and the like, which were perceived to be too onerous. See S. Conf. Rep. No. 1236, 94th Cong., 2d Sess. 539, 542 (1976). Indeed, the Conference Report cautioned that no inference about Congress's intent should be drawn even with respect to provisions of the proposed regulations, if they were not commented upon. *Id.* at 542. The 1976 statute manifestly does not suggest that Congress intended to disapprove of the application to ESOPs of the basic *statutory* duty of prudence.

Petitioners also advert (Br. 36) to Internal Revenue Code provisions favoring ESOPs. ESOPs' tax-favored treatment, however, only underscores the importance of steadfastly enforcing the duty of prudence that Congress did not see fit to relax for ESOPs. Congress surely did not intend to provide tax benefits to plans that invest their employees' retirement savings in securities that are materially overpriced as a result of market misrepresentations.

Other citations in petitioners' brief are similarly inapposite. Petitioners take out of context a sentence fragment from ERISA's Conference Report discussing an exemption from ERISA's prohibited-transactions provisions (see 29 U.S.C. 1106-1108) for loans to a subclass of ESOPs ("leveraged" ESOPs). The passage states only that a frequent characteristic of such plans is that they are "designed to build equity ownership of shares of the employer corporation for its employees *in a nondiscriminatory manner*." Conference Report 313 (emphasis added) (quoted in part at Pet. Br. 26). The Conference Committee stressed the narrow scope of the exception and the need for "special scrutiny" to ensure that the transac-

tions are primarily for the benefit of plan participants and beneficiaries, *ibid.*, and hence did not suggest that the basic rule of prudence does not apply to ESOPs. Petitioners also cite (Br. 27) a special report of a Senate subcommittee published sixteen years after ERISA was enacted and that did not accompany any legislation. See Staff of the Senate Special Comm. on Aging, 101st Cong., 2d Sess., *Developments in Aging: 1989 Volume 1*, at 94-96 (Comm. Print 1990). The short discussion of ESOPs in that report explained only that the Tax Reform Act of 1986 required employers to allow the partial diversification of ESOPs for older workers to protect their retirement savings.

Aside from those sources, petitioners rely (Br. 27, 38 n.15) on a committee staff report issued six years after ERISA's enactment indicating that an ESOP is not "primarily" a retirement vehicle, and a Senator's 1983 floor statement introducing a bill that was never enacted. It is telling that these scattered statements over the decades since ERISA's enactment are all petitioners have been able to muster for the view that, notwithstanding the explicit text of ERISA itself, Congress intended courts to apply a virtually insurmountable presumption of prudence for ESOP fiduciaries.

iii. Accordingly, in determining whether a fiduciary administered an ESOP in the way that a prudent person would manage "an enterprise of a like character and with like aims," 29 U.S.C. 1104(a)(1)(B), a court must consider how a prudent person would operate a fund that, although exempt from strict diversification requirements if invested in employer securities, nevertheless has the "exclusive purpose" of providing retirement benefits to participants (and

defraying administrative expenses), 29 U.S.C. 1104(a)(1)(A). A prudent person administering such a fund would not continue to make investments in assets she knows, or should know, are materially overpriced. Petitioners are therefore wrong in arguing that the prudent-person standard requires a court to countenance continued investment in artificially inflated employer stock (with the resulting diminishment in the value of employees' retirement savings) so long as the company was not on the brink of collapse.

c. Petitioners point (Br. 30-34) to the "deviation doctrine" in the common law of trusts. As described by petitioners, that doctrine requires a trustee to follow the terms of the trust "unless compliance is impossible or illegal or there has been such a change of circumstances that compliance would defeat or substantially impair the accomplishment of the trust purposes." *Id.* at 32 (citation and internal quotation marks omitted). But as discussed above, see pp. 12-13, *supra*, Congress directed that ERISA's fiduciary duties trump contrary plan terms, 29 U.S.C. 1104(a)(1)(D), specifically to address the problem that "the trust law in many states" had shielded trustees from liability for investment decisions "if the settlor specifie[d] that the trustee shall be allowed to make investments which might otherwise be considered imprudent." Senate Report 29; see House Report 12 (same). The incorporation of the "deviation doctrine" into ERISA in the way petitioners urge would effectively overturn Congress's deliberate decision to depart from trust law in that respect. Indeed, petitioners' line of reasoning would support a nearly irrebuttable presumption of prudence not only for ESOPs, but for any plan specifying that certain investment

funds will be offered to plan participants, regardless of whether those options are prudent or sufficiently diversified. That plainly is not what Congress envisioned when it enacted Section 1104(a)(1)(D). And in fact, the deviation doctrine, as set forth in the passage quoted by petitioners above, requires a trustee to follow the terms of the trust "unless compliance is * * * illegal" (Pet. Br. 32); here Section 1104(a)(1)(D) renders it illegal for a fiduciary to follow the terms of the plan if it would be imprudent to do so.

d. Petitioners also try to draw an analogy between the presumption of prudence and the abuse-of-discretion standard that courts apply in reviewing individual benefit determinations by plan fiduciaries who have been vested with discretion to decide claims or to interpret the terms of a plan. See Pet. Br. 41-42 (citing *Firestone Tire & Rubber Co.* v. *Bruch*, 489 U.S. 101, 111 (1989)); see *Metropolitan Life Ins. Co.* v. *Glenn*, 554 U.S. 105, 111 (2008). That analogy is inapt, because the abuse-of-discretion standard does not pose the virtually insurmountable hurdle to recovery that petitioners urge. But more fundamentally, this Court developed the abuse-of-discretion standard because "ERISA does not set out the appropriate standard of review for actions * * * challenging benefit eligibility determinations." *Firestone Tire & Rubber Co.*, 489 U.S. at 109. In contrast, Congress has expressly prescribed the standard to be applied to claims of fiduciary mismanagement: the prudent-person standard. That standard does not demand "rare and extraordinary circumstances" before an investment can be deemed imprudent.

e. Finally, petitioners emphasize (Br. 22-23, 35) that a presumption of prudence was first articulated

by the Third Circuit in 1995 and has recently been adopted by five other courts of appeals. The Department of Labor, however, has consistently taken the position that "fiduciaries are obligated to follow plan terms[] requiring investment in employer stock only to the extent that doing so is otherwise consistent with fiduciary duties" and has opposed the sort of preclusive presumption that petitioners favor. Secretary of Labor Amicus Br., 2006 WL 5952409, at *10, *Kirschbaum* v. *Reliant Energy, Inc.* (5th Cir. Aug. 17, 2006); see, *e.g.*, Secretary of Labor Amicus Br., 1994 WL 16012393, at *9-*23, *Moench*, *supra* (3d Cir. 1994). That longstanding view is entitled to some weight. See *Mead Corp.* v. *Tilley*, 490 U.S. 714, 722 (1989).

3. Petitioners' policy rationales do not justify a presumption of prudence

Petitioners and their amici identify various policy reasons that in their view support a nearly absolute presumption of prudence. Those policy assertions do not warrant a judicially fashioned barrier to relief that has no mooring in ERISA's text.

a. Petitioners predict that without a presumption of prudence, ESOP fiduciaries will be subject to liability because the company's "share price fell." Pet. Br. 16; see *id.* at 17-18, 24, 34, 51. That concern miscomprehends the prudent-person standard. Just as with fiduciaries of other types of ERISA plans, see pp. 13-14, *supra*, a claim that the price of a publicly traded stock decreased, even substantially, is insufficient to state a claim against an ESOP fiduciary.

Amicus Delta Airlines (Br. 5) is therefore correct that "[w]hen there is no allegation that a company's stock price reflected anything other than its true value, claims challenging a plan fiduciary's investment

in employer stock" should typically be dismissed. But where a plaintiff plausibly alleges that the fiduciary *knew*, or *should have known*, that the employer stock "traded at an artificially inflated price due to fraud, improper accounting practices, overvaluation of assets, or material misstatements about the company's prospects," *id.* at 7, and yet neither stopped investing in it and offering it as an investment option, nor made corrective disclosures so that plan participants could decide to stop investing in it, he has stated a claim for breach of fiduciary duty. Petitioners' extreme position—that even when fiduciaries know that the company's financial statements do not reflect its true financial health and the market price therefore does not accurately reflect the actual value of the stock, they *never* have an obligation to take action to protect plan participants unless the company is on the "brink of collapse" (Br. 34 (citation omitted))—would thwart the basic objective of ERISA to promote retirement security.

Petitioners and their amici cite what they see as a significant number of meritless suits against ESOP fiduciaries. See, *e.g.*, Chamber of Commerce Amicus Br. 18-21. Even if their characterizations of those suits are accurate, however, any decision to heighten the ordinary pleading standards in this context should be made by Congress. Cf. *e.g.*, Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737. And in any event, permitting suits based on "allegations that the share price was overvalued and the fiduciaries knew of that overvaluation" will not open the door to baseless claims. Delta Airlines Amicus Br. 18.

b. Petitioners further contend that "insufficient deference to ESOP fiduciaries would give rise to unintended and avoidable conflicts with securities law." Pet. Br. 42 (capitalization altered). That argument also lacks merit.

i. Petitioners argue that without a presumption of prudence, a fiduciary who is also a corporate insider might be forced to violate the securities laws by trading on inside information on behalf of plan participants. It is true that a fiduciary may not sell stock on behalf of participants, or notify participants that they should do so, based on inside information. See 15 U.S.C. 77q(a); 78j(b); 17 C.F.R. 240.10b-5. That securities-law limitation restricts the range of options that an ESOP fiduciary who is also a corporate insider may have available to fulfill his obligation to "discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries." 29 U.S.C. 1104(a)(1). But it does not leave him without options. As petitioners acknowledge (Br. 43), a fiduciary can publicly disclose information to the market that brings the price of the employer stock in line with its value, cease further purchases of the stock, or both. Cf. 29 U.S.C. 1021(i)(2)(C)(i) and (7)(B)(i) (provisions relating to suspension of plan trading due to ERISA's fiduciary duties or the securities laws). The fiduciary can also alert the proper regulatory agencies, such as the Securities and Exchange Commission (SEC) or the Department of Labor, to any alleged misstatements in securities filings. Those courses do not violate the securities laws.

Petitioners argue that public disclosure would decrease the value of the assets already held by the plan. That would be true if the price has been artificially

inflated by the company's public misrepresentations. But if so, a similar or greater drop might well occur if correction of the misrepresentations were delayed—potentially months or years later, after even more of the employees' retirement savings have been invested in the overpriced assets. It better serves the interests of the plan participants if the fiduciaries take immediate actions to bring the price of the stock in line with its true value by disclosing the material nonpublic information.

Petitioners contend (Br. 44) that if a fiduciary stops investing in employer stock without disclosing the information to the market, the market could overreact and cause the price to drop by more than it would if the information was disclosed. That might be so. A prudent fiduciary, therefore, should use her judgment to determine whether public disclosure in conjunction with a cessation in purchasing would better fulfill her obligations to plan participants and their beneficiaries. The timing and consequences of public disclosure, moreover, should be taken into account in computing any damages awarded for a breach of the duty of prudence.

ii. Petitioners also maintain (Br. 44) that without a presumption of prudence, corporations will be required to disclose material nonpublic information at earlier times than when disclosure is required by the securities laws. That is not so. The Department of Labor does not take the position that an ESOP fiduciary, to avoid liability for a breach of the duty of prudence, must disclose information to the public sooner than when federal securities laws would require disclosure. For example, certain triggering events must be disclosed through SEC *Form 8-K* within four busi-

ness days of their occurrence. Other information must be disclosed quarterly or annually through *Form 10-K* and *Form 10-Q*. The securities laws reflect a reasonable judgment about how soon particular categories of information must be disclosed to investors, and it is sensible to interpret ERISA's duty of prudence harmoniously with those requirements.

But where, as here, it is plausibly alleged that the fiduciaries knew, or would have known if they had conducted an adequate investigation, that the company was making material misstatements to the public about the soundness of its business—*i.e.*, that the corporate insiders were *violating* the securities laws—no justification exists to shield them from liability to plan participants who entrusted the fiduciaries with their retirement savings. The securities laws certainly do not require that result.

iii. Even if corporate officers who are ESOP fiduciaries were required in some respects to adhere to stricter obligations than what the securities laws require, that would be a consequence of the corporation's own decision to establish an ESOP and to install its officers as plan fiduciaries. There is nothing remarkable about the fact that the decision to take on strict fiduciary obligations to plan participants would limit the range of options available to corporate insiders with respect to the disclosure of inside information.

In any event, the consequences that petitioners posit can largely be avoided if an employer assigns a non-insider, such as an outside financial institution, to be the investment fiduciary of the ESOP. Although a designated employee of the company or another person would have responsibility for monitoring the per-

formance of the investment fiduciary, and would therefore have a fiduciary duty to keep the trustee informed of any pertinent information, the company could place a person in that role who is not likely to know material inside information.

More generally, in light of the common-law origins and statutory purposes of ERISA, it would be anomalous if the fact that some ESOP fiduciaries are corporate insiders gave rise to a more lenient standard of prudence. At common law, a trustee corporation's "peculiar knowledge of the value of [its own] shares [was] a factor to be considered in determining whether the making or the retention of an investment in its own shares is negligent." 2 *Scott* § 170.15, at 1339. And ERISA's legislative history expressed the concern that "where the investments may inure to the direct or indirect benefit of the plan sponsor * * * participants might be subject to pressure with respect to investment decisions." Conference Report 305. It is therefore difficult to believe, as petitioners contend, that Congress would have intended courts to almost completely defer to employers in this context.

4. No reason exists to apply a presumption of prudence at the summary-judgment or trial stages either

The Sixth Circuit has conceived of the presumption of prudence as a framework for weighing evidence and therefore has not required plaintiffs to plead facts overcoming the presumption. Pet. App. 11-12; *Pfeil* v. *State St. Bank & Trust Co.*, 671 F.3d 585, 592-593, cert. denied, 133 S. Ct. 758 (2012). But it has nevertheless stated that the presumption imposes a "demanding burden" on plaintiffs at the summary-judgment and factfinding stages. *Pfeil*, 671 F.3d at

595. Although that version of the presumption is preferable to a standard in which a plaintiff would have to plead "rare and extraordinary circumstances" (Pet. Br. 34), it is inconsistent with ERISA as well.

Courts sometimes impose special evidentiary presumptions when the party who would otherwise bear the burden of proof is poorly positioned to establish a particular fact—for example, because "the facts with regard to an issue lie peculiarly in the knowledge of [the other] party." *Smith* v. *United States*, 133 S. Ct. 714, 720 (2013) (citation omitted); see, *e.g.*, *McDonnell Douglas Corp.* v. *Green*, 411 U.S. 792, 802-803 (1973). Evidentiary presumptions also can be justified by "considerations of fairness, public policy, and probability, as well as judicial economy." *United States Dep't of Justice* v. *Landano*, 508 U.S. 165, 174 (1993) (internal quotation marks and citation omitted).

Those considerations do not justify any special presumption in the context of claims that ESOP fiduciaries breached the duty of prudence by continuing to invest in employer stock. The burden of alleging and proving a breach of the fiduciary duty of prudence already rests with the plaintiff.[5] However it is articulated, therefore, the only function of a special presumption would be to establish a threshold for proving the plaintiff's claim greater than that required to show by a preponderance of the evidence that the fiduciary knew or reasonably should have known that

---

[5] Some courts of appeals have held that once a plaintiff has demonstrated a breach of fiduciary duty and made a prima facie showing of loss, the burden shifts to the fiduciary to prove that a loss would have occurred even without the breach. See, *e.g.*, *Martin* v. *Feilen*, 965 F.2d 660, 671 (8th Cir. 1992), cert. denied, 506 U.S. 1054 (1993).

the employer securities were materially overvalued. Such a heightened burden would be particularly onerous in this context given that the critical question is often whether the defendants failed to conduct an adequate investigation—information uniquely within the defendants' possession. The only purpose of increasing the burden on the plaintiff would thus be simply to make claims arising out of ESOP investment decisions very difficult to win. That is not a justification for a judicially fashioned presumption.

B. Respondents Stated A Claim For Breach Of ERISA's Duty Of Prudence

Respondents' complaint (J.A. 15-117) adequately stated a claim for breach of the duty of prudence. Their detailed allegations did not rest on a "mere decline in stock price." Pet. Br. 17, 34. The gravamen of their claims was that petitioners knew—or, if they had conducted a reasonable investigation, would have known—that Fifth Third stock was not worth what the Plan was paying for it, in large part because the company's subprime mortgage lending practice was misleadingly or insufficiently disclosed. Pet. App. 4-5; J.A. 98-104.

That claim was supported by detailed allegations. Respondents alleged, for example, that in publicly describing what types of mortgages were contained in Fifth Third's loan portfolio, petitioners failed to disclose "the Company's internal working definition of 'prime,' which was utterly and completely inconsistent with commonly accepted definitions of the term within the banking industry." J.A. 57. They also alleged that the company did not disclose that it had been originating loans in which the borrowers did not meet the requisite qualifications. J.A. 63. Fifth Third's portfo-

lio, they claimed, "was riddled with under-collateralized loans issued to borrowers that lacked sufficient incomes or assets to repay their loans." J.A. 65.

Respondents further alleged that petitioners, due to their positions within the company, knew about these problems and numerous others detailed in the complaint. J.A. 86-87, 98-99, 102. They claimed that petitioners "failed to conduct an appropriate investigation into whether Fifth Third Stock was a prudent investment for the Plan and, in connection therewith, failed to provide Plan participants and beneficiaries with information regarding Fifth Third's problems so that participants could make informed decisions." J.A. 87-88, 99. Petitioners, they maintained, could have taken such actions as "discontinuing further contributions to and/or investment in Fifth Third Stock" or "consulting with the [Department of Labor] or independent fiduciaries regarding appropriate measures." J.A. 88-89, 103. But petitioners "failed to take any action to protect participants." J.A. 89. As a result, "[t]he Plan suffered millions of dollars in principal losses." J.A. 113.

Those allegations are not "[t]hreadbare recitals of the elements of a cause of action, supported by mere conclusory statements." *Ashcroft* v. *Iqbal*, 556 U.S. 662, 678 (2009). Fifth Third may not have been on the "brink of collapse," and thus petitioners' "rare and extraordinary circumstances" test would not be met. But respondents have sufficiently alleged that petitioners invested employees' retirement savings in securities that they knew or reasonably should have known were materially overpriced. That suffices to state a claim for breach of the duty of prudence.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

DONALD B. VERRILLI, JR.
Solicitor General
EDWIN S. KNEEDLER
Deputy Solicitor General
JOHN F. BASH
Assistant to the Solicitor General

M. PATRICIA SMITH
Solicitor of Labor
G. WILLIAM SCOTT
Acting Associate Solicitor
ELIZABETH HOPKINS
Counsel for Appellate and Special Litigation
THOMAS TSO
Attorney
Department of Labor

MARCH 2014

STATUTORY APPENDIX

1. Section 803(h) of the Tax Reform Act of 1976, Public Law No. 94-455 provides:

TITLE VIII—CAPITAL FORMATION

* * * * *

Sec. 803. EMPLOYEE STOCK OWNERSHIP PLANS; STUDY OF EXPANDED STOCK OWNERSHIP

* * * * *

(h) INTENT OF CONGRESS CONCERNING EMPLOYEE STOCK OWNERSHIP PLANS.—The Congress, in a series of laws (the Regional Rail Reorganization Act of 1973, the Employee Retirement Income Security ACT of 1974, the Trade Act of 1974, and the Tax Reduction Act of 1975) and this Act has made clear its interest in encouraging employee stock ownership plans as a bold and innovative method of strengthening the free private enterprise system which will solve the dual problems of securing capital funds for necessary capital growth and of bringing about stock ownership by all corporate employees. The Congress is deeply concerned that the objectives sought by this series of laws will be made unattainable by regulations and rulings which treat employee stock ownership plans as conventional retirement plans, which reduce the freedom of the employee trusts and employers to take the necessary steps to implement the plans, and which otherwise block the establishment and success of these plans. Because of the special purposes for which employee stock ownership plans are established, it is consistent with the intent of Congress to permit these plans (whether structured as

pension, stock bonus, or profit–sharing plans) to distribute income on employer securities currently.

2. 29 U.S.C. 1001 provides:

Congressional findings and declaration of policy

(a) Benefit plans as affecting interstate commerce and the Federal taxing power

The Congress finds that the growth in size, scope, and numbers of employee benefit plans in recent years has been rapid and substantial; that the operational scope and economic impact of such plans is increasingly interstate; that the continued well-being and security of millions of employees and their dependents are directly affected by these plans; that they are affected with a national public interest; that they have become an important factor affecting the stability of employment and the successful development of industrial relations; that they have become an important factor in commerce because of the interstate character of their activities, and of the activities of their participants, and the employers, employee organizations, and other entities by which they are established or maintained; that a large volume of the activities of such plans are carried on by means of the mails and instrumentalities of interstate commerce; that owing to the lack of employee information and adequate safeguards concerning their operation, it is desirable in the interests of employees and their beneficiaries, and to provide for the general welfare and the free flow of commerce, that disclosure be made and safeguards be provided with respect to the establish-

ment, operation, and administration of such plans; that they substantially affect the revenues of the United States because they are afforded preferential Federal tax treatment; that despite the enormous growth in such plans many employees with long years of employment are losing anticipated retirement benefits owing to the lack of vesting provisions in such plans; that owing to the inadequacy of current minimum standards, the soundness and stability of plans with respect to adequate funds to pay promised benefits may be endangered; that owing to the termination of plans before requisite funds have been accumulated, employees and their beneficiaries have been deprived of anticipated benefits; and that it is therefore desirable in the interests of employees and their beneficiaries, for the protection of the revenue of the United States, and to provide for the free flow of commerce, that minimum standards be provided assuring the equitable character of such plans and their financial soundness.

(b) Protection of interstate commerce and beneficiaries by requiring disclosure and reporting, setting standards of conduct, etc., for fiduciaries

It is hereby declared to be the policy of this chapter to protect interstate commerce and the interests of participants in employee benefit plans and their beneficiaries, by requiring the disclosure and reporting to participants and beneficiaries of financial and other information with respect thereto, by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and by providing for appropriate remedies, sanctions, and ready access to the Federal courts.

(c) Protection of interstate commerce, the Federal taxing power, and beneficiaries by vesting of accrued benefits, setting minimum standards of funding, requiring termination insurance

It is hereby further declared to be the policy of this chapter to protect interstate commerce, the Federal taxing power, and the interests of participants in private pension plans and their beneficiaries by improving the equitable character and the soundness of such plans by requiring them to vest the accrued benefits of employees with significant periods of service, to meet minimum standards of funding, and by requiring plan termination insurance.

3. 29 U.S.C. 1002 provides in pertinent part:

Definitions

For purposes of this subchapter:

* * * * *

(18) The term "adequate consideration" when used in part 4 of subtitle B of this subchapter means (A) in the case of a security for which there is a generally recognized market, either (i) the price of the security prevailing on a national securities exchange which is registered under section 78f of Title 15, or (ii) if the security is not traded on such a national securities exchange, a price not less favorable to the plan than the offering price for the security as established by the current bid and asked prices quoted by persons independent of the issuer and of any party in interest; and (B) in

the case of an asset other than a security for which there is a generally recognized market, the fair market value of the asset as determined in good faith by the trustee or named fiduciary pursuant to the terms of the plan and in accordance with regulations promulgated by the Secretary.

* * * * *

(21)(A) Except as otherwise provided in subparagraph (B), 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. Such term includes any person designated under section 1105(c)(1)(B) of this title.

(B) If any money or other property of an employee benefit plan is invested in securities issued by an investment company registered under the Investment Company Act of 1940 [15 U.S.C.A. § 80a-1 et seq.], such investment shall not by itself cause such investment company or such investment company's investment adviser or principal underwriter to be deemed to be a fiduciary or a party in interest as those terms are defined in this subchapter, except insofar as such investment company or its investment adviser or principal underwriter acts in connection with an employee benefit plan

covering employees of the investment company, the investment adviser, or its principal underwriter. Nothing contained in this subparagraph shall limit the duties imposed on such investment company, investment adviser, or principal underwriter by any other law.

* * * * *

(34) The term "individual account plan" or "defined contribution plan" means a pension 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, and any forfeitures of accounts of other participants which may be allocated to such participant's account.

4. 29 U.S.C. 1104 provides in pertinent part:

Fiduciary duties

(a) Prudent man standard of care

(1) Subject to sections 1103(c) and (d), 1342, and 1344 of this title, a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and—

(A) for the exclusive purpose of:

(i) providing benefits to participants and their beneficiaries; and

(ii) defraying reasonable expenses of administering the plan;

(B) 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 in the conduct of an enterprise of a like character and with like aims;

(C) 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; and

(D) in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with the provisions of this subchapter and subchapter III of this chapter.

(2) In the case of an eligible individual account plan (as defined in section 1107(d)(3) of this title), the diversification requirement of paragraph (1)(C) and the prudence requirement (only to the extent that it requires diversification) of paragraph (1)(B) is not violated by acquisition or holding of qualifying employer real property or qualifying employer securities (as defined in section 1107(d)(4) and (5) of this title).

* * * * *

(c) Control over assets by participant or beneficiary

(1)(A) In the case of a pension plan which provides for individual accounts and permits a participant or beneficiary to exercise control over the assets in his account, if a participant or beneficiary

exercises control over the assets in his account (as determined under regulations of the Secretary)—

(i) such participant or beneficiary shall not be deemed to be a fiduciary by reason of such exercise, and

(ii) no person who is otherwise a fiduciary shall be liable under this part for any loss, or by reason of any breach, which results from such participant's or beneficiary's exercise of control, except that this clause shall not apply in connection with such participant or beneficiary for any blackout period during which the ability of such participant or beneficiary to direct the investment of the assets in his or her account is suspended by a plan sponsor or fiduciary.

(B) If a person referred to in subparagraph (A)(ii) meets the requirements of this subchapter in connection with authorizing and implementing the blackout period, any person who is otherwise a fiduciary shall not be liable under this subchapter for any loss occurring during such period.

(C) For purposes of this paragraph, the term "blackout period" has the meaning given such term by section 1021(i)(7) of this title.

(2) In the case of a simple retirement account established pursuant to a qualified salary reduction arrangement under section 408(p) of Title 26, a participant or beneficiary shall, for purposes of paragraph (1), be treated as exercising control over the assets in the account upon the earliest of—

(A) an affirmative election among investment options with respect to the initial investment of any contribution,

(B) a rollover to any other simple retirement account or individual retirement plan, or

(C) one year after the simple retirement account is established.

No reports, other than those required under section 1021(g) of this title, shall be required with respect to a simple retirement account established pursuant to such a qualified salary reduction arrangement.

(3) In the case of a pension plan which makes a transfer to an individual retirement account or annuity of a designated trustee or issuer under section 401(a)(31)(B) of the Internal Revenue Code of 1986, the participant or beneficiary shall, for purposes of paragraph (1), be treated as exercising control over the assets in the account or annuity upon—

(A) the earlier of—

(i) a rollover of all or a portion of the amount to another individual retirement account or annuity; or

(ii) one year after the transfer is made; or

(B) a transfer that is made in a manner consistent with guidance provided by the Secretary.

(4)(A) In any case in which a qualified change in investment options occurs in connection with an individual account plan, a participant or beneficiary shall not be treated for purposes of paragraph (1) as not exercising control over the assets in his account in connection with

such change if the requirements of subparagraph (C) are met in connection with such change.

(B) For purposes of subparagraph (A), the term "qualified change in investment options" means, in connection with an individual account plan, a change in the investment options offered to the participant or beneficiary under the terms of the plan, under which—

(i) the account of the participant or beneficiary is reallocated among one or more remaining or new investment options which are offered in lieu of one or more investment options offered immediately prior to the effective date of the change, and

(ii) the stated characteristics of the remaining or new investment options provided under clause (i), including characteristics relating to risk and rate of return, are, as of immediately after the change, reasonably similar to those of the existing investment options as of immediately before the change.

(C) The requirements of this subparagraph are met in connection with a qualified change in investment options if—

(i) at least 30 days and no more than 60 days prior to the effective date of the change, the plan administrator furnishes written notice of the change to the participants and beneficiaries, including information comparing the existing and new investment options and an explanation that, in the absence of affirmative investment instructions from the participant or beneficiary to the contrary, the account of

the participant or beneficiary will be invested in the manner described in subparagraph (B),

(ii) the participant or beneficiary has not provided to the plan administrator, in advance of the effective date of the change, affirmative investment instructions contrary to the change, and

(iii) the investments under the plan of the participant or beneficiary as in effect immediately prior to the effective date of the change were the product of the exercise by such participant or beneficiary of control over the assets of the account within the meaning of paragraph (1).

(5) DEFAULT INVESTMENT ARRANGEMENTS.—

(A) IN GENERAL.—For purposes of paragraph (1), a participant or beneficiary in an individual account plan meeting the notice requirements of subparagraph (B) shall be treated as exercising control over the assets in the account with respect to the amount of contributions and earnings which, in the absence of an investment election by the participant or beneficiary, are invested by the plan in accordance with regulations prescribed by the Secretary. The regulations under this subparagraph shall provide guidance on the appropriateness of designating default investments that include a mix of asset classes consistent with capital preservation or long-term capital appreciation, or a blend of both.

(B) NOTICE REQUIREMENTS.—

(i) IN GENERAL.—The requirements of this subparagraph are met if each participant or beneficiary—

(I) receives, within a reasonable period of time before each plan year, a notice explaining the employee's right under the plan to designate how contributions and earnings will be invested and explaining how, in the absence of any investment election by the participant or beneficiary, such contributions and earnings will be invested, and

(II) has a reasonable period of time after receipt of such notice and before the beginning of the plan year to make such designation.

(ii) FORM OF NOTICE.—The requirements of clauses (i) and (ii) of section 401(k)(12)(D) of Title 26 shall apply with respect to the notices described in this subparagraph.

5. 29 U.S.C. 1106(a) provides:

Prohibited transactions

(a) Transactions between plan and party in interest

Except as provided in section 1108 of this title:

(1) A fiduciary with respect to a plan shall not cause the plan to engage in a transaction, if he

knows or should know that such transaction constitutes a direct or indirect—

(A) sale or exchange, or leasing, of any property between the plan and a party in interest;

(B) lending of money or other extension of credit between the plan and a party in interest;

(C) furnishing of goods, services, or facilities between the plan and a party in interest;

(D) transfer to, or use by or for the benefit of a party in interest, of any assets of the plan; or

(E) acquisition, on behalf of the plan, of any employer security or employer real property in violation of section 1107(a) of this title.

(2) No fiduciary who has authority or discretion to control or manage the assets of a plan shall permit the plan to hold any employer security or employer real property if he knows or should know that holding such security or real property violates section 1107(a) of this title.

6. 29 U.S.C. 1107 provides:

Limitation with respect to acquisition and holding of employer securities and employer real property by certain plans

(a) Percentage limitation

Except as otherwise provided in this section and section 1114 of this title:

(1) A plan may not acquire or hold—

(A) any employer security which is not a qualifying employer security, or

(B) any employer real property which is not qualifying employer real property.

(2) A plan may not acquire any qualifying employer security or qualifying employer real property, if immediately after such acquisition the aggregate fair market value of employer securities and employer real property held by the plan exceeds 10 percent of the fair market value of the assets of the plan.

(3)(A) After December 31, 1984, a plan may not hold any qualifying employer securities or qualifying employer real property (or both) to the extent that the aggregate fair market value of such securities and property determined on December 31, 1984, exceeds 10 percent of the greater of—

(i) the fair market value of the assets of the plan, determined on December 31, 1984, or

(ii) the fair market value of the assets of the plan determined on January 1, 1975.

(B) Subparagraph (A) of this paragraph shall not apply to any plan which on any date after December 31, 1974; and before January 1, 1985, did not hold employer securities or employer real property (or both) the aggregate fair market value of which determined on such date exceeded 10 percent of the greater of

(i) the fair market value of the assets of the plan, determined on such date, or

(ii) the fair market value of the assets of the plan determined on January 1, 1975.

(4)(A) After December 31, 1979, a plan may not hold any employer securities or employer real property in excess of the amount specified in regulations under subparagraph (B). This subparagraph shall not apply to a plan after the earliest date after December 31, 1974, on which it complies with such regulations.

(B) Not later than December 31, 1976, the Secretary shall prescribe regulations which shall have the effect of requiring that a plan divest itself of 50 percent of the holdings of employer securities and employer real property which the plan would be required to divest before January 1, 1985, under paragraph (2) or subsection (c) of this section (whichever is applicable).

(b) Exception

(1) Subsection (a) of this section shall not apply to any acquisition or holding of qualifying employer securities or qualifying employer real property by an eligible individual account plan.

(2)(A) If this paragraph applies to an eligible individual account plan, the portion of such plan which consists of applicable elective deferrals (and earnings allocable thereto) shall be treated as a separate plan—

(i) which is not an eligible individual account plan, and

(ii) to which the requirements of this section apply.

(B)(i) This paragraph shall apply to any eligible individual account plan if any portion of the plan's applicable elective deferrals (or earnings allocable thereto) are required to be invested in qualifying employer securities or qualifying employer real property or both—

(I) pursuant to the terms of the plan, or

(II) at the direction of a person other than the participant on whose behalf such elective deferrals are made to the plan (or a beneficiary).

(ii) This paragraph shall not apply to an individual account plan for a plan year if, on the last day of the preceding plan year, the fair market value of the assets of all individual account plans maintained by the employer equals not more than 10 percent of the fair market value of the assets of all pension plans (other than multiemployer plans) maintained by the employer.

(iii) This paragraph shall not apply to an individual account plan that is an employee stock ownership plan as defined in section 4975(e)(7) of Title 26.

(iv) This paragraph shall not apply to an individual account plan if, pursuant to the terms of the plan, the portion of any employee's applicable elective deferrals which is required to be invested in qualifying employer securities and qualifying employer real property for

any year may not exceed 1 percent of the employee's compensation which is taken into account under the plan in determining the maximum amount of the employee's applicable elective deferrals for such year.

(C) For purposes of this paragraph, the term "applicable elective deferral" means any elective deferral (as defined in section 402(g)(3)(A) of Title 26) which is made pursuant to a qualified cash or deferred arrangement as defined in section 401(k) of Title 26.

(3) CROSS REFERENCES.—

(A) For exemption from diversification requirements for holding of qualifying employer securities and qualifying employer real property by eligible individual account plans, see section 1104(a)(2) of this title.

(B) For exemption from prohibited transactions for certain acquisitions of qualifying employer securities and qualifying employer real property which are not in violation of 10 percent limitation, see section 1108(e) of this title.

(C) For transitional rules respecting securities or real property subject to binding contracts in effect on June 30, 1974, see section 1114(c) of this title.

(D) For diversification requirements for qualifying employer securities held in certain individual account plans, see section 1054(j) of this title.

(c) Election

(1) A plan which makes the election, under paragraph (3) shall be treated as satisfying the requirement of subsection (a)(3) of this section if and only if employer securities held on any date after December 31, 1974 and before January 1, 1985 have a fair market value, determined as of December 31, 1974, not in excess of 10 percent of the lesser of—

(A) the fair market value of the assets of the plan determined on such date (disregarding any portion of the fair market value of employer securities which is attributable to appreciation of such securities after December 31, 1974) but not less than the fair market value of plan assets on January 1, 1975, or

(B) an amount equal to the sum of (i) the total amount of the contributions to the plan received after December 31, 1974, and prior to such date, plus (ii) the fair market value of the assets of the plan, determined on January 1, 1975.

(2) For purposes of this subsection, in the case of an employer security held by a plan after January 1, 1975, the ownership of which is derived from ownership of employer securities held by the plan on January 1, 1975, or from the exercise of rights derived from such ownership, the value of such security held after January 1, 1975, shall be based on the value as of January 1, 1975, of the security from which ownership was derived. The Secretary shall prescribe regulations to carry out this paragraph.

(3) An election under this paragraph may not be made after December 31, 1975. Such an election shall be made in accordance with regulations prescribed by the Secretary, and shall be irrevocable. A plan may make an election under this paragraph only if on January 1, 1975, the plan holds no employer real property. After such election and before January 1, 1985 the plan may not acquire any employer real property.

(d) Definitions

For purposes of this section—

(1) The term "employer security" means a security issued by an employer of employees covered by the plan, or by an affiliate of such employer. A contract to which section 1108(b)(5) of this title applies shall not be treated as a security for purposes of this section.

(2) The term "employer real property" means real property (and related personal property) which is leased to an employer of employees covered by the plan, or to an affiliate of such employer. For purposes of determining the time at which a plan acquires employer real property for purposes of this section, such property shall be deemed to be acquired by the plan on the date on which the plan acquires the property or on the date on which the lease to the employer (or affiliate) is entered into, whichever is later.

(3)(A) The term "eligible individual account plan" means an individual account plan which is (i) a profit-sharing, stock bonus, thrift, or savings plan;

(ii) an employee stock ownership plan; or (iii) a money purchase plan which was in existence on September 2, 1974, and which on such date invested primarily in qualifying employer securities. Such term excludes an individual retirement account or annuity described in section 408 of Title 26.

(B) Notwithstanding subparagraph (A), a plan shall be treated as an eligible individual account plan with respect to the acquisition or holding of qualifying employer real property or qualifying employer securities only if such plan explicitly provides for acquisition and holding of qualifying employer securities or qualifying employer real property (as the case may be). In the case of a plan in existence on September 2, 1974, this subparagraph shall not take effect until January 1, 1976.

(C) The term "eligible individual account plan" does not include any individual account plan the benefits of which are taken into account in determining the benefits payable to a participant under any defined benefit plan.

(4) The term "qualifying employer real property" means parcels of employer real property—

(A) if a substantial number of the parcels are dispersed geographically;

(B) if each parcel of real property and the improvements thereon are suitable (or adaptable without excessive cost) for more than one use;

(C) even if all of such real property is leased to one lessee (which may be an employer, or an affiliate of an employer); and

(D) if the acquisition and retention of such property comply with the provisions of this part (other than section 1104(a)(1)(B) of this title to the extent it requires diversification, and sections 1104(a)(1)(C), 1106 of this title, and subsection (a) of this section).

(5) The term "qualifying employer security" means an employer security which is—

(A) stock,

(B) a marketable obligation (as defined in subsection (e) of this section), or

(C) an interest in a publicly traded partnership (as defined in section 7704(b) of Title 26), but only if such partnership is an existing partnership as defined in section 10211(c)(2)(A) of the Revenue Act of 1987 (Public Law 100-203).

After December 17, 1987, in the case of a plan other than an eligible individual account plan, an employer security described in subparagraph (A) or (C) shall be considered a qualifying employer security only if such employer security satisfies the requirements of subsection (f)(1) of this section.

(6) The term "employee stock ownership plan" means an individual account plan—

(A) which is a stock bonus plan which is qualified, or a stock bonus plan and money purchase

plan both of which are qualified, under section 401 of Title 26, and which is designed to invest primarily in qualifying employer securities, and

(B) which meets such other requirements as the Secretary of the Treasury may prescribe by regulation.

(7) A corporation is an affiliate of an employer if it is a member of any controlled group of corporations (as defined in section 1563(a) of Title 26, except that "applicable percentage" shall be substituted for "80 percent" wherever the latter percentage appears in such section) of which the employer who maintains the plan is a member. For purposes of the preceding sentence, the term "applicable percentage" means 50 percent, or such lower percentage as the Secretary may prescribe by regulation. A person other than a corporation shall be treated as an affiliate of an employer to the extent provided in regulations of the Secretary. An employer which is a person other than a corporation shall be treated as affiliated with another person to the extent provided by regulations of the Secretary. Regulations under this paragraph shall be prescribed only after consultation and coordination with the Secretary of the Treasury.

(8) The Secretary may prescribe regulations specifying the extent to which conversions, splits, the exercise of rights, and similar transactions are not treated as acquisitions.

(9) For purposes of this section, an arrangement which consists of a defined benefit plan and an indi-

vidual account plan shall be treated as 1 plan if the benefits of such individual account plan are taken into account in determining the benefits payable under such defined benefit plan.

(e) Marketable obligations

For purposes of subsection (d)(5) of this section, the term "marketable obligation" means a bond, debenture, note, or certificate, or other evidence of indebtedness (hereinafter in this subsection referred to as "obligation") if—

(1) such obligation is acquired—

(A) on the market, either (i) at the price of the obligation prevailing on a national securities exchange which is registered with the Securities and Exchange Commission, or (ii) if the obligation is not traded on such a national securities exchange, at a price not less favorable to the plan than the offering price for the obligation as established by current bid and asked prices quoted by persons independent of the issuer;

(B) from an underwriter, at a price (i) not in excess of the public offering price for the obligation as set forth in a prospectus or offering circular filed with the Securities and Exchange Commission, and (ii) at which a substantial portion of the same issue is acquired by persons independent of the issuer; or

(C) directly from the issuer, at a price not less favorable to the plan than the price paid currently for a substantial portion of the same issue by persons independent of the issuer;

(2) immediately following acquisition of such obligation—

(A) not more than 25 percent of the aggregate amount of obligations issued in such issue and outstanding at the time of acquisition is held by the plan, and

(B) at least 50 percent of the aggregate amount referred to in subparagraph (A) is held by persons independent of the issuer; and

(3) immediately following acquisition of the obligation, not more than 25 percent of the assets of the plan is invested in obligations of the employer or an affiliate of the employer.

(f) Maximum percentage of stock held by plan; time of holding or acquisition; necessity of legally binding contract

(1) Stock satisfies the requirements of this paragraph if, immediately following the acquisition of such stock—

(A) no more than 25 percent of the aggregate amount of stock of the same class issued and outstanding at the time of acquisition is held by the plan, and

(B) at least 50 percent of the aggregate amount referred to in subparagraph (A) is held by persons independent of the issuer.

(2) Until January 1, 1993, a plan shall not be treated as violating subsection (a) of this section solely by

holding stock which fails to satisfy the requirements of paragraph (1) if such stock—

(A) has been so held since December 17, 1987, or

(B) was acquired after December 17, 1987, pursuant to a legally binding contract in effect on December 17, 1987, and has been so held at all times after the acquisition.

7. 29 U.S.C. 1108(e) provides:

Exemptions from prohibited transactions

* * * * *

(e) Acquisition or sale by plan of qualifying employer securities; acquisition, sale, or lease by plan of qualifying employer real property

Sections 1106 and 1107 of this title shall not apply to the acquisition or sale by a plan of qualifying employer securities (as defined in section 1107(d)(5) of this title) or acquisition, sale or lease by a plan of qualifying employer real property (as defined in section 1107(d)(4) of this title)—

(1) if such acquisition, sale, or lease is for adequate consideration (or in the case of a marketable obligation, at a price not less favorable to the plan than the price determined under section 1107(e)(1) of this title),

(2) if no commission is charged with respect thereto, and

(3) if—

(A) the plan is an eligible individual account plan (as defined in section 1107(d)(3) of this title), or

(B) in the case of an acquisition or lease of qualifying employer real property by a plan which is not an eligible individual account plan, or of an acquisition of qualifying employer securities by such a plan, the lease or acquisition is not prohibited by section 1107(a) of this title.

8. 29 U.S.C. 1110(a) provides:

Exculpatory provisions; insurance

(a) Except as provided in sections 1105(b)(1) and 1105(d) of this title, any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part shall be void as against public policy.

9. 29 C.F.R. 2550.404a-1 provides:

SUBCHAPTER F—FIDUCIARY RESPONSIBILITY UNDER THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974

PART 2550—RULES AND REGULATIONS FOR FIDUCIARY RESPONSIBILITY

* * * * *

Investment duties.

(a) In general. Section 404(a)(1)(B) of the Employee Retirement Income Security Act of 1974 (the Act) provides, in part, that a fiduciary shall discharge his duties with respect to a plan 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 in the conduct of an enterprise of a like character and with like aims.

(b) *Investment duties.*

(1) With regard to an investment or investment course of action taken by a fiduciary of an employee benefit plan pursuant to his investment duties, the requirements of section 404(a)(1)(B) of the Act set forth in subsection (a) of this section are satisfied 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.

(2) For purposes of paragraph (b)(1) of this section, "appropriate consideration" shall include, but is not necessarily limited to,

(i) 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 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, and

(ii) Consideration of the following factors as they relate to such portion of the portfolio:

(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.

(3) An investment manager appointed, pursuant to the provisions of section 402(c)(3) of the Act, to manage all or part of the assets of a plan, may, for purposes of compliance with the provisions of paragraphs (b)(1) and (2) of this section, rely on, and act upon the basis of, information pertaining to the plan provided by or at the direction of the appointing fiduciary, if—

(i) Such information is provided for the stated purpose of assisting the manager in the performance of his investment duties, and

(ii) The manager does not know and has no reason to know that the information is incorrect.

(c) *Definitions.* For purposes of this section:

(1) The term investment duties means any duties imposed upon, or assumed or undertaken by, a person in connection with the investment of plan assets which make or will make such person a fiduciary of an employee benefit plan or which are performed by such person as a fiduciary of an employee benefit plan as defined in section 3(21)(A)(i) or (ii) of the Act.

(2) The term investment course of action means any series or program of investments or actions related to a fiduciary's performance of his investment duties.

(3) The term plan means an employee benefit plan to which title I of the Act applies.