UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

UNITED STATES SECURITIES AND EXCHANGE COMMISSION,	)	
Plaintiff,	)	
v.	)	Case No. 1:06-cv-04859 Hon. Robert W. Gettleman
AA CAPITAL PARTNERS, INC. AND JOHN A. ORECCHIO,	)	
Defendants.	)	

BRIEF OF THE SECRETARY OF LABOR AS AMICUS CURIAE IN OPPOSITION TO THE GENERAL PARTNERS' MOTION FOR ATTORNEYS' FEES IN THE MILLWRIGHTS CASE

INTEREST OF THE SECRETARY OF LABOR

The General Partners' motion in this case (Docket No. 468) for the release of funds to pay attorneys' fees and defense costs in Millwrights' Local No. 1102 Supplemental Pension Fund, et al. v. AA Private Equity Investors Management LLC, et al., Case No. 08-cv-7183 (N.D. Ill.), raises an important issue concerning the scope of section 410 of the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. § 1110, which voids any agreements or instruments that purport to relieve fiduciaries of their liabilities and responsibilities under ERISA. The Secretary of Labor has primary authority for enforcing and interpreting Title I of ERISA and, therefore, a direct interest in ensuring the proper treatment of indemnification arrangements that may be void under section 410.

The Trustees of the Millwrights' Local No. 1102 Supplemental Pension Fund (MSPF) brought their case under ERISA to, among other things, recover losses to the MSPF allegedly caused by the General Partners' fiduciary breaches. Moreover, on April 10, 2008, the Secretary brought her own suit against some of the same defendants in the Millwrights case, making

additional and related allegations of ERISA violations against them.[1] Because this Court's ruling is likely to affect the ability of the plaintiffs in the Millwrights case to obtain a full recovery, even if they are successful, and may likewise affect the Secretary's related suit with regard to the plans in this case, the Secretary has a strong interest in presenting her views on the proper resolution of the indemnification issue.

The question addressed by the Secretary in this brief is whether, consistent with ERISA section 410, a general partnership serving as investment manager to ERISA plans can enforce indemnification provisions contained in limited partnership agreements between it and the limited partners (the plans) to the extent the indemnification provisions would effectively release the general partnership and its principal employees from ERISA liability for breaching their fiduciary duty to the plans' participants or permit the advancement of defense fees from plan assets without any showing of an ability to reimburse the ERISA-covered plans in the event they are found liable. In particular, the brief addresses concerns the Secretary has regarding the indemnification provision in each of the Limited Partnership Agreements (LPAs) at issue in this case, which expressly exclude indemnification where there has been a final adjudication finding that the indemnitee acted with gross negligence or willful misconduct or in breach of their fiduciary duty to the Partnership. See Fund I LPA § 12 (Attachment B); Fund II LPA § 12 (Attachment C). The indemnification provisions also provide for repayment in the event the indemnitee is found liable for a fiduciary breach covered by the aforementioned exclusion. Id.

The fiduciary-breach exclusion is contrary to ERISA to the extent it is read as permitting indemnification so long as the indemnitees are found to have not violated their non-ERISA fiduciary duties toward the General Partnership. As is evident from the suit brought by a limited partner (the Millwrights) against the General Partners, the General Partnership's interest is not

---

[1] The Secretary has alleged that AA Capital Partners, Inc., John Orecchio, Mary Elizabeth Stevens, and AA Capital Liquidity Management, LLC breached their ERISA fiduciary duties by, among other things, spending plan assets for non-plan purposes in violation of ERISA sections 404(a)(1)(A) and 406(a)(1)(D), (b)(1) & (b)(2), and paying unauthorized fees in violation of ERISA sections 404(a)(1)(A) & (D) and 406(b)(1) & (2). The Secretary seeks a court order directing the defendants to restore all losses, disgorge all ill-gotten gains, and correct the prohibited transactions, and permanently enjoining the defendants from serving as fiduciaries or service providers to any ERISA-covered employee benefit plan. See First Amended Complaint filed in Chao v. AA Capital Partners, Inc., Case No. 1:08-cv-02029 (N.D. Ill.) (Docket No. 28) (Attachment A).

necessarily aligned with the plans or their participants. Furthermore, while each LPA requires the General Partners to execute an undertaking prior to receiving advanced attorneys' fees, there is no requirement that the General Partners provide proof of ability to repay the fees in the event they are found not to be entitled to indemnification. For these reasons, the indemnification provision found in each LPA is valid under ERISA section 410 only if it is read to preclude indemnification where the General Partners are found to have breached their ERISA fiduciary duties. In addition, absent this Court's requiring proof of ability to repay in the event of liability, the advancement of attorneys' fees under the indemnification clause is impermissible because it would effectively insulate the General Partners from liability for breach of their ERISA fiduciary duties.

STATEMENT OF FACTS

1. AA Capital is an investment management firm that primarily provides investment management and advisory services to ERISA-qualified union pension plans ("ERISA Plans"), including the MSPF. See First Amended Complaint filed in Chao v. AA Capital Partners, Inc., Case No. 1:08-cv-02029 (N.D. Ill.) ("Sec. Comp.") ¶¶ 4-5; Complaint filed in Millwrights' Local No. 1102 Supplemental Pension Fund, et al. v. AA Private Equity Investors Management LLC, et al., Case No. 08-cv-7183 (N.D. Ill.) ("Millwrights Comp.") ¶¶ 21-22 (Attachment D). AA Capital served as the "investment manager" of the ERISA Plans' assets entrusted to it for purposes of section 3(38) of ERISA, 29 U.S.C. §1002(38). Sec. Comp. ¶¶ 6-9; Millwrights Comp. ¶¶ 21-22, 26-27, 34-35. As the Secretary and the Millwrights allege, AA Capital and its employees established a number of affiliated limited partnerships and limited liability companies through which they controlled and personally profited from the investment of the ERISA Plans' assets.

Specifically, AA Capital and its principals established several private equity funds (the Funds), including AA Capital Equity Fund, LP (Fund I) and AA Capital Equity Fund II, LP (Fund II), as limited partnerships governed by the LPAs. Sec. Comp. ¶¶ 17, 27, 28; Millwrights Comp. ¶¶ 23-24, 29, 32. AA Capital then invested the ERISA Plans' assets in the Funds. Sec. Comp. ¶ 30. The ERISA Plans "subscribed" to the Funds pursuant to the LPAs, becoming "limited partners" in the Funds that collectively hold the majority of each Fund's equity interest. Sec. Comp. ¶ 30-31; Millwrights Comp. ¶¶ 25, 33. The minority equity interest in each Fund is

held by a "General Partner" – a limited liability company comprised of senior AA Capital employees that is solely responsible for operating the Funds and investing the Funds assets. Sec. Comp. ¶¶ 17-18; Millwrights Comp. ¶¶ 5-6, 24, 32. The General Partner is entitled to receive a percentage of any profits remaining after the investors recover their full contributions plus a preferred return on the money invested. Millwrights Comp. ¶¶ 30-31, 38-39.

2. The LPAs for Fund I and Fund II both contain general exculpation provisions stating that, "[t]o the furthest extent permitted by applicable law," the individual General Partners shall not be liable "for any loss, damage, liability, interest, penalty, cost and expense (including, without limitation, attorneys' fees)" that relate to their involvement in the Partnership if the individual seeking exculpation determines that their "conduct was in or not opposed to the best interest of the Partnership" and the conduct "did not constitute a breach of such Person's fiduciary duty to the Partnership, a material breach of this Agreement, fraud, or unlawful misconduct of such Covered Person." Fund I LPA, First Amendment to § 12.1.1(a) at p. 1; Fund II LPA at § 12.1.1(a). Fund II's LPA additionally specifically states that "applicable law" includes ERISA. Fund II LPA at § 12.1.1(a).

The LPAs also include a broad, similarly worded indemnification provision which states that, "[t]o the furthest extent permitted by applicable law," the General Partners "shall be indemnified and held harmless, subject to the other provisions of this Agreement, by the Partnership (only out of Partnership assets, including the proceeds of liability insurance)" against any claim in connection with any action that relates to their involvement in the Partnership. Fund I and Fund II LPAs at § 12.2.1. However, indemnification is not available where the indemnitee has been finally adjudicated "not to have acted in the reasonable belief that the Indemnitee's action was in, or not opposed to, the best interests of the Partnership or to have acted with unlawful misconduct, or in breach of such Person's fiduciary duty to the Partnership." Fund I LPA, First Amendment to § 12.2.2 at p. 2; Fund II LPA at § 12.2.2. "Partners" is a defined term encompassing the General Partners and the limited partners, including the ERISA Plans that invested in the AA Capital Partners Funds. See, e.g., Fund I LPA Appendix I (Definitions) at p. 6 (Attachment E). The LPAs further provide for advanced payment of expenses upon receipt of an enforceable undertaking to repay the payment if the indemnitee is determined to not be entitled to indemnification pursuant to Article 12. Fund I and Fund II LPA at § 12.2.4.

3. On September 8, 2006, the Securities and Exchange Commission (SEC) brought an emergency enforcement action under the Investment Advisers Act of 1940, 15 U.S.C. § 80, to halt ongoing fraudulent conduct by AA Capital Partners and its president (collectively, the "defendants"). (Docket No. 1 at ¶¶ 1, 11-13). The SEC alleges that the defendants misappropriated at least $10.7 million from their clients. Id. Shortly after the complaint was filed, the Court appointed a Receiver over the firm's assets (Docket No. 21). The Receiver order vests the Receiver with broad power to oversee all aspects of AA Capital's operations, including full power over all funds, assets, causes of action, books, records and other property belonging to or in the possession or control of AA Capital. The Receiver now holds the accounts of the General Partnerships and has control over the Funds. On October 30, 2008, this Court held (Docket No. 428) that, with respect to Fund I, the LPA requires the Receiver to release money from the accounts it holds on behalf of the partnerships so that the General Partner may pay its lawyers, and instructed the General Partner to file a more detailed request for attorneys' fees.

On December 16, 2008, one of the union pension plans that had engaged AA Capital as an investment manager and is a limited partner of Fund II (hereafter, the "Millwrights") filed a suit against the General Partnerships of two funds (Fund I and Fund II) and various current or former employees of defendant AA Capital Partners, Inc., alleging violations of ERISA's prohibited transaction provisions with respect to the creation of the Fund I and Fund II General Partnerships. Millwrights' Local No. 1102 Supplemental Pension Fund, et al. v. AA Private Equity Investors Management LLC, et al., Case No. 08-cv-7183 (N.D. Ill.). The Millwrights allege that AA Capital invested the pension investors' assets in an arrangement by which its individual officers and employees, through the construct of the General Partnerships, took ownership of a portion of the pension investors' assets, and further allege that this transfer to ERISA parties in interest is a prohibited transaction under section 406 of ERISA, 29 U.S.C. §1106. Millwrights' Comp. ¶¶ 43-44.

On February 4, 2009, the General Partners of Funds I and II filed a motion in this SEC case for payment of attorneys' fees incurred in the Millwrights case and a supporting memorandum (Docket Nos. 468 & 469). Specifically, the General Partners seek an order directing the Receiver to release funds from Funds I and II necessary for the General Partners to retain and pay counsel in connection with the defense of the Millwrights case. The General Partners argue that the Receiver's refusal to release funds necessary for them to retain and pay

counsel in the Millwrights litigation is inconsistent with the LPAs, the Management Agreements and the Court's October 30, 2008 Order. General Partners' Motion at 2 (Docket No. 468), General Partners' Memorandum in Support of Motion (GP Memo) at 1, 6 (Docket No. 469).

The Receiver, the Millwrights, and two other union limited partners filed objections (Docket Nos. 486, 488, 490, 491). Among other things, the Receiver (Docket No. 490 at 7-8) and the Millwrights (Docket No. 491 at 12) argue that the General Partners' contractual claim to fees violates ERISA section 410's express prohibition on contractual provisions that purport to relieve a fiduciary from "responsibility or liability for any responsibility, obligation, or duty" under ERISA. 29 U.S.C. § 1110(a).

ARGUMENT

THIS COURT SHOULD DENY THE GENERAL PARTNER'S REQUEST FOR ATTORNEYS' FEES IN THE MILLWRIGHTS SUIT BECAUSE ADVANCE PAYMENT OF LEGAL FEES INCURRED IN THE DEFENSE OF THE ERISA CLAIMS AGAINST THE GENERAL PARTNERS WOULD VIOLATE ERISA SECTION 410

ERISA is a comprehensive statute designed to promote the interests of employees and their beneficiaries in employee benefit plans by establishing standards of conduct, responsibility, and obligations for fiduciaries. 29 U.S.C. § 1001(b); Shaw v. Delta Air Lines, Inc., 463 U.S. 85, 90 (1983). At the core of ERISA's fiduciary obligations are the duties of loyalty and prudence, which are based on trust law principles, and are among the "highest known to law." Donovan v. Bierwirth, 680 F.2d 263, 272 n.8 (2d Cir. 1982); see also Harzewski v. Guidant, 489 F.3d 799, 805 (7th Cir. 2007) ("[t]he duty of care, diligence, and loyalty imposed by the fiduciary principle is far more exacting than the duty imposed by tort law . . ."); Armstrong v. LaSalle Bank Nat'l Assoc., 446 F.3d 728, 732 (7th Cir. 2006) ("[t]he duty of an ERISA trustee to behave prudently in managing the trust's assets . . . is fundamental"). To assure that ERISA fiduciaries are held to the highest standards, ERISA section 410(a) provides that "any provision in an agreement or instrument 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." 29 U.S.C. § 1110(a). Thus, ERISA section 410 invalidates any instruments or agreements that exculpate plan fiduciaries from liability for their misconduct, and thereby seeks "to avoid provisions which circumvent express statutory requirements to the detriment of Plan

beneficiaries." Wells Fargo Bank v. Bourns, Inc., 860 F. Supp. 709, 716 (N.D. Cal. 1994); see also Chicago Board Options Exchange, Inc. v. Connecticut General Life Ins. Co., 713 F.2d 254, 259 (7th Cir. 1983) ("As the legislative history of this provision makes clear, 'exculpatory provisions which relieve a fiduciary from liability for breach of the fiduciary responsibility are to be void and of no effect.'") (citing H.R.Rep. 1280, 93d Cong., 2d Sess., *reprinted in* 1974 U.S.Code Cong. & Ad. News 4639, 5038, 5101).

.As we explain below, the indemnification provisions, to be valid under section 410, must be read as forbidding indemnification where the indemnitees are found to have committed fiduciary breaches under ERISA; otherwise, they are invalid since none of the insurance options permitted by section 410 or by the Secretary's interpretation of 410 applies. In any event, section 410 forbids advancement of attorneys' fees where, as here, there is no proof of ability to repay. Therefore, the Court should deny the General Partners' motion for attorneys' fees in the Millwrights suit.

A. The indemnification provisions are enforceable under ERISA section 410 only to the extent they are read to preclude indemnification if the indemnitees are found to have breached their ERISA fiduciary duties

1. The scope of the indemnification provisions are limited by Section 410's prohibitions on exculpating ERISA fiduciary liability.

In Millwrights, the defendants are accused of breaching their fiduciary duties under ERISA sections 406(a)(1)(B)&(D) and 406(b)(1), (2) & (3), 29 U.S.C. §1106(a), (b), by engaging in transactions (the transfer of plan assets to AA Capital employees, who are themselves general partners and thus parties in interest to the limited partners' plans) that are expressly prohibited by ERISA (subject to certain exceptions set forth in section 408, 29 U.S.C. §1108).[2] Millwrights Comp. ¶ 43. The General Partners now seek to have their defense fees

[2] The Millwrights allege that the MSPF is a "pension plan" as defined in ERISA, 29 U.S.C. § 1002(2)(A). Millwrights Comp. ¶¶ 2, 22. Because AA Capital had complete discretion and control over the investment of the Millwrights' assets, AA Capital, its principals and senior employees are ERISA fiduciaries. Id.; 29 U.S.C. §1002(21)(A). The Millwrights allege that AA Capital's creation of the Funds violated ERISA's prohibited transaction provisions because AA Capital's principals and senior employees – who were ERISA fiduciaries with respect to the plan assets of the ERISA investors – through their interest in the General Partners acquired a personal

advanced to them from the Funds under LPAs that purport to require the Funds to bear such costs. This request raises serious questions of compliance with section 410.

As a threshold matter, enforcement of the indemnification provisions here is permissible under ERISA section 410 only if the provisions are read to preclude indemnification in the event the indemnitees are found to have breached their ERISA fiduciary duties. Such a reading is warranted because the general exculpation provision in the LPAs states that indemnification is available only "[t]o the furthest extent permitted by applicable law," Fund I and Fund II LPAs § 12.1.1(a), and is not available where there has been a final adjudication that the indemnitee acted with "unlawful" or "willful" misconduct, id. at § 12.2.2. Unless the provisions are read to preclude indemnification where the General Partners are found to have breached their ERISA fiduciary duties, they are void under ERISA section 410 and cannot be used to relieve the General Partners of their liability if the Millwrights' allegations of numerous serious breaches of their fiduciary duties to the plans are upheld.

Insofar as the Funds contain plan assets, as the Millwrights have alleged, the General Partners are ERISA fiduciaries and any Fund proceeds that are used to pay for their legal expenses – to defend in a suit in which they are accused of fiduciary misconduct with respect to the Funds – will reduce the value of the MSPF plan assets proportionately. It would be wholly inconsistent with section 410's text and protective purposes to enforce indemnification provisions that would operate to require an injured plan and its participants to foot the bill for a fiduciary defendant's misconduct and for the defense of a case involving such misconduct. See IT Corp. v. General Am. Life Ins. Co., 107 F.3d 1415, 1418 (9th Cir. 1997) (recognizing that "a contract exonerating an ERISA fiduciary from fiduciary responsibilities is void as a matter of law" under section 410); Wells Fargo Bank, 860 F. Supp. at 716 ("In rendering void as against public policy certain exculpatory agreements, ERISA § 410 seeks to avoid provisions which circumvent express statutory requirements to the detriment of Plan participants."); Leigh v. Engle, 619 F.Supp. 154, 158 (N.D. Ill. 1985) ("Indemnification from liability for breach of fiduciary duty by a trust is not allowed under ERISA") (citing Chicago Board Options Exchange, 713 F.2d at 254).

---

interest in the pension plan assets entrusted to the management of AA Capital. Millwrights Comp. ¶¶ 1, 15, 24, 30-32, 38-39, 43. The individual General Partners each own one percent of their respective Fund and each also has an interest in a percentage of the Fund's profits. Id. at ¶¶ 16, 24, 30-32, 38-39; 29 U.S.C. §1002(14)(H) (defining employee of service provider as "party in interest").

Here, the wording of the indemnification agreements is at best ambiguous and at worst impermissibly broad. They specify that the General Partners will be indemnified so long as their conduct did not constitute a breach of fiduciary duty to the Partnership, fraud, negligence, or unlawful or willful misconduct. But a fiduciary's actions with respect to a plan need not rise to this level to constitute a fiduciary breach. A fiduciary breaches his duties under ERISA where he fails 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 in the conduct of an enterprise of a like character and with like aims." See 29 U.S.C. § 1104(a)(1)(B). Fiduciaries need not engage in willful misconduct or gross negligence to be found liable for an ERISA violation of their fiduciary duties.

Moreover, use of the word "Partnership" is itself ambiguous. "Partners" is a defined term encompassing the limited partners, including all the union plans that invested in the AA Capital Partners Funds. See, e.g., Fund I LPA Appendix I (Definitions) at p. 6. But the phrase is also defined as including the General Partnership. Id. From the ERISA perspective, a fiduciary owes undivided loyalty to the plan's participants and beneficiaries. Accordingly, the indemnification provisions cannot be read as consistent with section 410 simply because the General Partners have been found not to have violated a duty they owed under the LPAs towards the General Partnership or one or more general partners, if they also acted disloyally and imprudently toward the ERISA plans/limited partners (and indirectly toward the plans' participants).

To be saved, the indemnification provisions must be read to preclude indemnification where the indemnitees have been found to have breached their ERISA fiduciary duties. Otherwise, by their terms, the agreements purport to indemnify the General Partners even where their actions violate ERISA. The agreements would effectively require the Fund – i.e. the Fund's investors, and ultimately the MSPF participants – to pay breaching fiduciaries for the expense of defending and satisfying their liability under ERISA, thereby absolving the fiduciaries of full responsibility for their misconduct. Unless the provisions are read to preclude indemnification in instances of ERISA fiduciary breach, the agreements would impermissibly exonerate the General Partners from their ERISA responsibilities and are void as a matter of law. See, e.g., IT Corp., 107 F.3d at 1418.

It is not clear that the General Partners acknowledge that the indemnification provisions, which they describe as "very broad," are limited by section 410's prohibition on indemnifying

fiduciary misconduct. See GP Memo at 7-8 (suggesting that the Millwrights' complaint lacks "allegations of bad faith or breach of fiduciary duty" requiring the repayment of advanced fees if it is eventually found they are not entitled to indemnification "in accordance with the [LPA]s"). Indeed, their use of ellipses, id. at 7, when quoting the applicable provision (§12.2.1 of the LPA), purposely leaves out the prefatory "[t]o the furthest extent permitted by applicable law," which we read as a necessary limiting principle incorporating section 410 into the provisions. But absent such acknowledgement, it is particularly important that the Court not give carte blanche to the General Partners' request for the advancement of fees, and all the more so because the indemnification provisions purport to cover not only expenses such as legal fees, but also "any loss, damage, liability, interest, penalty cost and expense." Unless read to preclude indemnification in instances of any ERISA fiduciary breach (not just those involving "bad faith"), enforcing the agreements would effectively make it impossible for the Millwrights trustees to recover fully, or possibly at all, the "losses to the plan" despite ERISA section 409's express authorization for such recovery. 29 U.S.C. § 1109.

Thus, as long as the General Partners' liability is deemed to fall within the indemnification provisions and not to be subject to its limitations or section 410's prohibitions, any judgment in favor of the Millwrights would amount to an order requiring the MSPF to pay itself for its own losses to the extent of the remaining, limited resources of the Funds; and the General Partners would be excused to the extent of those payments from their statutory obligations to make the plan whole for the losses caused by their misconduct. Section 410, however, does not allow fiduciaries to evade their duties and liabilities at the expense of the plan and its participants in this manner.

2. The exceptions to section 410 do not apply.

Not surprisingly, therefore, none of Section 410's exceptions to ERISA's broad prohibition on exculpatory provisions is applicable here. Section 410(b) states that:

Nothing in this subpart shall preclude –

> (1) a plan from purchasing insurance for its fiduciaries or for itself to cover liability or losses occurring by reason of the act or omission of a fiduciary, if such insurance permits recourse by the insurer against the fiduciary in the case of the breach of a fiduciary obligation by such fiduciary;

> (2) a fiduciary from purchasing insurance to cover liability under this part from or for his own account; or
>
> (3) an employer or an employee organization from purchasing insurance to cover potential liability of one or more persons who serve in a fiduciary capacity with regard to an employee benefit plan.

29 U.S.C. § 1110(b). Thus, section 410 allows some forms of indemnification through "purchasing insurance" in certain enumerated circumstances. In addition, a longstanding interpretative rule of the Secretary permits forms of indemnification that are akin to, and as protective of the plan, as the purchase of insurance expressly permitted by the statute. Interpretive Bulletin 75-4, 29 C.F.R. § 2509.75-4. The Secretary has thus interpreted section 410 "to permit indemnification agreements which do not relieve a fiduciary of responsibility or liability" under ERISA, reasoning that provisions "which leave the fiduciary fully responsible and liable, but merely permit another party to satisfy any liability incurred by the fiduciary in the same manner as insurance purchased under section 410(b)(3), are therefore not void under section 410(a)." Id.[3]

The payment of defense fees here does not come within the literal terms of section 410(b), however, because the arrangements do not involve the purchase of insurance. Nor is enforcement justified under the Secretary's interpretive bulletin, which emphasizes that it does not cover arrangements which "in effect, relieve the fiduciary of responsibility and liability to the plan by abrogating the plan's right to recovery from the fiduciary for breaches of fiduciary obligations." Most significantly, the bulletin rejects, on that basis, arrangements where "indemnification of a fiduciary of an employee benefit plan [is made] by the plan." 29 C.F.R. § 2509.75-4.

Section 410 makes no mention of plan assets, but instead broadly "void[s] as against public policy" any agreement that purports "to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under" ERISA. Here, it is clear that any Fund amounts

[3] See also DOL Advisory Opinion 2003-08A ("indemnification provisions that leave the fiduciary fully responsible and liable, but merely permit another party to satisfy any liability incurred by the fiduciary in the same manner as insurance . . . are . . . not void under § 410(a)"); cf. DOL Advisory Opinions 93-15A, 93-16A, and 93-18A (finding reimbursement agreement between welfare plan and legal services plan "not prohibited by § 410(a)").

spent on defense costs pursuant to the indemnification provisions means less money for the plans and ultimately for the plan participants. The advancement of fees from the Funds in this case would have precisely the "effect" of "reliev[ing] the fiduciaries" of liability by "abrogating the plan's right to recover," and, consequently, cannot be said to "merely permit[] another party [other than the plan] to satisfy any liability incurred by the fiduciary in the same manner as insurance purchased under section 410(b)(3)," as contemplated in the Secretary's interpretation. 29 C.F.R. § 2509.75-4 (emphasis added). As numerous courts have held, it would be inconsistent with the broad terms of, and public policy expressed in, ERISA section 410 to allow an individual who has breached his fiduciary duties to a plan to be effectively indemnified by the plan under such circumstances, because the plan would indirectly bear the financial burden and the fiduciary would be "reliev[ed] from . . . liability" at the expense of the plan and its participants in precisely the way section 410 forbids. See discussion of Interpretive Bulletin 75-4 in Delta Star Inc. v. Patton, 76 F.Supp.2d 617, 640-41 (W.D. Pa. 1999); Wells Fargo, 860 F. Supp. at 716; Engle, 619 F.Supp. at 158; Donovan v. Cunningham, 541 F. Supp. 276, 289 (S.D. Tex. 1982), aff'd in part, vacated in part, rev'd in part, on other grounds, 716 F.2d 1455 (5th Cir. 1983).

The Millwrights allege in their Complaint that Funds I and II contain plan assets and that the General Partners are ERISA fiduciaries with respect to those assets. Millwrights Comp. ¶ 15. These allegations should be accepted as true for purposes of deciding the General Partners' Motion. See, e.g., Cunningham, 541 F. Supp. at 289 (no adjudication of fiduciary status necessary for court to rule that agreement indemnifying any party to the ERISA suit is void under section 410, where the effect of the agreement is that the plan would indirectly bear the financial burden). Furthermore, the Secretary has conducted her own analysis with respect to Fund II and has determined that it contains plan assets and that the General Partners are fiduciaries with respect to Fund II. See Sec. Comp. ¶¶ 17-23. At a minimum, the Court should not even consider authorizing advancement unless and until the General Partners are able to prove that they are not fiduciaries with respect to either Fund. If the Court permits advancement of attorneys' fees in this case based on the General Partners' unproven assertions that they are not fiduciaries with respect to the Funds, and later determines that the General Partners are fiduciaries with respect to the Funds and have breached their ERISA fiduciary duties, the plans

will have no means of recovering the advanced fees, an outcome that is plainly impermissible under section 410. See Section B, infra.

In the present context, therefore, indemnification by the Fund of an alleged fiduciary's legal expenses in defending a suit for fiduciary breach brought by an ERISA plan violates section 410 because it relieves the fiduciary of liability for the consequences of its wrongdoing and deprives the plan of its statutory right to recovery for its losses. Such arrangements therefore run afoul of the statutory interpretation of section 410 set forth in the bulletin, and the Secretary's interpretation of this interpretative regulation is entitled to controlling deference. See Kennedy v. Plan Administrator for DuPont Sav. & Inv. Plan, 2009 WL 160440, at *6 & n.7 (2009).

* * * * * * * * * * * *

For these reasons – because enforcing these provisions as broadly as the General Partners suggest would result in the very fiduciaries accused of breaching their duties to the MSPF having their defense costs (and eventually their liability) paid out of the Fund accounts that would otherwise be paid to MSPF participants and beneficiaries – it behooves the Court, before considering the advancement of fees under the LPA indemnification agreements, to construe the scope of those provisions in a manner that comports fully with the statute and its manifest purposes.

B. The General Partners' agreements to repay, in limited circumstances, the fees advanced to them are insufficient to save the void indemnification arrangements

In appropriate circumstances, section 410 permits the advancement of attorneys' fees and defense costs subject to an obligation to repay them if the fiduciaries are found liable for fiduciary breach. These are not appropriate circumstances, however. Because the indemnification provisions in the LPAs fail to ensure a means of recovering advanced fees, the General Partners may not rely on the exception in ERISA section 410(b)(1) authorizing the purchase of recourse insurance by a plan, or the Secretary's interpretation of that exception at 29 C.F.R. § 2509.75-4 as permitting "indemnification provisions which . . . merely permit another party to satisfy any liability . . . in the same manner as insurance purchased under section 410(b)(3)." This is true even though the agreements require the General Partners to sign undertakings in which they agree to pay back the fees if it is ultimately determined that they are

held liable for "unlawful misconduct" (which, as the Secretary argues here, must be interpreted to include acts which violate ERISA).

Absent proof of ability to repay the funds in the event the General Partners are found liable for fiduciary breach, advanced payment of attorneys' fees would leave the plans, as the limited partners of the Funds, without adequate remedy and would let the breaching fiduciaries shift their liability back to the plans. Ability to repay is part and parcel of Section 410's authorization of advanced payments subject to recourse in the event the indemnitees are ultimately adjudged liable for a fiduciary breach under ERISA. For this reason, the recourse provision in the agreements is insufficient to satisfy ERISA requirements respecting the issue of advanced fees. While the LPAs allow for advancement of attorneys' fees upon receipt of a valid undertaking to repay the fees in the event the indemnitee is found not to be entitled to indemnification, § 12.2.4, there is no requirement to show that the indemnitee is able to repay the advanced amount plus reasonable interest in the event he or she is adjudged to have violated ERISA. Thus, the undertakings required here differ from the undertakings that were found permissible in DOL Opinion Letter 77-66/67A. The agreements at issue in the Opinion Letter permitted advancement of legal defenses only "upon receipt of an undertaking by such person to repay such amount plus reasonable interest in the event that in the final judgment of a court of competent jurisdiction such person is found to have breached this Agreement or any duties or responsibilities undertaken pursuant to this Agreement, and proof satisfactory to the Trustees that such person is financially capable of repaying such amount in the event it is found liable for the amount alleged as damages in the action." Furthermore, the Opinion Letter states that payment pursuant to such agreements is permissible "only if the Fund obtains a written opinion of legal counsel . . . that . . . the acts of the fiduciary in question do not constitute a breach of a fiduciary obligation by such fiduciary." Here, there is no requirement to obtain the opinion of independent legal counsel, nor is there a requirement that the indemnitees prove that they are financially capable of repaying the funds.[4] Absent such proof, in the event the indemnitee is unable to repay, he or she would be effectively insulated from fiduciary liability, ultimately at the expense

[4] According to the Receiver, "The only significant asset of the General Partners is the interest they hold in their respective Funds. If those interests are found to be unlawful, the General Partners will have no assets, and no ability to repay the illegal indemnification they have received." Receiver's Objection at 9 (Docket No. 490).

of the MSPF and in violation of section 410. The arrangement is thus not equivalent to the purchase of recourse insurance.

Finally, the General Partners suggest that invalidating the agreements will have far-reaching, negative policy implications. However, the plan-protective policies of ERISA in general and section 410 in particular, which expressly "void[s]" exculpatory indemnification agreements as "against public policy," take precedence. Through section 410, Congress has struck a balance between the general policy in favor of permitting contractual agreements to indemnify corporate officers and directors and the overriding policy objective of ERISA (and derived from trust law) of holding fiduciaries personally liable for their fiduciary misconduct. Fiduciaries cannot be permitted to negate section 410 and ERISA's remedial provisions by the simple expedient of having a Fund in which ERISA plans have invested indemnify them for any breaches.

CONCLUSION

For these reasons, the Secretary respectfully requests the Court to deny the General Partners' motion for attorneys' fees in the Millwrights case.

Respectfully submitted,

CAROL A. DEDEO
Deputy Solicitor for National Operations

TIMOTHY D. HAUSER
Associate Solicitor, Plan Benefits Security Division

NATHANIEL I. SPILLER
Counsel for Appellate and Special Litigation
Plan Benefits Security Division

By: */s/ Robyn M. Swanson*
ROBYN M. SWANSON, # 6284098
Trial Attorney
Plan Benefits Security Division
200 Constitution Ave. NW
Suite N-4611
Washington, D.C. 20210
Tel: (202) 693-5803
Fax: (202) 693-5610
Email: swanson.robyn@dol.gov
Attorneys for Amicus Curiae,
United States Department of Labor