SCOTUS v. the Ninth Circuit on Failure to Enforce ERISA Stock-Drop Pleading Standard

February 29, 2016

In a terse per curiam opinion, the U.S. Supreme Court in *Amgen Inc. v. Harris*, No. 15-278 (U.S. Jan. 25, 2016), made clear that it expects lower courts to faithfully apply the pleading requirements for "stock-drop" cases under the Employee Retirement Income Security Act (ERISA) outlined in the Court's earlier opinion in *Fifth Third Bancorp v. Dudenhoeffer*, 134 S. Ct. 2459 (2014). In *Amgen*, the Supreme Court simultaneously granted the Amgen stock plan fiduciaries' petition for a writ of certiorari and reversed the U.S. Court of Appeals for the Ninth Circuit for its failure to adhere to the Court's *Fifth Third* pleading guidance. Only time will tell how rigorously the lower courts will apply the *Fifth Third* pleading strictures following the Supreme Court's admonition to the Ninth Circuit in *Amgen*. Nevertheless, the *Amgen*opinion is encouraging news for stock-drop defendants, who should continue to have a meaningful opportunity to defeat specious cases at the motion-to-dismiss stage. ***Amgen* Background**

The underlying case has a lengthy history, which can be summarized thusly: The *Amgen* plaintiffs are former employees who participated in two Amgen-sponsored defined contribution retirement programs that qualified as "eligible individual account plans" (EIAPs) under ERISA. Like traditional employee stock ownership plans (ESOPs), the Amgen plans offered an Amgen common stock fund as an investment option to participating employees. Each *Amgen* plaintiff had holdings in the Amgen stock fund. In 2007, after Amgen's stock price suffered an appreciable decline, the *Amgen* plaintiffs filed a putative class action against Amgen and other alleged fiduciaries of the plans. Among other things, the plaintiffs claimed that the fiduciary defendants breached their duties by allowing the stock fund to remain available as a plan investment option while knowing through their "insider" status that the stock price was artificially inflated due to the pharmaceutical company's improper "off-label" marketing of one of its most popular drugs in the face of undisclosed, adverse clinical trial results. The plaintiffs asserted that Amgen's stock price declined when certain health risks associated with the drug were ultimately revealed to the public through the media and other sources. The U.S. District Court for the Central District of California dismissed the original complaint on standing and other grounds relating to the identification of the appropriate parties to the suit. The

Ninth Circuit reversed and remanded, allowing the plaintiffs to amend the complaint. *Harris v. Amgen, Inc.*, 573 F.3d 728, 731 (9th Cir. 2009). The district court dismissed the amended complaint against Amgen on the ground that it was not a fiduciary and against the other defendants for failure to state a claim. The district court's Rule 12(b)(6) dismissal was based in part on the then-accepted "presumption of prudence" (or "*Moench* presumption") in favor of stock plan fiduciaries. As followers of this realm of ERISA jurisprudence are aware, in specified circumstances, the*Moench* presumption (coined from the Third Circuit's seminal opinion in *Moench v. Robertson*, 62 F.3d 553 (3d Cir. 1995)) had effectively protected ESOP and similar stock plan fiduciaries from ERISA liability in price decline cases for nearly two decades before the Supreme Court's *Fifth Third* decision. In the years between *Moench* and before *Fifth Third*, every other court of appeals to confront the issue likewise adopted some strain of the fiduciary-friendly presumption—either at the pleading stage or as an "evidentiary presumption" applicable later in the proceedings. *See, e.g.*, *White v. Marshall & Ilsley Corp.*, 714 F.3d 980, 989 (7th Cir. 2013); *In re Citigroup ERISA Litig.*, 662 F.3d 128, 139–40 (2d Cir. 2011); *Quan v. Comput. Scis. Corp.*, 623 F.3d 870, 882 (9th Cir. 2010); *Kirschbaum v. Reliant Energy, Inc.*, 526 F.3d 243, 256 (5th Cir. 2008); *Edgar v. Avaya, Inc.*, 503 F.3d 340 (3d Cir. 2007); *Kuper v. Iovenko*, 66 F.3d 1447, 1459 (6th Cir. 1995). The Ninth Circuit again reversed, holding that the fiduciary defendants were not entitled to rely on the presumption of prudence under the facts alleged in the case. *Harris v. Amgen, Inc.*, 738 F.3d 1026 (9th Cir. 2013). At this point, the plan fiduciaries sought certiorari for the first time, setting the stage for the Supreme Court's intervention in the case. **A Look Back at *Fifth Third***

Appreciating the significance of the Supreme Court's *Amgen* rulings requires stepping back briefly to the Court's opinion in *Fifth Third*. As a threshold matter, the *Fifth Third* Court ruled that the long-followed presumption of prudence in favor of ESOP fiduciaries' stock purchase and hold activities has no support under ERISA. According to the Court, no such presumption should be applied at the pleading stage or otherwise in ERISA stock-drop cases. *Fifth Third*, 134 S. Ct. at 2467 ("In our view, the law does not create a special presumption favoring ESOP fiduciaries."). "Instead, ESOP fiduciaries are subject to the same duty of prudence that applies to ERISA fiduciaries in general, except that they need not diversify the fund's assets." *Id.* at 2463 (citing 29 U.S.C. § 1104(a)(2)). Moreover, the Court stated, ERISA "makes clear that the duty of prudence trumps the instructions of a plan document, such as an instruction to invest exclusively in employer stock even if financial goals demand the contrary." *Id.* at 2468 (citing 29 U.S.C. §§ 1104(a)(1)(D), 1110(a)). With the presumption jettisoned, the *Fifth Third* Court turned to a discussion of the stock-drop plaintiff's affirmative pleading obligations. The Court's pivot to this topic was based on an apparent concern that it shared with petitioner Fifth Third. That concern involved the potential for conflict between ERISA's duty of prudence and the federal securities law's prohibition of insider trading. *See id.* at 2469 ("This [petitioner] concern is a legitimate one."). As the Court observed:

> The potential for conflict arises because ESOP fiduciaries often are company insiders and because suits against insider fiduciaries frequently allege, as the complaint in this case alleges, that the fiduciaries were imprudent in failing to act on inside information they had about the value of the employer's stock.

Id. Although the Court concluded that this legitimate concern did not warrant preserving the presumption of prudence, the Court did find that there were "alternative means of dealing with the potential for conflict," while also paying heed to ERISA's "'careful balancing' between ensuring fair and prompt enforcement of rights under a plan and the encouragement of the creation of such plans" *and* addressing the petitioner's plea for an effective mechanism "to weed out meritless lawsuits." *Id.* at 2470. As the Court observed, "one important mechanism for weeding out meritless claims [is] the motion to dismiss for failure to state a claim." *Id.* at 2471. Citing *Ashcroft v. Iqbal*, 556 U.S. 662, 677–80 (2009), and *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 554–63 (2007), the Court emphasized that the pleading-stage motion to dismiss "requires careful judicial consideration of whether the complaint states a claim that the defendant has acted imprudently" and that, in light of the nature of the ERISA duty of prudence under 29 U.S.C. § 1104(a)(1)(B), "the appropriate inquiry will necessarily be context specific." *Fifth Third*, 134 S. Ct. at 2471. The Court then laid out several important "considerations" for the lower courts to take into account when applying the *Twombly*/*Iqbal* "plausibility" standard to a duty-of-prudence claim in a stock-drop case. The guidance that would prove most important to the recent outcome in *Amgen* related to the plaintiffs' claim that Fifth Third's ESOP fiduciaries failed to act prudently based on nonpublic information that was allegedly available to them because they were Fifth Third insiders. The Court observed:

> To state a claim for breach of the duty of prudence on the basis of inside information, a plaintiff must plausibly allege *an alternative action that the defendant could have taken* that would have been consistent with the securities laws and *that a prudent fiduciary in the same circumstances would not have viewed as more likely to harm the fund than to help it*.

Fifth Third, 134 S. Ct. at 2472 (emphasis added). With respect to claims (like those asserted by the *Amgen* plaintiffs) that the ESOP fiduciary should have refrained from additional stock purchases or disclosed inside information to the public so that the stock would no longer be overvalued, the Supreme Court instructed the lower courts to "consider the extent to which an ERISA-based obligation either to refrain on the basis of inside information from making a planned trade or to disclose inside information to the public could conflict with the complex insider trading and corporate disclosure requirements imposed by the federal securities laws or with the objectives of those laws." *Id.* at 2473. In this regard, the Court notably observed that "[t]he U.S. Securities and Exchange Commission has not advised us of its views on these matters, and we believe those views may well be relevant." *Id.* The Court further advised that lower courts should evaluate whether the complaint has plausibly alleged that a prudent fiduciary could *not* have concluded that

> stopping purchases—which the market might take as a sign that insider fiduciaries viewed the employer's stock as a bad investment—or publicly disclosing negative information *would do more harm than good* to the fund by causing a drop in the stock price and a concomitant drop in the value of the stock already held by the fund.

Id. (emphasis added). Thus, in *Fifth Third*, the Supreme Court both giveth to and taketh away from

the class action plaintiffs' bar. In sum and substance, the Court held that ESOP fiduciaries *are not entitled* to a defense-friendly presumption at any stage in the litigation but *are entitled* to require stock-drop plaintiffs, at the pleading stage, to satisfy the *Twombly*/*Iqbal* plausibility standard in very specific ways—unique to the nature of ERISA stock-drop claims—as a means "to weed out meritless lawsuits." *See generally Fifth Third*, 134 S. Ct. at 2467–73. With that, we return to the Supreme Court's skirmish with the Ninth Circuit in *Amgen*.

Supreme Court to Ninth Circuit Post-*Fifth Third*: Two Strikes and You're Out

The Supreme Court deferred ruling on the *Amgen* defendants' initial petition for certiorari while *Fifth Third* was under consideration. However, in June 2014, after the Supreme Court issued its opinion in *Fifth Third*, the Court granted the *Amgen* defendants' petition and in turn vacated the Ninth Circuit's reversal of the district court's dismissal order. *Amgen Inc. v. Harris*, 134 S. Ct. 2870 (2014). In light of the Supreme Court's elimination of the *Moench*presumption, the Court remanded the case to the Ninth Circuit with instructions to revisit the plaintiffs' complaint allegations under the fresh pleading guidance set out in *Fifth Third*. On remand, the Ninth Circuit again upheld the viability of the plaintiffs' amended complaint and—over a vigorous four-judge dissent—denied the defendants' petition for rehearing en banc. *Harris v. Amgen, Inc.*, 788 F.3d 916 (9th Cir. 2015), *amending and superseding* 770 F.3d 865 (9th Cir. 2014). In reviving the complaint once again, the Ninth Circuit panel somewhat cavalierly explained that its pre-*Fifth Third* opinion "had already assumed" the standards for pleading ERISA fiduciary liability that the Supreme Court subsequently introduced in *Fifth Third*. *Harris*, 788 F.3d at 940. Notwithstanding the Supreme Court's pleading requirements specific to ERISA fiduciaries as announced in *Fifth Third*,the panel found that the district court's pre-*Fifth Third* decision in a separate federal securities class action against Amgen "based on the same alleged sequence of events" should be determinative in the ERISA case against the plan fiduciaries. The Ninth Circuit stated:

> If the alleged misrepresentations and omissions, scienter, and resulting decline in share price in *Connecticut Retirement Plans* were sufficient to state a claim that defendants violated their duties under Section 10(b), the alleged misrepresentations and omissions, scienter, and resulting decline in share price in this case are sufficient to state a claim that defendants violated their duty of care under ERISA.

Id. at 936. *See also Conn. Ret. Plans & Tr. Funds v. Amgen, Inc.*, 660 F.3d 1170 (9th Cir. 2011), *aff'd*, *Amgen Inc. v. Conn. Ret. Plans & Tr. Funds*, 133 S. Ct. 1184 (2013). Judge Kozinski, on behalf of the en banc dissenters, expressed concern for his colleagues' actions: "The panel's decision creates almost unbounded liability for ERISA fiduciaries, plainly at odds with what the Court instructed. . . . I sincerely regret that a majority of our court did not see fit to take this case en banc. I expect the Supreme Court will promptly correct our error." *Harris*, 788 F.3d at 923. The *Amgen* defendants again sought certiorari. Judge Kozinski was right. Without a doubt, the Supreme Court was not pleased with the Ninth Circuit's approach when it took up *Amgen* the second time. In its latest *Amgen* ruling, the Supreme Court was unambiguous in expressing its view that the Ninth Circuit did not diligently follow the Court's June 2014 remand instructions. As the Ninth Circuit dissenters predicted, the

Court first held that "the Ninth Circuit failed to properly evaluate the complaint," which the Court independently found *not* to contain "sufficient facts and allegations" to state a claim against the plan fiduciaries. *Amgen Inc. v. Harris*, No. 15-0278, slip op. at 3–4 (Jan. 25, 2016). In particular, the Court concluded that the Ninth Circuit "failed to assess whether the complaint in its current form 'has plausibly alleged' that a prudent fiduciary in the same position 'could not have concluded' that the alternative action [of removing the Amgen stock fund as a plan investment option] 'would do more harm than good.'" *Id.* at 3. While noting that "[t]he Ninth Circuit's proposition that removing the Amgen Common Stock Fund from the list of investment options was an alternative action that could plausibly have satisfied *Fifth Third*'s standards," the Court held that, "[i]f so, the facts and allegations supporting that proposition should appear in the stockholders' complaint." *Id.* at 4. Observing that "the stockholders are the masters of their complaint," the Court ultimately determined that it would "leave[] to the District Court in the first instance whether the stockholders may amend [the complaint] in order to adequately plead a claim for breach of the duty of prudence guided by the standards provided in *Fifth Third*." *Id.* **Moving Forward in *Amgen* and Beyond**

The Supreme Court's *Amgen* message is clear: The lower courts must conscientiously apply the *Fifth Third* pleading standards when evaluating a fiduciary defendant's motion to dismiss in an ERISA stock-drop case. Like the plaintiffs in *Fifth Third*, the *Amgen* plaintiffs alleged a "nonpublic information" or "insider" fiduciary claim. As a result, the *Amgen* plaintiffs must overcome the "[no] more harm than good" pleading hurdle to sustain their complaint. The Supreme Court has already ruled that the plaintiffs failed to satisfy this hurdle in their current complaint. Under the Supreme Court's latest directive, it will be up to the district court to decide whether the *Amgen* plaintiffs will get another opportunity to do so through an amended complaint. With signs of a bear market emerging and corporate scandals always in play, more ERISA stock-drop cases are sure to come. The degree to which the lower federal courts, as the primary gatekeepers in such cases, permit plaintiffs to take a formulaic approach to satisfy their *Fifth Third*/*Amgen* pleading burden—or instead require more substantive, detailed factual allegations to overcome the hurdle—remains to be seen. Ultimately, the Supreme Court may be called upon once again in *Amgen* or elsewhere to correct the line that is drawn. **Republished with permission by the American Bar Association**

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