Supreme Court Declines To Rule on ERISA Breach of Fiduciary Duty Pleading Standard for ESOP Cases

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Four Times Square
New York, NY 10036
212.735.3000

The U.S. Supreme Court today in *Retirement Plans Committee of IBM v. Jander*, No. 18-1165 (2020) (*per curiam*), declined to resolve questions about the pleading standard for a breach of fiduciary duty claim against fiduciaries of an employee stock ownership plan (ESOP) under the Employee Retirement Income Security Act of 1974 (ERISA) and remanded the case to the Second Circuit for further proceedings.

The respondents were participants in IBM's 401(k) Plus Plan (the Plan) who invested in the IBM Stock Fund (the ESOP) and allegedly suffered losses from the ESOP's investment in IBM stock. The Plan participants allege that IBM misrepresented the value of its Microelectronics business, thus artificially inflating the value of IBM stock, and that, as corporate insiders, the ESOP's fiduciaries (petitioners) were aware of the alleged fraud and should have disclosed it. The Plan participants allege that by failing to disclose the overvaluation of the Microelectronics business, the ESOP fiduciaries breached their fiduciary duty of prudence under ERISA.

The Supreme Court previously grappled with the challenges inherent in being an insider fiduciary to an ESOP in 2014 in *Fifth Third Bancorp v. Dudenhoeffer*, 573 U.S. 409 (2014). Prior to *Dudenhoeffer*, most federal courts viewed a decision to invest in employer stock as presumptively prudent, regardless of a fiduciary's potential insider information suggesting that the stock was overvalued. The Supreme Court rejected a presumption of prudence in *Dudenhoeffer*, holding that ESOP participants can defeat a motion to dismiss if they "plausibly allege an alternative action that the [ESOP fiduciary] could have taken that would have been consistent with the securities laws and that a prudent fiduciary in the same circumstances would not have viewed as more likely to harm the [ESOP] than to help it." *Id*. at 428. The Court reasoned that this standard appropriately took into account both the need to protect participants and the reality that an ESOP fiduciary may find himself "between a rock and a hard place" when deciding whether the ESOP should continue investing in company stock, because he or she could be accused of imprudence for retaining the stock but accused of disobeying plan documents for reducing the stock. *Id*. at 424. In *Dudenhoeffer*'s wake, courts have dismissed most suits alleging imprudent retention of employer stock in an ESOP under the *Dudenhoeffer* pleading standard.

At issue in *Jander* was whether the pleading standard established in *Dudenhoeffer* can be satisfied by generalized allegations that the harm of an inevitable discovery of alleged fraud generally increases over time. The U.S. District Court for the Southern District of New York held that Plan participants had failed to satisfy *Dudenhoeffer*, but the Second Circuit reversed, holding that the participants had plausibly alleged a breach of fiduciary duty because the fiduciaries could not have concluded that a corrective disclosure would do more harm than good.

On appeal to the Supreme Court, however, both the petitioners and the government "focused their arguments primarily upon other matters." *Retirement Plans Committee of IBM v. Jander*, No. 18-1165 (2020) (*per curiam*). Specifically, the petitioners asserted that ERISA could not impose a duty on an ESOP fiduciary to disclose inside information, and the government argued that an ERISA-based duty to disclose would conflict with the objectives of the federal securities laws. In a *per curiam* opinion, the Supreme Court declined to address those arguments, observing that they had not yet been addressed by the lower courts. The Court remanded the case to the Second Circuit, leaving it up to that court to decide whether to address the petitioners' and the government's arguments.

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Justice Elena Kagan (joined by Justice Ruth Bader Ginsburg) and Justice Neil Gorsuch filed separate concurring opinions. Justice Kagan opined that, as an initial matter, the Second Circuit may decline to consider the arguments raised by the petitioners and the government if it determines that they were not properly preserved. *Retirement Plans Committee of IBM v. Jander*, No. 18-1165 (2020) (Kagan, J., concurring). In addition, Justice Kagan opined that contrary to the petitioner's position, *Dudenhoeffer* "makes clear that an ESOP fiduciary at times" has a duty to act on insider information. *Id*.

Justice Gorsuch, on the other hand, stated that the Second Circuit should consider the merits of the petitioners' and the government's arguments, which, if not addressed, would "only prove unavoidable later." *Retirement Plans Committee of IBM v. Jander*, No. 18-1165 (2020) (Gorsuch, J., concurring). Justice Gorsuch also opined that it would be "odd" if insider ESOP fiduciaries could be held liable under ERISA for failing to make a corrective disclosure, observing that such fiduciaries "necessarily would be acting in their capacities as corporate officers, not ERISA fiduciaries." *Id*. "Run-of-the-mill ERISA fiduciaries," he continued, "cannot, after all, order corporate disclosures on behalf of their portfolio companies." *Id*.

Although the decision in *Jander* does not resolve the underlying issue, it does highlight the myriad difficulties faced by ESOP fiduciaries who are also corporate insiders, including whether plan sponsors should consider engaging an independent fiduciary to manage their ESOP in appropriate circumstances.

View the opinion.

Contacts

James R. Carroll
Partner / Boston
617.573.4801
james.carroll@skadden.com

Eben P. Colby
Partner / Boston
617.573.4855
eben.colby@skadden.com

Michael S. Hines
Partner / Boston
617.573.4863
michael.hines@skadden.com

Jonathan Marcus
Of Counsel / Washington, D.C.
202.371.7596
jonathan.marcus@skadden.com

Mary E. Grinman
Associate / Boston
617.573.4893
mary.grinman@skadden.com

Emily Kline
Associate / Boston
617.573.4848
emily.kline@skadden.com