1 IN THE SUPREME COURT OF THE UNITED STATES

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3 FIFTH THIRD BANCORP, ET AL., :

4 Petitioners : No. 12-751

5 v. :

6 JOHN DUDENHOEFFER, ET AL. :

7 - - - - - - - - - - - - - - - - - - x

8 Washington, D.C.

9 Wednesday, April 2, 2014

10

11 The above-entitled matter came on for oral

12 argument before the Supreme Court of the United States

13 at 10:29 a.m.

14 APPEARANCES:

15 ROBERT A. LONG, JR., ESQ., Washington, D.C.; on behalf

16 of Petitioners.

17 RONALD MANN, ESQ., New York, N.Y.; on behalf of

18 Respondents.

19 EDWIN S. KNEEDLER, ESQ., Deputy Solicitor General,

20 Department of Justice, Washington, D.C.; on behalf of

21 the United States, as amicus curiae, supporting

22 Respondents.

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C O N T E N T S

ORAL ARGUMENT OF PAGE

ROBERT A. LONG, JR., ESQ.

On behalf of the Petitioners 3

ORAL ARGUMENT OF

RONALD MANN, ESQ.

On behalf of the Respondents 24

ORAL ARGUMENT OF

EDWIN S. KNEEDLER, ESQ.

On behalf of the United States, as

amicus curiae, supporting Respondents 43

REBUTTAL ARGUMENT OF

ROBERT A. LONG, JR., ESQ.

On behalf of the Petitioners 53

1 P R O C E E D I N G S

2 (10:29 a.m.)

3 THE COURT: We'll hear argument this morning

4 in Case 12-751, Fifth Third Bancorp v. Dudenhoeffer.

5 Mr. Long.

6 ORAL ARGUMENT OF ROBERT A. LONG, JR.

7 ON BEHALF OF THE PETITIONERS

8 MR. LONG: Mr. Chief Justice, and may it

9 please the Court:

10 A fiduciary's decision to do exactly what an

11 employee stock ownership plan is designed to do and what

12 the plan requires by continuing to offer employer stock

13 as an investment option is presumptively prudent.

14 Statutory language, trust law, congressional policy, and

15 practical considerations all support this result.

16 JUSTICE KENNEDY: You -- you want us to say

17 that we have sort of a coach class trustee. We're all

18 traveling in coach class when we have an ESOP. Once --

19 once we go down that road, how -- how do we define what

20 the duties of the trustee are?

21 MR. LONG: Well, we're not asking for a

22 coach class trustee. I mean, we're -- we're saying to

23 look at the statutory definition of the duty of prudence

24 in Section 1104(a)(1)(b), which says that the duty of

25 prudence must take into account the character and aims

1 of the enterprise. So when we talk about ESOPs, we're
2 talking about a pension plan of a very specific kind.
3 It is designed, the definition --
4 JUSTICE SOTOMAYOR: This does -- this plan
5 didn't require you to invest solely in employer stock,
6 did it?
7 MR. LONG: This plan --
8 JUSTICE SOTOMAYOR: It gave you the option
9 to do it and to go above the 10 percent. But it didn't
10 require you to buy only employer stock, did it?
11 MR. LONG: Well -- well, ERISA, the statute,
12 requires that an ESOP invest primarily in employer's
13 stock. This particular plan, like many plans, requires
14 that all of the assets in the ESOP be invested in
15 employer stock except the amount that needs to be in
16 cash for short-term management requirements. So -- so
17 Congress both --
18 JUSTICE SOTOMAYOR: Could you point to the
19 part of your plan that did that? Because I looked at it
20 and I didn't see the plan requiring 100 percent
21 investment.
22 MR. LONG: If -- Your Honor, if you look at
23 page 735 of the Joint Appendix, you'll find in -- in
24 part 3.3, it states, "However, in all events, the Fifth
25 Third stock fund as described shall be an investment

1 option."

2 And then if you look on 736 and then

3 continuing on to 737, it says that, "The funds shall be

4 invested primarily in Fifth Third stock." It says, "It

5 may also be invested in short-term liquid investments to

6 the extent the administrator determines they are

7 desirable to accommodate expected short run liquidity

8 needs."

9 But then it says, "The trustee shall have no

10 discretionary authority to sell Fifth Third Bancorp

11 shares or refrain from acquiring additional Fifth Third

12 Bancorp shares with funds not held for short run

13 liquidity needs."

14 So we think that --

15 JUSTICE SOTOMAYOR: You use the word

16 "primarily." There's an allegation here that you should

17 have stopped buying stock once you understood that there

18 was a serious condition in the company. That you've

19 breached your duty of loyalty, not of prudence. What do

20 you do with that allegation?

21 MR. LONG: Well, what we say is that these

22 duties -- again, we're not asking for coach class

23 duties. These are first class, if you will, duties, but

24 they have to be understood in the context of this

25 special kind of plan with special purposes. The -- the

1 purpose of an ESOP is to own company stock, to give the
2 employees a piece of the rock, an ownership interest in
3 the company. And so when -- when the issue is, as
4 you're -- as you're posing it, Justice Sotomayor, at
5 what point does a duty of prudence or a duty of loyalty,
6 either one, require the trustee to break the plans of
7 the term, deviate from the plan's --
8 JUSTICE SOTOMAYOR: It doesn't say you have
9 to. It says "primarily." It doesn't say you have to
10 continue buying.
11 MR. LONG: Well, again, I mean, I -- I
12 quoted the language. As we read the plan, and I think
13 the government agrees with us on this, the -- the
14 instructions of the plan are to invest all the money in
15 Fifth Third stock except as needed for short-term cash
16 requirements.
17 Now, there is the duty of prudence, and
18 we're not asking for a second class duty. But we think
19 in this context, given this special kind of plan, what
20 that duty means is can the purpose of this --
21 JUSTICE GINSBURG: Mr. Long, there is no
22 presumption written into this statute. There is an
23 exception from the diversification requirements in ESOP.
24 The whole object is to buy the company's stock, and so
25 you don't need to diversify. But apart from that, the

1 statutory requirement on loyalty and prudence is
2 undiluted. And so I don't know where this presumption
3 comes from. It's not in the statute itself.
4 MR. LONG: Well -- well, we do think it
5 comes from the text of the statute. It comes from the
6 duty of prudence itself which looks to the character and
7 aims of the plan, and then in Section 1107(d)(6), an
8 ESOP is defined in ERISA to be a plan that's designed to
9 invest primarily in the employer's own stock. So we
10 think that defines the special character name of the
11 plans. Congress has also spoken to this in other
12 statutory enactments --
13 JUSTICE KAGAN: Mr. Long --
14 JUSTICE SCALIA: Section 1104 of ERISA,
15 which this -- this plan is not exempted from, says that
16 the fiduciaries must manage a plan, and I quote, "for
17 the exclusive purpose of providing benefits to
18 participants and their beneficiaries." Do you
19 acknowledge that that's binding on the --
20 MR. LONG: It -- it is. And the government
21 adds the word "retirement" before benefits, and they say
22 an ESOP must be managed exclusively to provide
23 retirement benefits, but that --
24 JUSTICE SCALIA: Well, I don't add that.
25 I'm just saying providing benefits. I mean, that's --

1 that's --

2 MR. LONG: Oh, yes.

3 JUSTICE SCALIA: -- that's quite different

4 from running a plan to -- to own stock in the company.

5 That's -- that's not the basic purpose of it.

6 MR. LONG: Well, -- well, but,

7 Justice Scalia, plans -- ERISA plans provide different

8 kinds of benefits. The pension plans themselves can

9 provide death benefits, hardship benefits, disability

10 benefits. So if the benefit is stock in the company, a

11 piece of the rock, you know, the duty of the fiduciary

12 is to manage that as best as it can be managed to

13 produce the largest benefit for the participants. But

14 it's -- but it's not -- to go back to your question to

15 say, well, you know, it looks like some other investment

16 would be a better investment this week or this month.

17 JUSTICE KENNEDY: Is there anything in the

18 trust law or the common law that allows us to define

19 benefits that way?

20 MR. LONG: Well, I mean, I don't think we're

21 asking for a special definition of benefits. We're just

22 saying that what this plan -- and trust law does say the

23 settlor has a great deal of leeway to define the -- the

24 benefits that are being provided. This is a particular

25 kind of benefit, though, that Congress not only

1 authorized, but has strongly encouraged. I mean,
2 employers are strongly encouraged to offer this benefit.
3 So to say that prudence or loyalty or -- or
4 any of these fiduciary duties requires a sort of
5 continuous monitoring of the company to see whether --
6 this is no longer such a good investment.
7 JUSTICE SCALIA: You say the benefits
8 referred to in the -- providing benefits to
9 participants, and you're saying the benefits to
10 participants is their ownership of company stock,
11 including worthless company stock.
12 MR. LONG: Well -- well, no, not at all,
13 Justice Scalia. I mean, the -- the idea is that the
14 company stock is valuable, and the hope is --
15 JUSTICE SCALIA: But when it ceases to be
16 valuable, it seems to me you're not.
17 MR. LONG: Well, and -- and we agree as --
18 as every court of appeals has -- has held, that has
19 looked at this, all seven, that there -- there does come
20 a time when the purpose of the ESOP, of allowing the
21 employees to build an ownership stake in the company,
22 can no longer be realized because the company is in
23 serious peril, serious jeopardy.
24 JUSTICE KAGAN: But -- but there are
25 occasions, Mr. Long, outside of that very narrow

1 category of cases that you define in which the stock is
2 going to be way, way, way, overvalued relative to what
3 the fiduciaries know is the company's actual value.
4 Let's just say it -- the -- the market price is four
5 times more than the actual value, and the fiduciaries
6 know that because of inside information that they have.
7 It just sort of defies language to say that some -- a
8 prudent person would retain the investment in that kind
9 of wildly overvalued stock, doesn't it?
10 MR. LONG: Well, I mean, if I could take
11 that in several steps. I mean, that material
12 overvaluation standard, which no court has ever
13 accepted, we think, is unworkable. I mean, first of
14 all, before you get to the inside information, which I
15 think is the kernel of it that's left at the end, if you
16 have a stock that is traded on an active market, you
17 really can't tell the fiduciary, absent possibly inside
18 information, Well, you need to outsmart the market.
19 JUSTICE KAGAN: No. But I'm talking about a
20 case in which the fiduciary has inside information
21 that -- that -- that enables him to know that the stock
22 price is way overvalue in the actual value of the
23 company.
24 MR. LONG: But when you -- when you get to
25 that point of the analysis, and this is what all the

1 courts have recognized, you have to then bring in
2 securities law, and you have to recognize to trade on
3 that inside information would violate securities laws.
4 So prudence or loyalty cannot require a violation of
5 securities law.
6 So what -- what are the other options? You
7 could halt trading. That would not itself violate
8 securities law. But that could do great damage to the
9 participants if the company -- if the company's own ESOP
10 said, well, we think something is so wrong that we're
11 shutting down the --
12 JUSTICE KAGAN: Well, I -- I suppose it
13 could, but a prudent manager might say that it would do
14 greater damage to the -- to the participants in the plan
15 to enable this misinformation to exist and to keep
16 putting -- to keep buying stock, to keep putting more
17 and more of their retirement investments into something
18 that is really overvalued.
19 MR. LONG: Well, I mean, our point is that
20 that public announcement, that the ESOP has stopped
21 allowing purchases of company stock, could cause a sort
22 of collapse in the stock price that would be terrible
23 for the participants, and saying that prudence requires
24 that is kind of risky gamble.
25 JUSTICE KAGAN: Well, you assume that

1 truthful information will out in the end, and is it
2 better to keep on putting more money into something that
3 is -- is -- you know, is really not a good investment
4 for the participants and the beneficiaries?
5 MR. LONG: Well, but -- but by -- you know,
6 stopping immediately it could cause even greater harm.
7 But let -- I think your initial question --
8 JUSTICE SOTOMAYOR: So what's wrong with
9 following the law and disclosing that material
10 information to the public and stopping the -- the
11 employees from losing more money in worthless stock --
12 MR. LONG: And I think that's ultimate --
13 JUSTICE SOTOMAYOR: -- or almost worthless
14 stock?
15 MR. LONG: That's ultimately where the
16 government comes in. Now, we've moved a huge distance
17 from let's, you know, shut down the ESOP to let's
18 release information.
19 But there we would say, again, we think you
20 have to consider this in connection with securities law
21 that if -- if you announce, well, there's this sort of
22 general duty to release information -- I mean, first of
23 all, that would be quite a big change in ERISA.
24 There's -- there are many specific requirements for
25 disclosure of information in ERISA.

1 And what the lower courts --

2 JUSTICE KENNEDY: It's just background

3 information for this point you're discussing. Can --

4 can you tell me, is it a very common practice for the

5 directors and officers of the company themselves to be

6 the trustees? I had just assumed that that didn't

7 happen much anymore. Can you just tell me, because a

8 lot of these problems would be taken care of, insider

9 information and so forth, if there was an outside

10 trustee. And I assume -- tell me if I'm wrong -- that

11 the reason for the trust -- for the company themselves

12 to do it is because it saves money. It's -- it's

13 cheaper than hiring an outside investment. Maybe I'm

14 wrong about that. But can you --

15 MR. LONG: Well, in several --

16 JUSTICE KENNEDY: Can you just tell us what

17 the -- what the landscape is?

18 MR. LONG: First -- first of all, it is

19 common. So this -- this happens quite a lot.

20 You know, second of all, this -- this idea

21 of, well, we could appoint an independent trustee, would

22 not really solve all the problems because then you'd

23 have to have a monitoring trustee who would have to give

24 the independent trustee any inside information that they

25 had.

1 So the government's suggestion is, well,
2 okay, you'd get a low-level employee to be the
3 monitoring trustee. Well, that could itself violate
4 ERISA if you had somebody so low down that they wouldn't
5 know anything, that -- that also could be a violation.
6 So it's --
7 CHIEF JUSTICE ROBERTS: I mean, part of --
8 I'm sorry. If you want to --
9 MR. LONG: So -- so it's -- it's really not
10 a solution, but it is common to have the officers of the
11 company, and I think it's not just to save money. It's
12 because it's a very important part of what the company
13 does, and they want to have their top people running it.
14 CHIEF JUSTICE ROBERTS: I mean, the dilemma
15 we're talking about, which is you've got inside
16 information and if you do something with it, it's going
17 to hurt the beneficiary, I mean, isn't that just a
18 reflection of the fact that these are really bad
19 investments? I mean, you're putting all your eggs in
20 one basket. Your -- your -- your job depends on the
21 company and your -- your retirement depends on the
22 company.
23 MR. LONG: Well --
24 CHIEF JUSTICE ROBERTS: So that's why you're
25 in this awkward position of saying if the company is

1 doing something bad, you know, having inside -- inside
2 information that should be disclosed because it affects
3 the stock price, then it's going to hurt not only the
4 company, but also your retirement stock.
5 MR. LONG: Well, I mean, first of all, it's
6 quite right that an ESOP, because it's totally
7 undiversified, is not by itself a good retirement plan.
8 And we think that just confirms that the -- the special
9 nature and -- and aims of an ESOP is not solely for
10 retirement benefits.
11 JUSTICE GINSBURG: But it is -- it is a
12 purpose, Mr. Long, isn't it? You said -- you quoted the
13 statute, and the statute just says benefits. But isn't
14 the plan -- doesn't the plan itself mention retirement?
15 MR. LONG: Oh, yes. And -- and -- and the
16 hope, of course, is that these plans will produce lots
17 of retirement benefits. The third plan, for long
18 periods of its history, has been extremely successful at
19 producing retirement benefits.
20 Our -- our basic argument is, though, that
21 because of the nature of this plan, because it is linked
22 to the company's stock, and because Congress recently
23 looked at this exact issue after Enron and said, we want
24 employees to have choices, but company stock can still
25 be a choice and we actually encourage that --

1 JUSTICE SCALIA: Well, the participants --
2 MR. LONG: -- but you don't shut it down as
3 soon as there's trouble. If a company --
4 JUSTICE SCALIA: Why do you need a special
5 rule for -- for ESOPs? I mean, the -- the factors that
6 you mentioned, it seems to me, apply to any trustee
7 who's managing. You say, oh, you should have sold
8 because the stock was overvalued on the -- on the stock
9 market. Well, how is the trustee supposed to know that?
10 MR. LONG: It's -- it's --
11 JUSTICE SCALIA: Is he going to outguess the
12 market?
13 MR. LONG: Right. Absolutely.
14 JUSTICE SCALIA: Surely you don't demand
15 that a prudent trustee outguess the market. Okay? So
16 if it's not the market that's overvalued, it must be
17 inside knowledge --
18 MR. LONG: Inside --
19 JUSTICE SCALIA: -- that causes him to know.
20 MR. LONG: And I want to come --
21 JUSTICE SCALIA: And you have the same
22 problem about not being able to use that inside
23 knowledge.
24 MR. LONG: You can't use it.
25 And let me come back to Justice --

1 JUSTICE SCALIA: So -- so why do we need a
2 special rule for ESOPs I'm saying? All the points you
3 make apply to any -- any kind of trustee, whether it's
4 only company stock or not. Why do we need a special
5 rule for -- for company stock operations?
6 MR. LONG: Well, because if it were just an
7 ordinary investment --
8 JUSTICE SCALIA: Right.
9 MR. LONG: -- where the purpose really is
10 just to maximize retirement benefits --
11 JUSTICE SCALIA: Right.
12 MR. LONG: -- there you do look at the
13 risk-return ratio and the expenses and all --
14 JUSTICE SCALIA: No. But you have the
15 same -- the same -- the same problems that -- that you
16 justify doing nothing for the ESOP, justifies doing
17 nothing in the other -- in the other plans; namely, you
18 can't expect me to -- to outsmart the market, number
19 one, nor can you expect me to use my inside knowledge.
20 That violate the securities laws.
21 So those are your two points, but it seems
22 to me those points apply. We don't have to adopt a
23 special law for this.
24 MR. LONG: Well -- well, but, again,
25 Justice Scalia, we're -- we are agreeing with the lower

1 courts. There is absolutely a duty of prudence, and we
2 don't deny that there would be a point when a prudent
3 ESOP fiduciary --
4 JUSTICE KAGAN: But even in saying that,
5 Mr. Long, you have a category where you would say the
6 duty of prudence applies, and it's this category of
7 where the company is on the verge of collapse.
8 But even there, you would face the exact
9 same securities law problems that you're -- that you're
10 saying should preclude --
11 MR. LONG: Well --
12 JUSTICE KAGAN: -- the government's test.
13 Because there, too, you would have this kind of, I don't
14 know what to do, I'm between a rock and a hard place,
15 the securities laws prevent me from selling on inside
16 information. The same problems apply.
17 MR. LONG: Well, no. What -- what we're
18 saying is using public information, the chances that the
19 company is going to be able to provide employee
20 ownership for the long term may become so low that a
21 prudent fiduciary would decide to shut it down.
22 But I do -- I do want to answer your
23 question on inside information because I think that's
24 the nub of it, and you raised the point of, if the
25 fiduciary actually knows the inside information, don't

1 they have to do something, make it public.
2 We talked about the securities law problem
3 with trading on it. The government says, Well, just --
4 just make it public. Just release it to the public.
5 There we think the problem is, first of all,
6 that that would create this new sort of general ERISA
7 duty to provide information when it's not spelled out in
8 ERISA as -- you know, which has very specific
9 requirements. But --
10 JUSTICE SOTOMAYOR: That's not an ERISA
11 responsibility. It's an SEC responsibility. It's 10b-5
12 responsibility. Aren't you supposed to disclose any
13 information that a reasonable investor --
14 MR. LONG: And -- and that's --
15 JUSTICE SOTOMAYOR: -- would real --
16 MR. LONG: -- that's really exactly our
17 point, Justice Sotomayor. This is -- if there's inside
18 information that has to be disclosed, the securities law
19 provides a complete legal regime for this. The
20 government even agrees that in terms of the timing of
21 disclosure, the SEC timing should govern.
22 JUSTICE SOTOMAYOR: So what's -- what's
23 wrong with a rule that simply says a fiduciary has to do
24 whatever it's -- possible to protect beneficiaries
25 within the bounds of the law?

1 MR. LONG: Well, it -- it --
2 JUSTICE SOTOMAYOR: And so if the law
3 required you to disclose it, and you didn't, you've
4 breached your duty of prudence and of loyalty, because
5 you've protected the company --
6 MR. LONG: Well --
7 JUSTICE SOTOMAYOR: -- but not the
8 beneficiaries.
9 MR. LONG: It sounds good, but I think it
10 would create serious problems. I mean, you would have,
11 then, two sources of information about the company, the
12 ESOP fiduciary, which you would be saying would have an
13 independent duty to decide when it thinks there's been
14 some material misstatement or some inside information
15 and the company, which could create great confusion.
16 JUSTICE SOTOMAYOR: You -- you don't --
17 you're -- you have an absolute duty to the beneficiary.
18 MR. LONG: Well, but -- but the -- I guess
19 the point is, Justice Sotomayor, from the -- the
20 fiduciary can say, Look, if there's been a securities
21 law violation about disclosure or material
22 misstatements, there's a securities law remedy for that,
23 and the plan participants will get that remedy.
24 JUSTICE KAGAN: Well, then, what if the --
25 JUSTICE ALITO: In an ESOP -- in an ESOP,

1 can the fiduciary take into account the interests of the
2 participants as employees as opposed to their interests
3 as investors? It doesn't seem to me that those will
4 necessarily always be the same. And there may be
5 situations in which something that would be potentially
6 good for the participants as investors would be quite
7 bad for them as employees.
8 They want to keep their jobs. They want the
9 company to stay afloat. Can that properly be taken into
10 account, or is that outside of the bounds?
11 MR. LONG: I mean, I -- I don't think you
12 have to do that. I think you -- you know, you look at
13 the interest of the participants who are both employees
14 and participants in the plan, you know. So -- so I
15 don't think it's necessary to say, Well, we're not even
16 looking at them as participants in the plan. We're
17 looking at them only as employees. Are -- we think --
18 JUSTICE ALITO: No, I'm not saying only as
19 employees, but I'm saying can you take that into account
20 at all? If you're in the situation where stopping
21 trade -- stopping purchases in company stock would be a
22 signal that would potentially trigger bankruptcy and
23 liquidation for the company, can that be taken into
24 account?
25 It might not be in the best interests -- if

1 the -- if the -- if these participants were simply
2 investors, it might be in their best interests to stop
3 buying the stock. But if taking that step would have
4 the consequences that I mentioned, it might be very much
5 not in their best interests as employees.
6 MR. LONG: Well, I mean, I think I'd say
7 that that would be one way to sort of work this out.
8 It -- that's another way of getting to the -- the bottom
9 line that we think is correct here, which is that an
10 ESOP is a special kind of pension plan, and the whole
11 nature of it is to own company stock. And therefore --
12 JUSTICE KENNEDY: Well, how do you fine --
13 define the standard or the duty that's responsive to
14 Justice Alito's concern? And I had the same problem.
15 Let's assume that trustees in a non-ESOPs
16 plan have a duty to maximize returns and provide stable
17 investments. Is it somehow different when it's an ESOP?
18 MR. LONG: Yes, I -- I think it is. If
19 there's --
20 JUSTICE KENNEDY: And if so, what is the
21 duty?
22 MR. LONG: The -- I think the --
23 JUSTICE KENNEDY: How do you define it?
24 MR. LONG: I think the -- the duty is to
25 maximize the returns for this special kind of a vehicle,

1 which is a vehicle that owns stock in only one company,
2 the -- the employee's company, and for reasons that --
3 this kind of goes to -- to Justice Alito's point but in
4 a different way -- for reasons that go beyond just the
5 returns.
6 It's -- it is because it is the -- the
7 employees' company. Congress thought it was beneficial
8 for many reasons to encourage employee ownership of
9 companies, and so you don't look to whether, you know,
10 this appears to be a bad investment as compared to a
11 mutual fund.
12 JUSTICE KENNEDY: Well, if I'm the trustee,
13 I don't know what my duty is based on your answer. I
14 don't know what I'm supposed to do.
15 MR. LONG: Well, I mean, the courts of
16 appeals have had a fairly uniform approach to this for
17 now almost 20 years, and it has -- it has not been
18 causing a great deal of -- of trouble. The approach
19 they've all been taking is that because of the special
20 nature of ESOPs and, you know, when the plan requires
21 that all the funds be invested in the ESOP at least,
22 that's what the fiduciary must do, and that is
23 presumptively prudent.
24 It's not necessarily prudent, and there
25 would be, you know -- the way we think the Courts have

1 best expressed it, if -- and they draw this from trust
2 law -- if the special aims of this plan, employee
3 ownership, can no longer reasonably be achieved, then
4 prudence requires the plan to be shut down. That is not
5 a bright-line standard, but that is the standard
6 the courts have adopted.
7 I'd like to save the balance of my time, if
8 I may.
9 CHIEF JUSTICE ROBERTS: Thank you, Mr. Long.
10 Mr. Mann.
11 ORAL ARGUMENT OF RONALD MANN
12 ON BEHALF OF THE RESPONDENTS
13 MR. MANN: Thank you, Mr. Chief Justice, and
14 may it please the Court:
15 I think what I can most usefully do is talk
16 first about the question of the relevant benefits that
17 was raised by some of you, and then second address this
18 so-called "rock and a hard place" problem which we think
19 is essentially a confession of disloyalty by my most
20 able opposing counsel.
21 First, the nature of the benefits in the
22 statute, the reference to benefits in 404(a)(2)(A) is
23 quite plain. It refers to the basic type of plan that's
24 covered by ERISA, which is an employee benefit plan as
25 defined in Section 1002 sub 3 --

1 JUSTICE GINSBURG: Mr. Mann, I think the
2 point that raised that the employee benefit --
3 MR. MANN: Section 1002, Sub 3 describes
4 employee benefit plans, which are the subject of ERISA.
5 And there are two types of employee benefit plans as
6 defined in that section. There are plans that provide
7 welfare benefits and plans that provide pension
8 benefits. And I think there is no doubt that the
9 benefits that must be exclusive purpose of an ERISA plan
10 are those benefits that are required to be governed by
11 ERISA.
12 And I think we need to remember the grand
13 bargain of ERISA, reflection of the statute is, if
14 employees are going to provide these kinds of benefits,
15 the people that manage the retirement and welfare plans
16 must accept fiduciary duties. That's the bargain of
17 ERISA. If you are going to provide these kinds of
18 benefits, you have to accept fiduciary duties.
19 And the sole purpose of the plan under the
20 statute is to provide those benefits.
21 Now, I'd like to talk about this idea of
22 this "rock and a hard place" that was first raised by
23 Justice Kagan.
24 I think that the best way to think about
25 this is, essentially, what the petitioners are saying

1 is, if I decide to put myself in a position where I owe
2 duties to two different people, my employer on the one
3 hand and the beneficiaries of the plan, because I've put
4 myself in a conflicted situation, it's perfectly right
5 for me to just do nothing.
6 That's not the way it works. You can
7 imagine a lawyer that undertakes to represent two
8 clients with conflicting interests. If it comes to the
9 point where the interests are in conflict, well, the
10 lawyer has already made a mistake. The lawyer cannot
11 simply say, well, I choose to protect one client, not
12 the other. They have to be something, and they're going
13 to violate some --
14 JUSTICE BREYER: I would say that -- well,
15 what the problem -- but can you give me any example of
16 any case? There may be so many you can't even give me
17 your best one. But trusts have been around for probably
18 800 years. And can you give me an example of one where
19 a court said a trustee has breached its fiduciary
20 obligation because he failed to use inside information?
21 MR. MANN: Oh, no, I -- I think there
22 probably isn't such a case, but I would --
23 JUSTICE BREYER: You think there is not such
24 a case?
25 MR. MANN: I think there probably is not

1 such a case. The court of appeal --
2 JUSTICE BREYER: Fine. If there is not such
3 a case, what's the problem? Because what's the rock and
4 the hard place?
5 MR. MANN: Well, the --
6 JUSTICE BREYER: The person has an
7 obligation to act prudently in respect to the
8 fiduciaries -- to the beneficiaries, of course. But he
9 cannot, irrespective of that, have an obligation to use
10 inside information. End of the matter. What -- what's
11 wrong with saying just that?
12 MR. MANN: I -- I'm not sure what you mean
13 by that, but I'd like to --
14 JUSTICE BREYER: What I mean by it is just
15 what I said. There is no rule of trust or ERISA law
16 that you can breach a duty to a beneficiary by failing
17 to use inside information, period. I don't know what
18 the SEC's brief is. I'm going to ask --
19 MR. MANN: I think I --
20 JUSTICE BREYER: -- the SEC what their
21 opinion is because they don't seem to appear on this
22 brief.
23 MR. MANN: I think I would respectfully
24 disagree with that, and I think it's important to
25 understand why, Justice Breyer and Justice Kagan.

1 JUSTICE BREYER: The answer is there's not
2 been a case ever holding the contrary --
3 MR. MANN: But that's --
4 JUSTICE BREYER: -- but you yourself
5 disagree with it.
6 MR. MANN: But that is --
7 JUSTICE BREYER: Now, what the reason you
8 disagree with it?
9 MR. MANN: That is because the courts of
10 appeals unanimously, as Mr. Long says, have held that
11 the trustees of these plans have no duties at all. And
12 so if trustees have no duties at all, it's of course
13 quite difficult for them to breach the duties. Now,
14 my --
15 JUSTICE BREYER: I'm sorry. I'm saying go
16 back to England. There are many cases where settlors
17 have said what kinds of things you should invest in, and
18 they invest in them. They have inside information that
19 it is a bad investment. Is there any case that says
20 they have a duty of obligation not to do what the
21 settlor says? I wouldn't have been surprised if you had
22 found some cases, but I'm also not surprised that there
23 aren't any. That's why I asked the question.
24 MR. MANN: With respect to that particular
25 question, and I -- I did not understand your question

1 that way, and I don't -- I can't say whether there is or
2 has never been such a case.
3 But what's important from our perspective is
4 the trustees in this case undertook to represent
5 conflicting interests. Ordinarily when people undertake
6 to represent conflicting interests --
7 JUSTICE SOTOMAYOR: Let me just continue to
8 Justice Breyer's question. There are some legal duties.
9 I don't know of a trustee who has to break the law.
10 They can't sell on the basis of inside information, and
11 that's a legal prohibition.
12 MR. MANN: I think that's clearly true, but
13 I think they, at the same time, at their peril, breach
14 their duties of loyalty to those for whom they've
15 accepted a fiduciary duty. And the --
16 JUSTICE SOTOMAYOR: So your claim rises and
17 falls on the fact that you think they're -- they've
18 breached their duty of loyalty by having the inside
19 information and -- or exactly what is your claim? What
20 could they have done that wouldn't breach the law?
21 MR. MANN: My claim does not rise or fall at
22 all on that. And I don't think there is any reason why
23 you need to address that, given the particular nature of
24 the complaint. The complaint in this case alleges that
25 the trustees knew or would have known, if they had

1 undertaken a reasonable investigation of the type that
2 is required by ordinary principles of prudence, that the
3 stock was materially overvalued, and the stock was a
4 much more risky investment than it was at the time that
5 the plan was designed.
6 JUSTICE SOTOMAYOR: How would they --
7 JUSTICE ALITO: What do they have to do
8 then? You said they can't sell the stock based on that
9 information. What are they supposed to do? Or is it
10 your argument that they just never -- you never should
11 have insiders serving as trustees; you always have to
12 have an outside running these ESOPs?
13 MR. MANN: Well, I wouldn't say that you
14 always have to, but I do think that the situation is
15 quite parallel to the situation that corporate directors
16 face when they come into a conflicted situation. In the
17 corporate context where directors ordinarily are
18 protected by the business judgment rule, if a situation
19 arises in which their interests patently diverge from
20 the interests of the shareholders, they don't simply
21 decide to represent both interests but pick one over the
22 other. They instead step aside and appoint -- and, you
23 know, allow independent people to represent the
24 shareholders.
25 JUSTICE ALITO: So you're basically saying

1 that if it's not flatly prohibited, it is very unwise.
2 It generally shouldn't happen. You're putting yourself
3 in an impossible position if you are an insider and
4 you're going to serve as a trustee of an ESOP.
5 MR. MANN: Well, I think it's a plain
6 implication of Justice Kennedy's opinion in Glenn and
7 the majority opinion in Glenn that the structure of the
8 fiduciary and the relationship to the trust being
9 conflicted should raise a red flag.
10 JUSTICE BREYER: Here when you say -- I am
11 totally with you on this. We walk into the trustee's
12 office. It's like Ralph Nader investigating the FTC
13 years ago. There is someone asleep on the sofa. In his
14 inbox is ten feet of papers telling him about all
15 public -- telling him about the corporation's condition.
16 It's apparent he's never read them. If he had read
17 them, he would have taken action. Of course you would
18 have a case, I would think.
19 MR. MANN: But that is our complaint.
20 JUSTICE BREYER: But you want to go beyond
21 that?
22 MR. MANN: No. Our complaint is they have
23 the information in step one. They didn't do anything.
24 Step one, they did not --
25 JUSTICE BREYER: Not just information.

1 Remember I carefully said all this was publicly
2 available information. You want to say it also applies
3 when it's not publicly available information. Am I
4 right or wrong?
5 MR. MANN: You are correct. I would like to
6 say that, but I would like to point out our complaint
7 alleges a large amount of information that is one,
8 public; two, false information promulgated by the
9 petitioners, the falsity of which perhaps could have
10 been undertaken by -- discovered by considerable
11 investigation.
12 And instead of conducting a reasonable
13 investigation that a trustee for a billion dollar
14 pension plan ordinarily would conduct -- and just to be
15 clear for the earlier discussion, this is not a plan
16 that is invested solely in Fifth Third stock. This plan
17 has a variety of investments. There is one particular
18 fund that has 1 to $200 million --
19 JUSTICE KENNEDY: Suppose you were a
20 legislature or a congressman. You are absolutely
21 committed to the idea that it's important and salutary
22 to have employees own stock in the company for which
23 they work. How would you write the statute?
24 MR. MANN: I think Congress has done a great
25 job of writing the statute. Congress has wrote a

1 statute that tells employers you can set up these plans,
2 and the trustees don't have to diversify, which is
3 inherent in having a plan that has employee stock --
4 JUSTICE KENNEDY: Well, once you say the
5 trustee doesn't have the duty to diversify, it seems to
6 me you are living in something of a different world.
7 MR. MANN: I think that's right. And that's
8 why we believe that this standard of prudence is
9 affected by the fact that it's an employee stock
10 ownership plan rather than just a portion of the fund
11 that owes employers' stock. But that doesn't mean that
12 there's no duty of loyalty. It shouldn't affect that at
13 all.
14 CHIEF JUSTICE ROBERTS: Well, but affected
15 is not quite enough. I mean, this trustee's job is to
16 buy the company's stock. In that particular fund, it's
17 100 percent, other than the money you need to buy and
18 sell. So he has the easiest job in the world. He gets
19 up in the morning and says, "I think I will buy some of
20 this company's stock."
21 (Laughter.)
22 CHIEF JUSTICE ROBERTS: That's what he's
23 supposed to do. And I think that what every Court of
24 Appeals has recognized is that that is by definition
25 prudent, because that is the settlor's objective with

1 one exception. If everything is going, you know, south
2 and the company's collapsing, well, then he does have
3 the obligation to do something.
4 So I don't understand how you keep -- can
5 say that he has breached a fiduciary duty of prudence
6 when the people investing in this ought to know what
7 they're going to get is the company's stock.
8 MR. MANN: I think it's -- I'm glad that you
9 asked that question, because I think that's central at
10 the disagreement between respondents and petitioners.
11 Now, the first answer, of course, is that
12 you can't look at the statute without thinking that
13 Congress had a different understanding of the duties.
14 And if I just could just mention a couple of things
15 about the statute. It's not only the point that Justice
16 Scalia made that Section 404(a)(2) specifically carves
17 out some duties but not others.
18 It's also that it only forgives prudence to
19 the extent of diversification, which means that prudence
20 has to mean something other than diversification. And
21 then it still further limits the scope of forgiveness.
22 It only forgives it with respect to the acquisition or
23 holding of qualifying employee securities -- employer
24 securities, which is much narrower than the fiduciary
25 duty defined in Section 403 to manage and control the

1 assets of the plan.

2 But what's important for our purposes, it

3 would not -- if you ask the question, although the

4 statute resolves it, it would not have been sensible for

5 Congress to tell the people that manage employer stock

6 ownership plans that they have no duties of prudence or

7 loyalty to the employers whose retirement funds are at

8 stake.

9 CHIEF JUSTICE ROBERTS: Well, what is

10 exactly the duty of prudence? Presumably, you buy --

11 you invest the funds in the company's stock, whether

12 it's going up or going down, right? If you have the

13 funds, all you can do is invest them. The stock is down

14 half a point or whatever. You still buy it, right?

15 MR. MANN: Okay. So I'd like to say, first,

16 there is the duty of loyalty. And it does breach the

17 duty of loyalty, for example, as the Court said in

18 Varity, and I don't think it's controversial, to lie to

19 the beneficiaries.

20 CHIEF JUSTICE ROBERTS: Well, what's the

21 answer to my question?

22 MR. MANN: With respect to the duty -- so

23 the duty of loyalty is enough to sustain --

24 CHIEF JUSTICE ROBERTS: No, no. I didn't

25 ask a question about the duty of loyalty.

1 MR. MANN: With respect to --

2 CHIEF JUSTICE ROBERTS: I asked a question

3 of whether or not the trustee is imprudent because he

4 buys the stock because it's gone down -- you know, gone

5 down 10 percent.

6 MR. MANN: Okay. The most fundamental thing

7 about the duty of prudence that you would get from your

8 statement of trust is that the outcome of the investment

9 is not what's relevant. What's relevant is, and Justice

10 Scalia when he was on the D.C. Circuit that wrote a long

11 opinion in Fink, which discusses in detail, and you'd

12 see the same thing in the comments to Section 90 of the

13 restatement, the most important thing is what you might

14 call procedural prudence. Okay. These people are

15 managing a fund of $1 billion. The relevant question is

16 what would a reasonable trustee of a billion-dollar fund

17 have done to investigate the situation? Would someone

18 with a billion-dollar fund and 100 to $200 million of

19 Fifth Third stock have routinely been collecting

20 information about the nature of that investment, whether

21 they should take some action?

22 It well might be -- it well might be that

23 they should not in a flighty or haphazard way dispose of

24 the stock, because that's the baseline of this plan, is

25 to invest in the stock. But that's entirely different

1 from doing absolutely nothing, not telling the employers
2 information --
3 JUSTICE ALITO: Do you think the trustee has
4 a duty to acquire inside information? The trustees say,
5 I don't want to know insider information. I'm going to
6 put myself in exactly the position of an outside
7 trustee, so I'm going to take into account only public
8 information, I'm not going to do an investigation.
9 MR. MANN: Our position is that the duty of
10 the trustee is to behave as a prudent fiduciary would
11 behave, and if the trustee is unable to do that because
12 the trustee has conflicting interests to serve, then the
13 trustee is violating the duty of loyalty and should
14 arrange the situation differently.
15 JUSTICE ALITO: What's the answer to my
16 question? Assuming that --
17 MR. MANN: The answer to your question --
18 JUSTICE ALITO: -- permissible for an
19 insider to be in this position, can the insider behave
20 like an outsider?
21 MR. MANN: I think it's plain in the case
22 that if the trustee does not undertake the investigation
23 that a prudent fiduciary would take, because of their
24 concern about acquiring insider information of the
25 employer, then they would violate the ordinary standard

1 of prudence.

2 CHIEF JUSTICE ROBERTS: Well, can we talk

3 concretely instead of just saying, well, they've got to

4 do what a prudent fiduciary can do? Are they allowed to

5 take into account the impact of a decision to stop

6 buying on the beneficiaries? The stock is going down,

7 if the trustee stops buying, that's going to cause a

8 drop in the value of the shares and that's going to hurt

9 the beneficiaries. So what does he do? Does he say, I

10 shouldn't buy any more because I think it's going to go

11 down some more? Or should he say, I should keep buying

12 because otherwise all of the holdings, and this is all

13 they are invested in, their holdings are going to go

14 down?

15 MR. MANN: I think the obligation of the

16 fiduciary at all times is to behave prudently in

17 managing investment prudently. There might --

18 CHIEF JUSTICE ROBERTS: I asked for an

19 answer to the question. And I -- it doesn't -- it's not

20 going to help me to have this mantra as opposed to --

21 MR. MANN: Well, I don't -- I don't believe

22 that the question is whether they must sell or mustn't

23 sell. I think they have to decide would it be in the --

24 based on the facts we know right now, do we believe that

25 this is a short-term blip in the stocks and it will rise

1 back up, in which case, we --

2 JUSTICE BREYER: In a way, what happens is

3 that the trustee, knowing that the company has announced

4 an enormous oil strike, is having to sit on a private

5 meeting where three people come in and you say, yeah,

6 there was an oil strike, but it's impossible to get the

7 oil out. Ha, ha, we put one over on that time. Okay.

8 MR. MANN: If the --

9 JUSTICE BREYER: Now, what's that trustee

10 supposed to do?

11 MR. MANN: I think I lost track of whether

12 the oil strike was true or false.

13 JUSTICE BREYER: No. There's a false.

14 MR. MANN: Okay.

15 JUSTICE BREYER: He alone, when two other

16 people, know that this oil is worthless. The market

17 doesn't. It's totally inside information. What, in

18 your opinion, is he supposed to do?

19 MR. MANN: I believe that the trustee

20 violates the duty of loyalty and the duty of prudence if

21 the trustee, believing that the stock is overvalued, in

22 fact, does not take action to protect the beneficiaries.

23 JUSTICE BREYER: Okay. So your answer is,

24 totally inside information, he sells, right?

25 MR. MANN: I didn't say that. I think he

1 needs to do something.

2 (Laughter.)

3 JUSTICE KENNEDY: I just don't see what the

4 trustee is supposed to do. You have the company stock.

5 By comparing it with other stocks, there will be many

6 investments that are just as good or better. When does

7 he have to make the investment, in other words, just as

8 good or better? I don't understand. I don't understand

9 what -- how we're going to implement what Congress

10 wanted to implement.

11 MR. MANN: Well, we believe that the

12 traditional fiduciary standard is not that hard to

13 implement. It's a standard that's been imposed on

14 fiduciaries for centuries. It's a standard that all

15 managers of trusts have undertaken. The only thing

16 that's really different about these particular trustees

17 is that they're managing funds that are worth, you know,

18 billions of dollars.

19 JUSTICE GINSBURG: You said you were going

20 to deal with the rock and a hard place. But if the

21 trustee goes out and sells, that would be a signal that

22 things are bad with the company. So it will end up

23 being worse for the beneficiaries of the plan.

24 MR. MANN: We certainly believe that if the

25 trustee's view, based on the information, is that

1 selling the stock would be bad for the beneficiaries,
2 then a decision not to sell is prudent. If the trustee
3 decides selling would be bad for the beneficiaries so
4 we're not going to sell, that is a prudent decision. It
5 might be right. It might be wrong. But if that's their
6 decision, I think that's prudent. If a trustee decides
7 selling would be beneficial to the beneficiaries, it
8 might be right, it might be wrong, but if that's what
9 they actively decide, then I think they need to do
10 something. And that's our position.
11 Now, the rock and the hard place, I
12 understand that some of the Justices have disagreed.
13 But I mean, our position on that is quite clear. The
14 only reason petitioners are between a rock and a hard
15 place is they have undertaken to have interests that
16 directly conflict with their fiduciary obligation to
17 these employees' retirement benefits. There is nothing
18 in the statute. There is no practical consideration
19 that petitioners have suggested. There is no reason
20 that these funds need to be managed by insiders. As far
21 as we --
22 JUSTICE GINSBURG: But beyond the -- outside
23 trustees, they have to get information from the insider
24 and we're back in the same place.
25 MR. MANN: Well, of course, if you wait

1 until you are in possession of information and you know
2 the stock is overvalued, you can't solve the problem by
3 stepping aside then. But if you set up the trust in the
4 hands of an independent investment manager in the
5 beginning, we believe that if you look carefully to
6 provisions of Section 1105(c) and (d), you will see that
7 Congress has provided a great deal of protection for the
8 person it appoints. Of course, it's true that if the
9 person in the company that appoints a fiduciary knows
10 that there is a breach of fiduciary duty by the
11 investment manager, they're still liable. But what else
12 could Congress possibly say? Congress couldn't write a
13 statute that says people that knowingly breach fiduciary
14 duties of the employees are not supposed to be liable,
15 so --
16 CHIEF JUSTICE ROBERTS: The status of the
17 trustee, whether it's an interested party or a
18 disinterested fiduciary, is disclosed to the
19 beneficiaries, I take it, at the outset? They can
20 decide that they don't want to invest in that particular
21 fund and there are nine other options because of that
22 potential conflict?
23 MR. MANN: Yes, they are advised of that.
24 Their ability not to invest in that particular fund is
25 limited during the class period because all of the

1 matching contributions for all of the class period went
2 directly into this fund. So employees would have to
3 take that active step to remove them from the fund.
4 CHIEF JUSTICE ROBERTS: If they wanted --
5 but hopefully, they got four percent matching funds if
6 they were in that fund?
7 MR. MANN: That is correct.
8 I think the most important thing for us to
9 emphasize is the point of ERISA is that if an employer
10 is going to provide employee benefits, the people that
11 manage those benefits have to accept fiduciary duties.
12 There is nothing unusual about that. The standard is
13 not unworkable. It's a standard that is provided for
14 centuries. And if the only reason that the people
15 managing the fund can't comply with those duties is
16 because they have obligations to the employers, then
17 that is not something that ERISA can tolerate.
18 Thank you.
19 CHIEF JUSTICE ROBERTS: Thank you, counsel.
20 Mr. Kneedler.
21 ORAL ARGUMENT OF EDWIN S. KNEEDLER
22 ON BEHALF OF THE UNITED STATES,
23 AS AMICUS CURIAE, SUPPORTING RESPONDENTS
24 MR. KNEEDLER: Mr. Chief Justice, and may it
25 please the Court:

1 Several points at the outset. Justice Alito
2 asked about taking into account the interests of
3 employees as employees. But Section 1104 speaks in
4 terms of operating the plan for the exclusive purpose of
5 providing benefits to participants and their
6 beneficiaries, which means the interests of employees
7 are taken into account only insofar as they are
8 participants in the plan, not more generally.
9 And the second and related point I would
10 like to make with respect to that is the use of the word
11 "benefits" in 1104(a) that says that the plan must be
12 operated for the exclusive purpose of providing benefits
13 to participants. We have that on page 6(a) of our
14 petition appendix. Further up on that is the definition
15 in 1234 of an individual account plan, which --
16 JUSTICE SOTOMAYOR: Mr. Kneedler, a stock
17 drop in and of itself, I don't think, can prove a lack
18 of prudence because --
19 MR. KNEEDLER: Agree.
20 JUSTICE SOTOMAYOR: You agree with that?
21 MR. KNEEDLER: Yes, we do. I mean, there
22 are situations in which there may be additional unusual
23 circumstances, but simply a stock drop would not. But I
24 think that, as Justice Scalia pointed out, that would
25 also be true in a diversified plan.

1 JUSTICE SOTOMAYOR: Exactly. It's true
2 almost anywhere because you can't outsmart the market.
3 MR. KNEEDLER: At least we're not
4 insisting that a fiduciary in order to be prudent
5 must --
6 JUSTICE SOTOMAYOR: So how do you deal with
7 what has been vexing us, the issue of what a fiduciary
8 should or can do when they are an insider and have only
9 inside information, not public information?
10 MR. KNEEDLER: Right.
11 JUSTICE SOTOMAYOR: So where is the breach
12 of fiduciary duty? Where's the breach of loyalty? What
13 can it consist of, and what does someone have to prove
14 in a complaint? Because this has to do with a pleading
15 presumption and a marriage presumption.
16 MR. KNEEDLER: Right. And if there is a
17 substantive principle here, that would have to be
18 pleaded. If it is an evidentiary presumption, as the
19 Sixth Circuit said, that would not have to be pleaded in
20 the complaint.
21 But several points on that. First of all,
22 in response to Justice Breyer's question about inside
23 information, we would point out on page 31 of our brief,
24 quoting Scott, that if a fiduciary has peculiar
25 knowledge about a corporation's stock's value, that is a

1 factor to be taken into account in terms of the way the
2 trustee exercises his responsibility.
3 JUSTICE BREYER: Well, the -- the union
4 brief says the thing to do in that situation is, without
5 saying anything, turn the trusteeship over to a person
6 who doesn't have that knowledge. That takes care of the
7 problem. And the reason I raised the question, of
8 course, is there are trillions of dollars probably
9 managed by ERISA funds. I don't know what percentage of
10 those involve stocks. Not this kind -- of this kind.
11 Maybe you know, but my guess is a lot.
12 And obviously, before I wrote a word that
13 said what you have to do or don't have to do with inside
14 information, I would like to know directly, not
15 indirectly, what the SEC thinks.
16 MR. KNEEDLER: Well --
17 JUSTICE BREYER: And maybe you can tell me.
18 But the SEC isn't here. And at least there's no SEC
19 lawyer that signed your brief. So I don't know the
20 extent to which that's --
21 MR. KNEEDLER: I mean, this is primarily a
22 labor case. The security --
23 JUSTICE BREYER: It might be you might have
24 a good reason for it.
25 MR. KNEEDLER: Right.

1 JUSTICE BREYER: But right now I am supposed
2 to write some words or join some words.
3 MR. KNEEDLER: Right.
4 JUSTICE BREYER: And those words will tell
5 trustees of possibly -- I have no idea -- but maybe
6 hundreds of billions, or maybe billions anyway, of -- of
7 assets in the stock market, what they're supposed to do
8 when they learn some inside information that affects the
9 company's stock. And I hate to tell you, I don't know
10 anything in this area about what the likely effects are.
11 And, therefore, I'd like to know what they think. And
12 the closest I came to it was the ALF-CIO brief, frankly,
13 where they said what you're supposed to do here is -- is
14 turn this over. So what do I do?
15 MR. KNEEDLER: Well, that is, of course, one
16 option if -- if circumstances get very bad. This was
17 true in the WR Grace situation. The trustee -- the
18 inside trustees appointed an outside trustee to do an
19 evaluation. But the first -- the first step that --
20 that Mr. Mann pointed out is, I think, a fundamental one
21 that should not be overlooked here. And that is that
22 the fiduciaries have an obligation to actually exercise
23 their discretion and actually investigate. And here,
24 the allegation is that these trustees did not even do
25 that. So if you're going to be giving deference to a

1 trustee under --

2 JUSTICE SOTOMAYOR: I'm sorry. Investigate

3 what, the nonpublic information? Investigate --

4 MR. KNEEDLER: Investigate -- investigate

5 the consequences of the nonpublic -- this would be true

6 of public information, too, that the -- this is not -- a

7 plan like this, even though it is exempt from -- from

8 requirements of diversification, are still prudence

9 duties, which include investigation and -- and

10 monitoring of the -- of the investment. So the -- the

11 fiduciaries of a plan like this do have an ongoing

12 obligation to investigate and to keep themselves

13 apprised of how the company is doing.

14 CHIEF JUSTICE ROBERTS: Well, what exactly,

15 concrete terms, what do you do as the trustee? You have

16 this information, inside information that says that the

17 stock is overvalued. Do you sell? In which case the

18 beneficiaries' holdings go way down and they sue you, or

19 do you not sell? In which case when the information

20 comes out, the beneficiaries sue you because their value

21 goes down. What are you supposed to do?

22 MR. KNEEDLER: In -- in the category of

23 cases we're talking about here, and these are the ones

24 that are of the greatest concern to the Department of

25 Labor, the stock is materially overvalued because of the

1 inside information. In that situation -- and I think
2 this is the point Justice Kagan was making -- it
3 would -- it would ordinarily be the right thing to do to
4 sell, the truth will out eventually. But -- and there
5 may be -- there may be a precipitous drop. But the
6 stock has already been at a -- at a level and -- and
7 stock has already been purchased at an inflated level,
8 which means that the employees are not getting what they
9 were entitled to.
10 JUSTICE ALITO: But you say they should sell
11 based on the inside information?
12 MR. KNEEDLER: No, he can't -- he can't sell
13 on the basis of inside information. He could -- I'm
14 sorry, he could stop purchasing, which is --
15 JUSTICE BREYER: But the market will see
16 through that in about two seconds. But the --
17 MR. KNEEDLER: Well, no, this is the --
18 JUSTICE BREYER: That isn't really my
19 question. It's a numerical question. What -- you know,
20 I was making up numbers wildly. What are the actual
21 numbers? That is, approximately how much in assets is
22 accounted for by ownership of the company's -- you know,
23 this kind of a plan where you buy the company's stock.
24 Do you know?
25 MR. KNEEDLER: I don't know the amount of

1 assets, but --

2 JUSTICE BREYER: About?

3 MR. KNEEDLER: -- as I -- as I recall, I

4 think there are perhaps 12 or 14,000 ESOP plans.

5 Some -- about half the employees covered are in publicly

6 traded -- in publicly traded corporations.

7 I want to make another point in terms of the

8 purposes of an ESOP. The -- Congress has provided for

9 investment in -- in employer stock, but it has not

10 excepted the fiduciaries from the general duty of -- of

11 prudence. The statute -- the statute makes that clear.

12 And in 2006, Congress provided that employees of

13 publicly traded companies must be given the right to

14 diversify, which reflects the judgment --

15 JUSTICE KENNEDY: But your -- your argument,

16 at least according to the Petitioners's brief, and I

17 think they're correct, you go away from the purity

18 standard. You have your own standard whether or not

19 it's materially overvalued in this instance. Or are you

20 saying --

21 MR. KNEEDLER: For inside -- where there's

22 inside information and is it -- is it materially

23 overvalued. And there could -- there can

24 be circumstances --

25 JUSTICE KENNEDY: But -- but then -- but

1 then you are creating a special standard which is just
2 what you're accusing the Petitioners of doing.
3 MR. KNEEDLER: Well, the question is what's
4 the general standard of prudence. And it would always
5 be imprudent for a diversified or non-diversified plan
6 for the fiduciaries to purchase a -- an asset that
7 they -- or hold on to an asset that they know to be --
8 or should know with reasonable investigation is
9 materially overvalued.
10 JUSTICE ALITO: Well, let me give you this
11 example. It's helpful to have something concrete here
12 and not just general statements of -- of -- about
13 fiduciary duty.
14 Let's say that the trustee receives inside
15 information that someone has alleged that corporate
16 office -- a particular corporate officer has engaged in
17 illegal conduct. And if it turns out that that conduct
18 actually took place, that -- that information -- that
19 will cause damage to the company. But it's -- it's --
20 it hasn't been proven. There's simply been an
21 allegation.
22 Now, what -- at that point, what does the
23 trustee -- what do you think the trustee has to do? If
24 that information were available to the public, let's say
25 it would cause the price of the stock to go down, so

1 it's material -- it's material information, but at a
2 somewhat preliminary stage. What do you do? Completely
3 stop buying the stock? You can't sell. Disclose the
4 information? What is supposed to be done?
5 MR. KNEEDLER: There is no absolute answer
6 in that situation. Stop buying might be the right
7 approach. That's not uncommon, and there are blackout
8 periods where -- where plans in companies bar trading in
9 the stock. But if it's material information that the
10 securities laws require to be disclosed, there is no
11 reason why the participants in an ERISA plan should be
12 unprotected when that material information affects
13 the --
14 JUSTICE ALITO: Well, that's -- no. But --
15 but would that information have to be disclosed under
16 the securities laws? Let's say there was no prior -- no
17 prior misleading statement regarding this matter.
18 MR. KNEEDLER: It would have to be
19 disclosed.
20 JUSTICE ALITO: Eventually.
21 MR. KNEEDLER: If it's major, it might have
22 to be disclosed within 4 days under -- under 8(k).
23 Otherwise, it would be quarterly or annually. And we
24 are -- we are suggesting that the -- that disclosure
25 obligations should be geared to what the securities law

1 provides --

2 JUSTICE KENNEDY: The Chief Justice

3 indicated -- if I can ask just one question. Is this a

4 case in which we must decide what the fiduciary standard

5 is quite without regard to inside information? Is

6 inside information just an added issue in the case or is

7 it the key issue in the case?

8 MR. KNEEDLER: We think in this case it

9 is -- it is the key issue. The Court does not have to

10 decide what fiduciary obligations the fiduciary of an

11 ESOP would have in -- in dire circumstances where the --

12 where you have a failing company or mismanagement or

13 something like that. We are focused here on inside

14 information that materially enhances the value of the

15 stock, overvalues it, and in that situation, we think

16 that a fiduciary of an ESOP, just like the fiduciary of

17 any other plan, has a -- has a duty of prudence not to

18 remain invested in or to purchase materially overvalued

19 stock.

20 CHIEF JUSTICE ROBERTS: Thank you, counsel.

21 Mr. Long, you have five minutes.

22 REBUTTAL ARGUMENT OF ROBERT A. LONG, JR.

23 ON BEHALF OF THE PETITIONERS

24 MR. LONG: The ESOP association brief

25 reports at page 2 that there are $1.07 trillion in these

1 employee stock plans, and we think really that's the
2 key, are all of the Courts of Appeals considering many
3 cases, you know, with many different fact patterns have
4 not disagreed. There is no circuit split on the issue
5 that we've spent all our time discussing this morning.
6 The only circuit split is on whether this presumption
7 applies at the motion to dismiss stage.
8 The real point here, as -- as Justice
9 Kennedy said, Congress strongly supports ESOPs. It
10 wants to encourage them so it --
11 JUSTICE SOTOMAYOR: I -- I appreciate that.
12 But if I'm listening to the government carefully and
13 understanding its position, it's basically saying if
14 there's been a violation of a securities law that a
15 fiduciary knows, then why shouldn't it be liable both
16 under the company, under 10b-5, and the director of the
17 plan or the trustee of the plan as a breach of loyalty
18 to -- or -- or of prudence to the beneficiaries?
19 MR. LONG: Well, again -- again --
20 JUSTICE SOTOMAYOR: It's like -- yes, it's a
21 double remedy, but there's lots of things that provide
22 double remedies. So if that person should have
23 disclosed.
24 MR. LONG: Well, I mean, securities law will
25 provide the first remedy. And if you're going to add an

1 additional --

2 JUSTICE SOTOMAYOR: Well, it won't as a

3 trustee.

4 MR. LONG: If you're going to add an

5 additional --

6 JUSTICE SOTOMAYOR: It will against the

7 company.

8 MR. LONG: Well, but -- but the additional

9 ERISA remedy in this ESOP context is going to create

10 these tremendous problems. I -- I couldn't begin to

11 understand what the ESOP fiduciary was supposed to do in

12 these circumstances, I mean, in terms of --

13 JUSTICE SOTOMAYOR: Obey the law. I think

14 that that's the simple answer.

15 MR. LONG: Well, but you will create two

16 different centers of communication now out of each

17 corporation with an ESOP. The corporation's own

18 statements and then the ESOP.

19 JUSTICE SOTOMAYOR: You know they created

20 the conflicts.

21 MR. LONG: Well, I think -- I think --

22 JUSTICE SOTOMAYOR: I'm not shrugging my

23 shoulder out of lack of sympathy but out of reality.

24 The loyalty is to the beneficiaries. If you're going to

25 place someone there who comes to inside knowledge,

1 you're going to create potentially a problem.
2 MR. LONG: Well, but --
3 JUSTICE SOTOMAYOR: But I think your
4 adversary was saying that's a self-induced problem, not
5 one that the law should excuse you from following
6 whatever the law is.
7 MR. LONG: Well, but -- but two points. I
8 mean, you -- I would submit you should be very cautious
9 about interpreting these duties in ways that will make
10 ESOPs unworkable, and I think that would basically cause
11 many companies to say we can't put fiduciaries in that
12 situation, so we're not going to have ESOPs at all.
13 And the -- you know, again, because the
14 special purpose of an ESOP is to give the employees a
15 piece of the rock, ownership in the company, if the
16 company is going through temporary hard times, even if
17 there's a situation where there's some, you know,
18 material misinformation that is out in the market, that
19 may all be corrected in the long term. You know, in
20 this case, if the fiduciaries had shut down the ESOP,
21 they would certainly have been sued because they would
22 have violated the plan terms, and the -- the plan has
23 done very well. It's gone up from $2 to over $22.
24 So they might have had a very hard time
25 winning that case because they would have been

1 challenged that prudence didn't really require you to
2 shut it down. Yes, we were going through some severe
3 problems, but we came through them.
4 That's the razor's edge. That's the rock
5 and the hard place. They're going to be sued unless you
6 recognize this presumption that every court of appeals
7 has recognized to give the ESOP fiduciary some leeway.
8 They're going to be different from any other fiduciary
9 in any other plan because it's the company's stock.
10 And if they, you know -- if -- if the stock
11 goes down under this open-ended duty of prudence,
12 they're going to be sued for not having anticipated that
13 and done something, sold, stopped trading, put out
14 information. But if they don't do it and the stock goes
15 up, they're going to be sued for that.
16 And, in fact, you know, if you recognize the
17 government's approach, there'll be a whole new class of
18 cases, which is, if the stock goes up, their --
19 plaintiffs' lawyers will be able to argue, well, the
20 fiduciary should have -- should have anticipated that,
21 and the participants who were selling and deciding to
22 move over to the S&P 500 fund, you let them sell their
23 stock too cheaply, and that's a violation. So it's --
24 it's unworkable.
25 We submit.

1 CHIEF JUSTICE ROBERTS: Thank you, counsel.
2 The case is submitted.
3 (Whereupon, at 11:30 a.m., the case in the
4 above-entitled matter was submitted.)
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18
19
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21
22
23
24
25

A

$1 36:15
$1.07 53:25
$2 56:23
$200 32:18 36:18
$22 56:23
a.m 1:13 3:2 58:3
ability 42:24
able 16:22 18:19 24:20 57:19
above-entitled 1:11 58:4
absent 10:17
absolute 20:17 52:5
absolutely 16:13 18:1 32:20 37:1
accept 25:16,18 43:11
accepted 10:13 29:15
accommodate 5:7
account 3:25 21:1,10,19,24 37:7 38:5 44:2 44:7,15 46:1
accounted 49:22
accusing 51:2
achieved 24:3
acknowledge 7:19
acquire 37:4
acquiring 5:11 37:24
acquisition 34:22
act 27:7
action 31:17 36:21 39:22
active 10:16 43:3
actively 41:9
actual 10:3,5,22 49:20
add 7:24 54:25 55:4
added 53:6
additional 5:11 44:22 55:1,5,8
address 24:17 29:23
adds 7:21
administrator 5:6
adopt 17:22
adopted 24:6
adversary 56:4
advised 42:23
affect 33:12
afloat 21:9
ago 31:13
agree 9:17 44:19 44:20
agreeing 17:25
agrees 6:13 19:20
aims 3:25 7:7 15:9 24:2
AL 1:3,6
ALF-CIO 47:12
Alito 20:25 21:18 30:7,25 37:3,15,18 44:1 49:10 51:10 52:14,20
Alito's 22:14 23:3
allegation 5:16 5:20 47:24 51:21
alleged 51:15
alleges 29:24 32:7
allow 30:23
allowed 38:4
allowing 9:20 11:21
allows 8:18
amicus 1:21 2:11 43:23
amount 4:15 32:7 49:25
analysis 10:25
announce 12:21
announced 39:3
announcement 11:20
annually 52:23
answer 18:22 23:13 28:1 34:11 35:21 37:15,17 38:19 39:23 52:5 55:14
anticipated 57:12,20
anymore 13:7
anyway 47:6
apart 6:25
apparent 31:16
appeal 27:1
appeals 9:18 23:16 28:10 33:24 54:2 57:6
appear 27:21
APPEARAN... 1:14
appears 23:10
appendix 4:23 44:14
applies 18:6 32:2 54:7
apply 16:6 17:3 17:22 18:16
appoint 13:21 30:22
appointed 47:18
appoints 42:8,9
appreciate 54:11
apprised 48:13
approach 23:16 23:18 52:7 57:17
approximately 49:21
April 1:9
area 47:10
argue 57:19
argument 1:12 2:2,5,8,12 3:3 3:6 15:20 24:11 30:10 43:21 50:15 53:22
arises 30:19
arrange 37:14
aside 30:22 42:3
asked 28:23 34:9 36:2 38:18 44:2
asking 3:21 5:22 6:18 8:21
asleep 31:13
asset 51:6,7
assets 4:14 35:1 47:7 49:21 50:1
association 53:24
assume 11:25 13:10 22:15
assumed 13:6
Assuming 37:16
authority 5:10
authorized 9:1
available 32:2,3 51:24
awkward 14:25

B

back 8:14 16:25 28:16 39:1 41:24
background 13:2
bad 14:18 15:1 21:7 23:10 28:19 40:22 41:1,3 47:16
balance 24:7
Bancorp 1:3 3:4 5:10,12
bankruptcy 21:22
bar 52:8
bargain 25:13 25:16
based 23:13 30:8 38:24 40:25 49:11
baseline 36:24
basic 8:5 15:20 24:23
basically 30:25 54:13 56:10
basis 29:10 49:13
basket 14:20
beginning 42:5
behalf 1:15,17 1:20 2:4,7,10 2:14 3:7 24:12 43:22 53:23
behave 37:10,11 37:19 38:16
believe 33:8 38:21,24 39:19 40:11,24 42:5
believing 39:21
beneficial 23:7 41:7
beneficiaries 7:18 12:4 19:24 20:8 26:3 27:8 35:19 38:6,9 39:22 40:23 41:1,3,7 42:19 44:6 48:18,20 54:18 55:24
beneficiary 14:17 20:17 27:16
benefit 8:10,13 8:25 9:2 24:24 25:2,4,5
benefits 7:17,21 7:23,25 8:8,9,9

8:10,19,21,24 9:7,8,9 15:10 15:13,17,19 17:10 24:16,21 24:22 25:7,8,9 25:10,14,18,20 41:17 43:10,11 44:5,11,12
best 8:12 21:25 22:2,5 24:1 25:24 26:17
better 8:16 12:2 40:6,8
beyond 23:4 31:20 41:22
big 12:23
billion 32:13 36:15
billion-dollar 36:16,18
billions 40:18 47:6,6
binding 7:19
blackout 52:7
blip 38:25
bottom 22:8
bounds 19:25 21:10
breach 27:16 28:13 29:13,20 35:16 42:10,13 45:11,12 54:17
breached 5:19 20:4 26:19 29:18 34:5
break 6:6 29:9
Breyer 26:14,23 27:2,6,14,20 27:25 28:1,4,7 28:15 31:10,20 31:25 39:2,9 39:13,15,23 46:3,17,23 47:1,4 49:15 49:18 50:2
Breyer's 29:8 45:22
brief 27:18,22 45:23 46:4,19 47:12 50:16 53:24
bright-line 24:5
bring 11:1
build 9:21
business 30:18
buy 4:10 6:24 33:16,17,19 35:10,14 38:10 49:23
buying 5:17 6:10 11:16 22:3 38:6,7,11 52:3,6
buys 36:4

C

C 2:1 3:1
call 36:14
care 13:8 46:6
carefully 32:1 42:5 54:12
carves 34:16
case 3:4 10:20 26:16,22,24 27:1,3 28:2,19 29:2,4,24 31:18 37:21 39:1 46:22 48:17,19 53:4 53:6,7,8 56:20 56:25 58:2,3
cases 10:1 28:16 28:22 48:23 54:3 57:18
cash 4:16 6:15
category 10:1 18:5,6 48:22
cause 11:21 12:6 38:7 51:19,25 56:10
causes 16:19
causing 23:18
cautious 56:8
ceases 9:15
centers 55:16
central 34:9
centuries 40:14 43:14
certainly 40:24 56:21
challenged 57:1
chances 18:18
change 12:23
character 3:25 7:6,10
cheaper 13:13
cheaply 57:23
Chief 3:8 14:7 14:14,24 24:9 24:13 33:14,22 35:9,20,24 36:2 38:2,18 42:16 43:4,19 43:24 48:14 53:2,20 58:1
choice 15:25
choices 15:24
choose 26:11
circuit 36:10 45:19 54:4,6
circumstances 44:23 47:16 50:24 53:11 55:12
claim 29:16,19 29:21
class 3:17,18,22 5:22,23 6:18 42:25 43:1 57:17
clear 32:15 41:13 50:11
clearly 29:12
client 26:11
clients 26:8
closest 47:12
coach 3:17,18,22 5:22
collapse 11:22 18:7
collapsing 34:2
collecting 36:19
come 9:19 16:20 16:25 30:16 39:5
comes 7:3,5,5 12:16 26:8 48:20 55:25
comments 36:12
committed 32:21
common 8:18 13:4,19 14:10
communication 55:16
companies 23:9 50:13 52:8 56:11
company 5:18 6:1,3 8:4,10 9:5,10,11,14 9:21,22 10:23 11:9,21 13:5 13:11 14:11,12 14:21,22,25 15:4,24 16:3 17:4,5 18:7,19 20:5,11,15 21:9,21,23 22:11 23:1,2,7 32:22 39:3 40:4,22 42:9 48:13 51:19 53:12 54:16 55:7 56:15,16
company's 6:24 10:3 11:9 15:22 33:16,20 34:2,7 35:11 47:9 49:22,23 57:9
compared 23:10
comparing 40:5
complaint 29:24 29:24 31:19,22 32:6 45:14,20
complete 19:19
Completely 52:2
comply 43:15
concern 22:14 37:24 48:24
concrete 48:15 51:11
concretely 38:3
condition 5:18 31:15
conduct 32:14 51:17,17
conducting 32:12
confession 24:19
confirms 15:8
conflict 26:9 41:16 42:22
conflicted 26:4 30:16 31:9
conflicting 26:8 29:5,6 37:12
conflicts 55:20
confusion 20:15
Congress 4:17 7:11 8:25 15:22 23:7 32:24,25 34:13 35:5 40:9 42:7 42:12,12 50:8 50:12 54:9
congressional 3:14
congressman 32:20
connection 12:20
consequences 22:4 48:5
consider 12:20
considerable 32:10
consideration 41:18
considerations 3:15
considering 54:2
consist 45:13
context 5:24

6:19 30:17 55:9
continue 6:10 29:7
continuing 3:12 5:3
continuous 9:5
contrary 28:2
contributions 43:1
control 34:25
controversial 35:18
corporate 30:15 30:17 51:15,16
corporation 55:17
corporation's 31:15 45:25 55:17
corporations 50:6
correct 22:9 32:5 43:7 50:17
corrected 56:19
counsel 24:20 43:19 53:20 58:1
couple 34:14
course 15:16 27:8 28:12 31:17 34:11 41:25 42:8 46:8 47:15
court 1:1,12 3:3 3:9 9:18 10:12 24:14 26:19 27:1 33:23 35:17 43:25 53:9 57:6
courts 11:1 13:1 18:1 23:15,25 24:6 28:9 54:2
covered 24:24 50:5
create 19:6 20:10,15 55:9 55:15 56:1
created 55:19
creating 51:1
curiae 1:21 2:11 43:23

D

d 3:1 42:6
D.C 1:8,15,20 36:10
damage 11:8,14 51:19
days 52:22
deal 8:23 23:18 40:20 42:7 45:6
death 8:9
decide 18:21 20:13 26:1 30:21 38:23 41:9 42:20 53:4,10
decides 41:3,6
deciding 57:21
decision 3:10 38:5 41:2,4,6
deference 47:25
defies 10:7
define 3:19 8:18 8:23 10:1 22:13,23
defined 7:8 24:25 25:6 34:25
defines 7:10
definition 3:23 4:3 8:21 33:24 44:14
demand 16:14
deny 18:2
Department 1:20 48:24
depends 14:20 14:21
Deputy 1:19
described 4:25
describes 25:3
designed 3:11 4:3 7:8 30:5
desirable 5:7
detail 36:11
determines 5:6
deviate 6:7
different 8:3,7 22:17 23:4 26:2 33:6 34:13 36:25 40:16 54:3 55:16 57:8
differently 37:14
difficult 28:13
dilemma 14:14
dire 53:11
directly 41:16 43:2 46:14
director 54:16
directors 13:5 30:15,17
disability 8:9
disagree 27:24 28:5,8
disagreed 41:12 54:4
disagreement 34:10
disclose 19:12 20:3 52:3
disclosed 15:2 19:18 42:18 52:10,15,19,22 54:23
disclosing 12:9
disclosure 12:25 19:21 20:21 52:24
discovered 32:10
discretion 47:23
discretionary 5:10
discusses 36:11
discussing 13:3 54:5
discussion 32:15
disinterested 42:18
disloyalty 24:19
dismiss 54:7
dispose 36:23
distance 12:16
diverge 30:19
diversification 6:23 34:19,20 48:8
diversified 44:25 51:5
diversify 6:25 33:2,5 50:14
doing 15:1 17:16 17:16 37:1 48:13 51:2
dollar 32:13
dollars 40:18 46:8
double 54:21,22
doubt 25:8
draw 24:1
drop 38:8 44:17 44:23 49:5
Dudenhoeffer 1:6 3:4
duties 3:20 5:22 5:23,23 9:4 25:16,18 26:2 28:11,12,13 29:8,14 34:13 34:17 35:6 42:14 43:11,15 48:9 56:9
duty 3:23,24 5:19 6:5,5,17 6:18,20 7:6 8:11 12:22 18:1,6 19:7 20:4,13,17 22:13,16,21,24 23:13 27:16 28:20 29:15,18 33:5,12 34:5 34:25 35:10,16 35:17,22,23,25 36:7 37:4,9,13 39:20,20 42:10 45:12 50:10 51:13 53:17 57:11

E

E 2:1 3:1,1
earlier 32:15
easiest 33:18
edge 57:4
EDWIN 1:19 2:9 43:21
effects 47:10
eggs 14:19
either 6:6
emphasize 43:9
employee 3:11 14:2 18:19 23:8 24:2,24 25:2,4,5 33:3,9 34:23 43:10 54:1
employee's 23:2
employees 6:2 9:21 12:11 15:24 21:2,7 21:13,17,19 22:5 23:7 25:14 32:22 41:17 42:14 43:2 44:3,3,6 49:8 50:5,12 56:14
employer 3:12 4:5,10,15 26:2 34:23 35:5 37:25 43:9 50:9
employer's 4:12 7:9
employers 9:2 33:1,11 35:7 37:1 43:16
enable 11:15

enables 10:21
enactments 7:12
encourage 15:25 23:8 54:10
encouraged 9:1 9:2
engaged 51:16
England 28:16
enhances 53:14
enormous 39:4
Enron 15:23
enterprise 4:1
entirely 36:25
entitled 49:9
ERISA 4:11 7:8 7:14 8:7 12:23 12:25 14:4 19:6,8,10 24:24 25:4,9 25:11,13,17 27:15 43:9,17 46:9 52:11 55:9
ESOP 3:18 4:12 4:14 6:1,23 7:8 7:22 9:20 11:9 11:20 12:17 15:6,9 17:16 18:3 20:12,25 20:25 22:10,17 23:21 31:4 50:4,8 53:11 53:16,24 55:9 55:11,17,18 56:14,20 57:7
ESOPs 4:1 16:5 17:2 23:20 30:12 54:9 56:10,12
ESQ 1:15,17,19 2:3,6,9,13
essentially 24:19 25:25
ET 1:3,6
evaluation 47:19
events 4:24
eventually 49:4 52:20
evidentiary 45:18
exact 15:23 18:8
exactly 3:10 19:16 29:19 35:10 37:6 45:1 48:14
example 26:15 26:18 35:17 51:11
excepted 50:10
exception 6:23 34:1
exclusive 7:17 25:9 44:4,12
exclusively 7:22
excuse 56:5
exempt 48:7
exempted 7:15
exercise 47:22
exercises 46:2
exist 11:15
expect 17:18,19
expected 5:7
expenses 17:13
expressed 24:1
extent 5:6 34:19 46:20
extremely 15:18

F

face 18:8 30:16
fact 14:18 29:17 33:9 39:22 54:3 57:16
factor 46:1
factors 16:5
facts 38:24
failed 26:20
failing 27:16 53:12
fairly 23:16
fall 29:21
falls 29:17
false 32:8 39:12 39:13
falsity 32:9
far 41:20
feet 31:14
fiduciaries 7:16 10:3,5 27:8 40:14 47:22 48:11 50:10 51:6 56:11,20
fiduciary 8:11 9:4 10:17,20 18:3,21,25 19:23 20:12,20 21:1 23:22 25:16,18 26:19 29:15 31:8 34:5,24 37:10 37:23 38:4,16 40:12 41:16 42:9,10,13,18 43:11 45:4,7 45:12,24 51:13 53:4,10,10,16 53:16 54:15 55:11 57:7,8 57:20
fiduciary's 3:10
Fifth 1:3 3:4 4:24 5:4,10,11 6:15 32:16 36:19
find 4:23
fine 22:12 27:2
Fink 36:11
first 5:23 10:13 12:22 13:18,18 15:5 19:5 24:16,21 25:22 34:11 35:15 45:21 47:19,19 54:25
five 53:21
flag 31:9
flatly 31:1
flighty 36:23
focused 53:13
following 12:9 56:5
forgiveness 34:21
forgives 34:18 34:22
forth 13:9
found 28:22
four 10:4 43:5
frankly 47:12
FTC 31:12
fund 4:25 23:11 32:18 33:10,16 36:15,16,18 42:21,24 43:2 43:3,6,15 57:22
fundamental 36:6 47:20
funds 5:3,12 23:21 35:7,11 35:13 40:17 41:20 43:5 46:9
further 34:21 44:14

G

G 3:1
gamble 11:24
geared 52:25
general 1:19 12:22 19:6 50:10 51:4,12
generally 31:2 44:8
getting 22:8 49:8
GINSBURG 6:21 15:11 25:1 40:19 41:22
give 6:1 13:23 26:15,16,18 51:10 56:14 57:7
given 6:19 29:23 50:13
giving 47:25
glad 34:8
Glenn 31:6,7
go 3:19 4:9 8:14 23:4 28:15 31:20 38:10,13 48:18 50:17 51:25
goes 23:3 40:21 48:21 57:11,14 57:18
going 10:2 14:16 15:3 16:11 18:19 25:14,17 26:12 27:18 31:4 34:1,7 35:12,12 37:5 37:7,8 38:6,7,8 38:10,13,20 40:9,19 41:4 43:10 47:25 54:25 55:4,9 55:24 56:1,12 56:16 57:2,5,8 57:12,15
good 9:6 12:3 15:7 20:9 21:6 40:6,8 46:24
govern 19:21
governed 25:10
government 6:13 7:20 12:16 19:3,20 54:12
government's 14:1 18:12 57:17
Grace 47:17
grand 25:12
great 8:23 11:8 20:15 23:18 32:24 42:7
greater 11:14 12:6
greatest 48:24
guess 20:18 46:11

H

ha 39:7,7
half 35:14 50:5
halt 11:7
hand 26:3
hands 42:4
haphazard 36:23
happen 13:7 31:2
happens 13:19 39:2
hard 18:14 24:18 25:22 27:4 40:12,20 41:11,14 56:16 56:24 57:5
hardship 8:9
harm 12:6
hate 47:9
hear 3:3
held 5:12 9:18 28:10
help 38:20
helpful 51:11
hiring 13:13
history 15:18
hold 51:7
holding 28:2 34:23
holdings 38:12 38:13 48:18
Honor 4:22
hope 9:14 15:16
hopefully 43:5
huge 12:16
hundreds 47:6
hurt 14:17 15:3 38:8

I

idea 9:13 13:20 25:21 32:21 47:5
illegal 51:17
imagine 26:7
immediately 12:6
impact 38:5
implement 40:9 40:10,13
implication 31:6
important 14:12 27:24 29:3 32:21 35:2 36:13 43:8
imposed 40:13
impossible 31:3 39:6
imprudent 36:3 51:5
inbox 31:14
include 48:9
including 9:11
independent 13:21,24 20:13 30:23 42:4
indicated 53:3
indirectly 46:15
individual 44:15
inflated 49:7
information 10:6,14,18,20 11:3 12:1,10 12:18,22,25 13:3,9,24 14:16 15:2 18:16,18,23,25 19:7,13,18 20:11,14 26:20 27:10,17 28:18 29:10,19 30:9 31:23,25 32:2 32:3,7,8 36:20 37:2,4,5,8,24 39:17,24 40:25 41:23 42:1 45:9,9,23 46:14 47:8 48:3,6,16,16 48:19 49:1,11 49:13 50:22 51:15,18,24 52:1,4,9,12,15 53:5,6,14 57:14
inherent 33:3
initial 12:7
inside 10:6,14 10:17,20 11:3 13:24 14:15 15:1,1 16:17 16:18,22 17:19 18:15,23,25 19:17 20:14 26:20 27:10,17 28:18 29:10,18 37:4 39:17,24 45:9,22 46:13 47:8,18 48:16 49:1,11,13 50:21,22 51:14 53:5,6,13 55:25
insider 13:8 31:3 37:5,19 37:19,24 41:23 45:8
insiders 30:11 41:20
insisting 45:4
insofar 44:7
instance 50:19
instructions 6:14
interest 6:2 21:13
interested 42:17
interests 21:1,2 21:25 22:2,5 26:8,9 29:5,6 30:19,20,21 37:12 41:15 44:2,6
interpreting 56:9
invest 4:5,12 6:14 7:9 28:17 28:18 35:11,13 36:25 42:20,24
invested 4:14 5:4,5 23:21 32:16 38:13 53:18
investigate 36:17 47:23 48:2,3,4,4,12
investigating 31:12
investigation 30:1 32:11,13 37:8,22 48:9 51:8
investing 34:6
investment 3:13 4:21,25 8:15 8:16 9:6 10:8 12:3 13:13 17:7 23:10 28:19 30:4 36:8,20 38:17 40:7 42:4,11 48:10 50:9
investments 5:5 11:17 14:19 22:17 32:17 40:6
investor 19:13
investors 21:3,6 22:2
involve 46:10
irrespective 27:9
issue 6:3 15:23 45:7 53:6,7,9 54:4

J

jeopardy 9:23
job 14:20 32:25 33:15,18
jobs 21:8
JOHN 1:6
join 47:2
Joint 4:23
JR 1:15 2:3,13 3:6 53:22
judgment 30:18 50:14
Justice 1:20 3:8 3:16 4:4,8,18 5:15 6:4,8,21 7:13,14,24 8:3 8:7,17 9:7,13 9:15,24 10:19 11:12,25 12:8 12:13 13:2,16 14:7,14,24 15:11 16:1,4 16:11,14,19,21 16:25 17:1,8 17:11,14,25 18:4,12 19:10 19:15,17,22 20:2,7,16,19 20:24,25 21:18 22:12,14,20,23 23:3,12 24:9 24:13 25:1,23 26:14,23 27:2 27:6,14,20,25 27:25 28:1,4,7 28:15 29:7,8 29:16 30:6,7 30:25 31:6,10 31:20,25 32:19 33:4,14,22 34:15 35:9,20 35:24 36:2,9 37:3,15,18 38:2,18 39:2,9 39:13,15,23 40:3,19 41:22 42:16 43:4,19 43:24 44:1,16 44:20,24 45:1 45:6,11,22 46:3,17,23 47:1,4 48:2,14 49:2,10,15,18 50:2,15,25 51:10 52:14,20 53:2,2,20 54:8 54:11,20 55:2 55:6,13,19,22

56:3 58:1
Justices 41:12
justifies 17:16
justify 17:16

K

Kagan 7:13 9:24 10:19 11:12,25 18:4,12 20:24 25:23 27:25 49:2
keep 11:15,16 11:16 12:2 21:8 34:4 38:11 48:12
Kennedy 3:16 8:17 13:2,16 22:12,20,23 23:12 32:19 33:4 40:3 50:15,25 53:2 54:9
Kennedy's 31:6
kernel 10:15
key 53:7,9 54:2
kind 4:2 5:25 6:19 8:25 10:8 11:24 17:3 18:13 22:10,25 23:3 46:10,10 49:23
kinds 8:8 25:14 25:17 28:17
Kneedler 1:19 2:9 43:20,21 43:24 44:16,19 44:21 45:3,10 45:16 46:16,21 46:25 47:3,15 48:4,22 49:12 49:17,25 50:3 50:21 51:3 52:5,18,21 53:8
knew 29:25
know 7:2 8:11 8:15 10:3,6,21 12:3,5,17 13:20 14:5 15:1 16:9,19 18:14 19:8 21:12,14 23:9 23:13,14,20,25 27:17 29:9 30:23 34:1,6 36:4 37:5 38:24 39:16 40:17 42:1 46:9,11,14,19 47:9,11 49:19 49:22,24,25 51:7,8 54:3 55:19 56:13,17 56:19 57:10,16
knowing 39:3
knowingly 42:13
knowledge 16:17,23 17:19 45:25 46:6 55:25
known 29:25
knows 18:25 42:9 54:15

L

labor 46:22 48:25
lack 44:17 55:23
landscape 13:17
language 3:14 6:12 10:7
large 32:7
largest 8:13
Laughter 33:21 40:2
law 3:14 8:18,18 8:22 11:2,5,8 12:9,20 17:23 18:9 19:2,18 19:25 20:2,21 20:22 24:2 27:15 29:9,20 52:25 54:14,24 55:13 56:5,6
laws 11:3 17:20 18:15 52:10,16
lawyer 26:7,10 26:10 46:19
lawyers 57:19
learn 47:8
leeway 8:23 57:7
left 10:15
legal 19:19 29:8 29:11
legislature 32:20
let's 10:4 12:17 12:17 22:15 51:14,24 52:16
level 49:6,7
liable 42:11,14 54:15
lie 35:18
limited 42:25
limits 34:21
line 22:9
linked 15:21
liquid 5:5
liquidation 21:23
liquidity 5:7,13
listening 54:12
living 33:6
long 1:15 2:3,13 3:5,6,8,21 4:7 4:11,22 5:21 6:11,21 7:4,13 7:20 8:2,6,20 9:12,17,25 10:10,24 11:19 12:5,12,15 13:15,18 14:9 14:23 15:5,12 15:15,17 16:2 16:10,13,18,20 16:24 17:6,9 17:12,24 18:5 18:11,17,20 19:14,16 20:1 20:6,9,18 21:11 22:6,18 22:22,24 23:15 24:9 28:10 36:10 53:21,22 53:24 54:19,24 55:4,8,15,21 56:2,7,19
longer 9:6,22 24:3
look 3:23 4:22 5:2 17:12 20:20 21:12 23:9 34:12 42:5
looked 4:19 9:19 15:23
looking 21:16,17
looks 7:6 8:15
losing 12:11
lost 39:11
lot 13:8,19 46:11
lots 15:16 54:21
low 14:4 18:20
low-level 14:2
lower 13:1 17:25
loyalty 5:19 6:5 7:1 9:3 11:4 20:4 29:14,18 33:12 35:7,16 35:17,23,25 37:13 39:20 45:12 54:17 55:24

M

major 52:21
majority 31:7
making 49:2,20
manage 7:16 8:12 25:15 34:25 35:5 43:11
managed 7:22 8:12 41:20 46:9
management 4:16
manager 11:13 42:4,11
managers 40:15
managing 16:7 36:15 38:17 40:17 43:15
Mann 1:17 2:6 24:10,11,13 25:1,3 26:21 26:25 27:5,12 27:19,23 28:3 28:6,9,24 29:12,21 30:13 31:5,19,22 32:5,24 33:7 34:8 35:15,22 36:1,6 37:9,17 37:21 38:15,21 39:8,11,14,19 39:25 40:11,24 41:25 42:23 43:7 47:20
mantra 38:20
market 10:4,16 10:18 16:9,12 16:15,16 17:18 39:16 45:2 47:7 49:15 56:18
marriage 45:15
matching 43:1,5
material 10:11 12:9 20:14,21 52:1,1,9,12 56:18
materially 30:3 48:25 50:19,22 51:9 53:14,18
matter 1:11 27:10 52:17 58:4
maximize 17:10 22:16,25
mean 3:22 6:11 7:25 8:20 9:1 9:13 10:10,11 10:13 11:19 12:22 14:7,14

14:17,19 15:5 16:5 20:10 21:11 22:6 23:15 27:12,14 33:11,15 34:20 41:13 44:21 46:21 54:24 55:12 56:8
means 6:20 34:19 44:6 49:8
meeting 39:5
mention 15:14 34:14
mentioned 16:6 22:4
million 32:18 36:18
minutes 53:21
misinformation 11:15 56:18
misleading 52:17
mismanageme... 53:12
misstatement 20:14
misstatements 20:22
mistake 26:10
money 6:14 12:2 12:11 13:12 14:11 33:17
monitoring 9:5 13:23 14:3 48:10
month 8:16
morning 3:3 33:19 54:5
motion 54:7
move 57:22
moved 12:16
mustn't 38:22
mutual 23:11

N

N 2:1,1 3:1
N.Y 1:17
Nader 31:12
name 7:10
narrow 9:25
narrower 34:24
nature 15:9,21 22:11 23:20 24:21 29:23 36:20
necessarily 21:4 23:24
necessary 21:15
need 6:25 10:18 16:4 17:1,4 25:12 29:23 33:17 41:9,20
needed 6:15
needs 4:15 5:8 5:13 40:1
never 29:2 30:10 30:10 31:16
new 1:17 19:6 57:17
nine 42:21
non-diversified 51:5
non-ESOPs 22:15
nonpublic 48:3 48:5
nub 18:24
number 17:18
numbers 49:20 49:21
numerical 49:19

O

O 2:1 3:1
Obey 55:13
object 6:24
objective 33:25
obligation 26:20 27:7,9 28:20 34:3 38:15 41:16 47:22 48:12
obligations 43:16 52:25 53:10
obviously 46:12
occasions 9:25
offer 3:12 9:2
office 31:12 51:16
officer 51:16
officers 13:5 14:10
oh 8:2 15:15 16:7 26:21
oil 39:4,6,7,12 39:16
okay 14:2 16:15 35:15 36:6,14 39:7,14,23
once 3:18,19 5:17 33:4
ones 48:23
ongoing 48:11
open-ended 57:11
operated 44:12
operating 44:4
operations 17:5
opinion 27:21 31:6,7 36:11 39:18
opposed 21:2 38:20
opposing 24:20
option 3:13 4:8 5:1 47:16
options 11:6 42:21
oral 1:11 2:2,5,8 3:6 24:11 43:21
order 45:4
ordinarily 29:5 30:17 32:14 49:3
ordinary 17:7 30:2 37:25
ought 34:6
outcome 36:8
outguess 16:11 16:15
outset 42:19 44:1
outside 9:25 13:9,13 21:10 30:12 37:6 41:22 47:18
outsider 37:20
outsmart 10:18 17:18 45:2
overlooked 47:21
overvaluation 10:12
overvalue 10:22
overvalued 10:2 10:9 11:18 16:8,16 30:3 39:21 42:2 48:17,25 50:19 50:23 51:9 53:18
overvalues 53:15
owe 26:1
owes 33:11
ownership 3:11 6:2 9:10,21 18:20 23:8 24:3 33:10 35:6 49:22 56:15
owns 23:1

P

P 3:1
page 2:2 4:23 44:13 45:23 53:25
papers 31:14
parallel 30:15
part 4:19,24 14:7,12
participants 7:18 8:13 9:9 9:10 11:9,14 11:23 12:4 16:1 20:23 21:2,6,13,14 21:16 22:1 44:5,8,13 52:11 57:21
particular 4:13 8:24 28:24 29:23 32:17 33:16 40:16 42:20,24 51:16
party 42:17
patently 30:19
patterns 54:3
peculiar 45:24
pension 4:2 8:8 22:10 25:7 32:14
people 14:13 25:15 26:2 29:5 30:23 34:6 35:5 36:14 39:5,16 42:13 43:10,14
percent 4:9,20 33:17 36:5 43:5
percentage 46:9
perfectly 26:4
peril 9:23 29:13
period 27:17 42:25 43:1
periods 15:18 52:8
permissible 37:18
person 10:8 27:6 42:8,9 46:5 54:22
perspective 29:3
petition 44:14
petitioners 1:4 1:16 2:4,14 3:7 25:25 32:9 34:10 41:14,19 51:2 53:23
Petitioners's

50:16
pick 30:21
piece 6:2 8:11 56:15
place 18:14 24:18 25:22 27:4 40:20 41:11,15,24 51:18 55:25 57:5
plain 24:23 31:5 37:21
plaintiffs 57:19
plan 3:11,12 4:2 4:4,7,13,19,20 5:25 6:12,14 6:19 7:7,8,15 7:16 8:4,22 11:14 15:7,14 15:14,17,21 20:23 21:14,16 22:10,16 23:20 24:2,4,23,24 25:9,19 26:3 30:5 32:14,15 32:16 33:3,10 35:1 36:24 40:23 44:4,8 44:11,15,25 48:7,11 49:23 51:5 52:11 53:17 54:17,17 56:22,22 57:9
plan's 6:7
plans 4:13 6:6 7:11 8:7,7,8 15:16 17:17 25:4,5,6,7,15 28:11 33:1 35:6 50:4 52:8 54:1
pleaded 45:18 45:19
pleading 45:14
please 3:9 24:14 43:25
point 4:18 6:5 10:25 11:19 13:3 18:2,24 19:17 20:19 23:3 25:2 26:9 32:6 34:15 35:14 43:9 44:9 45:23 49:2 50:7 51:22 54:8
pointed 44:24 47:20
points 17:2,21 17:22 44:1 45:21 56:7
policy 3:14
portion 33:10
posing 6:4
position 14:25 26:1 31:3 37:6 37:9,19 41:10 41:13 54:13
possession 42:1
possible 19:24
possibly 10:17 42:12 47:5
potential 42:22
potentially 21:5 21:22 56:1
practical 3:15 41:18
practice 13:4
precipitous 49:5
preclude 18:10
preliminary 52:2
Presumably 35:10
presumption 6:22 7:2 45:15 45:15,18 54:6 57:6
presumptively 3:13 23:23
prevent 18:15
price 10:4,22 11:22 15:3 51:25
primarily 4:12 5:4,16 6:9 7:9 46:21
principle 45:17
principles 30:2
prior 52:16,17
private 39:4
probably 26:17 26:22,25 46:8
problem 16:22 19:2,5 22:14 24:18 26:15 27:3 42:2 46:7 56:1,4
problems 13:8 13:22 17:15 18:9,16 20:10 55:10 57:3
procedural 36:14
produce 8:13 15:16
producing 15:19
prohibited 31:1
prohibition 29:11
promulgated 32:8
properly 21:9
protect 19:24 26:11 39:22
protected 20:5 30:18
protection 42:7
prove 44:17 45:13
proven 51:20
provide 7:22 8:7 8:9 18:19 19:7 22:16 25:6,7 25:14,17,20 43:10 54:21,25
provided 8:24 42:7 43:13 50:8,12
provides 19:19 53:1
providing 7:17 7:25 9:8 44:5 44:12
provisions 42:6
prudence 3:23 3:25 5:19 6:5 6:17 7:1,6 9:3 11:4,23 18:1,6 20:4 24:4 30:2 33:8 34:5,18 34:19 35:6,10 36:7,14 38:1 39:20 44:18 48:8 50:11 51:4 53:17 54:18 57:1,11
prudent 3:13 10:8 11:13 16:15 18:2,21 23:23,24 33:25 37:10,23 38:4 41:2,4,6 45:4
prudently 27:7 38:16,17
public 11:20 12:10 18:18 19:1,4,4 31:15 32:8 37:7 45:9 48:6 51:24
publicly 32:1,3 50:5,6,13
purchase 51:6 53:18
purchased 49:7
purchases 11:21 21:21
purchasing 49:14
purity 50:17
purpose 6:1,20 7:17 8:5 9:20 15:12 17:9 25:9,19 44:4 44:12 56:14
purposes 5:25 35:2 50:8
put 26:1,3 37:6 39:7 56:11 57:13
putting 11:16,16 12:2 14:19 31:2

Q

qualifying 34:23
quarterly 52:23
question 8:14 12:7 18:23 24:16 28:23,25 28:25 29:8 34:9 35:3,21 35:25 36:2,15 37:16,17 38:19 38:22 45:22 46:7 49:19,19 51:3 53:3
quite 8:3 12:23 13:19 15:6 21:6 24:23 28:13 30:15 33:15 41:13 53:5
quote 7:16
quoted 6:12 15:12
quoting 45:24

R

R 3:1
raise 31:9
raised 18:24 24:17 25:2,22 46:7
Ralph 31:12
ratio 17:13
razor's 57:4
read 6:12 31:16 31:16
real 19:15 54:8
reality 55:23
realized 9:22
really 10:17 11:18 12:3 13:22 14:9,18

17:9 19:16 40:16 49:18 54:1 57:1
reason 13:11 28:7 29:22 41:14,19 43:14 46:7,24 52:11
reasonable 19:13 30:1 32:12 36:16 51:8
reasonably 24:3
reasons 23:2,4,8
REBUTTAL 2:12 53:22
recall 50:3
receives 51:14
recognize 11:2 57:6,16
recognized 11:1 33:24 57:7
red 31:9
reference 24:22
referred 9:8
refers 24:23
reflection 14:18 25:13
reflects 50:14
refrain 5:11
regard 53:5
regarding 52:17
regime 19:19
related 44:9
relationship 31:8
relative 10:2
release 12:18,22 19:4
relevant 24:16 36:9,9,15
remain 53:18
remedies 54:22
remedy 20:22,23 54:21,25 55:9
remember 25:12 32:1
remove 43:3
reports 53:25
represent 26:7 29:4,6 30:21 30:23
require 4:5,10 6:6 11:4 52:10 57:1
required 20:3 25:10 30:2
requirement 7:1
requirements 4:16 6:16,23 12:24 19:9 48:8
requires 3:12 4:12,13 9:4 11:23 23:20 24:4
requiring 4:20
resolves 35:4
respect 27:7 28:24 34:22 35:22 36:1 44:10
respectfully 27:23
respondents 1:18,22 2:7,11 24:12 34:10 43:23
response 45:22
responsibility 19:11,11,12 46:2
responsive 22:13
restatement 36:13
result 3:15
retain 10:8
retirement 7:21 7:23 11:17 14:21 15:4,7 15:10,14,17,19 17:10 25:15 35:7 41:17
returns 22:16,25 23:5
right 15:6 16:13 17:8,11 26:4 32:4 33:7 35:12,14 38:24 39:24 41:5,8 45:10,16 46:25 47:1,3 49:3 50:13 52:6
rise 29:21 38:25
rises 29:16
risk-return 17:13
risky 11:24 30:4
road 3:19
ROBERT 1:15 2:3,13 3:6 53:22
ROBERTS 14:7 14:14,24 24:9 33:14,22 35:9 35:20,24 36:2 38:2,18 42:16 43:4,19 48:14 53:20 58:1
rock 6:2 8:11 18:14 24:18 25:22 27:3 40:20 41:11,14 56:15 57:4
RONALD 1:17 2:6 24:11
routinely 36:19
rule 16:5 17:2,5 19:23 27:15 30:18
run 5:7,12
running 8:4 14:13 30:12

S

S 1:19 2:1,9 3:1 43:21
S&P 57:22
salutary 32:21
save 14:11 24:7
saves 13:12
saying 3:22 7:25 8:22 9:9 11:23 14:25 17:2 18:4,10,18 20:12 21:18,19 25:25 27:11 28:15 30:25 38:3 46:5 50:20 54:13 56:4
says 3:24 5:3,4,9 6:9 7:15 15:13 19:3,23 28:10 28:19,21 33:19 42:13 44:11 46:4 48:16
Scalia 7:14,24 8:3,7 9:7,13,15 16:1,4,11,14 16:19,21 17:1 17:8,11,14,25 34:16 36:10 44:24
scope 34:21
Scott 45:24
SEC 19:11,21 27:20 46:15,18 46:18
SEC's 27:18
second 6:18 13:20 24:17 44:9
seconds 49:16
section 3:24 7:7 7:14 24:25 25:3,6 34:16 34:25 36:12 42:6 44:3
securities 11:2,3 11:5,8 12:20 17:20 18:9,15 19:2,18 20:20 20:22 34:23,24 52:10,16,25 54:14,24
security 46:22
see 4:20 9:5 36:12 40:3 42:6 49:15
self-induced 56:4
sell 5:10 29:10 30:8 33:18 38:22,23 41:2 41:4 48:17,19 49:4,10,12 52:3 57:22
selling 18:15 41:1,3,7 57:21
sells 39:24 40:21
sensible 35:4
serious 5:18 9:23,23 20:10
serve 31:4 37:12
serving 30:11
set 33:1 42:3
settlor 8:23 28:21
settlor's 33:25
settlors 28:16
seven 9:19
severe 57:2
shareholders 30:20,24
shares 5:11,12 38:8
short 5:7,12
short-term 4:16 5:5 6:15 38:25
shoulder 55:23
shrugging 55:22
shut 12:17 16:2 18:21 24:4 56:20 57:2
shutting 11:11
signal 21:22 40:21
signed 46:19
simple 55:14
simply 19:23 22:1 26:11 30:20 44:23 51:20
sit 39:4

situation 21:20 26:4 30:14,15 30:16,18 36:17 37:14 46:4 47:17 49:1 52:6 53:15 56:12,17
situations 21:5 44:22
Sixth 45:19
so-called 24:18
sofa 31:13
sold 16:7 57:13
sole 25:19
solely 4:5 15:9 32:16
Solicitor 1:19
solution 14:10
solve 13:22 42:2
somebody 14:4
somewhat 52:2
soon 16:3
sorry 14:8 28:15 48:2 49:14
sort 3:17 9:4 10:7 11:21 12:21 19:6 22:7
Sotomayor 4:4,8 4:18 5:15 6:4,8 12:8,13 19:10 19:15,17,22 20:2,7,16,19 29:7,16 30:6 44:16,20 45:1 45:6,11 48:2 54:11,20 55:2 55:6,13,19,22 56:3
sounds 20:9
sources 20:11
south 34:1
speaks 44:3
special 5:25,25 6:19 7:10 8:21 15:8 16:4 17:2 17:4,23 22:10 22:25 23:19 24:2 51:1 56:14
specific 4:2 12:24 19:8
specifically 34:16
spelled 19:7
spent 54:5
split 54:4,6
spoken 7:11
stable 22:16
stage 52:2 54:7
stake 9:21 35:8
standard 10:12 22:13 24:5,5 33:8 37:25 40:12,13,14 43:12,13 50:18 50:18 51:1,4 53:4
statement 36:8 52:17
statements 51:12 55:18
states 1:1,12,21 2:10 4:24 43:22
status 42:16
statute 4:11 6:22 7:3,5 15:13,13 24:22 25:13,20 32:23,25 33:1 34:12,15 35:4 41:18 42:13 50:11,11
statutory 3:14 3:23 7:1,12
stay 21:9
step 22:3 30:22 31:23,24 43:3 47:19
stepping 42:3
steps 10:11
stock 3:11,12 4:5,10,13,15 4:25 5:4,17 6:1 6:15,24 7:9 8:4 8:10 9:10,11 9:14 10:1,9,16 10:21 11:16,21 11:22 12:11,14 15:3,4,22,24 16:8,8 17:4,5 21:21 22:3,11 23:1 30:3,3,8 32:16,22 33:3 33:9,11,16,20 34:7 35:5,11 35:13 36:4,19 36:24,25 38:6 39:21 40:4 41:1 42:2 44:16,23 47:7 47:9 48:17,25 49:6,7,23 50:9 51:25 52:3,9 53:15,19 54:1 57:9,10,14,18 57:23
stock's 45:25
stocks 38:25 40:5 46:10
stop 22:2 38:5 49:14 52:3,6
stopped 5:17 11:20 57:13
stopping 12:6,10 21:20,21
stops 38:7
strike 39:4,6,12
strongly 9:1,2 54:9
structure 31:7
sub 24:25 25:3
subject 25:4
submit 56:8 57:25
submitted 58:2 58:4
substantive 45:17
successful 15:18
sue 48:18,20
sued 56:21 57:5 57:12,15
suggested 41:19
suggesting 52:24
suggestion 14:1
support 3:15
supporting 1:21 2:11 43:23
supports 54:9
suppose 11:12 32:19
supposed 16:9 19:12 23:14 30:9 33:23 39:10,18 40:4 42:14 47:1,7 47:13 48:21 52:4 55:11
Supreme 1:1,12
sure 27:12
Surely 16:14
surprised 28:21 28:22
sustain 35:23
sympathy 55:23

T

T 2:1,1
take 3:25 10:10 21:1,19 36:21 37:7,23 38:5 39:22 42:19 43:3
taken 13:8 21:9 21:23 31:17 44:7 46:1
takes 46:6
talk 4:1 24:15 25:21 38:2
talked 19:2
talking 4:2 10:19 14:15 48:23
tell 10:17 13:4,7 13:10,16 35:5 46:17 47:4,9
telling 31:14,15 37:1
tells 33:1
temporary 56:16
ten 31:14
term 6:7 18:20 56:19
terms 19:20 44:4 46:1 48:15 50:7 55:12 56:22
terrible 11:22
test 18:12
text 7:5
Thank 24:9,13 43:18,19 53:20 58:1
thing 36:6,12,13 40:15 43:8 46:4 49:3
things 28:17 34:14 40:22 54:21
think 5:14 6:12 6:18 7:4,10 8:20 10:13,15 11:10 12:7,12 12:19 14:11 15:8 18:23 19:5 20:9 21:11,12,15,17 22:6,9,18,22 22:24 23:25 24:15,18 25:1 25:8,12,24,24 26:21,23,25 27:19,23,24 29:12,13,17,22 30:14 31:5,18 32:24 33:7,19 33:23 34:8,9 35:18 37:3,21 38:10,15,23 39:11,25 41:6 41:9 43:8 44:17,24 47:11 47:20 49:1

50:4,17 51:23 53:8,15 54:1 55:13,21,21 56:3,10
thinking 34:12
thinks 20:13 46:15
third 1:3 3:4 4:25 5:4,10,11 6:15 15:17 32:16 36:19
thought 23:7
three 39:5
time 9:20 24:7 29:13 30:4 39:7 54:5 56:24
times 10:5 38:16 56:16
timing 19:20,21
tolerate 43:17
top 14:13
totally 15:6 31:11 39:17,24
track 39:11
trade 11:2 21:21
traded 10:16 50:6,6,13
trading 11:7 19:3 52:8 57:13
traditional 40:12
traveling 3:18
tremendous 55:10
trigger 21:22
trillion 53:25
trillions 46:8
trouble 16:3 23:18
true 29:12 39:12 42:8 44:25 45:1 47:17 48:5
trust 3:14 8:18 8:22 13:11 24:1 27:15 31:8 36:8 42:3
trustee 3:17,20 3:22 5:9 6:6 13:10,21,23,24 14:3 16:6,9,15 17:3 23:12 26:19 29:9 31:4 32:13 33:5 36:3,16 37:3,7,10,11 37:12,13,22 38:7 39:3,9,19 39:21 40:4,21 41:2,6 42:17 46:2 47:17,18 48:1,15 51:14 51:23,23 54:17 55:3
trustee's 31:11 33:15 40:25
trustees 13:6 22:15 28:11,12 29:4,25 30:11 33:2 37:4 40:16 41:23 47:5,18,24
trusteeship 46:5
trusts 26:17 40:15
truth 49:4
truthful 12:1
turn 46:5 47:14
turns 51:17
two 17:21 20:11 25:5 26:2,7 32:8 39:15 49:16 55:15 56:7
type 24:23 30:1
types 25:5

U

ultimate 12:12
ultimately 12:15
unable 37:11
unanimously 28:10
uncommon 52:7
understand 27:25 28:25 34:4 40:8,8 41:12 55:11
understanding 34:13 54:13
understood 5:17 5:24
undertake 29:5 37:22
undertaken 30:1 32:10 40:15 41:15
undertakes 26:7
undertook 29:4
undiluted 7:2
undiversified 15:7
uniform 23:16
union 46:3
United 1:1,12,21 2:10 43:22
unprotected 52:12
unusual 43:12 44:22
unwise 31:1
unworkable 10:13 43:13 56:10 57:24
use 5:15 16:22 16:24 17:19 26:20 27:9,17 44:10
usefully 24:15

V

v 1:5 3:4
valuable 9:14,16
value 10:3,5,22 38:8 45:25 48:20 53:14
variety 32:17
Varity 35:18
vehicle 22:25 23:1
verge 18:7
vexing 45:7
view 40:25
violate 11:3,7 14:3 17:20 26:13 37:25
violated 56:22
violates 39:20
violating 37:13
violation 11:4 14:5 20:21 54:14 57:23

W

wait 41:25
walk 31:11
want 3:16 14:8 14:13 15:23 16:20 18:22 21:8,8 31:20 32:2 37:5 42:20 50:7
wanted 40:10 43:4
wants 54:10
Washington 1:8 1:15,20
way 8:19 10:2,2 10:2,22 22:7,8 23:4,25 25:24 26:6 29:1 36:23 39:2 46:1 48:18
ways 56:9
We'll 3:3
we're 3:17,21,22 3:22 4:1 5:22 6:18 8:20,21 11:10 14:15 17:25 18:17 21:15,16 40:9 41:4,24 45:3 48:23 56:12
we've 12:16 54:5
Wednesday 1:9
week 8:16
welfare 25:7,15
went 43:1
wildly 10:9 49:20
winning 56:25
word 5:15 7:21 44:10 46:12
words 40:7 47:2 47:2,4
work 22:7 32:23
works 26:6
world 33:6,18
worse 40:23
worth 40:17
worthless 9:11 12:11,13 39:16
wouldn't 14:4 28:21 29:20 30:13
WR 47:17
write 32:23 42:12 47:2
writing 32:25
written 6:22
wrong 11:10 12:8 13:10,14 19:23 27:11 32:4 41:5,8
wrote 32:25 36:10 46:12

X

x 1:2,7

Y

yeah 39:5
years 23:17 26:18 31:13
York 1:17

Z

0

1

1 32:18
10 4:9 36:5
10:29 1:13 3:2

100 4:20 33:17 36:18
1002 24:25 25:3
10b-5 19:11 54:16
11:30 58:3
1104 7:14 44:3
1104(a) 44:11
1104(a)(1)(b) 3:24
1105(c) 42:6
1107(d)(6) 7:7
12 50:4
12-751 1:4 3:4
1234 44:15
14,000 50:4

2

2 1:9 53:25
20 23:17
2006 50:12
2014 1:9
24 2:7

3

3 2:4 24:25 25:3
3.3 4:24
31 45:23

4

4 52:22
403 34:25
404(a)(2) 34:16
404(a)(2)(A) 24:22
43 2:11

5

500 57:22
53 2:14

6

6(a) 44:13

7

735 4:23
736 5:2
737 5:3

8

8(k) 52:22
800 26:18

9

90 36:12