



ESOP Fiduciaries Lose "Presumption of Prudence"

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A unanimous U.S. Supreme Court held last week that employee stock ownership plan (ESOP) investment in employer stock is not entitled to a special ERISA "presumption of prudence". The decision provides important guidance for ERISA plan fiduciaries.

In *Fifth Third Bancorp v. Dudenhoeffer*, ESOP participants claimed that Fifth Third breached its ERISA fiduciary duty by failing to shield plan participants from a 74 percent drop in the price of Fifth Third stock from July, 2007 to September, 2009. Plan participants asserted that despite public and nonpublic information available to plan fiduciaries demonstrating that Fifth Third stock was a risky investment, the fiduciaries imprudently continued to hold and buy employer securities.

Fifth Third argued that a "presumption of prudence" should apply to an ESOP fiduciary's decision to follow plan terms and invest in employer stock. Such a presumption, commonly known as the "*Moench* presumption", had been adopted by several lower courts. Under the *Moench* presumption, an ESOP fiduciary's investment of plan assets in employer stock satisfies ERISA's fiduciary duty requirements unless there are dire circumstances threatening the employer's viability.

Rejecting the *Moench* presumption, the Supreme Court held that ERISA does not alter the playing field in favor of ESOP fiduciaries. Instead, an ESOP fiduciary's decision to invest in employer stock is subject to the same ERISA scrutiny that applies to all other investments of plan assets. An imprudent investment of ESOP assets in employer stock violates ERISA's fiduciary duty requirements. In arriving at this conclusion, the Court's opinion provides the following guidance for plan fiduciaries.

- ***The plan document does not always control.*** The fact that an ESOP plan document requires plan assets to be invested in employer stock does not shield a fiduciary from scrutiny. According to the Court, "the duty of prudence trumps the instructions of a plan document."
- ***Fiduciaries are not required to "outsmart the market."*** When investing plan assets in publicly

traded stock, fiduciaries may assume that the market price is an accurate estimate of the value of the stock.

- ***ERISA does not compel fiduciaries to break the law.*** ERISA's fiduciary duty does not compel plan fiduciaries to engage in insider trading in violation of securities laws. Fiduciaries are not required to make plan investment decisions based on nonpublic information.
- ***Fiduciaries may consider the unintended consequences.*** A fiduciary may consider how stopping purchases of employer stock may impact the market. Such action could harm participants by causing a drop in the price of employer stock already held by the ESOP.

After *Dudenhoeffer*, ESOP plan fiduciaries need to apply the scrutiny and analysis of investments in employer stock that apply to all other plan investments. Plan investment committees should regularly review the performance of employer stock. The analysis and reasoning supporting employer stock investment decisions should be well-documented.

The Williams Mullen Employee Benefits Group will continue to monitor the impact of this important case. Please contact any member of the practice group if you have questions regarding this article.

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