The Second Circuit Adopts the "Moench Presumption," Rejects Stock Drop Claims Against Citigroup

Joining at least the Third, Fifth, Sixth, and Ninth Circuits in finding a presumption of prudence attaches when defined contribution plans offer employer stock as an investment option, a divided panel of the Second Circuit has affirmed the dismissal of ERISA "stock drop" claims against Citigroup in *In re: Citigroup ERISA Litigation*, 09-3804 (Sept. 28, 2010).

Judges Walker and Cabranes voted to affirm dismissal of the complaint, which alleged that plan fiduciaries had breached their ERISA duty of prudence by not limiting the 401(k) Plan's investments in Citigroup stock in the face of mounting subprime mortgage exposure. The Court also affirmed the dismissal of plaintiffs' claim that defendants breached their ERISA duty of loyalty by not disclosing inside information about these exposures to plan participants.

The court affirmed dismissal of the prudence claim because: 1) the Citigroup plan required offering a Citigroup stock fund and 2) the inclusion of that fund as an investment option is entitled to the "presumption of prudence" first articulated by the Third Circuit in *Moench v Robertson*, 62 F.3d 553 (3d Cir. 1995). Under *Moench*, an employee stock ownership plan or "eligible individual account plan" participant may only recover from an ERISA fiduciary for failing to eliminate company stock investments if the court finds (under an abuse of discretion standard) that he has overcome a presumption that offering the stock investment is prudent.

Importantly, the Second Circuit found that this rule could be applied at the motion to dismiss stage. The plaintiffs' allegations that the defendants knew of the bank's subprime mortgage exposure and failed to evaluate the ongoing prudence of Citigroup stock were insufficient to overcome the presumption under an abuse of discretion standard of review. To state a viable claim plaintiffs would have had to allege "circumstances placing the employer in a 'dire situation' that was objectively unforeseeable by the [plan's] settlor" in order to require them to override the plan's terms requiring that employer stock be offered as an investment. Although Citigroup's stock price fell more than 50% during the class period, that was not a sufficiently dire situation in the Court's view.

The Court also found that ERISA fiduciaries have no duty to disclose non-public information regarding the performance of plan investment options and that the plaintiffs had not supported their claim that plan fiduciaries made knowingly false statements.

Judge Straub dissented, arguing that the *Moench* presumption improperly guts ERISA's fiduciary duties. Judge Straub would have reviewed the fiduciaries' conduct under a plenary standard of review, a standard he found ill suited for resolution at the pleadings stage. Judge Straub found plausible allegations of misstatements by at least one plan fiduciary and would have reversed as to the disclosure claim as well.

In a companion ruling issued the same day, the Second Circuit in *Gearren v. McGraw-Hill Cos.*, Case No. 10-792, affirmed the dismissal of a complaint, holding that plaintiffs failed to allege facts sufficient to demonstrate that defendant fiduciaries abused their discretion by retaining an employer stock fund as an investment option

I*n re: Citigroup ERISA Litigation* is a significant decision for employers as it furthers the trend of judicial skepticism to stock drop claims. Indeed, as more circuits adopt the *Moench* presumption, plaintiffs seeking to bring ERISA stock-drop claims against plans with "hard wired" company stock funds will have an increasingly difficult time doing so. In light of this decision, employers with company stock-funds should consider hard-wiring these funds into the governing plan document and reviewing their internal documentation and practices to ensure that they are consistent with a hard-wired company stock fund.

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