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NO. 12-751

In the
Supreme Court of the United States

FIFTH THIRD BANCORP, ET AL.,

Petitioners,

v.

JOHN DUDENHOEFFER, ET AL.,

Respondents.

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

BRIEF OF *AMICUS CURIAE* DELTA AIR LINES, INC., IN SUPPORT OF PETITIONERS

PAUL D. CLEMENT
Counsel of Record
JEFFREY M. HARRIS
BARBARA A. SMITH
BANCROFT PLLC
1919 M Street NW
Suite 470
Washington, DC 20036
(202) 234-0090
pclement@bancroftpllc.com

Counsel for Amicus Curiae

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INTEREST OF *AMICUS CURIAE*

Delta Air Lines, Inc. is one of the world's largest airlines.[1] Delta operates more than 5,000 flights each day and has nearly 80,000 employees. Since 1971, Delta has offered its employees a pension and profit-sharing plan known as the Delta Family Care Savings Plan ("Plan") that has encouraged investments in Delta stock; Delta also made matching contributions to employees' accounts in the form of company stock.

Delta has learned first-hand how a precipitous drop in share price can attract ERISA litigation that employs 20/20 hindsight to question fiduciaries' decision to invest in company stock. Since 2004, Delta has been embroiled in "stock drop" class-action litigation under ERISA, in which the plaintiffs allege that the Plan's fiduciaries should have liquidated all holdings of Delta stock when the company—and, indeed, the entire airline industry—experienced business challenges in the early 2000s. *See Smith v. Delta Air Lines*, No. 04-cv-2592 (N.D. Ga.), *appeal pending* No. 13-15155 (11th Cir.).

That litigation does not involve allegations that material information was withheld from the market, such that Delta stock was trading at an artificially inflated price. Nor was Delta subject to securities actions making similar allegations. Instead, Delta has spent years litigating a case premised on the notion that fiduciaries of a Plan designed to foster employee

[1] This brief was not written in whole or in part by counsel for any party, and no person or entity other than *amici* and their counsel has made a monetary contribution to the preparation and submission of this brief. The parties have consented to the filing of this brief.

ownership of Delta stock invested in Delta stock at the wrong time.

Delta accordingly has a strong interest in ensuring that ERISA is properly interpreted in light of the unique features of employee stock ownership plans.

INTRODUCTION AND SUMMARY OF ARGUMENT

Congress has long viewed employee ownership of employer stock as "a goal in and of itself." *Moench v. Robertson*, 62 F.3d 553, 568 (3d Cir. 1995). That is, Congress views employee stock ownership plans as a "device for expanding the national capital base among employees—an effective merger of the roles of capitalist and worker." *Donovan v. Cunningham*, 716 F.2d 1455, 1458 (5th Cir. 1983). Countless employers, including Delta, offer ERISA-regulated plans that include investments in company stock. Consistent with Congress' policy goals, the purpose of these plans is to align incentives between employees and stockholders, ensure that employees have a vested stake in the company's long-term growth, and provide an additional source of retirement savings.

Many of those same companies have also been targeted by plaintiffs' lawyers in class-action suits under ERISA. Although such lawsuits often include allegations of fraud or accompany securities litigation, plaintiffs have not viewed such allegations as necessary. Rather, companies that offer investments in employer stock have faced meritless and burdensome ERISA litigation often premised on a drop in stock price alone, without any allegation of fraud, illegality, improper accounting, or other wrongdoing.

Delta's experience in this regard has been indicative of companies that have had to endure years of litigation because they decided to adopt an employee stock ownership plan ("ESOP") and, in hindsight, their stock proved to be a poor investment during certain time periods. During the early 2000s, Delta—like every other full-service airline—faced a number of business challenges, including reduced consumer demand in the wake of the 9/11 attacks, high fuel prices, and vigorous competition from new entrants. But at the same time, Delta took aggressive and unprecedented steps to turn the company around and position it for long-term success. At every step of this process, all relevant information about Delta and the airline industry was known to the market; there is no allegation that Delta misstated earnings, overvalued assets, covered up negative results, or took any other steps that would have caused its stock price to be artificially inflated.

Instead, the plaintiffs in Delta's ERISA case simply allege that the fiduciaries of Delta's ESOP plan should have been able to foresee that the company's turnaround efforts would not succeed. The plaintiffs contend that ERISA required the fiduciaries of Delta's ESOP plan to disregard their specific instructions and divest the plan of all Delta stock while the turnaround plans were proceeding. And they insist that a significant stock drop, combined with amorphous allegations of "mismanagement," should be enough to survive a motion to dismiss.

Delta strongly agrees with Petitioners that ERISA fiduciaries' decisions to allow investments in employer stock should be subject—at the pleading stage—to a highly deferential abuse-of-discretion standard. Indeed, such a deferential standard is particularly appropriate in mere stock-drop cases. Whatever this Court decides about the appropriateness of that standard more generally, it is vital that a deferential standard apply when plaintiffs allege no more than a stock-drop or offer only vague allegations of mismanagement.

Such a standard is necessary to effectuate the basic congressional policy behind ESOPs. The policies behind ESOPs apply fully whether share prices are falling or rising, and a falling market allows employees to obtain a larger share of the company "on the cheap." Investments in company stock are typically made for the long-run, and fiduciaries cannot be expected to engage in a quixotic effort to avoid losses by trading in response to short-term price swings. To be sure, an employee's shares, like management's shares, can lose much of their value if the company ultimately fails. But fiduciaries of an ESOP cannot be expected to outsmart the market, nor can they be made insurers against the risk of bankruptcy.

Even the United States concedes that a plaintiff should not be able to state a claim merely because "the company or industry was suffering financial difficulties." But the government then advocates several steps—such as eliminating the deferential standard of review altogether—that would eviscerate companies' primary protections against such frivolous claims. At a minimum, this Court should convert the government's concession into a concrete rule that will protect fiduciaries from claims that they should have anticipated a stock drop. When there is no allegation that a company's stock price reflected anything other than its true value, claims challenging a plan fiduciary's investments in employer stock should be subject, at the pleading stage, to a highly deferential abuse-of-discretion standard of review.

ARGUMENT

I. The ERISA Class-Action Claims Against Delta Exemplify The Meritless Stock-Drop Claims That Should Be Subject To A Deferential Standard Of Review.

A. The class-action ERISA claims that have been pending against Delta since 2004 offer a prime example of why a deferential standard of review is needed to protect ESOP fiduciaries from meritless "stock drop" litigation. *See Smith v. Delta Air Lines*, No. 04-cv-2592 (N.D. Ga.).

Since 1971, Delta has offered eligible employees a defined-contribution "401(k)" benefit plan, which is funded through employees' own voluntary contributions as well as matching funds contributed by the company. For their voluntary contributions, plan participants could choose from a number of different investment options, one of which was a fund that invested in Delta common stock. The plan also provided that Delta's matching contributions would be made using Delta stock. In short, Delta took advantage of Congress' invitation to create an ESOP that gave employees a direct stake in the company. The fiduciaries of the plan could not alter that foundational feature of the plan without changing its fundamental character as an ESOP.

Like every other full-service airline, Delta encountered a number of significant business challenges in the early 2000s. The September 11th attacks led to a sharp decrease in consumer demand, as well as higher fuel prices as a result of the subsequent conflicts in the Middle East. Full-service carriers also faced new competition from low-cost entrants at the same time that they were struggling with expensive union contracts signed during flush times in the late 1990s. As a result of these challenges, Delta incurred several straight quarters of losses, and its stock price fell significantly between 2000 and 2004.

At the same time, Delta was taking aggressive steps to address each of those challenges. Among other measures, Delta cut prices and revamped its fare structure; laid off 16,000 employees; replaced its CEO; reduced frequent-flier benefits; sold several new jets and a fuel hedge portfolio to generate cash; built up cash and liquidity reserves; and launched a new low-cost subsidiary. In short, Delta faced multiple challenges but was taking decisive action to confront those challenges and position the company for long-term profitability and growth. At several times during this difficult period, Delta's stock price outperformed the market, thus suggesting that the market believed Delta's turnaround efforts were on the right track.

Nonetheless, in August 2004, Delta made a decision to alter the plan terms to authorize an independent assessment of whether continued investments in Delta shares were advisable. An independent investment manager ultimately decided to suspend such purchases in September 2004, and Delta entered bankruptcy in September 2005.

B. Delta has been embroiled in class-action ERISA litigation since 2004. Relying solely on hindsight, the plaintiffs allege that the fiduciaries of Delta's plan *should have known* as early as September 2000 that Delta stock was an imprudent investment and that the company would ultimately go bankrupt. *See* Amended Complaint ¶¶ 182-84, *Smith v. Delta Air Lines*, No. 04-cv-2592 (N.D. Ga. Mar. 16, 2005) (DN 42). The plaintiffs contend that—in light of Delta's falling stock price—the plan's fiduciaries had a duty under ERISA to deviate from the clear terms of the plan and liquidate all holdings of Delta stock. *Id.* ¶¶ 205-13.

The claims against Delta exemplify everything that is wrong with stock-drop class actions under ERISA. The plaintiffs' allegations are based solely on publicly available press releases, financial statements, and news sources. The complaint does not identify any material information about Delta's financial situation that was known by the fiduciaries but not disclosed to the market. Nor does it allege that Delta's stock traded at an artificially inflated price due to fraud, improper accounting practices, overvaluation of assets, or material misstatements about the company's prospects. And Delta has never faced an SEC enforcement action or private securities litigation under Rule 10b-5.

In short, at every step of the way, Delta's stock price reflected the market's collective judgment about the value of the company and its prospects for future growth. The crux of the plaintiffs' complaint is that the fiduciaries of Delta's plan should have known *better* than the market what the future held for Delta, and that they should have used that perfect foresight to depart from the clear terms of the plan and liquidate all holdings of Delta stock.

In Delta's ERISA case, the district court has correctly concluded (twice) that the plaintiffs' stock-drop allegations fail to state a claim under ERISA. *See* Order, *Smith v. Delta Air Lines*, No. 04-cv-2592 (N.D. Ga. Nov. 1, 2013) (DN 121); *Smith v. Delta Air Lines*, 422 F. Supp. 2d 1310 (N.D. Ga. 2006). But those decisions relied in part on the deferential standard of review for a plan's investments in employer stock. And the plaintiff continues to argue on appeal that a stock drop plus amorphous allegations of "mismanagement" should be sufficient to survive a motion to dismiss and proceed to discovery. *See* No. 13-15155 (11th Cir.).

As explained below, however this Court resolves any broader questions about the presumption of prudence for fiduciaries of ESOPs, it should make clear that simple stock-drop claims such as the claims against Delta are subject to a deferential abuse-of-discretion standard that is fully applicable at the motion-to-dismiss stage of the litigation.

II. A Deferential Abuse-Of-Discretion Standard Should Apply When There Are No Plausible Allegations That The Employer's Stock Price Was Artificially Inflated Or Overvalued.

Even the United States apparently agrees that claims against an ESOP fiduciary alleging nothing more than a stock drop—such as the claims against

Delta—do not suffice and should be dismissed for failure to state a claim. In a single sentence in its invitation brief, the United States concedes (at 12) that "a plaintiff cannot state a claim merely because the company or industry was suffering financial difficulties." That concession is important. The whole point of ESOPs is to encourage employee ownership of the employer's stock. The policies behind employee ownership are not limited to a rising market or to companies that experience steady growth. Thus, fiduciaries need to be protected against litigation when the employer's stock turns out in hindsight to have been a relatively unattractive investment over a defined period of time.

But while the United States is clear that such allegations do not suffice, it is far less clear how fiduciaries and companies will be protected against such litigation going forward. In practice, the primary protection against frivolous stock-drop litigation has been robust application of the abuse-of-discretion standard at the motion-to-dismiss stage. Yet the United States would discard that standard and, in all events, argues that the deferential standard should not apply at the motion-to-dismiss stage. The United States is wrong on both counts, as Petitioners explain at length.

But at a bare minimum, this Court must convert the government's concession into concrete protection for defendants faced with nothing more than allegations that the stock dropped and the fiduciaries should have known that poor performance—or even bankruptcy—was imminent. In those circumstances, the abuse-of-discretion standard should apply with full force at the motion-to-dismiss stage. This Court should expressly hold that complaints merely alleging a stock drop—without more—do not state a claim under ERISA and should be dismissed.

A. At a Minimum, Fiduciaries of an ESOP Plan Should Have No Obligation To Deviate from the Plan Unless They Know That the Market Price Is Artificially Inflated.

As Petitioners ably explain, *all* decisions by an ESOP fiduciary to invest in employer stock should be governed by a deferential standard of review that can be overcome only in extraordinary circumstances. *See* Pet. Br. 21-44. But, at the very least, this Court should hold that the deferential abuse-of-discretion standard applies to claims alleging nothing more than a stock drop, with no allegations that the stock price was artificially inflated or overvalued by information withheld from the market.

1. Congress has long expressed a clear policy in favor of employee ownership of employer stock, as reflected in ERISA and a number of other federal statutes. The ultimate goal of employee stock ownership plans is to "merge[] the roles of capitalist and worker," *Donovan*, 716 F.2d at 1458, to ensure that employees have a vested stake in the success of their employer.

That policy of promoting employee stock ownership applies with full force whether a company is enjoying good times or struggling through a difficult period. It would hardly serve Congress' goals—and, indeed, would directly undermine them—if ERISA were construed to place fiduciaries in legal jeopardy merely because they continued to allow investments in company stock after the price had recently fallen. "Buy low and sell high" is a bedrock principle of investing. If plan participants are allowed to invest in company stock when the price is low, they will have the opportunity to earn very strong returns if the company subsequently returns to profitability. And allowing employees to purchase their employer's shares at historical lows would also mean that employees could obtain a relatively large number of shares, which would mean an even greater degree of employee ownership in the event of a turnaround.

To take just one example, in the mid-1990s, Apple faced major business challenges and its stock fell to a 10-year low of approximately $4 per share (down nearly 80% from its peak). The company was "hemorrhaging money and market share and lacked leadership," and it had "flooded the market" with a "confusing array" of new products. *See* Jason D. O'Grady, *Apple Inc.* 34 (2009). Apple "should, by all accounts, have gone bankrupt sometime in 1995 or 1996," and was "on its deathbed in 1997." *Id.* Yet if the fiduciaries of Apple's benefit plan had liquidated their holdings of company stock during that difficult period, they would have deprived employees of a 15,000% return over the next 15 years as the company recovered and returned to profitability. Nothing in ERISA should be construed as requiring fiduciaries to unload company stock just because the going has gotten tough.

Relatedly, courts have emphasized that employee stock ownership plans are typically "designed for the long haul," and "[m]arket timing is not how prudent pension fund investing usually works." *Lanfear v. Home Depot, Inc.*, 679 F.3d 1267, 1282 (11th Cir. 2012). At any given point in time, the price of a stock is the "best estimate available … of the company's value." *Summers v. State Street Bank*, 453 F.3d 404, 408 (7th Cir. 2006). Nothing in ERISA requires a fiduciary to "act on the assumption that the market was overvaluing" the employer's stock. *Id.*

The United States contends (at 13) that the deferential standard of review should not apply if "it is plausibly alleged that petitioners knew (or should have known) that the stock price was significantly inflated due to market misrepresentations or could have ascertained that fact from a proper investigation." Even under those circumstances, there are strong arguments, persuasively presented by Petitioners, that a presumption of prudence should still apply. Pet. Br. 42-44. For example, even if the fiduciaries are aware of information suggesting that the company's stock is overvalued, they could determine that any drop in price is likely to be temporary, and that the stock remains a good long-term investment. And, as Petitioners explain, nothing in ERISA imposes an obligation on fiduciaries to trade based on inside information. Pet. Br. 42-43.

But, in all events, this Court should hold at an absolute minimum that when there are no allegations that the stock price is artificially inflated or overvalued, fiduciaries are entitled to deferential abuse-of-discretion review when they invest in employer stock pursuant to the terms of the plan. Any other rule would impose on fiduciaries an impossible burden of omniscience. As Judge Posner has explained on behalf of the Seventh Circuit, "determining the 'right' point, or even range of 'right' points, for an ESOP fiduciary to break the plan and start diversifying may be beyond the practical capacity of the courts to determine." *Summers*, 453 F.3d at 411.

Plan fiduciaries are not insurers of a stock's successful performance, and when they allow investments in company stock pursuant to the plain terms of an ESOP plan, they should be protected by a strong presumption that their actions were entirely appropriate. As noted, the congressional policies behind ESOPs are not limited to bull markets or growth stocks. In similar fashion, fiduciaries of ESOP plans should be fully entitled to rely on the market price for the company stock, and fully entitled to purchase equity for the employees on the cheap, even in a falling market.

Delta generally agrees with Petitioners' formulation of the test. Consistent with decisions such as *Moench*, 62 F.3d 553, and *Lanfear*, 679 F.3d 1267, Petitioners contend that a plaintiff should not be able to state a claim absent "extraordinary circumstances that would render continued investment in employer securities imprudent *in the context of an ESOP*." Pet. Br. 19, 23-24, 30, 45. But certain language in Petitioners' brief could be construed as suggesting a narrower protection for plan fiduciaries. *See* Pet. Br. 16 ("serious threat to the employer's viability"); *id.* at 17 ("serious threat to the company's ongoing viability"); *id.* at 28, 34 (same). It should take more than a "serious threat" to trigger an obligation to break the terms of the plan and divest an

ESOP of company stock. As noted above, many companies will ultimately recover from "serious threats," and employees should not be deprived of the opportunity to invest in a company during its turnaround.

Consistent with well-established precedent among the lower courts, this Court should hold that a fiduciary has no obligation to divest a plan of employer stock unless the circumstances are so dire that *no reasonable fiduciary* could have concluded that employer stock remained a prudent investment. *See Lanfear*, 679 F.3d at 1281; *White v. Marshall & Ilsey Corp.*, 714 F.3d 980, 988 (7th Cir. 2013) (plaintiffs challenging the prudence of holding employer stock must show that "the circumstances were so compelling that no reasonable fiduciaries would have thought they should continue to offer the stock as directed in the plan"); *In re Citigroup ERISA Litig.*, 662 F.3d 128, 140 (2d Cir. 2011). Any less-deferential standard would not provide adequate protection for fiduciaries who allow employees to continue investing in company stock during difficult times so that the employees could also share in the gains if the company subsequently recovers.

2. The fact that a company ultimately filed for bankruptcy should not affect application of the deferential standard of review to simple stock-drop claims. A fiduciary's decision to allow investments in employer stock must be judged "based upon information available to the fiduciary at the time of each investment decision and not 'from the vantage point of hindsight.'" *Citigroup*, 662 F.3d at 140; *see DiFelice v. U.S. Airways*, 497 F.3d 410, 424 (4th Cir.

2007) ("whether a fiduciary's actions are prudent cannot be measured in hindsight, whether this hindsight would accrue to the fiduciary's detriment or benefit"). That is, "the ultimate outcome of an investment is not proof of imprudence" because ERISA "'requires prudence, not prescience.'" *DeBruyne v. Equitable Life Assurance Soc'y*, 920 F.2d 457, 465 (7th Cir. 1990).

Following a downturn, some companies may quickly return to profitability, while others will ultimately be forced to file for bankruptcy. The latter situation is of course unfortunate, but it is unfortunate for all shareholders, whether management, employees, or third parties. A plan fiduciary cannot be expected to know in advance whether a company's turnaround efforts will succeed or fail. *See Wright v. Oregon Metallurgical Corp.*, 360 F.3d 1090, 1099 (9th Cir. 2004) (the "[s]tock price benefits" from a company's actions might only be realized "years into the future"). Congress was well aware that investment in the stock of a single company could carry "significant risk," but it nonetheless concluded that "the possible benefits to employees and employers from undiversified investments in employer stock … out-weigh the risks inuring from such strategy." *DiFelice*, 497 F.3d at 424-25.

For similar reasons, plaintiffs should not be allowed to plead around the deferential standard of review by alleging a stock drop plus amorphous claims of "mismanagement." For example, in Delta's case, the plaintiffs argue that the company *must* have been mismanaged because it ultimately filed for bankruptcy. *See* Appellant's Br. at 44-45, *Smith v.*

Delta Air Lines, No. 13-15155 (11th Cir. Dec. 30, 2013).

Such arguments are the very definition of impermissible hindsight. Every time a company files for bankruptcy, it is easy to allege, with perfect hindsight, that the company's managers should have made different decisions and that fiduciaries should have realized the turnaround strategy was destined to fail. But, absent specific allegations that the fiduciaries were aware of information that had not been disclosed to the market, there is no reason to think that the shares were mispriced. Companies facing serious difficulties generally trade at substantial discounts, which reflect the possibility of a turnaround or bankruptcy. If fiduciaries cannot rely on the market in such situations, employees will lose out on historic buying opportunities when bankruptcy is avoided. And when bankruptcy is not avoided, alleging mismanagement hardly justifies eliminating the appropriately deferential standard of review. Turnaround efforts can fail based on factors entirely outside the control of management.

B. The Deferential Standard of Review Should Apply at the Motion-To-Dismiss Stage.

A deferential standard of review for fiduciaries' investments in employer stock—especially when there are no allegations that the market price of the stock reflected anything other than the true price—is critical to achieving Congress' goal of promoting employee ownership of employer stock. But it is not sufficient. The Court should also hold that the deferential standard of review is a substantive rule of law that applies with full force at the motion-to-dismiss stage. *See* Pet. Br. 45-50.

As noted above, the United States concedes (at 12) that "a plaintiff cannot state a claim merely because the company or industry was suffering financial difficulties." In support of that proposition, the government cites the Fourth Circuit's decision in *DiFelice v. U.S. Airways*, 497 F.3d 410. Like the claims against Delta, *DiFelice* involved stock-drop claims against an airline arising out of the difficulties faced by the airline industry in the early 2000s. *See id.* at 415-16. The Fourth Circuit correctly held that "the Employees cannot succeed in this lawsuit simply by demonstrating that U.S. Airways offered the Company Fund during a time of grave uncertainty for the company, no matter how significant the Employees' ultimate financial losses." *Id.* at 425.

But the Fourth Circuit reached that conclusion only after years of litigation and a full-blown bench trial.[2] There is thus a profound disconnect between the government's proclamation that "a plaintiff cannot *state a claim*" merely by alleging financial difficulties, which suggests a motion to dismiss standard, and its citation of the Fourth Circuit's post-trial determination in *DiFelice*. Indeed, the government's proposed resolution of this case—*i.e.*, eliminating the presumption of prudence and/or applying that standard only at a late stage of the proceedings—

[2] Similarly, stock-drop claims against the trustees of United Air Lines' ESOP were dismissed only after discovery and summary judgment briefing. *See Summers*, 453 F.3d at 407-09 (fiduciaries were not "required to act on the assumption that the market was overvaluing United").

would only make it more likely that cases such as *DiFelice* survive a motion to dismiss.

The presumption of prudence and its availability at the motion-to-dismiss stage are the primary tools courts have used to conclude that stock-drop cases do not state a claim for relief. Eliminating those tools will all but guarantee plaintiffs an opportunity to obtain costly discovery even in cases where plaintiffs cannot state a valid claim. As Judge Cabranes recently explained on behalf of the Second Circuit, "the prospect of discovery in a suit claiming breach of fiduciary duty is ominous, potentially exposing the ERISA fiduciary to probing and costly inquiries and document requests about its methods and knowledge at the relevant times." *PBGC v. Morgan Stanley*, 712 F.3d 705, 719 (2d Cir. 2013). Needless to say, allowing meritless claims to survive for years of discovery and pre-trial proceedings would not advance the purposes of ERISA.

The bottom line is that a fiduciary of an ESOP plan investing in the company's stock is an utterly predictable and congressionally sanctioned occurrence. Before that act can be the basis for a federal lawsuit, plaintiffs should have to allege far more than a price-drop and "mismanagement." Indeed, in the absence of specific allegations that the share price was overvalued and the fiduciaries knew of that overvaluation, there is no plausible basis for the fiduciaries to do anything other than continue to purchase equity for employees. Without such allegations, fiduciaries should not have to endure the burdens of a trial as in *DiFelice*. Rather, courts need the tools to dismiss such actions at the threshold.

CONCLUSION

For the reasons articulated by the Petitioners, this Court should reverse the judgment of the Sixth Circuit and hold that claims against an ESOP fiduciary arising out of investments in employer stock are governed, at all stages of the proceedings, by a deferential abuse-of-discretion standard. At a minimum, however, the Court should hold that defendants are entitled to deferential review when there are no allegations that the price of the company's stock was artificially inflated or overvalued. Congress has made a reasoned policy decision that employee ownership of employer stock is "a goal in and of itself," *Moench*, 62 F.3d at 568, and fiduciaries who act in furtherance of that goal should not be forced to reckon with years of litigation based on specious claims that they should have outsmarted the market.

Respectfully submitted,

PAUL D. CLEMENT
Counsel of Record
JEFFREY M. HARRIS
BARBARA A. SMITH
BANCROFT PLLC
1919 M Street NW
Suite 470
Washington, DC 20036
(202) 234-0090
pclement@bancroftpllc.com

Counsel for Amicus Curiae

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