No. 17-1711

UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

JOHN BROTHERSTON and JOAN GLANCY, individually and as representatives of a class of similarly situated persons, and on behalf of the Putnam Retirement Plan,

Plaintiffs-Appellants,

v.

PUTNAM INVESTMENTS, LLC; PUTNAM INVESTMENT MANAGEMENT LLC; PUTNAM INVESTOR SERVICES, INC.; THE PUTNAM BENEFITS INVESTMENT COMMITTEE; THE PUTNAM BENEFITS OVERSIGHT COMMITTEE; and ROBERT REYNOLDS,

Defendants-Appellees.

On Appeal from the United States District Court
for the District of Massachusetts (No. 15-13825) (Hon. William G. Young)

BRIEF FOR THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA, AMERICAN BENEFITS COUNCIL, AND SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION AS *AMICI CURIAE* IN SUPPORT OF DEFENDANTS-APPELLEES AND AFFIRMANCE

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 26.1 of the Federal Rules of Appellate Procedure, counsel for *Amici Curiae* certifies as follows:

- The Chamber of Commerce of the United States of America has no parent corporation, and no company holds 10 percent or more of its stock.
- The Securities Industry and Financial Markets Association has no parent corporation, and no company holds 10 percent or more of its stock.
- The American Benefits Council has no parent corporation, and no company holds 10 percent or more of its stock.

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INTEREST OF THE AMICI CURIAE

The **Chamber of Commerce of the United States of America** (Chamber) is the world's largest business federation.[1] It represents 300,000 direct members and indirectly represents the interests of more than three million businesses and professional organizations of every size, in every industry sector, and from every region of the country. The Chamber's members include many employers that offer ERISA-governed benefit plans to their employees, as well as insurers who fund and/or administer such plans.

The **American Benefits Council** (Council) is a national non-profit organization dedicated to protecting and fostering privately sponsored employee-benefit plans. Its approximately 435 members are primarily large, multistate employers that provide employee benefits to active and retired workers and their families. The Council's membership also includes organizations that provide employee-benefit services to employers of all sizes. Collectively, the Council's members either directly sponsor or provide services to retirement and health plans covering virtually all Americans who participate in employer-sponsored benefit programs.

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[1] All parties have consented to the filing of this brief. No counsel for a party authored this brief in whole or in part. No party, no counsel for a party, and no person other than *Amici*, their members, and their counsel made a monetary contribution intended to fund the preparation or submission of this brief.

The **Securities Industry and Financial Markets Association** (SIFMA) is the voice of the U.S. securities industry, representing the interests of securities firms, banks, and asset managers across the United States. SIFMA members not only sponsor 401(k) plans for their own employees, they also regularly provide administrative, investment advisory, and other services to retirement plans. SIFMA members also manage more than $67 trillion in assets for individual and institutional clients, including mutual funds and retirement plans.

Each organization has a strong interest in ERISA litigation and regularly participates as *amicus curiae* in this Court and in other courts on issues that affect employee benefit plan design or administration, including *Fifth Third Bancorp v. Dudenhoeffer*, 134 S. Ct. 2459 (2014), and *Ellis v. Fidelity Management Trust Co.*, No. 17-1693 (1st Cir.).

Amici's members are among the plan sponsors, fiduciaries, and service providers that benefit from Congress's decision to create, through ERISA, an employee-benefit system that is not "so complex that administrative costs, or litigation expenses," unduly burden plan sponsors. *Conkright v. Frommert*, 559 U.S. 506, 517 (2010) (quotation marks omitted). A key element of that carefully balanced system is the provision in 29 U.S.C. § 1109(a) making a fiduciary liable for losses to an ERISA plan *only* to the extent those losses "result[ed] from" the fiduciary's own "breach" of duty—*i.e.*, that the fiduciary made an "objectively

imprudent" decision. *In re Unisys Sav. Plan Litig.*, 74 F.3d 420, 436 (3d Cir. 1996) (citation omitted). Plaintiffs' proffered standard for satisfying this element, which shifts the burden of proof to an ERISA defendant and permits an ERISA plaintiff to simply *assume* the objective imprudence of a plan's entire investment portfolio after a procedural breach, allows plaintiffs to recover millions in damages even for "objectively prudent" decisions—decisions that a prudent and unconflicted fiduciary could have made. That is just the type of rule that "would impose high insurance costs upon persons who regularly deal with and offer advice to ERISA plans, and hence upon ERISA plans themselves." *Mertens v. Hewitt Assocs.*, 508 U.S. 248, 262 (1993). Plan sponsors and plan fiduciaries alike, including *Amici*'s members that administer, insure, and provide services to ERISA plans, have a strong interest in averting such a result.

SUMMARY OF ARGUMENT

ERISA makes fiduciaries liable *only* for losses that actually "result[ed] from" a breach of fiduciary duty. 29 U.S.C. § 1109(a). That requirement—known as "loss causation"—is the crucial element that prevents a windfall recovery by participants beyond the benefits promised under a plan. It also protects fiduciaries from being forced to insure the plan against anything that might go wrong following a lapse in process, without regard to whether the lapse actually caused a

loss. Congress adopted the loss causation requirement because, as in court, some errors are harmless.

Plaintiffs have argued that whenever a fiduciary errs in the way it selects the investment options the plan makes available to plan participants, an ERISA plaintiff is not required to demonstrate that the funds the fiduciary selected were bad funds. Even though loss causation is an element of an ERISA claim for breach of fiduciary duty, Plaintiffs here argue that they need only show a "prima facie case of loss" (a term they never define) and that the burden of persuasion must then shift to the fiduciary to *dis*prove loss causation.

The majority of circuits disagree and follow the "ordinary default rule" that the Supreme Court has applied to statutory claims for decades: unless the statute says otherwise, the "burden of persuasion lies where it usually falls, upon the party seeking relief." *Schaffer v. Weast*, 546 U.S. 49, 56, 58 (2005). Plaintiffs have provided no reason for this Court to depart from the Supreme Court's direction when interpreting ERISA.

Furthermore, even if Plaintiffs' "prima facie case of loss" rule were correct, their proffered standard for meeting that requirement is untenable. Plaintiffs argue that rather than demonstrate that any of the funds chosen by the fiduciary actually suffered from performance or other issues, an ERISA plaintiff should instead be able to simply *assume* that the entire portfolio was filled with bad investments and

demonstrate loss based on the difference in returns between the funds selected and an "alternative portfolio" of investments whose returns they prefer. Of course, because this "alternative portfolio" is one that the plaintiff would cherry-pick with the benefit of 20/20 hindsight, it inevitably would consist of alternatives with better returns during the selected time period—even if the alternatives bear little to no resemblance to the funds that were actually offered to plan participants or that the fiduciary would have chosen. This standard would write the loss causation requirement right out of the statute. There are nearly 10,000 mutual funds available on the market today, and many more other investment vehicles, such as separate accounts or the collective investment trusts that Plaintiffs include in their "alternative portfolio." There will always be innumerable combinations of investment options that *could have* reasonably been offered to plan participants. But saying, with the benefit of hindsight, that the funds the fiduciary selected *produced lower returns* than a hypothetical "alternative portfolio," as Plaintiffs do here, does not mean that the funds that the fiduciary selected *were imprudent funds* and caused harm to the plan.

Plaintiffs' proposed rule would make a fiduciary a guarantor of optimal 401(k) performance any time there is any sort of perceived shortcoming in a fiduciary's investment-selection process. Such a consequence would expose plan fiduciaries to such undue "administrative costs, or litigation expenses" that it

would "discourage employers from offering [ERISA] plans in the first place." *Conkright v. Frommert*, 559 U.S. 506, 517 (2010) (alteration in original) (quotation marks omitted). That is precisely what Congress sought to avoid when it enacted ERISA. *Id*.

The Court should affirm the judgment below and hold that Plaintiffs failed to meet their loss-causation burden.

ARGUMENT

I. The Burden Of Proof Never Shifts To An ERISA Defendant To *Dis*prove Loss Causation.

Plaintiffs spend a significant portion of their brief advocating for a loss-causation standard that would shift the burden to ERISA defendants to *dis*prove loss causation—an essential element of an ERISA damages claim. Defendants are correct that even under a burden-shifting scheme Plaintiffs have failed to demonstrate a prima face case of loss (Putnam Br. 21-49), but this Court should *not* apply a burden-shifting standard under ERISA.

A. Under The Well-Established Default Rule Governing The Burden Of Proof For Federal Statutory Claims, ERISA Plaintiffs Must Prove Loss Causation.

Plaintiffs contend (at 57) that the common law of trusts employed a burden-shifting scheme regarding loss causation; they argue that since ERISA is silent about which party bears the burden of proof on this element, "there is no reason to deviate from the common-law standard." But Plaintiffs have the inquiry exactly

backward: under well-established Supreme Court precedent, where Congress is silent about the burden of proof on an element of a statutory claim, the "default rule" is that "the burden of persuasion lies where it usually falls, upon the party seeking relief." *Schaffer*, 546 U.S. at 56, 58. To be sure, this default rule has exceptions, but those exceptions "are extremely rare" and generally well-established. *Id.* at 57. "For example, the burden of persuasion as to certain elements of a plaintiff's claim may be shifted to defendants, when such elements can fairly be characterized as affirmative defenses or exemptions," *id.* at 57—like ERISA's statute of limitations or repose, 29 U.S.C. § 1113, or its exemptions to ERISA's prohibited-transaction provisions, *e.g.*, 29 U.S.C. § 1108. Similarly, this Court has recognized an exception to the default rule in some circumstances where the facts that must be proved are "peculiarly within the knowledge of [the plaintiff's] adversary." *Hernandez-Miranda v. Empresas Diaz Masso, Inc.*, 651 F.3d 167, 176 (1st Cir. 2011) (citation omitted) (employers are in the "best position to establish how many employees they have at a given time"). None of these exceptions applies here. Plaintiffs do not dispute that loss causation is an element of an ERISA claim rather than an exemption or affirmative defense, as the district court noted (ADD-60),[2] and the proof that a fiduciary's investment decision was

[2] *See Silverman v. Mut. Benefit Life Ins. Co.*, 138 F.3d 98, 105 (2d Cir. 1998) (two-judge concurrence) ("Causation of damages is therefore an element of the claim . . . ."); *DeBruyne v. Equitable Life Assurance Soc'y of U.S.*, 920 F.2d 457, 467

objectively imprudent is not information that is within ERISA defendants' internal records. *Id.* Thus, it is not Defendants who must provide a "reason to deviate from the common-law standard," Pls.' Br. 57; rather, Plaintiffs must demonstrate "some reason to believe that Congress intended" to deviate from the longstanding burden-of-persuasion default rule, *Schaffer*, 564 U.S. at 57.

Plaintiffs, making no mention of *Schaffer* and instead citing *Smith v. United States*, 568 U.S. 106 (2013), argue that this Court should presume that Congress silently adopted a burden-shifting rule from the common law of trusts. Pls.' Br. 57-58. But *Smith* was a criminal case, and the relevant issue was who bore the burden of proving (or disproving) *an affirmative defense* to criminal liability, consistent with the Due Process Clause's limits on burden-shifting in criminal statutes. At common law the burden of proving affirmative defenses was on the criminal defendant, and the Court presumed that Congress allocated it the same way. *Smith*, 568 U.S. at 112. That says nothing about the burden of persuasion as to a key statutory element of a civil plaintiff's own case; as noted above, loss causation cannot be recharacterized as an affirmative defense. And when a statute is silent about the burden of persuasion *for an element of a claim*, that burden stays with "the party seeking relief." *Schaffer*, 546 U.S. at 56, 58. Nothing in *Smith* changes that rule.

(7th Cir. 1990) (causation is "another element of [a plaintiff's] claim" in securities and ERISA cases).

Plaintiffs have pointed to nothing in ERISA's text or legislative history that provides any "reason to believe that Congress intended" to place the burden on Defendants to prove loss causation, which Plaintiffs do not dispute is an element of an ERISA claim. *Schaffer*, 546 U.S. at 57. Thus, the default rule applies.

B. The Majority Of The Circuits Follow The Default Rule And Place The Loss-Causation Burden On ERISA Plaintiffs.

Consistent with the ordinary default rule, seven courts of appeals have stated that the burden of proving a fiduciary breach *and* a loss as a result of that breach rests with an ERISA plaintiff. *See, e.g.*, *Silverman v. Mut. Benefit Life Ins. Co.*, 138 F.3d 98, 105 (2d Cir. 1998) (two-judge concurrence); *Gavalik v. Cont'l Can Co.*, 812 F.2d 834, 838 (3d Cir. 1987); *Kuper v. Iovenko*, 66 F.3d 1447, 1459–60 (6th Cir. 1995), *abrogated on unrelated grounds by Fifth Third Bancorp v. Dudenhoeffer*, 134 S. Ct. 2459 (2014); *Peabody v. Davis*, 636 F.3d 368, 373 (7th Cir. 2011); *Wright v. Oregon Metallurgical Corp.*, 360 F.3d 1090, 1099 (9th Cir. 2004); *Pioneer Centres Holding Co. Emp. Stock Ownership Plan & Tr. v. Alerus Fin., N.A.*, 858 F.3d 1324, 1337 (10th Cir. 2017), *petition for cert. pending*, No. 17-667 (filed Nov. 2, 2017); *Willett v. Blue Cross & Blue Shield of Ala.*, 953 F.2d 1335, 1343–44 (11th Cir. 1992). Plaintiffs fail to acknowledge that body of caselaw in their brief.

The Tenth Circuit recently addressed this issue at length and held "that the burden falls squarely on the plaintiff" to prove loss causation. *Pioneer*, 858 F.3d at

1337. *Pioneer* involved a proposed employee stock purchase that had to be approved by a third party. *Id.* at 1327, 1332. The transaction failed because the independent trustee for the transaction failed to execute the transaction documents, and the plaintiffs sued for breach of fiduciary duty. *Id.* at 1333. But because the plaintiffs failed to demonstrate that third-party approval would have occurred even if the fiduciary had acted prudently, the district court "bypassed" the question whether the defendant had breached its fiduciary duties, as "it concluded the [plaintiffs] had not established loss." *Id.* at 1332.

On appeal, the plaintiffs argued (as Plaintiffs do here) that the district court should have shifted the burden to the defendants to disprove causation, relying on the common law of trusts. *Id.* at 1327. The Tenth Circuit "reject[ed] outright" the plaintiffs' burden-shifting argument, noting the Supreme Court's prior statement that the "law of trusts often will inform, but will not necessarily determine the outcome of, an effort to interpret ERISA's fiduciary duties." *Id.* at 1336, 1337 (quoting *Varity Corp. v. Howe*, 516 U.S. 489, 497 (1996)).

The court stated that there was "nothing in the language of § 1109(a) or in its legislative history that indicates a Congressional intent to shift the burden to the fiduciary to disprove causation." *Id.* at 1336. Thus, it saw "no reason to depart from the 'ordinary default rule that plaintiffs bear the risk of failing to prove their claims.'" *Id.* at 1337 (quoting *Schaffer*, 546 U.S. at 56); *see also id.* ("Where the

plain language of the statute limits the fiduciary's liability to losses *resulting from* a breach of fiduciary duty, there seems little reason to read the statute as requiring the plaintiff to show only that the loss is *related* to the breach."). It also observed that a "burden-shifting framework could result in removing an important check on the otherwise sweeping liability of fiduciaries under ERISA," which could discourage companies from willingly undertaking fiduciary responsibility for an ERISA plan. *Id.* (citing *Silverman*, 138 F.3d at 106 (two-judge concurrence)).

Just three circuits have articulated a different rule.[3] The Fifth Circuit has never actually analyzed whether a burden-shifting framework is appropriate. In *McDonald v. Provident Indemnity Life Insurance Co.*, 60 F.3d 234 (5th Cir. 1995), which Plaintiffs cite (at 58), the court simply recited that once an ERISA plaintiff has proven a breach of a fiduciary duty and a prima facie case of loss, the burden shifts to the fiduciary to disprove causation, and it cited an Eighth Circuit case without any discussion or analysis of the issue. *Id.* at 237 & n.14. In doing so the court ignored existing circuit precedent holding that an ERISA plaintiff "has the

[3] Plaintiffs suggest (at 58) that the Seventh Circuit has also adopted a burden-shifting rule for ERISA loss causation. Not so. *See Peabody*, 636 F.3d at 373 ("To prevail [in an action for damages] under § 502(a)(2)," which provides a private right of action for relief under 29 U.S.C. § 1109(a), "the plaintiff must show a breach of fiduciary duty, *and its causation of an injury*." (emphasis added)). The case Plaintiffs rely on, *Leigh v. Engle*, 727 F.2d 113 (7th Cir. 1984), addresses an ERISA defendant's obligation to provide *rebuttal* evidence regarding profit-based *disgorgement*, *id.* at 138-39—a form of "other equitable or remedial relief" that is distinct from "losses to the plan resulting from [a] breach." *See* 29 U.S.C. § 1109(a).

burden of proving that [the defendants] violated their co-fiduciary duties resulting in loss to the [plan]." *Sommers Drug Stores Co. Emp. Profit Sharing Tr. v. Corrigan*, 883 F.2d 345, 352 (5th Cir. 1989). Indeed, *McDonald* was not even addressing the question of causation of losses to the plan, as here. Instead, the question was whether losses that indisputably *did* result from the fiduciary decision (in the form of higher insurance premiums for participants) but that *did not* impact the plan as a whole were recoverable under ERISA. *Id.* at 237-38.[4]

The Eighth Circuit has similarly stated that burden-shifting applies without analyzing the issue. In the first case to recite the burden-shifting standard, the court stated that it "agree[d]" that "the burden of persuasion shifts to the fiduciary" to disprove loss causation. *Martin v. Feilen*, 965 F.2d 660, 671 (8th Cir. 1992). In reaching that decision, the court did not interpret (or even examine) the text of ERISA, address the longstanding default rule that applies to federal statutory claims, or explain why the common law of trusts should overcome the default rule. Instead, it simply cited a trust-law treatise and cases from the Second, Seventh, and Ninth Circuits, *id.*[5]—courts that have all subsequently *rejected* a burden-shifting

[4] The only other two Fifth Circuit decisions to recite this burden-shifting language did not involve loss causation at all; the claims failed because the Plaintiffs failed to establish any breach of fiduciary duty. *See Timmons v. Special Ins. Servs., Inc.*, 167 F.3d 537 (5th Cir. 1998) (unpublished); *Smith v. Prager*, 154 F.3d 417 (5th Cir. 1998) (unpublished).

[5] None of these cases held that an ERISA defendant has the burden to disprove loss causation to avoid liability for breach of ERISA's fiduciary duties of prudence and

loss-causation standard. *See supra* p. 9. Subsequent Eighth Circuit decisions have simply recited the burden-shifting framework, citing *Martin*, without any further discussion. *See Eckelkamp v. Beste*, 315 F.3d 863, 867 (8th Cir. 2002); *Roth v. Sawyer-Cleator Lumber Co.*, 16 F.3d 915, 917 (8th Cir. 1994).

The only court to have adopted a burden-shifting standard after examining the issue in depth (and after *Schaffer* reiterated the correct default rule) is the Fourth Circuit, which held over a vigorous dissent by Judge Wilkinson that a breaching fiduciary "bears the burden of proof on loss causation" under "long-recognized trust law." *Tatum v. RJR Pension Inv. Comm.*, 761 F.3d 346, 363 (4th Cir. 2014). The court acknowledged the ordinary default rule that applies to elements of federal statutory claims but concluded that ERISA should be an "exception" because the burden was different under the common law of trusts. *Id.* at 362. The court did not identify any indication in the text of ERISA that Congress intended to depart from the ordinary default rule. Rather, it relied on a series of reasons grounded in perceived "fairness." It repeated the district court's view that a burden-shifting rule would be "the 'most fair' approach," because the

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loyalty. *Donovan v. Bierwirth*, 754 F.2d 1049, 1056 (2d Cir. 1985), addressed a defendant's burden of rebutting a plaintiff's damages figure after the plaintiff had already proven a breach and resulting loss. *Marshall v. Snyder*, 572 F.2d 894, 900 (2d Cir. 1978), addressed the burden of proving a statutory *exemption*, not loss causation. *Leigh*, 727 F.2d at 138-139, and *Kim v. Fujikawa*, 871 F.2d 1427, 1430-31 (9th Cir. 1989), addressed a defendant's burden of rebutting the plaintiff's showing of losses that resulted from prohibited transactions.

loss-causation issue arises only once the plaintiffs have proved a breach (reasoning that would justify shifting the burden in *every* statutory loss-causation case). *Id.* at 362 (quoting *Tatum v. R.J. Reynolds Tobacco Co.*, 926 F. Supp. 2d 648, 684 (M.D.N.C. 2013)). And it concluded that a burden-shifting framework would be consistent with the "structure and purpose of ERISA," which, in its view, aims to protect the interests of plan participants; the court treated those considerations as calling for a rule that makes proof easier for plaintiffs. *Id.* at 363. The court expressed concern that a contrary rule would "create significant barriers" for ERISA plaintiffs and "provide an unfair advantage to a defendant." *Id.* (citation omitted).

As Judge Wilkinson recognized in dissent, the court's holding was inconsistent with the ordinary default rule and with prior circuit precedent, which had rejected "the novel proposition that, whenever a breach of the obligation by a trustee has been proved, the burden shifts to the trustee to establish that any loss suffered by the beneficiaries of the trust was not proximately due to the default of the trustee." *Id.* at 375 (Wilkinson, J., dissenting) (quoting *U.S. Life Ins. Co. v. Mechs. & Farmers Bank*, 685 F.2d 887, 896 (4th Cir. 1982)). He also noted that the burden-shifting framework was contrary to ERISA's remedial scheme, which permits some remedies where a fiduciary's breach does not result in losses but permits *damages* "only upon a finding of loss causation." *Id.* at 376.

No circuit court since *Tatum* has followed the Fourth Circuit's rule. This Court should not be the first. If this Court reaches this question, it should follow "[t]he weight of circuit precedent [that] supports keeping the burden of proof on the party bringing suit." *Tatum*, 761 F.3d at 375 (Wilkinson, J., dissenting).

C. Plaintiffs' Policy Considerations Do Not Defeat The Default Rule.

Plaintiffs advance a variety of purported policy and pragmatic considerations in support of their preferred burden-shifting framework, none of which warrants departure from the ordinary default rule. First, they argue (at 59) that public policy supports burden-shifting because ERISA's goal is to protect plan participants from fiduciary misconduct. But neither ERISA as a whole, nor its private civil remedy in particular, seeks single-minded alignment with plan participants. To the contrary, Congress sought to create a system that would "induc[e] employers to offer benefits," *Rush Prudential HMO, Inc. v. Moran*, 536 U.S. 355, 379 (2002), and that would not create such high "administrative costs, or litigation expenses" that it would "unduly discourage employers from offering welfare benefit plans in the first place." *Varity*, 516 U.S. at 497.

Indeed, the Supreme Court has repeatedly "recognized that ERISA represents a careful balancing between ensuring fair and prompt enforcement of rights under a plan and the encouragement of the creation of such plans." *Conkright*, 559 U.S. at 517 (quotation marks omitted); *see also, e.g.*, *Mertens*, 508

U.S. at 262 (discussing ERISA's dual goals of benefitting employees and containing pension costs); H.R. Rep. No. 93-533, at 1, 9 (1974) (expressing concerns with the cost to employers of federal standards governing benefit plans and noting Congress's "effort to strike an appropriate balance" between plan sponsors and plan participants). Courts must "take account of" those "competing congressional purposes," *Varity*, 516 U.S. at 497, and cannot bend the statutory cause of action just for the sake of favoring plaintiffs—especially not in ways that contravene the statute's text and the ordinary rules of statutory interpretation that apply to it.

A rule that penalizes employers with significant monetary damages, even if the plaintiffs cannot establish that procedural missteps actually resulted in an objectively imprudent investment selection, is precisely the type of rule that would discourage employers from offering retirement plans in the first place. Congress carefully balanced these competing interests when it crafted ERISA. If Congress wanted to depart from the ordinary default rule and place the burden on plan fiduciaries to disprove causation to escape damages liability, it could have done so expressly—just as it effectively did when it made fiduciaries liable for equitable relief irrespective of loss causation. 29 U.S.C. § 1109(a). Given Congress's failure to do so—and the lack of any indication from the statute itself or the

legislative history that it intended to depart from the ordinary default rule—Plaintiffs' "public policy" argument provides no reason to do so either.

Second, Plaintiffs argue (at 60-61) that a burden-shifting framework is necessary because loss causation is too uncertain to prove and yet likely enough to presume. In their view, fiduciary breaches will usually "result in" a loss because "it is highly unlikely that the fiduciary will happen upon a prudent Plan menu through sheer coincidence, for the same reason that a blindfolded dart player is unlikely to hit as close to the target as one who can see the board." Pls.' Br. 60. Plaintiffs make it seem as if there is only one prudent investment fund option, and that everything outside that tiny bull's-eye counts as a miss. But the reason loss causation cannot be presumed is because there are so many available investment options that are entirely consistent with the duty of prudence. A blindfold matters much less if there are acceptable targets all over the room. Put another way, a blindfolded diner may actually have an excellent chance of selecting a good meal if the diner chooses from a menu containing many high-quality options.

For instance, there are nearly 10,000 mutual funds available on the marketplace, several thousands of which are offered in retirement plans.[6] And the funds themselves have strong incentives to operate in a way that makes them prudent investment options. These funds are not only highly regulated under the

[6] Investment Company Institute, *2017 Investment Company Factbook* 19 (57th ed. 2017), *available at* https://www.ici.org/pdf/2017_factbook.pdf.

Investment Company Act of 1940, they are subject to marketplace competition made all the more intense by the legally required disclosure of information about investment returns, risks, and the like.[7] Mutual fund companies have every incentive to maintain high performance consistent with the intended risk and investment objectives of the funds. Companies like Putnam ensure that fund managers share these objectives by tying their compensation incentives to fund achievement, not assets under management. Putnam Br. 13-14 n.10.

Thus, in selecting a slate of funds to offer to plan participants, fiduciaries are not "blindfolded dart player[s]" all wildly seeking to hit a single elusive target. They have thousands of prudent options available to them. And even if Plaintiffs were correct and fiduciaries could rarely select a prudent option without a perfect decision-making process, then it would be easy for Plaintiffs to carry their burden of demonstrating that a procedural shortcoming led to an objectively imprudent investment. There is no justification for relieving Plaintiffs of that burden.

II. Even A Prima Facie Case Of Loss Cannot Be Established By Assuming The Imprudence Of An Entire Portfolio Of Funds And Comparing Its Performance To An Inapt "Alternative Portfolio" Created With The Benefit Of Hindsight.

Even if the statute did incorporate some form of burden-shifting, Plaintiffs' version of it would still be untenable. Plaintiffs contend that their initial burden is

[7] *See* SEC, *Mutual Funds and Exchange-Traded Funds (ETFs)—A Guide for Investors*, https://www.sec.gov/reportspubs/investor-publications/investorpubs inwsmfhtm.html (last updated Jan. 26, 2017).

so light and so easy to carry that the ultimate burden will *always* shift, leaving the loss-causation requirement entirely hollow. Plaintiffs contend that in a "procedural breach" case like this one, they can demonstrate a "prima facie case of loss" on a portfolio-wide basis without demonstrating that any specific fund in the plan's portfolio could not have been chosen through a prudent and unconflicted process. Pls.' Br. 52-56. In other words, they can *assume* that all the funds in the plan's portfolio were unreasonable investments and demonstrate loss based on the difference in returns between the funds selected and an "alternative portfolio" of investments whose returns they prefer with the benefit of hindsight.

Plaintiffs' standard would eliminate ERISA's loss-causation requirement. While Plaintiffs suggest that this standard is narrowly cabined to cases involving a "procedural breach," that is no limitation at all: *every* case alleging breach of the duties of prudence or loyalty by a 401(k) plan fiduciary is a procedural-breach case, because these duties "focus[] on a fiduciary's *conduct* in arriving at an investment decision, not on its *results*." *In re Unisys*, 74 F.3d at 434 (emphases added).

Moreover, the entire point of the loss-causation requirement is that *proving a breach is not enough*, because some breaches are harmless. As then-Judge Scalia put it, "I know of no case in which a trustee who has happened—through prayer, astrology or just blind luck—to make (or hold) objectively prudent investments

(*e.g.*, an investment in a highly regarded 'blue chip' stock) has been held liable for losses from those investments because of his failure to investigate and evaluate beforehand." *Fink v. Nat'l Sav. & Tr. Co.*, 772 F.2d 951, 962 (D.C. Cir. 1985) (Scalia, J., concurring in part, dissenting in part). If "a fiduciary's failure to investigate an investment decision *alone* is not sufficient to show that the [investment] was not reasonable," *Kuper*, 66 F.3d at 1459—and even a circuit that applies burden-shifting agrees that it is not, *accord Plasterers' Local Union No. 96 Pension Plan v. Pepper*, 663 F.3d 210, 218 n.9 (4th Cir. 2011)—then surely it is not enough to simply *presume* the objective unreasonableness of the investment. Even in a world of burden-shifting, therefore, the plaintiff's initial burden of showing prima facie loss must be a meaningful one. But Plaintiffs' version is substantively indistinguishable from a presumption of imprudence.

Plaintiffs' standard is particularly problematic because Plaintiffs argue that prima facie loss can be established by comparing the investment returns of the plan's line-up—consisting largely of actively managed mutual funds—to the investment returns of "alternative portfolios" consisting entirely of index funds or collective investment trusts (CITs). But the investments in these "alternative portfolios" are not analogous to the funds Plaintiffs challenge. Active funds aim "to beat the market—to get better returns by choosing investments [the fund manager] believes to be top-performing selections." Financial Industry Regulatory

Authority, *Mutual Funds*, http://www.finra.org/investors/mutual-funds (last visited Jan. 16, 2018). Sometimes active funds beat the market and sometimes they do not, but they give plan participants the opportunity to take that risk if desired.

Index funds, by contrast, are not actively managed; instead, index-fund portfolio managers simply track the performance of an established index (*e.g.*, the S&P 500) by "buy[ing] a portfolio that includes all of the stocks in that index in the same proportions as they are represented in the index." *Id.* It would be highly unlikely that a fiduciary would replace a portfolio of mostly active funds with a slate of five or six dozen index funds, all of which simply try to track the market. Indeed, other plaintiffs might allege that such an approach was imprudently *cautious*.[8]

CITs are even less analogous to the funds in the Putnam plan's line-up. CITs are not mutual funds at all. Instead, they are investment vehicles in which multiple plans pool their assets and invest them together. *See* Harry Sit, *Collective Trust vs Mutual Fund: What's the Difference*, The Finance Buff, Feb. 13, 2012,

[8] *Cf. Brown v. Am. Life Holdings, Inc.*, 190 F.3d 856, 859-60 (8th Cir. 1999) (assuming without deciding that "the fiduciary duty of prudent diversification can be breached by maintaining an investment portfolio that is *too safe and conservative*"). Two cases involving allegations of overly conservative investment approaches are currently pending before this Court. *See* Compl., *Barchock v. CVS Health Corp.*, No. 16-cv-61 (D.R.I. Feb. 11, 2016), ECF No. 1, *appeal pending*, No. 17-1515 (1st Cir.) (argued Dec. 4, 2017); Compl., *Ellis v. Fidelity Mgmt. Tr. Co.*, No. 15-cv-14128 (D. Mass. Dec. 11, 2015), ECF No. 1, *appeal pending*, No. 17-1693 (1st Cir.) (argued Jan. 9, 2018).

https://thefinancebuff.com/collective-trust-vs-mutual-fund-whats-the-difference.html. While CITs and similar pooled vehicles like separate accounts have some benefits—primarily savings in fees—they also have considerable drawbacks. Unlike mutual funds, they do not pay dividends. *Id.* Moreover, they offer less transparency and ease of valuation, *see Loomis v. Exelon Corp.*, 658 F.3d 667, 671-72 (7th Cir. 2011), less portability of funds for plan participants exiting a plan who may wish to retain their investments, *id.* at 672, and fewer regulatory safeguards than mutual funds.[9] These types of pooled investment vehicles have some value, which is why many plans (including Putnam's) offer them, but they are less familiar to participants, making it extremely unlikely that a fiduciary would replace an entire portfolio of mutual funds with nothing but pooled investment vehicles.

If ERISA plaintiffs could demonstrate a prima facie case of loss simply through a comparison of hindsight investment returns—particularly a comparison of investment options that are dissimilar from the funds challenged—then this essential element of an ERISA damages claim would be rendered toothless. Unless the fiduciary has selected the Platonic ideal of portfolios, a lineup that outperformed literally everything else on the market, the plaintiff will *always* be

[9] For example, pooled investment vehicles are exempt from various investment diversification requirements, limitations on leverage, and mandatory oversight by a primarily independent board of directors, *see* 15 U.S.C. § 80a-18(f); 26 U.S.C. § 851(b)(3); 17 C.F.R. § 270.0-1(a)(7).

able to assemble a better-performing hypothetical portfolio in hindsight. That cannot be the standard. Given the tens of thousands of mutual funds and other investment vehicles available on the market today, there will always be a virtually innumerable combination of investment options that *could have* reasonably been offered to plan participants. The fact that the challenged funds had lower returns than other funds that could have been chosen does not mean the funds the fiduciary selected were imprudent or that they caused harm to the plan.

III. Plaintiffs' Loss-Causation Standard Would Discourage Employers From Offering Retirement Plans And Incentivize Meritless Procedural Challenges To Fiduciary Investment Decisions.

By requiring loss causation, Congress gave courts a powerful tool to weed out ERISA strike suits. But Plaintiffs' loss causation standard, which essentially eliminates the element of loss causation for procedural-prudence claims, would encourage plaintiffs' attorneys to "file first and build claims later" in hopes of a windfall judgment whenever the market drops.[10] Even if the market is thriving, plaintiffs' attorneys will be incentivized to rush to court so long as they can identify an "alternative portfolio" that had better investment returns, with 20/20

[10] The requirement of having to plausibly *plead* procedural imprudence to make it into discovery has not been an adequate deterrent. Courts commonly (though incorrectly) allow breach-of-fiduciary-duty claims to proceed into discovery where plaintiffs allege no facts about a fiduciary's decision-making process whatsoever, based solely on circumstantial allegations such as allegations of fund underperformance or the existence of alternative investment options with lower fees. *See, e.g.*, *Braden v. Wal-Mart Stores, Inc.*, 588 F.3d 585, 596 (8th Cir. 2009).

hindsight, than the returns of a plan sponsored by a company that counsel believes can pay a judgment, or even a settlement. *See PBGC ex rel. St. Vincent Catholic Med. Ctrs. Ret. Plan v. Morgan Stanley Inv. Mgmt. Inc.*, 712 F.3d 705, 719 (2d Cir. 2013) (*PBGC*) (noting that many ERISA cases result in what the Second Circuit has dubbed "settlement extortion"—the use of "discovery to impose asymmetric costs on defendants in order to force a settlement advantageous to the plaintiff regardless of the merits of his suit") (citation omitted). Such lawsuits have long been common when a company that has an employee stock ownership plan (ESOP) or simply offers corporate stock as an investment option for its 401(k) plan suffers a significant decline in its stock value.[11]

[11] *See* José Martin Jara, *What Is the Correct Standard of Prudence in Employer Stock Cases*?, 45 J. Marshall L. Rev. 541, 544 (2012) (reporting that "over the past decade," settlements in ERISA stock-drop cases "have totaled over $1 billion"); René E. Thorne et al., *ERISA Stock-Drop Cases: Evolution and Future*, Law360.com, Dec. 11, 2008, http://www.law360.com/articles/80013/erisa-stock-drop-cases-evolution-and-future (discussing the dramatic increase in stock-drop cases filed in 2007 and 2008); *see also, e.g.*, *Sims v. First Horizon Nat'l Corp.*, No. 08-2293-STA, 2009 WL 3241689, at *20 (W.D. Tenn. Sept. 30, 2009) (plaintiffs alleged numerous procedural defects, including "failing to review the appropriateness of First Horizon Stock as an investment in the plan," "failing to engage independent fiduciaries that could make independent judgments regarding the Plan's investments in First Horizon Stock," and "failing to take such other steps as were necessary to ensure that participants' interests were loyally and prudently served" and seeking to recover "losses of millions of dollars"); *In re Regions Morgan Keegan ERISA Litig.*, 692 F. Supp. 2d 944, 956-58 (W.D. Tenn. 2010) (plaintiffs alleged the fiduciaries' failure to engage in a prudent process before selecting to offer affiliated funds to plan participants as an alternative to company stock).

Given these perverse incentives, adopting Plaintiffs' standard would undoubtedly create significant "undu[e]" administrative expenses. *Conkright*, 559 U.S. at 516-17. In order to protect against windfall judgments, plan fiduciaries and the plan sponsors that appoint or engage them may allocate substantial resources to ensuring that the fiduciaries' decision-making process is not only prudent, but as close to bulletproof as possible. Without a meaningful element of loss causation, any procedural deviation could result in massive liability, so fiduciaries must spend their time flyspecking their own decisions and papering the record thoroughly even in the easiest cases—the cases in which the fiduciary is selecting among a number of indisputably prudent options.

Even if sponsors and fiduciaries do engage in a process sufficiently thorough to protect themselves against liability, they still will face significant "undu[e]" litigation expenses. *Conkright*, 559 U.S. at 516-17. Just defending such suits entails significant cost, as courts have recognized: "[T]he prospect of discovery in a suit claiming breach of fiduciary duty is ominous, potentially exposing the ERISA fiduciary to probing and costly inquiries and document requests about its methods and knowledge at the relevant times." *PBGC*, 712 F.3d at 719.

For the large number of plan sponsors that are small or mid-sized businesses,[12] there is a real risk that these additional undue administrative and litigation costs may discourage them from offering, or continuing to offer, benefits under ERISA—just as Congress feared. *See Conkright*, 559 U.S. at 517. And the risk and expense that Plaintiffs' loss-causation standard would create threatens harm to the sponsors, fiduciaries, *and beneficiaries* of every plan subject to that rule—harm from crimping investment decisions; raising the costs of services, indemnification, and insurance; and ultimately diverting resources from other key aspects of employee-benefit programs, such as 401(k) matching contributions or subsidization of healthcare premiums. That result is thoroughly at odds with Congress's design.

[12] *See* Deloitte Development LLC, *Annual Defined Contribution Benchmarking Survey* 6 (2014), *available at* http://www2.deloitte.com/content/dam/Deloitte/us/Documents/human-capital/us-cons-annual-defined-contribution-benchmarking-survey2013-081914.pdf (reporting that more than one-third of plan sponsors surveyed by Deloitte in 2013 and 2014 employed 500 or fewer employees); Stuart Robinson, *Three Myths Keeping Small Businesses From Starting A 401(k)*, Forbes, Sept. 25, 2013, http://www.forbes.com/sites/stuartrobertson/2013/09/25/three-myths-keeping-small-businesses-from-starting-a-401k (reporting that 24% of businesses with fewer than 50 employees offer a 401(k) plan).

CONCLUSION

The Court should affirm the judgment below and hold that Plaintiffs failed to meet their loss-causation burden.

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CERTIFICATE OF COMPLIANCE

I certify that this brief complies with the type-volume limitations set forth in Fed. R. App. P. 29(a)(5) and 32(a)(7)(B) because this brief contains 6,463 words, excluding those parts of the brief exempted by Fed. R. App. P. 32(f). I further certify that the brief complies with the typeface requirements of Fed. R. App. 32(a)(5) and the style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface, 14-point Times New Roman, using Microsoft Word.

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CERTIFICATE OF SERVICE

I hereby certify that on January 17, 2018, I electronically filed the foregoing brief using the Court's CM/ECF system, which will send notice of such filing to counsel for all parties.

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