

10-1303-cv

IN THE
United States Court of Appeals
FOR THE SECOND CIRCUIT

ISADORE FISHER, on behalf of themselves and a class of persons similarly situated, and on behalf of the JP Morgan Chase 401(k) Savings Plan, JANNA WOOTEN, KELLI M. BUNN, TAMMY SOILEAU, AMY K. HARVEY,

Plaintiffs-Appellants,

—against—

JP MORGAN CHASE & CO., MARC J. SHAPIRO, RICHARD DONALDSON, JR., JOHN DOES, 1-30, J.P. MORGAN INVESTMENT SERVICES, THE PLAN INVESTMENT MANAGEMENT COMMITTEE, THE BENEFITS FIDUCIARY COMMITTEE, INA R. DREW, DINA DUBLON, PATRICK L. EDSPARR, JOHN J. FARRELL, PETER H. KOPP, MARIA ELENA LAGOMASINO, BLYTHE S. MASTER, EDWARD MCGANN, JOHN C. WILMOT, HANS W. BECHERER, RILEY P. BECHTEL, FRANK A. BENNACK, LAWRENCE A. BOSSIDY, M. ANTHONY BURNS, H. LAURENCE FULLER, ELLEN V. FUTTER, WILLIAM H. GRAY, III, WILLIAMS B. HARRISON, JR., HELENE L. KAPLAN, LEE R. RAYMOND, JOHN R. STAFFORD, LLOYD D. WARD,

Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

**AMICUS CURIAE BRIEF OF THE SECURITIES INDUSTRY
AND FINANCIAL MARKETS ASSOCIATION
IN SUPPORT OF APPELLEES REQUESTING AFFIRMANCE**

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RULE 26.1 CORPORATE DISCLOSURE STATEMENT

Amicus curiae Securities Industry and Financial Markets Association (“SIFMA”) is a non-profit corporation. It has no parent corporation and no publicly held corporation owns 10% or more of its stock.

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STATEMENT OF IDENTITY AND INTEREST

The Securities Industry and Financial Markets Association (“SIFMA”) brings together the shared interests of hundreds of securities firms, banks and asset managers.¹ SIFMA’s mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (“GFMA”).

SIFMA has an interest in this case because the issues about to be decided by this Court are vitally important to the operation, and even continued viability, of employer stock funds as an investment alternative for 401(k) plan participants. Given the widespread use of employer stock funds by its members, i.e., employers within the financial services industry, and the role of financial service providers in advising and creating employer stock funds for their customers, SIFMA is interested that Congress’s longstanding encouragement of

¹ Pursuant to Federal Rule of Appellate Procedure 29(a), all parties have consented to the filing of this amicus brief. Also, pursuant to Local Rule 29.1(b), no party’s counsel authored the brief in whole or in part, no party’s counsel contributed money that was intended to fund preparing or submitting this brief, and no other individual or entity contributed money that was intended to fund preparing or submitting of this brief.

employer stock funds is not chilled by a reversal of the lower court's well-reasoned decision.

A decision by this Court to reverse the lower court's grant of defendants' motion for judgment on the pleadings would run counter to the essence of employer stock funds and threaten their very existence as a viable investment alternative in 401(k) plans. Plaintiffs ask this Court to strip plan managers of a presumption of prudence when they invest in an employer's stock, even when the 401(k) plan presupposes that an employer stock fund be offered as an investment alternative and when there is no basis to think that the employer's viability is in jeopardy.

Imposing an obligation on plan managers to diversify or divest an employer stock fund when the employer's stock prices decline, or when the employer is impacted by financial downturns, would leave plan managers with an impossible choice: they could either (a) deviate from the plan documents and face inevitable claims of liability for breaching their fiduciary duty to comply with the terms and spirit of the plan, especially if the employer's stock later rebounds, or (b) adhere to the terms and spirit of the plan documents and still face liability. Many employers placed in such an invidious position would inevitably abandon employer stock funds.

Creating an environment in which employers abandon employer stock funds would run counter to the well-documented Congressional intent to encourage employee ownership of employer stock, as well as the various surveys and studies supporting employer stock plans as valuable tools for savings and economic growth. The opinion of the District Court demonstrates that it gave thoughtful consideration to the legal issues governing the claims in this case, and that it ruled correctly, consistent with legal authority and sound policy. Respectfully, the District Court's decision should not be disturbed on appeal.

INTRODUCTION

This case arises out of claims brought by a putative class of current and former employees of defendant JPMorgan Chase & Co. and its predecessor (together, "JPMorgan Chase"), who participated in a retirement plan offered by JPMorgan Chase between April 1, 1999 and January 2, 2003 (the "Plan"). (A. 46 at ¶ 1; A. 1773 at n.1.)² Plaintiffs bring their claims pursuant to the Employee Retirement Income Security Act of 1974, as amended ("ERISA").

² JPMorgan Chase was formed by merger, on December 31, 2000, of the former J.P. Morgan & Co., Inc. ("JPM") and Chase Manhattan Bank ("Chase"). (A. 1775.) The Plan is a continuation of, and successor to, the Chase Manhattan Bank 401(k) Savings Plan (the "Chase Plan"). (*Id.*) As of December 31, 2001, the Deferred Profit Sharing Plan of Morgan Guarantee Trust Company of New York and Affiliated Companies for United States Employees (the "JPM Plan") was merged into the Chase Plan and was renamed the Plan and restated effective January 1, 2002. (A 46; A. 147.)

The Plan is an employee pension benefit plan, as defined in 29 U.S.C. § 1002(2)(A), and an eligible individual account plan (“EIAP”), as defined in 29 U.S.C. § 1107(d)(3). (A. 61 at ¶¶ 34-35; A. 1775.) Plaintiffs voluntarily participated in the Plan and could select from a number of different investment options, including investing their contributions in JPMorgan Chase common stock through the JPMorgan Common Stock Fund (the “Stock Fund”). (A. 61 ¶ 36; A. 155 at § 1.44; A. 172-176 at §§ 7.1-7.7.)

Although the Plan affords fiduciary discretion to add and remove certain of the investment funds as options (A. 1775), the Plan presupposes that the Stock Fund will be offered as an investment option. There are numerous references to the Stock Fund found throughout the Plan. The Stock Fund is the only investment fund explicitly defined in the Plan. (A. 155 at § 1.47.) The Stock Fund is designated in the Plan as an employee stock ownership plan (“ESOP”) within the meaning of Section 409 of the Internal Revenue Code of 1986, as amended, to invest in qualifying employer securities. The Plan expressly provides that the ESOP “invests primarily” in JPMorgan Chase’s common stock (“Common Stock”). (*Id.*)³

³ An ESOP is one of several types of pension plans categorized as an EIAP, 29 U.S.C. § 1107(d)(3)(A), and, as discussed in more detail below, ESOPs and other employer stock funds in EIAPs are Congressionally mandated investment structures designed to expand employee ownership of employer stock.

The Plan sets forth specific provisions regarding investments in the Stock Fund. As emphasized by the District Court, the Plan states that, “[s]ubject to compliance with any investment elections made by [p]articipants . . . up to 100 percent of the Trust may be invested in shares of Common Stock [of JPMorgan Chase].” (A 1775; A. 172 at § 7.3.) The Plan mandates that, prior to October 1, 2002, 50% of the matching contributions that JPMorgan Chase provided to the account of Plan participants who had achieved certain age and service requirements would be automatically invested in the Stock Fund. (A. 173-174 at § 7.7(b)(i).) The Plan also mandates that, under certain circumstances, JPMorgan Chase’s matching contributions to Plan participants will continue to be invested in the Stock Fund after September 30, 2002. (A. 174 at § 7.7(b)(ii)(A)(II).)

The Plan also sets forth specific details on how dividends on participant interests in Common Stock are to be reinvested or distributed. (A. 176 at § 7.12.) The Plan provides that participants may take distributions from the Plan in cash, Common Stock or a combination of both cash and Common Stock. (A. 193 at § 11.9.) The Plan describes the rights of Plan participants in respect of voting their interest in Common Stock (A. 195-196 at § 12.1), and their rights in the event of a tender offer (A. 196-197 at § 12.2). The Plan also delineates other

procedures with respect to the Common Stock held by Plan participants. (A. 973 at § 12.3.)⁴

Given the multiple references to the Stock Fund throughout the Plan, it is clear that the Plan presupposes that the Stock Fund is and will remain an investment alternative for the Plan participants. Indeed, as one district court recently observed in a factually similar case, “[a]ll of the provisions that prescribe, for example, how assets can be moved into and out of the Stock Fund would be at best incongruous and at worse meaningless if the Fund’s very existence was left purely to the discretion of the fiduciaries.” *Herrera v. Wyeth*, No. 08 Civ. 4688 (RJS), 2010 WL 1028163, at *6 (S.D.N.Y. Mar. 17, 2010).

Plaintiffs allege that the Plan fiduciaries’ decision to continue to offer the Stock Fund was improper because they knew that JPMorgan Chase had \$2.6 billion in undisclosed loss exposure to Enron Corporation. (A. 47-49.) Specifically, plaintiffs allege that JPMorgan Chase engaged in a series of transactions known as “prepays,” which essentially were disguised loans from JPMorgan Chase to Enron. (*Id.*) However, JPMorgan Chase allegedly failed to account for the prepays as loans in violation of Generally Accepted Accounting

⁴ Prior to the JPM/Chase merger, the Chase Plan included the “Chase Common Stock Fund,” which similarly invested “primarily” in Chase common stock. (A. 358; A. 424.) Like the Plan, the Chase Plan clearly intended to offer

Principles. (*Id.*) Once it became clear that Enron would be unable to repay JPMorgan Chase, the price of the Common Stock fell rapidly. (A. 69-74.) Plaintiffs further allege that one of JPMorgan Chase's subsidiaries systematically engaged in purported violations of the federal securities laws, which, once discovered, also contributed to the drop in the Common Stock's price. (A. 76-77.)

Thus, plaintiffs contend that the Plan fiduciaries breached their fiduciary duties to the Plan participants in a variety of ways. Count I of the plaintiffs' Complaint alleges that defendants negligently permitted Plan participants to purchase and hold Common Stock through the Stock Fund when it was imprudent to do so. (A. 47-49 at ¶ 3(a).) Count II alleges the defendants negligently misrepresented and failed to disclose material facts to Plan participants. (A. 49 at ¶ 3(b).) Count III alleges that certain defendants failed to appoint appropriate fiduciaries, failed to monitor them and failed to supply them with sufficient information. (A. 49 at ¶ 3(c).)

Defendants filed a motion for judgment on the pleadings pursuant to Federal Rule of Civil Procedure 12(c), which the District Court granted in its entirety. *Fisher v. JP Morgan Chase & Co.*, No. 03 Civ. 3252, 2010 WL 1257345, at *13 (S.D.N.Y. Mar. 31, 2010). In granting that motion, the District Court joined

Chase common stock as an investment alternative. (A. 375 at § 7.3; A. 376 at § 7.7(b); A. 394 at § 11.9; A. 396-397 at § 12.2; A. 397-398 at § 12.3.)

numerous courts in this Circuit and elsewhere holding that a presumption of prudence applies to a plan fiduciary's decision to continue to offer an employer stock fund as an investment alternative for plan participants when the plan clearly contemplates the existence of such a fund. *Id.* at *6-*7.

The District Court further held that a plaintiff may overcome the presumption of prudence “only ‘by establishing that the fiduciary abused its discretion by investing in employer securities.’” *Id.* (quoting *Moench v. Robertson*, 62 F.3d 553, 571 (3d Cir. 1995)). The District Court ruled that, to survive a motion to dismiss, a complaint therefore must contain facts that, if true, “would make it plausible that a fiduciary could not reasonably have believed that its chosen course of action regarding the offering of employer stock—whether the decision to do so was made through the exercise of its discretion or pursuant to a plan mandate—‘was in keeping with the settlor’s expectations of how a prudent trustee would operate.’” *Id.* at *7 (quoting *Edgar v. Avaya, Inc.*, 503 F.3d 340, 348 (3d Cir. 2007)).

The District Court found that plaintiffs had failed to plead facts that, if true, would rebut the presumption of prudence. As the District Court held, plaintiffs’ allegations “provide ‘no indication’ that, during the class period, JP Morgan’s ‘viability as a going concern was ever threatened.’” *Id.* at *9 (citing *Kirschbaum v. Reliant Energy, Inc.*, 526 F.3d 243, 255 (5th Cir. 2008)). Although

JPMorgan Chase stock price dipped significantly, the District Court noted that its Common Stock still retained significant value throughout the purported class period. *Id.* The Court, as result, dismissed plaintiffs' imprudence claim.

The District Court also dismissed plaintiffs' misrepresentation and disclosure claim based on alleged misstatements or omissions in SEC filings. The District Court held that ERISA does not impose an affirmative duty on plan fiduciaries to disclose non-public information beyond that required by the securities laws. *Id.* at *10. Further, the District Court found that plaintiffs had failed to point to any language in any SEC filing made within the purported class period that was materially misleading. *Id.* at *11.

Finally, the District Court dismissed plaintiffs' remaining claims as derivative of their other claims.

ARGUMENT

Respectfully, the District Court's dismissal of plaintiffs' Complaint should be affirmed. Defendants, as Plan fiduciaries, owe no duty to diversify or divest an employer stock fund, such as the Stock Fund, where there are no allegations suggesting that JPMorgan Chase's viability was ever threatened. Imposing such a duty would have a significant chilling effect on Congress's well-documented encouragement of employees owning employer stock through investment vehicles such as ESOPs and other employer stock funds within EIAPs.

We provide a more comprehensive and detailed description of the purposes and legislative history of ERISA, and studies and statistics demonstrating the success of employer stock funds, in order to illustrate how reversing the District Court and holding plaintiffs' claims to the legally sufficient would frustrate the purposes and operation of ESOPs and similar employer stock funds within EIAPs.⁵

A. Purposes Of ESOPs: The Importance Of Employee Stock Ownership

Though ESOPs and other EIAPs are governed by ERISA, their distinct characteristics and purposes led Congress to provide for certain exceptions from some of the requirements of traditional retirement plans under ERISA. They are exempted from ERISA's requirement that plan assets must be diversified, and they are also exempted from the prohibition against self-dealing, in so far as the acquisition and holding of employer securities would otherwise constitute self-dealing by the employer. *See* 29 U.S.C. § 1104(2). Specifically, "the diversification requirement and the prudence requirement (only to the extent that it

⁵ As noted above, an ESOP is one of "several types of pension plans categorized under ERISA as 'Eligible Individual Account Plans' or 'EIAPs.'" *Edgar v. Avaya, Inc.*, 503 F.3d 340, 347 (3d Cir. 2007) (citing 29 U.S.C. § 1107(d)(3)(A)). ESOPs and other employer funds within EIAPs both share the purpose of promoting employee investment in company stock. *Id.* Consequently, as to the issues before this Court, "nearly all of the points made about ESOPs apply

requires diversification) is not violated by acquisition or holding of qualifying employer securities.” *Moench v. Robertson*, 62 F.3d 553, 568 (3d Cir. 1995), quoting 29 U.S.C. § 1104(a)(2) (internal quotations omitted). As the Third Circuit explained:

[U]nder normal circumstances, ESOP fiduciaries cannot be taken to task for failing to diversify investments, regardless of how prudent diversification would be under the terms of an ordinary non-ESOP pension plan. ESOPs also are exempted from ERISA’s strict prohibition against dealing with a party in interest, and against self-dealing, that is, dealing with the assets of the plan in his own interest or for his own account.

Moench, 62 F.3d at 568, citing *Martin v. Feilen*, 965 F.2d 660, 665 (8th Cir. 1992), citing 29 U.S.C. § 1106(b)(1), *cert. denied*, 506 U.S. 1054 (1993) (internal quotations omitted).

ESOPs and employer stock funds within EIAPs are exempted from the diversification requirement and the prohibition against self-dealing because the nature and purpose of employer stock funds are substantially different from those of traditional retirement plans governed by ERISA. ESOPs were designed to invest primarily in the securities of the plan’s sponsoring company. *See Donovan v. Cunningham*, 716 F.2d 1455, 1458 (5th Cir. 1983), *cert. denied*, 467 U.S. 1251 (1984); *see also* 29 U.S.C. § 1107(d)(6)(A). Accordingly, “ESOPs, unlike pension

equally to EIAPs.” *In re Citigroup ERISA Litig.*, No. 07 Civ. 9790, 2009 WL 2762708, at *11 (S.D.N.Y. Aug. 31, 2009).

plans, are not intended to guarantee retirement benefits, and indeed, by its very nature ‘an ESOP places employee retirement assets at a much greater risk than does the typical diversified ERISA plan.’” *Moench*, 62 F.3d at 568, *quoting Martin*, 965 F.2d at 664; *see also Edgar v. Avaya, Inc.*, 503 F.3d 340, 347 (3d Cir. 2007); *Wright v. Oregon Metallurgical Corp.*, 360 F.3d 1090, 1094 (9th Cir. 2004) (explaining that EIAPs “place employee retirement assets at a much greater risk” than traditional ERISA plans).

Moreover, from a public policy perspective, ESOPs and other EIAPs that offer employer stock funds are expressly intended to “give employees an ownership interest and thus a stake in the financial successes and failures of the companies for which they work.” *In re Citigroup ERISA Litig.*, No. 07 Civ. 9790, 2009 WL 2762708 (S.D.N. Y Aug. 31. 2009), at *12, *quoting Steinman v. Hicks*, 352 F.3d 1101, 1103 (7th Cir. 2003).

As the case law in this area makes abundantly clear, employer stock funds, whether offered as an ESOP or as an investment alternative within an EIAP, serve different purposes than traditional retirement plans. As explained more fully in the sections that follow, the purposes of employer stock funds have been consistently expressed throughout their legislative history, with an eye towards expanding employee ownership.

B. Legislative History: Consistent Support For ESOPs

In light of its policy judgment that employee ownership of stock in their employers is a laudable goal, Congress has passed numerous pieces of legislation in order to further and encourage employee ownership through ESOPs and other employer stock funds within EIAPs. In so doing, Congress has repeatedly shown its support of ESOPs and employer stock funds by offering tax and other incentives to make their creation and maintenance both attractive and uncomplicated. Certainly, the statutes passed over the past several decades have done much to expand and strengthen the original purposes and benefits of those plans.

Shortly after the passage of ERISA in 1974, Congress began passing legislation supporting the formation of ESOPs. In 1975, Congress passed the Tax Reduction Act of 1975, which gave ESOPs a corporate tax credit of 11%. *See* Tax Reduction Act of 1975, Pub. L. No. 94-12, 89 Stat. 26 (1975).

The following year, Congress passed the Tax Reform Act of 1976 (“TRA 1976”) as the next significant piece of legislation to encourage employers to establish ESOPs. The text of the statute expressly demonstrates Congress’s concern that the purpose of ESOPs will be frustrated by applying rules applicable to traditional retirement plans:

The Congress is deeply concerned that the objectives sought by [the series of laws encouraging ESOPs] will be made unattainable by regulations and rulings which treat employee stock ownership plans as conventional retirement plans, which reduce the freedom of the employee trusts and employers to take the necessary steps to implement the plans, and which otherwise block the establishment and success of these plans.

TRA 1976, Pub. L. No. 94-455, § 803(h), 90 Stat. 1590 (1976), *quoted in Moench*, 62 F.3d at 569. The TRA 1976, as well as articulating Congress's intent and policy judgment with respect to ESOPs, also amended the Internal Revenue Code by doubling the dollar amount that could be allocated to a participant's account invested in employer stock in a given year. Jack Curtis & Anna Jeans, *ESOPs – A Decade of Congressional Encouragement*, 12 Tax Mgmt. Comp. Planning J. 377, 378 (Dec. 1984).

In 1981, Congress enacted another piece of legislation supporting the creation and retention of ESOPs—the Economic Recovery Tax Act (“ERTA”). *See* Economic Recovery Tax Act, Pub. L. 97-34, 95 Stat. 172 (1981). ERTA provided an important tax benefit for ESOPs. Prior to the enactment of ERTA, employers making contributions to ESOPs could only deduct up to 25% of interest paid on loans made from an ESOP. *Id.*, *cited in* Robert W. Smiley, Jr., *ESOP Legislative History Summary* in 2 Employee Stock Ownership Plans (2007), at A20-1. ERTA made such employer contributions fully deductible by the

employer. Curtis & Jeans, *ESOPs – A Decade of Congressional Encouragement*, 12 Tax Mgmt. Comp. Planning J. 380.

Three years later, Congress enacted the Tax Reform Act of 1984 (“TRA 1984”), which provided significant tax incentives for companies sponsoring ESOPs. TRA 1984, Pub. L. No. 98-369, 98 Stat. 494 (1984). The TRA 1984 provided the following benefits for ESOPs:

(a) A tax exclusion for commercial lenders of 50% of the interest income received on loans made to finance ESOP acquisition of employer stock; (b) A deferral of taxation on gains from a sale of stock to an ESOP by the owner of a closely held corporation to the extent that the ESOP owns at least 30% of the common equity after the transaction and the proceeds of the sale are reinvested in securities of other U.S. operating companies; (c) A tax deduction for dividends ‘passed through’ in cash to ESOP participants; and (d) A provision allowing an ESOP to assume the obligation for payments of estate tax liability in exchange for stock worth at least as much as the tax liability in those situations where closely held company stock qualified an estate for installment payments of federal estate tax.

Smiley, *ESOP Legislative History Summary*, *supra*, at A20-2, citing TRA 1984, Pub. L. No. 98-369.

Congress next enacted the Tax Reform Act of 1986, which provided even further support for ESOPs in the form of additional tax credits. Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 383 (1986).

The consistent Congressional support for ESOPs had the desired effect: it increased the popularity of ESOPs from 500,000 participants in 1974 to

ten million in 1986, a *twenty-fold* increase. Stephen Friedmann & Peter W. Gehnrich, *Pending Tax Legislation Will Change ESOP Rules*, 22 Pension World 42, 42 (Mar. 1986).

In 1996, Congress passed the Small Business Job Protection Act of 1996 (“SBJPA”). The SBJPA widened the availability of ESOPs by permitting S corporation shareholders to participate in ESOPs. Small Business Job Protection Act of 1996, Pub. L. No. 104-188, 110 Stat. 1755 (1996); *see also* Fred J. Diss, *Unwinding SESOPs*, 32 Tax Mgmt. Comp. Planning J. 362 (2004).

The following year, Congress enacted the Taxpayer Relief Act of 1997 (“1997 Act”) providing further tax benefits for ESOPs and clarifying the provisions of the SBJPA as they related to the taxation of S corporations. Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788 (1997); *see also* Smiley, *ESOP Legislative History Summary*, *supra*, at A20-3. The 1997 Act extended an important tax exemption to S corporation ESOPs previously available only to C corporations. *Id.* It also effectively eliminated any federal tax imposed on an S corporation’s income prorated to the ESOP by allowing S corporation ESOPs to distribute cash to plan participants and repealing any business income tax on the ESOP’s share of its S corporation sponsor’s taxable income. *Id.*

The Economic Growth and Tax Relief Reconciliation Act of 2001 (“EGTERRA”), was enacted to prevent abuse and to further encourage the creation

and operation of ESOPs. Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, 115 Stat. 38 (2001); *see also* John A. Kober, *The New S Corporation Law*, 30 Tax Mgmt. Comp. Planning J. 36 (2002).⁶

Congress again evidenced its support of ESOPs and employer stock funds within EIAPs in the American Jobs Creation Act of 2004 (“Jobs Act”), Pub. L. No. 108-357, 118 Stat. 1418 (2004). The Jobs Act encouraged the formation of ESOPs in S corporations by permitting S corporations to use distributions on stock held by its ESOP to repay loans used by the ESOP to acquire stock for employees. *See* Jobs Act, Pub. L. No. 108-357 at § 240; *see also* Press Release, The ESOP Association, The American Jobs Creation Act of 2004 – A Victory for ESOPs (November 2004), *available at* http://www.esopassociation.org/pdfs/tips11_04.pdf (last visited July 30, 2010). The Jobs Act “greatly benefits plan participants because it enables ESOPs to repay their loan amounts on a much faster basis.” Smiley, *ESOP Legislative History Summary*, *supra*, at A20-4.

Since the formal recognition of ESOPs in 1974 by their inclusion in ERISA, Congress has continuously examined and altered the operation and

⁶ EGTERA imposed certain new taxes, which may appear to have restricted the expansion of certain ESOPs. However, the taxes were intended to prevent abuse and were “promoted by supporters of ESOPs who authored the 1996 and 1997 S corporation ESOP laws in order to further the intent of Congress to promote widespread employee ownership through ESOPs and to ensure that

requirements of ESOPs, with the aim of making ESOPs easier and more attractive to establish for all types of companies, both large and small.

C. Further Support Of The Benefits Of ESOPs: Statistics and Studies

ESOPs and other employer stock funds within EIAPs have enjoyed not only continuous legislative support, but also academic support, through various studies and surveys. Those studies and surveys have consistently revealed the positive and beneficial effects of employee stock ownership for a company's growth and overall vitality. However, it is not just corporations that benefit from employee ownership. As the following studies demonstrate, employees of corporations with ESOPs or employer stock funds in EIAPs are more motivated and productive, undoubtedly due to their participation in the ownership of their employers.

In 1986, the National Center for Employee Ownership ("NCEO") published the first study to show a causal link between employee stock ownership and improved corporate performance. Michael Quarrey & Corey Rosen, *How Well is Employee Ownership Working?*, Harv. Bus. Rev., Sept.–Oct. 1987, at 126, *cited in* Corey M. Rosen, *Employee Ownership and Corporate Performance*, in 1

arrangements that did not do so would not lead to cutbacks in [other exemptions]." Smiley, *ESOP Legislative History Summary*, *supra*, at A20-3.

Employee Stock Ownership Plans, *supra*, at 2–1, 2–2; *see also* Gerald Kalish, *ESOPs: The Handbook of Employee Stock Ownership Plans* 275 (1989).

The NCEO study examined the performance of employee ownership companies five years before and five years after they set up ESOPs, finding that “ESOP companies had sales growth rates 3.4% per year higher and employment growth rates 3.8% per year higher in the post-ESOP period than would have been expected based on pre-ESOP performance.” *Id.* As the results of the study indicated, companies with ESOPs performed better and grew at a higher rate than their competitors after establishing ESOPs. Thus, ESOPs are good for businesses and their employees, generating increased productivity and resulting in more jobs.

Similarly, two studies—one in New York in 1992 and the other in Washington State in 1993—concluded that corporate performance increased due to the existence of ESOPs within a company, combined with participative management. Gorm Winther, *Employee Ownership: A Comparative Analysis of Growth Performance* (1995) (the “New York Study”); Gorm Winther & Richard Marens, *Participatory Democracy May Go a Long Way: Comparative Growth Performance of Employee Ownership Firms in New York and Washington States*, *Economic & Industrial Democracy*, Aug. 1997, at 393–422 (the “Washington Study”), *cited in* Rosen, *supra*, at 2–2 to 2–3. For example, in the Washington

Study, companies combining ESOPs and participative management grew in employment 10.9% per year, while sales grew 6% per year more. *Id.*

In 2000, in perhaps the largest ESOP study completed to date, researchers tracked 1,100 ESOP companies with 1,100 comparable non-ESOP companies and recorded their performance for over a decade. Joseph Blasi & Douglas Kruse, *Largest Study Yet Shows ESOPs Improve Performance and Employee Benefits* (“Rutgers Study”), available at <http://www.nceo.org/main/article.php/id/25> (last visited July 30, 2010). The Rutgers Study found that “ESOPs appear to increase sales, employment, and sales per employee by about 2.3% to 2.4% per year over what would have been expected absent an ESOP.” *Id.* The study also found that ESOP companies are more likely to stay in business than comparable companies that do not offer ESOPs. *Id.*

On August 17, 2009, the Employee Ownership Foundation released the results of its 18th annual “ESOP Economic Performance Survey” (the “Performance Survey”). Press Release, Employee Ownership Foundation, ESOP Companies Outperform Stock Market in 2008 (Aug. 17, 2009), available at http://www.esopassociation.org/media/media_stock_market_outperform.asp (last visited July 30, 2010). The Performance Survey revealed, as it has every year since the survey’s creation, that an overwhelming majority of companies surveyed report that the creation of ESOPs was a “good business decision that has helped the

company.” *Id.* In addition, the Performance Survey revealed that “88.5% of ESOP companies outperformed the stock market in 2008,” even despite the severe economic downturn. *Id.* The President of the Employee Ownership Foundation, J. Michael Keeling, made the following remarks regarding the Performance Survey:

In a turbulent year, these results speak wonders for the power of employee ownership. On the other hand, this survey and most news reports show that American companies are hurting, profits are down, and layoffs are taking place across the country. Objective academic research evidences that employee owned companies are higher performing, have high employee retention rates, and have employees that are more motivated and productive. Our national leaders need to promote policies to encourage more companies to become employee owned through an ESOP to create a more fair and equitable society.

Id.

Companies that offer employer stock funds enjoy more success, especially when combined with participative management, than those without employee ownership. Importantly, employees benefit from stock ownership in very real ways. Employer stock funds produce more satisfied and productive employees, which creates a more successful corporation, and in turn spurs job creation and overall growth.

D. The Purposes And Legislative History Of ESOPs, Along With Statistics And Studies, Strongly Support A Decision By This Court Affirming The District Court's Order

As is clear from the above-cited legislative history and academic and empirical studies, employee stock ownership plays a critical role in the fabric of the American workforce, with important benefits accruing to both employer-companies and their employee-stockholders. Since it enacted ERISA 35 years ago, Congress has continuously and repeatedly incentivized the use of ESOPs and other employer stock funds within EIAPs, with the aim of making employee stock ownership easier and more attractive to establish for all types of companies, large and small.

If plaintiffs' claims were allowed to proceed, companies would surely refrain from establishing and retaining such plans as a result of the unsettled liability issues that would be presented. Forcing fiduciaries to decide between either divesting or diversifying their employer stock funds when the value of the stock value declines, or to adhere to plan terms that clearly contemplate that the Plan will include an employer stock choice despite the decline—facing liability no matter the decision—would place companies and their fiduciaries in an impossible situation. When faced with that impossible choice, the most rational course of action would be to avoid the decision entirely and forgo offering an ESOP or similar employer stock funds within EIAPs as an investment option.

We respectfully urge this Court to recognize the deleterious effects that a reversal of the lower court's decision would have on the progression and steady growth of ESOPs to date. Not only would such a reversal frustrate decades of Congressional policy, but it would also prevent companies and employees from enjoying the many benefits of ESOPs, including enhanced performance and growth.

In order to avoid those undesirable results, we respectfully request that this Court affirm the District Court's decision. That result would promote the original purpose of employer stock funds, and, as the District Court observed, ERISA's "strong preference for employee ownership in the context of ESOPs and EIAPs." *Fisher*, 2010 WL 1257345, at *6.

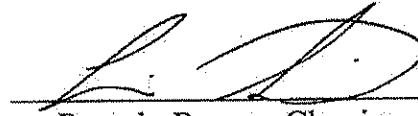
CONCLUSION

For all of the foregoing reasons, we urge this Court to affirm the decision of the Southern District of New York and dismiss the plaintiffs' Amended ERISA Complaint in its entirety.

Dated: August 4, 2010

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

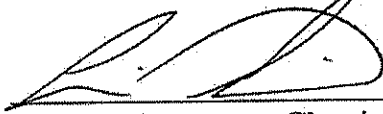
1. This brief complies with the type-volume limitation of Fed. R. App. 32(a)(7)(B) and Fed. R. App. 29(d) because it contains 5,251 words, excluding the parts of the brief exempted by Fed. R. App. 32(a)(7)(B)(iii).

2. This brief complies with the typeface requirements of Fed. R. App. 32(a)(5) and the type style requirements of Fed. R. App. 32(a)(6) because it has been prepared in a proportionally spaced typeface using Microsoft Word 2003 in Times New Roman size 14-point font.

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