No. 18-3616

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

DEBORAH VIGEANT, et al.,

Plaintiffs-Appellants,

v.

MICHAEL MEEK, et al.,

Defendants-Appellees.

On Appeal from the United States District Court for the
District of Minnesota

BRIEF FOR THE SECRETARY OF LABOR AS AMICUS CURIAE IN SUPPORT OF PLAINTIFFS-APPELLANTS FOR REVERSAL

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STATEMENT OF THE ISSUES

The Lifetouch Employee Stock Ownership Plan (ESOP) was a retirement plan that invested primarily in Lifetouch Inc. stock and was covered by the Employee Retirement Income Security Act (ERISA), 29 U.S.C. § 1001, et seq. ESOP Participants sued the ESOP's fiduciaries after Lifetouch stock lost 50% of its appraised value between 2015 and 2018. The Participants allege the fiduciaries violated their ERISA fiduciary duties by failing to monitor and properly value the Lifetouch stock and to take appropriate action to minimize the ESOP's losses. One factual allegation is that the fiduciaries inflated the plan's annual valuation of its stock in 2015 and 2016, before its precipitous decline, by "providing inaccurate and misleading information to the ESOP's independent appraiser." Vigeant v. Meek, No. 18-CV-577, 2018 WL 5839792, at *3 (D. Minn. Nov. 7, 2018).

The district court concluded that "providing inaccurate and misleading information to the independent appraiser . . . sounds in fraud" and struck the underlying allegations because they did not meet the heightened pleading requirement of Federal Rule of Civil Procedure 9(b) to state the circumstances with particularity. Vigeant, 2018 WL 5839792, at *3. Based on the remaining allegations, the court dismissed the Participants' claims because (1) the trustees satisfied their duty to monitor the stock by conducting an annual valuation of the stock and (2) the Participants did not plausibly allege that Lifetouch was on the brink of collapse. The Secretary's brief addresses two questions:

1. Whether allegations that an ERISA fiduciary provided inaccurate and misleading information to an appraiser of plan assets, by themselves, trigger the heightened pleading standard in Federal Rule of Civil Procedure 9(b)?

- In re NationsMart Corp. Sec. Litig., 130 F.3d 309 (8th Cir. 1997).
- Meiners v. Wells Fargo & Co., 898 F.3d 820 (8th Cir. 2018).
- Olin v. Dakota Access, LLC, 910 F.3d 1072 (8th Cir. 2018).

2. Whether an ERISA fiduciary fulfills his duty to monitor a plan's stock investments under Tibble v. Edison Int'l, 135 S. Ct. 1823 (2015), by conducting an annual valuation of the stock and has no further duty to monitor or take action to minimize losses unless the company issuing the stock is on the brink of collapse?

- Fifth Third Bancorp v. Dudenhoeffer, 573 U.S. 409 (2014).
- Tibble v. Edison Int'l, 135 S. Ct. 1823 (2015).
- Tibble v. Edison Int'l, 843 F.3d 1187 (9th Cir. 2016).

STATEMENT OF IDENTITY, INTEREST, AND AUTHORITY TO FILE

The Secretary of Labor has primary authority to enforce and interpret the provisions of Title I of ERISA. 29 U.S.C. §§ 1132, 1135. Secretary of Labor v. Fitzsimmons, 805 F.2d 682, 688-91 (7th Cir. 1986) (en banc). First, the Secretary has an interest in ensuring allegations that a fiduciary provided misleading information do not alone trigger Rule 9(b)'s heightened pleading standard. Such a rule would impose Rule 9(b)'s strictures on a wide swath of ERISA complaints, which frequently include allegations that a fiduciary provided incorrect or incomplete information. Because participants and beneficiaries cannot be expected to know all of the specific circumstantial details of fiduciary misconduct, such a rule risks insulating breaching fiduciaries from liability by prematurely dismissing potentially meritorious claims for lack of specifics, even though their allegations do "not implicate an important purpose of Rule 9(b), [which is] to ensure that defendants may promptly respond to specific allegations of immoral conduct," Streambend Properties II, LLC v. Ivy Tower Minneapolis, LLC, 781 F.3d 1003, 1013 (8th Cir. 2015). That result contravenes Congressional intent to provide "ready access to the Federal courts" to protect the interests of the participants and beneficiaries. See 29 U.S.C. § 1001(b); Anderson v. Alpha Portland Indus., Inc., 752 F.2d 1293, 1300 (8th Cir. 1985) (en banc).

Second, the Secretary has an interest in correcting the district court's anomalous views on the fiduciary's duty to monitor investments that are inconsistent with the Supreme Court's decisions in Tibble v. Edison, 135 S. Ct. 1823 (2015) and Fifth Third Bancorp v. Dudenhoeffer, 573 U.S. 409 (2014). Both holdings on Rule 9(b) and the fiduciary's duty to monitor would implicate the Secretary's own enforcement actions.

The Secretary files this brief as amicus curiae under Federal Rule of Appellate Procedure 29(a).

STATEMENT OF THE CASE

I. Factual Allegations and Fiduciary Breach Claims

Lifetouch is a photography company that "focused primarily on the school picture business" and was "employee owned" through an employee stock ownership plan. Am. Compl. ¶¶ 4-5, 55. In 2015, Lifetouch's value began to decline. Am. Compl. ¶ 5. In 2015 and 2016, Lifetouch closed many "of their J.C. Penney and Target portrait studios" and closed its "Charlotte, North Carolina production facility" in November 2015. Am. Compl. ¶¶ 13, 59.

During this time, "Lifetouch senior executives . . . inflated [the] value of Lifetouch stock." Am. Compl. ¶ 61. Because Lifetouch is not a publicly traded stock, the share price "is determined by the Trustee[s] with an opinion of an independent appraiser." Am. Compl. ¶ 54. "One of the metrics used to calculate" the stock's value is the number of "photo sittings" or "sits." Am. Compl. ¶ 61. "Lifetouch's practice during [2015 and 2016] was to manipulate this figure to make the value of the Company look greater than it actually was," which "inflated" the company's valuation. Am. Compl. ¶ 61. Also in 2015 and 2016, multiple "senior executives . . . [began] to retire . . . benefit[ing] from the overvalued stock price when their Plan accounts were distributed upon retirement," and they received the inflated value of the stock in cash. Am. Compl. ¶ 77.

Plan Participants were cashed out by Lifetouch upon separation, and, during this period, they were cashed out at inflated prices. Am. Compl. ¶¶ 19, 55. Consequently, "more than $1 billion was paid out to former Plan Participants during the Class Period at inflated prices— including to senior executives . . . . These payouts deprived the Plan of funds that rightfully should be shared proportionately among all Plan Participants." Am. Compl. ¶ 72. Due to the inflated prices, the Plan overpaid for shares "and thus Plan Participants received fewer shares in their individual accounts" than if the Plan had paid at the proper price. Am. Compl. ¶ 16.

Lifetouch stock's value decreased by 10% in fiscal year 2015, 5% in fiscal year 2016, and 36% in fiscal year 2017. Am. Compl. ¶¶ 5, 58, 61. "[D]espite the 36% drop in share price, Defendants bought even more shares of Lifetouch for the Plan," Am. Compl. ¶ 17, even though they knew or had reason to know of "an upcoming sale of the company due to slowed growth and cash flow problems . . . and that further stock price declines were in the offing." Am. Compl. ¶ 67. On January 30, 2018, Lifetouch announced its "acquisition by Shutterfly for $825 million, which [] indicates a further decrease of 17.5%." Am. Compl. ¶ 6.

Participants alleged the ESOP's fiduciaries breached their fiduciary duties in three ways. Count one alleges the ESOP's trustees breached their duty of prudence by failing to "conduct an appropriate investigation of the merits of continued investment in Lifetouch stock," despite knowing or having reason to know the ESOP's value was artificially inflated in 2015 and 2016. Am. Compl. ¶¶ 58-61, 99(e). Count two alleges certain members of Lifetouch's board of directors (the "Board Defendants") failed to monitor the trustees and are liable for the trustees' breaches as co-fiduciaries under ERISA section 405, 29 U.S.C. § 1105. Am. Compl. ¶ 106. Count three alleges the Board Defendants and Lifetouch breached their duty of loyalty by failing to "avoid conflicts of interest" that arose when they artificially inflated the value of Lifetouch stock "to financially enrich retiring senior executives." Am. Compl. ¶ 115.

II. Decision Below

The district court granted the fiduciaries' motion to dismiss. It applied Rule 9(b) to the complaint's allegation that Lifetouch executives "manipulated data provided to the independent appraiser." Vigeant, 2018 WL 5839792, at *3-4 & n.2. But in explaining its reasoning, the court broadly described the "alleged conduct" that triggered Rule 9(b) as "providing inaccurate and misleading information to the independent appraiser," which it said "sounds in fraud." Id. at *4. The court then concluded the allegation in the Complaint's paragraph 61 did not meet Rule 9(b)'s heightened pleading standard because it failed to allege the circumstances with particularity. Id.

The court held the remaining allegations failed to state a claim that the trustees violated its duty of prudence (Count 1) for two reasons. Id. at *5. First, Participants' "own allegations . . . that the Trustee[s] annually determined the fair market value of Lifetouch stock" was "inconsistent with [their] assertion that [fiduciaries] conducted absolutely no monitoring of the Plan's investment in the face of changed financial circumstances." Id. Second, "Lifetouch stock was not so risky as to make the company stock an imprudent investment" because Participants failed to allege Lifetouch was "on the verge of collapse." Id. at *6. The Court then dismissed the duty-to-monitor claim against the Board Defendants (Count 2), concluding it was derivative of the failed prudence claim. Id. Finally, the court dismissed the duty-of-loyalty claim (Count 3), reasoning the "Trustees relied on an independent appraiser to evaluate the stock value" and Participants did not "plausibly allege that senior executives manipulated the financial data." Id. The district court concluded that company executives left Lifetouch when it was experiencing financial difficulty, which did not "suggest malfeasance" but was an "action[] that 'one would expect.'" Id. (quoting Braden v. Wal-Mart Stores, Inc., 588 F.3d 585, 595 (8th Cir. 2009)).

SUMMARY OF THE ARGUMENT

1. The district court incorrectly held allegations of "providing inaccurate and misleading information to the independent appraiser," without more, are subject to Federal Rule of Civil Procedure 9(b). This rule contravenes both the text of Rule 9(b) and Eighth Circuit law. Moreover, such a rule would inappropriately apply a heightened pleading standard to many ERISA cases because such claims are common. But they do not, based on those allegations alone, "sound in fraud."

2. The district court also erred in dismissing Participants' duty-to-monitor claim. First, it conflated an Internal Revenue Code requirement to conduct an annual valuation of an ESOP's stock with a fiduciary's duty to monitor investments. In evaluating appraised values, the unanimous case law requires fiduciaries to conduct an independent review of stock valuations. Second, the court erroneously limited the plan fiduciaries' duty to monitor investments under Tibble, 135 S. Ct. at 1828, to situations where the company sponsoring the ESOP is on the verge of collapse. Both Tibble, 135 S. Ct. at 1828, and Dudenhoeffer, 573 U.S. at 422-23, rejected such rigid rules that limit the fiduciary's duty only to specific circumstances, such as a verge of collapse.

ARGUMENT

I. Allegations of Providing Inaccurate and Misleading Information Alone Do Not Trigger Rule 9(b)'s Heightened Pleading Standard

Rule 9(b) provides: "In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake." "Claims 'grounded in fraud' must meet this heightened pleading requirement." Streambend Properties II, LLC v. Ivy Tower Minneapolis, LLC, 781 F.3d 1003, 1010 (8th Cir. 2015). Whether a claim is grounded in fraud is a "pleading-specific inquiry in which the focus is on the elements of the claims asserted." Olin v. Dakota Access, LLC, 910 F.3d 1072, 1076 (8th Cir. 2018). This Court has noted, however, that even where fraud is not an essential element of a claim, Rule 9(b) applies to particular allegations of fraud. See Streambend Properties II, 781 F.3d at 1011, 1013 (considering whether claim based on statutory provision "not explicitly grounded in fraud" had any "specific averments of fraud" or "only allegations of innocent or negligent misrepresentations and omissions").

A. The District Court's Broad Rule Contravenes this Court's Requirement to Make a Pleading-Specific Inquiry That Examines Whether General Allegations of Providing Inaccurate or Misleading Information Are Grounded in Fraud

The district court ruled broadly that Rule 9(b) applies to allegations of "providing inaccurate and misleading information to the independent appraiser" because the conduct "sounds in fraud." Vigeant, 2018 WL 5839792, at *4. If upheld, this rule applies Rule 9(b) to a wide swath of fiduciary conduct without making a pleading-specific inquiry that focuses on the elements of the specific claim and whether the claim has any "specific averments of fraud." Its broad rule that applies Rule 9(b) to any fiduciary-breach claim arising from inaccurate and misleading statements, without more, contravenes Eighth Circuit precedent. While plaintiffs may assert fraud in support of a fiduciary breach claim—and those allegations would be subject to Rule 9(b) under Streambend II—fraud is not an essential element of an ERISA fiduciary-breach claim. See, e.g., Streambend Properties II, 781 F.3d at 1010, 1013; Concha v. London, 62 F.3d 1493, 1502 (9th Cir. 1995) ("In fact, the London Defendants cite no case from any jurisdiction requiring plaintiffs to comply with Rule 9(b) when they allege breaches of fiduciary duty—under ERISA or any other law—but do not plead the commission of fraud.").

In the ERISA context, Rule 9(b) does not generally apply to the elements of fiduciary breach claims, because fiduciary breach claims do not include any element of fraud. Indeed, the word "fraud" appears nowhere in ERISA's description of fiduciary breaches or the elements of such claims. See 29 U.S.C. §§ 1104-06. Nor did Congress mention fraud in declaring the purpose of ERISA's fiduciary responsibility rules. 29 U.S.C. § 1001. While nothing in ERISA condones fraud by fiduciaries, of course, fiduciary-breach claims under

ERISA are not "grounded in fraud," because they are based on the affirmative duty to serve plan participants with prudence and loyalty, whereas fraud is only based on the general duty to refrain from harming others. See, e.g., Jander v. Ret. Plans Committee of IBM, 910 F.3d 620, 632 (2d Cir. 2018) (distinguishing between ERISA breach of fiduciary duty and fraud claims).

Notably, this Court applied the less stringent standard required by Rule 8 to ERISA breach of fiduciary duty claims, including those based on a failure to "disclose details about [] revenue sharing payments." Braden v. Wal-Mart Stores, Inc., 588 F.3d 585, 599 (8th Cir. 2009). In Braden, this Court held the district court "misapplied" Rule 8 to an ERISA fiduciary breach claim by requiring the plaintiff to "describe directly the ways in which [fiduciaries] breached their fiduciary duties," that is, to meet a heightened standard of pleading. Id. In applying Rule 8 to ERISA fiduciary breach claims without any heightened standard, this Court was expressly guided by "ERISA's remedial purpose and evident intent to prevent through private civil litigation 'misuse and mismanagement of plan assets.'" Id. at 597. "If plaintiffs cannot state a claim without pleading facts which tend systemically to be in the sole possession of defendants, the remedial scheme of the statute will fail, and the crucial rights secured by ERISA will suffer." Id. at 598. The Court must consider these purposes when applying pleading standards to ERISA fiduciary breach claims, and the district court's broad rule overlooks those purposes.

Importantly, ERISA claims do not require one of the bedrock elements of fraud claims subject to Rule 9(b) – detrimental reliance. The Supreme Court has made clear that "there is no general principle that 'detrimental reliance' must be proved before a remedy is decreed" for fiduciary misrepresentations. CIGNA Corp. v. Amara, 563 U.S. 421, 443 (2011). In contrast, "[r]easonable, detrimental reliance upon a misrepresentation is an essential element of a cause of action for fraud." Learning Works, Inc. v. The Learning Annex, Inc., 830 F.2d 541, 546 (4th Cir. 1987) (citing Rule 9(b)); see also Murphy v. Aurora Loan Servs., LLC, 699 F.3d 1027, 1032 (8th Cir. 2012); IAS Servs. Grp., L.L.C. v. Jim Buckley & Assocs., Inc., 900 F.3d 640, 648 (5th Cir. 2018) ("Rule 9(b)'s particularity requirements are tied to the elements of fraud, specifically detrimental reliance.").

Accordingly, courts consistently reject the argument that Rule 9(b) broadly applies to all ERISA fiduciary breach claims because they are grounded in fraud. E.g., Fulghum v. Embarq Corp., 785 F.3d 395, 417 (10th Cir. 2015) ("[T]he district court erred when it dismissed Plaintiffs' breach of fiduciary duty claims based on Rule 9(b)."); Concha v. London, 62 F.3d 1493, 1503 (9th Cir. 1995) ("Rule 9(b) is not applicable in cases in which the complaint alleges breaches of fiduciary duty under ERISA, and does not allege fraud or mistake."). Some courts have applied Rule 9(b) to specific allegations of fraud in ERISA fiduciary breach claims; others have not. Compare, Vivien v. Worldcom, Inc., No. C 02-01329, 2002 WL 31640557, at *7 (N.D. Cal. July 26, 2002) (applying Rule 9(b) to an ERISA fiduciary-breach claim that "point[ed] to nine generic improper business practices to demonstrate falsity and misrepresentations" without providing specifics), with Crowley v. Corning, Inc., 234 F. Supp. 2d 222, 230-31 (W.D.N.Y. 2002) (allegations that fiduciary breached its duty by providing information that is "false or misleading" is not fraud claim and not subject to Rule 9(b)'s requirements).

In any case, an allegation of the provision of inaccurate and misleading information by itself is not fraudulent for two reasons. First, any allegation of a provision of inaccurate information to the appraiser must be analyzed within its context. As ERISA fiduciaries, the Trustees must "employ[ ] the appropriate methods to investigate the merits of the investment" Roth v. Sawyer-Cleator Lumber Co., 16 F.3d 915, 918 (8th Cir. 1994) (quoting Katsaros v. Cody, 744 F.2d 270, 279 (2d Cir. 1984)), including the basis for its valuation of Lifetouch stock, e.g., Chao v. Hall Holding Co., 285 F.3d 415, 434 (6th Cir. 2002). Plausible claims that a fiduciary failed to prudently investigate the factual basis for a valuation, and thereby overvalued the stock to the detriment of the plan, only require an assertion that the basis was inaccurate or flawed, not that it was fraudulent. E.g., Chao, 285 F.3d at 434.

In other words, the mere allegations that fiduciaries imprudently used or supplied inaccurate data in their overvaluation is separate and independent from allegations that fraud created the underlying inaccuracies.[1] The Court may assess the plausibility of the former without considering the allegations of fraudulent conduct. In fact, a central obligation of an ESOP fiduciary tasked with determining the fair market value of privately held stock is to "provide [the ESOP's appraiser] with complete and accurate information." Hall Holding Co., 285 F.3d at 430; Leckey v. Stefano, 501 F.3d 212, 225 (3d Cir. 2007); Perez v. Bruister, 823 F.3d 250, 263 (5th Cir. 2016); Keach v. U.S. Tr. Co., 419 F.3d 626, 637 (7th Cir. 2005); see also Martin v. Feilen, 965 F.2d 660, 666-68 (8th Cir. 1992) (recognizing the breach as failing to correct the impairment or

[1] Here, the complaint alleges the Trustees breached their fiduciary duties by "overvalu[ing] Lifetouch stock on the June 30, 2015 and June 30, 2016 fair market value determination dates." Am. Compl. ¶¶ 56, 62 ("The Trustee[s] should not have overvalued Lifetouch stock in the first place."). "The Trustee[s'] improper valuation of Lifetouch stock in 2015 and 2016 harmed Plan participants . . . . Because the shares were overvalued by the Trustee[s], the contribution that Lifetouch made to the Plan in those years was not able to purchase as many shares of Lifetouch stock, which resulted in fewer shares of stock available to distribute to Plan participant accounts." Am. Compl. ¶ 60. The Participants alleged that "[h]ad the Trustee[s] properly utilized the extensive professional resources available for determining the value of Lifetouch stock, perhaps the stock price would not have been so grossly overvalued in 2015 and 2016." Am. Compl. ¶ 57.

manipulation of a plan's investment). Allegations that the fiduciary provided misleading or inaccurate statements to the independent fiduciary or that those statements impaired the ESOP's investment suffice to allege a fiduciary breach and do not require fraud.

Second, to state a claim for a fiduciary breach based on alleged misrepresentations, such as providing inaccurate information to the appraiser, one need not allege the elements of common-law fraud subject to Rule 9(b), including detrimental reliance, supra p. 12-13, and scienter. Negligent misrepresentations suffice to state an ERISA claim for breach of fiduciary duties. Griggs v. E.I. DuPont de Nemours & Co., 237 F.3d 371, 383 (4th Cir. 2001) (permitting negligent misrepresentation claim as the breach of an ERISA fiduciary's duty). This Court explicitly declined to apply Rule 9(b) to allegations of "innocent or negligent misrepresentation and omissions," which are not "averments of fraud." Streambend Properties II, 781 F.3d at 1013. "[N]ot every misstatement qualifies as a fraud." Gamez v. Ace Am. Ins. Co., 638 F. App'x 850, 852 (11th Cir. 2016) (unpublished); see Streambend Properties II, 781 F.3d at 1013. The district court's broad rule that applies Rule 9(b) to any fiduciary-breach claim arising from any statement of inaccurate or misleading information contravenes these precedents.

B. Eighth Circuit Precedents Confirm That The Provision of Inaccurate or Misleading Information Alone Is Insufficient to Trigger Rule 9(b)

Eighth Circuit decisions addressing the Securities Act of 1933 (Securities Act) support the conclusion that an ERISA fiduciary breach claim alleging fiduciaries provided inaccurate or misleading information alone is not grounded in fraud and should not trigger Rule 9(b). See In re NationsMart Corp. Sec. Litig., 130 F.3d 309, 315 (8th Cir. 1997); Romine v. Acxiom Corp., 296 F.3d 701, 704 (8th Cir. 2002). In those cases, the allegation that misleading information was provided in securities registration statements sufficiently states a claim for violation of Section 11 of the Securities Act, 15 U.S.C. § 77k(a). "Section 11 imposes civil liability on persons preparing and signing materially misleading registration statements. . . . A registration statement is materially misleading if it contains an untrue statement of material fact or if it omits a material fact necessary to prevent the statement from being misleading. . . . Any person who purchases a registered security is entitled to sue under this section." NationsMart, 130 F.3d at 314-15.

This Court rejected the application of Rule 9(b) to Section 11 claims. Id. at 315 ("To establish a prima facie § 11 claim, a plaintiff need show only that he bought the security and that there was a material misstatement or omission. Scienter is not required for establishing liability under this section."). In

NationsMart, plaintiffs "alleged that the defendants omitted material information [by] failing to disclose adverse trends the company was experiencing in the months immediately preceding the public offering." Id. at 317. Still, "Rule 9(b) does not apply to claims brought under § 11. The allegations of false statements of historical fact and of material omissions were sufficient to state a claim." Id.; see also Hanjy v. Arvest Bank, 94 F. Supp. 3d 1012, 1030 (E.D. Ark. 2015) (refusing to apply Rule 9(b) to claims that defendant "provided inaccurate balance information to plaintiffs and other customers through its electronic network").

Similarly, allegations that fiduciaries provided inaccurate or misleading information to the plan, especially to the appraiser of an ESOP's stock, may be sufficient by themselves to state a claim. See supra p. 15. If the district court's overly broad rule is upheld and an allegation that a fiduciary provided inaccurate or misleading information triggers Rule 9(b), then a large swath of ERISA fiduciary duty claims would suddenly be subject to a heightened pleading standard even though fraud allegations are unnecessary to state a claim. Such a result undermines ERISA's remedial purposes and its promise of providing "participants in employee benefit plans . . . ready access to the Federal Courts." Pilot Life Ins. Co. v. Dedeaux, 481 U.S. 41, 44 (1987) (quoting 29 U.S.C. § 1001(b)). It also would be contrary to "ERISA's . . . evident intent to prevent . . . misuse and mismanagement of plan assets" and would subvert congressional intent to impose stringent duties on ERISA fiduciaries by prematurely dismissing otherwise meritorious claims. See Braden, 588 F.3d at 597-98; Fitzsimmons, 805 F.2d at 690 (discussing the "remedial and protective purposes of ERISA"). In short, the district court erred in holding that allegations of providing inaccurate and misleading information to the independent appraiser alone was enough to trigger Rule 9(b).

II. An Annual Valuation Does Not Satisfy A Fiduciary's Duty To Monitor Investments; Nor Is That Duty Triggered Only When The Company Is On the Verge of Collapse.

Participants allege the fiduciaries breached their duty to monitor the ESOP's investment in Lifetouch stock by (1) failing to determine if it remained a prudent investment when it rapidly lost appraised value between 2015 and 2018 and (2) failing to take appropriate action to minimize losses. Am. Compl. ¶¶ 13, 16-21, 97-102. The district court dismissed this claim, reasoning Participants' allegations that the "Trustee[s] annually determined the fair market value of Lifetouch stock with the opinion of an independent appraiser" contradicted the claim that the fiduciaries "conducted absolutely no monitoring of the Plan's investment in the face of changed financial circumstances." Vigeant, 2018 WL 5839792, at *5.

The court also reasoned that the Participants failed to state a claim for imprudence and disloyalty because the level of Lifetouch's financial hardship alleged in the complaint was not high enough to trigger a duty to monitor the stock and take appropriate action to minimize the Plan's loss. The court found that Plaintiffs did not allege that Lifetouch was on the verge of "financial collapse" and cited two cases holding that ESOP fiduciaries breached their duties only after the companies incurred losses of over 90%. Id. Both lines of reasoning are wrong.

A. An ERISA Fiduciary Does Not Fulfill His Duty to Monitor By Merely Conducting an Annual Valuation

An ESOP's trustee does not satisfy his duty to monitor by merely conducting an annual valuation of the ESOP's stock. The Internal Revenue Code *requires* an annual valuation of the company's stock "to be an ESOP" within the meaning of the Code. 26 C.F.R. § 54.4975-11(d)(5). Meeting the bare minimum requirements to be an ESOP in no way demonstrates that a fiduciary fulfilled its duties. A contrary conclusion would insulate all ESOP fiduciaries from ERISA liability because an ESOP fiduciary must conduct an annual valuation.

Additionally, this conclusion undermines the unanimous case law that valuations can be flawed, particularly valuations of stock in closed corporations, which are not traded on public stock exchanges. See, e.g., Bruister, 823 F.3d at 262. Stock that is publicly traded in a stock exchange has a value set by the market and can be readily bought or sold for that amount. On the other hand, the value of stock in closed corporations is not determined by a market but by a fallible appraisal expert. See, e.g., id. It is long-established law that fiduciaries may not blindly rely on expert valuations in determining a fair market value; rather, they must conduct a prudent investigation and must independently scrutinize the valuations to make certain they are reasonably justified. See, e.g., Donovan v. Cunningham, 716 F.2d 1455, 1462-63 (5th Cir. 1983); Howard v. Shay, 100 F.3d 1484, 1490 (9th Cir. 1996); Hall Holding, 285 F.3d at 435-37; see also Bussian v. RJR Nabisco, Inc., 223 F.3d 286, 301 (5th Cir. 2000).

The Supreme Court in Tibble v. Edison Int'l, 135 S. Ct. at 1828, also confirmed the fiduciary's "duty to monitor trust investment." On remand, the Ninth Circuit noted that, in evaluating participants' claims, the district court should recognize that the "scope of [a] fiduciary duty to monitor investments" is defined by analogous trust law. Tibble v. Edison Int'l, 843 F.3d 1187, 1197 (9th Cir. 2016) (en banc). "Under trust law, a trustee must 'systematic[ally] conside[r] all the investments of the trust at regular intervals' to ensure that they are appropriate." Id. (quoting A. Hess, G. Bogert, & G. Bogert, Law of Trusts and Trustees § 684, pp. 147–48 (3d ed. 2009)). The district court in this case did not consider whether the complaint plausibly alleges a violation of this duty and focused exclusively on the mere fact that the fiduciaries conducted an annual valuation. It should do so on remand. See Allen v. GreatBanc Tr. Co., 835 F.3d 670, 678–79 (7th Cir. 2016) ("These facts support an inference that [the independent fiduciary] breached its fiduciary duty, either by failing to conduct an adequate inquiry into the proper valuation of the shares or by intentionally facilitating an improper transaction.”).

B. The Duty to Monitor Stock Investments is not Triggered Only When a Company is on the Brink of Collapse

The district court’s reliance on Dudenhoeffer fails to justify its broad rule that annual valuations of the stock in closed corporations are sufficient to satisfy the fiduciary’s duties of prudence. In Dudenhoeffer, the Supreme Court reversed many circuit courts’ application of a presumption that ESOP fiduciaries act prudently when purchasing company stock. 573 U.S. 409 (abrogating Moench v. Robertson, 62 F.3d 553, 571 (3d Cir. 1995)). In some circuits this “Moench presumption” required a plaintiff to “allege and ultimately prove that the company faced ‘impending collapse.’” Dudenhoeffer, 573 U.S. at 418. The Supreme Court concluded ERISA “makes no reference to a special ‘presumption’” and “[i]t does not require plaintiffs to allege that the employer was on the ‘brink of collapse.’” Id. Rather, ERISA section 404’s standards, 29 U.S.C. § 1104, not extra-statutory tests, governed these claims. Id.

While the district court did not cite to Moench directly, its rationale – that the “facts demonstrate financial hardship, but not a company on the verge of collapse,” Vigeant, 2018 WL 5839792, at *5 – is the same rationale Dudenhoeffer rejected. 573 U.S. at 417. As with the lower courts in Dudenhoeffer, the district court improperly presumed the fiduciaries satisfied their duties to monitor Lifetouch stock as long as Lifetouch was not on the verge of collapse.

The district court's reliance on a broad rule that would presume prudence in monitoring investments absent a company's collapse also contravenes Tibble. The Supreme Court admonished the Ninth Circuit in Tibble when the Ninth Circuit assumed only "significant changes" that occurred with plan investments could trigger a fiduciary's duty to monitor investments. 135 S. Ct. at 1827–28. "The Ninth Circuit did not recognize that under trust law a fiduciary is required to conduct a regular review of its investment with the nature and timing of the review contingent on the circumstances." Id. The district court failed to consider the specific circumstances when adopting a simplistic rule that only a collapse triggers the fiduciary's duty to monitor and take any corrective actions.

C. Dudenhoeffer's Standard is Inapplicable to Lifetouch Because it is Privately Held Stock

Further, the application of Dudenhoeffer's standard here is inapt. Dudenhoeffer involved stock that is publically traded in an exchange. This case concerns an expert's opinion and prediction about the value of privately held stock. Dudenhoeffer does not speak to ESOPs that hold closely held stock, where the duty of prudence requires the fiduciary to monitor and determine for himself the proper value for the stock using the valuation only as a tool for that determination. See Allen, 835 F.3d 679.

Moreover, in Dudenhoeffer, "where a stock is publicly traded, allegations that a fiduciary should have recognized from publicly available information alone that the market was over- or undervaluing the stock are implausible as a general rule." 573 U.S. at 426. Here, the fiduciary is responsible for assessing the ESOP stock's value, and cannot point to a market price in defense. Unlike publicly traded stock, a fiduciary's failure to ensure private stock is properly valued will cause serious harm to the plan, including the cashing out of Participants at inflated values and the misuse of plan assets to purchase stock at inflated values. The court's implicit application of the Moench presumption directly contravenes Dudenhoeffer and Tibble.

CONCLUSION

The Secretary respectfully requests this Court reverse the district court's holdings on the two issues presented in this brief.

Respectfully submitted,

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Dated: February 22, 2019

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Dated: February 22, 2019

CERTIFICATE OF SERVICE

I hereby certify that on February 22, 2019, I electronically filed the foregoing with the Clerk of the Court for the United States Court of Appeals for the Eighth Circuit by using the appellate CM/ECF system.

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