No. 18-1165

In the Supreme Court of the United States

RETIREMENT PLANS COMMITTEE OF IBM et al.,

Petitioners,

v.

LARRY W. JANDER et al.,

Respondents.

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

BRIEF OF THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION, THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA, AND THE BUSINESS ROUNDTABLE AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

NANCY G. ROSS
Mayer Brown LLP
71 South Wacker Drive
Chicago, Illinois 60606
(312) 782-0600

NICOLE A. SAHARSKY
BRIAN D. NETTER
Counsel of Record
MATTHEW A. WARING
Mayer Brown LLP
1999 K Street, NW
Washington, DC 20006
(202) 263-3000
bnetter@mayerbrown.com

Counsel for Amici Curiae

Additional counsel listed on inside cover

Continued from front cover

KEVIN M. CARROLL
Securities Industry and Financial Markets Association
1101 New York Avenue, NW
Washington, DC 20005

Counsel for the Securities Industry and Financial Markets Association

DARYL JOSEFFER
JANET GALERIA
U.S. Chamber Litigation Center
1615 H Street, NW
Washington, DC 20062

Counsel for the Chamber of Commerce of the United States of America

LIZ DOUGHERTY
Business Roundtable
300 New Jersey Avenue, NW, Ste. 800
Washington, DC 20001

Counsel for the Business Roundtable

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

CASES

TABLE OF AUTHORITIES—continued

Page(s)

TABLE OF AUTHORITIES—continued

Page(s)

TABLE OF AUTHORITIES—continued

Page(s)

STATUTES, RULES AND REGULATIONS

TABLE OF AUTHORITIES—continued

Page(s)

TABLE OF AUTHORITIES—continued

Page(s)

MISCELLANEOUS

INTEREST OF THE *AMICI CURIAE*[1]

The Securities Industry and Financial Markets Association (SIFMA) is a trade association that brings together the shared interests of more than 600 securities firms, banks, and asset managers. SIFMA's mission is to promote policies and practices to expand and perfect markets, foster the development of new products and services, and create efficiencies for member firms, while preserving and enhancing the public's trust and confidence in the markets and the industry. SIFMA works to represent its members' interests locally and globally, including by regularly filing *amicus curiae* briefs in cases raising issues about the securities laws.

The Chamber of Commerce of the United States of America (the Chamber) is the world's largest business federation. It represents 300,000 direct members and indirectly represents the interests of more than 3 million companies and professional organizations of every size, in every industry sector, and from every region of the country. An important function of the Chamber is to represent the interests of its members in matters before Congress, the Executive Branch, and the courts. To that end, the Chamber regularly files *amicus curiae* briefs in cases that raise issues of concern to the nation's business community.

The Business Roundtable (the BRT) is an association of chief executive officers who lead companies with nearly 16 million employees and more than $7

[1] No party or counsel for a party authored this brief in whole or in part, and no one other than *amici*, their members, or their counsel funded the preparation or submission of this brief. *See* Sup. Ct. R. 37.6. Counsel for petitioners and respondents have provided their written consent to the filing of this brief.

trillion in annual revenues. The BRT was founded on the belief that businesses should play an active and effective role in the formulation of public policy, and the organization regularly files *amicus curiae* briefs in cases where important business interests are at stake.

Amici regularly file briefs in this Court's cases addressing the Employee Retirement Income Security Act (ERISA), 29 U.S.C. § 1001 *et seq*. *See, e.g.*, *Tibble* v. *Edison Int'l*, 135 S. Ct. 1823 (2015) (No. 13-550); *Fifth Third Bancorp* v. *Dudenhoeffer*, 573 U.S. 409 (2014) (No. 12-751).

The key issue in this case is whether a plaintiff in a case alleging a violation of ERISA's duty of prudence based on a drop in the price of company stock can withstand a motion to dismiss based on generalized allegations that the fiduciary should have acted differently. In *amici*'s view, the answer is no. As this Court recognized in *Fifth Third*, courts should carefully scrutinize these types of claims, because they are so easy for plaintiffs to allege and so costly to defend under the Second Circuit's approach that they threaten the very viability of ESOPs. *Amici*'s members have a substantial interest in the question presented, and they urge this Court to provide much-needed guidance to weed out meritless claims.

INTRODUCTION AND SUMMARY OF ARGUMENT

This is an ERISA case where respondents, former employees of IBM Corp. (IBM) and participants in its ERISA plan, allege that petitioners, the plan's fiduciaries, breached their duty of prudence in administering the plan. The ERISA plan is an employee stock ownership plan (ESOP), which invests primarily in IBM stock. Respondents sued when the price of the

company's stock dropped, claiming that petitioners knew certain adverse information about the company and failed to disclose that information or to prevent participants from buying company stock.

In *Fifth Third Bancorp* v. *Dudenhoeffer*, 573 U.S. 409 (2014), this Court considered a similar claim against an ESOP. The Court recognized that plaintiffs can easily assert a breach of fiduciary duty when the price of a company's stock drops, and so courts must take steps to "divide the plausible sheep from the meritless goats." *Id.* at 425. What is required, the Court explained, is "careful, context-sensitive scrutiny of a complaint's allegations." *Ibid.*

This case gives the Court the opportunity to offer concrete and helpful guidance so district courts can separate claims with merit from those without.

A. Meritless stock-drop cases pose serious risks to the continued viability of ESOPs. Stock-drop claims are easy to allege: When a public company's stock price drops, thereby decreasing the value of the company's ESOP, a plaintiffs' lawyer can swiftly file suit and assert that the fiduciaries should have done something different. These lawsuits can be lucrative because of the massive amounts of money invested in ESOPs. In the era before *Fifth Third*, dozens of these types of stock-drop lawsuits could be filed in federal court in any given year. Courts grew frustrated with meritless suits, and so they adopted a presumption that a fiduciary's investment in company stock was prudent.

In *Fifth Third*, this Court recognized the importance of ESOP plans, and the threats that meritless lawsuits posed to them. But the Court deter-

mined that the lower courts had gone too far in adopting a presumption of prudence. The duty of prudence is the same for all ERISA fiduciaries, the Court explained, but there is a way to "readily divide the plausible sheep from the meritless goats": by carefully scrutinizing a complaint's allegations. 573 U.S. at 425. In particular, the Court explained that a court should grant a motion to dismiss in an ESOP stock-drop case based on generalized allegations that a fiduciary should have done something differently. The plaintiff's burden, the Court warned, is a significant one—to plausibly allege that any reasonable fiduciary, balancing the costs and benefits of disclosing nonpublic information, would have chosen disclosure.

The cottage industry of ERISA stock-drop litigation declined in prominence after *Fifth Third*—in no small part because of the Court's emphasis that only cases with specific allegations tailored to a unique factual circumstance could potentially survive. The Second Circuit's understanding of *Fifth Third* dispenses with the requirement of particularity by endorsing a perfectly generic theory of stock-drop liability that could be replicated against dozens of public companies each year. That outcome would risk a return to the era of prolific stock-drop litigation. Such a return would be undesirable because it is costly to defend against meritless stock-drop lawsuits—and those costs are ultimately borne by plan participants.

B. This Court should reverse the Second Circuit's decision and provide important guidance to the lower courts.

First, the Court should explain that a fiduciary need not consider information obtained outside of a fiduciary capacity when making decisions in a fiduciary

capacity. Unlike under the law of trusts, ERISA recognizes that fiduciaries can wear multiple hats. They are fiduciaries only to the extent that they are performing discretionary functions associated with the plan; otherwise, their conduct is not subject to fiduciary scrutiny. Despite that key attribute of ERISA, the Second Circuit's approach requires ERISA fiduciaries to leverage all information that they acquire in their non-fiduciary roles to the benefit of plan participants. That rule is a mistake. The Court should hold that, when evaluating whether a fiduciary has made appropriate decisions on behalf of plan participants, the fiduciary need account for only that information reasonably available to the fiduciary as a fiduciary—regardless of what other corporate roles that individual may fill. A contrary rule would make ERISA's "two hats" concept unworkable and would discourage plan sponsors from appointing knowledgeable executives to fiduciary oversight boards, to the detriment of plan participants.

Second, this Court should hold that ERISA's fiduciary duties may not exceed the scope of existing federal securities laws in creating a cause of action for failing to provide disclosures about regulated securities. Nothing in ERISA speaks specifically to the sorts of disclosures that the plaintiffs insist should have been made by IBM's fiduciary committee. Rather, the plaintiffs' theory is that the requirement to make the disclosures is a component of ERISA's general duty of prudence. The standard of care theorized by plaintiffs cannot find an origin in the law of trusts because the law of trusts did not permit trustees to wear multiple hats in the first instance. Thus, ERISA could require the disclosures asserted by the plaintiffs only as a matter of federal common law. But the federal courts

have no authority to develop common law obligations when Congress has already imposed a standard.

Congress has imposed a robust system of securities laws on public companies like IBM. Indeed, an action alleging that IBM violated federal securities law for the same nondisclosure challenged here was swiftly dismissed. *Int'l Ass'n of Heat & Frost Insulators & Asbestos Workers Local #6 Pension Fund* v. *IBM Corp.*, 205 F. Supp. 3d 527 (S.D.N.Y. 2016). The complaint in this case can survive, then, only if ERISA imposes broader disclosure obligations than the federal securities laws. The Court should reject that proposition and instead hold that ERISA's general duty of prudence creates no obligations to make disclosures about publicly traded securities beyond what the securities laws already require. ERISA retains a role to play—offering, for example, equitable remedies against fiduciaries that would not be within the domain of the SEC—but ERISA's role should not be to permit individual judges to second-guess the regulatory regime carefully tailored by Congress and expert regulators.

Third, the Court should reaffirm its precedent that a plaintiff can state a claim for fiduciary breach only by alleging facts that plausibly suggest that no prudent fiduciary could have taken the defendants' course. The complaint in this case does not state a claim for fiduciary breach. The pleading standard requires the plaintiff to come forward with specifics. The complaint in this case offers only generalities—generalities that shed no light on the costs and benefits of the alternative courses of action for IBM's fiduciaries, or on whether a reasonable fiduciary could have followed IBM's course.

C. Without this close, careful scrutiny of stock-drop claims, employers wishing to invest in ESOPs will continue to face massive litigation costs and burdens. These costs and burdens, in turn, will provide a strong disincentive to offering ESOPs—which is precisely the opposite of what Congress wanted.

Congress has expressed a desire to facilitate employee ownership, based on its view that employee ownership would benefit employers and employees alike—an assessment supported by modern-day data. Fiduciary breach lawsuits should be available to combat fiduciary misconduct, but they should not be a weapon for extracting settlements from meritless lawsuits. If ERISA is interpreted to permit stock-drop lawsuits routinely to proceed to discovery, then fiduciaries will have every incentive to discontinue their ESOPs, contrary to Congress's design.

ARGUMENT

RESPONDENTS' COMPLAINT FAILS TO STATE A PLAUSIBLE CLAIM FOR BREACH OF THE DUTY OF PRUDENCE

A. The Second Circuit's Decision Will Encourage Meritless Stock-Drop Lawsuits Against ESOPs

1. Many companies offer ERISA retirement plans like the one at issue in this case. As the 401(k) plan has become the dominant form of retirement saving, these plans have grown in importance, to workers and to the American economy. These retirement plans "now hold over $5 trillion in assets"—and that is "without counting the even larger amount of assets that start in 401(k)s but end up in Individual Retirement Accounts (IRAs)." George S. Mellman & Geoffrey T. Sanzenbacher, *401(k) Lawsuits: What Are the*

Causes and Consequences? 2, Ctr. for Ret. Res., Issue Br. 18-8 (2018), bit.ly/2H53ygV.

When a company sponsors an ERISA retirement plan, it can choose which investments to offer to participants. Public companies often choose to include the companies' own stock as an investment option. These plans are known as employee stock ownership plans (ESOPs). Congress made the deliberate choice to encourage those plans because of the benefits they offer to employees and to the economy. Tax Reform Act of 1976, § 803(h), 90 Stat. 1520, 1590. Congress made fiduciaries in those plans subject to ERISA's fiduciary duties, 29 U.S.C. § 1104(a)(1)(A)-(B), but exempted them from ERISA's diversification requirement, 29 U.S.C. § 1104(a)(1)(C) and (2).

That encouragement has borne fruit. Now, more than six percent of retirement plan assets are invested in such funds, totaling hundreds of billions of dollars. See Inv. Co. Inst., *Frequently Asked Questions About 401(k) Plan Research* (June 2019), bit.ly/2H1YPfZ.

That volume of assets has proven alluring to plaintiffs' lawyers. Seemingly anytime a company's stock price drops, a plaintiffs' lawyer is ready to swoop in and file a lawsuit alleging that the ERISA plan's fiduciaries should have done something different to avoid the price drop. Before this Court's decision in *Fifth Third*, plaintiffs' lawyers routinely filed these types of lawsuits. Dozens of class-action lawsuits would be filed in a given year, each alleging that ERISA fiduciaries failed to protect plan participants from the decline in the value of their employer's stock. See Kivanç Kirgiz, *Trends in ERISA Stock Drop Litigation*, INSIDE COUNSEL (Aug. 20, 2012) (Kirgiz), bit.ly/2MV6DUi.

Many courts recognized how easy it was for plaintiffs to allege these types of fiduciary breach claims, and how costly it was for companies to defend against those meritless claims. That burden on companies was significant and raised a serious concern that employers might stop offering ESOPs altogether if these meritless suits were allowed to proceed. *White* v. *Marshall & Ilsley Corp.*, 714 F.3d 980, 987 (7th Cir. 2013); *see Conkright* v. *Frommert*, 559 U.S. 506, 517 (2010). Courts responded by affording ESOP fiduciaries a presumption that company stock offerings were prudent. *See, e.g.*, *Moench* v. *Robertson*, 62 F.3d 553, 571 (3d Cir. 1995).

Even with that presumption, lawsuits continued to proliferate. As many as 35 new class actions were filed in a single year alleging that fiduciaries breached their duties to ESOP participants by failing to anticipate stock drops. Kirgiz, *supra*.

2. This Court's decision in *Fifth Third* ushered in a new era. In that case, participants in an ESOP filed a class-action lawsuit, alleging that plan fiduciaries breached the duties of loyalty and prudence by continuing to offer an ESOP that bought and held Fifth Third stock, rather than disclosing inside information, selling the Fifth Third stock, or canceling the ESOP. 573 U.S. at 413. The Court appropriately noted that meritless stock-drop claims posed serious risks to the continued viability of ESOP ERISA plans. *Id.* at 424-25. The Court explained that the way to address that concern was not through a presumption that ESOPs are prudent. Such a presumption could not be justified under ERISA because "the same standard of prudence applies to all ERISA fiduciaries, including ESOP fiduciaries." *Id.* at 418-19.

Instead, a court should weed out bad claims though a "careful, context-sensitive scrutiny of a complaint's allegations." *Fifth Third*, 573 U.S. at 425. A motion to dismiss, the Court observed, is an "important mechanism for weeding out meritless claims." *Ibid.*

The Court provided a few guideposts for this close scrutiny. First, the court must consider the fiduciary's actions in light of the "'circumstances . . . prevailing' at the time the fiduciary" acts, and not with the benefit of hindsight. *Fifth Third*, 573 U.S. at 425 (quoting 29 U.S.C. § 1104(a)(1)(B)). Further, if the case is one where the plaintiffs allege that the fiduciaries should have disclosed or acted on confidential company information—as many stock-drop lawsuits do—then the plaintiffs have to allege, with specificity, what the fiduciaries should have done differently. That is, the plaintiff "must plausibly allege an alternative action that the defendant could have taken" that "a prudent fiduciary in the same circumstances would not have viewed as more likely to harm the fund than to help it." *Id.* at 428.

The Court recognized that fiduciaries must comply with the securities laws, and that those laws may limit an insider's ability to disclose confidential company information. *Fifth Third*, 573 U.S. at 428. Even if securities laws would have allowed the actions the plaintiffs claim the fiduciary should have taken, the Court warned that those actions may still have been unwise because they "would do more harm than good," such as if the fiduciary disclosed confidential information that caused the company's stock price to drop. *Id.* at 430.

Fifth Third made clear that the lower courts should not reflexively approve generic allegations of

imprudence. Instead, they should carefully scrutinize the complaint and require plaintiffs to plead, with specificity, not only what the fiduciaries should have done differently, but that taking that action was permitted by law and would not have made the plan worse off. Only when there were specific and plausible allegations of fiduciary breach would the fiduciaries be required to submit to discovery in stock-drop cases.

By and large, *Fifth Third* has had its intended effect. Since the decision, there has been a general decline in ERISA stock-drop litigation, and many (but not all) of the new actions that have been filed have been dismissed at the outset. *E.g.*, *Coburn* v. *Evercore Tr. Co.*, 844 F.3d 965 (D.C. Cir. 2016); *Fentress* v. *Exxon Mobil Corp.*, 304 F. Supp. 3d 569 (S.D. Tex. 2018); *In re HP ERISA Litig.*, No. 3:12-cv-6199-CRB, 2015 WL 3749565, at *1 (N.D. Cal. June 15, 2015), *aff'd sub nom. Laffen* v. *Hewlett-Packard Co.*, 721 F. App'x 642 (9th Cir. 2018); *but see, e.g.*, *In re SunTrust Banks, Inc. ERISA Litig.*, No. 1:08-cv-3384-RWS, 2015 WL 12724074 (N.D. Ga. June 18, 2015); *Gedek* v. *Perez*, 66 F. Supp. 3d 368 (W.D.N.Y. 2014). This Court reaffirmed its commitment to the principles in *Fifth Third* when it summarily reversed a decision that would have advanced a complaint that failed to meet the *Fifth Third* requirements. *Amgen Inc.* v. *Harris*, 136 S. Ct. 758 (2016) (per curiam).

3. The Second Circuit's decision in this case represents an aberration. The Second Circuit reversed the dismissal of a stock-drop complaint even though the complaint was plainly insufficient. The plaintiffs alleged that IBM breached its duty of prudence by failing to protect IBM's ESOP participants from IBM's overvalued stock, based on the fiduciaries' knowledge

of undisclosed problems with the performance of IBM's microelectronics unit. After the district court dismissed the complaint, *Jander* v. *Retirement Plans Cmte. of IBM*, 272 F. Supp. 3d 444 (S.D.N.Y. 2017), the Second Circuit reversed, *Jander* v. *Retirement Plans Cmte. of IBM*, 910 F.3d 620 (2d Cir. 2018). That court held that the plaintiffs had plausibly alleged that IBM's fiduciary committee knew that IBM's microelectronics unit was impaired (because the committee included IBM executives) and that the committee could have disclosed the overvaluation (because the IBM executives on the committee had responsibility, in their non-fiduciary jobs, for IBM's SEC disclosures). *Id.* at 628-29.

The court further found that the plaintiffs had plausibly alleged that the failure to disclose the microelectronics overvaluation hurt IBM's long-term prospects, on the theory that delayed disclosures become more costly over time. The court cast aside the district court's concern that the plaintiffs' theory was not particular to the facts of this case and based on untested economic theories. Under the Second Circuit's view, "the possibility of similar allegations in other ERISA cases does not undermine their plausibility here." *Id.* at 629. The court therefore concluded that a reasonable fiduciary would have prompted an earlier disclosure. *Ibid.*

The Second Circuit's permissive motion-to-dismiss standard threatens a return to the time before *Fifth Third*. The Second Circuit's approach runs counter to a series of established ERISA standards—not the least of which being this Court's decision in *Fifth Third*—and creates a morass of bad law and bad policy. If permitted to stand, plan participants would

lose access to valuable investment opportunities, contrary to Congress's expressed intent.

If this Court were to accept the Second Circuit's position, it would no doubt encourage lawsuits like this one. The allegations against IBM are generic; they are the type of allegations that could be levied against just about any public company that offers employer stock in one of the Nation's 555,000 401(k) plans. *See* Inv. Co. Inst., Frequently Asked Questions About 401(k) Plan Research, *supra*. If, however, the Court reinstates the judgment of the district court, then this area of law will continue along the trajectory established by *Fifth Third*—where successful ERISA stock-drop actions are rare, as they should be.

B. This Court Should Reverse The Second Circuit's Decision And Provide Additional Guidance For Evaluating Stock-Drop Complaints

The Second Circuit committed a series of errors in ruling that the complaint in this case was sufficient to state a claim for breach of ERISA's fiduciary duties. To state a claim, the plaintiffs were required to allege plausibly that an individual, while acting in a fiduciary capacity, breached the standard of care prescribed by ERISA and thereby caused harm to the plan.

In enacting ERISA, Congress departed from trust law by permitting fiduciaries to serve non-fiduciary functions for the same company, so long as they act in the sole interest of participants when serving fiduciary functions. The Second Circuit failed to honor that distinction between fiduciary and non-fiduciary acts. Instead, it adopted a standard of care that impermissibly would allow ERISA to supersede federal securities laws, and it deemed plausible a generic theory of

injury that makes sense neither in the abstract nor in the particular factual setting of this case.

1. ERISA provides that fiduciaries may wear two hats.

a. The complaint in this lawsuit alleges that, because IBM appointed senior executives to the committee overseeing its retirement plan, those executives should have used their knowledge that the microelectronics unit was troubled and their power to influence IBM's SEC disclosures to alert plan participants that IBM's stock was overvalued. J.A. 134.

By accepting this theory of liability, the Second Circuit conflated the fiduciary and non-fiduciary roles of IBM's committee members. In practical terms, the Second Circuit's approach would eviscerate the "two hats" rule, which recognizes that individuals may alternate between corporate and fiduciary roles. In place of that rule, the Second Circuit would require fiduciaries to act always in their fiduciary capacity, treating all information that they acquire (in their fiduciary capacity or otherwise) as the participants' information, and using all of their powers (as fiduciaries or otherwise) for plan participants.

ERISA expressly *permits* individuals to serve in multiple capacities. This Court should therefore hold that, when making decisions on behalf of plan participants, a fiduciary must consider the information reasonably available to individuals in their fiduciary capacity, and a fiduciary must weigh the responses available to individuals acting in a fiduciary capacity. However, fiduciaries do not need to assess information acquired outside a fiduciary context, nor must they use their corporate powers to serve fiduciary functions.

b. Although "ERISA abounds with the language and terminology of trust law," *Firestone Tire & Rubber Co.* v. *Bruch*, 489 U.S. 101, 110 (1989), Congress did not merely codify the law of trusts when it enacted ERISA. See *Varity Corp.* v. *Howe*, 516 U.S. 489, 497 (1996); *Mertens* v. *Hewitt Assocs.*, 508 U.S. 248, 251 (1993). Rather, after completing "'a decade of congressional study of the Nation's private employee benefit system,'" Congress adopted "a 'comprehensive and reticulated statute'" designed to depart from trust law in critical respects. *Mertens*, 508 U.S. at 251 (quoting *Nachman Corp.* v. *Pension Benefit Guar. Corp.*, 446 U.S. 359, 361 (1980)). Those "depart[ures] from common-law trust requirements" are reflected throughout ERISA: in "the language of the statute, its structure, [and] its purposes." *Varity Corp.*, 516 U.S. at 497.

Most notably for present purposes, Congress departed from trust-law norms in permitting employers also to serve as plan administrators and fiduciaries. Under the common law, a trustee cannot hold a separate post in which his interests are at odds with those of his trust's beneficiaries. *NLRB* v. *Amax Coal Co.*, 453 U.S. 322, 329-30 (1981). But ERISA specifically contemplates that officers and employees of the plan sponsor will serve as fiduciaries. *See* 29 U.S.C. §§ 1002(16), 1108(c)(3).

Under ERISA, then, even when individuals assume fiduciary responsibility over a benefits plan, they are fiduciaries only "'to the extent' that [they] 'exercise[] any discretionary authority or discretionary control respecting management' of the plan, or 'ha[ve] any discretionary authority or discretionary responsibility in the administration' of the plan." *Varity Corp.*, 516 U.S. at 498 (quoting 29 U.S.C. § 1002(21)(A)(iii)). Even as to an individual who acts as a fiduciary in

some contexts, "ERISA's fiduciary duty requirement simply is not implicated" when the fiduciary acts in a *non-fiduciary* context. *Hughes Aircraft Co.* v. *Jacobson*, 525 U.S. 432, 444 (1999). ERISA thus permits fiduciaries to wear two hats; its concern is "that the fiduciary with two hats wear only one at a time, and wear the fiduciary hat when making fiduciary decisions." *Pegram* v. *Herdrich*, 530 U.S. 211, 225 (2000). A defendant's fiduciary status must therefore be assessed at the outset of any challenge:

> In every case charging breach of ERISA fiduciary duty, then, the threshold question is not whether the actions of some person employed to provide services under a plan adversely affected a plan beneficiary's interest, but whether that person was acting as a fiduciary (that is, was performing a fiduciary function) when taking the action subject to complaint.

Id. at 226.

The Court applied the two-hats standard to a question of participant disclosures in *Varity Corp.* In that case, the plaintiffs alleged that Varity, the corporate parent of their former employer, Massey-Ferguson, Inc., had encouraged them to transfer their employment to Massey Combines, a separately incorporated Varity subsidiary, by making false representations about the security of the benefits plans at Massey Combines. The Court held that these misrepresentations constituted fiduciary acts because "Varity *intentionally* connected its statements about Massey Combines' financial health to statements it made about the future of benefits, so that its intended communication about the security of benefits was rendered materially misleading." 516 U.S. at 505.

In so holding, the Court emphasized that it was *not* holding "that Varity acted as a fiduciary simply because it made statements about its expected financial condition or because an ordinary business decision turned out to have an adverse impact on the plan." 516 U.S. at 505 (internal quotation marks and alteration omitted).

The Second Circuit's approach would eliminate those limitations on the Court's holding. If ESOP fiduciaries must use their corporate powers in the sole interests of ESOP participants, then there are no nonfiduciary "statements about [a company's] expected financial condition." And if ESOP fiduciaries must use corporate information for the benefit of ESOP participants, then there can be no "ordinary business decisions" that end up affecting the ESOP. Rather, under the Second Circuit's approach, fiduciaries would always need to wear their fiduciary hats.

But the statute applies fiduciary duties to individuals only "to the extent" that they act in a fiduciary capacity, not perpetually. *See* 29 U.S.C. § 1002(21)(A). And Congress determined not to create unpredictable traps that would increase the burdens of administering benefit plans. *See Mass. Mut. Life Ins. Co.* v. *Russell*, 473 U.S. 134, 148 n.17 (1985). Neither of these objectives would be served by the Second Circuit's rule.

c. In addition to undermining the two-hats rule, the Second Circuit's reinterpretation of a fiduciary's role makes exceedingly bad policy. The plaintiffs could not have alleged that IBM's Retirement Plans Committee had an obligation to act on inside information about the microelectronics division if the Committee had not included senior executives (namely,

the Chief Financial Officer, the Chief Accounting Officer, and the General Counsel) who allegedly possessed knowledge of that division's true valuation. But IBM should be lauded—not penalized—for appointing such individuals to serve on its Committee.

Individuals who have risen to senior management posts bring a breadth of knowledge, experience, judgment, and financial sophistication that can help fiduciary committees to make good decisions on behalf of plan participants. It likewise benefits plan participants to have senior executives who are well versed in the nuances of employee benefits. So it would not advance Congress's statutory design—to establish boards of fiduciary experts making critical decisions on behalf of participants—to incentivize corporations to downgrade committee membership, just in order to ensure that fiduciaries lack information that would create fiduciary exposure and disruption.

d. Just as fiduciaries must honor the wall between their corporate and fiduciary capacities, plaintiffs should be subject to the same limitation: they should not be permitted to use information that a fiduciary obtained in a non-fiduciary capacity to require the individual (when later wearing a fiduciary hat) to take action.

That approach is consistent with the objective standard of prudence prescribed by the statute. A fiduciary must act "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims," 29 U.S.C. § 1104(a)(1)(B). The statute thus asks how individuals—when perched within their fiduciary bubbles—would process the information typically

available to individuals in similar circumstances. There is no statutory obligation for fiduciaries to acquire inside information unavailable to the market; so there should be no obligation for fiduciaries to leverage non-fiduciary information for fiduciary purposes.

The Second Circuit's failure to honor the division between fiduciary and non-fiduciary activities would eliminate Congress's chosen mechanism for resolving conflicts. When acting as fiduciaries, individuals must act "solely in the interest of the participants and beneficiaries." 29 U.S.C. § 1104(a)(1). But when wearing a different hat, fiduciaries may well have obligations to advance others' interests. The two-hats rule permits individuals to serve different roles at different times. The Second Circuit's rule would create conflicts for fiduciaries that could not be resolved.

2. ERISA should not be interpreted to create its own system of securities law.

a. Apart from the question of who constitutes a fiduciary—and for what purposes—the Second Circuit erred by concluding that fiduciaries can be liable under ERISA for failures to disclose that are not actionable under federal securities laws.

Although ERISA identifies specific disclosures that fiduciaries must make to plan participants, *see* 29 U.S.C. §§ 1022, 1024(b)(1), 1025(a), none of its terms address the sorts of public statements about future stock performance that are at issue here. The Second Circuit held that the additional disclosures were required as a component of ERISA's duty of prudence.

Rather than opening the door to a new regime of quasi-securities enforcement, this Court should adopt

a simple rule: if an ERISA claim for breach of fiduciary duty sounds in securities fraud based on public disclosures to the market, but is not actionable under federal securities laws, then it is not actionable under ERISA, either.

b. This Court interprets ERISA's duty of prudence as part of the "federal common law of rights and obligations under ERISA-regulated plans." *Pilot Life Ins. Co.* v. *Dedeaux*, 481 U.S. 41, 56 (1987). The Court will sometimes resort to trust law to understand the contours of fiduciary responsibility. *Firestone*, 489 U.S. at 110. But fiduciary-duty precedents will not inform Congress's intent here, because the question presented—whether a fiduciary wearing two hats has the obligation to make disclosures based on information acquired in a non-fiduciary capacity—could not have arisen under the common law of trusts. *See Pegram*, 530 U.S. at 225 ("[T]he analogy between ERISA fiduciary and common law trustee becomes problematic . . . because the trustee at common law characteristically wears only his fiduciary hat when he takes action to affect a beneficiary, whereas the trustee under ERISA may wear different hats.").

For purposes of this case, it is sufficient that Congress has elsewhere established an intricate system of disclosures specifically tailored to securities laws, coupled with a civil enforcement regime that balances the interests of investors against the systemic costs of incentivizing meritless lawsuits. This Court should not use its gap-filling role to arrogate to the federal courts the responsibility to set new rules of federal securities regulation.

Constitutional principles of separation of powers demand as much. "Once Congress, exercising its delegated powers, has decided the order of priorities in a

given area, it is for the Executive to administer the laws and for the courts to enforce them when enforcement is sought." *Tennessee Valley Auth.* v. *Hill*, 437 U.S. 153, 194 (1978). This Court's "commitment to the separation of powers is too fundamental to continue to rely on federal common law by judicially decreeing what accords with common sense and the public weal when Congress has addressed the problem." *City of Milwaukee* v. *Illinois*, 451 U.S. 304, 315 (1981) (internal quotation marks omitted); *see also Dutra Group* v. *Batterton*, 139 S. Ct. 2275, 2286 (2019) (declining to expand federal admiralty law beyond the contours of the Jones Act).

Likewise, Congress provided within the text of ERISA that, except where expressly indicated, the statute should not be "construed to alter, amend, modify, invalidate, impair, or supersede any law of the United States . . . or any rule or regulation issued under such law." 29 U.S.C. § 1144(d). Combining these constitutional and statutory norms, this Court has recognized that "the scope of permissible judicial innovation is narrower in areas where other federal actors are engaged." *Fifth Third*, 573 U.S. at 429.

Here, it is only sensible for the securities laws to govern securities violations. Corporate executives make statements about corporate performance in their corporate capacities—not in their fiduciary capacities. The securities laws properly govern those disclosures.

c. The involvement of other federal actors in securities regulation is beyond reasonable dispute. After enacting the Securities Act of 1933, Congress adopted the Securities Exchange Act of 1934 to "perfect the mechanisms of a national market system for securities." 15 U.S.C. § 78b. Since 1934, the SEC has had

primary responsibility for enforcing the federal securities laws.

The SEC enforces a robust disclosure system, under which public companies must make annual (10-K), quarterly (10-Q), and intermediate (8-K) disclosures of financial results, with additional disclosures governing shareholder meetings, executive compensation, insider transactions, beneficial ownership, and business combinations—not to mention the disclosures (such as a registration statement and prospectus) that accompany the issuance of a security in the first instance. Violations of these disclosure requirements can be enforced through criminal or civil sanctions or through private rights of action. *See, e.g.*, 15 U.S.C. §§ 77x, 78ff(a), 80a-48, 80b-17 (criminal sanctions); 15 U.S.C. §§ 78o(b)(4) and (6), 78o-4 to 7, 78q-1 (civil sanctions); *Central Bank of Denver, N.A.* v. *First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994) (private right of action).

When Congress has deemed the securities laws to be insufficiently tailored to the needs of the marketplace, it has amended the securities laws. *See, e.g.*, Securities Acts Amendments of 1964, 78 Stat. 565; Securities Acts Amendments of 1975, 89 Stat. 97; Private Securities Litigation Reform Act of 1995, 109 Stat. 737; Securities Litigation Uniform Standards Act of 1998, 112 Stat. 3227. The SEC has simultaneously pursued a robust regulatory and enforcement agenda. *See generally* 17 C.F.R. parts 200-301.

d. The Second Circuit held that, even accepting that there was no cause of action against IBM for violating the securities laws, there was still a viable action under ERISA. That approach is erroneous. Because Congress intended for the SEC and federal securities laws to dictate federal securities policy,

ERISA should not be interpreted to imply a cause of action where the securities laws offer none.

Under that rule, ERISA would retain an important role. Although a breach of federal securities laws would not necessarily mean that fiduciaries had breached their duties, if there were a circumstance in which both the securities laws and ERISA were violated, then ERISA would provide access to additional remedies that arise under the law of equity. *See, e.g.*, *U.S. Airways, Inc.* v. *McCutchen*, 663 F.3d 671, 678–79 (3d Cir. 2011) (recognizing reformation of a plan's terms as a remedy available for fiduciary breach under ERISA); *Chao* v. *Malkani*, 452 F.3d 290 (4th Cir. 2006) (affirming removal of a fiduciary for breach of ERISA's duties).

In any event, allowing ERISA to exceed the footprint of the securities laws would be disruptive and costly to regulated parties—and all in the name of permitting securities lawsuits that Congress has necessarily deemed undesirable. This Court should not allow such actions.

3. The plaintiffs did not plausibly allege a breach of the standard of care.

ERISA plaintiffs must plausibly allege that the defendants caused harm to the plan by breaching those duties.

The Second Circuit made two primary errors in concluding that Plaintiffs had satisfied this test:

a. First, the court applied the wrong legal standard. In *Fifth Third*, this Court held that an ERISA stock-drop plaintiff must plausibly allege "that a prudent fiduciary in the defendant's position could not have concluded that stopping purchases" of employer

stock would do more harm than good. 573 U.S. at 429-30. Despite the clarity of that rule, the Second Circuit pondered whether it would be sufficient for a plaintiff to allege only that a prudent fiduciary *would* not have shared the defendants' conclusion, even if a prudent fiduciary *could* have agreed. 910 F.3d at 628 ("We need not here decide which of the two standards the parties champion is correct.").

This is, however, an important issue that goes to the essence of ERISA's fiduciary responsibility. A fiduciary will rarely be presented with a binary decision in which one option is only virtue while the other is only vice. Courts therefore regularly recognize that multiple fiduciaries can decide similar questions differently without either fiduciary violating ERISA. *See, e.g.*, *Chao* v. *Merino*, 452 F.3d 174, 182 (2d Cir. 2006) (ERISA imposes on fiduciaries no "duty to take any particular course of action if another seems preferable") (internal quotation marks omitted). A rule of law that imposes liability for fiduciaries who acted contrary to how some alternative fiduciary "would" have acted would divest fiduciaries of the discretion to use their judgment to do what they actually think is best. They would instead be forced to guess how other fiduciaries would act. *See, e.g.*, *Renfro* v. *Unisys Corp.*, 671 F.3d 314, 322 (3d Cir. 2011) (approving "of an approach examining whether a questioned decision led to objectively prudent investments"); *Kuper* v. *Iovenko*, 66 F.3d 1447 (6th Cir. 1995) (similar).

In the stock-drop context, this Court already decided, in *Fifth Third*, that the appropriate question is whether a prudent individual *could* have reached the same decision. 573 U.S. at 429-30. But even if this were an open question, *Twombly* quickly confirms this Court's holding. A plaintiff cannot state a claim

merely by alleging conduct that is consistent with *either* lawful or unlawful conduct. *Bell Atl. Corp.* v. *Twombly*, 550 U.S. 544, 554 (2007). The same principle applies here. If *any* prudent fiduciary could have concluded that taking action on IBM stock would have been a net negative, then the plaintiffs necessarily cannot use the failure of these defendants to take action as a basis for "divid[ing] the plausible sheep from the meritless goats." *Fifth Third*, 573 U.S. at 425.

b. The Second Circuit also erred by accepting a generic theory of liability. The court endorsed the plaintiffs' reference to an academic theory that a firm suffers an ever-increasing reputational burden by delaying corrective disclosures. 910 F.3d at 629-30.

At most, the plaintiffs have identified a phenomenon that exists *in the aggregate*, when averaged across many corporate disclosures. But that hardly suffices to imply how IBM's particular stock would have responded to an earlier disclosure led by the fiduciary committee. And even if the plaintiffs' allusion to academic research could readily be applied to IBM stock, it would not dictate that IBM's plan—a net seller of IBM stock, *Jander*, 272 F. Supp. 3d at 450—would have benefited from an earlier depreciation of the security.

This is all to say that a superficial reference to an academic theory should give the Court little comfort that the plaintiffs have identified the rare circumstance in which 401(k) plan fiduciaries should be making extraordinary disclosures of inside corporate information. After all, ERISA's "fiduciary duty of care . . . requires prudence, not prescience." *DeBruyne* v. *Equitable Life Assurance Soc'y of the U.S.*, 920 F.2d 457, 465 (7th Cir. 1990). Unless the plaintiffs can explain how, in the particular case of IBM, an extraordinary

disclosure was so clearly beneficial that every reasonable fiduciary would have made one, then the plaintiffs have not plausibly alleged a fiduciary breach.

The Second Circuit failed to "weed[] out meritless claims." *Fifth Third*, 573 U.S. at 425.

C. The Second Circuit's Approach Imperils Employee Stock Ownership

1. Unless this Court corrects the errors identified above, ERISA stock-drop lawsuits can be expected to proliferate. "[T]he prospect of discovery in a suit claiming breach of fiduciary duty is ominous, potentially exposing the ERISA fiduciary to probing and costly inquiries and document requests about its methods and knowledge at the relevant times." *Pension Ben. Guar. Corp. ex rel. Saint Vincent Catholic Med. Centers Ret. Plan* v. *Morgan Stanley Inv. Mgmt. Inc.*, 712 F.3d 705, 719 (2d Cir. 2013). That burden brings with it high risks that ESOP offerors will submit to *in terrorem* settlements. Such settlements would then set into motion a vicious cycle of the filing and settling of meritless claims.

These risks are not hypothetical. *See* Kirgiz, *supra*. This Court has acknowledged, from ERISA's early days, that the statute reflects a balance between protecting the interests of plan participants and "encouraging the formation of employee benefit plans." *Pilot Life*, 481 U.S. at 54. Indeed, in adopting ERISA, Congress "resolved innumerable disputes between powerful competing interests—not all in favor of potential plaintiffs." *Mertens*, 508 U.S. at 262. Increasing the risks of operating an ESOP will naturally prompt employers to drop them.

2. Discouraging the formation and retention of ESOPs would be exactly the opposite of what Congress intended. When ERISA was under development by Congress, ESOPs were viewed as a win-win proposition: "provid[ing] low-cost capital for the employer" and "the most important form of job enrichment known to man: Enrichment for each employee in the form of a reasonable capital holding," which was believed to "generate labor-management harmony" and to curtail "the structurally inevitable inflation" that results from employees whose interests fall out of alignment with their employers. 119 CONG. REC. 40,754 (Dec. 11, 1973) (statement of Sen. Russell B. Long, Chairman, S. Comm. on Fin.). In practice, those lofty objectives are frequently met. When businesses take steps to encourage employee ownership, they tend to see increased productivity and better employee relations. *See* Corey M. Rosen, *Employee Ownership and Corporate Performance*, *in* 1 EMPLOYEE STOCK OWNERSHIP PLANS 2-1 to 2-3 (Robert W. Smiley, Jr. et al. eds., 2006).

Instead of prompting wholesale abandonments of ESOPs, contrary to Congress's design, this Court should continue down the path articulated by *Fifth Third*—a path that prompts fiduciaries to act thoughtfully in the interests of participants, not out of fear that they will be targeted with a cookie-cutter lawsuit.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

KEVIN M. CARROLL
Securities Industry and Financial Markets Association
1101 New York Ave., NW
Washington, DC 20005

Counsel for the Securities Industry and Financial Markets Association

DARYL JOSEFFER
JANET GALERIA
U.S. Chamber Litigation Center
1615 H Street, NW
Washington, DC 20062

Counsel for the Chamber of Commerce of the United States of America

LIZ DOUGHERTY
Business Roundtable
300 New Jersey Ave., NW, Ste. 800
Washington, DC 20001

Counsel for the Business Roundtable

NICOLE A. SAHARSKY
BRIAN D. NETTER
Counsel of Record
MATTHEW A. WARING
Mayer Brown LLP
1999 K Street, NW
Washington, DC 20006
(202) 263-3000
bnetter@mayerbrown.com

NANCY G. ROSS
Mayer Brown LLP
71 South Wacker Drive
Chicago, Illinois 60606
(312) 782-0600

Counsel for Amici Curiae

AUGUST 2019