No. 04-56136

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

MICHAEL MILOFSKY, et al.

Plaintiffs-Appellants,

v.

AMERICAN AIRLINES, INC., et al.

Defendants-Appellees.

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS

BRIEF AS AMICUS CURIAE ELAINE L. CHAO, SECRETARY OF THE UNITED STATES DEPARTMENT OF LABOR SUPPORTING THE PLAINTIFFS'-APPELLANTS' PETITION FOR REHEARING EN BANC

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INTEREST OF THE SECRETARY

The Secretary of Labor (the "Secretary") has primary authority to interpret and enforce the provisions of Title I of ERISA. 29 U.S.C. §§ 1132, 1135. See Donovan v. Cunningham, 716 F.2d 1455, 1462-63 (5th Cir. 1983). The Secretary's interests further include promoting the uniform application of the Act, protecting plan participants and beneficiaries, and ensuring the financial stability of plan assets. Secretary of Labor v. Fitzsimmons, 805 F.2d 682 (7th Cir. 1986) (en banc). This case presents a question concerning the duties of fiduciaries with regard to individual account plans. Read broadly, the decision of the panel could undermine, if not eliminate, the ability of participants in such plans (and perhaps the Secretary) to bring suit on behalf of the plan under sections 502(a)(2) and 409(a), 29 U.S.C. §§ 1132(a)(2), 1109(a), to remedy fiduciary breaches where not every plan participant's account has suffered a loss. This is likely to effectively remove from the remedial reach of ERISA $1.75 trillion in plan assets held in 401(k) plans. The Secretary has a strong interest in ensuring that this Court does not reach such a result.

ARGUMENT

The plaintiffs, 218 pilots who were participants in a 401(k) plan, brought suit under ERISA section 502(a)(2), 29 U.S.C. § 1132(a)(2), after their company was acquired by American Airlines and their account balances were transferred

from another plan in an allegedly untimely and imprudent manner. Milofsky v. American Airlines, Inc., No. 03-11087, 2005 WL 605754, at *1 (5th Cir. Mar. 16, 2005). They sued the fiduciaries of the American plan, as well as the benefits consulting firm for the plan, alleging they were misled about how the transfer would be accomplished, and that because of fiduciary breaches with regard to the timeliness of the transfer, the value of their accounts, and thus the overall value of the plan, decreased. Id. They requested actual damages to be paid to the plan and allocated among their individual accounts. Id.

Relying on Massachusetts Mutual Life Insurance Co. v. Russell, 473 U.S. 134 (1985), the panel affirmed the district court's dismissal of the case, holding that "plaintiffs lack standing because this case in essence is about an alleged particularized harm targeting a specific subset of plan beneficiaries . . . who seek only to benefit themselves and not the entire plan as required by § 502(a)(2)." Milofsky, 2005 WL 605754, at *7. En banc rehearing is warranted because, read broadly, the panel's ruling eliminates the ability of participants in individual account plans, as well as the Secretary, to sue the fiduciaries under sections 409(a) and 502(a)(2) of ERISA, 29 U.S.C. §§ 1109(a) and 1132(a)(2), and obtain monetary relief for the plan, when alleged fiduciary breaches affected some, but not all (or most), of the plan participants' accounts. Moreover, the decision creates a conflict on the issue with the decision of the Sixth Circuit in Kuper v. Iovenko,

66 F.3d 1447 (1995). See Fed. R. App. P. 35(b)(1)(A) (a conflict with the decision of other circuits is of exceptional importance and justifies en banc rehearing). Because the result reached by the panel is unwarranted by Supreme Court and prior Fifth Circuit precedent and is inconsistent with the plain language of the statute and its purposes, this Court should hear the case en banc and reverse the decision of the panel.

I. THE PANEL'S DECISION IS OF EXCEPTIONAL IMPORTANCE BECAUSE OF ITS LIKELY IMPACT ON PLANS

By reading section 502(a)(2) to disallow enforcement by plan participants who allege fiduciary breaches that harmed the accounts of some but not all plan participants, the decision is likely to adversely affect all 401(k) plans and all other defined contribution plans that offer a number of investment options to plan participants. All pension plans under ERISA are either defined benefit or defined contribution plans. See Nachman Corp. v. Pension Benefit Guar. Corp., 446 U.S. 359, 364 n.5 (1980) (describing the two types of plans). Under section 3(34) of ERISA, 29 U.S.C. § 1002(34), a defined contribution plan is a "pension plan which provides for an individual account for each participant and for benefits based solely upon the amount contributed to the participant's account, and any income, expenses, gains, and losses, and any forfeitures of accounts of other participants which may be allocated to such participant's account." The plan's assets – consisting of all contributions and earnings – are statutorily required to be

held in trust by one or more trustees who have authority and discretion to manage and control the assets of the plan. See 29 U.S.C. § 1103(a); IRC § 401(a). The "contributions are made to a single funding vehicle," and "as amounts are contributed to the trust," (and as earnings and losses occur within particular investments) these amounts "are allocated to the participant's account" through accounting or bookkeeping entries. David A. Littell et al., Retirement Savings Plans: Design, Regulation, and Administration of Cash or Deferred Arrangements 6 (1993). Thus, although the plan assets are allocated to individual "accounts" in this manner, ownership of the accounts or their assets never passes to the participants; rather legal title of all the trust assets is held by the trustee. See Rev. Rul. 89-52, 1989-1 C.B. 110, 1989 WL 572038 (Apr. 10, 1989) ("While a qualified trust may permit a participant to elect how amounts attributable to the participant's account-balance will be invested, it may not allow the participant to have the right to acquire, hold and dispose of amounts attributable to the participant's account balance at will.") (citations omitted).

It is estimated that these defined contribution plans or individual account plans now hold over $2.3 trillion in assets, which is more than half of all pension plan assets. Board of Governors of the Federal Reserve Sys., Flow of Fund Accounts of the United States: Annual Flows and Outstandings, Second Quarter 2004, Fed. Res. Statistical Release Z.1, at 113 (Sept. 16, 2004). Some of these are

employee stock option plans ("ESOPs") that solely or primarily hold company stock and most likely would not be affected by the panel's holding. However, 401(k) plans, which typically offer numerous investment options, hold over $1.75 trillion in assets, according to Department of Labor estimates based on Form 5500 filings by plans.[1] All of these 401(k) plans and their participants potentially will be negatively affected by the panel's decision because even in plans where all participants hold employer stock, not every participant will be invested in every option.

Thus, while the panel's decision will not affect such cases as Tittle v. Enron, No. 01-3913 (S.D. Tex. filed Nov. 13, 2001) and Langbecker v. Elec. Data Sys. (EDS), No. 04-41760 (5th Cir. filed Dec. 29, 2004), where, because of the employers' matching contributions in company stock, every plan participants' account is likely to have been directly affected by the alleged fiduciary mismanagement of the company stock funds, it is likely to preclude all suits for losses to these plans with regard to fiduciary mismanagement or malfeasance of every other investment option held by such 401(k) plans. In such plans, because it

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[1] Such plans are growing rapidly. According to Department of Labor estimates, total contributions by employers and employees to 401(k) type plans increased from $152 billion in 1999 to $170 billion in 2000. Moreover, according to a survey conducted in 2003, 82.2% of eligible employees participated in 401(k) plans. Profit Sharing/401k Council of America, 47th Annual Survey of Profit Sharing and 401(k) Plans: Overview of Survey Results, available at http://www.psca.org/DATA/47th.html.

is highly unlikely that every participant will be invested in every other (non-employer stock) investment option during a given period, the investment decisions and actions of fiduciaries with regard to these options will not be subject to regulation under ERISA sections 409 and 502(a)(2) if the panel's decision is allowed to stand. This would preclude, for instance, suits such as the one brought by plan participants against the Unisys Corporation for imprudently investing in a contract purchased from Executive Life Insurance Co. just before the insurance company was placed in receivership. In re Unisys Sav. Plan Litig., 74 F.3d 420 (3d Cir. 1996).[2] Similarly, the panel's ruling would preclude a suit under section

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[2] Another example is found in United States Department of Labor v. Kirkland, No. CV-02-441-HA (D. Or. filed Apr. 4. 2002) (Judge Haggerty) and the companion private class action Schultz v. Kirkland, No. CV-00-1377-HA (D. Or. filed Oct. 10. 2000) (Judge Haggerty). In these actions, the Secretary and the private plaintiffs brought claims under section 502(a)(2) alleging imprudence by the trustees of a Taft-Hartley plan. The 401(k) plan allowed participants to invest in a number of funds, such as a cash management fund, a fixed income fund, an equity fund, a balanced fund, and a private investment fund. The trustees of the 401(k) plan hired Capital Consultants, LLC ("CCL") as the investment manager for these funds, and CCL, in turn, placed substantial assets in risky private placement investments including loans that a reasonably prudent lender would not have made. Virtually all of these loans by CCL were to sub-investment grade borrowers such as Wilshire Credit Corporation ("WCC") and were inadequately secured. WCC, the largest single borrower from CCL, eventually filed for bankruptcy, and, as a result, the 401(k) plan lost millions of dollars. After the 401(k) plan hired CCL as an investment manager, however, the Plan also added three mutual funds as investment options. Most participants remained invested in the original funds managed by CCL, but some chose to move their investments to the newly added mutual funds. Therefore, when CCL's private placement investments collapsed, it appears that some participants' accounts did not suffer any losses. The suits to

502(a)(2), such as the one at issue in Bannistor v. Ullman, 287 F.3d 394 (2002), against fiduciaries who fail to forward employee contributions to their plans, so long as the fiduciaries merely pocket the contributions of some, rather than all, participants. Moreover, if left standing, the panel's ruling would preclude the suit brought by the participants in the WorldCom plan to recoup the enormous losses to their 401(k) plan stemming from serious fiduciary malfeasance and undisclosed corporate wrongdoing, simply because the company did not provide a match in company stock and consequently not every participants' accounts held investments in such stock. In re WorldCom ERISA Litig., 263 F. Supp. 2d 754, 754-55 (S.D.N.Y. 2003).

These results are not only unwarranted under the statute, they are also antithetical to the primary purpose of ERISA, which is designed to prevent "the misuse and mismanagement of plan assets," Russell, 473 U.S. at 140 n.8, as well as to the specific purposes of section 502(a)(2), which is designed to allow suits to enforce "fiduciary obligations related to the plan's financial integrity," in accordance with the "special congressional concern about plan asset management" reflected in section 409. Varity Corp. v. Howe, 516 U.S. 489, 511, 512 (1996).

Indeed, consistent with its broad protective purposes, the plain statutory terms of section 409(a) expressly provide for recovery of "any losses" to the plan

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recover these substantial plan losses would not be allowed under the panel's analysis.

caused by a fiduciary breach. 29 U.S.C. § 1109(a). And ERISA section 502(a)(2), in turn, permits an action to be brought by plan participants, fiduciaries or the Secretary for "appropriate relief under § 409." 29 U.S.C. § 1132(a)(2). These provisions do not, as the panel's decision assumes, limit a suit under section 502(a)(2) to those seeking to recover "losses to the plan as a whole," and given the "evident care" with which the civil enforcement provisions were crafted, Russell, 473 U.S. at 140, 147, the panel erred in reading such a limitation into the provisions where none is expressly stated. See Harris Trust & Sav. Bank v. Salomon Smith Barney Inc., 530 U.S. 238, 246 (2000) (refusing to read a limitation into the possible defendants under section 502(a)(3)); cf. Varity, 516 U.S. at 515 ("We are not aware of any ERISA-related purpose that denial of a remedy would serve.").[3] As the panel correctly stated, the court's "'task is to apply the text, not to improve upon it.'" Milofsky, 2005 WL 605754, at *7 (citation omitted).

[3] Indeed, Congress declared it to be the policy of ERISA to protect "the continued well-being and security of millions of employees and their dependants," as well as employment stability and commerce, by "establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and by providing for appropriate remedies, sanctions, and ready access to the Federal courts." 29 U.S.C. § 1001(a), (b). Considering these statements in the statute, it defies common sense to believe that Congress meant, without expressly saying so, to exempt from the reach of ERISA's primary remedial provision all individual account plans that suffer losses, so long as those losses do not affect every participant's account.

This is not to suggest that the decisions of the Supreme Court in Russell and of this Court in Matassarin v. Lynch, 174 F.3d 549 (5th Cir. 1999), are wrong. Rather, as Judge King stated in her dissent from the panel's decision, "[b]oth of these cases are distinguishable from the present case, and neither justifies the majority's conclusions." Milofsky, 2005 WL 605754, at *8.

Unlike this case, Russell involved a claim by a plaintiff for direct recovery of individual damages stemming from a denial of plan benefits. In Russell, a plan's disability committee terminated and then reinstated a participant's disability benefits. Claiming losses from the interruption in benefit payments, the participant brought suit under section 502(a)(2) for compensatory and punitive damages, payable not to the plan for a loss of plan assets, but directly to the individual participant for injuries she personally sustained. 473 U.S. at 137-38. After reviewing the text of section 409, the provisions defining the duties of a fiduciary and the provisions defining the rights of a beneficiary, the Supreme Court held that the participant did not have standing to seek extra-contractual compensatory or punitive damages for improper or untimely processing of a benefit claim under sections 409 and 502(a)(2) of ERISA. Although sections 409 and 502(a)(2) of ERISA provide for the recovery of plan losses, the Court held that those remedial provisions do not create an extra-contractual remedy for the individual injuries sustained by the participant in connection with her benefit claim. In so holding,

the Court stated "that recovery for a violation of § 409 inures to the benefit of the plan as a whole." Id. at 140.

Russell distinguished relief to be paid to a plan as damages for the mismanagement of plan assets, as sought here, from relief to be paid to an individual as damages for personal pain and suffering caused by a benefit payment delay, as sought in Russell, 473 U.S. at 143-44. In Russell, the plaintiff sought individualized relief, payable to herself, for alleged injuries that she personally incurred without regard to whether the plan had suffered any loss or diminution of assets. She did not allege any injury to the plan or reduction of its assets, nor did she seek a recovery payable to the plan. Thus, the language in Russell that recoveries under sections 409(a) and 502(a)(2) must "inure[] to the benefit of the plan as a whole," id. at 140, cannot in any way be read to suggest, much less require, that losses are recoverable under sections 409(a) and 502(a)(2) only if they are allocated to every participant in the plan.[4]

Nor does the Matassarin case in any way support this reading of section 502(a)(2). The plaintiff in Matassarin was a beneficiary in an ESOP by virtue of a

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[4] Moreover, we agree with Judge King's observation that Russell does not, in any event, "stand for the proposition that the 'plan as a whole' is synonymous with 'all participants of the plan,'" as several courts have recognized. Milofsky, 2005 WL 605754, at *12 n.4, citing Kuper v. Iovenko, 66 F.3d at 1453; Kling v. Fidelity Mgmt. Trust Co., 270 F. Supp. 2d 121, 124-27 (D. Mass. 2003); Colleen E. Medill, Stock Market Volatility and 401(k) Plans, 34 U. Mich. J.L. Reform 469, 538-39 (2001).

qualified domestic relations order ("QDRO") obtained at the time of her divorce. She brought suit alleging that her account balance under the QDRO was miscalculated and she sought an immediate benefit distribution. She also alleged that the plan fiduciaries had breached their duties by failing to comply with the tax code, which jeopardized the tax qualified status of the plan, by buying back shares of stock from a few participants who cashed out of the plan for less than fair market value, and by failing to diversify her account. As the Court there correctly noted, only the allegation regarding the plan's tax qualification was properly brought under section 502(a)(2) because it involved the interest of the plan as a whole. 174 F.3d at 565-66. The Court held that the allegation that the stock of those who received distributions was purchased back for less than fair market value, only asserted harm to those who cashed out, not to the plan itself, and that, similarly, the failure to diversify the plaintiff's account was consistent with the QDRO's terms and did not cause any losses to the plan. Id. at 567-68.

As Judge King noted in her dissent, Matassarin is easily distinguishable on a number of bases, Milofsky, 2005 WL 605754, at *9, most saliently because the plaintiff there did not, and could not, assert a diminution of the plan's assets, but instead claimed that she had been treated differently than other plan members and sought only a distribution of her benefits. Contrary to the panel's suggestion that the plaintiffs here are simply requesting "that damages be paid to the plan instead

of directly to" themselves, id. at *3; in fact, because the plaintiffs are not currently entitled to a distribution of benefits, the relief they seek can only "be paid to the plan and then distributed within it to individual accounts." Id. at *9 (King, J., dissenting). This distinction is not formalistic, but is essential to an understanding of the nature of the plan and its assets.

The panel's decision does indicate that a suit that affected less than all of the participant accounts could "inure[] to the benefit of the plan, . . . when the suit seeks to vindicate the rights of the plan as an entity when alleged fiduciary breaches targeted the plan as a whole." 2005 WL 605754, at *12 n.16 (emphasis in original). We agree with Judge King that this exception, which is not grounded in the statute, is unsatisfactory because the majority does not "explain how a court should determine if an alleged fiduciary breach targeted the plan as a whole." Id. at *12 n.3. Furthermore, although we argued in our amicus brief in EDS, No. 04-41760, that the breaches alleged there (imprudence with regard to the selection and retention of a particular stock option for the plan) were clearly so targeted because they concern the imprudent nature of an investment option, not for any one individual, but for the plan as a whole, we nevertheless think the distinction is essentially unworkable in a great many other situations. For instance, if the panel is correct in its questionable conclusion that the breaches alleged in Milofsky – mismanagement in the transfer of plan assets – are not targeted at the plan as

whole, it would seem that other breaches, such as allowing excessive fees to be charged with regard to an individual investment option, would likewise not be remedial under section 502(a)(2). This result is not warranted for all the reasons discussed above. Instead, we believe the appropriate question is whether the claim alleges something like damages resulting from a failure to pay someone a benefit due (which is really akin to an individual claim against the plan, not on behalf of the plan) or instead alleges that the fiduciary took some action with respect to the investment of plan assets (including those allocated to individual accounts) that violated fiduciary obligations – such as offering participants as an investment option the fiduciary's brother-in-law's get-rich-quick scheme. The fact that less than all plan participants decided to go with the get-rich-quick scheme as an investment option should not, as a matter of law or logic, provide a defense for the fiduciary from an ERISA claim.

II. THE PANEL'S HOLDING CREATES A CONFLICT WITH A DECISION OF THE SIXTH CIRCUIT

The panel's decision is of exceptional importance for another reason: it creates a conflict with the Sixth Circuit's decision in Kuper, which, on similar facts, rejected the reading of section 502(a)(2) adopted by the court here that disallows a claim for plan losses stemming from fiduciary breach if not all participant accounts would benefit from a recovery. See Milofsky, 2005 WL

605754, at *12 n.19 (recognizing an "arguable conflict" with Kuper); id. at *7 (King, J., dissenting) (the "majority's holding . . . squarely conflicts" with Kuper).

As here, Kuper also involved a delay in the transfer of assets of a group of participants from one plan to another and a diminution in the value of the assets during the delay. The defendants alleged that the plaintiff class failed to state a claim for breach of fiduciary duty under section 409 because the class did not include all of the plan's beneficiaries. 66 F.3d at 1452. The Sixth Circuit cited cases holding that recovery under section 409 must go to the plan, and stated that the relevant cases "distinguish between a plaintiff's attempt to recover on his own behalf and a plaintiff's attempt to have the fiduciary reimburse the plan." Id. at 1452-53. The Sixth Circuit concluded that a subclass of plan participants may sue for a breach of fiduciary duty under section 409 reasoning that "Defendants' argument that a breach must harm the entire plan to give rise to liability under § 409 would insulate fiduciaries who breach their duty so long as the breach does not harm all of a plan's participants. Such a result clearly would contravene ERISA's imposition of a fiduciary duty that has been characterized as "the highest known to law." Id. at 1453 (citation omitted). Accord Kling v. Fidelity Mgmt. Trust Co., 270 F. Supp. 2d 121, 126-27 (D. Mass. 2003). See also Steinman v. Hicks, 352 F.3d 1101 (7th Cir. 2003) (clarifying that a claim for losses relating to financial mismanagement is properly brought under section 502(a)(2) even if the relief

ultimately flows to individuals). The Sixth Circuit's analysis is on target, and the same result should pertain here.

CONCLUSION

For the reasons discussed above, the Secretary, as amicus curiae, requests that this Court rehear this matter en banc and reverse the decision of the panel.

Respectfully submitted this 11th day of April, 2005.

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CERTIFICATE OF SERVICE

I hereby certify that two (2) copies of the Brief of Amicus Curiae Elaine L. Chao, Secretary of the United States Department of Labor, Supporting the Plaintiffs'-Appellants' Petition for Rehearing En Banc, along with a diskette in PDF format, were mailed, via federal express overnight delivery, on this 11th day of April 2005 to the following parties:

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CERTIFICATE OF COMPLIANCE

As required by Fed. R. App. 32(a)(7)(B), I certify that this brief is proportionally spaced, using Times New Roman 14-point font size, and contains 3,827 words.

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Dated: April 11, 2005

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