No. _____

In the Supreme Court of the United States

JEFFREY SCHWEITZER, JONATHAN SAPP, RAUL RAMOS, DONALD FOWLER,
Petitioners,

v.

INVESTMENT COMMITTEE OF THE PHILLIPS 66 SAVINGS PLAN, SAM FARACE, JOHN DOES 1-10, INCLUSIVE,
Respondents.

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

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Is an ERISA fiduciary entitled to dismissal on the pleadings of a plan participant's claim that the fiduciary imprudently maintained an undiversified, single-stock fund in a defined contribution plan where the plan does not restrict participants' ability to sell their shares of the undiversified fund and reinvest in other, diversified funds?

LIST OF PARTIES TO THE PROCEEDINGS

Petitioners Jeffrey Schweitzer, Jonathan Sapp, Raul Ramos, and Donald Fowler were plaintiffs in the district court and appellants in the court of appeals.

The following respondents were defendants in the district court and appellees in the court of appeals: Investment Committee of the Phillips 66 Savings Plan, Sam Farace, and John Does 1-10.

RELATED PROCEEDINGS

This case arises from the following proceedings:

Schweitzer on behalf of Phillips 66 Sav. Plan v. Inv. Comm. of Phillips 66 Sav. Plan, 312 F. Supp. 3d 608 (S.D. Tex. 2018)

Schweitzer v. Inv. Comm. of Phillips 66 Sav. Plan, 960 F.3d 190 (5th Cir. 2020)

There are no related proceedings.

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The Fifth Circuit's opinion is reported at 960 F.3d 190 (5th Cir. 2020). App. 1a. The order of the Fifth Circuit denying the plaintiffs' petition for rehearing en banc is not reported. App. 48a. The district court's order granting the defendants' motion to dismiss is reported at *Schweitzer on behalf of Phillips 66 Sav. Plan v. Inv. Comm. of Phillips 66 Sav. Plan*, 312 F. Supp. 3d 608 (S.D. Tex. 2018).

JURISDICTION

The Fifth Circuit filed its opinion on May 22, 2020, and denied a petition for rehearing en banc on October 8, 2020. This Court has jurisdiction under 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STAUTORY PROVISIONS INVOLVED

29 U.S.C. § 1104(a)(1)(B) provides that:

> a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries 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)(C) requires a fiduciary to "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."

STATEMENT

A. Statutory background

Congress enacted ERISA to "promote the interests of employees and their beneficiaries in employee benefit

plans." *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 90 (1983). Congress's primary concern was "the mismanagement of funds accumulated to finance employee benefits and the failure to pay employees benefits from accumulated funds." *Massachusetts v. Morash*, 490 U.S. 107, 115 (1989). The "inadequacy" of existing management standards, it found, was a threat to "the soundness and stability of plans." 29 U.S.C. § 1001(a). Congress thus imposed safeguards intended to "insure against the possibility that the employee's expectation of the benefit would be defeated through poor management." *Morash*, 490 U.S. at 115.

To that end, the law imposes "strict standards of trustee conduct … derived from the common law of trusts." *Fifth Third Bancorp v. Dudenhoeffer*, 573 U.S. 409, 416 (2014). Those standards include "a number of detailed duties and responsibilities, which include 'the proper management, administration, and investment of [plan] assets.'" *Mertens v. Hewitt Assocs.*, 508 U.S. 248, 251–52 (1993). "Courts have often called these fiduciary duties the 'highest known to the law.'" *Stegemann v. Gannett Co., Inc.*, 970 F.3d 465, 469 (4th Cir. 2020).

This case involves two distinct but related duties under ERISA. *First*, the duty to diversify requires a plan fiduciary to "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). *Second*, the duty of prudence requires that fiduciaries act "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use." *Id.* § 1104(a)(1)(B). Prudence requires fiduciaries to "determine that each investment is

reasonably designed, as part of the portfolio, to further the purposes of the plan, taking into consideration the risk of loss and the opportunity for gain." App. 9a (cleaned up).

Although the two statutory duties are separate, they significantly "overlap[]," because diversification is itself a key principle of prudent investing. *Id.* at 5a. "In a 'diversified' portfolio, that is, one which contains a variety of investments, 'the risks of the various components of such a portfolio tend to cancel out; that is the meaning and objective of diversification.'" *Gannett*, 970 F.3d at 475 (quoting *Summers v. State St. Bank & Tr. Co.*, 453 F.3d 404, 409 (7th Cir. 2006)). Thus, "trust law, ERISA case law, and the text of ERISA all understand diversification as an element of prudence." *Id.* at 477; *see* 29 U.S.C. § 1104(a)(2) (recognizing that "the prudence requirement" normally "requires diversification"); *Armstrong v. LaSalle Bank Nat'l Ass'n*, 446 F.3d 728, 732 (7th Cir. 2006) ("The duty to diversify is an essential element of the ordinary trustee's duty of prudence … ."); *see also* Restatement (Third) of Trusts § 90 cmt. e(1). "After all, the point of the duty to diversify is not diversification for diversification's sake, but risk management." *Gannett*, 970 F.3d at 477.

Finally, section 1104(a)(2) exempts investments in employer stock from "the diversification requirement of paragraph (1)(C) and the prudence requirement (only to the extent it requires diversification) of paragraph (1)(B)." Congress would not have exempted employer stock from the prudence requirement "to the extent it requires diversification" unless diversification was an element of prudence.

Accordingly, ERISA actually creates two duties to diversify: the freestanding diversification duty under section 1104(a)(1)(C), and the diversification required for

prudent investing under section 1104(a)(1)(B). Under the "somewhat circular" structure of those provisions, "each duty implicates the other." *Gannett*, 970 F. 3d at 474 n.7.

B. Factual and procedural background

In 2012, oil-and-gas company ConocoPhillips Corp. spun off its downstream refining, marketing, and transportation operations to a new, independent company called Phillips 66. App. 2a. Before the spinoff, the retirement accounts of many ConocoPhillips employees included investments in single-stock funds of the company's own stock. *Id.* The accounts of employees who transferred from ConocoPhillips to the newly spun-off Phillips 66, for that reason, included investments in ConocoPhillips stock. *Id.*

As a consequence, Phillips 66's employee retirement plan wound up with a substantial proportion of its investments in single-stock funds exclusively holding stock in ConocoPhillips—now a separate company. *Id.* at 2a–3a. Indeed, about 30% of the plan's total assets at the time of the spinoff were invested in ConocoPhillips stock. *Id.* at 3a. But although the defendants froze new investments in the single-stock funds, they continued maintaining the funds for years as ConocoPhillips stock fluctuated in value—first rising, then plummeting to less than half its value. *Id.* at 3a.

Four participants in Phillips 66's retirement plan filed suit under ERISA, claiming that Phillip 66's investment committee violated its fiduciary duty to diversify under section 1104(a)(1)(C) and duty of prudence under section 1104(a)(1)(B) by failing to monitor and timely divest from the ConocoPhillips stock funds. *Id.* at 3a–4a. The district court granted the defendants' motion to dismiss for failure to state a claim. *Id.* at 4a. As to the plaintiffs' duty-to-

diversify claim, the court held that the complaint did not allege a breach of the duty because the participants could have withdrawn from the ConocoPhillips stock funds and independently created their own, more diversified portfolios. *Id.* As to the duty-of-prudence claim, the court held that the claim was foreclosed by this Court's decision in *Dudenhoeffer*. *Id.*

The Fifth Circuit affirmed, but for different reasons. Relying on the Second Circuit's unpublished decision in *Young v. Gen. Motors Inv. Mgmt. Corp* ., the court rejected the plaintiffs' duty-to-diversify claim on the ground that the duty "looks to a pension plan as a whole, not to each investment option." *Id.* at 7a–9a (citing *Young v. Gen. Motors Inv. Mgmt. Corp.*, 325 F. App'x 31, 33 (2d Cir. 2009)). In a defined-contribution plan like the one at issue here, it held, fiduciaries "need only provide investment options that enable participants to create diversified portfolios; they need not ensure that participants actually diversify their portfolios." *Id.* at 8a. Because the plaintiffs had "not alleged that the Fiduciaries did not offer sufficient investment options," it concluded, "their § 1104(a)(1)(C) claim fails." *Id.*

As to the plaintiffs' duty-of-prudence claim, on the other hand, the Fifth Circuit held that the plaintiffs had "plausibly alleged that the ConocoPhillips Funds, by its resulting concentration of investment, became an imprudent investment with the spinoff." *Id.* at 13a. In reaching that conclusion, the court first rejected the district court's conclusion that *Dudenhoeffer* foreclosed the plaintiffs' claim. *Id.* at 11a. "Unlike the claim in *Dudenhoeffer*," it noted, the plaintiffs' claim "that the ConocoPhillips Funds were imprudent because of the risk inherent in failing to diversify" did "not turn on publicly available information

or whether Fiduciaries can beat the market." *Id.* "Moreover, *Dudenhoeffer* … involved employer securities, which are exempt from the duty of prudence 'to the extent that it requires diversification.'" *Id.* (quoting 29 U.S.C. § 1104(a)(2)). It thus did not "address the prudence of holding a single-stock fund in the first place." *Id.* For those reasons, the Fifth Circuit concluded, the plaintiffs' "duty-of-prudence claim [did] not implicate *Dudenhoeffer*." *Id.*

The court next held that the duty of prudence, unlike the duty to diversify, applies to individual funds rather than just to the plan as a whole. *Id.* at 12a. Although "ERISA contains no prohibition on individual account plans' offering single-stock funds," the court recognized, "a single-stock investment option may be imprudent in some circumstances, as it may encourage investors to put too many eggs in one basket." *Id.* at 11a–12a. The court relied on the Fourth Circuit's holding in *DiFelice v. U.S. Airways, Inc.* in "rejecting the view that 'any single-stock fund … would be prudent if offered alongside other diversified Funds.'" *Id.* at 15a n.49 (quoting *DiFelice v. U.S. Airways, Inc.*, 497 F.3d 410, 423-24 (4th Cir. 2007)). Such funds, it noted, "'carr[y] significant risk, and so would seem generally imprudent for ERISA purposes.'" *Id.* at 13a (quoting *DiFelice*, 497 F.3d at 424).

Nevertheless, the court affirmed the district court's dismissal of the plaintiffs' claims. The defendants, it noted, had closed the ConocoPhillips stock fund to new investments. App. 15a. At that point, the plaintiffs "were free to sell off their investments at any time and reinvest in other funds." *Id.* Because they chose not to, it concluded, the plaintiffs could not "blame the Fiduciaries for declining to second guess that judgment." *Id.* at 16a. For that reason,

the court affirmed the district court's dismissal on the pleadings. *Id.* at 16a.

REASONS FOR GRANTING THE PETITION

The pending petition for a writ of certiorari in *Gannett Co. v. Quatrone*, No. 20-609, asks this Court to resolve a purported circuit split between the Fourth Circuit there and the Fifth Circuit in this case on the question whether a plan fiduciary's duty under ERISA requires only that the fiduciary offer a diversified "menu of investment options," or whether the fiduciary must also diversify "each separate option on the menu"—whether, in other words, the fiduciary's duty to diversify applies at the plan or the fund level. The petition argues (at i) that the Fifth Circuit's decision here, along with the Second Circuit's unpublished decision in *Young*, 325 F. App'x at 33, "require fiduciaries to provide a diversified menu, but do not require that each separate option on the menu be diversified." But the Fourth Circuit, it claims, "expressly disagreed" with those decisions by applying the duty instead to "each available fund on a menu." *Id.*

For the reasons explained in the respondent's brief (at 9–14) in *Gannett*, the purported circuit split does not exist. The decision below *agreed* with the Fourth Circuit that single-stock funds "'carr[y] significant risk, and so would seem generally imprudent for ERISA purposes.'" App. 13a (quoting *DiFelice*, 497 F.3d at 424). Indeed, the court relied on Fourth Circuit precedent in "rejecting the view that 'any single-stock fund … would be prudent if offered alongside other diversified Funds.'" *Id.* at 15a n.49 (quoting *DiFelice*, 497 F.3d at 423-24). Instead, the court held, "the prudence of investments or classes of investments offered by a plan must be judged *individually*." App. 15a n.49 (emphasis added). And it concluded that, under

that test, the plaintiffs had "plausibly alleged that the ConocoPhillips Funds, by its resulting concentration of investment, became an imprudent investment with the spinoff." *Id.* at 13a. That is exactly what the petitioners in *Gannett* (at 16) argue that the Fourth Circuit held there.

Although the petitioners in *Gannett* rely heavily on the Fourth Circuit's statement that it "disagree[d]" with the Fifth Circuit's decision here, *see Gannett*, 970 F.3d at 481, that disagreement relates to a separate timing issue that the Fifth Circuit appears to have simply overlooked. The Fourth Circuit in *Gannett*, like the decision below, recognized that a plan participant's choice to invest in a single-stock fund can defeat the participant's claim that the fund is imprudently diversified. *See id.* But the Fourth Circuit went one step further, examining the *stage* of the case at which participant choice becomes a relevant consideration. *See id.* at 481–82. Relying on ERISA's text, its implementing regulations, and the consensus of other circuits, the court concluded that participant choice is an affirmative defense turning on questions of fact that are inappropriate for resolution on a motion to dismiss. *See id.* For that reason, it vacated the district court's dismissal on the pleadings, leaving the defendant free to assert its defense on remand. *See id.* at 484. That is the only issue on which the Fourth Circuit in *Gannett* "disagree[d]" with the Fifth Circuit's decision here.

Because the decision below appears to have simply assumed that dismissal on the pleadings was proper, nothing in the decision touches on, let alone conflicts with, the Fourth Circuit's contrary conclusion. And although the Fifth Circuit ignored the issue here, earlier Fifth Circuit precedent holds—exactly like the Fourth Circuit in *Gannett*—that participant choice is an affirmative defense

unfit for resolution on the pleadings. *See Kopp v. Klein*, 722 F.3d 327, 335 (5th Cir. 2013). Notwithstanding the decision below's silence on the issue, that earlier precedent remains the law of the Fifth Circuit. *See Smith v. Penrod Drilling Corp.,* 960 F.2d 456, 459 n.2 (5th Cir. 1992) (holding that the decision of an earlier Fifth Circuit panel controls). Although the decision below was thus wrongly decided under ERISA and the Fifth Circuit's own precedent, it does not create a circuit split requiring this Court's review.

If, however, this Court agrees with the petitioners in *Gannett* and grants certiorari to resolve a split between the Fourth Circuit and the Fifth Circuit's decision here, the same question would necessarily be implicated in both cases. Accordingly, the Court should hold this petition pending the disposition of *Gannett*, and then dispose of the petition in light of its decision in that case.

CONCLUSION

The petition for a writ of certiorari should be held pending this Court's disposition of *Gannett Co. v. Quatrone*, No. 20-609, and then disposed of accordingly.

Respectfully submitted,

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