24-3141(L), 24-3271(XAP)

United States Court of Appeals for the Second Circuit

MATTHEW T. SHAFER, individually and on behalf of all others similarly situated, MACE TAMSE, STEVE SHERESKY, GEORGE LIVANOS, JEFFREY SHOVER, MARK LOFTUS, SANDY JUKEL, STEVE NADLER, SHERI HAUGABOOK, JEFFREY SHERESKY, PETER HEIDT, JEFFREY SAMSEN,

Plaintiffs-Appellees-Cross-Appellants,

v.

MORGAN STANLEY, MORGAN STANLEY SMITH BARNEY LLC, MORGAN STANLEY COMPENSATION MANAGEMENT DEVELOPMENT AND SUCCESSION COMMITTEE,

Defendants-Appellants-Cross-Appellees,

JOHN/JANE DOES, 1-20,

Defendant.

On Appeal from the United States District Court for the Southern District of New York, Case No. 20-cv-11047 (Hon. Paul G. Gardephe)

BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AND THE ERISA INDUSTRY COMMITTEE AS *AMICI CURIAE* IN SUPPORT OF DEFENDANTS APPELLANTS-CROSS-APPELLEES

ANDREW J. PINCUS
ARCHIS A. PARASHARAMI
DANIEL E. JONES
Mayer Brown LLP
1999 K Street NW
Washington, DC 20006
(202) 263-3000

Counsel for Amici Curiae

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The ERISA Industry Committee states that it is a non-profit, tax-exempt organization incorporated in the District of Columbia. ERIC has no parent corporation and no publicly held company has 10% or greater ownership.

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INTEREST OF *AMICI CURIAE*[1]

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

The ERISA Industry Committee (ERIC) is a national non-profit business trade association representing approximately 100 of the nation's largest employers in their capacity as sponsors of employee benefit plans for their workers, retirees, and families. ERIC routinely

[1] No counsel for a party authored this brief in whole or in part, and no person or entity, aside from *amici curiae*, their members, or their counsel, made any monetary contribution intended to fund the preparation or submission of this brief. *See* Fed. R. App. P. 29(a)(4)(E). All parties have consented to the filing of this brief.

participates as *amicus curiae* in cases implicating the scope and content of the regulation of employee benefits.

Amici's members include many employers that, in addition to maintaining retirement plans, offer a variety of deferred incentive compensation or long-term incentive arrangements to their employees. These arrangements play a vital role—both in the financial services industry and beyond—in efforts to retain valuable employees, reward their loyalty, and discourage misconduct. The orders below threaten the continued utility of these arrangements.

The district court never should have addressed whether Morgan Stanley's deferred compensation awards are employee pension benefit plans governed by the Employee Retirement Income Security Act of 1974 (ERISA): that merits question was for arbitrators to resolve. That is reason enough to vacate the orders below. But if this Court reaches the substantive ERISA issue, *amici* have a strong interest in this Court's rejection of the district court's improper extension of ERISA to deferred compensation arrangements like the ones in this case. Allowing the district court's interpretation to stand would harm employers and employees alike by threatening to eliminate or curtail these beneficial compensation arrangements.

INTRODUCTION AND SUMMARY OF ARGUMENT

The principal underlying merits issue in this case is whether the deferred compensation award programs offered by Morgan Stanley are "employee benefit pension plans" (pension plans) under ERISA. In the course of compelling arbitration, the district court determined that they are. For all of the reasons explained by Morgan Stanley, the district court should never have reached the ERISA-coverage issue, which the parties agreed to resolve in arbitration. This Court should accordingly vacate the orders below and allow the arbitrators to decide the issue in the first instance.

If this Court reaches the parties' dispute over whether Morgan Stanley's programs are ERISA pension plans, *amici* write separately to explain why the district court's interpretation of the statute is both incorrect and detrimental to employers and employees alike.

The court below extended ERISA's reach far beyond what the statute and its implementing regulations allow. Both the express terms and the surrounding circumstances of Morgan Stanley's deferred compensation arrangements (which are similar to incentive award arrangements used across employers) demonstrate that they are not pension plans, but rather reward current employees for their continued service and good conduct. The text of the statute, the Department of Labor's regulatory exemption for "bonus" incentive programs, and the overwhelming consensus among judicial and Department of Labor decisions all point to the same result: the arrangements are not ERISA pension plans.

Broader workplace dynamics—both in and beyond the securities and financial services industries—further confirm that arrangements like Morgan Stanley's are not ERISA plans. Deferred incentive compensation and long-term incentive programs are in widespread use, and employers offer them for a variety of reasons that have nothing to do with providing income after retirement. Those programs play a critical role in promoting retention of productive employees, rewarding good conduct, and deterring or penalizing misconduct.

The district court's interpretation of ERISA, if upheld, would harm employers and employees alike. It would encourage a wave of litigation in which the ERISA plaintiffs' bar seizes on ERISA's strict vesting and anti-forfeiture rules to expose employers to potentially astronomical liability for legitimate cancellations of incentive awards that have not vested. *See* 29 U.S.C. § 1053; 29 C.F.R. § 2530. It would undermine employers' justifiable reliance on nearly fifty years of case law and regulatory guidance and deprive employers of their ability to offer attractive and flexible compensation programs. It also would pressure some employers into eliminating their deferred incentive compensation programs altogether, stripping them of a valuable tool in their efforts to retain talented employees and depriving employees of a beneficial compensation arrangement.

ARGUMENT

The District Court's Erroneous Expansion Of ERISA's Coverage Threatens Adverse Consequences For Both Employers And Employees.

A. The Deferred Compensation Arrangements In This Case Are Not ERISA Pension Plans.

Congress passed ERISA in 1974 to "promote the interest of employees and their beneficiaries in employee benefit plans." *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 90 (1983). Congress defined the term "employee benefit plan" to include "both *pension* plans and welfare plans." *Id.* at 90-91 (emphasis added). Welfare plans (such as plans providing health or disability benefits) are not at issue here. And a pension plan, as the term suggests, refers to a program that provides for retirement or other *post*-employment income, not a program designed to compensate current employees.

That is clear from the statutory text. To qualify as an "employee benefit pension plan" under ERISA, a program must, "by its express terms or as a result of surrounding circumstances," either "(i) provide[] retirement income to employees" or "(ii) result[] in a deferral of income by employees for periods extending to the *termination* of covered employment *or beyond*." 29 U.S.C. § 1002(2)(A) (emphasis added). The Department of Labor has by regulation further exempted from ERISA's coverage a program providing "payments made by an employer to some or all of its employees as bonuses for work performed, unless such payments are *systematically* deferred to the termination of covered employment or beyond." 29 C.F.R. § 2510.3-2(c) (emphasis added).

As Morgan Stanley's brief explains, its deferred compensation arrangements do not meet the statutory definition of a "pension plan" and are independently exempt from ERISA's coverage under the DOL's definition of a "bonus" plan. Opening Br. 38-58. The district court's contrary determinations also conflict with the overwhelming weight of case law and DOL guidance concluding that arrangements that share many features with Morgan Stanley's are not covered by ERISA.

Numerous characteristics of Morgan Stanley's deferred compensation arrangements confirm that they fall outside ERISA's scope. Among other things, Morgan Stanley's deferred cash or stock awards are:

- Unvested—i.e., unearned—unless and until an advisor stays at Morgan Stanley in good standing for the specified vesting period;
- Automatically distributed directly to the advisor once vested, and are not eligible to be deferred by either the advisor or Morgan Stanley;
- As a result, distributed to current employees except when one of the narrow enumerated exceptions to the vesting rules applies, which may result in payment being made to a former employee;
- Overwhelmingly distributed to current employees (in fact between 85-92% of the time);

- Expressly described in the program terms as a "reward" for "your continued Employment and service to the Firm in the future and your compliance with the Firm's policies (including the Code of Conduct)" and *not* "as a source of retirement income"; and
- Taxed as ordinary bonus income, not retirement income.

Opening Br. 7-11, 57-58.

The district court acknowledged that these awards do not provide retirement income. SPA30. Instead, the district court seized on the exceptions permitting distribution of an award to former advisors who leave Morgan Stanley before the vesting period ends due to death, disability, not-for-cause layoff, ordinary course retirement, or transition to government service. According to the district court, those exceptions mean that payments "sometimes occur at the end of employment or beyond" and therefore bring the programs within the scope of 29 U.S.C. § 1002(2)(A)(ii). SPA37-39.

That outlier result departs from an otherwise uniform consensus among courts and the Department of Labor that "incidental" payments to former employees under plans generally designed to compensate current employees are insufficient to trigger ERISA's coverage. *Oatway v. Am. Int'l Grp., Inc.*, 325 F.3d 184, 189 (3d Cir. 2003) (following *Murphy v. Inexco Oil Co.*, 611 F.2d 570 (5th Cir. 1980) and "the unbroken line of cases that have followed *Murphy*'s reasoning"); *Murphy*, 611 F.2d at 574-75; DOL Advisory Op. 98-02A, 1998 WL 103654, at *1-2; *see also* Opening Br. 41-42 (collecting additional cases and DOL opinions).[2]

That consensus is for good reason: this Court and others have admonished that ERISA's definition of "pension plan" is "not to be read as an elastic girdle that can be stretched to cover any content that can conceivably fit within its reach." *Pasternack v. Shrader*, 863 F.3d 162,

[2] The district court relied on *Tolbert v. RBC Cap. Mkts. Corp.*, 758 F.3d 619 (5th Cir. 2014), but *Tolbert* is readily distinguishable. Unlike the programs here, under which awards automatically distribute when vested and cannot be deferred by employees, the plan in *Tolbert* expressly allowed employees to voluntarily defer their earned compensation awards *until the end of their employment*. *Id.* at 622, 625-26. That characteristic made termination or post-termination payments entirely within the control of the employee rather than incidental, and placed the plan squarely within the statutory definition for plans that "result[] in a deferral of income *by employees* for periods extending to the termination of covered employment or beyond." 29 U.S.C. § 1002(2)(A)(ii) (emphasis added). If anything, *Tolbert* further supports the consensus view in favor of Morgan Stanley's position, reaffirming the Fifth Circuit's earlier decision in *Murphy* and explaining that the "'mere fact' of post-termination payments" is not enough to transform a deferred compensation program into an ERISA pension plan. 758 F.3d at 625 (quoting *Murphy*, 611 F.2d at 575).

168 (2d Cir. 2017) (quoting *Murphy*, 611 F.2d at 574-75). Like many forms of long-term incentive or deferred compensation programs, the awards here are designed to, and do, provide additional compensation to current employees to reward them for continued service and good conduct. That is a far cry from a program aimed at providing retirement or post-termination income; and it explains why these plans cannot be shoehorned into the category of an ERISA pension plan.

Finally, the district court also erred by determining that the DOL's exemption for bonuses does not apply. Other courts of appeals analyzing the regulation, and the DOL, have uniformly taken the view that an "incentive plan designed to provide a financial incentive for employees to remain" with their employer "and improve their performance there" falls within ERISA's exemption for bonus plans. *Oatway*, 325 F.3d at 186-89; *see also*, *e.g.*, *Emmenegger v. Bull Moose Tube Co.*, 197 F.3d 929, 931-34 (8th Cir. 1999); *McKinsey v. Sentry Ins.*, 986 F.2d 401, 406 (10th Cir. 1993); Opening Br. 51-52 (collecting additional cases and DOL opinions).

That is exactly the purpose of the awards here, both under the express terms of Morgan Stanley's programs and in practice. The district court took the view that the awards cannot be bonuses because they are calculated based on past revenue generated by the advisor. SPA37. But that approach ignores the reality that bonuses are frequently tied to past revenue generation, as courts and the DOL have repeatedly recognized. Opening Br. 51-52.

In sum, the awards here are ERISA-exempt bonuses. That should end the inquiry, because there is no reasonable dispute that the payments are not "systematically deferred to the termination of covered employment or beyond." 29 C.F.R. § 2510.3-2(c). The DOL has made clear that the "systemically deferred" standard is a high one, under which an "inordinate percentage" of payments under the program must be made after employment and the economic benefits of the program allocated "disproportionately to retirees." DOL Advisory Op. 98-02A, 1998 WL 103654, at *2; *accord* DOL Advisory Op. 2002-13A, 2002 WL 31846478, at *3 n.3. The incidental payments to former advisors here come nowhere close to meeting that stringent regulatory standard.

B. Employers Routinely Use Deferred Incentive Compensation Arrangements Like Those In This Case To Encourage Employee Retention And Reward Loyalty, Not To Provide Retirement Benefits.

Broader workplace dynamics, both in the securities and financial services industries and beyond, confirm that employers offer arrangements like Morgan Stanley's to retain and reward current employees, not to provide retirement or post-termination income.

Employers face significant challenges in retaining productive employees. Those challenges have been particularly acute during the past few years, with workers voluntarily leaving their jobs at historically high rates—a phenomenon known as the "Great Resignation." *See*, *e.g.*, Vincent Amanor-Boadu, *Empirical evidence for the "Great Resignation"*, Monthly Labor Review, U.S. Bureau of Labor Statistics (Nov. 2022), https://www.bls.gov/opub/mlr/2022/article/empirical-evidence-for-the-great-resignation.htm; Eduardo Rivera Greenwood, *Workers are leaving. What can you do about it?*, Deloitte (Oct. 5, 2022), https://action.deloitte.com/insight/2737/workers-are-leaving.-what-can-you-do-about-it.

Professional and business services firm resignations spiked during the Great Resignation. Bureau of Labor Statistics data show that approximately 3.4 million workers in that industry quit their jobs in just the five months between May and September of 2021—representing 17% of the 20 million Americans who resigned during that time period. *See* Sam Cook, *The Professional Services Industry Is Leading The Office Worker Revolt*, MentorcliQ (Dec. 1, 2021), https://www.mentorcliq.com/

blog/the-professional-services-industry-is-leading-the-office-worker-revolt-2.

This turnover is tremendously costly to businesses. Generally, a "conservative estimate" of the cost to replace a departing worker is "one-half to two times the employee's annual salary." Shane McFeely & Ben Wigert, *This Fixable Problem Costs U.S. Businesses $1 Trillion*, Gallup (Mar. 13, 2019), https://www.gallup.com/workplace/247391/fixable-problem-costs-businesses-trillion.aspx. These costs can be even greater for client-focused professional services firms, where financial advisors and similar workers maintain and cultivate client relationships, and those clients may follow their advisors to a new firm. *See*, *e.g.*, *Merrill Lynch, Pierce, Fermer &. Smith, Inc. v. Brennan*, 2007 WL 632904, at *2 (N.D. Ohio Feb. 23, 2007) (noting the "fluid nature" of the financial services industry, where "brokers routinely switch firms and take their client lists with them").

Indeed, the employees who are most successful at developing extensive client networks are often the target of competition among firms, with firms offering "eye-popping bonuses to woo talent." Mason Braswell, *Recruiting Bonuses for Top Producers Flirt with 400%, Hitting*

Fresh Highs, AdvisorHub (Sept. 21, 2022), https://www.advisorhub.com/recruiting-bonuses-for-top-producers-flirt-with-400-hitting-fresh-highs/ (reporting that signing bonuses for brokers can reach up to four times the broker's prior 12-month revenue).

To address this problem, employers have adopted a variety of deferred incentive compensation arrangements designed to promote employee loyalty and longevity. *See*, *e.g.*, Andreas Stuermann, *Employers, Are You Ready For The Great Resignation? Actionable Ideas To Recruit, Retain, And Reward Key Talent*, Stuermann Consulting (Feb. 2022), https://www.stuermannconsulting.com/wp-content/uploads/2022/02/SCIgreatresignationblogfinal.pdf. Among the most common and effective features of such arrangements is the use of mandatory vesting periods—like those in Morgan Stanley's programs—requiring employees to remain at the firm for a certain period of time in good standing prior to receiving an award of additional cash or equity. *See generally* J.P. Morgan, *A Quick Guide to Long Term Incentive Plans (LTIPs)* (Mar. 13, 2024), https://www.globalshares.com/insights/long-term-incentive-plan-design-what-you-need-to-know/; *Long-term incentive plans: A* *comprehensive guide for HR*, Rippling (Dec. 12, 2024), https://www.rippling.com/blog/long-term-incentive-plan.

Employers across a variety of industries use these arrangements "to further enhance retention." Pearl Meyer, *Looking Ahead to Executive Pay Practices in 2024*, at 7, https://pearlmeyer.com/sites/default/files/knowledge-share/research-report/looking-ahead-to-executive-pay-practices-in-2024-executive-summary.pdf (reporting that nearly 20% of responding employers that offer long-term incentive arrangements increased participation levels in those arrangements in 2023). And employers are increasingly starting to offer long-term incentive awards to employees below the executive level. *See*, *e.g.*, J.P. Morgan, *supra* (53% of publicly traded companies reported granting long-term incentives to employees below the vice president level) (citing Pearl Meyer, *supra*); *see also* Bartek Podolski, *Ask an Advisor: What is a long-term incentive plan and how can it help us?*, EBN (July 15, 2022), https://www.benefitnews.com/advisers/news/can-long-term-incentive-plans-help-employersattract-talent (similarly noting that "[m]any companies are starting to offer [LTIPs] to employees below the executive level").[3]

Finally, deferred incentive compensation arrangements not only reward loyalty and good conduct, but also discourage misconduct by providing real consequences in the form of cancelled incentive awards. Indeed, financial regulators have exercised their statutory mandate under Section 956 of the Dodd-Frank Act to direct regulated firms to use multi-year vesting periods and subject incentive awards to cancellation to deter and penalize excessive risk-taking and other harmful behaviors. *See* 12 U.S.C. § 5641 (requiring federal regulators to "prescribe regulations or guidelines" prohibiting incentive-based payment arrangements "that the regulators determine encourage[] inappropriate risks by covered financial institutions"); Opening Br. 9-10 & n.5

[3] Because employers are increasingly offering deferred compensation arrangements to employees other than executives and senior management, ERISA's separate exclusion of "top hat" plans from the fiduciary duties imposed by ERISA, 29 U.S.C. § 1101(a)(1), is no solution to the district court's overbroad reading of the statute. Top hat plans must be maintained "primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees" (*id.*), rather than a broader set of the employer's workforce.

(discussing directives from FINRA, the SEC, and other financial regulators).

C. Adopting The District Court's Overbroad Reading Of ERISA Would Harm Employers And Employees Alike.

Upholding the district court's outlier interpretation of ERISA's reach would harm employers and employees.

To begin with, the district court's construction would encourage a wave of litigation threatening employers in a variety of sectors who use deferred compensation with potentially enormous liability for past cancellation of unvested deferred compensation. It is no secret that the ERISA plaintiffs' bar is dominated by a small number of specialized firms that sometimes target businesses with theories of liability that challenge well-established legal understandings and seek to push the boundaries of liability under the statute.[4]

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[4] For example, since the fall of 2023 the ERISA plaintiffs' bar has filed a wave of lawsuits asserting the "novel theory" that employers are violating ERISA when they use 401(k) plan forfeitures—employer contributions that participants forfeit when they leave the plan before those contributions vest—to offset future employer contributions. Deborah S. Davidson et al., *A Chubb Special Report: A Primer on 401(k) Forfeiture Litigation*, Chubb (Oct. 2024). So far, "courts' reactions to plaintiffs' theories have been mixed," with some courts granting motions to dismiss and others allowing the claims to proceed past the pleadings stage. *Id.*

This case embodies that trend: Recognizing that ERISA's strict vesting and anti-forfeiture rules, if they apply, could require employers to pay unearned or cancelled deferred compensation, the ERISA plaintiffs' bar is trying to push for the expansion of the statute beyond bona fide retirement plans to reach deferred incentive compensation and long-term incentive arrangements that have long been understood not to be covered by ERISA.

Indeed, the plaintiffs' firms leading the series of cases and arbitrations against Morgan Stanley (*see* Opening Br. 20-21) have also advanced a similar theory in a suit against Merrill Lynch. *See*, *e.g.*, *Milligan v. Merrill Lynch*, No. 24-cv-440 (W.D.N.C. filed Apr. 30, 2024).

And if their theory succeeds, these plaintiffs' firms will have no reason to stop with the financial services industry. It is not difficult for a single firm or set of firms to bring dozens of cookie-cutter lawsuits—that is already par for the course in ERISA litigation. An attorney need only identify a theory that applies to a large number of employers before blanketing the country with a series of similar complaints to see which ones gain traction. *See* note 4, *supra*.

Defending lawsuits designed to extract lucrative settlements from commonplace and useful compensation arrangements would force employers to expend enormous resources. As this Court has recognized, the prospect of "asymmetric" discovery for defendants in ERISA actions comes at an "ominous" price, entailing "probing and costly inquiries." *PBGC ex rel. St. Vincent Catholic Med. Ctrs. Ret. Plan v. Morgan Stanley Inv. Mgmt., Inc.*, 712 F.3d 705, 719 (2d Cir. 2013). But the harmful consequences of this increase in costs would not be limited to employers. Market forces will pass the uptick in litigation costs to customers in the form of higher prices or less attractive service offerings, and to employees in the form of reduced compensation.

Relatedly, if this Court were to uphold the district court's departure from nearly fifty years of case law and regulatory guidance on the meaning of an ERISA pension plan, that change in the law would undermine employers' settled expectations and introduce substantial uncertainty. Consistent application of the statutory text and regulatory exemptions is critical to give employers clear guidance about what legal regimes apply to their compensation arrangements and to allow them to structure their arrangements accordingly.

That uncertainty, and the prospect of burdensome and costly ERISA litigation, may cause employers to stop offering deferred incentive compensation arrangements altogether. That would injure employers because they would lose a valuable tool for retaining employees and discouraging misconduct. And it would harm employees who would otherwise reap the rewards for their long-term contributions to their employer.

In the securities and financial services context in particular, firms must satisfy the expectations of financial regulators that firms will use cancellable deferred compensation subject to multi-year vesting periods as a tool for policing misconduct. But adopting such plans would run headlong into ERISA's requirements—if, as the district court mistakenly held, ERISA applied to deferred compensation arrangements like Morgan Stanley's.

At minimum, employers in all industries would be forced to offer deferred incentive compensation on much less attractive and flexible terms. For example, to avoid even incidentally paying awards to former employees, employers would be forced to jettison humanitarian and common-sense exceptions and impose a strict rule cancelling all deferred incentive compensation awards the moment an employee no longer works for the employer, even due to death, disability, or layoff. That harsh and inequitable result is not what ERISA's text requires.

CONCLUSION

The Court should vacate the orders below, and, if it reaches the ERISA-coverage issue, reverse the district court's determination on that issue.

Dated: January 29, 2025

Respectfully submitted,

/s/ Andrew J. Pincus
ANDREW J. PINCUS
ARCHIS A. PARASHARAMI
DANIEL E. JONES
Mayer Brown LLP
1999 K Street NW
Washington, DC 20006
(202) 263-3000

Counsel for Amici Curiae

CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitation of Cir. R. 29.1(c) because it contains 3,686 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(f).

This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type-style requirement of Fed. R. App. P. 32(a)(6) because it was prepared in a proportionately spaced typeface using Microsoft Word in Century Schoolbook 14-point type for text and footnotes.

Dated: January 29, 2025

/s/ Andrew J. Pincus
Andrew J. Pincus