No. 10-2447

IN THE UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

MARK RENFRO, et al., Plaintiffs-Appellants

v.

UNISYS, et al., Defendants-Appellees

On Appeal from the United States District Court
for the Eastern District of Pennsylvania

Brief Of The Secretary Of Labor, Hilda L. Solis, As Amicus Curiae In Support Of Plaintiffs-Appellants And Requesting Reversal

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STATEMENT OF THE ISSUES

This brief addresses the following issues:

1. Whether the plaintiffs plausibly alleged that the defendants breached their fiduciary duties under the Employee Retirement Income Security Act ("ERISA"), 29 U.S.C. § 1001, et seq., by causing the pension plan in which they participated to pay excessive fees and expenses for administrative and investment management services.

2. Whether the district court erred in dismissing the claims based on the court's conclusion that ERISA section 404(c), 29 U.S.C. § 1104(c), immunizes fiduciaries from liability for imprudence in selecting and maintaining plan investment options that allegedly charged the plan excessive fees.

STATEMENT OF IDENTITY, INTEREST AND AUTHORITY TO FILE

The Secretary of Labor has primary enforcement authority for Title I of ERISA. At issue in this case are ERISA's fiduciary provisions, which were enacted to ensure the prudent management of pension plan assets and to safeguard the security of retirement benefits. More specifically, this case concerns a 1992 Department of Labor regulation that delineates when fiduciaries are relieved by a statutory provision, ERISA section 404(c), 29 U.S.C. § 1104(c), from liability for their fiduciary breaches with regard to

certain participant-directed individual account plans, such as 401(k) plans. 29 C.F.R. § 2550.404c-1. The Secretary has a strong interest in ensuring that this regulation is not construed to absolve fiduciaries of liability for plan losses caused by their own improper actions.

The Secretary files this brief as amicus curiae under Fed. R. App. P. 29(a).

STATEMENT OF THE CASE

1. This appeal stems from a putative class action brought by two participants in the Unisys Corporation Savings Plan (the "Plan") on behalf of the Plan and its similarly situated participants or beneficiaries. The Plan is a defined contribution plan under ERISA section 3(34), 29 U.S.C. § 1002(34), and a tax-qualified 401(k) plan. Second Amended Complaint (SAC) ¶ 33. The suit alleges the defendants – the Unisys Corporation, along with the Unisys Corporation Employee Benefits Administrative Committee, the Unisys Corporation Savings Plan Manager, the Pension Investment Review Committee, and the individual members of the Finance Committee, as well as Fidelity Management Trust Company ("FMTC") and its affiliates – breached their fiduciary duties under ERISA by causing the Plan to pay excessive fees for administrative and investment management services. Id. ¶¶ 5-20.

Under the Plan, qualified employees may contribute up to 20% of their pre-tax income to the Plan, and Unisys will match those contributions up to 4% of an employee's compensation. SAC ¶ 34. During the relevant period, Plan participants could choose from a menu of funds selected and monitored by the defendants. SAC ¶ 36. From 2000 to 2007, the Plan's assets exceeded $2 billion, placing it in the largest 1% of all 401(k) plans in the United States. SAC ¶ 44. Nearly $1.9 billion of those assets were held in Fidelity-brand retail mutual funds. Id.

The plaintiffs allege that the defendants violated their fiduciary duties under ERISA by allowing the Plan to pay excessive administrative and investment management fees. SAC ¶ 2. In particular, the plaintiffs allege, among other things, that the defendants failed to benchmark available the costs for the same management services available to other 401(k) plans of a similar size, "failed to recognize that, given the size of the Plan, the costs were excessive in light of the services provided," failed to consider "far less expensive" options "that provided the same or similar services," failed to establish a prudent procedure for determining the reasonableness of the fees, and failed to ensure that the fees "decreased or did not increase as the assets in the Plan increased without a commensurate increase in the level of services being provided." Id. ¶¶ 50, 55, 75, 80.

2. The district court dismissed the plaintiffs' claims against all of the defendants under Fed. R. Civ. P. 12(b)(6) and alternatively granted the Unisys defendants' motion for summary judgment. Renfro v. Unisys Corp., No. 07-2098, 2010 WL 1688540, at *1 (E.D. Pa. Apr. 26, 2010). The district court relied heavily on the Seventh Circuit's decision in Hecker v. Deere & Co., 556 F.3d 575 (7th Cir.), reh'g denied, 569 F.3d 708 (2009), noting that in that case, the plan offered 23 mutual funds with fees ranging from .07% to just over 1%, and the Plan at issue here offered more than 70 funds with fees ranging from .1% to 1.21%. 2010 WL 1688540, at *1. The district court agreed with Hecker's reasoning that a plan fiduciary is not obligated to select the cheapest fund available, and it noted that the fees charged by the funds were disclosed to participants who could choose among them. Id. The court concluded that the funds in the Plan were "offered to investors in the general public, and so the expense ratios necessarily were set against the backdrop of market competition." Id. (quoting Hecker, 556 F.3d at 586). The district court therefore granted the Unisys Defendants' motion to dismiss, holding that "[t]he Plan 'offered a sufficient mix of investments for their participants' and that no rational trier of fact could find, on the basis of the facts alleged in the operative complaint, that the Unisys Defendants breached an ERISA fiduciary duty by

offering this particular array of investment vehicles." Id. at *5 (quoting Hecker, 556 F.3d at 586).

Alternatively, the court held that, even assuming the plaintiffs had stated a claim against the Unisys defendants for breaching their fiduciary duties to the Plan by allowing the Plan to pay excessive fees, the Unisys defendants were entitled to summary judgment under ERISA section 404(c), 29 U.S.C. § 1104(c). Renfro, 2010 WL 1688540, at *7-*9. The plaintiffs had argued that this statutory provision is inapplicable because it provides only a limited exception from liability for losses that "result[] from" a participant's or beneficiary's exercise of control over his or her individual account in an individual account plan. Relying on the Secretary's regulation, 29 C.F.R. § 2550.404c-1, the plaintiffs pointed out that because the inclusion of investment options with excessive fees in the Plan necessarily preceded the participants' decisions to invest in particular funds, any losses to the Plan resulted from the fiduciaries' actions and not from the participants' exercise of control over their individual accounts. The court rejected this argument, declining to accord deference to the Department of Labor's interpretation of her own regulation. Renfro, 2010 WL 1688540, at *8.[1]

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[1] The court also dismissed the claims against the Fidelity Defendants, concluding that they were not shown to be Plan fiduciaries. Renfro, 2010

SUMMARY OF ARGUMENT

Under federal pleading standards, a complaint need do no more than put the defendants on notice of the grounds for the claim and plausibly state a claim for which relief is available. The complaint in this case alleges that Plan fiduciaries, who are impressed by ERISA with strict duties of prudence and loyalty, violated their duties by allowing one of the country's largest 401(k) plans to pay excessive retail-level fees for its investments when it could have obtained the same investments and services for less. Fees are an important component of the overall performance of ERISA defined contribution plans and, therefore, ensuring the reasonableness of those fees is a critical component of a prudent fiduciary's responsibilities. Because the complaint alleges that the fees charged by many of the Plan's investments were excessive compared to the services provided and that these investments were selected pursuant to an imprudent process, it is akin to the complaint that the Eighth Circuit held sufficient to state a fiduciary breach claim in Braden v. WalMart and distinguishable from the complaint that was dismissed in Hecker v. Deere. The district court's order dismissing this suit on plausibility grounds not only misconstrues ERISA's fiduciary duties with

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WL 1688540, at *4-*5. The Secretary's brief does not address this fact-bound issue.

regard to plan fees, it also directly undermines ERISA's expressly stated intent to provide plan participants and beneficiaries "ready access to the Federal courts." Nothing in the federal pleading standards supports this result.

The district court likewise misconstrued ERISA section 404(c) and consequently erred in granting summary judgment to the defendants on this basis. The statutory safe harbor in section 404(c) does not immunize fiduciaries for losses caused by their own imprudence. The Secretary's regulation interpreting section 404(c), issued after notice and comment pursuant to an express delegation of authority, reasonably interprets 404(c) as providing no defense to the imprudent selection or retention of an investment option by the fiduciaries of an individual account plan that provides for participant-directed investments. Instead, it ensures that plan fiduciaries retain responsibility – and accountability – for the prudent selection and monitoring of plan investment options in accordance with ERISA's stringent fiduciary obligations. This interpretation is underscored in the preamble to the regulation, and has been consistently adhered to by the Secretary in briefs and opinion letters. It is therefore entitled to controlling deference and the district court erred in holding to the contrary.

ARGUMENT

I. ALLEGATIONS THAT FIDUCIARIES IMPRUDENTLY SELECTED INVESTMENT CHOICES THAT CHARGED EXCESSIVE FEES IN RELATION TO THE SERVICES PROVIDED PLAUSIBLY STATE AN ERISA CLAIM FOR FIDUCIARY BREACH

ERISA is a comprehensive statute designed to promote the interests of employees and their beneficiaries in employee benefit plans. Shaw v. Delta Air Lines, Inc., 463 U.S. 85, 90 (1983). It does this primarily by imposing a number of stringent duties on plan fiduciaries, including a duty of loyalty, a duty to act for the exclusive purposes of providing plan benefits and defraying reasonable expenses, and a duty of care grounded in the trust law's prudent man standard. 29 U.S.C. § 1104(a)(1)(A), (B). And ERISA grants plan participants and their beneficiaries "ready access to the Federal courts," 29 U.S.C. § 1001(b), to enforce these fiduciary duties and to recover plan losses stemming from the breach of these duties. Id. §§ 1109, 1132(a)(2).

To state a claim under ERISA, as elsewhere, Fed. R. Civ. P. 8(a) "'requires only a short and plain statement of the claim showing that the pleader is entitled to relief,' in order to 'give the defendant fair notice of what the . . . claim is and the grounds upon which it rests.'" Phillips v. County of Allegheny, 515 F.3d 224, 231 (3d Cir. 2008) (quoting Bell Atlantic v. Twombly, 550 U.S. 544, 555 (2007)). To meet this standard and survive a

motion to dismiss under Fed. R. Civ. P. 12(b)(6), "a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" Ashcroft v. Iqbal, 129 S. Ct. 1937, 1949 (2009) (quoting Twombly, 550 U.S. at 570). The plausibility standard articulated in Twombly merely "reflects the threshold requirement of Rule 8(a)(2) that the 'plain statement' possess enough heft to 'sho[w] that the pleader is entitled to relief.'" Twombly, 550 U.S. at 231 (alteration in original) (quoting Conley v. Gibson, 355 U.S. 41, 47 (1957)).

The plausibility standard is not a "probability requirement." Iqbal, 129 S. Ct. at 1949; Phillips, 515 F.3d at 234. A district court may not dismiss a complaint "merely because it appears unlikely that the plaintiff can prove those facts or will ultimately prevail on the merits." Phillips, 515 F.3d at 231. Instead, when presented with well-pleaded factual allegations, a district court "should assume their veracity and then determine whether they plausibly give rise to an entitlement to relief." Iqbal, 129 S. Ct. at 1950. Thus, the court's task is simply to assess whether, drawing all reasonable inferences in the plaintiffs' favor, the factual allegations in the complaint plausibly state a claim for relief. As the Supreme Court explained in Twombly, the plausibility standard merely clarifies that fair notice of the

grounds for a claim is still the measure by which the adequacy of a pleading is judged. 550 U.S. at 557.

The plaintiffs allege in their amended complaint that defendants are Plan fiduciaries and that they breached their fiduciary duty of prudence because a substantial majority of the investment options offered by the Plan charged fees that were excessive considering the services provided. In particular, the plaintiffs allege that because of a faulty selection process the defendants "failed to recognize that, given the size of the Plan, the costs were excessive in light of the services provided," and failed to consider "far less expensive" options "that provided the same or similar services." SAC ¶ 50.

The Secretary's previous pronouncements support the plausibility of the participants' assertion that the fiduciaries were imprudent if, as they allege, they failed to consider lower cost institutional funds or use their institutional leverage to secure lower fees or greater services for the investment fees the Plan participants are charged. See, e.g., Letter from the Pension and Welfare Benefits Administration, U.S. Department of Labor, to Douglas O. Kant, 1997 WL 1824017, at *2 (Nov. 26, 1997) ("plan fiduciaries must consider, among other things, any costs or fees associated with the investments, and their effect on investment returns to the plan

participants and beneficiaries"); Study of 401(k) Plan Fees & Expenses, Pension Welfare Benefit Administration (Apr. 13, 1998)("institutional mutual funds typically charge lower expense ratios than do the retail funds with similar holdings and risk characteristics" and this can result in substantial savings for "very large plans," those with assets over $500 million). Other economic research and academic literature likewise support that fee levels are an important component in the consideration of overall plan performance. See Estelle James, Gary Ferrier, James Smalhout, and Dimitri Vittas, Mutual Funds and Institutional Investments: What is the Most Efficient Way to Set Up Individual Accounts in a Social Security System?, National Bureau of Economic Research ("NBER") Working Paper 7049, p. 16[2]; see also Sarah Holden and Michael Hadley, Investment Company Institute Research Fundamentals, The Economics of Providing 401(k) Plans: Services, Fees, and Expenses, 2007, Vol. 17, No. 5, 6-12 (Dec. 2008)[3] 401(k) plan participants tend to be invested in low-cost, "no load" funds); Hewitt Associates, Be a Responsible Fiduciary: Ask the Right Questions About 401(k) Plan Fees, (Oct. 2008);[4] Hewitt Associates,

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[2] Available at http://www.nber.org/papers/w7049.

[3] Available at http://www.icief.org/pdf/fm-v18n6.pdf.

[4] Available at http://www.hewittassociates.com/_MetaBasicCMAssetCache_/Assets/Articles/2008/Hewitt_POV_401K_1_online.pdf.

Building the Ideal 401(k) Plan: Providing Optimal Accumulation and Effective Distribution, (Oct. 2008).[5]

Consideration of fee levels is important because, under common circumstances, an annual fee of 1% can reduce retirement accumulations by 20% for a lifetime contributor. Estelle James, James Smalhout, and Dimitri Vittas, Development Research Group, the World Bank, Administrative Costs and the Organization of Individual Retirement Account Systems: A Comparative Perspective, p. 4 (2005)[6] ("[t]he institutional market, which caters to large investors, benefits from scale economies without large marketing costs, hence its total costs are much lower"). As researchers have found, "[t]he same assets can be amassed with much lower distribution and record-keeping expenses from large institutions than from small individuals." Mutual Funds and Institutional Investments, p.16. In this case, the plaintiffs allege that the Plan holds more than $2 billion in assets, making it a large institutional investor. Not surprisingly, large institutional investors often taken advantage of their size to secure lower fees (or greater

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[5] Available at http://www.hewittassociates.com/_MetaBasicCMAssetCache_/Assets/Articles/2009/hewitt_pov_ideal401k_0109.pdf.

[6] Available at http://www.nabe.com/ps2000/jamescst.pdf.

services) See Mutual Funds and Institutional Investments, p. 12 (expense ratios fall as total assets in fund increase).

So too with ERISA plans, "[t]he size of the plan in terms of assets and participants and the average account balance are key factors in the pricing of fund services." The Economics of Providing 401(k) Plans, p. 17 n.49; Robert C. Pozen, The Mutual Fund Business 359 (2nd ed. 2002) (noting that plan fiduciaries are putting pressure on the price structure of mutual funds, saying that their plans deserve the lower prices they pay in the institutional market to reflect the economies of scale they bring, and that they deserve a significant price break on the distribution fees because they are bringing thousands of investors to the fund at once).

We point out this literature, not to establish that the participants' allegations are necessarily correct, but rather as demonstrating that their allegations are plausible and cannot be resolved at the motion to dismiss stage. Whether particular fiduciaries acted imprudently depends on the facts and circumstances of the particular case and cannot be determined based on a mere paper review of the pleadings. That is a strong reason not to rule on the pleadings. It was therefore error for the district court to decide at this stage that under any plausible inference based on the facts as alleged, the defendants could not possibly have acted imprudently when they selected

investment options charging retail-level fees and providing retail-level services without, according to the allegations, attempting to obtain the fees (or services) that plans of comparable size are expected to secure in the institutional-fund market. Assuming the facts as pleaded are true, as the court must, the plaintiffs have adequately plead a claim for breach of fiduciary duty by the Unisys defendants and the district court here erred in holding that the amended complaint fell short of meeting the "short and plain statement" requirement of the notice-pleading standard embodied in Rule 8(a).[7]

This dismissal was especially inappropriate given the fact-intensive nature of most ERISA fiduciary-breach claims, and the near monopoly defendants often have over many of the determinative facts. E.g., Herman v. NationsBank Trust Co., 126 F.3d 1354, 1369 (11th Cir. 1997); Harley v. Minnesota Mining & Mfg. Co., 42 F. Supp.2d 898, 907 (D. Minn. 1999), aff'd, 284 F.3d 901 (8th Cir. 2002). Indeed, the Eighth Circuit recently reversed a district court's grant of a motion to dismiss in an ERISA case alleging excessive fees in terms very similar to the allegations here, recognizing the presumptive inappropriateness of dismissing a prudence

[7] This brief should not be construed as suggesting that it is per se illegal for ERISA employee benefit plans to include or only offer retail mutual fund options.

claim at the pleadings stage. Braden v. Wal-Mart, 588 F.3d 585, 595 (8th Cir. 2009).

In Braden, the court held that the plaintiff met the pleading requirements of Twombly and Iqbal and was not required to plead additional facts explaining precisely how the fiduciaries' conduct was unlawful. The court noted that, before discovery, plan participants generally lack inside information of many of the details of the fiduciary breach, but that this lack of detail was not fatal:

> Thus, while a plaintiff must offer sufficient factual allegations to show that he or she is not merely engaged in a fishing expedition or strike suit, we must also take account of their limited access to crucial information. 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.

588 F.3d at 597-98.[8]

As in Braden, the plaintiffs here allege facts that put the defendants on notice of the grounds for the claim and that are "enough to raise a right to relief above the speculative level." Twombly, 550 U.S. at 555. Moreover, the alleged facts—that the fees were excessive when measured against

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[8] The court specifically held in that case that the allegations of excessive fees did not need to spell out the process by which the plan was managed because it was reasonable to infer from what was alleged that the process was flawed. Braden, 588 F.3d at 596. The court further held that the plaintiff was not required to plead facts tending to rebut all possible lawful explanations for defendants' conduct. Id.

comparable options available in the marketplace to similarly large plans, that the Plan's size gave it leverage to obtain lower fees or higher services, but it failed to do so, that the participants did not receive a higher level of service commensurate with the level of their fees, and that the defendants failed to engage in a prudent process to select and manage these investment options – are no less detailed or plausible in giving rise to an inference of liability than those pleaded in the Braden complaint.

Moreover, the complaint in this case is distinguishable from the complaint held insufficient to state a claim in Hecker. Although the Seventh Circuit in Hecker upheld the dismissal of a complaint alleging that a somewhat similar range of fees was imprudent, the court emphasized throughout the rehearing opinion that its decision was "tethered closely to the facts before the court," 569 F.3d at 711, and was not meant to give plan fiduciaries carte blanche to select imprudent investment options so long as participants are also given some prudent investment choices. Id. at 710, 711. Most significantly, the rehearing opinion clarified that the complaint was deficient principally because the allegations that the fiduciaries offered only investments charging retail-level fees did not include allegations that they only received retail-level services, and therefore did not expressly allege that the price they paid as a large institutional investor was excessive in relation

to the services received. Id. at 711 ("the complaint is silent about the services that Deere participants received. It would be one thing if they were treated exactly like all other retail market purchasers of Fidelity mutual fund shares; it would be quite another if, for example, they received extra investment advice from someone dedicated to the Deere accounts, or if they received other extra services.").

In this case, the amended complaint specifically alleges that "the costs were excessive in light of the services provided," and that the defendants failed to consider "far less expensive" options "that provided the same or similar services." SAC ¶ 50. The amended complaint thus corrects the main deficiency that the court in Hecker found to be significant.

The district court therefore erred in viewing Hecker as holding broadly that fees within the range paid in Hecker are per se reasonable. Certainly, Hecker does not hold as a matter of law that there can never be a claim for imprudence in paying too much in fees. Furthermore, the holding that fiduciaries are not duty-bound to "scour the market" to find the lowest possible fees should not be read to mean they are free to pay any fee the market bears, without making a diligent effort to assure that they are getting reasonable services for the fees comparable to what prudently managed plans of similar size and type receive. Given the significant impact fee

levels have on the net return of investment over time, plan fiduciaries' duty to select prudent investment options necessarily includes consideration of the reasonableness of the fees charged and the services received in payment of those fees.

Even if the Hecker decision were broadly read to sanction payment of a similar range of fees, neither the Hecker court nor the court below explained why this range of fees was reasonable in light of the allegation that the Plan, a large institutional investor, could have gotten institutional rather than retail rates. Cf. Restatement (Third) of Trusts § 90 Cmt. f(1) (2007) ("Trustees, like other prudent investors, prefer (and, as fiduciaries, ordinarily have a duty to seek) the lowest level of risk and cost for a particular level of expected return—or, inversely, the highest return for a given level of risk and cost").

The Hecker holding is thus not a substitute for the "facts and circumstances" analysis appropriate to fiduciary-breach cases. Iqbal, 129 S. Ct. at 1950 (determining whether a complaint should survive a motion to dismiss is a "context-specific task that requires the reviewing court to draw on its judicial experience and common sense"). Certainly, Hecker cannot reasonably be read as establishing, as a legal proposition, that the particular range of fees for the plans' investment options in that case (.07% to just over

1%) was per se prudent, without regard to the particular facts, circumstances, and context of the particular case before the court.[9]

Whether these fiduciaries acted prudently in establishing a particular fee structure necessarily depends on myriad factual considerations and questions, most of which can only be resolved through the consideration of evidence after discovery. Relevant considerations include the particular charges for particular funds; how many and which of the funds are concentrated at the higher end of the range of fees; the relationship between the size of the fees and the level of services provided; the fees paid by plans of comparable size for comparable funds; the diligence with which the

[9] It might be one thing, for example, if virtually all of the funds were at the lower end of the cited range of fees (.1%). It is quite another, however, if most of the funds on the plan's investment menu were concentrated at the high end of the range (1.21%), or if there were equivalent but cheaper funds available at every point in the continuum of fees. In a recent article in the New York Times, John Bogle, the founder of the Vanguard Group, is quoted as stating that charges levied on mutual fund investors generally are much higher than those that the identical firms charge pension customers, an average fee of 0.08 percent to pension customers, as compared with 0.61 percent to mutual fund investors. Gretchen Morgenson, He Doesn't Let Money Managers Off the Hook, N.Y. Times, April 11, 2009, at 2009 WLNR 6839746. While both .08 percent and .61 percent fall within the range cited by the court in Hecker, it would raise a significant issue under the prudence standard if a plan fiduciary chose to pay .61 percent if he had the ready option of paying .08 percent for essentially the exact same investment. See Tibble v. Edison Intern., 2010 WL 2757153, at *30 (C.D. Ca. July 8, 2010) ("In light of the fact that the institutional share classes offered the exact same investment at a lower fee, a prudent fiduciary acting in a like capacity would have invested in the institutional share classes.").

fiduciaries compared fees for comparable funds; and generally whether the fiduciaries used a reasonable process to determine whether the particular funds were reasonable investments in light of their fees and other attributes. Rather than allow the parties to develop and present evidence on the many factors relevant to the prudence analysis, the court erroneously concluded that the mere existence of fee ratios comparable to (although higher than) those in Hecker (.07% to just over 1% in Hecker, 0.1% to 1.21% in this case) meant that the fees must be reasonable and the allegations did not even state a cognizable fiduciary-breach claim based on imprudence.[10] Nothing in ERISA establishes that a particular numerical range of fees is per se prudent, without regard to what the evidence actually shows after the plaintiffs have been given an opportunity to present their case at trial or on summary judgment.

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[10] Moreover, the court speculated that "Unisys had no incentive to waste the money that it is contributing to the plan by directing a large portion of it to a plan service provider rather than to the workers for whose benefit the plan was established." 2010 WL 1688540, at * 6. However, the plaintiffs need not allege that the defendants intentionally wasted the Plan's money to state a claim for imprudence under ERISA and survive a motion to dismiss. The pertinent inquiry is not whether the defendants intentionally caused the Plan to pay excessive fees to benefit the service providers, but whether they acted "with the care, skill, prudence, and diligence under the circumstances then prevailing" expected of a prudent fiduciary in managing a plan "of a like character and with like aims." 29 U.S.C. § 1104(a)(1)(B).

II. ERISA SECTION 404(c) DOES NOT PROVIDE A DEFESNE TO DEFENDANTS' ALLEGED IMPRUDENT SELECTION OF INVESTMENT OPTIONS WITH EXCESSIVE FEES

The district court also erred when it granted summary judgment to the defendants based on ERISA section 404(c), thereby failing to accord deference to the Secretary's regulation interpreting section 404(c). Congress enacted ERISA expressly to safeguard the "financial soundness" of employee benefit plans "by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and by providing appropriate remedies, sanctions," and, as we have noted, "ready access to the Federal courts." 29 U.S.C. § 1001(a), (b). Although ERISA fiduciaries are generally responsible for all plan losses caused by their breaches, see 29 U.S.C. §§ 1132(a)(2), 1109(a), section 404(c) provides a limited exception for losses resulting from a participant's or beneficiary's exercise of control over his or her individual account in a defined contribution plan. 29 U.S.C. § 1104(c). Under section 404(c)(1)(B), "in the case of a pension plan which provides for individual accounts and permits a participant or beneficiary to exercise control over the assets in his account, if a participant or beneficiary exercises control over the assets in his account (as determined under regulations of the Secretary) . . . no person who is otherwise a fiduciary shall be liable under this part for any loss, or by reason of any breach, which

results from such participant's or beneficiary's exercise of control." Id. § 1104(c)(1)(B) (emphasis added).

Under the terms of the Act and the Secretary's 404(c) regulation, plan fiduciaries are shielded only for losses "which result[] from" the participant's exercise of control and not from losses caused by their own fiduciary misconduct. 29 U.S.C. § 1104(c)(1)(B); 29 C.F.R. § 2550.404c-1. Consequently, section 404(c) does not give fiduciaries a defense to liability for their own imprudence in the selection or monitoring of investment options available under the plan. The selection of the particular funds to include and retain as investment options in the Plan was the responsibility, and indeed solely within the power of the fiduciaries, and logically precedes (and thus cannot "result from") a participant's decision to invest in any particular option. It was the fiduciaries' responsibility to choose investment options in a manner consistent with the core fiduciary duties of prudence and loyalty. If they have done so, section 404(c) relieves them from liability for losses that "result from" the participants' exercise of authority over their own accounts. If, however, as alleged here, the funds offered to the participants were imprudently selected or monitored, the fiduciaries remain liable for the losses attributable to their own imprudence.

This straightforward interpretation of the statute is reflected in the 404(c) regulation, which provides: "If a plan participant or beneficiary of an ERISA section 404(c) plan exercises independent control over assets in his individual account in the manner described in [the regulation]," then the fiduciaries may not be held liable for any loss or fiduciary breach "that is the direct and necessary result of that participant's or beneficiary's exercise of control." 29 C.F.R. § 2550.404c-1(d)(2)(i); see also 29 C.F.R. § 2550.404c-1(b)(2)(i)(B)(1)(i).

The preamble to the regulation explains that:

> the act of designating investment alternatives . . . in an ERISA section 404(c) plan is a fiduciary function to which the limitation on liability provided by section 404(c) is not applicable. All of the fiduciary provisions of ERISA remain applicable to both the initial designation of investment alternatives and investment managers and the ongoing determination that such alternatives and managers remain suitable and prudent investment alternatives for the plan.

57 Fed. Reg. 46,922 (Oct. 13, 1992). The preamble further explains, in a footnote, that the fiduciary act of making a plan investment option available is not a direct and necessary result of any participant direction, and thus not subject to the 404(c) defense:

> In this regard, the Department points out that the act of limiting or designating investment options which are intended to constitute all or part of the investment universe of an ERISA 404(c) plan is a fiduciary function which, whether achieved through fiduciary designation or express plan language, is not a direct or necessary result of any participant direction of such plan. Thus, . . . the plan fiduciary has a

> fiduciary obligation to prudently select . . . [and] periodically evaluate the performance of [investment] vehicles to determine . . . whether [they] should continue to be available as participant investment options.

Id. at 46,922 n.27. In other words, although the participants in such defined contribution plans are given control over investment decisions among the options presented to them, the plan fiduciaries nevertheless retain the duty to prudently choose and monitor the investment options, and the responsibility for those choices.[11]

This regulatory interpretation is consistent with ERISA's purposes and overall structure, which place stringent trust-based fiduciary duties at the heart of the statutory scheme. See 29 U.S.C. §§ 1001(b), 1104. Under this regulatory structure, fiduciaries are defined not simply by their titles, but also functionally, based on the discretionary authority they are granted and

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[11] The Secretary has adhered to this interpretation in numerous regulatory pronouncements and amicus briefs. See, e.g., Department of Labor Opinion Letter No. 98-04A, 1998 WL 326300, at *3, n.1 (May 28, 1998); Letter from the Pension and Welfare Benefits Administration, U.S. Department of Labor, to Douglas O. Kant, 1997 WL 1824017, at *2 (Nov. 26, 1997); Braden v. Wal-Mart, Brief of the Sec'y of Labor as Amicus Curiae in Support of the Plaintiffs-Appellants, available at http://www.dol.gov/sol/media/briefs/braden(A)-03-13-2009.pdf; Hecker v. Deere & Co., Amended Brief of the Sec'y of Labor as Amicus Curiae in Support of the Plaintiffs-Appellants, available at http://www.dol.gov/sol/media/briefs/deere(A)-04-02-2008.htm; Tittle v. Enron Corp., Amended Brief of the Sec'y of Labor as Amicus Curiae Opposing Motion to Dismiss, available at http://www.dol.gov/sol/media/briefs/enron(A)-8-30-02.htm.

the control they exercise over the plan and its assets. See 29 U.S.C. § 1002(21). Thus, the Supreme Court has noted that ERISA "allocates liability for plan-related misdeeds in reasonable proportion to the respective actor's power to control and prevent the misdeeds." Mertens v. Hewitt Assocs., 508 U.S. 248, 262 (1993). Consistent with these principles, the statute provides that if a fiduciary exercises control over the plan or its assets, it must do so prudently and loyally, and the fiduciary is relieved from liability only in the limited circumstances where the control that the fiduciary would otherwise have exercised is properly delegated to and exercised by someone else. See, e.g., section 405(c)(1), 29 U.S.C. § 1105(c)(1) (permitting the named fiduciary in some circumstances to designate other fiduciaries to carry out specific functions, and relieving the named fiduciary of liability except with respect to appointing or monitoring the designee); 29 C.F.R. § 2550.408b-2(e)(2) (explaining that a fiduciary does not self-deal under section 406(b)(1) if "the fiduciary does not use any of the authority, control, or responsibility which makes such person a fiduciary to cause the plan to pay additional fees"). The Secretary's 404(c) regulation and her interpretation of that regulation are consistent with, and indeed best serve, these statutory principles. Certainly, the participants in this case were in no position to use the bargaining power associated with the

management of a $2 billion plan to secure the best deal for Plan participants. Only the Plan's fiduciaries could comparison shop between competing funds, negotiate a proper fee structure, and construct a prudent fund menu. If the fiduciaries failed to do so, they and not the Plan's participants are appropriately held accountable for the resulting losses.

The district court relied on the Third Circuit's decision in In re Unisys Sav. Plan Litig., 74 F.3d 420, 445 (3d Cir. 1996), for the proposition that "section 1104(c) applies even when a fiduciary breaches its duty by selecting an inappropriate fund for the Plan." Renfro, 2010 WL 1688540, at *8 (citing Unisys, 74 F.3d at 445). That earlier Unisys decision (which was unrelated to this case) does not, however, support this proposition. In fact, the Unisys court held that the defendants there were not "entitled to summary judgment on its section 404(c) defense." Id. at 446. In reaching this conclusion, the Unisys court noted, in dicta, that section 404(c) "allows a fiduciary, who is shown to have committed a fiduciary breach in making an investment decision, to argue that despite the breach, it may not be held liable because the alleged loss resulted from a participant's exercise of control." Id. at 445 (emphasis added). But the court acknowledged that the statutory text "neither defines nor clarifies its central element—the 'control' a pension plan may permit a participant or beneficiary to exercise." Id. It is such

"control," (or lack thereof) that determines the applicability of the section 404(c) defense in any given case. This dicta is thus fully consistent with the Secretary's regulatory interpretation of the concept of control in this case.

The district court thus erred in holding that deference to the Secretary's regulatory interpretation was inappropriate under Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 842-43 (1984), because the Unisys court's decision was based on the "plain language" of the statute. First, because the panel ultimately held that Unisys had not shown that the participants in fact exercised "control" as required by the statute, and thus was not entitled to the section 404(c) defense, the court's interpretation of 404(c)'s language in that case was dicta that is not binding on this panel. In any event, the Unisys decision recognized that the key statutory term, "control," is ambiguous. Thus, even if this reasoning were part of the holding rather than simply dicta in the case, "[a] court's prior judicial construction of a statute trumps an agency construction otherwise entitled to Chevron deference only if the prior court decision holds that its construction follows from the unambiguous terms of the statute and thus leaves no room for agency discretion." Nat'l Cable & Telecom. Ass'n v. Brand X Internet Servs., 545 U.S. 967, 982 (2005) (emphasis added); Levy v. Sterling Holding Co., LLC, 544 F.3d 493, 502-03 (3d Cir. 2008), cert. denied, 129 S.

Ct. 2827 (2009). Significantly, the Unisys court noted that because the conduct took place before the regulation's effective date, the regulation "does not apply or guide our analysis in this case." Id. at 444 n.21.

The 404(c) regulation does guide the analysis here. It was issued after notice-and-comment rulemaking pursuant to an express delegation of authority to the Secretary to determine the circumstances under which "a participant or beneficiary exercises control over the assets in his account." 29 U.S.C. § 1104(c). Because ERISA section 404(c) expressly granted the Secretary ample "room for agency discretion," her regulation is entitled to controlling deference under Chevron. See Long Island Care at Home v. Coke, 551 U.S. 158, 171-72 (2007); United States v. Mead Corp., 533 U.S. 218, 229-30 (2001).

The Secretary's interpretation of section 404(c) and of her own regulation is likewise entitled to the highest degree of deference because it is longstanding and consistently held, thoroughly considered, and based on the Secretary's consideration of relevant policy concerns. See, e.g., Yellow Transp., Inc. v. Michigan, 537 U.S. 36, 45 (2002) (giving Chevron deference to an agency's interpretation of a federal statute that was made in explanatory statement announcing the promulgation of the regulation rather than the regulatory text). The preamble language explaining the scope of the

regulatory and statutory exemption, and declining to shield fiduciaries from liability for losses attributable to their own imprudent selection and monitoring of investment options represents the Secretary's authoritative interpretation of her own regulation and was itself the product of the same notice-and-comment rulemaking. The Supreme Court has stressed the strength and importance of deference in such circumstances, Geier v. Am. Honda Motor Co., Inc., 529 U.S. 861, 877-80 (2000) (giving controlling deference to interpretation in preamble), and consistently has given controlling weight even to interpretations of regulations that were made later in much less formal settings. See Long Island Care, 551 U.S. at 171 (controlling deference to agency's interpretation of regulation set out in an advisory memorandum in response to litigation); Auer v. Robbins, 519 U.S. 452, 462 (1997) (controlling deference to an interpretation made for the first time in a legal brief).

Even to the extent that the statutory language – which limits the section 404(c) defense to losses that "result[] from a participant's exercise of control" – leaves open how strict a standard of causation ought to apply, the Secretary's resolution of that issue ought to prevail. See Brand X, 545 U.S. at 982 (Chevron established a "'presumption that Congress, when it left ambiguity in a statute meant for implementation by an agency, understood

that the ambiguity would be resolved, first and foremost, by the agency, and desired the agency (rather than the courts) to possess whatever degree of discretion the ambiguity allows'") (quoting Smiley v. Citibank (South Dakota), N.A., 517 U.S. 735, 740-41(1996)). As explained above, there are good policy reasons to conclude that losses that flow from a fiduciary's imprudent selection of investment options with excessive fees should be understood to result from the fiduciary's decisions rather than the individual participant's subsequent decision to select a flawed option. The Secretary's regulation sensibly draws the line between losses that "result from" a participant's own imprudence while exercising independent control and those that do not.

If, as alleged, the defendants violated their fiduciary duties by selecting investment options with excessive fees, section 404(c) provides no defense to their fiduciary misconduct. The district court thus erred in holding that ERISA section 404(c) immunizes fiduciaries from liability for any resulting losses as the basis for dismissing the plaintiffs' claims.

CONCLUSION

For the foregoing reasons, the Secretary respectfully requests that the Court reverse the decision of the district court.

Respectfully submitted,

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CERTIFICATION OF BAR MEMBERSHIP

Pursuant to Local Rules 28.3(d) and 46.1(e), the undersigned counsel certifies that she has been admitted to this Court.

_/s/____________________
Elizabeth Hopkins
Dated: September 16, 2010

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I certify that on this 16th day of September, 2010, I caused the Brief of the Secretary of Labor as Amicus Curiae to be electronically filed via the Court's CM/ECF system. I further certify that I caused 10 copies of the Brief to be dispatched to the Clerk of this Court by Federal Express. I certify that I served of this Brief electronically on the following counsel of record:

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