No. 11-1497

IN THE UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

DEBRA GRIFFIN, ET AL.,
Plaintiffs-Appellants,

v.

FLAGSTAR BANCORP, INC., ET AL.,
Defendants-Appellees.

BRIEF OF THE SECRETARY OF LABOR, HILDA L. SOLIS, AS AMICUS CURIAE IN SUPPORT OF PLAINTIFFS-APPELLANTS AND REQUESTING REVERSAL

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

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STATEMENT OF THE ISSUE

Whether plaintiffs alleged facts sufficient to state a claim that defendants, fiduciaries to the 401(k) plan in which plaintiffs were participants, breached their fiduciary duty of prudence under the Employee Retirement Income Security Act ("ERISA"), 29 U.S.C. § 1101 et seq., by failing to divest the Flagstar retirement plan of its employer stock holdings and eliminate the employer stock fund as an investment option for plan participants as Flagstar suffered huge losses due to its many non-performing mortgages.

STATEMENT OF INTEREST, IDENTITY, AND AUTHORITY TO FILE

As the head of the federal agency with primary responsibility for Title I of ERISA, the Secretary of Labor has a strong interest in ensuring that courts correctly interpret the statute. See Secretary of Labor v. Fitzsimmons, 805 F.2d 682, 692-93 (7th Cir. 1986) (en banc) (discussing the significance to the "national economy and commerce" of the protection afforded to pension plans by the enforcement of ERISA). Some courts, including the district court here, have heightened the pleading standard in ERISA cases involving investment of retirement funds in employer stock by applying a presumption that fiduciaries who allow pension plans to invest in the stock of the sponsoring company are acting prudently unless the company is on

the verge of collapse or in dire financial circumstances. The application of this presumption to dismiss fiduciary breach claims on the pleadings not only infringes on ERISA's stated purpose that plan participants have "ready access to the Federal courts," 29 U.S.C. § 1001(b), but also undermines the strict fiduciary standard of care that governs the actions of fiduciaries under ERISA, and is therefore wholly unwarranted. The Secretary has an interest in ensuring that this presumption is not applied to dismiss otherwise valid claims of fiduciary breach.

The Secretary files this brief pursuant to her authority under Fed. R. App. P. 29(a).

STATEMENT OF THE FACTS

I. FACTUAL BACKGROUND

Plaintiffs Debra Griffin and Joy Gardner are former employees of Flagstar Bancorp, Inc. ("Flagstar") and participants in the Flagstar Bank 401(k) Plan ("Plan") whose individual accounts included investments in Flagstar common stock. Compl. ¶¶ 10-11. They purport to represent a class of all current and former Plan participants whose accounts also held shares of Flagstar stock anytime after December 31, 2006. Id. ¶ 1.

Flagstar is a Michigan-based savings and loan holding company that conducts business through its subsidiary, Flagstar Bank, FSB, which is a

federally chartered stock savings bank. Id. ¶ 12. It administers the Flagstar Bank 401(k) Plan ("Plan"), which is a defined contribution plan within the meaning of ERISA section 3(34), 29 U.S.C. § 1002(34). Compl. ¶¶ 12-13, 27. At all times relevant to plaintiffs' complaint, the Plan operated in the same basic manner: Plan fiduciaries selected a set of investment options, and Plan participants directed the allocation of their individual funds within those options. Id. ¶¶ 29, 34; Griffin v. Flagstar Bancorp, Inc., --- F. Supp. 2d ---, No. 2:10-cv-10610, 2011 WL 1261196, at *1 (E.D. Mich. Mar. 31, 2011).[1] Plan documents did not mandate that the fiduciaries include Flagstar stock or any other particular investment option. Compl. ¶ 29. Throughout the class period, defendants chose to include Flagstar stock as one of twenty-three such options. Compl. ¶ 28; Griffin, 2011 WL 1261196, at *1.

Flagstar operates banking and home loan centers across the United States. Compl. ¶ 12. From 2006 to 2010, as the recession hit and the housing market declined, Flagstar was exposed to significant credit risk, in particular because its holdings included mortgages. Id. ¶¶ 39, 69. During that time, Flagstar's profits decreased and ultimately turned to losses. Id. ¶¶ 40-43, 45, 49, 53, 58, 62, 75-76, 78, 81. These developments were

[1] In 2008, the original Plan document was superseded by an amended Plan document. Griffin, 2011 WL 1261196, at *1. It does not appear, nor has either party asserted, that any distinctions between the documents is of significance to this case.

documented in the company's SEC filings, reflected in the downgrading of Flagstar's credit rating, and consistent with news reports regarding the mortgage industry. See id. ¶¶ 40-87. In August 2009, 11.2% of Flagstar's loans were non-performing and the company's equity-to-assets ratio was 5.4%; an article in Bloomberg news citing these numbers explained that a percentage of non-performing loans above five percent, especially when coupled with a low equity-to-asset ratio, put a company's survival at risk. Id. ¶ 79. The price of Flagstar stock decreased significantly over the class period: it was $14.95 per share on January 3, 2007; $10.90 on July 31, 2007; $6.07 on November 1, 2007; $7.67 on February 20, 2008; $4.65 on May 16, 2008; $2.78 on June 24, 2008; $1.64 on November 3, 2008; $1.09 on January 3, 2009; and $.68 on April 28, 2010. Id. ¶¶ 44, 46, 52, 55, 59, 63, 73, 91. Thus, from early 2007 to mid-2010, the stock lost 95% of its value. Flagstar avoided collapse by securing infusions of money, first in May 2008 by selling equity for approximately $100 million, id. ¶ 54, and again in February 2009 when it received $250 million from the U.S. Treasury Department as part of the government's Troubled Asset Relief Program ("TARP"), as well as another $250 million of private funds, id. ¶¶ 67, 70, 74.

On February 11, 2010, plaintiffs filed suit in the U.S. District Court for the Eastern District of Michigan against Flagstar and several named and

unnamed corporate officers who took part in the administration of the Plan. Plaintiffs allege that during the class period, Flagstar stock was an imprudent investment option for the Plan. Compl. ¶¶ 32, 40. Their Complaint sets forth three counts of violations of fiduciary duties under ERISA: failure to prudently and loyally manage the Plan's assets, id. ¶¶ 95-104; breach of duty to avoid conflicts of interest, id. ¶¶ 105-10; and failure to adequately monitor other fiduciaries and provide them with accurate information, id. ¶¶ 111-24. Defendants moved to dismiss plaintiffs' complaint in its entirety.

II. THE DISTRICT COURT DECISION

The district court granted defendants' motion, dismissing plaintiffs' complaint pursuant to Fed. R. Civ. P. 12(b)(6). Griffin, 2011 WL 1261196, at *1. The court first rejected defendants' argument that plaintiffs lacked standing to bring their suit, relying on Bridges v. American Electric Power Co., 498 F.3d 442, 444-45 (6th Cir. 2007). Griffin, 2011 WL 1261196, at *7.[2]

Next, the district court considered plaintiffs' claim that defendants breached their duty to act prudently in managing the Plan and its assets by failing to divest the Plan's holdings in Flagstar stock during the class period.

[2] The court also rejected defendants' argument that the court lacked subject matter jurisdiction over plaintiffs' claims. Griffin, 2011 WL 1261196, at *6 n.3.

Although the court agreed with plaintiffs that defendants had discretionary authority over the selection of the Plan's investment options and therefore had fiduciary duties with regard to the selection of those options, Griffin, 2011 WL 1261196, at *8, the court nevertheless held that plaintiffs failed to state a claim that defendants breached their fiduciary duties by failing to divest the Plan's Flagstar stock, reasoning that Plan documents gave participants, not defendants, control over the holdings of individual accounts. Id. at *9 n.6.

With regard to the claim that the fiduciaries acted imprudently by maintaining the Flagstar stock fund as an investment option and thus allowing the Plan to continue to purchase Flagstar stock, the court cited Moench v. Robertson, 62 F.3d 553 (3d Cir. 1995), in which the Third Circuit first established a presumption that plan fiduciaries act prudently when they invest in employer stock where plan documents require such investment. Griffin, 2011 WL 1261196, at *9-10. The court noted that the Sixth Circuit adopted the presumption in Kuper v. Iovenko, 66 F.3d 1447 (6th Cir. 1995), which held that "[a] plaintiff may rebut this presumption of reasonableness by showing that a prudent fiduciary acting under similar circumstances would have made a different investment decision." Griffin, 2011 WL 1261196, at *10 (quoting Kuper, 66 F.3d at 1459) (internal quotation marks

omitted). To assess plaintiffs' claim that the fiduciaries acted imprudently in maintaining the Flagstar stock fund, the court then posed and answered a series of questions regarding the applicability of the presumption to this case. Id. at *10-16.

First, the district court asked whether the Kuper presumption applied to the Flagstar Plan. Griffin, 2011 WL 1261196, at *10. It concluded that it did apply because "[Plan] administrators are 'more than simply permitted to make [investments in Flagstar stock].'" Id. at *10 (quoting Moench, 62 F.3d at 571). Pointing to a provision in a document describing investment guidelines for the Plan that exempted Flagstar stock from those guidelines, the court determined that the "creat[ion of] a special type of preference for Flagstar stock . . . evidences an intent that the Stock Fund be offered as an investment option." Griffin, 2011 WL 1261196, at *11.

The court then turned to the question of whether the Kuper presumption applies to all eligible individual account plans ("EIAPs") that hold employer stock rather than only to the subset of EIAPs known as employee stock ownership plans ("ESOPs"). Griffin, 2011 WL 1261196, at *11.[3] Because other circuit courts have extended the presumption of

[3] An ESOP is a defined contribution plan, or individual account plan, that is designed to invest primarily in employer stock and is qualified under section 401 of the Internal Revenue Code. 29 U.S.C. § 1107(d)(6). An EIAP is an

prudence to apply to all EIAPs and based on the logic that Congress intended EIAPs, like ESOPs, to encourage employee ownership of company stock, the court concluded that the presumption applied to the Plan even though it is not an ESOP. Id. at *11-12 (citing Kirschbaum v. Reliant Energy, Inc., 526 F.3d 243 (5th Cir. 2008); Edgar v. Avaya, Inc., 503 F.3d 340 (3d Cir. 2007)).

Next, the court asked whether the presumption of prudence applies in considering a motion to dismiss. Griffin, 2011 WL 1261196, at *12. It acknowledged that authority is split as to whether the presumption is an evidentiary standard best addressed at the summary judgment or merits stage or a pleading standard that can be resolved earlier in the case. Id. (citing various cases reaching each conclusion). It decided that "in this context the presumption merely indicates the standard required for plaintiffs to state claims in 'stock drop' cases" and, therefore, it was appropriate to apply the presumption in ruling on defendants' motion to dismiss. Id.

After determining that the Kuper presumption applied to plaintiffs' claim, the court addressed what facts plaintiffs must allege in order to rebut it. Griffin, 2011 WL 1261196, at *12-13. Following one line of split

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individual account plan that is either invested primarily in employer stock or that provides explicitly for the acquisition and holding of such stock. Id. § 1107(d)(3). Both are exempted from ERISA's diversification provision with respect to employer stock. Id. § 1104(a)(2).

precedent, the court concluded that "Plaintiffs' allegations must demonstrate that Flagstar was on the verge of impending collapse or other dire circumstances." Id. at *13-14 (citing numerous cases addressing the question of what factual allegations are sufficient to overcome the presumption of prudence). Because "Flagstar Bank did not fail; Flagstar's common stock continues to be traded on the New York Stock Exchange; Flagstar received private capital infusions, and Flagstar participated in the federal TARP program," the court determined that Flagstar "was, and is, a viable company." Id. at *15. Furthermore, the court noted, plaintiffs had not made any allegations of fraud or accounting irregularities. Id. Finally, although plaintiffs had pointed to Flagstar's poor credit ratings in support of their claim, the court found it significant that defendants had provided with their motion to dismiss examples of recommendations from financial experts to hold Flagstar stock during the class period. Id. at *16.

The court next ruled in the alternative that even if the Kuper presumption did not apply to plaintiffs' breach of the duty of prudence claim, dismissal of that claim was appropriate. Griffin, 2011 WL 1261196, at *16. Specifically, the court ruled that plaintiffs' allegations failed to state a claim under Bell Atlantic Corp. v. Twombly, 550 U.S. 544 (2007), and Ashcroft v. Iqbal, --- U.S. ---, 129 S. Ct. 1937 (2009). Griffin, 2011 WL 1261196, at

*16. To reach this conclusion, the court relied on two facts: the summary plan description warned Plan participants that they, and not Plan fiduciaries, were responsible for losses based on their investment instructions, and, as it turned out, Flagstar "continued to be a viable banking institution." Id. at *16.

The court went on to dismiss plaintiffs' remaining claims. Id. at *17-23.

SUMMARY OF THE ARGUMENT

The district court erred in dismissing this case. Contrary to the court's conclusion, plaintiffs plausibly stated a claim for breach of fiduciary duty by alleging that Plan fiduciaries failed to divest the Plan's holdings in employer securities and continued to allow for the additional purchases during a period when Flagstar's allegedly precarious financial situation made the stock an imprudent investment for a pension plan. Under Sixth Circuit and Supreme Court precedent, no more is required.

The district court thus erred in concluding on the pleadings that the fiduciaries acted prudently simply because the Flagstar Plan specified that participants could direct the assets in their accounts among the investment alternatives offered, including the employer stock fund. A fiduciary always retains the duty to act in accordance with ERISA's requirements, including

its stringent standard of care, in selecting and maintaining plan investment options. Nor was dismissal supported by the fact that Flagstar stock, which lost 95% of its value, did not become completely worthless.

The court likewise erred in dismissing the case based on the presumption of prudence adopted by the Court in Kuper. First, the Kuper presumption does not apply where, as appears to be the case here, a plan does not require that employer stock be offered as an investment option. Second, the presumption is an evidentiary matter and, as such, should not be applied at the pleadings stage. Third, under Kuper, a plaintiff need only show that "a prudent fiduciary acting under similar circumstances would have made a different investment decision," 66 F.3d at 1459, and is not required to allege that a company was on the verge of collapse or in similarly dire circumstances, as the district court assumed, in order to state a claim for breach of the duty of prudence. Finally, even if a "verge of collapse" or "dire circumstances" standard is appropriate, plaintiffs have made sufficiently plausible allegations to survive this motion to dismiss.

ARGUMENT

THE DISTRICT COURT ERRED IN HOLDING THAT PLAINTIFFS FAILED TO ALLEGE FACTS SUFFICIENT TO STATE A CLAIM THAT DEFENDANTS BREACHED THEIR FIDUCIARY DUTY OF PRUDENCE BY ALLOWING THE PLAN TO CONTINUE TO HOLD AND INVEST IN FLAGSTAR STOCK

Congress enacted ERISA 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 ready access to the Federal courts." 29 U.S.C. § 1001(a), (b). To this end, section 404 of ERISA requires plan fiduciaries to act "for the exclusive purpose" of "providing benefits to participants and their beneficiaries" and "defraying reasonable expenses of administering the plan" as well as with the same level of care that "a prudent man acting in like capacity and familiar with such matters would use" in similar circumstances. 29 U.S.C. § 1104(a)(1)(A), (B). Plan fiduciaries' obligations also include diversification of plan investments. Id. § 1104(a)(1)(C).

ERISA allows one limited modification to these duties for fiduciaries of EIAPs. Specifically, such fiduciaries are exempted from this duty to diversify with respect to investments in employer stock. Id. § 1104(a)(2) (excepting individual account plans from the diversification requirement with respect to employer stock and from ERISA's prudence requirement "only to the extent that it requires diversification"). As this Court has recognized, ERISA does not otherwise modify or eliminate the obligation of EIAP fiduciaries to adhere to section 404's standards of loyalty and care.

Kuper, 66 F.3d at 1458 (explaining that the diversification exemption does not relieve a fiduciary of the obligation to "discharge his duties respecting the plan solely in the interests of plan participants and beneficiaries and in a prudent fashion" (quoting Martin v. Feilen, 965 F.2d 660, 665 (8th Cir. 1992))).[4]

A. Under applicable pleading standards, plaintiffs' allegations are sufficient to state a claim that defendants violated their fiduciary duty to prudently manage the Plan and its assets

1. By describing the precarious financial position of Flagstar, plaintiffs alleged facts that plausibly state a claim for breach of the duty of prudence

Under the notice pleading requirements of federal civil procedure, plaintiffs need only allege facts that plausibly support a claim for relief. See CNH Am. LLC v. United Auto., Aerospace & Agr. Implement Workers of America (UAW), --- F.3d ---, 2011 WL 1833202, at *8 (6th Cir. May 16,

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[4] ERISA permits a "participant" in an ERISA plan to bring a civil action for relief where a fiduciary has breached any of these duties. 29 U.S.C. § 1132(a)(2). Defendants argued below that plaintiffs, as former rather than current Flagstar employees, are not participants for purposes of this provision and therefore do not have standing to bring this suit. The district court correctly determined that this argument is meritless. ERISA defines "participant" to include any employee or former employee . . . who is or may be expected to receive a benefit of any type from an employee benefit plan." 29 U.S.C. § 1002(7) (emphasis added). This Court has explicitly held that former employees who seek to recover losses to their 401(k) accounts have standing to sue as participants under this broad statutory definition. Bridges v. Am. Elec. Power Co., Inc., 498 F.3d 442, 445 (6th Cir. 2007) (citing Harzewski v. Guidant Corp., 489 F.3d 799, 804 (7th Cir. 2007)).

2011) (referring to the "modest notice-pleading requirements of Civil Rule 8(a)," which are met by "plausible" factual allegations (citing Iqbal, 129 S. Ct. at 1949; Twombly, 550 U.S. at 556-57)). Here, plaintiffs allege that a prudent fiduciary would have divested the Plan's holdings in Flagstar stock and eliminated it as an investment option because Flagstar's precarious financial situation during the class period made investment in its stock an unreasonably risky choice for the Plan. Compl. ¶¶ 39-87. Plaintiffs offer more than "labels and conclusions" to support their claim, Iqbal, 129 S. Ct. at 1949 (quoting Twombly, 550 U.S. at 557), by including specific allegations that defendants continued to allow the Plan to invest in Flagstar stock even as Flagstar's profits turned to losses, observers predicted the company would fail even with a government bail-out, and the value of Flagstar stock fell by 95%. Compl. ¶¶ 39-87. These allegations raise "above the speculative level," Twombly, 550 U.S. at 570, the possibility that defendants did not 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," 29 U.S.C. § 1104(a)(1)(B). The claim is therefore sufficient to survive a motion to dismiss.

2. Plaintiffs' ability to direct investments in their accounts does not support dismissal of their claim

Moreover, contrary to the district court's reasoning, that fact that the Plan participants could direct the investments in their accounts among specified alternatives does not support dismissal of their claim that defendants acted imprudently in continuing to offer the Flagstar stock fund as an option and in failing to divest the stock when a prudent fiduciary would not have done so. ERISA imposes strict duties on those who act as fiduciaries and makes them personally liable for any losses to the plan stemming from their breaches, as well as jointly and severally liable for breaches by other fiduciaries of which they have knowledge. See 29 U.S.C. §§ 1132(a)(2), 1109(a), 1105. As this Court recognizes, "the duties charged to an ERISA fiduciary are 'the highest known to the law.'" Chao v. Hall Holding Co., Inc., 285 F.3d 415, 426 (6th Cir. 2002) (quoting Howard v. Shay, 100 F.3d 1484, 1488 (9th Cir. 1996)); see also James v. Pirelli Armstrong Tire Corp., 305 F.3d 439, 448 (6th Cir. 2002); Krohn v. Huron Memorial Hosp., 173 F.3d 542, 547 (6th Cir. 1999). If the district court were correct that ERISA fiduciaries are nevertheless absolved of liability for any resulting losses simply because a 401(k) plan provides, as most do, that the plan participants and beneficiaries may allocate the assets in their

individual accounts among different plan investments, then most fiduciaries to such plans would never be liable for losses stemming from even egregious lapses of their duties.

But the district court is not correct. In any 401(k) plan, participants are entitled to the prudent selection and oversight of the investment options available to them. Howell v. Motorola, Inc., 633 F.3d 552, 567 (7th Cir. 2011); DiFelice v. U.S. Airways, Inc., 497 F.3d 410, 418 (4th Cir. 2007). Thus, if it was imprudent for the Plan to hold and retain Flagstar stock as a Plan option, defendants may be held liable for any resulting losses.

The limited exception to this rule, which arises under ERISA section 404(c), 29 U.S.C. § 1104(c), does not apply in this case because that provision does not immunize fiduciaries from losses that result from their selection of imprudent investment options. Specifically, section 404(c)(1)(A) provides:

> 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.

29 U.S.C. § 1104(c)(1)(A) (emphasis added).

Under the Secretary's regulation, fiduciaries are shielded from liability only for losses that are "the direct and necessary result of that participant's or beneficiary's exercise of control." 29 C.F.R. § 2550.404c-1(d)(2). Moreover, the preamble to the regulation explains that the fiduciary act of "limiting or designating investment options . . . 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." 57 Fed. Reg. 46,906, 46,922 n.27 (Oct. 13, 1992); see also Fiduciary Requirements for Disclosure in Participant-Directed Individual Account Plans, 75 Fed. Reg. 64,910, 64,946 (Oct. 20, 2010) (to be codified at 29 C.F.R. § 2550.404c-1(d)(2)(iv)) (explaining that section 404(c) "does not serve to relieve a fiduciary from its duty to prudently select and monitor any . . . designated investment alternative offered under the plan").

Accordingly, in a 404(c) plan, a fiduciary that oversees appropriate investment funds has no responsibility for the participant's own decisions as to how to allocate investments between funds. For example, even if a participant chooses to invest his entire account in a particular fund or a mix of funds that is wholly incompatible with his particular retirement needs, 404(c) makes clear that the fiduciary is not responsible for the participant's poor judgment. But because "section 404(c) . . . creates a safe harbor only

with respect to decisions that the participant can make, . . . the selection of plan investment options and the decision to continue offering a particular investment vehicle are acts to which fiduciary duties attach, and the [404(c)] safe harbor is not available." Howell, 633 F.3d at 567. Thus, fiduciaries are obliged to construct a prudent menu of investment options, and they are liable for losses resulting from any breach of that responsibility.

The Secretary's regulation 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). 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, see 56 Fed. Reg. 10,724, 10,832 n. 21 (Mar. 13, 1991), and is entitled to the highest degree of deference. See, e.g., Yellow Trans., Inc. v. Michigan, 537 U.S. 36, 45 (2002) (giving controlling deference to agency interpretation in explanatory statement announcing the promulgation of the regulation rather than the regulatory text); Geier v. Am. Honda Motor Co.,

Inc., 529 U.S. 861, 877-80 (2000) (giving controlling deference to interpretation in preamble); Long Island Care at Home, Ltd. v. Coke, 127 S. Ct. 2339, 2349-50 (2007) (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 regulatory interpretation made for the first time in a legal brief).

The district court also erred in holding that because the Plan documents gave participants authority to direct the allocation of investments in their individual accounts and did not specify that the fiduciaries could divest in the absence of such direction, plaintiffs cannot state a claim for fiduciary breach for their failure to divest Flagstar securities when that stock became an imprudent investment. Griffin, 2011 WL 1261196, at *9 & n.6. Where holding plan assets in a particular stock is imprudent, fiduciaries violate ERISA's duty of prudence by failing to divest that stock even if plan documents do not contemplate such an action. ERISA imposes the familiar prudent man standard of care on plan fiduciaries and forbids them from contracting out of that standard. See 29 U.S.C. § 1104(a)(1)(D) (requiring plan fiduciaries to follow plan documents only "insofar as such documents and instruments are consistent with the provisions" of Title I and Title IV of ERISA). Thus, as this Court has recognized, "a fiduciary may only follow

plan terms to the extent that the terms are consistent with ERISA." Kuper, 66 F.3d at 1457 (citing 29 U.S.C. § 1104(a)(1)(D)); see also In re Ford Motor Co. ERISA Litig., 590 F. Supp. 2d 883, 889 (E.D. Mich. 2008) ("ERISA would be almost impotent if it permitted settlors to exempt their fiduciaries from its requirements with a simple stroke of the pen.").[5]

Accordingly, the district court erred in concluding that, even in the absence of any presumption of prudence, plaintiffs' allegations are insufficient to state a claim for breach of fiduciary duty. Moreover, as discussed next, the court also erred in its application of the Kuper presumption and thus erred in dismissing the suit on that basis as well.

B. The Kuper presumption does not require dismissal

In Kuper, this Court adopted a presumption favoring the purchase of employer stock by an ESOP that was expressly "'designed to invest primarily in qualified'" employer securities. Kuper, 66 F.3d at 1450

[5] Nor is dismissal supported, as the district court thought, by the fact that Flagstar "continued to be a viable banking institution" and consequently its stock did not become entirely worthless. Griffin, 2011 WL 1261196, at *16. As discussed below, see supra part B.3, even where a presumption of prudence is applicable, it is certainly the case that, at least in some circumstances, a prudent fiduciary would sell plan stock (or would determine it was not an appropriate investment for a retirement plan) before it becomes worthless. See In re Syncor ERISA Litig., 516 F.3d 1095, 1102 (9th Cir. 2008) ("A prudent man standard based only upon a company's alleged financial viability does not take into account the myriad of circumstances that could violate the standard.").

(quoting plan document). In adopting a presumption of prudence for employer stock investments by such plans, this Court has made clear that "ESOPs cannot override ERISA's goal of ensuring the proper management and soundness of employee benefit plans." Id. at 1457. Consequently, although this Court will "review an ESOP fiduciary's decision to invest in employer securities for an abuse of discretion" and "presume that a fiduciary's decision to remain invested in employer securities was reasonable," plaintiffs can "rebut this presumption of reasonableness by showing that a prudent fiduciary acting under similar circumstances would have made a different investment decision." Id. at 1459 (citations omitted). But, as this Court also recognized, ERISA does not otherwise modify, eliminate or change section 404's standards of loyalty and care. Id. at 1458. Accordingly, ESOP fiduciaries, like all fiduciaries, owe "an unwavering duty to act both as a prudent person would act in a similar situation and with single-minded devotion to those same plan participants and beneficiaries," and they may offer and retain a plan's investment in company stock only if a prudent fiduciary in similar circumstances would do the same. Id. (citations omitted). This presumption does not support dismissal in this case because: (1) it is only applicable to plans like the ESOP in Kuper, which require investment in employer stock; (2) it is an evidentiary standard that is not

applicable at the pleadings stage; (3) it does not require a showing that the company was on the verge of collapse or in dire financial circumstances; and (4) in any event, the plaintiffs have pled that the company was in such circumstances and should be allowed to proceed to the merits of this claim.

1. The Kuper presumption does not apply here because Plan documents do not mandate investment in employer stock

In Kuper, this Court noted the conflict between Congress' expressed intent to encourage the formation of ESOPs and its intent to protect the interests of plan participants through strict standards of fiduciary responsibility. Kuper, 66 F.3d at 1458 (citing Donovan v. Cunningham, 716 F.2d 1455 (5th Cir. 1983)). ESOP fiduciaries are "expected to administer ESOP investments consistent with the provisions of both a specific employee benefits plan" that requires investment primarily in employer stock and with ERISA. id. at 1458 (quoting Moench, 62 F.3d at 569). Noting that the "conflict becomes particularly evident when an employee claims that a fiduciary breached his ERISA duties" by failing to "liquidate the ESOP," the Court adopted "the Third Circuit's holding [in Moench] that a proper balance between the purpose of ERISA and the nature of ESOPs requires that we . . . presume that a fiduciary's decision to remain invested in employer securities was reasonable." Id. at 1458-59.

Here, the plan is not an ESOP, but is a 401(k) plan under which the fiduciaries are given broad authority to select "Permissible Investments" among which participants can choose to allocate funds. Amended Plan Document §§ 2.01(mm), 8.01 (defining "Permissible Investment" as "each investment specified by the Employer as available for investment of assets of the Trust" and requiring that participants' funds be invested in Permissible Investments); see also id., Addendum § 13.2 (requiring that the Plan have at least three Permissible Investments other than employer stock, "each of which must be diversified and have materially different risk and return characteristics," and placing no other requirements on the selection of investment options). Although defendants included Flagstar stock as an investment option throughout the class period, no provision in any Plan document attached to the parties' filings below specifies any particular securities that must be included as investment options, and none requires that the Plan offer Flagstar stock. This lack of a mandate distinguishes this case from Kuper, where the ESOP was, as all ESOPs are, expressly designed to invest primarily in employer securities.

The Third Circuit itself has refused to extend its Moench presumption to plans under which the fiduciaries are simply permitted and not required to make investments in company stock. In re Schering-Plough Corp. ERISA

Litig., 420 F.3d 231, 237 n.5 (3d Cir. 2005) (finding the "Moench decision inapposite because the fiduciaries here were 'simply permitted to make . . . investments' in 'employer securities'" (quoting Moench, 62 F.3d at 571)); see also Edgar v. Avaya, 503 F.3d at 343, 347 n.12 (applying the presumption of prudence to a plan that required the inclusion of employer stock as an investment option but was not an ESOP and distinguishing the plan at issue in Schering-Plough because that plan "did not even direct plan fiduciaries to offer employer stock as an investment option"). In this case, the parties have included in the record no Plan document that requires such investment. Although the district court found significant a document setting forth the Plan's investment guidelines that stated those guidelines did "not apply to employer securities," Griffin, 2011 WL 1261196, at *11, this attenuated reference to employer stock is a far cry from a mandate that such stock be offered to Plan participants as an investment option. In the absence of such a mandate,[6] there is no rationale for presuming that fiduciaries acted prudently by selecting Flagstar stock as an investment option and holding Plan assets in that stock. Only the duty of prudence, and no competing

[6] To the extent that it cannot be determined from the record before the court whether the fiduciaries were directed to offer employer stock or "simply permitted" to do so, Moench, 63 F.3d at 571, and thus whether the presumption should apply at all, this lack of certainty arises because the case was prematurely dismissed on the pleadings.

settlor interest in employee ownership of Flagstar, dictated the fiduciaries' obligations. Accordingly, the district court should not have held that the Kuper presumption applies to this Plan.

2. The presumption of prudence, as an evidentiary standard, does not apply at the pleadings stage

Even if the Kuper presumption applies to the Flagstar Plan, the district court should not have evaluated whether plaintiffs rebutted that presumption before plaintiffs had an opportunity to develop their evidence. The presumption is an evidentiary standard, not a pleading requirement. Cf. Swierkiewicz v. Sorema N.A., 534 U.S. 506, 512 (2002) (holding that because "[t]he prima facie case under [the burden-shifting framework applied in Title VII discrimination cases] operates as an evidentiary standard, not a pleading requirement, it should not be transposed into a rigid pleading standard"). Kuper was decided on summary judgment after the submission of evidence, and this Court concluded that plaintiffs had not successfully rebutted the presumption because they were unable to present evidence proving that the defendants acted unreasonably by holding employer stock. See Kuper, 66 F.3d at 1459-60; see also Sims v. First Horizon Nat'l Corp., 2009 WL 3241689, at *24 (W.D. Tenn. 2009) (reasoning that Kuper's use of the term "showing" in its holding that plaintiffs "may rebut the presumption by showing that a prudent fiduciary

acting under similar circumstances would have made a different investment decision" indicates that the presumption is an evidentiary standard) (quoting Kuper, 66 F.3d at 1459). The Third Circuit's language in Moench similarly supports this conclusion. See Moench, 62 F.3d at 571 (holding that "[i]n attempting to rebut the presumption, the plaintiff may introduce evidence" supporting the proposition that investment in employer stock was unreasonable (emphasis added)). In accordance with this reasoning, district courts in the Sixth Circuit "have overwhelmingly declined to apply the presumption of prudence at the pleading [stage]." In re Regions Morgan Keegan ERISA Litig., 741 F. Supp. 2d 844, 849 (W.D. Tenn. 2010) (listing cases). Moreover, the district court opinion relied on and indeed weighed evidence beyond the pleadings – specifically, reports of rating agencies submitted as attachments to defendants' motion to dismiss to counter plaintiffs' allegations that Flagstar stock was downgraded during the relevant period – in reaching the conclusion that plaintiffs' allegations regarding the value of Flagstar stock did not successfully rebut the Kuper presumption. Griffin, 2011 WL 1261196, at *16. This weighing of evidence on a motion to dismiss was inappropriate and demonstrates that application and resolution of the Kuper presumption should not occur at the pleadings stage.

3. This Court should reject "impending collapse" as the standard for rebutting the presumption because it is inconsistent with ERISA and Kuper

Furthermore, this court should reject the "impending collapse" standard for rebutting the Kuper presumption. As described by the district court, this standard requires a plaintiff to "allege facts that, if true, prove [the employer] was on the verge of economic collapse or other 'dire circumstances' in order to rebut the presumption," seemingly regardless of what a prudent fiduciary would do in like circumstances. Griffin, 2011 WL 1261196, at *15; see also Kirschbaum v. Reliant Energy, Inc., 526 F.3d at 255; Quan v. Computer Sciences Corp., 623 F.3d 870 (9th Cir. 2010). This standard unduly narrows and is thus inconsistent with the fact-intensive and objective statutory test of prudence described in Kuper. See Kuper, 66 F.3d at 1458-59 (discussing the high standard of prudence imposed by ERISA and holding that the presumption may be rebutted "by showing that a prudent fiduciary acting under similar circumstances would have made a different investment decision"). Only Congress has the ability to establish pleading and proof requirements for particular claims, which courts are not free to alter. Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 327 (2007); see also City of Milwaukee v. Illinois and Michigan, 451 U.S. 304,

312 (1981) (explaining that courts should only resort to making federal common law when "compelled to consider federal questions which cannot be answered from federal statutes alone"); Flacch v. Sun Life Assurance Co. of Canada (U.S.), 958 F.2d 730, 735 (6th Cir.1992) (rejecting an argument for altering the meaning of "fiduciary" in the ERISA context, explaining that courts should not "develop common-law alternative definitions for terms that are clearly defined by statute"). Congress established such requirements in ERISA by imposing identical fiduciary standards of prudence on all ERISA fiduciaries, including fiduciaries in employer-stock plans. S. Rep. No. 93-127, reprinted in 1974 U.S.C.C.A.N. 4838, 4863 (1973) ("the core principles of fiduciary conduct . . . place a . . . duty on every fiduciary"). Specifically, the statute requires that fiduciaries 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." 29 U.S.C. § 1104(a)(1)(B). The "prudent investor rule" of trust law rejects any legal determination that "classif[ies] specific investments or courses of action as prudent or imprudent in the abstract." Restatement (Third) of Trusts § 90 cmt. e (2007). Because the statute defines the prudence obligation even for fiduciaries of employer stock plans in terms of a

"prudent fiduciary acting under similar circumstances," Kuper, 66 F.3d at 1459, there is no statutory gap to fill with an "impending collapse" standard found nowhere in the statute.

Indeed, such a court-created rule would, in a fundamental way, convert Kuper's flexible presumption into a "safe harbor," or "prudence per se" rule in all but the most extreme cases. See Quan, 623 F.3d at 881, 883. For these reasons, many district courts in this Circuit and elsewhere have recognized that Kuper does not support such a restrictive requirement. See, e.g., In re Ford Motor Co. ERISA Litig., 590 F. Supp. 2d at 891 (rejecting an impending collapse standard as contrary to the statutory prudent man standard and noting that "nowhere in the [Kuper] opinion does the Sixth Circuit use the words 'impending collapse'"); In re Goodyear Tire & Rubber Co. ERISA Litig., 438 F. Supp. 2d 783, 794 (N.D. Ohio 2006) ("Moench does not limit its holding to companies facing an 'impending collapse' and Kuper . . . never uses the words 'impending collapse.'") (quoting In re Ferro Corp. ERISA Litig., 422 F. Supp. 2d 850, 862 (N.D. Ohio 2006)). Accordingly, plaintiffs' allegations of circumstances from which a factfinder could infer that a prudent fiduciary would have divested from Flagstar stock and removed it as an investment option were sufficient to state a claim for fiduciary breach.

4. Plaintiffs' allegations are sufficient to survive a motion to dismiss even if the Kuper presumption applies at this stage of the case and the court adopts the "impending collapse" standard

Finally, even if this court adopts an "impending collapse" or "dire circumstances" standard, the allegations in plaintiffs' complaint are sufficient to survive dismissal. Although Flagstar did not ultimately fail, that fact is not determinative of whether defendants should have divested from and ceased to permit new investment in Flagstar stock. Plaintiffs' complaint alleges that Flagstar reported losses during the class period, Compl. ¶¶ 49, 76, 78, 81, and financial experts lowered their assessments of Flagstar stock, id. ¶¶ 48, 50, 61. The complaint suggests that only extraordinary measures, including a bail-out from the government, saved the company from collapse. Id. ¶¶ 67, 70, 74. Indeed, plaintiffs allege that even after infusions of government and other funds, the company still had little chance of survival. Id. ¶ 79. The price of Flagstar stock fell 95%, from $14.95 to $.68 per share, between the beginning of the class period and plaintiffs' filing of an amended complaint in April 2010. Id. ¶ 91. Plaintiffs' allegations of dire financial circumstances, poor prospects, and imprudence are more than sufficient to withstand a motion to dismiss plaintiffs' claim of breach of the duty of prudence, even under an "impending collapse" or "dire circumstances" standard. Cf. In re Ford Motor Co., 590 F. Supp. 2d at 908

("Lowering the prudence bar to the point that a fiduciary is required to sell company stock only after it has become worthless is impossible to square with ERISA's stated mission of 'establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and . . . providing for appropriate remedies, sanctions, and ready access to the Federal courts.'") (quoting 29 U.S.C. § 1001(b)).

CONCLUSION

For these reasons, the Secretary respectfully requests that this Court reverse the district court's dismissal of plaintiffs' claim for breach of the duty of prudence.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE
WITH FED. R. APP. P. 32(A)(7)(B)

I certify that the foregoing brief complies with the type-volume limitation set forth in Fed. R. App. P. 32(a)(7)(B)(i). The brief contains 6,997 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii). The brief was prepared using Microsoft Office Word, 2003 edition.

Dated: June 30, 2011

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CERTIFICATE OF SERVICE

I hereby certify that on June 30, 2011, I electronically filed the foregoing with the Clerk of the Court for the United States Court of Appeals for the Sixth Circuit by using the appellate CM/ECF system.

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