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UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF OHIO
EASTERN DIVISION

IN RE CARDINAL HEALTH, INC. ERISA LITIGATION	))))))	NO. C2-04-643 Judge Marbley Magistrate Judge King **ORAL ARGUMENT REQUESTED**

DEFENDANT PUTNAM FIDUCIARY TRUST COMPANY'S MOTION TO DISMISS THE CONSOLIDATED AMENDED ERISA COMPLAINT AND JURY DEMAND

Pursuant to Federal Rule of Civil Procedure 12(b)(6), defendant Putnam Fiduciary Trust Company ("Putnam") hereby moves to dismiss the Consolidated Amended ERISA Complaint and Jury Demand dated April 29, 2005 ("Complaint"). Among the reasons requiring dismissal: (i) the Complaint does not adequately allege that Putnam had fiduciary status with respect to investment of assets of the Cardinal Health 401(k) Savings Plan and its predecessor plans (collectively, the "Plan") in the Employer Common Stock Fund (the "Stock Fund"), and thus Putnam cannot be liable for breach of fiduciary duty for such investments; (ii) as a directed trustee, Putnam was not subject to ERISA's prudence requirement; (iii) Putnam cannot be liable for following directions to invest Plan assets in the Stock Fund because, as alleged, such directions were not contrary to ERISA or the terms of the Plan; (iv) Putnam had no duty to question directions to invest in Cardinal Health, Inc. ("Cardinal") stock because there are no allegations in the Complaint of any clear and compelling public indicators that called into serious question Cardinal's viability as a going concern; and, (v) in any event, plaintiffs do not allege,

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nor could they, that Putnam had any knowledge of the purported accounting improprieties that allegedly made Cardinal stock an imprudent investment.

Points and authorities in support of this motion are set forth in the accompanying Memorandum of Law. Given the complexity of the legal issues, defendants respectfully request oral argument on the issues raised in this motion pursuant to Local Rule 7.1(b)(2).

Respectfully submitted,

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I. PRELIMINARY STATEMENT

Plaintiffs claim that defendant Putnam Fiduciary Trust Company ("Putnam") breached fiduciary duties under ERISA[1] by investing their retirement plan assets in the common stock of their employer, Cardinal Health, Inc. ("Cardinal" or the "Company"). Plaintiffs' claim is without merit. Under the facts pleaded in the Consolidated Amended ERISA Complaint and Jury Demand dated April 29, 2005 ("Complaint"), the claim is contrary to the governing plan documents, established caselaw and Department of Labor guidance. Accordingly, the Complaint should be dismissed as to Putnam.

II. SUMMARY OF ARGUMENT

- Putnam cannot be liable for breach of ERISA §404(a)(1), which imposes duties on "fiduciaries," because, upon the allegations in the Complaint and the documents on which plaintiffs' claims are based, Putnam was not a fiduciary with respect to purchasing and holding Cardinal stock by Cardinal's 401(k) plan.[2] Putnam had no discretion in the selection of the Plan's investment options and had no discretion in deciding how Plan assets would be invested. The governing Plan documents state, among other things: "The Trustee shall not be responsible for the investment or reinvestment of the assets of the Master Trust" and "*Putnam has no obligation to monitor, control or in any way exercise any powers or discretion* in the handling or disposition of any Plan assets, including the disposition of any funds, securities or other assets under the Plan. . . . Cardinal specifically intends that Putnam have *no discretionary authority to determine the investment of the Trust assets*." (Emphasis added.) Because discretion is a prerequisite to fiduciary status, Putnam was not a fiduciary with respect to the Plan's investment in Cardinal stock. In the absence of relevant fiduciary status, Putnam cannot be liable for breach of fiduciary duty. Grindstaff v. Green, 133 F.3d 416, 426 (6th Cir. 1998).

- Putnam also cannot be liable for violation of §404(a)(1) because, under the allegations of the Complaint and the plan documents on which plaintiffs' claims are based, Putnam was a directed trustee and the Complaint alleges no facts that would give rise to a duty on Putnam's part to question directions it received to invest in Cardinal stock. First, ERISA §403(a)(1) provides that directed trustees may follow "proper directions . . . which are made in accordance with the terms of

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[1] Employee Retirement Income Security Act of 1974, as amended, 29 U.S.C. §1001, et. seq.

[2] The Cardinal Health 401(k) Savings Plan and its predecessor plans are collectively referred to herein as the "Plan."

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the plan and which are not contrary to [ERISA]." ERISA's legislative history explains that §403(a)(1) requires a trustee to follow directions unless it is "clear on their face" that the directed actions are not in accordance with the plan or would be "prohibited" by ERISA. Directions to invest in Cardinal stock do not run afoul of this test. On the one hand, the directions were in accordance with the Plan because the Plan documents expressly provided for the investment. On the other, those directions were not facially contrary to ERISA because ERISA expressly contemplates the investment of plan assets in employer stock. LaLonde v. Textron, Inc., 270 F. Supp. 2d 272, 278, 281-82 (D.R.I. 2003), aff'd on other grounds, 369 F.3d 1 (1st Cir. 2004). Second, even under more stringent standards articulated by recent Department of Labor guidance, a directed trustee's duty to act arises only where the trustee knows material adverse non-public information about the plan sponsor or "[i]n limited, extraordinary circumstances, where there are clear and compelling public indicators, as evidenced by an 8-K filing with the Securities and Exchange Commission (SEC), a bankruptcy filing or similar public indicator, that call into serious question a company's viability as a going concern." However, the Complaint does not allege, nor could it, that Putnam had any knowledge of material adverse non-public information about Cardinal or of any clear and compelling public indicators that called into serious question Cardinal's viability as a going concern. In re WorldCom, Inc. ERISA Litigation, 354 F. Supp. 2d 423, 450 (S.D.N.Y. 2005).

- Regardless of the standard of duty applicable to its actions, Putnam cannot be liable for breach of ERISA fiduciary duties because the Complaint alleges no facts supporting a theory that Putnam knew or should have known that Cardinal stock was an imprudent investment. Putnam is not alleged to have had any knowledge of the accounting improprieties that form the basis of plaintiffs' allegation of imprudence; indeed, the Complaint itself alleges that these facts were hidden from the public. The only pleaded facts knowable to Putnam show nothing more than normal corporate fortunes. LaLonde v. Textron, Inc., 369 F.3d 1, 7 (1st Cir. 2004).

- Putnam cannot be liable under ERISA §405(a) co-fiduciary provisions because the Complaint contains no facts in support of its conclusory allegation as to co-fidcuiary liability. Crowley v. Corning, Inc., 234 F. Supp. 2d 222, 230 (W.D.N.Y. 2002).

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III. FACTS[3]

A. Parties

Plaintiffs participated in the Plan during the purported class period, October 24, 2000 to the present. (Compl. ¶¶1, 7-9.) Defendant Cardinal was the sponsor and administrator of the Plan. (Compl. ¶54.) Other defendants include: Cardinal's Employee Benefits Policy Committee (the "Plan Committee"), eight individual members of the Plan Committee, and fourteen individual Cardinal directors. (Compl. ¶¶12-37.) The final defendant is Putnam, which was the Plan's former trustee (the "Trustee") from the beginning of the purported class period until December 2004. (Compl. ¶39.)

B. The Plan

The Plan is an ERISA-regulated "employee benefit plan." (Compl. ¶47.) The Plan is also an "individual account plan" within the meaning of ERISA §3(34), 29 U.S.C. §1002(34), in that the Plan provides for each participant to have an individual account. (Compl. ¶48.) During the period that Putnam served as Trustee the Plan was governed by Plan documents amended and restated as of July 1, 1998 ("1998 Plan") and July 1, 2002 ("2002 Plan," collectively the "Plan documents".) (App. Ex. Tabs 1 and 2.)[5] Participant accounts were funded through participant elective contributions and matching employer contributions. (1998 and 2002 Plan §§3.01, 3.02, 3.06, 9.05, App. Ex. Tabs 1 and 2.)

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[3] The facts are taken from the Complaint (cited as "Compl. ¶____") and from the operative Plan documents, Trust Agreements and Service Agreements (collectively, the "Plan Documents") (the Plan Documents are cited as "App. Ex ____", indicating reference to Putnam's Appendix of Plan Documents filed with its motion to dismiss.) The Court may consider the Plan Documents on a motion to dismiss. See infra, pp. 7-8.

[5] The 1998 Plan was revised as of 2001 and 2002. The 1998 Plan did not change in any respects material to this motion in those iterations. Putnam understands that plaintiffs' counsel have been provided with all three versions of the 1998 Plan but it will provide additional copies to plaintiffs' counsel or the Court upon request.

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The Plan specified that Cardinal was the named administrator. (Compl. ¶54, quoting Plan documents.) As Plan sponsor, Cardinal appointed and later removed Putnam as Trustee. Cardinal had the authority to appoint and remove Putnam as Trustee at any time. (Id.) The Plan additionally reserved for Cardinal and its designated committee the right "to change the investment options available under the Plan and the rules governing investment designations at any time and from time to time." (1998 and 2002 Plans §8.05, App. Ex. Tabs 1 and 2.)

The Plan also specified that the Trustee was "authorized to maintain the 'Employer Common Stock Fund' as one of the Investment Funds." (1998 and 2002 Plans §8.05, App. Ex. Tabs 1 and 2.) The Plan expressly directed that:

> The Employer Common Stock Fund shall consist of stock of the Company and cash or cash equivalents needed to meet obligations of such fund or for the purchase of stock of the Company. One of the purposes of the Plan is to provide Participants with ownership interests in the Company. To the extent practicable, all available assets of the Employer Common Stock Fund shall be used to purchase Shares,[7] which shall be held by the Trustee . . . (Id.)

Plaintiffs allege that their damage was caused by the Plan's investment in the Employer Common Stock Fund (the "Stock Fund"). (See Compl. ¶¶1, 3.)

C. The Trust Agreements and Service Agreements

Putnam served as the Plan's Trustee pursuant to trust agreements between it and Cardinal dated July 1, 1998 ("1998 TA") and January 2, 2001 ("2001 TA," collectively, the "Trust Agreements"). (App. Ex. Tabs 3 and 4.) In all respects relevant to this action, Putnam served as Trustee in an exclusively "directed" capacity. Consistent with the Plan, the Trust Agreements

7 "Shares" are defined in Plan §1.40 as "[t]he no par value common shares of [Cardinal]." (App. Ex. Tabs 1 and 2.)

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provided that Putnam was to be directed by the Administrator in the selection of investment funds made available to participants. The 1998 Trust Agreement stated that:

- "The Trustee shall transfer to each such Investment Fund such portion of the assets of the Trust as the Administrator or Plan members *direct* in accordance with the specific provisions of the Plan and in the manner provided in the Service Agreement." (1998 TA §8(a), App. Ex. Tab 3.) (Emphasis added.)

- "If, and to the extent, specifically authorized by the Plan and provided in the Service Agreement, the Administrator may *direct* the Trustee to establish an Investment Fund all, or substantially all, of the assets of which shall be invested in shares of the stock of the Company . . ." (Id.) (Emphasis added.)

- "*The Administrator as named fiduciary shall continually monitor the suitability of acquiring and holding* Company Stock under the fiduciary duty rules of Section 404(a)(1) of ERISA (as modified by Section 404(a)(2) of ERISA) and the requirements of Section 404(c) of ERISA. The Trustee *shall not be liable for any loss, or by reason of any breach, which arises from a direction* of the Administrator with respect to the acquisition and holding of Company Stock." (1998 TA §9(b), App. Ex. Tab 3.) (Emphasis added.)[8]

Similarly, the 2001 Trust Agreement expressly placed responsibility for the investment of Plan assets with designated Cardinal officials:

> The Trustee shall not be responsible for the investment or reinvestment of the assets of the Master Trust, which investment and reinvestment shall be the responsibility of the investment manager as delegated by the Administrator as provided in Section 4 hereof, and if not so delegated, of the Administrator. (2001 TA §1, App. Ex. Tab 4.)[9]

As contemplated by the Trust Agreements, Putnam's obligations to the Plan were further spelled out in service agreements effective as of July 1, 1998 ("1998 SA") and July 1, 2002 ("2002 SA," collectively, the "Service Agreements"). (App. Ex. Tabs 5 and 6.) (See, e.g., 1998 TA §§2, 5, 6, 8, 10, 17, 18, App. Ex. Tab 3; 2002 TA §3, App. Ex. Tab 4.) Like the Trust

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[8] In the 1998 Trust Agreement, "Administrator" is defined as the "Plan Administrator" (1998 TA §4(b), App. Ex. Tab 3), which, in turn, was defined in the 1998 Plan as Cardinal or its designee. (1998 Plan §1.29, App. Ex. Tab 3.)

[9] The 2001 Trust Agreement defines "Administrator" in the 8th Whereas Clause as being the group of individuals forming the committee appointed by the Cardinal Board of Directors to assist Cardinal in performing its duties. (App. Ex. Tab 4.)

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Agreements, the Service Agreements expressly established that Putnam had no discretion with respect to the investment of Plan assets:

> *Putnam has no obligation to monitor, control or in any way exercise any powers or discretion* in the handling or disposition of any Plan assets, including the disposition of any funds, securities or other assets under the Plan. . . . The Employer/Cardinal specifically intends that Putnam have *no discretionary authority to determine the investment of the Trust assets.* (1998 and 2002 SA §IV.E, App. Ex. Tabs 5 and 6.) (Emphasis added.)

The Service Agreements also contained the "initial available investment options" selected by Cardinal to be available to Plan participants. (1998 and 2002 SA §IV.M, App. Ex. Tabs 5 and 6.) Consistent with the Plan provisions, the first investment option listed in each relevant Service Agreement was the Stock Fund. (See id.)

D. Claims Asserted Against Putnam

Only one of the three counts asserted in the Complaint names Putnam as a defendant. Plaintiffs claim in Count I that all defendants, including Putnam, breached their ERISA fiduciary and co-fiduciary duties under ERISA §§404(a)(1) and 405(a), 29 U.S.C. §§1104(a)(1) and 1105(a), by allowing the Plan to purchase Cardinal common stock when it was allegedly imprudent to do so.[10] The Complaint bases its claim on alleged artificial inflation of the stock price caused by "undisclosed materially adverse information," (Compl. ¶78), such as the improper recognition and allocation of revenue and income, improper reporting of reserves and failure to comply with generally accepted accounting principles. (See Compl. ¶¶79-83.) The Complaint contains no fact allegation that Putnam knew of this alleged undisclosed, material information. Only one paragraph of the Complaint identifies public information about Cardinal;

[10] Count II alleges that all defendants except Putnam failed to disclose material information and Count III alleges that Cardinal and the director defendants failed to monitor the appointed members of the Plan Committee.

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namely, a rating of Cardinal debt by the Fitch, Inc. ratings service ("Fitch"), which stated that "Cardinal remains on Rating Watch Negative." (Compl. ¶85.)[11]

IV. ARGUMENT

A. Motion To Dismiss Legal Standard

Under Fed. R. Civ. P. 12(b)(6), dismissal is warranted where a plaintiff fails to allege facts sufficient to establish any essential element of his claim. To survive a motion to dismiss in this circuit "[a] complaint must contain either direct or inferential allegations with respect to *all* material elements necessary to sustain a recovery under some viable legal theory." Weiner v. Klais & Co., 108 F.3d 86, 88 (6th Cir. 1997) (citing Allard v. Weitzman (In re DeLorean Motor Co.), 991 F.2d 1236, 1240 (6th Cir. 1993)) (emphasis added). Conclusory allegations, moreover, must be supported by facts; a court "need not accept as true legal conclusions or unwarranted factual inferences." BP Care, Inc. v. Thompson, 337 F. Supp. 2d 1021, 1025 (S.D. Ohio 2003) (quoting Gregory v. Shelby County, 220 F.3d 433, 446 (6th Cir. 2000)). Stated differently, "more than bare assertions of legal conclusions is ordinarily required to satisfy federal notice pleading requirements." Begala v. PNC Bank, Ohio, Nat. Ass'n, 214 F.3d 776, 779 (6th Cir. 2000) (quoting Scheid v. Fanny Farmer Candy Shops, Inc., 859 F.2d 434, 436 (6th Cir. 1988)).

In considering Putnam's motion to dismiss, it is proper for the Court to take the Plan Documents into account. Courts may consider ERISA plan documents not attached to a complaint where claims are "based on rights under the plans which are controlled by the plans' provisions as described in the plan documents" and where the documents are "incorporated through reference to the plaintiff's rights under the plans, and they are central to plaintiff's

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[11] As discussed in greater detail below, in this report, Fitch rated Cardinal as BBB+/F2, indicating that Cardinal's debt was believed to be investment grade; it also opined that Cardinal's "2005 cash flow should be strong" and that an upcoming scheduled earnings call to discuss first-quarter 2005 results "preclude[ed] any need for bank extensions, thus alleviating short-term liquidity concerns." (App. Ex. Tab 7.)

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claims." Weiner, 108 F.3d at 89. See also City of Monroe Employees Retirement System v. Bridgestone Corp., 399 F.3d 651, 659 n.6 (6th Cir. 2005) (considering annual reports referenced in the complaint).[12] Courts routinely grant motions by directed trustees to dismiss ERISA cases where the complaint does not allege facts or provisions of the governing plan documents establishing a duty to act. See Grindstaff v. Green, 946 F. Supp. 540 (E.D. Tenn. 1996), aff'd, 133 F.3d 416 (6th Cir. 1998)); Beddall v. State Street Bank and Trust Co., 137 F.3d 12, 21 (1st Cir. 1998); LaLonde v. Textron, Inc., 270 F. Supp. 2d 272 (D.R.I. 2003), aff'd on other grounds, 369 F.3d 1 (1st Cir. 2004).

B. Putnam Cannot Be Liable For Breach Of ERISA Fiduciary Duty Because, Under the Complaint's Allegations And The Terms Of The Plan Documents On Which Plaintiffs' Claims Rest, Putnam Was A Directed Trustee And Not A Fiduciary As To Investments In Cardinal Common Stock

Putnam cannot be held liable under ERISA §404(a)(1), which imposes duties on "fiduciaries," because it had no fiduciary duty related to purchasing and holding Cardinal stock and allowing Plan participants to buy or hold interests in the Stock Fund through their Plan accounts.

It is well settled that "[i]n every case charging breach of ERISA fiduciary duty . . . the threshold question is not whether the actions of some person employed to provide services under

[12] Here, the Plan documents are cited as a source of alleged fiduciary responsibility and cited repeatedly. (Compl. ¶¶12, 14-19, 52, 54, 55, 57, 58, 60, 62, 63, 71-73, 103.) Similarly, the Complaint explicitly references the Trust Agreements as establishing Putnam's role as Trustee. (Compl. ¶¶59, 61.) In turn, the Trust Agreements contemplate that Putnam's obligations with respect to the Plan will be further set forth in the Service Agreements. (1998 TA §§2, 5, 6, 8, 10, 17, 18, App. Ex. Tab 5; 2002 TA §3, App. Ex. Tab 6.) Most importantly, the breach of ERISA fiduciary duty claims asserted in the Complaint depend on the scope and allocation of fiduciary duties that are necessarily provided for in the Plan Documents. Accordingly, these documents may properly be considered in connection with Putnam's motion to dismiss.

In addition, it is proper for the Court to take into account (i) the October 27, 2004 Fitch report ("Fitch Report") as it is quoted at length in paragraph 85 of the Complaint, see BP Care, 337 F. Supp. 2d at 1025, and (ii) the filings with the United Stated Securities and Exchange Commission ("SEC") submitted along with Cardinal's motion to dismiss. See New England Health Care Employees Pension Fund v. Ernst & Young, LLP, 336 F.3d 495, 501 (6th Cir. 2003) (appropriate to take judicial notice of publicly filed court document); Kramer v. Time Warner, Inc., 937 F.2d 767, 774 (2d Cir. 1991) (taking into account SEC filings).

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a plan adversely affected a plan beneficiary's interest, but whether that person was acting as a fiduciary (that is, was performing a fiduciary function) when taking the action subject to complaint." Seaway Food Town, Inc. v. Medical Mut. of Ohio, 347 F.3d 610, 617 (6th Cir. 2003) (quoting Pegram v. Herdrich, 530 U.S. 211, 226 (2000)).

The law in the Sixth Circuit is clear. If there is no discretion, then there is no fiduciary duty. See, e.g., Hamilton v. Carell, 243 F.3d 992, 998 (6th Cir. 2001) (discretion is the "*sine qua non* of fiduciary status") (citing approvingly Pohl v. Nat'l Benefits Consultants, 956 F.2d 126, 129 (7th Cir. 1992)); Baxter v. C.A. Muer Corp., 941 F.2d 451, 456 (6th Cir. 1991) (administrator not fiduciary when it acts only "in accordance with the terms of the plan").[13] Fiduciary duty under ERISA is imposed only "to the extent" that a person performs or has the power to perform discretionary functions. Grindstaff, 946 F. Supp. at 552 ("Fiduciary status under §1002(21)(A) is not an all or nothing concept. A court must ask whether a person is a fiduciary with respect to the particular activity in question.") (quoting Maniace).

The Grindstaff decision is particularly instructive. There, plaintiffs challenged the procedures for voting shares of company stock owned by an ERISA plan. The district court

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[13] These and other cases are based on the text of ERISA Section 3(21)(A), 29 U.S.C. §1002(21)(A), which states:

> a person is a fiduciary with respect to a plan to the extent (i) he exercises any *discretionary authority or discretionary control* respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any *discretionary authority or discretionary responsibility* in the administration of such plan. (Emphasis added.)

See generally Maniace v. Commerce Bank, 40 F.3d 264, 267 (8th Cir. 1994) (trustee not fiduciary regarding company stock under rule that "discretion is the benchmark for fiduciary status under ERISA"), cert. denied, 514 U.S. 1111 (1995); Izzarelli v. Rexene Products Co., 24 F.3d 1506, 1525, n.34 (5th Cir. 1994) (no fiduciary duty to the extent bank "had no duty, discretion, or responsibility . . . "); Arizona State Carpenters Pension Trust Fund v. Citibank, 125 F.3d 715, 721 (9th Cir. 1997) (bank not a fiduciary where it did not have "independent authority or managerial responsibility over the operation or administration of the" plan). See also Crowley v. Corning, Inc., 234 F. Supp. 2d 222, 228-29 (W.D.N.Y. 2002) (dismissing complaint where defendants did not have discretionary control over decision to invest plan assets in employer stock); Hull v. Policy Mgmt. Sys. Corp., No. CIV.A.3:00-778-17, 2001 WL 1836286, at *7-8 (D.S.C. Feb. 9, 2001) (same).

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dismissed the action. The court determined that under the applicable plan documents, the trustee, First American National Bank ("First American"), lacked any discretionary authority with respect to voting the plan's shares; that it could act solely in a directed capacity. Id. at 551-52. Thus, First American did not have relevant fiduciary status and consequently could not be liable for breach of fiduciary duty. See id. at 552. In affirming dismissal, the Sixth Circuit made clear that a "person is a fiduciary only with respect to those aspects of the plan over which he exercises authority or control." 133 F.3d at 426. The court stated:

> First American is a *directed* trustee and is not a fiduciary to the extent it does not control the 'management or disposition' of the ESOP stock it holds in trust.

Id. (emphasis in original).

Here, there is no allegation in the Complaint that Putnam possessed relevant discretionary authority relating to investing Plan assets in Cardinal common stock, other than what is contained in the Plan Documents. (See Compl. ¶¶59-63.) Contrary to plaintiffs' allegations, the Plan Documents establish that Putnam was not allocated any responsibility "to monitor, control or in any way exercise any powers or discretion in the handling or disposition of any Plan assets, including the disposition of any funds, securities or other assets under the Plan." (1998 and 2002 SA §IV.E, App. Ex. Tabs 5 and 6.) The Plan documents contemplate that an employer stock fund be one of the participant investment options, and that "[t]o the extent practicable, all available assets of the Employer Common Stock Fund shall be used to purchase [s]hares [of Cardinal stock]. . . ." (1998 and 2002 Plans §8.05, App. Ex. Tabs 1 and 2.) Indeed, offering the Stock Fund was necessary to achieve one of the express purposes of the Plan, namely, "to provide Participants with ownership interests in the Company." (Id.) Both Service Agreements

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recited that, consistent with the Plan documents, Cardinal selected the Stock Fund as an available Plan investment option. (1998 and 2002 SA §IV.M, App. Ex. Tabs 5 and 6.)

In short, as discussed supra, pp. 3-6, the Plan Documents uniformly establish that Putnam had "no discretionary authority to determine the investment of the Trust assets." (1998 and 2002 SA §IV.E, App. Ex. Tabs 5 and 6.) Accordingly, Putnam was not performing a fiduciary function for the Plan with respect to investment of Plan assets in the Stock Fund and thus it should be dismissed for lack of relevant fiduciary status.[14]

C. Putnam Cannot Be Liable For Breach Of ERISA Fiduciary Duty Because, As A Directed Trustee, It Could Properly Follow Directions To Invest In Cardinal Stock Under The Complaint's Allegations And The Terms Of The Plan Documents On Which Plaintiffs' Claims Rest

1. The Allegations of the Complaint Fail to Allege any Duty on Putnam's Part to Act Contrary to Directions to Invest in Cardinal Stock as those Directions were Not Clearly on their Face Contrary to ERISA or the Terms of the Plan

Putnam is not liable because it satisfied the standard that applies to directed trustees. By statute, directed trustees are required to follow "proper directions of [the named] fiduciary which

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[14] Notwithstanding these provisions, the Complaint nonetheless alleges that Putman had discretion with respect to investment in Cardinal stock, citing primarily the Plan provisions which state: (i) "in no event shall participants be permitted to direct that such Accounts and/or such additional contributions be invested in the Employer Common Stock Fund until Cardinal Health, Inc., the Plan, the Trustee and all other relevant parties have fully complied with such requirements, including, but not limited to, federal and state securities laws, as the Committee deems to be applicable" and (ii) "[t]he Trustee, together with the Committee, was required to 'establish rules governing the administration of Investment Funds and procedures for Participant direction of investment.'" (Compl. ¶¶62-63, quoting, in part, 1998 Plan §9.05, App. Ex. Tab 1.) However, these allegations are insufficient. First, the cited provisions do not bestow on Putnam fiduciary responsibility for investment of assets in the Stock Fund. The modifying language in the quoted passage in Complaint paragraph 62, "as the Committee deems to be applicable," places all discretion in the hands of someone other than Putnam. Paragraph 63 of the Complaint also omits language in the Plan immediately following the quoted passage, language that similarly places all relevant discretion in the hands of entities other than Putnam: "The Committee and the Employer reserve the right to change the investment options available under the Plan and rules governing investment designations from time to time." (1998 and 2002 Plans, §9.05, first para., App. Ex. Tabs 1 and 2.) Second, the allegation that Putnam had discretion is contradicted by other allegations in the Complaint itself that people and entities other than Putnam possessed discretion over the investment of Plan assets. (See, e.g., Compl. ¶¶54-58.) Third, the allegation is inconsistent with the allocation of responsibilities contained in the Plan Documents when viewed as a whole, and the specific provisions cited in the text, above, placing no relevant discretion in Putnam's hands.

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are made in accordance with the terms of the plan and which are not contrary to [ERISA]." ERISA §403(a)(1), 29 U.S.C. §1103(a)(1). §403(a)(1)'s requirement that a trustee must follow directions unless they are not "in accordance with" the plan or are "contrary to" ERISA supplants the fiduciary duty imposed under §404(a). See Wright v. Oregon Metallurgical Corp., 360 F.3d 1090, 1102 (9th Cir. 2004) ("Directed trustees, as a result, cannot be held liable for following the investment instructions provided by a plan's named fiduciaries."); Herman v. NationsBank Trust Co., 126 F.3d 1354, 1361 (11th Cir. 1997) ("[I]nsofar as a trustee acts at the direction of a named fiduciary in accordance with the terms of the plan and ERISA's requirements, he is not subject to the fiduciary requirement in §1104(a) to act prudently.") (Citations omitted.)[15] Otherwise, ERISA's explicit distinction between "directed" trustees and other trustees would be meaningless.[16] As the Eighth Circuit explained in Maniace, 40 F.3d at 268:

> The obligations of a directed trustee are something less than that owed by typical fiduciaries. [The trustee] was not required to weigh the merits of an investment in [the company's] stock against all other investment options every time it was directed to purchase said stock by the [management c]ommittee.
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[15] See also Ershick v. United Missouri Bank of Kansas City, N.A., 948 F.2d 660, 665 (10th Cir. 1991) (directed trustee "not required to weigh the merits of an investment in [company] stock against all other investment vehicles . . ."); Springate v. Weighmasters Murphy Inc. Money Purchase Plan, 217 F. Supp. 2d 1007, 1015 (C.D. Cal. 2002) (directed trustee "did not have the power to determine where Plan assets should be invested and did not have a fiduciary duty to review the appropriateness of Plan investments"); Newton v. Van Otterloo, 756 F. Supp. 1121, 1132-33 (N.D. Ind. 1991) (no duty to investigate named fiduciary's direction; instead, directed trustee was "bound by . . . the plan document and by 29 U.S.C. §1103(a)(1) to follow the instruction [of the named fiduciary], and it did so").

[16] This reading of the interplay between §403(a)(1) and §404(a) is also consistent with the "the general principle of statutory construction that more specific provisions in a statute govern over those generally worded." Ehlmann v. Kaiser Foundation Health Plan of Texas, 198 F.3d 552, 555 (5th Cir.) (holding that ERISA's specific disclosure provisions, §§101-111, take precedence over §404's general fiduciary duty provision), reh'g and reh'g en banc denied, 210 F.3d 365, cert. dismissed, 530 U.S. 1291 (2000). The reading is further consistent with ERISA's general approach in allowing parties to allocate fiduciary responsibilities.

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> Imposing any 'residual' duties on [the trustee] would, in effect, abrogate the distinction between trustees and directed trustees clearly intended by ERISA.

ERISA's legislative history explains that §403(a)(1) requires a trustee to follow directions of a named fiduciary, such as the sponsoring employer or an investment committee, unless it is "clear on their face" that the directed actions would be "prohibited" by ERISA:

> If the [ERISA] plan so provides, the trustee who is directed by an investment committee is to follow that committee's directions unless it is *clear on their face* that the actions to be taken under those directions would be prohibited by the fiduciary responsibility rules of the bill or would be contrary to the terms of the plan or trust.

H.R. Rep. No. 93-1280, at 298 (1974) (Conf. Rep.), as reprinted in 1974 U.S.C.C.A.N. 5038, 5079. (Emphasis added.)[17] As the Complaint recognizes, the Plan Documents establish this standard to govern Putnam's conduct. (See Compl. ¶61 (The Trust Agreements provided that Putnam "may not follow the requests or instructions of Cardinal Health, the Plan Committee or any other person if 'it is clear on the face of such order, request or instruction that the actions to be taken thereunder would be prohibited by the fiduciary rules of ERISA or would be contrary to the terms of the Plan or this Agreement.'") (Quoting successor to 2001 TA §10, App. Ex. Tab 4.))

The "clear on their face" standard requires a directed trustee to assure only the facial validity of a direction it receives, not to assess underlying circumstances. Thus, directed trustees are not required to determine the prudence of actions required by directions involving investment

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[17] The legislative history also reflects congressional intent that a directed trustee not incur liability for following directions:

> . . . the plan may also provide that the trustee is to be subject to the direction of named fiduciaries with respect to investment decisions. In this case, if the trustee properly follows the instructions of the named fiduciaries, the trustee generally is not to be liable for losses that arise out of following these instructions.

Id. at 302. Cf. Moench v. Robertson, 62 F.3d 553, 571 (3d Cir. 1995) (ERISA "fiduciaries should not be immune from judicial inquiry, as a directed trustee essentially is"), cert. denied, 516 U.S. 1115 (1996).

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of assets in a sponsor's securities. See generally Grindstaff, 946 F. Supp. at 552; NationsBank, 126 F.3d at 1361; Maniace, 40 F.3d at 268. Indeed, the Sixth Circuit recently reversed a trial court with instructions to enter judgment where a directed trustee disregarded directions that were clearly on their face proper. See Benefits Committee of Saint-Gobain Corp. v. Key Trust Co., 313 F.3d 919, 932-33 (6th Cir. 2003) (court would not "condone the disregard by the Trustee of the [plan document] and the direction of the Benefits Committee to which he is supposed to answer" when the trustee failed to follow an instruction to repay a loan).[18]

Here, the directions Putnam received to invest Plan assets in the Stock Fund were both in accordance with the Plan and not contrary to ERISA; therefore, they were clearly on their face proper. First, the directions were in accordance with terms of Plan because holding Cardinal common stock was *required* by the Plan Documents. Under the Plan document, "[t]o the extent practicable, all available assets of the Employer Common Stock Fund shall be used to purchase Shares [of Cardinal common stock]." (1998 and 2002 Plan §8.05, App. Ex. Tabs 1 and 2.) Consistent with the stated Plan purpose of providing participants with ownership interests in Cardinal, the Service Agreements memorialize Cardinal's selection of the Stock Fund as one available investment option. (1998 and 2002 SA §IV.M, App. Ex. Tabs 5 and 6.)

Second, directions to make the Stock Fund an available investment option were not on their face prohibited by ERISA because the statute expressly contemplates that "eligible individual account plans," such as the Plan, may invest in securities issued by the employer/plan sponsor. ERISA §407(d)(3)(A), 29 U.S.C. §1107(d)(3)(A). Indeed, ERISA exempts such plans'

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[18] Requiring a directed trustee to examine the prudence of a named fiduciary's direction would entail duplication of fiduciary services. Because undertaking responsibilities of discretionary review of the prudence of investment in employer stock would require use of investment management resources and would expose directed trustees to greater risk, directed trustees would have to be compensated commensurately. This, in turn, would necessarily increase plan expenses, a result that would be contrary to ERISA's goal of avoiding unnecessary costs to employee benefits plans. See generally Mertens v. Hewitt Associates, 508 U.S. 248, 262-63 (1993); Beddall, 137 F.3d at 21 (affirming dismissal of directed trustee).

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investments in employer securities from the statute's investment diversification requirements and its specific aggregate limitations on investments in employer securities. See ERISA §§404(a)(2) and 407(b)(1), 29 U.S.C. §§1104(a)(2) and 1107(b)(1). See generally Foltz v. U.S. News & World Report, Inc., 865 F.2d 364, 373 (D.C. Cir.) (ERISA "specifically favors" employee ownership), cert. denied, 490 U.S. 1108 (1989). Thus, Putnam cannot have acted contrary to ERISA in carrying out these directions. See Maniace, 40 F.3d at 267-68 (§403(a) not violated by following directions to invest plan assets in employer stock); Ershick, 948 F.2d at 668-69 (same).

2. The Complaint Fails to Allege any Duty on Putnam's Part to Act Contrary to Directions to Invest in Cardinal Stock under the Department of Labor's Two Pronged Standard for Trustees Directed to Invest Plan Assets in Publicly Held Securities of the Plan Sponsor

The Department of Labor (the "Department" or "DOL") recently disseminated its views as to a directed trustee's duty under ERISA §403(a)(1) when instructed to invest in publicly traded stock issued by the plan sponsor. See Field Assistance Bulletin No. 2004-03, dated December 17, 2004 ("FAB") (attached hereto as Exhibit A). The Department's guidance addresses two scenarios: where a directed trustee possesses material, non-public information about the sponsor and where its only information is public. Even under the DOL's standards, which are more stringent than the congressionally articulated "clear on their face" test, Putnam cannot be liable on the allegations in the Complaint.

As a threshold matter, the Department recognizes that directed trustees do not have "the independent obligation to determine the prudence of every transaction" or "to duplicate or second-guess the work of the plan fiduciaries that have discretionary authority." FAB at 4. Indeed, the duty of directed trustees to question directions to invest in publicly traded stocks is "quite limited." Id.

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In then articulating its views of directed trustee duty, the Department first addresses the case where a directed trustee possesses "material non-public information that is necessary for a prudent decision." FAB at 4. This is considered by the Department to be the "primary circumstance" where when an "an obligation" might arise. Id. If a directed trustee possesses such material non-public information about the sponsor, it has a duty to inquire whether the named fiduciary knows of and has considered such information. See id.

Turning to the more common situation, where the trustee does not possess any inside information, the Department states that the trustee "will rarely have an obligation under ERISA to question the prudence of a direction to purchase publicly traded securities at the market price." FAB at 5. The Department bases this position on three principles: (i) that public markets are generally efficient, with stock prices reflecting available information and known risks, (ii) the securities laws impose substantial obligations on the reporting company, its officers and accountants to state their financial records accurately and (iii) ERISA imposes a "stringent standard of care" on the directing, or front-line, fiduciary. Id. at 5. Thus, the Department believes that directed trustees may have an obligation to question a named fiduciary's direction to invest in publicly traded stock of the employer, when the trustee possesses no more than public information, only in those very rare instances where there are clear and compelling public indicators that call into serious question the company's viability as a going concern:

> [i]n limited, extraordinary circumstances, where there are *clear and compelling public indicators*, as evidenced by an 8-K filing with the Securities and Exchange Commission (SEC), a bankruptcy filing or similar public indicator, that *call into serious question a company's viability as a going concern*, the directed trustee may have a duty not to follow the named fiduciary's instruction without further inquiry.

Id. at 6. (Emphasis added.)

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Under this standard, as endorsed by the Southern District of New York, the only public information that would trigger a directed trustee's duty to question directions by a named fiduciary is "fundamental perspective-shifting information that would disclose the impending collapse of the company." In re WorldCom, Inc. ERISA Litigation, 354 F. Supp. 2d 423, 450 (S.D.N.Y. 2005) (granting summary judgment to directed trustee). WorldCom held that "[k]nowledge that a company's fortunes are declining does not impose a duty of inquiry" and "even in the case of a distressed company in bankruptcy, it might not be imprudent for a directed trustee to follow a direction to purchase or hold stock in that company . . . ." Id. at 448, 449. The WorldCom court held that that the directed trustee in that case, Merrill Lynch, could not be liable for breach of fiduciary duty arising from the continued holding of WorldCom stock while that company's fortunes declined. Id. at 449. WorldCom specifically recognized that under the FAB, opinions about a company's fortunes held by persons outside the company, such as analysts' reports, are insufficient to require a directed trustee to act; similarly, even knowledge of a pending SEC investigation is insufficient to trigger any duty. See id. at 438, 449-50.

The threshold set by the FAB and WorldCom as to when a directed trustee must take some action is simply not met here. The first prong of the FAB analysis does not apply because there simply is no allegation that Putnam possessed any material, non-public information about Cardinal, least of all information that would be necessary for a "prudent decision."

Nor is the second test met. The Complaint makes no allegation of any clear and compelling public indicator calling into serious question Cardinal's viability as a going concern. Cardinal is not alleged to have approached "impending collapse" or even a bankruptcy filing. The only public information of any type cited in the Complaint is the October 27, 2004 Fitch Report. (Compl. ¶85.) But this report is insufficient to trigger any duty under the FAB and

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WorldCom. The FAB expressly states that a directed trustee's duty is only triggered by public indicators similar to the issuer's own 8-K filing with the SEC or its bankruptcy filing -- statements by the company and not opinions of outsiders. The FAB expressly states that no duty is triggered by analyses about corporate affairs or prospects. See FAB at 6, and 6, n.5 ("[a] directed trustee's actual knowledge of media or other public reports or analyses . . . does not, in and of itself, constitute knowledge of clear and compelling evidence"); see also WorldCom, 354 F. Supp. 2d at 449 ("Analyst recommendations to sell WorldCom securities do not represent reliable information regarding the company's viability.")

Those publicly filed statements by the Company that should be considered under the Department guidance, the SEC filings, show that Cardinal was profitable and not in danger of imminent collapse. The annual statement for the period ending June 30, 2004 shows that since 2000, Cardinal was reporting increasing year-over-year revenue, earnings and assets. (See Exhibit J to Appendix in Support of Certain Defendant's Motion to Dismiss the Consolidated Amended ERISA Complaint ("Cardinal App."), at 26-27.) It reported positive earnings through the end of Putnam's tenure as Trustee in December 2004. (See id. at 26, Cardinal App. Ex. I at 3.) As to cash on hand, a reflection of a company's liquidity, Cardinal reported an increase from $544 million on December 31, 2003 to $1.27 billion on December 31, 2004. (See Cardinal App. Ex. I at 5.) These public indicators do not call into serious question Cardinal's viability as a going concern; indeed, they negate any inference of Cardinal's imminent collapse. Because the DOL standard is not met here, Putnam cannot be liable.[19]

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[19] Even if the Fitch Report was relevant under the Department's standard, which it is not, it, too, does not call into serious question the Company's viability as a going concern. A full copy of the report is attached as App. Ex. Tab 7. (It is proper to consider the full report for the reasons cited supra, p. 8 n.12.) Fitch rated Cardinal as BBB+/F2, indicating that Cardinal's debt was believed to be investment grade. Moreover, the Fitch Report provides a number of observations precluding a likelihood of collapse. For example, it states that the Company's "2005 cash flow should be strong" and that an upcoming scheduled earnings call to discuss first-

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D. This Case Is Indistinguishable From The First Circuit Ruling Which Affirmed Dismissal Under Rule 12(b)(6) Of A Virtually Identical Complaint Against Putnam

Under any legal standard of duty applicable to directed trustees, Putnam should be dismissed because the Complaint alleges no facts supporting its conclusory assertion that Putnam knew or should have known that Cardinal stock was an imprudent investment (see Compl. ¶87), just as the First Circuit affirmed dismissal under Federal Rule of Civil Procedure 12(b)(6) of an equally lacking complaint against Putnam in LaLonde v. Textron, 369 F.3d 1, 7 (1st Cir. 2004), aff'g in relevant part, 270 F. Supp. 2d 272 (D.R.I. 2003).

In LaLonde, plaintiffs alleged that, among other things, various defendants could be liable under ERISA's fiduciary and co-fiduciary provisions by reason of a defined contribution plan's continued holding and investment of assets in Textron, Inc. ("Textron") stock. Putnam was one of those defendants. Plaintiffs claimed that Textron stock was an imprudent investment for the plan's assets for at least four reasons: (i) Textron's earnings per share declined by over 70% during a two year period; (ii) Textron engaged in a restructuring that was expected to result in layoffs of roughly 10% of the company's employees; (iii) Textron common stock underperformed other stocks; and (iv) Textron artificially inflated the price of its stock by concealing internal difficulties. See 369 F.3d at 3.

The district court in LaLonde dismissed the complaint against Putnam. It held that the plan documents, including trust and service agreements, did not confer on Putnam any discretionary authority with respect to investment in Textron common stock. See 270 F. Supp. 2d at 282. Indeed, those documents contained relevant terms that are identical to the ones here that allocate all discretionary authority to people and entities other than Putnam. See, e.g., id.

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quarter 2005 results "preclude[ed] any need for bank extensions, thus alleviating short-term liquidity concerns." (App. Ex. Tab 7.)

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(quoting §6 of the relevant Textron trust agreement, which stated: "the Trustee shall transfer to each such Investment Fund such portion of the assets of the Trust as the Administrator or Plan members *direct* in accordance with the specific provisions of the Plan and in the manner provided in the Service Agreement"). (Emphasis in original.) (Compare 1998 TA §8(a), App. Ex. Tab 3, containing identical language.) The district court commented that plaintiffs' theory that Putnam should have disregarded the plan documents and directions it received to invest in Textron common stock "turns the relationship between the Plan and the Trustee on its head. If Putnam had done what the Plaintiffs suggest it would have been fired and sued by the Plan." 270 F. Supp. 2d at 282.

The First Circuit affirmed dismissal of Putnam, albeit on different grounds. The appellate court expressly reserved the question of Putnam's fiduciary status and thus the nature of its duty. See 369 F.3d at 5 n.8, 7. Instead, it held that the LaLonde complaint contained no well-pleaded allegation stating a claim that Putnam violated ERISA by investment in employer stock, where there were no allegations that Putnam knew or had any reason to know that the price of Textron's common stock was artificially inflated. The court held that the public information knowable by Putnam, namely, the corporate restructuring, drop in stock price and declining earnings, were insufficient to state a claim under any theory of duty on Putnam's part. The Court stated:

> there is absolutely nothing in the complaint which permits an inference that Putnam abused any discretion it might have had. Putnam is not alleged to have knowledge of any malfeasance within Textron; it is alleged only to have learned (as the events were unfolding) that Textron's stock price and profits were declining and that the company was undergoing a restructuring. As the district court aptly observed, this simply is not enough to ground a finding that Putnam violated any duties it might have owed to the class. It would subvert the purposes of ERISA to permit lawsuits against plan fiduciaries (again, assuming that Putnam is a

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> plan fiduciary) every time a company's fortunes took a relatively unexceptional turn for the worse.

LaLonde v. Textron, 369 F.3d 1, 7 (1st Cir. 2004).[20]

Similarly, here, Putnam should be dismissed regardless of the standard applied to its conduct. The Complaint is not materially different than the one in LaLonde. Putnam is not alleged to have had any knowledge of the accounting improprieties that form the basis of plaintiffs' allegation of imprudence. The Complaint itself alleges that these facts were hidden from the public. (See Compl. ¶87 (alleging "*undisclosed* materially adverse information") (emphasis added).) There is no allegation that Putnam had access to any inside information about Cardinal. (See Compl. ¶¶78-84.) The only public information alleged in the Complaint is the Fitch rating, which, even if properly considered, hardly forecasts impending collapse.

E. Under The Bare, Conclusory Allegations Of The Complaint, Putnam Cannot Be Liable Under ERISA's Co-Fiduciary Provisions

The Complaint contains one paragraph alleging that each defendant is liable for the acts of the others as a co-fiduciary. (Compl. ¶90.) Plaintiffs provide no facts in support of this conclusory allegation, they merely recite the statutory text of ERISA §405(a). This is impermissible pleading and for this reason alone the co-fiduciary claim should be dismissed. See generally Crowley, 234 F. Supp. 2d at 230 (conclusory allegation of breach of ERISA fiduciary duty is insufficient to support liability). Plaintiffs have pleaded no facts indicating that Putnam had the requisite knowledge of any other fiduciary's breach to establish a claim under

[20] Accord In re McKesson HBOC, Inc. ERISA Litig., No. C00-20030RMW, 2002 WL 31431588, at *12 (N.D. Cal. Sept. 30, 2002) ("The complaint alleges only the conclusory assertion that Chase knew, should have known, or is deemed to have known, that McKesson had become an unsuitable and imprudent investment as a result of HBOC's improper accounting practices. The court need not accept conclusory allegations as true on a motion to dismiss where those allegations do not follow from the description of the facts as alleged. Here, no *facts* are alleged that would give rise to a conclusion that Chase knew the investment directions it received from the McKesson Plan were imprudent, that Chase had any knowledge of the HBOC accounting irregularities, or that the McKesson Plan Fiduciaries were abusing their discretion in continuing to fund the McKesson Plan pursuant to the Plan terms. Absent such facts, Chase is not liable, and absent non-conclusory allegations of those facts, Chase should not have to defend against the claim.") (emphasis in original) (citation omitted).

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either ERISA §§405(a)(1) or 405(a)(3). See Keach v. U.S. Trust Co., 240 F. Supp. 2d 840, 844 (C.D. Ill. 2002) ("It is well-established that actual knowledge by a fiduciary is required in order for co-fiduciary liability to attach under §405(a).") (citing Donovan v. Cunningham, 716 F.2d 1455, 1475 (5th Cir. 1983)).[21]

Finally, it is axiomatic that there can be no liability under ERISA §§405(a)(1) or (3) if there was no breach of fiduciary duty in the first instance. See Maniace, 40 F.3d at 268-69 (no breach of co-fiduciary liability where plaintiffs "failed to plead or offer facts" indicating that there was an underlying fiduciary breach). As Cardinal demonstrates in its motion to dismiss, there was no underlying breach of any fiduciary duty by any person. Accordingly, Putnam cannot be liable under §405.

V. CONCLUSION

For the foregoing reasons, the Consolidated Amended ERISA Complaint and Jury Demand should be dismissed with prejudice as against Putnam Fiduciary Trust Company.[22] Under Local Rule 7.1(b)(2), Putnam respectfully requests oral argument on this motion.

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[21] Section 405(a)(2) requires a violation of §404(a)(1) before liability can attach. For the reasons described supra, Putnam could not have violated §405(a)(2) because Putnam did not violate §404(a)(1). See generally Brandt v. Grounds, 687 F.2d 895, 898-99 (7th Cir. 1982) (affirming dismissal of claim under §405(a)(2) where bank was not a fiduciary in the first instance, and did not breach §404(a)(1)'s fiduciary duties).

[22] Putnam also joins in the motion to dismiss the Complaint filed by Cardinal and the other defendants to the extent applicable to Putnam. Specifically, Putnam joins the arguments raised in Certain Defendants' Motion to Dismiss the Consolidated Amended ERISA Complaint Sections IV.A. (monetary damages not allowed under ERISA §502(a)(3), 29 U.S.C. §1132(a)(3)), IV.B. (offering Cardinal stock was not an abuse of discretion by any defendant) and IV.G. (no claim stated for co-fiduciary liability).

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Respectfully submitted,

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Dated: August 24, 2005

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that on August 24 2005, a true and accurate copy of Defendant Putnam Fiduciary Trust Company's Motion to Dismiss the Consolidated Amended ERISA Complaint and Jury Demand and accompanying Memorandum in Support was filed electronically. Notice of this filing will be sent today to all parties, by operation of the Court's electronic filing system. Parties may access this filing through the Court's system. Copies of this filing will also be sent via regular mail to:

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EXHIBIT A

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U.S. Department of Labor

Employee Benefits Security Administration
Washington, D.C. 20210

FIELD ASSISTANCE BULLETIN NO. **2004-03**

DATE: DECEMBER 17, 2004

MEMORANDUM FOR: VIRGINIA C. SMITH, DIRECTOR OF ENFORCEMENT
REGIONAL DIRECTORS

FROM: ROBERT J. DOYLE
DIRECTOR OF REGULATIONS
& INTERPRETATIONS

SUBJECT: FIDUCIARY RESPONSIBILITIES OF DIRECTED TRUSTEES

ISSUE: In the context of publicly traded securities, what are the fiduciary responsibilities of a directed trustee?

BACKGROUND

Many employee pension plans use directed trustees to carry out transactions according to instructions from a named fiduciary of the plan. During investigations of such transactions by the Department, difficult questions may arise regarding the scope of the directed trustee's fiduciary duties. Recent court decisions, addressing this issue in the context of purchases and holdings of publicly traded employer securities in particular, have focused attention on the nature and scope of a directed trustee's fiduciary duties. This bulletin provides general guidance to EBSA regional offices regarding the Department's views on the responsibilities of directed trustees under ERISA, particularly with respect to directions involving employer securities.

FIDUCIARY STATUS OF DIRECTED TRUSTEE

Section 403(a) provides that a plan trustee "shall have exclusive authority and discretion to manage and control the assets of the plan." Section 3(21)(A) provides that a person is a fiduciary with respect to a plan "to the extent . . . he . . . exercises any authority or control respecting management or disposition of its assets." A plan trustee, therefore, will, by definition, always be a "fiduciary" under ERISA as result of its authority or control over plan assets. Not all

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trustees, however, have the same authority or discretion to manage or control the assets of a plan. In this regard, section 403(a) specifically recognizes that a trustee or trustees will have limited authority or discretion when:

> (1) the plan expressly provides that the trustee or trustees are subject to the direction of a named fiduciary who is not a trustee, in which case the trustees shall be subject to proper directions of such fiduciary which are made in accordance with the terms of the plan and which are not contrary to this Act.

While section 403(a)(1) does not remove a directed trustee from section 3(21)'s purview, it significantly limits such a trustee's responsibilities as a plan fiduciary. As the district court in In re Enron Corp. Securities, Derivative & ERISA Litig., 284 F. Supp. 2d 511, 601 (S.D. Tex. 2003), recognized:

> At least some fiduciary status and duties of a directed trustee are preserved, even though the scope of its exclusive authority and discretion to manage and control the assets of the plan' has been substantially constricted by the directing named fiduciary's correspondingly broadened role . . . .

The court in In re WorldCom, Inc. ERISA Litig., 263 F. Supp. 2d 745, 762 (S.D.N.Y. 2003) also noted that, while the directed trustee provision serves as a limiting principle, "section 403(a) does not . . . eliminate the fiduciary status or duties that normally adhere to a trustee with responsibility over ERISA assets." See also FirsTier Bank, N.A. v. Zeller, 16 F.3d 907, 9110 (8th Cir.), cert. denied sub nom, Vercoe v. FirsTier Bank, N.A., 513 U.S. 871 (1994); Herman v. NationsBank Trust Co., 126 F.3d 1354, 1361-62, 1370 (11th Cir. 1997).

The duties of a directed trustee under section 403(a)(1) are therefore significantly narrower than the duties generally ascribed to a discretionary trustee under common law trust principles.[1]

DETERMINING WHETHER A DIRECTION IS "PROPER"

Under section 403(a)(1), a directed trustee is subject to proper directions of a named fiduciary. For purposes of section 403(a)(1), a direction is proper only if the direction is "made in accordance with the terms of the plan" and "not contrary to the Act [ERISA]." Accordingly, when a directed trustee knows or

[1] It is assumed for purposes of this guidance that discretionary authority or control over plan assets, beyond that discussed herein as applicable to a person serving as a directed trustee under section 403(a)(1), has not been conferred upon a directed trustee under the terms of the plan, including trust and service provider agreements.

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should know that a direction from a named fiduciary is not made in accordance with the terms of the plan or is contrary to ERISA, the directed trustee may not, consistent with its fiduciary responsibilities, follow the direction.

In accordance with plan terms

Under section 403(a)(1), a directed trustee may not follow a direction that the trustee knows or should know is inconsistent with the terms of the plan. In order to make such determinations, directed trustees necessarily have a duty to request and review all the documents and instruments governing the plan that are relevant to its duties as directed trustee. Accordingly, if a directed trustee either fails to request such documents or fails to review the documents furnished in response to its request and, as a result of such failure, follows a direction contrary to the terms of the plan, the directed trustee may be liable for following such direction because the directed trustee had a duty to request and review pertinent plan documents and, therefore, should have known that the direction was not in accordance with the terms of the plan. If a directed trustee follows an improper direction, as would be the case where the purchase of a particular stock at the direction of the plan's named fiduciary is contrary to the plan's investment policy, the directed trustee may be liable for a breach of its fiduciary duty to follow only proper directions.

It is the view of the Department that a direction is consistent with the terms of a plan if the documents pursuant to which the plan is established or operated do not prohibit the direction. It is also the view of the Department that if, in the course of reviewing the propriety of a particular direction, a directed trustee determines that the terms of the relevant documents are ambiguous with respect to the permissibility of the direction, the directed trustee should obtain a clarification of the plan terms from the fiduciary responsible for interpreting such terms in order to ensure that the direction is proper. In this regard, the directed trustee may rely on the interpretation of such fiduciary.

Not contrary to ERISA

Even when a direction is consistent with the terms of the plan, the direction may nonetheless fail to be a proper direction because it is contrary to ERISA. Under section 403(a)(1), a directed trustee may not follow a direction that the trustee knows or should know is contrary to ERISA. For example, the directed trustee cannot follow a direction that the directed trustee knows or should know would require the trustee to engage in a transaction prohibited under section 406 or violate the prudence requirement of section 404(a)(1). The following discussion further clarifies the duties of a directed trustee in this area.

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Prohibited transaction determinations

A directed trustee must follow processes that are designed to avoid prohibited transactions. A directed trustee could satisfy its obligation by obtaining appropriate written representations from the directing fiduciary that the plan maintains and follows procedures for identifying prohibited transactions and, if prohibited, identifying the individual or class exemption applicable to the transaction. A directed trustee may rely on the representations of the directing fiduciary unless the directed trustee knows that the representations are false.

Prudence determinations

The named fiduciary has primary responsibility for determining the prudence of a particular transaction, whether the transaction involves buying, selling or holding particular assets. Accordingly, as the courts and the Department have long recognized, the scope of a directed trustee's responsibility is significantly limited. A directed trustee does not, in the view of the Department, have an independent obligation to determine the prudence of every transaction. The directed trustee does not have an obligation to duplicate or second-guess the work of the plan fiduciaries that have discretionary authority over the management of plan assets and does not have a direct obligation to determine the prudence of a transaction. See In re WorldCom ERISA Litig., 263 F. Supp. 2d at 761; Herman v. NationsBank Trust Co., 126 F.3d at 1361-62, 1371 (directed trustee does not have a direct obligation of prudence under ERISA section 404; its obligation is simply "to make sure" the "directions were proper, in accordance with the terms of the plan, and not contrary to ERISA").

Duty to act on non-public information

The directed trustee's obligation to question market transactions involving publicly traded stock on prudence grounds is quite limited. The primary circumstance in which such an obligation could arise is when the directed trustee possesses material non-public information regarding a security. If a directed trustee has material non-public information that is necessary for a prudent decision, the directed trustee, prior to following a direction that would be affected by such information, has a duty to inquire about the named fiduciary's knowledge and consideration of the information with respect to the direction. For example, if a directed trustee has non-public information indicating that a company's public financial statements contain material misrepresentations that significantly inflate the company's earnings, the trustee could not simply follow a direction to purchase that company's stock at an artificially inflated price.

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Generally, the possession of non-public information by one part of an organization will not be imputed to the organization as a whole (including personnel providing directed trustee services) where the organization maintains procedures designed to prevent the illegal disclosure of such information under securities, banking or other laws.[2] If, despite such procedures, the individuals responsible for the directed trustee services have actual knowledge of material non-public information, the directed trustee, prior to following a direction that would be affected by such information, has a duty, as indicated above, to inquire about the named fiduciary's knowledge and consideration of the information with respect to the direction. Similarly, if the directed trustee performs an internal analysis in which it concludes that the company's current financial statements are materially inaccurate, the directed trustee would have an obligation to disclose this analysis to the named fiduciary before making a determination whether to follow a direction to purchase the company's security. The directed trustee would not have an obligation to disclose reports and analyses that are available to the public.

Duty to act on public information

Absent material non-public information, a directed trustee, given its limited fiduciary duties as determined by statute, will rarely have an obligation under ERISA to question the prudence of a direction to purchase publicly traded securities at the market price solely on the basis of publicly available information. Three considerations counsel in favor of this view: (1) markets generally are assumed to be efficient so that stock prices reflect publicly available information and known risks; (2) in the case of employer securities, the securities laws impose substantial obligations on the company, its officers, and its accountants to state their financial records accurately; and (3) ERISA section 404 requires the instructing fiduciary to adhere to a stringent standard of care.[3] Furthermore, because stock prices fluctuate as a matter of course, even a steep drop in a stock's price would not, in and of itself, indicate that a named fiduciary's direction to purchase or hold such stock is imprudent and, therefore, not a proper direction.

In limited, extraordinary circumstances, where there are clear and compelling public indicators, as evidenced by an 8-K filing with the Securities and Exchange

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[2] The Department expresses no view as to whether, or under what circumstances, other procedures established by an organization to limit the disclosure of information will serve to avoid the imputation of information to a directed trustee.

[3] It should be noted that, in the case of an individual account plan, the diversification requirements of section 404(a)(1)(C) do not apply to the acquisition or holding of qualifying employer securities within the meaning of section 407(d)(5).

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Commission (SEC), a bankruptcy filing or similar public indicator, that call into serious question a company's viability as a going concern,[4] the directed trustee may have a duty not to follow the named fiduciary's instruction without further inquiry.[5] For example, if a company filed for bankruptcy under circumstances which make it unlikely that there would be any distribution to equity-holders, or otherwise publicly stated that it was unlikely to survive the bankruptcy proceedings in a manner that would leave current equity-holders with any value, the directed trustee would have an obligation to question whether the named fiduciary has considered the prudence of the direction.[6] It also is the view of the Department that, in situations where a fiduciary who is a corporate employee gives an instruction to buy or hold stock of his or her company subsequent to the company, its officers or directors, being formally charged by state or Federal regulators with financial irregularities, the directed trustee, taking such facts into account, may need to decline to follow the direction or may need to conduct an independent assessment of the transaction in order to assure itself that the instruction is consistent with ERISA.[7] If, however, an independent fiduciary was appointed to manage the plan's investment in company stock, a directed trustee could follow the proper directions of the independent fiduciary without having to conduct its own independent assessment of the transaction.

EFFECT OF QUESTIONING DIRECTIONS ON FIDUCIARY STATUS

It is the view of the Department that the nature and scope of a directed trustee's fiduciary responsibility, as discussed herein, does not change merely because the

[4] We note that section 409 of the Sarbanes-Oxley Act of 2002, 15 U.S.C. 78(m)(l), requires public companies to disclose "on a rapid and current basis" material information regarding changes in the company's financial condition or operations as the SEC by rule determines to be necessary or useful for the protection of investors or in the public interest. The SEC has recently updated its disclosure requirements related to Form 8-K, expanding the number of reportable events and shortening the filing deadline for most items to four business days after the occurrence of the event triggering the disclosure requirements of the form. 69 FR. 15594 (Mar. 25, 2004). Not all 8-K filings regarding a company would trigger a duty on the part of a directed trustee to question a direction to purchase or hold securities of that company. Only those relatively few 8-Ks that call into serious question a company's ongoing viability may trigger a duty on the part of the directed trustee to take some action.

[5] A directed trustee's actual knowledge of media or other public reports or analyses that merely speculate on the continued viability of a company does not, in and of itself, constitute knowledge of clear and compelling evidence concerning the company sufficient to give rise to a directed trustee's duty to act.

[6] Even under such circumstances, it might not be imprudent to purchase or hold stock in a distressed company in bankruptcy. There may be situations in which the plan's fiduciaries could reasonably conclude that the stock investment makes sense, even for a long-term investor, in light of the proposed restructuring of the company's debts or other factors.

[7] Nothing in the text should be read to suggest that a directed trustee would have a heightened duty whenever a regulatory body opens an investigation of a company whose securities are the subject of a direction, merely based on the bare fact of the investigation.

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directed trustee, in carrying out its duties, raises questions concerning whether a direction is "proper" or declines to follow a direction that the directed trustee does not believe is a proper direction within the meaning of section 403(a)(1). For example, information provided to a named fiduciary concerning the prudence of a direction is not investment advice for purposes of ERISA §3(21)(A)(ii). Similarly, if a named fiduciary changes a direction in response to a directed trustee's inquiries or information, the directed trustee's fiduciary responsibility with respect to the changed direction remains governed by section 403(a)(1). The directed trustee does not become primarily responsible for the prudence of the direction.

CO-FIDUCIARY DUTIES

Under ERISA section 405(a)(1), a fiduciary is liable for the breach of another fiduciary if the fiduciary "participates knowingly" in the breach of the other fiduciary. Accordingly, if a directed trustee has knowledge of a fiduciary breach, the directed trustee may be liable as a co-fiduciary unless the directed trustee takes reasonable steps to remedy the breach. Thus, if the directed trustee knew that the named fiduciary was failing to discharge its obligations in accordance with ERISA's requirements, it could not simply follow directions from the breaching fiduciary. Efforts to remedy a breach (or to prevent an imminent breach) may include reporting the breach to other fiduciaries of the plan or the Department of Labor.

CONCLUSION

Although its responsibilities are significantly limited under the statute, a directed trustee is a fiduciary under ERISA and must exercise its duties prudently and solely in the interest of the plan participants and beneficiaries. Particularly in the context of purchasing, selling or holding publicly traded securities on a generally recognized market, the trustee may follow the named fiduciary's directions absent extraordinary circumstance as discussed above.