No. 05-3417

IN THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

JUAN ARMSTRONG et al.,

Plaintiffs-Appellants

v.

LASALLE BANK NATIONAL ASSOCIATION,

Defendant-Appellee

On Appeal from the United States District Court
for the Northern District of Illinois

BRIEF FOR THE SECRETARY OF LABOR AS AMICUS CURIAE

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STATEMENT OF INTEREST

The Secretary of Labor has primary authority to interpret and enforce the provisions of Title I of the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. §§1001 et seq., and therefore has an interest in the correct application of ERISA's duty of prudence in the administration of plan assets. See Secretary of Labor v. Fitzsimmons, 805 F.2d 682, 692-93 (7th Cir. 1986) (en banc). The district court held that a deferential arbitrary and capricious standard should be applied by courts in reviewing whether an "independent" trustee breached its fiduciary duties under ERISA in performing its annual valuation of company stock for the retirement plan at issue. Adoption of this standard by this Court would undermine the protection that these duties are intended to provide to ERISA plans and their participants and beneficiaries. The Secretary therefore has a strong interest, both in her own cases and in private litigation, in ensuring that courts do not review fiduciary actions under such a deferential standard, but rather undertake a searching inquiry into whether fiduciaries performing such vital functions as valuing a plan's assets have met ERISA's exacting standard of care.

STATEMENT OF THE ISSUE

Whether the district court erred by applying a deferential standard of review to a stock valuation decision by the trustee of an employee stock ownership plan

("ESOP"), in determining whether the trustee met the duty of prudence that ERISA imposes on all plan fiduciaries.

STATEMENT OF THE CASE

A. Nature of the case, course of proceedings, and disposition below

This private ERISA litigation was brought by a class of ESOP participants against their employer, Amsted Industries, Inc., several individuals associated with Amsted, and LaSalle Bank, the trustee responsible for conducting an annual valuation of Amsted stock on behalf of the ESOP. Plaintiffs challenged a series of decisions made by fiduciaries of the Amsted ESOP in 1999 and 2000, which plaintiffs claim were imprudent, violated ERISA, and led to substantial losses in the value of the ESOP's assets. After extensive discovery, the parties filed cross-motions for summary judgment. The district court granted summary judgment to all defendants. Plaintiffs appealed and later settled with the Amsted defendants. As a result, the current appeal involves only LaSalle Bank, and plaintiffs' claim that LaSalle's approval of the 1999 Amsted stock valuation violated ERISA's prudence standard, 29 U.S.C. § 1104(a)(1)(B).

B. Statement of the facts

1. Amsted, a manufacturer of industrial products, has been wholly employee-owned through its ESOP since 1986. July 29, 2004 Mem. Op. & Order

("App.") 2.[1] LaSalle Bank served as the trustee of the ESOP, responsible under the plan documents for setting the fair market value of Amsted's stock each year. App. 3. Since its inception, the ESOP had contained a "put" option that allowed employees who left the company, regardless of age or length of service, to obtain an immediate, lump sum cash distribution of their vested shares in the ESOP, at the price set each year by LaSalle. App. 4-5, 11-12.[2] Amsted thus had a "longstanding, mature ESOP" with a "very generous immediate lump sum payout provision." R.204-¶105. Historically, because Amsted carried very little debt on its books and had relatively low redemption rates, it had been able to honor this repurchase obligation without creating liquidity problems for the company or the ESOP. App. 4, 13-14; R.183-II-6(c)-L000724-5.

On August 16, 1999, Amsted purchased the Varlen Corporation, another manufacturer, and took on an unprecedented amount of new debt, nearly $800

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[1] Citations to "App. __" are to the original pagination of the district court's July 29, 2004 memorandum opinion and order, included in the short appendix to Appellants' brief. Citations to the record (R.) refer to the district court clerk's document number followed by the relevant volume number, tab number, paragraph number or page number, using the same format as Appellants' brief.

[2] To ensure that plan participants can cash out their stock upon retirement, the Internal Revenue Code requires ESOPs to allow participants to sell their shares to the employer "under a fair valuation formula" if their securities are not readily tradable on an established market. 26 U.S.C. § 409(h)(1)(B). The ESOP participant's right of redemption is called a "put option" and the employer's corresponding financial burden is called its "repurchase obligation." See App. 11.

million. App. 2; R.204-¶50. Amsted financed the purchase with a $1 billion unsecured loan from Citibank. App. 2.

On October 27, 1999, LaSalle approved a valuation of Amsted stock at $184.41 per share as of September 30, 1999, a 32% increase from its 1998 value. App. 3. Duff & Phelps, LLC ("D&P") performed the valuation at LaSalle's request. LaSalle asked D&P to determine the value of Amsted stock as if it were publicly traded, with no consideration of stock illiquidity. R.183-I-2(F)-D&P0008, D&P0014; R.150-I-6-81-82. LaSalle did not ask D&P to investigate or analyze Amsted's repurchase obligation, R.204-¶¶69, 103, nor did LaSalle itself undertake any independent analysis of that obligation. R.183-II-6-59-60. The valuation did not discuss Amsted's repurchase obligation, nor did it apply or discuss whether to apply a discount to reflect the lack of marketability of the closely-held Amsted stock. App. 3, 26; R.204-¶¶75, 89.[3] LaSalle did not ask D&P to make any changes to its 1999 valuation report after it was presented to LaSalle. R.183-I-2-131.

Historically, Amsted repurchased from 7.8% to 10.9% of its outstanding shares from departing employees each year. App. 13. After the 1999 share

[3] Such a discount is based on the recognition that, "[s]ince ownership interests in closely-held businesses do not, by definition, enjoy the ready market of a publicly traded stock, a share in a privately held company usually is worth less than an otherwise comparable share in a publicly held company." Shannon P. Pratt et al., <u>Valuing a Business: The Analysis and Appraisal of Closely Held Companies</u> 45 (3d ed. 1996); <u>accord</u> <u>Eyler v. Comm'r</u>, 88 F.3d 445, 452 (7th Cir. 1996).

valuation was announced, however, distribution requests increased sharply, and Amsted ultimately had to repurchase some 32% of its outstanding shares in fiscal year 2000. App. 3-4, 11-14, 28-29. By January 2000, the company faced a serious liquidity crisis and began to consider ways to protect its cash reserves. App. 4. By April 2000, Amsted was obligated to pay $180 million to repurchase ESOP shares for the first three quarters of the fiscal year, and expected to owe some $240 million for the entire year, an amount well in excess of Amsted's available credit after the Varlen acquisition. App. 3, 4.

In response to the liquidity crisis, the Amsted board of directors took a number of steps in the first half of 2000 to amend the ESOP and reduce its cash drain on the company. Amsted eliminated the lump-sum cash payout, eliminated joint and survivor annuities, substituted quarterly share valuations for annual ones, imposed minimum age and length of service or disability requirements for ESOP distributions, and decreased company contributions to participants' ESOP accounts. App. 4-5. The company survived, but the appraised value of its shares dropped sharply. R.182-¶20.

As relevant here, plaintiffs alleged that LaSalle's approval of the 1999 stock valuation violated ERISA's prudence standard, 29 U.S.C. § 1104(a)(1)(B), because: (1) it failed to ensure that D&P had complete and correct information and made proper assumptions for its valuation, especially regarding the Varlen acquisition and Amsted's repurchase obligation; and (2) it failed to apply a discount for lack of marketability. App. 24. In plaintiffs' view, the imprudent overvaluation of Amsted's stock in 1999 contributed to a major upturn in distribution requests and a drain on company assets that eventually led to a sharp drop in Amsted's stock value and a significant depletion in the value of plan assets for participants who did not cash out when the price was $184.41 per share. See App. 20-28. LaSalle denied any imprudence, contended that the increase in distribution requests was not foreseeable, and argued that it was entitled to rely on the valuation of D&P, a respected valuation expert. Id.

2. Plaintiffs' expert on ESOP valuation, Kace Clawson, criticized LaSalle's approval of the 1999 D&P valuation on several grounds. In his opinion, the D&P report was incomplete because: (1) it did not assess the impact of the Varlen acquisition on the fair market value of Amsted, including the effect of the large acquisition debt; (2) it did not include any discussion of a discount for lack of marketability, a primary consideration in the valuation of privately held stock; and (3) it did not discuss Amsted's repurchase obligation, another important consideration for ESOP appraisers. R.183-V-38-1-2.

Clawson faulted LaSalle for approving the D&P valuation without considering a discount for lack of marketability, particularly given the large increase in debt from the Varlen acquisition. R.183-V-38-8. In light of this significant change in Amsted's borrowing capacity, and the fact that repurchase requests were running significantly higher in the July to September 1999 quarter than previously, he concluded that the appraisal should have included a 20% discount for lack of marketability. Id. at 7; see also R.182-¶15 (distribution requests received from July 1 to September 30 were paid at share valuation as of September 30).[4]

Clawson also faulted LaSalle for approving the D&P valuation without obtaining a comprehensive repurchase obligation analysis, R.183-V-38-8, which he described as "an actuarial analysis" that requires a "complete census of the employees," "breaking down those employees into groups," "estimating turnover rates and salary increases and death, disability, other actuarial factors that would apply to it," "estimating share price increases," and extrapolating all those factors out into the future. R.183-V-39-307; see also R.183-V-38-21-22. Clawson explained that, in this case, the increasing stock price was critical to the analysis of the repurchase obligation because "it stimulates employees who have an immediate cash-out benefit to potentially get it in their head that they might want to leave." R.183-V-39-175-176. Because the 1999 valuation failed to undertake this kind of

[4] Clawson relied on Shannon P. Pratt et al., Valuing a Business: The Analysis and Appraisal of Closely Held Companies 735 (3d ed. 1996), a valuation treatise, which lists the employer's liquidity, borrowing capacity, and repurchase liability as critical "economic factors that influence the discount for lack of marketability with regard to ESOP-owned employer corporation securities." R.183-V-38-5.

analysis of the repurchase obligation, Clawson considered it flawed and inaccurate. R.183-V-38-21-22.

In contrast, LaSalle's valuation expert, Robert Gross, opined that "it was reasonable for [D&P] to conclude that no discount for marketability was necessary or appropriate." R.183-V-42-12. According to Gross, ESOP valuation professionals agree that the usual discount for lack of marketability of closely-held stock should be either "reduced or eliminated in its entirety" because of the company's repurchase obligation, and "virtually all would agree that it should at least be reduced." Id. at 6. Stating that discounts from 0 to 10% are common, he added that "[i]t is the general prevailing view of experienced ESOP appraisers that the discount for lack of marketability could increase if there was evidence to suggest that the Company was incapable of honoring its legal obligation to reacquire a participant's shares." Id. at 6-7.

Gross then listed a series of factors that he believed that D&P considered in deciding not to apply a discount for lack of marketability to Amsted stock: (1) the existence of the ESOP put option; (2) the particular provisions of Amsted's put option; (3) the fact that previous Amsted valuations did not discount for lack of marketability; (4) provisions in Amsted's corporate by-laws that direct its valuation without a marketability discount; and (5) the absence of historical evidence to suggest that Amsted would be unable to pay benefits to participants as they became due. R.183-V-42-7-8.[5] However, Gross testified that he would have applied a 5% discount for lack of marketability if he had done the valuation report for Amsted, R.183-V-43-204-05, and acknowledged that his company regularly discusses the issue of a discount for lack of marketability in its ESOP valuations because it is a factor that bears on value. R.204-¶110.[6]

On the topic of repurchase liability, Gross stated that, although the 1999 valuation contained no narrative explanation of Amsted's repurchase liability, R.183-V-42-9, the information D&P reviewed in preparing the valuation "showed that the Company's cash flow was expected to be sufficient to fund repurchases at the anticipated levels within the context of the Company's overall cash demands." Id. at 10. Thus, he concluded that D&P was "correct in their analysis and treatment of Amsted's repurchase liability exposure in their Valuation." Id.

C. The district court decision

In granting LaSalle's motion for summary judgment, the district court held that, as an independent and experienced trustee, LaSalle was entitled to deferential arbitrary and capricious review for its valuation of the ESOP. App. 19-22. In the

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[5] We note that plaintiffs dispute whether the corporate by-laws (which do not appear to be in the record) actually directed such a valuation, whether D&P actually considered any of these factors in its 1999 valuation, and whether these factors outweighed other factors that supported using a discount for lack of marketability in 1999.

[6] LaSalle also admitted that the majority of the ESOP companies that it served as trustee applied a marketability discount, ranging from 2 to 12%. R.183-II-6-73.

alternative, the court held that, "[e]ven if the [prudence] standard developed in Howard [v. Shay, 100 F.3d 1484 (9th Cir. 1996),] applies to LaSalle, who was not involved in self-dealing or a prohibited transaction, a reasonable trier of fact could not find that this trustee violated it." App. 25.

In applying a deferential standard of review, the court relied primarily on three court of appeals decisions – Kuper v. Iovenko, 66 F.3d 1447, 1459 (6th Cir. 1995); Moench v. Robertson, 62 F.3d 553, 571 (3d Cir. 1995); and Ershick v. United Mo. Bank, 948 F.2d 660, 667 (10th Cir. 1991) – that applied a deferential standard in reviewing the decisions of ESOP fiduciaries to continue investing in employer stock. App. 20-21. The court rejected the stricter prudence standard applied in other court of appeals decisions – such as Howard, 100 F.3d at 1489; Eyler v. Comm'r, 88 F.3d 445, 454-55 (7th Cir. 1996); and Donovan v. Cunningham, 716 F.2d 1455 (5th Cir. 1983) – on the ground that the latter group of cases involved conflicted fiduciaries accused of prohibited transactions, rather than independent fiduciaries accused only of imprudence. App. 20-27. The court reasoned that "[t]he decisions of independent and experienced fiduciaries garner deferential review, while the decisions of fiduciaries with a conflict of interest or engaged in suspect transactions do not receive such deference." App. 22.

Applying that standard of review, the court concluded that LaSalle met ERISA's prudence standard in its 1999 valuation of Amsted stock. App. 24-27.

First, the court held that "it was not imprudent for LaSalle to accept D&P's assessment that the acquisition of Varlen, offset by the debt Amsted incurred for the purchase, did not affect Amsted's stock price." App. 26. The court further found that Varlen acquisition debt "was not the source of Amsted's cash flow problems," as it "still left about $200 million credit available for the repurchase of ESOP shares from its retiring employees, far more than historically had been necessary." App. 14.

Second, the court concluded that LaSalle and D&P adequately considered Amsted's repurchase obligation. App. 26-27. Although neither of the D&P employees who performed the valuation remembered seeing any repurchase forecasts, and their report contains no discussion of the topic, the court concluded that they "did take it into account as part of Amsted's projected future cash flows – flows that would be affected by the number of stock shares redeemed by terminating employees." App. 26. The court also found "no evidence that, even if Amsted had used less conservative assumptions in its forecasts, it would have predicted an increase in redemptions that would threaten its cash flow." App. 24.

Third, the court concluded that, "[g]iven Amsted's history of paying terminated participants their benefits quickly, and in full, its bylaws calling for the stock to be treated as if sold on the open market, and its precedent of not applying a marketability discount, no reasonable trier of fact could find that LaSalle breached its duty in accepting D&P's expert opinion," even though its report neither applied nor discussed a marketability discount. App. 28.

SUMMARY OF ARGUMENT

The district court erred by applying an arbitrary and capricious standard to determine whether LaSalle was imprudent in relying on the D&P valuation of Amsted stock. LaSalle admits that it was a fiduciary bound by ERISA's duty of prudence when it determined the value of Amsted's stock. LaSalle thus had an obligation to adhere to the exacting standard of care which ERISA imposes on all plan fiduciaries. This fundamental duty of prudence would be wholly undermined if the courts were to adopt the deferential standard of review advocated by LaSalle in this case.

ERISA requires substantially more of fiduciaries than mere avoidance of arbitrary or capricious conduct. When a fiduciary seeks to rely on expert advice, this Court has held that the fiduciary satisfies ERISA's duty of prudence only if it: (1) investigates the expert's qualifications, (2) provides the expert with complete and accurate information, and (3) makes certain that reliance on the expert's advice is reasonably justified under the circumstances. LaSalle's reliance on the appraisal was reasonably justified if it acted with the "care, skill, prudence, and diligence . . . that a prudent man acting in a like capacity and familiar with such matters would use." 29 U.S.C. § 1104(a)(1)(B). Thus, plaintiffs are entitled to defeat LaSalle's motion for summary judgment if they have offered evidence sufficient to show that there are genuine issues of material fact concerning LaSalle's compliance with this objective, statutory duty of prudence.

Nothing in ERISA's text, purposes, or case law supports the district court's view that a lower standard of prudence applies to fiduciaries that are not accused of self-dealing or conflicts of interest. Rather than deferring to fiduciaries that have allegedly engaged in fiduciary breaches, courts have uniformly engaged in a searching inquiry into their actions. At most, the courts have given some deference to fiduciary decisions in two unrelated contexts: (1) cases that involve the review of discretionary benefit determinations and administration; and (2) cases that challenge a fiduciary's decision to continue holding company stock pursuant to the provisions of ESOPs that contemplate such stock holdings. The reasons for deference in those two situations are completely absent when considering the application of ERISA's basic duty of care to the valuation of a plan's stock holdings.

ARGUMENT

THE DISTRICT COURT ERRED IN APPLYING A DEFERENTIAL STANDARD OF REVIEW TO LASALLE'S VALUATION OF AMSTED STOCK

A. ERISA's prudence standard applies to all decisions by plan fiduciaries, including stock valuation and other decisions that rely on expert advice

LaSalle admits that, as trustee to the Plan, it was an ERISA fiduciary with the duty to value Amsted stock "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims." 29 U.S.C. § 1104(a)(1)(B); Br. 8. The fiduciary provisions of ERISA were designed to codify and make applicable to plan fiduciaries certain principles developed in the law of trusts, including the prudent man rule, bearing in mind the special nature and purpose of employee benefit plans. S. Rep. No. 93-127, at 29 (1973); H.R. Rep. No. 93-1280, at 302 (1974); Firestone Tire & Rubber Co. v. Bruch, 489 U.S. 101, 110 (1989).

In determining whether fiduciaries have complied with ERISA's fundamental duty of prudence, the courts have applied an objective standard that asks whether the "trustees, at the time they engaged in the challenged transactions, employed the appropriate methods to investigate the merits of the investment and to structure the investment." Katsaros v. Cody, 744 F.2d 270, 279 (2d Cir. 1984) (quoting Donovan v. Mazzola, 716 F.2d 1226, 1232 (9th Cir.1983)); see also Eyler

v. Comm'r, 88 F.3d 445, 454-55 (7th Cir. 1996) (applying standard to a claim of fiduciary breach based on the imprudent valuation of closely-held stock). Prudence does not require prescience and is not judged based on hindsight. Keach v. U.S. Trust Co., 419 F.3d 626, 638 (7th Cir. 2005); Katsaros, 744 F.2d at 279. Nevertheless, the "fiduciary obligations of the trustees to the participants and beneficiaries of [an ERISA] plan are those of trustees of an express trust – the highest known to the law." Donovan v. Bierwirth, 680 F.2d 263, 272 n.8 (2d Cir. 1982); see Chao v. Hall Holding Co., 285 F.3d 415, 426 (6th Cir. 2002); Howard v. Shay, 100 F.3d 1484, 1488 (9th Cir. 1996).

Even when fiduciaries rely on expert advice, they must meet ERISA's exacting standard of prudence. The ERISA case law provides clear guidance on how the prudence standard applies to fiduciaries that seek and obtain advice from experts. "To use an independent appraisal properly, ERISA fiduciaries need not become experts in the valuation of closely-held stock – they are entitled to rely on the expertise of others." Donovan v. Cunningham, 716 F.2d 1455, 1474 (5th Cir. 1983); see also Martin v. Feilen, 965 F.2d 660, 671 (8th Cir. 1992). Independent expert advice is not a "whitewash," however. Bierwirth, 680 F.2d at 272. "An independent appraisal is not a magic wand that fiduciaries may simply wave over a transaction to ensure that their responsibilities are fulfilled. It is a tool and, like all tools, is useful only if used properly." Cunningham, 716 F.2d at 1474. "Although securing an independent assessment from a financial advisor or legal counsel is evidence of a thorough investigation . . . it is not a complete defense to a charge of imprudence." Howard, 100 F.3d at 1489. "[A]s the source of the information upon which the experts' opinions are based, the fiduciaries are responsible for ensuring that that information is complete and up-to-date." Cunningham, 716 F.2d at 1474. When a fiduciary reviews a valuation report, he "is required to make an honest, objective effort to read the valuation, understand it, and question the methods and assumptions that do not make sense." Howard, 100 F.3d at 1490.

Thus, the courts have adopted a three-part test for reliance on experts: the fiduciary making the decision must (1) "investigate the expert's qualifications," (2) "provide the expert with complete and accurate information" and (3) "make certain that reliance on the expert's advice is reasonably justified under the circumstances." Keach, 419 F.3d at 637 (ESOP) (internal quotation marks and citation omitted); accord Gregg v. Transp. Workers, 343 F.3d 833, 841 (6th Cir. 2003) (purchase of life insurance policy); Hall Holding, 285 F.3d at 430 (ESOP); Bussian v. RJR Nabisco, Inc., 223 F.3d 286, 300-01 (5th Cir. 2000) (selection of annuity provider); Howard, 100 F.3d at 1489 (ESOP). The use of an independent and qualified expert thus supports a finding of prudence, but does not end the analysis.

The parties do not appear to dispute the applicability of these prudence standards. Rather, they dispute whether LaSalle met the prudence standards and what standard of review the district court should have used in deciding whether LaSalle met those standards.

The Secretary of Labor takes no position on whether LaSalle satisfied ERISA's prudence standard in performing the 1999 Amsted stock valuation. We note, however, that a substantial body of ERISA case law (as well as expert opinion cited by both parties) recognizes that ESOP trustees should consider both the repurchase obligation and discounts for lack of marketability in valuing ESOP stock. See, e.g., Cunningham, 716 F.2d at 1472 n.35 (ESOP fiduciaries need to consider the "potential cash drain . . . when the company undertakes to repurchase shares distributed to participants upon termination of their interests in the plan"); Eyler, 88 F.3d at 452, 453 (affirming a decision that the share price paid by an ESOP should have included a marketability discount); Hall Holding, 285 F.3d at 423 n.8 (affirming a damages calculation that assigned a 5% marketability discount); Sommers Drug Stores Co. Employee Profit Sharing Trust v. Corrigan Enters., Inc., 793 F.2d 1456, 1462 (5th Cir. 1986) (faulting an employer stock valuation for failing to consider whether to apply a discount for lack of marketability); Conner v. Mid South Ins. Agency, 943 F. Supp. 647, 657 (W.D. La. 1995) (approving a 25% marketability and minority discount).

B. The district court should not have given deference to LaSalle in determining whether LaSalle met the statutory standard of prudence

As an ERISA fiduciary, LaSalle was obligated to comply with ERISA's standard of care, which applies to all fiduciaries, without the benefit of any special deference or presumption in its favor. ERISA does not merely require fiduciaries to refrain from conduct that is arbitrary, capricious, or in bad faith. It requires them to exercise the level of "care, skill, prudence, and diligence . . . that a prudent man acting in a like capacity and familiar with such matters would use." 29 U.S.C. § 1104(a)(1)(B). Nothing in ERISA supports the imposition of a lesser standard of care on professional or independent fiduciaries like LaSalle, or authorizes courts to substitute a duty merely to refrain from arbitrary conduct for the exacting prudence standard Congress placed in the statute itself. Meyer v. Berkshire Life Ins. Co., 250 F. Supp. 2d 544, 564 (D. Md. 2003) ("no deference is afforded to the defendant's conduct in cases involving plan administration or management of plan assets"), aff'd, 372 F.3d 261 (4th Cir. 2004); Ches v. Archer, 827 F. Supp. 159, 165 (W.D.N.Y. 1993) (applying the "'prudent man' standard of care, rather than the deferential arbitrary and capricious standard"); Kowalewski v. Detweiler, 770 F. Supp. 290, 294 (D. Md. 1991) ("the arbitrary and capricious standard of review is inapplicable to claims relating to the duty of the trustees to safeguard and properly manage and operate the Plan").

Thus, if plaintiffs can prove at trial, by a preponderance of the evidence, that LaSalle failed to act "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use," they would be entitled to a judgment in their favor.[7] 29 U.S.C. § 1104(a)(1)(B). Similarly, as the parties opposing LaSalle's motion for summary judgment, plaintiffs are entitled to proceed with their case if they have offered material evidence that would permit a reasonable fact-finder to find in their favor under a preponderance standard. 11 James Wm. Moore et al., Moore's Federal Practice § 56.03[4] (3d ed. 2005); Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 252 (1986). In either procedural posture, the district court should judge the prudence of LaSalle's conduct against the statutory standard, without any deference.

The district court believed that a more deferential standard of review should apply to the decisions of plan fiduciaries, like LaSalle, that are independent of the

[7] When the text of a statutory provision is silent regarding the burden of proof or standard of review, the courts typically apply "'the conventional rule of civil litigation'" that "requires a plaintiff to prove his case 'by a preponderance of the evidence.'" Desert Palace, Inc. v. Costa, 539 U.S. 90, 99 (2003) (citation omitted; accord Grogan v. Garner, 498 U.S. 279, 286 (1991); Herman & MacLean v. Huddleston, 459 U.S. 375, 389-90 (1983); see also Concrete Pipe & Prods. v. Constr. Laborers Pension Trust, 508 U.S. 602, 622-25 (1993) (distinguishing a burden of proof before a trier of fact from a standard of review before an appellate tribunal); Schaffer ex rel. Schaffer v. Weast, 126 S. Ct. 528, 534 (2005) (referring to the "ordinary default rule that plaintiffs bear the risk of failing to prove their claims" at an initial hearing).

plan sponsor and are not accused of self-dealing or conflicts of interest.[8] But neither the district court nor LaSalle points to anything in ERISA's text, structure, or legislative history that would relax the standard of review for "independent" fiduciaries or fiduciaries that are not accused of self-dealing or conflicts of interest. ERISA imposes the fundamental duties enumerated in section 404 on all fiduciaries, whether or not they have conflicts of interest, and imposes additional prohibitions in section 406, 29 U.S.C. § 1106, "to bar categorically" certain transactions where self-dealing and conflicts of interest are likely to be present, but need not be shown. See Comm'r v. Keystone Consol. Indus., Inc., 508 U.S. 152, 160 (1993). But the absence of self-dealing or conflicts of interest does not excuse a failure to meet ERISA's basic standard of care, or entitle a fiduciary to a deferential standard of review. As this Court noted in another prudence case with no evidence of self-dealing, "[h]onest but imprudent trustees can dissipate the

[8] Oddly, LaSalle asserts that it is entitled to deference because it is independent of Amsted, yet it primarily relies upon Amsted's consideration of the repurchase obligation as evidence of prudence, rather than its own independent evaluation of that obligation. Br. 20-22. Additionally, the appellees, like the district court, incorrectly cite Kuper v. Iovenko, 66 F.3d 1447 (6th Cir. 1995), and Moench v. Robertson, 62 F.3d 553 (3d Cir. 1995), as involving "decisions by independent ESOP fiduciaries." Br. 9; see also App. 22. In both cases, however, the fiduciaries that were charged with violating their duties were corporate insiders. See Kuper, 66 F.3d at 1451 (defendants included company itself and some of its directors and officers); Moench, 62 F.3d at 559 (defendants were members of the ESOP Committee, who were also members of the company's Board of Directors).

assets of a fund with speed comparable to dishonest trustees." Brock v. Robbins, 830 F.2d 640, 647 (7th Cir. 1987).

Nor does ERISA case law support reviewing a valuation determination by a plan fiduciary under an arbitrary and capricious standard of review. In general, courts deciding fiduciary breach cases have engaged in a searching, rather than deferential, inquiry into the actions of fiduciaries in determining whether they meet ERISA's statutory standard of prudence. See, e.g., Robbins, 830 F.2d at 648; Katsaros, 744 F.2d at 279; Struble v. N.J. Brewery Employees' Welfare Trust Fund, 732 F.2d 325, 332-34 (3d Cir. 1984). Such scrutiny is entirely appropriate, given ERISA's protective purposes and the exacting fiduciary standards it imposes. The courts have given some deference to fiduciary decisions in only two situations, neither of which is relevant here: (1) cases that involve the review of discretionary benefit determinations and administration; and (2) cases that challenge a fiduciary's decision to continue holding company stock pursuant to the provisions of ESOPs that contemplate such stock holdings.

The Supreme Court addressed the standard of review for ERISA benefit determinations in Firestone. Since ERISA does not prescribe a standard of review for benefit claims, the Court borrowed from trust law, which applies a de novo standard of review in construing plan terms or making benefit determinations, unless the fiduciary is acting under an express grant of discretion, in which case an abuse of discretion standard of review pertains. Id. at 111-15.

While Firestone permits deferential review of benefit determinations where plan documents confer discretion on fiduciaries, its scope is expressly limited to "the appropriate standard of review in § 1132(a)(1)(B) actions challenging denials of benefits based on plan interpretations." 489 U.S. at 108. This limitation makes sense because benefit claims differ in important ways from fiduciary breach claims. First, the issue in a benefit claim is whether a claimant is eligible for benefits under the terms of the plan, which often confer discretion on the fiduciary in making that determination. The issue in a fiduciary breach claim, on the other hand, is whether a fiduciary's conduct met the statutory standard of prudence, which is not discretionary.[9]

Benefit determinations also differ from other fiduciary decisions because a plan administrator considering a benefit claim acts in part as an adjudicator, who must follow detailed procedures set out in Labor Department claims regulations implementing 29 U.S.C. § 1133. See 29 C.F.R. § 2560.503-1. Accordingly, courts

[9] While plan sponsors are generally free to establish the terms and conditions of benefit plans, and to give the plan administrator discretionary authority over plan interpretation, they may not qualify or eliminate ERISA's strict statutory standards of prudence and loyalty. Section 410(a) of ERISA, 29 U.S.C. § 1110(a), declares that any provision "which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part shall be void as against public policy."

reviewing such determinations have adopted procedures similar to those in administrative law, which generally require claimants to exhaust plan remedies and limit review to the record before the plan. See, e.g., Ruttenberg v. United States Life Ins. Co., 413 F.3d 652, 662-63 (7th Cir. 2005). Thus, district courts reviewing benefit determinations by plans often act more like appellate tribunals than triers of fact. In fiduciary breach cases, in contrast, district courts are the initial triers of fact. Thus, analogies to the review of ERISA benefit claims shed no light on the appropriate standard for reviewing a fiduciary's adherence to statutory standards of prudence in handling plan assets.

Nor is LaSalle correct in asserting that it is entitled to a deferential standard of review because, under the common law of trusts, "a deferential standard of review applies whenever a trustee exercises discretionary powers." Br. 16. As a factual matter, the obligation to value the stock was not discretionary, but mandated by the express terms of the plan. More fundamentally, however, LaSalle did not have discretion to disregard ERISA's duty of prudence or overvalue the stock. LaSalle's reliance on Firestone's citation to section 187 of the Restatement (Second) of Trusts (1959) is therefore misplaced. That section provides that "[w]here discretion is conferred upon the trustee with respect to the exercise of a power, its exercise is not subject to control by the court, except to prevent an abuse by the trustee of his discretion." This statement, however, does not tell the whole story; the subsequent comment states:

> a. When powers are discretionary. The exercise of a power is discretionary except to the extent to which its exercise is required by the terms of the trust or by the principles of law applicable to the duties of trustees. As to the principles of law applicable to the duties of trustees, see §§ 169-185.

Restatement § 187 cmt. a. Among the "principles of law applicable to the duties of trustees" in the Restatement is the "[d]uty to [e]xercise [r]easonable [c]are and [s]kill," id. § 174, in other words, the duty of prudence.

Thus, the Restatement does not support reviewing the prudence of a fiduciary's actions for abuse of discretion but instead supports application of a non-deferential standard. See annotation to Restatement § 174 (citing Oscar A. Samos, M.D., Inc. v. Dean Witter Reynolds, Inc., 772 F. Supp. 715, 719-20 (D.R.I. 1991) (applying a non-deferential standard of review in determining whether fiduciary acted prudently)).

Other trust law treatises fully support this result. For instance, Bogert specifies that "[t]he grant of broad discretionary powers to the trustee does not relieve him from the duty to use ordinary skill and prudence in his administration of the trust." George G. Bogert & George T. Bogert, Law of Trusts & Trustees § 541, at 173 (rev. 2d ed. 1993). Nor does the common law support the application of a less stringent standard of review for the actions of professional fiduciaries like

LaSalle. Indeed, as another treatise notes, a number of common law cases support the view that "a corporate trustee, a bank, or trust company, may be held to a higher standard of care and skill than that which is required of individual trustees." 3 Austin W. Scott & William F. Fratcher, The Law of Trusts § 227.2, at 438 (4th ed. 1988).

Thus, LaSalle's reliance on Firestone finds no support in the text of ERISA, the common law of trusts, or the court decisions applying ERISA's fiduciary standards of prudence and loyalty. In fact, the Third Circuit has expressly recognized that the abuse of discretion standard that Firestone drew from the Restatement is inapplicable in a fiduciary breach claim. In re Unisys Sav. Plan Litig., 173 F.3d 145, 154-55 (3d Cir. 1999); see also Struble, 732 F.2d at 333-34 (pre-Firestone case expressly rejecting the arbitrary and capricious standard of review for judging ERISA's duties of prudence and loyalty). Other courts have also applied the stringent "prudent man" standard mandated by section 404 of ERISA in fiduciary breach cases, including cases valuing closely-held stock for an ESOP, and in practice have applied a searching review of the fiduciaries' conduct. See Unisys, 173 F.3d at 155; Howard, 100 F.3d at 1488; Struble, 732 F.2d at 333; Bierwirth, 680 F.2d at 271-72 & n.8.

The district court also mistakenly relied on a particular line of ESOP decisions that apply a deferential standard of review where plaintiffs are challenging an ESOP fiduciary's decision to continue investing plan assets in employer stock. For instance, in Moench v. Robertson, 62 F.3d 553, 571 (1995), the Third Circuit held that "an ESOP fiduciary who invests the assets in employer stock is entitled to a presumption that it acted consistently with ERISA," but "the plaintiff may overcome that presumption by establishing that the fiduciary abused its discretion by investing in employer securities." Id. Similarly, while recognizing that "ERISA imposes high standards of fiduciary duty upon those responsible for administering an ERISA plan and investing and disposing of its assets," the Sixth Circuit applied the Third Circuit's deferential Moench standard of review in reviewing a fiduciary decision to continue investing a large percentage of ESOP assets in employer securities. Kuper v. Iovenko, 66 F.3d 1447, 1458-59 (1995); accord Ershick v. United Mo. Bank, 948 F.2d 660, 667 (10th Cir. 1991); Steinman v. Hicks, 252 F. Supp. 2d 746, 760 (C.D. Ill.), aff'd, 352 F.3d 1101 (7th Cir. 2003).[10]

A number of factors, rooted in the text and purposes of ERISA, support giving a measure of deference to a fiduciary's decision to maintain an ESOP's investment in company stock: (1) ESOPs, by definition, are designed to invest

[10] In affirming, this Court did not expressly address the applicable standard of review of the fiduciary's decision, but instead observed only that "plaintiffs bore the burden of proof" to establish a violation of ERISA's prudence standards, and they failed to do so. Steinman v. Hicks, 352 F.3d 1101, 1106 (7th Cir. 2003).

primarily in employer stock, 29 U.S.C. § 1107(d)(6)(A); (2) ordinarily the terms of the plan require the stock investment, and these terms must be followed unless imprudent or otherwise illegal under ERISA, 29 U.S.C. § 1104(a)(1)(D); (3) ERISA permits non-diversified investments in employer stock by ESOPs, 29 U.S.C. § 1104(a)(2), thereby removing the most common objection to the reasonableness of holding employer stock; and (4) congressional policy favors the establishment and maintenance of ESOPs. However, no such rationales exist for deferring to a fiduciary decision that values any plan asset, including stock of the employer that sponsors the plan. Rather, ERISA and its purpose to protect the retirement savings of employees (29 U.S.C. § 1001(a)) amply support the fiduciary's duty to use "care, skill, prudence, and diligence" to determine the correct price. 29 U.S.C. § 1104(a)(1)(B). In other words, both ERISA and the plan documents support a presumption favoring holding employer stock in an employer stock ownership plan; there is no such presumption favoring any particular stock price.

For these reasons, the Third Circuit has made clear that the Moench arbitrary and capricious standard does not apply outside its specific context, and does not apply at all to ordinary prudence claims involving matters such as investments of plan assets. Unisys, 173 F.3d at 154-55; see also In re Schering-Plough Corp. ERISA Litig., 420 F.3d 231, 237-38 (3d Cir. 2005). Thus, the Moench line of cases is easily distinguishable from this case, and does not support the broad proposition that an arbitrary and capricious standard of review applies to all decisions by non-conflicted fiduciaries. See, e.g., Horn v. McQueen, 215 F. Supp. 2d 867, 875 (W.D. Ky. 2002) (refusing to extend Moench's arbitrary and capricious standard "to the case of an ESOP fiduciary accused of overpaying for employer securities," instead applying Cunningham's searching review of the prudence of the fiduciary's decision).

In sum, this Court should reject the district court's deferential arbitrary and capricious standard, which threatens to undermine the stringent fiduciary protections Congress enacted in ERISA three decades ago. Instead, in determining whether there were genuine issues of material fact sufficient to defeat LaSalle's motion for summary judgment under Rule 56(c), Fed. R. Civ. P., this Court should apply ERISA's statutory prudence standard and the three-part test for fiduciary reliance on experts that it previously adopted in Keach.

CONCLUSION

The Court should review the summary judgment record under the correct standard of review and determine whether genuine issues of material fact preclude summary judgment.

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Dated: December 1, 2005

CERTIFICATE OF SERVICE

I hereby certify that on December 1, 2005, two paper copies of the brief for the Secretary of Labor as amicus curiae supporting appellants for reversal were served using Federal Express, postage prepaid, upon the following counsel of record:

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