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IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
PEORIA DIVISION

JACKIE LYSENGEN, on behalf of the Morton Buildings, Inc. Leveraged Employee Stock Ownership Plan, and on behalf of a class of all other persons similarly situated, **Plaintiff,** **v.** **ARGENT TRUST COMPANY, JAN ROUSE, and EDWARD C. MILLER** **Defendants.**	**Case No. 1:20-cv-01177**

PLAINTIFF'S OPPOSITION TO DEFENDANTS' MOTION TO DISMISS

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Defendants' Motion to Dismiss (Dkt. 17) should be denied for numerous reasons. The Complaint (Dkt. 1) includes sufficient factual allegations—particularly given that ERISA plan participants lack visibility into due diligence processes in ESOP stock purchase transactions—to satisfy the *Twombly/Iqbal* pleading standard and put Defendants on notice of the claims against them. The motion conflates Plaintiff's prohibited transaction and breach of fiduciary duty claims in an attempt to foist the burden of pleading around an affirmative defense onto her. And the motion relies on irrelevant material outside the Complaint to argue that Plaintiff's allegations have been or can been refuted.

1. STANDARD FOR STATING ERISA CLAIMS

"In our system of notice pleading, complaints need only plead facts sufficient to put defendants on notice of the claims against them." *R3 Composites Corp. v. G&S Sales Corp.*, 960 F.3d 935, 942 (7th Cir. 2020). "[T]he federal courts require notice pleading, not fact pleading complete with all the minutiae. A complaint need only provide notice of a plausible claim . . ." *Auto Driveaway Franchise Systems, LLC v. Auto Driveaway Richmond, LLC*, 928 F.3d 670, 675 (7th Cir. 2019), *citing Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007), *and Ashcroft v. Iqbal*, 556 U.S. 662 (2009); *see also* Fed. R. Civ. P. 8(a)(2) (a viable pleading must include "a short and plain statement of the claim showing that the pleader is entitled to relief").

ERISA is a "remedial statute to be liberally construed in favor of employee . . . participants." *Kross v. W. Elec. Co., Inc.*, 701 F.2d 1238, 1242 (7th Cir. 1983). In the Seventh Circuit, a complaint brought under ERISA satisfies Rule 8(a)(2) "as long as the facts alleged tell a plausible story." *Allen v. GreatBanc Trust Co.*, 835 F.3d 670, 678 (7th Cir. 2016); *accord Alexander v. United States*, 721 F.3d 418, 422 (7th Cir. 2013) ("[T]he plausibility requirement demands only that a plaintiff provide sufficient detail 'to present a story that holds together.'")

(*quoting Swanson v. Citibank, N.A.*, 614 F.3d 400, 404 (7th Cir. 2010)). A complaint alleging breaches of ERISA fiduciary duty should be "read as a whole, not parsed piece by piece to determine whether each allegation, in isolation, is plausible." *Braden v. Wal-Mart Stores, Inc*., 588 F.3d 585, 594 (8th Cir. 2009) (citations omitted); *see also Allen*, 835 F.3d at 678.

2. ARGUMENT

a. Plaintiff states claims that Defendants violated ERISA's Prohibited Transaction Rules.

The Defendants here are not the first ESOP defendants to conflate prohibited transaction claims and breach of fiduciary claims in a motion to dismiss. But the Seventh Circuit, and courts following its clear precedent, have seen through these tactics, rejected them, and noted the distinct elements and burdens that apply to these separate claims. Once Plaintiff's prohibited transaction claims are disentangled from the breach of fiduciary duty claim, there is no question that Plaintiff satisfied Fed. R. Civ. P. 8.

To state an ERISA § 406(a) prohibited transaction claim against Defendant Argent Trust Company ("Argent") (Count I), Plaintiff must allege facts plausibly showing that Argent (1) was a fiduciary with respect to the Morton Buildings, Inc. Leveraged Employee Stock Ownership Plan (the "Plan"), (2) caused the Plan to engage in a transaction, and (3) knew or should have known the transaction was (a) a sale or exchange of Morton Buildings, Inc. ("Morton") stock between the Plan and a party in interest (§ 406(a)(1)(A) claim); (b) a lending of money or other extension of credit between the Plan and a party in interest (§ 406(a)(1)(B) claim); or (c) a transfer of Plan assets to a party in interest (§ 406(a)(1)(D) claim). Plaintiff alleges all those elements:

- Argent, as trustee for the Plan, was a fiduciary; Compl. ¶¶ 1, 6, 16-17, 41-42;

- Argent approved a stock transaction between the Plan and parties in interest; *Id*. ¶¶ 5, 7-8, 43;
- Morton was a party in interest to the Plan; *Id*. ¶¶ 37-38;
- Defendants Jan Rouse and Edward Miller (the "Selling Shareholders") were parties in interest because they were 10% or more shareholders of Morton; Rouse was a Director of Morton at the time of the ESOP Transaction; and Miller was a Director and officer of Morton at that time; *Id*. ¶¶ 19-20, 40;
- The Plan borrowed money from a party in interest—both Morton and a selling shareholder—to finance the Plan's purchase; *Id*. ¶¶ 5, 45; and
- The Plan paid its assets to a party in interest for the Morton stock. *Id*. ¶¶ 5, 7-8, 19-20, 38, 40, and 43.

To state an ERISA § 406(b) prohibited transaction claim against Argent (Count I), Plaintiff needs to allege facts sufficient to make it plausible that Argent (1) acted in the ESOP Transaction on behalf of the counterparties to the Plan, the McKinneys (§ 406(b)(2) claim), or (2) received consideration for its own personal account from Morton, which dealt with the Plan as lender in ESOP Transaction (§ 406(b)(3) claim). She did:

- Argent acted on behalf of the McKinneys in the ESOP Transaction; Compl. ¶¶ 7, 53-54, 74;
- Argent received consideration from Morton; *Id*. ¶¶ 57-58, 61, 75; and
- Morton was a lender in the ESOP Transaction. *Id*. ¶¶ 5, 45.

Likewise, to state a claim for a prohibited transaction against the Selling Shareholders (Count IV), Plaintiff needs to allege similar facts that they had actual or constructive knowledge of the circumstances that rendered the ESOP Transaction a prohibited transaction, and Plaintiff must be seeking "appropriate equitable relief." *See* 29 U.S.C. § 1132(a)(3); *Harris Trust & Sav. Bank v. Salomon Smith Barney, Inc.*, 530 U.S. 238 (2000). Again, Plaintiff alleges sufficient facts. The Selling Shareholders were aware of the prohibited transactions because they were directors and/or officers of Morton at the time of the ESOP Transaction; Morton appointed Argent as trustee; and the Selling Shareholders sold their shares in the ESOP Transaction. Compl. ¶¶ 8, 19-20, 40-41, 47, 99, 101-102. And Plaintiff seeks equitable relief from the Selling Shareholders. *Id.* ¶ 104.

Indeed, Defendants never argue that Plaintiff does not allege the actual elements of her prohibited transaction claims. Instead, they argue the prohibited transaction claims should be dismissed because "the ESOP did not overpay for Morton stock." Def. Mem. (Dkt. 18) p.18. But that goes to Defendants' ERISA § 408(e) affirmative defense that the Plan paid no more than adequate consideration for Morton stock. Defendants are therefore not arguing that Plaintiff failed to state a claim but rather that Plaintiff did not rebut the affirmative defense of adequate consideration. Defendants must know their argument has been addressed and rejected by the Seventh Circuit with respect to ESOPs and this very exemption. "[A]n ERISA plaintiff need not plead the absence of exemptions to prohibited transactions." *Allen*, 835 F.3d at 676; *see also Keach v. U.S. Tr. Co. N.A.*, 313 F. Supp. 2d 818, 866 (C.D. Ill. 2004) (Mihm, J.), *aff'd sub nom.* 419 F.3d 626 (7th Cir. 2005) ("A fiduciary who claims that ERISA § 408 exempts a transaction from the prohibitions of ERISA § 406(a) has the burden of proving that the employer securities were purchased for no more than adequate consideration within the meaning of ERISA § 3(18), 29 U.S.C. § 1002(18)"); *Fish v. GreatBanc Tr. Co.*, 749 F.3d 671, 687 (7th Cir. 2014). Defendants' attempts to dance around this Circuit's controlling authority speaks volumes about their motion. Further, the § 408(e) affirmative defense is only relevant to § 406(a) claims concerning the stock transaction, which means it is not a basis for dismissal of Plaintiff's § 406(a)(1)(B) and § 406(b) claims concerning the loan transaction and payments to Argent.

The analysis can end there. Defendants' sole basis for dismissing Counts I and IV is that Plaintiff failed to allege facts that the Seventh Circuit and this Court has said they are under no obligation to plead. Defendants' motion to dismiss Counts I and IV should be denied.

Defendants cite a decision whose parenthetical states the proposition that "[W]hen a plaintiff's complaint nonetheless sets out all of the elements of an affirmative defense, dismissal under Rule 12(b)(6) is appropriate." Def. Mem. p.18 (*citing NewSpin Sports, LLC v. Arrow Elecs., Inc.*, 910 F.3d 293, 299 (7th Cir. 2018)). But nowhere does Plaintiff's Complaint establish that Defendants have met their adequate consideration defense. If Defendants are mistakenly suggesting Plaintiff's only support for her eventual rebuttal to their adequate consideration defense are the swings in Morton's stock price, that is not a factual allegation on which their claims hinge, as discussed below. There is no basis to argue that Plaintiff pleaded herself out of court on the prohibited transaction claims. Furthermore, the burden of proof on § 408 affirmative defenses does not shift to the plaintiff due to allegations in a complaint. The Eighth Circuit explains:

> Appellees argue that Braden's allegations "put the exemption in play" and he therefore must plead sufficient facts to show that the payments were unreasonable. To the contrary, a plaintiff need not plead facts responsive to an affirmative defense before it is raised. See, e.g., *Goodman v. Praxair, Inc.*, 494 F.3d 458, 465-66 (4th Cir. 2007). Even if Braden's allegation of unreasonableness were seen as raising the exemption for pleading purposes, that does not mean he thereby assumes the burden of proof on the issue. See 5 Charles Alan Wright & Arthur R. Miller, Federal Practice and Procedure § 1276, at 624-25 (3d ed. 2004).

Braden, 588 F.3d at 601 n.10. And even if the burden of proof could *arguendo* shift to a plaintiff on a § 408 defense, dismissal would be improper here because Plaintiff's potential rejoinder to Defendant's affirmative defense was not "foreclosed by the allegations in the complaint."

Matassarin v. Grosvenor, No. 5:13–CV–913, 2015 WL 12734757, at *1 (W.D. Tex. July 24, 2015) (quoting *Jaso v. The Coca Cola Co.*, 435 F. App'x 346, 352 (5th Cir. 2011), and *Goodman v. Praxair, Inc.*, 494 F.3d 458, 466 (4th Cir. 2007)); *see also Kincaid v. Sangamon Cty.*, 435 F. App'x 533, 536 (7th Cir. 2011) (reversing dismissal and noting the "existence of a valid affirmative defense" must be "so plain from the face of the complaint that the suit can be regarded as frivolous"); *Brownmark Films v. Comedy Partners,* 682 F.3d 687, 690 (7th Cir.2012) ("courts should usually refrain from granting Rule 12(b)(6) motions on affirmative defenses").

b. Plaintiff States a Claim that Argent Breached its Fiduciary Duties.

Argent's attempt to dismiss the breach of fiduciary duty claim fares no better. To state a claim for breach of fiduciary duty, Plaintiff needs to allege: Argent was a fiduciary to the Plan; Argent breached its fiduciary duty; and the breach resulted in harm to the Plan. *See Allen*, 835 F.3d at 678. Plaintiff did exactly that. Plaintiff alleges Argent was the Trustee of the Plan and as such was a fiduciary. Compl. ¶ 16. Plaintiff includes numerous allegations which, if established, show Argent failed to undertake an appropriate and independent investigation of Morton's fair market value and otherwise put its own interests before the interests of the Plan:

- "Morton provided financial projections to Argent for the valuation for the ESOP Transaction. The financial projections were unreasonably optimistic." *Id.* ¶ 48.
- "The Plan paid a premium to remove Selling Shareholders including Getz family members, who were involved in other litigation, from ownership of Morton." *Id.* ¶ 50.
- "The Plan paid more than fair market value for Morton due to this payoff as well as a faulty valuation of the company." *Id.* ¶ 50.

- "Argent's due diligence in the ESOP Transaction was less extensive and thorough than the due diligence performed by third-party buyers in corporate transactions of similar size and complexity." *Id.* ¶ 53.
- "The Plan overpaid for Morton stock in the ESOP Transaction due to Argent's reliance on unrealistic growth projections, unreliable or out-of-date financials, improper discount rates, inappropriate guideline public companies for comparison, and/or its failure to test assumptions, failure to question or challenge underlying assumptions, and/or other factors that rendered the valuation of Morton stock in the ESOP Transaction faulty." *Id.* ¶ 53.
- "Incentives to Argent to act in favor of the Selling Shareholders in the ESOP Transaction included the possibility of business from sellers of companies who understood that Argent applied a lesser degree of due diligence in ESOP purchases of businesses than is typical for non-ESOP-buyers' purchases of businesses, engagement as the Plan's ongoing trustee after the ESOP Transaction and the fees paid for that engagement, and engagement as the custodian for the Morton Buildings, Inc. 401(k) and ESOP, which is also sponsored by Morton, and the fees paid for that engagement. Effective May 8, 2017, Argent was appointed custodian of the Morton Buildings, Inc. 401(k) and ESOP for its investments in Morton common stock and Fidelity Investments Money Market Treasury Portfolio I." *Id.* ¶ 54.
- "Argent was required to undertake an appropriate and independent investigation of the fair market value of Morton stock in or about May 2017 in order to fulfill its fiduciary duties, and an appropriate investigation would have revealed that the

valuation used for the ESOP Transaction did not reflect the fair market value of the Morton stock purchased by the Plan.” *Id*. ¶ 85.

- Plaintiff alleged that the breach resulted in harm to the Plan. *Id*. ¶¶ 3, 4, 7, 87.

Plaintiff’s allegations of breach need only “provide sufficient detail to present a story that holds together.” *Allen*, 835 F.3d at 678. As in *Allen*, the central allegations in Plaintiff’s Complaint is that the trustee (here Argent) failed to conduct an adequate inquiry into the value of the subject company’s stock. *See id*. In *Allen*, the Seventh Circuit noted that “[a]lthough the plaintiffs could not describe in detail the process [the trustee] used, no such precision was essential. It was enough to allege facts from which a factfinder could infer that the process was inadequate.” *Id*. The Court continued, “a district court errs in making the assumption that [the plaintiff] was required to describe directly the ways in which appellees breached their fiduciary duties; rather, it is sufficient for a plaintiff to plead facts indirectly showing unlawful behavior.” *Id*. (citation omitted). “This is particularly true in ERISA cases because ERISA plaintiffs generally lack the inside information necessary to make out their claims in detail unless and until discovery commences” and therefore “an ERISA plaintiff alleging breach of fiduciary duty does not need to plead details to which she has no access, as long as the facts alleged tell a plausible story.” *Id*. (citation omitted).[1]

Applying that standard, courts have found allegations similar to those alleged here—that the loan came from the employer-seller; that the valuation the trustee relied on had numerous

[1] While Defendants improperly cast them as “improper *ipse dixit* assertions of liability” (Def. Mem. p.10), factual allegations in the nature of “on information and belief” are allowed under the Rules, particularly where information is particularly within the possession and control of the defendant. *See Arista Records, LLC v. Doe 3*, 604 F.3d 110, 120 (2d Cir. 2010); *Johnson v. Johnson*, 385 F.3d 503, 531 (5th Cir. 2004). The “telling confession prefac[ing]” certain allegations, which Defendants criticize (Def. Mem. p.10), is recommended by Rule 11(b)(3).

flaws—were sufficient to state a claim. *Allen*, at 678-79; *see also Neil v. Zell*, 677 F. Supp. 2d 1010, 1020 (N.D. Ill. 2009), *as amended* (Mar. 11, 2010) ("Plaintiffs' allegations include, among others, that the deal saddled Tribune with so much debt that the company was very unlikely to succeed, that [the trustee] failed to ensure that the expert advice it sought was reasonable, and that [the trustee] failed to conduct its own thorough review of the deal."); *Zavala v. Kruse-W., Inc.*, 398 F. Supp. 3d 731, 746 (E.D. Cal. 2019) (plaintiffs stated a breach of fiduciary duty claim on the basis that the "stock based on unrealistic management projections" and "[a] prudent fiduciary who had conducted a prudent investigation would have concluded that ESOP was paying more than fair market value for the [subject] stock and/or the debt incurred in connection with the Transaction was excessive"); *Woznicki v. Raydon Corp.*, No. 618CV2090ORL78GJK, 2019 WL 5702728, at *2 (M.D. Fla. Nov. 4, 2019) (denying motion to dismiss where plaintiff alleged the trustee "fail[ed] to conduct an appropriate investigation")

Argent attempts to distinguish *Allen*'s controlling precedent in two ways: (1) the allegations listed above do not, for some reason, constitute "facts" as it conceive of that term and (2) there are other "facts" that exist somewhere outside the Complaint that run counter to Plaintiff's allegations. Neither argument is sufficient to dismiss the breach of fiduciary duty claim at the pleading stage.

i. Argent's Concept of "Facts" and Pleading Requirements are Misplaced.

Argent deems the factual allegations, bullet-pointed above, "naked assertions" or "legal conclusions." Def. Mem. p.10. It is unclear what would rise to the level of "fact" that would satisfy Argent but it is clear, based on the two cases it relies on, that its characterization lacks legal support. One of the decisions requiring additional factual support involved the heightened pleading standards of Fed. R. Civ. P 9(b). *See Pirelli Armstrong Tire Corp. Retiree Med. Benefits*

Tr. v. Walgreen Co., 631 F.3d 436, 442 (7th Cir. 2011). That pleading standard does not apply here. And the other case cited by Argent involved a plaintiff who *was also the administrator of the plan* and was thus "in a position to plead its claims with greater factual detail than is typically accessible to plaintiffs prior to discovery." *See Pension Ben. Guar. Corp. ex rel. St. Vincent Catholic Med. Centers Ret. Plan v. Morgan Stanley Inv. Mgmt. Inc.*, 712 F.3d 705, 709 (2d Cir. 2013). Again, those facts are not applicable here because Ms. Lysengen was not an insider and therefore was in the position of most ESOP plaintiffs who "lack the inside information necessary to make out their claims." *Allen*, 835 F.3d at 678. In short, Argent's attempts to define facts as "innuendo" and impose heightened pleading standards fails as a basis to dismiss this well-pleaded claim.

Argent continues to rely on cases outside the Rule 8(a) ESOP context in the next section of its motion, which contends Plaintiff's allegations "do not support liability" for "process-based" claims. See Def. Mem. pp.13-15. Despite the litany of cases, including *Allen*, noting that ERISA plaintiffs lack visibility into the fiduciary's process, Argent tries to take advantage of that information discrepancy and avoid discovery. Plaintiff alleges "Argent's due diligence in the ESOP Transaction was less extensive and thorough than the due diligence performed by third-party buyers in corporate transactions of similar size and complexity. The Plan overpaid for Morton stock in the ESOP Transaction due to Argent's reliance on unrealistic growth projections, unreliable or out-of-date financials, improper discount rates, inappropriate guideline public companies for comparison, and/or its failure to test assumptions, failure to question or challenge underlying assumptions . . ." Compl. ¶ 53. Argent again deems those factual allegations "speculation." Def. Mem. p.14.

More importantly, Argent's motion is based on the theory that the Complaint should be judged on an allegation-by-allegation basis. That approach ignores the requirement that a complaint "should be read as a whole, not parsed piece by piece to determine whether each allegation, in isolation, is plausible," which is especially vital to ERISA actions in which private individuals take the "important role" Congress placed on them to "enforc[e] ERISA's fiduciary duties" and "prevent through private civil litigation misuse and mismanagement of plan assets." *Braden*, 588 F.3d at 594, 597–98 (citations, punctuation omitted). A "holistic evaluation of an ERISA complaint's factual allegations" is counseled by plaintiff-participants' "limited access to crucial information" regarding facts that "tend systemically to be in the sole possession of defendants." *Id.* at 598; *accord Allen.*, 835 F.3d at 678; *cf. Johnson*, 385 F.3d at 531 n.19 ("'information and belief' pleadings are generally deemed permissible under the Federal Rules, especially in cases in which the information is more accessible to the defendant") (citing 5 Charles Allan Wright & Arthur R. Miller, Federal Practice and Procedure § 1224 (2d ed. 1990)).

Ignoring all of those cases that involved facts similar to the ESOP context here, and after improperly asking the Court to review allegations in isolation, Argent is forced to import decisions from 401(k) Plan fund selection cases that have minimal relevance for present purposes. Argent cites *Meiners v. Wells Fargo & Co.*, 898 F.3d 820, 821 (8th Cir. 2018), in which the plaintiff alleged his employer breached its fiduciary duties by: (1) retaining the employer's proprietary investment funds as options for the employees' 401(k) retirement plan, and (2) defaulting to these proprietary investment funds for plan participants who did not elect other options. The court noted a distinction between "facts about the funds themselves, which ERISA plaintiffs can research, or facts about the fiduciary's internal processes, which ERISA plaintiffs generally lack." *Id.* at 822–23. The plaintiff in *Meiners* failed to allege sufficient facts on publicly available performance information and thus provide the "benchmark" required by that Circuit in 401(k) fund cases. In this instant case, the "benchmark" requirement does not apply because this is not a 401(k) fund case and, therefore, Plaintiff is limited to those "facts about the fiduciary's internal processes, which ERISA plaintiffs generally lack." *Id*. at 822–23.

Argent will have its opportunity to prove that Plaintiff's allegations are not accurate, and are indeed "speculation," but declaring them so at the pleading stage does not make it so.

ii. Defendants Have Not Established Issue Preclusion.

Defendants next ask the Court to consider "facts" outside the Complaint that they claim defeat Plaintiff's well-pleaded allegations. Defendants argue that, unlike in *Allen* and other ESOP cases where similar motions to dismiss were denied, the "details of the transaction were litigated previously and remain publicly available" and should be considered at this pleading stage. Def. Mem. p.12. Defendants' attempt to distinguish this case from *Allen* and so many others on the basis of state court litigation involving different parties, different claims, and even a different time period fails for numerous reasons. Defendants skirt around what they are actually asking the Court to do—apply "issue preclusion"—because they cannot meet issue preclusion standards. The gist of Defendants' argument is that a decision issued on November 14, 2016 in Illinois Circuit Court, Tazewell County (the "State Court Decision"), is dispositive of claims raised in Plaintiff's Complaint and that Plaintiff should have included the decision in her Complaint. In so arguing, Defendants urge this Court to accept as true, ignoring all the rules of nonmutual collateral estoppel and res judicata, facts litigated by other parties in another case.

The problems with Defendants' argument begin with the very case they rely on. Contrary to Defendants' suggestion, the Court in *Parker v. Lyons*, No. 11-CV-1441, 2013 WL 12303944, at *7 (C.D. Ill. Jan. 10, 2013), did not dismiss the complaint based on a state-court order. But that court *did* lay out the test for issue preclusion: "(1) the issue decided in the prior adjudication is identical with the one presented in the suit in question, (2) there was a final judgment on the merits in the prior adjudication, and (3) the party against whom estoppel is asserted was a party or in privity with a party to the prior adjudication." *Id.* (citation omitted). As in *Parker*, issue preclusion does not apply here.

Plaintiff here was neither a party to nor in privity with a party in the State Court Decision. Likewise, the issues in the State Court Decision were not identical to those at issue here. Most importantly, the State Court Decision was entered in November 2016, and focuses on events before that date. The transaction before this Court occurred on May 8, 2017—after Judge Keith rendered his decision. *See* Compl. ¶¶ 1, 5. So it is just not true that "the transaction was litigated at length" in the State Court Decision, as Defendants claim, because the ESOP transaction before this Court *would not even take place until six months after the State Court Decision was entered.* Given that events from October 2016 to May 2017 had not yet occurred when the State Court decision was rendered, Defendants' representations that the state court resolved questions as to whether the share price paid by the Plan was "fair" or "negotiated in an arm's length process" (Def. Mem. p.11) is laughable.

There are additional reasons why issue preclusion does not apply. This is an ERISA action where the focus will be on Argent's process and decisions and the terms of its engagement. As noted above, it will be Argent's burden to show that the Plan paid no more than "adequate consideration," which under ERISA imposes a two-fold requirement: (1) the price paid must reflect the fair market value of the asset, and (2) the trustee must conduct a careful and independent investigation of the circumstances prevailing at the time of the investment. *Donovan* *v. Cunningham*, 716 F.2d 1455, 1467–68 (5th Cir. 1983).[2] "In reviewing the acts of ESOP fiduciaries under the objective prudent person standard, courts examine both the process used by the fiduciaries to reach their decision as well as an evaluation of the merits. This is true when determining whether an act was prudent under the general standard of [29 U.S.C.] § 1104 and whether an otherwise prohibited transaction under § 1106 is saved by 'adequate consideration' under § 1108(e)." *Fish*, 749 F.3d at 680 (*quoting Eyler v. Comm'r of Internal Revenue*, 88 F.3d 445, 455 (7th Cir. 1996)).

Although a trustee needs a valuation report, "[a]n independent appraisal is not a magic wand that fiduciaries may simply wave over a transaction to ensure that their responsibilities are filled." *Fish*, 749 F.3d at 680; *Donovan*, 716 F.2d at 1474. Rather, an ERISA trustee properly relies upon an expert's advice where he "'(1) investigate[s] the expert's qualifications, (2) provide[s] the expert with complete and accurate information, and (3) make[s] certain that reliance upon the expert's advice is reasonably justified under the circumstances.'" *Bussian v. RJR Nabisco, Inc.*, 223 F.3d 286, 301 (5th Cir. 2000) (*quoting Howard v. Shay*, 100 F.3d 1484, 1489 (9th Cir. 1996)) (additional citations omitted). "It is also important that the trustee and any advisors take care to avoid any conflicts of interest to ensure that they remain meaningfully

[2] The Department of Labor proposed a regulation elaborating on the definition of "adequate consideration." *See* Proposed Regulation Relating to the Definition of Adequate Consideration, 53 Fed. Reg. 17,632, 17,633 (May 17, 1988) (to be codified at 29 C.F.R. § 2510–3(18)(b)) ("Proposed Regulation"). Although the Proposed Regulation was not finalized, the Seventh Circuit has held that "this court and other courts of appeals have adopted this two-part standard for evaluating the adequacy of consideration." *Keach*, 419 F.3d at 636 n.5 (citing *Eyler*, 88 F.3d at 454-55); *accord Fish*, 749 F.3d at 680-81 (describing the "two requirements"). Defendants' representation that "adequate consideration" is about no more than the fair market value of a stock and a mere "regulators' term" (Def. Mem. p.2) ignores the due diligence component of adequate consideration and that it is required by the ERISA definition itself. *See* ERISA § 3(18), 29 U.S.C. § 1002(18) (adequate consideration is "the fair market value of the asset *as determined in good faith* by the trustee or named fiduciary pursuant to the terms of the plan and in accordance with regulations promulgated by the Secretary") (emphasis added).

independent from the sellers and their team of advisors. Otherwise, there is a significant risk that the ESOP's representatives will not sufficiently challenge the assumptions and representations that they are fed by those on the sell side of the transaction." *Brundle v. Wilmington Tr. N.A.*, 241 F. Supp. 3d 610, 633 (E.D. Va. 2017) (quotation omitted), *aff'd*, 919 F.3d 763 (4th Cir. 2019).

There were no ERISA claims resolved in the State Court Decision. Argent was (briefly) a party in the State Court Decision but a bit player at best. Nor was the Plan a party. The focus of the State Court Decision was the action of a minority shareholder in proposing, and then interfering with, a potential ESOP transaction. Argent's minimal role in the State Court Decision is not surprising given that the ESOP Transaction had not yet occurred and Argent was dismissed as a party a month after the case was filed. Argent's involvement is not even mentioned in the State Court Decision until page 23. Given that Argent was not a party to the case during the trial, it is not surprising that Argent's process was not given the probing and evaluation, under the ERISA-specific standards detailed above, that will be the focus of this case.

iii. Defendants' Justifications Must Be Ignored at the Pleading Stage.

Defendants' final attempt to distinguish *Allen* is that Plaintiff's allegations can be explained away. Def. Mem. pp.15-20. Although based on a false premise that the Complaint contains only two factual allegations—a point easily refuted above—Plaintiff will address Defendants' two arguments.

Defendants mistakenly accuse Plaintiff of stating facts "that are demonstrably wrong" (Def. Mem. p.1), while themselves withholding from their submission to the Court the portion of the Form 5500 that proves Plaintiff's allegation. Plaintiff noted that the valuation of Morton stock rose from \$58.04 on December 31, 2016 to \$75.25 on the date of the ESOP Transaction just over four months later on May 8, 2017, which greatly increased the amount the Plan paid for

Morton stock. Compl. ¶ 52. Defendants represent that the $58.04 value was subsequently corrected by Morton "due to a mistaken past valuation of Morton stock." Def. Mem. p.15. But that correction occurred on November 21, 2018, a year and a half after the ESOP Transaction, and there has been no discovery to show this was not a *post hoc* justification of the Plan's overpayment for Morton. Perhaps most importantly, Defendants misstate Plaintiff's position to claim she actually believes or relies upon any of the valuations of Morton stock. Plaintiff's point is that they are all suspect, that there are questions of fact about the value of Morton stock. Defendants' submission of an incomplete Form 5500 further proves these issues of fact exist. Defendants' Exhibit E excludes the Supplemental Schedule, dated November 21, 2018, that Plaintiff's Complaint relies upon, which reported to the DOL and IRS a share price of $58.04 as of December 31, 2016. *See* (Complete) Amended 2016 Form 5500 Annual Return/Report of Employee Benefit Plan (filed Nov. 21, 2018) attached as Exhibit A. That the same Form 5500 at the Schedule H also inconsistently reported the same stock to be valued at over $72.56 per share as of December 31, 2016, further shows issues of fact requiring denial of Defendants' motion.[3]

Even if there were not a question of fact as to which figure Morton supplied to the DOL was "accurate" (if any) there remain questions as to why Morton amended its 2016 valuation. Defendants provide one possible explanation—a change in accounting practice. However, that has not been established for purposes of this motion because Defendants have not established that issue preclusion would apply. But on a more basic level, the alleged correction occurred

[3] While the thrust of Defendants' motion is that paragraph 52 of the Complaint contains the factual allegations upon which Plaintiff's claims hinge, that is not the reality. Paragraph 52 simply, and accurately, states reported stock valuations that raise issues of fact. Plaintiff does not assume any of the valuations were accurate or argue that they prove her claims. Ultimately, the only value that matters is the value of Morton stock on the date of the ESOP Transaction, and that will require discovery and expert opinion to determine.

after the State Court Decision, so how could that decision resolve the issue?[4] It is just as plausible that Morton made the accounting change to increase the value of the shares that the Selling Shareholders would receive. And it is just as plausible that the Company filed a "corrected" value for year end 2016 to justify the value paid by the ESOP in May 2017. As noted in the State Court Decision, the appropriate treatment of "Billings in Excess of Cost" is wrapped up in questions of whether this was a control transaction and whether a control premium should have been applied—questions that will be heavily disputed in this case. Why the Company made this change and whether it was appropriate is a factual question has not been resolved by the parties to this litigation.

Defendants oversimplify the issue of the post-Transaction drop in Morton stock valuations by saying the drop can be explained by the debt incurred to pay for the shares. Def. Mem. pp.17-18. But if Argent had not caused the ESOP to overpay for the stock, and the subsequent valuations were accurate, that drop would have been smaller. And more importantly, even if true, the loan could only conceivably explain the December 31, 2017 valuation drop. But Plaintiff alleges that the stock price was yet lower in the December 31, 2018 valuation (Compl. ¶ 52)—this cannot be explained away by the debt incurred in the ESOP Transaction. This is just another in a long list of Defendants' mistaken attempts to isolate individual allegations and argue that, *by itself*, that allegation is insufficient.

Defendants' final argument against the breach of fiduciary duty claim —"The Fact That Argent Was Paid A Fee Does Not Support Liability." Def. Mem. pp.19-20—conflates two separate paragraphs of the Complaint and mischaracterizes the allegations.

[4] The State Court Decision was issued in November 2016, the Form 5500 with a $58.04 value was filed on October 2, 2017, while the amendment to the 5500 did not take place until November 21, 2018, two years after the State Court Decision.

Plaintiff alleges that Argent "received consideration for its own personal account from Morton for its services in the ESOP Transaction in the form of fees." Compl. ¶ 57. That allegation has *nothing* to do with Plaintiff's § 404 breach of fiduciary duty claim. That paragraph relates to the § 406(b)(3) prohibited transaction claim in Count I. *See id*. ¶¶ 73, 75-76.[5]

Wholly separate from that allegation, Plaintiff alleges Argent had an incentive to act in favor of the Selling Shareholders because, if it agreed to favorable terms, Argent would be given additional business *after* the ESOP Transaction. Compl. ¶ 54. And, in fact, Argent was so rewarded. *Id.* This is but another example Defendants claiming that one individual allegation is, by itself, insufficient. Plaintiff alleges much more and her Complaint must be "read as a whole, not parsed piece by piece to determine whether each allegation, in isolation, is plausible." *Braden*, 588 F.3d at 594; *see also Allen*, 835 F.3d at 678.

Plaintiff alleges that Argent caused the Plan to overpay and provides numerous reasons why that overpayment occurred. At the pleading stage, Defendants' denials, justifications, excuses, and insufficient attempts at issue preclusion, are insufficient to dismiss the breach of fiduciary duty claim.[6]

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[5] Although unclear, to the extent Defendants are suggesting that Argent's fees were reasonable and therefore there was no prohibited transaction, a similar attempt was recently rejected at the pleading stage. *See McMaken*, 2019 WL 1468157, at *8. In that case the trustee argued that the plaintiff failed to allege sufficiently that the fees were excessive, and therefore his claim fails because there is no self-dealing if the fees charged were reasonable in light of the services provided. The court was not persuaded, noting that the trustee was arguing an affirmative defense on which the trustee bore the burden of proof and also that "a majority of courts have found that the "reasonable compensation" exemptions under ERISA §§ 408(b)(2), (c)(2) apply only to prohibited transactions under ERISA § 406(a), and not ERISA § 406(b)." *Id*. (*citing Hi-Lex Controls, Inc. v. Blue Cross Blue Shield of Mich.*, 751 F.3d 740, 750 (6th Cir. 2014) (citing cases)).

[6] Defendants again claim that the Prohibited Transaction (Counts I and IV) claims should be dismissed "[b]ecause the Complaint fails to plead any facts that would support a reasonable inference that the ESOP overpaid . . ." Def. Mem. p.19. Again, Plaintiff does not have to plead

c. Plaintiff States a Claim that the Indemnification Agreement Violates ERISA §§ 404 and 410.

Plaintiff alleges that the indemnification provisions in Argent's engagement agreement (Compl. ¶¶ 59-60) or the Trust Agreement (*Id*. ¶¶ 61-64) run afoul of ERISA because they attempt to relieve Argent from responsibility or liability for violating ERISA's prohibited transaction rules (Count I).[7] *Id*. ¶¶ 89-95. Defendants spend several pages discussing which indemnification provision applies but only one paragraph on the pivotal question at this pleading stage: whether it covers the prohibited transaction claim. If the agreements allow Argent to be indemnified for that claim—and Argent never denies that point—then it violates ERISA and Argent's use of the indemnification in defense of Count I also violates ERISA.

The law prohibits Argent's indemnification agreements because they attempt to relieve Argent from responsibility or liability under ERISA. 29 U.S.C. § 1110(a). Although indemnification agreements that function as insurance are allowed, indemnification cannot come from the plan itself. 29 C.F.R. § 2509.75–4. Under the majority view, indemnification by an ESOP sponsor, such as Morton, functionally equates to an impermissible indemnification by the

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those facts to state a claim for a Prohibited Transaction and at no point did she "set out all of the elements" of the adequate consideration defense. Further, not all the prohibited transaction claims are about overpayment for stock, and Defendants have shown no grounds for dismissal of the § 406(a)(1)(B) or 406(b) claims.

[7] Defendants criticize Plaintiff for not being able to describe the Engagement Letter (Def. Mem. p.20), but that document was not in Plaintiff's possession. While Plaintiff requested contracts under which the Plan was established in a letter to the Plan Administrator, Morton refused to produce the Engagement Letter. See ERISA § 104(b)(4) request for Plan document (attached as Exhibit B) and Morton's response (attached as Exhibit C). Also, Defendants misread the Complaint where they allege Count III asks that "the Court should declare the indemnification agreement between Argent and Morton invalid and *disgorge the fees Argent received for its work as Trustee*." Def. Mem. p.4. Count III does not seek disgorgement of Argent's fee, but repayment to Morton, which is ESOP-owned, of Argent's indemnified litigation expenses and paid damages should Argent be held liable in Count I.

plan itself. See *McMaken v. GreatBanc Tr. Co.*, No. 17-CV-04983, 2019 WL 1468157, at *4 (N.D. Ill. Apr. 3, 2019); *Pfeifer v. Wawa, Inc.*, 214 F. Supp. 3d 366, 373 (E.D. Pa. 2016); *Johnson v. Couturier*, 572 F.3d 1067, 1080 (9th Cir. 2009) ("advancement is here tantamount to asking ESOP participants to pay for Defendants' defense costs"); *Fernandez v. K–M Indus. Hldg. Co.*, 646 F. Supp. 2d 1150, 1154–55 (N.D. Cal. 2009); *Delta Star, Inc. v. Patton*, 76 F. Supp. 2d 617, 640–41 (W.D. Pa. 1999); *Hurtado v. Rainbow Disposal Co.*, No. 817CV01605JLSDFM, 2018 WL 3372752, at *15 (C.D. Cal. July 9, 2018). On that basis alone, the motion to dismiss Count III should be denied.

The only response Argent can muster is that the prohibited transaction claim "turn[s] on a supposed overpayment for Morton Stock" and therefore, somehow, implicates an exception in its indemnification agreements for breaches of fiduciary duty. Def. Mem. p.24. This is another red herring. Count III relates to indemnification for the *prohibited transaction* claim, which impose *per se* liability. Argent can be liable for the prohibited transaction without any finding of "breach of fiduciary liability, gross negligence, or willful misconduct." So the "exception" relied on by Defendants would not even apply. Under the terms of the indemnification agreement, there is no way for the Plan not to pay for Argent's costs and liability under Count I. Because the prohibited transaction count survives without Plaintiff having to establish that the Plan overpaid or that Argent breached its fiduciary duties, and Morton may make payments to Argent to defend that claim, the indemnification provision and its use by Argent violates ERISA and Count III must survive for this additional reason.[8]

[8] Defendants cite Judge Easterbrook's comment in *Packer Eng'g, Inc. v. Kratville*, 965 F.2d 174, 176 (7th Cir. 1992), concerning indemnification of ERISA fiduciaries wrongly accused of misconduct. *First*, *Packer* was not an ESOP case and is therefore distinguishable for the reasons noted above. *Second*, as other courts have noted, Judge Easterbrook seemed offended by the lawsuit brought by a vengeful CEO against a manager that dared defy him. *See State St. Bank &*

3. Conclusion

For all of the reasons stated above, Defendants' motion to dismiss should be denied.

Dated: August 11, 2020

Respectfully submitted,

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Tr. Co. v. Salovaara, 326 F.3d 130, 141 (2d Cir. 2003). Finally, Plaintiff's claim here is based on a prohibited transaction claim that Defendants concede is not carved out from the indemnification provision.

CERTIFICATE OF SERVICE

I certify that on August 11, 2020, a true and correct copy of the foregoing document was filed with the Clerk of Court using the CM/ECF system, which will send electronic notification of such filing to all counsel of record.

/s/ Patrick Muench

CERTIFICATION

Pursuant to L.R. 7.1(B)(4), the undersigned attorney certifies that the foregoing memorandum does not contain more than 7,000 words or 45,000 characters, inclusive of all headings, footnotes, and quotations.

/s/ Patrick O. Muench