No. 17-1873(L), 17-2224, 17-2323, 17-2324, 18-1029

IN THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

TIM P. BRUNDLE, on behalf of the Constellis Employee Stock Ownership Plan,
Plaintiff-Appellee,
and

ANDREW HALLDORSON, on behalf of the Constellis Employee Stock Ownership Plan, and on behalf of a class of all other persons similarly situated,
Plaintiff,
v.

WILMINGTON TRUST, N.A., as successor to Wilmington Trust Retirement and Institutional Services Company,
Defendant-Appellee.

Appeal from the United States District Court for the Eastern District of Virginia,
No. 1:15-cv-01494-LMB-IDD, Honorable Leonie M. Brinkema

BRIEF FOR THE SECRETARY OF LABOR AS AMICUS CURIAE SUPPORTING PLAINTIFF-APPELLEE

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STATEMENT OF ISSUES

1. Whether the district court correctly refused to defer to Wilmington's or its adviser's determination of the fair market value of the Constellis stock when it determined that Wilmington's approval of the purchase of employer stock on behalf of an employee stock ownership plan ("ESOP") violated ERISA.

2. Whether the district court correctly held that the ESOP should not have paid an extra amount to acquire control of Constellis (a "control premium") because it did not actually acquire effective control of the company.

3. Whether the district court correctly held that Wilmington's liability for the ESOP's losses caused by purchasing employer stock at an excessive price may not be offset by the amount the ESOP received when it subsequently sold the stock in an independent transaction.

STATEMENT OF INTEREST

The Secretary of Labor has primary interpretative and enforcement authority for Title I of ERISA, 29 U.S.C. §§ 1001, et seq., which protects employee benefit plan participants by imposing stringent standards on fiduciaries, and has an interest in promoting ERISA's uniform application. Sec'y of Labor v. Fitzsimmons, 805 F.2d 682, 692-93 (7th Cir. 1986) (en banc). In particular, the Secretary is responsible for ensuring that when an employer establishes an ESOP to provide

retirement benefits for its employees, the ESOP's fiduciaries abide by ERISA and pay no more than fair market value for employer stock.

The Secretary has consistently taken the position that fiduciaries must make "good faith" determinations of the fair market value when they purchase employer stock for the ESOP and may not blindly rely on valuation professionals they retain. "[G]ood faith" means "they arrived at their determination of fair market value by way of a prudent investigation in the circumstances then prevailing." Donovan v. Cunningham, 716 F.2d 1455, 1467-68 (5th Cir. 1983). As part of that investigation, they must independently determine whether reliance on a valuation is reasonably justified. See, e.g., id. at 1462-63; Howard v. Shay, 100 F.3d 1484, 1490 (9th Cir. 1996); Bussian v. RJR Nabisco, Inc., 223 F.3d 286, 300-01 (5th Cir. 2000); Chao v. Hall Holding Co., Inc., 285 F.3d 415, 435-37 (6th Cir. 2002); Perez v. Bruister, 823 F.3d 250, 262-65 (5th Cir. 2016); Martin v. Harline, No. Civ.A. 87-NC-115J, 1992 WL 12151224, at *14 (D. Utah Mar. 30, 1992); Perez v. First Bankers Trust Services, Inc., 210 F. Supp. 3d 518, 531-33 (S.D.N.Y. 2016). Because Wilmington's arguments would undermine this well-established caselaw and diminish the fiduciary's obligations, the Secretary has a strong interest in urging this Court to follow the standards adopted by other circuits and rejected by none. The Secretary files this brief under Federal Rule of Appellate Procedure 29(a).

STATEMENT OF THE CASE

As part of their "exit strategy" from the business, members of Constellis's management group ("Sellers") decided in 2013 to form an ESOP to purchase all of their Constellis stock. Brundle I, 241 F. Supp. 3d 610, 615 (E.D. Va. 2017). ESOPs are pension plans "designed to invest primarily in" the stock of the participants' employer. 29 U.S.C. § 1107(d)(6)(A). Constellis retained defendant Wilmington Trust ("Wilmington") as the ESOP's independent trustee to review and approve any purchase of Constellis stock. Brundle I, 241 F. Supp. 2d at 616-17. As Constellis stock is not publicly traded, Wilmington hired Stout Risius Ross ("SRR") to appraise the stock. Id.

In its annual valuation of Constellis for management in January 2013, the McLean Group appraisers valued the voting stock at $1838.11 per share. Brundle I, 241 F. Supp. 3d at 619. For Wilmington, SRR appraised the stock as of December 2013 at $3865 to $4600 per share, with the median fair market value per share at $4232.50, which SRR rounded up to $4235. Id. at 621. Wilmington relied on SRR's valuation report and accepted the price of $4235 per share for 100% of Constellis's voting stock and agreed that the ESOP would pay an additional 10%-per-share "premium" to acquire control of Constellis. Id. at 619-22, 625.[1] The

[1] "'[T]he value of a controlling position in a corporation is worth more on a per share basis than a non-controlling interest.' . . . This enhanced value is termed a

Sellers retained shares of non-voting stock. App. Br. 12 n. 5. The management group that owned Constellis sold the ESOP 90% of the voting stock outright and gave the ESOP the remaining 10% in exchange for "equity-like" warrants entitling them to appoint a majority of the Board of Directors and to buy back equity in the future at a specified strike price. Id. at 615-16. The ESOP's financial stake in the company was also subject to provisions contemplating the issuance to Constellis management of Stock Appreciation Rights set at 7% of the equity value, as well as a cash bonus for key managers, set at 5% of the purchase price. Id. at 636. In December 2013, Wilmington paid a total of $201,529,032.77 for the stock (the "2013 Purchase"). Id. at 625. The funding for the transaction came from three sources: a cash contribution of more than $48 million from Constellis, amounting to 24% of the price; a loan from the Sellers for 69% of the price; and a loan from Constellis for 7% of the price. Id. at 616, 625.

In the transaction, the ESOP only received the power to appoint a single member of the five-member Board of Directors, in addition to the voting stock. Brundle I, 241 F. Supp. 3d at 626. The governing Plan document directed Wilmington to vote all shares in such manner as directed by the Constellis Board. Id. at 626-27. The Trust Agreement, another governing document, provided that

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control premium." City Nat'l Bank v. Am. Commonwealth Financial Corp., 801 F.2d 714, 715 n.1 (4th Cir. 1986).

Wilmington had to vote, tender, and exchange stock in the manner set forth in the Plan document to the extent consistent with ERISA. Id. at 627. Given these restrictions, Constellis's former counsel, when asked how the ESOP might stop an action by the Board if Wilmington felt it was inconsistent with ERISA, testified that Wilmington's only option would be to sue. Id.

Less than a year after the 2013 Purchase, the Board sold Constellis to Academi, a "strategic buyer," which was a competitor of Constellis in the private security market, for $288.3 million in July 2014 (the "2014 Sale"). Id. at 628-31. Although Academi initially proposed that the ESOP would receive no consideration because of "the significant amount of leverage outstanding" from the 2013 Purchase, Academi ultimately agreed to pay $20 million in cash to the ESOP in negotiations with Wilmington. Id. at 629. As a result of the 2014 Sale, the ESOP was terminated. Id. at 631.

In November 2015, participant Tim Brundle sued Wilmington, alleging that Wilmington engaged in a transaction prohibited by ERISA section 406(a), 29 U.S.C. § 1106(a), because the Plan overpaid for the stock by $103,862,000. Brundle I, 241 F. Supp. 3d at 613. Wilmington argued that the transaction, while prohibited, was subject to an exemption under ERISA section 408(e), 29 U.S.C. § 1108(e), which permits such transactions if the ESOP paid no more than "adequate consideration." Id. at 632-33. ERISA defines "adequate consideration" for stock

for which there is no "generally recognized market," such as the Constellis stock, as "the fair market value of the asset as determined in good faith by the trustee." 29 U.S.C. § 1002(18). As the district court held, whether a trustee has determined the fair market value in good faith is measured by the duty of the "prudent man standard of care," as set forth in 29 U.S.C. § 1104. Id. at 633. ERISA's fiduciary duties are the "highest known to the law," Tatum v. RJR Pension Inv. Committee, 761 F.3d 346, 355-56 (4th Cir. 2014), and require plan fiduciaries to adhere to a stringent standard of care when considering the views of experts, including appraisers. Brundle I, 241 F. Supp. 3d at 633-34.

After trial, the court found Wilmington liable for causing a non-exempt prohibited transaction because Wilmington had failed to meet its burden of proving that the ESOP paid no more than adequate consideration. In particular, it had failed, in multiple ways, to independently probe the gaps in SRR's valuation report to determine whether its conclusions were reasonably justified. Brundle I, 241 F. Supp. 3d at 634, 648-49. The court focused on the process Wilmington used and on whether Wilmington determined the value by a way of prudent investigation as measured by ERISA's exacting prudent man standard, the standard to which all ERISA fiduciaries must adhere, see 29 U.S.C. § 1104(a). Brundle I, 241 F. Supp. 3d at 632-33. After reviewing the evidence and assessing the credibility of experts

from both sides, the court decided that Wilmington failed to meet the statutory standard and caused the ESOP to overpay by $29,772,250. Id. at 613, 654, 658.

The court cited four major failures in Wilmington's conduct: (1) Wilmington neglected to consider the McLean report, which valued the stock as worth materially less than SRR's appraisal, id. at 619, 635; (2) Wilmington knew of red flags indicating that management's revenue projections might be inflated -- which inflated the stock value -- but did not closely question SRR's reliance on management's representations, id. at 636-38; (3) despite knowledge that the ESOP could not exercise any of the typical hallmarks of control, SRR failed to sufficiently explain why it added a control premium and Wilmington never probed why SRR added a control premium, id. at 625-27, 638-39; and (4) Wilmington failed to probe SRR's practice of regularly rounding numbers up, increasing Constellis's appraised value. Id. at 640. The court further noted "circumstantial evidence of Wilmington's neglect," and its tendency to rubberstamp SRR's valuations. Id. at 640-41, 643.

In reaching the loss figure, the court credited some but not all of the criticisms of SRR's valuation by Brundle's expert, Dana Messina. Brundle I, 241 F. Supp. 3d at 647. The court agreed that SRR should not have added a control premium, which alone inflated the purchase price by $8,186,000. Id. The court

concluded that overall, Wilmington's failures inflated the price by $29,773,250.00. Id. at 649-50.

Wilmington moved to amend the judgment, arguing that any damages from its breach were offset by the $20 million the ESOP received in the 2014 Sale. The court disagreed, noting that when calculating overpayments, courts "'generally' have 'estimate[d] the [fair market value] of the [company] stock at the time of [the] transaction and deduct[ed] it from the higher amount the ESOP actually paid'" and rejected offsets based on subsequent independent events. Brundle II, 258 F. Supp. 3d at 660 (citation omitted). The court held that the $20 million the ESOP obtained was an independent benefit and did not relieve Wilmington of liability for losses caused in the 2013 Purchase. Id.

SUMMARY OF ARGUMENT

Congress imposed high fiduciary standards on plan fiduciaries and also prohibited fiduciaries from engaging the plan in certain transactions with plan insiders that Congress recognized had inherently powerful incentives for abuse. Congress exempted certain transactions from these categorical bars if the transaction satisfied the terms of a statutory exemption.

It is undisputed that the Plan's purchase of employer stock from insiders was prohibited. Congress permitted that transaction, however, if the purchase price was no more than adequate consideration, defined as the fair market value

determined by fiduciaries after a prudent investigation. The fiduciaries bear a heavy burden to prove that the transaction meets that condition. The district court properly scrutinized Wilmington's conduct, the facts presented, and the credibility of witnesses to determine whether Wilmington satisfied its burden.

Wilmington attempts to evade this scrutiny with two flawed arguments. First, it argues that subjective intentions should affect the level of scrutiny. As well-established caselaw holds, a court's review of whether a fiduciary investigated the fair market value prudently is a review of the prudence of the fiduciary's objective conduct, not his subjective intentions. As the Fifth Circuit made clear, a court's review "is not a search for subjective good faith – a pure heart and an empty head are not enough." Cunningham, 716 F.2d at 1587.

Second, Wilmington argues that it hired an expert adviser and the district court should have deferred to the adviser's judgment, which Wilmington rubberstamped. The court correctly followed long-standing caselaw that calls for judicial scrutiny of fiduciary actions and holds that merely hiring an adviser cannot insulate fiduciaries from consequences of their decisions. A trustee must still understand and evaluate the advice given and exercise his own independent judgment, not blindly rely on what he's told. A court's thorough review protects the interests and rights of participants and ensures compliance with ERISA. As

hiring advisers for large transactions is commonplace, holding otherwise would shield trustees from liability and gut Congress's protections for participants.

The court correctly concluded that Wilmington should not have paid a control premium because the ESOP did not receive effective control of the company. The court weighed the facts and concluded that the ESOP did not receive any of the typical hallmarks of control despite holding 100% of the voting common stock shares. Based on its factual findings, the court properly held that the ESOP lacked any effective control, and thus a premium was unjustified.

The court correctly followed the universally accepted method of measuring the plan's losses when it overpays for assets: by subtracting the stock's actual fair market value from the higher price the ESOP paid. Wilmington attempts to diminish its overpayment by claiming that an amount the ESOP obtained in a subsequent independent transaction must offset those losses. Courts that have considered this issue in similar cases consistently and uniformly reject the application of an offset, because these subsequent transactions are independently conceived and executed; there is no reason in law or logic why a plan, like the ESOP here, cannot both receive a remedy for its losses and keep proceeds from other independent transactions.

ARGUMENT

I. The District Court Correctly Followed Long-Standing Caselaw When It Refused to Defer to Wilmington's Or Its Adviser's Determination Of Fair Market Value In Holding That Wilmington Violated ERISA

Fiduciaries must employ appropriate measures to investigate the merits of any plan investment and engage in a reasoned decision-making process consistent with that of a prudent man acting in a like capacity. Tatum, 761 F.3d at 355-56; 29 U.S.C. § 1104. When considering plan investments, fiduciaries must engage "at a minimum" in a scrupulous investigation of options to ensure that they act in the participants' best interest. Shay, 100 F.3d at 1489. In deciding to purchase Constellis stock, Wilmington was required to satisfy these fiduciary duties and comply with the statutory conditions that permit it to engage in this undisputed prohibited transaction.

ERISA section 406 imposes per se prohibitions on certain transactions that Congress considered rife with the potential for abuse, like those between a plan and its insiders, who ERISA refers to as "parties in interest." See 29 U.S.C. §§ 1106, 1002(14). As the Supreme Court has noted, "Congress enacted ERISA § 406(a)(1), which supplements the fiduciary's general duty of loyalty to the plan's beneficiaries, § 404(a), by categorically barring certain transactions deemed 'likely to injure the pension plan.'" Harris Trust & Sav. Bk. v. Salomon Smith Barney,

Inc., 530 U.S. 238, 241-42 (2000). Congress expressed concern that a company insider selling employer stock to the company's ESOP may be tempted to do so primarily for the employer's or shareholder's benefit, rather than for the benefit of participants and beneficiaries, and the price could be too high "so that plan assets might be drained off." H.R. Conf. Rep. No. 93-1280, at 5093 (1974). Accordingly, Congress expected "that all aspects of these transactions will be subject to special scrutiny by the Department of Labor and the Internal Revenue Service to ensure that they are primarily for the benefit of plan participants and beneficiaries." Id. (emphasis added); see also Shay, 100 F.3d at 1489-90.

Some transactions otherwise prohibited are exempt if they meet the conditions of an exemption in ERISA section 408, 29 U.S.C. § 1108, but the fiduciary bears the burden of proving that the transaction satisfies those conditions. Elmore v. Cone Mills Corp., 23 F.3d 855, 864 (4th Cir. 1994). "This burden is a heavy one." Shay, 100 F.3d at 1488. While Wilmington does not dispute that the 2013 Purchase was prohibited, it claims that it satisfied the exemption. Wilmington therefore has the burden to show that the ESOP purchased the stock for "adequate consideration," the condition for the exemption applicable to employer stock purchases, section 408(e). E.g., Cunningham, 716 F.2d at 1467-68.

"Adequate consideration" has two distinct requirements: the trustee must determine the value using a prudent process, and the stock must be purchased for

no more than fair market value. See, e.g., Hall Holding, 285 F.3d at 436-37; Keach v. U.S. Trust Co., 419 F.3d 626, 636-37 (7th Cir. 2005). When determining fair market value, fiduciaries "remain subject to the general [prudence] requirements of Section 404," with the "principal responsibility . . . to act with . . . care, skill, prudence, and diligence" in selecting investments. Cunningham, 716 F.2d at 1467.

To meet this exemption, it is long-established law that fiduciaries may not blindly rely on expert valuations in determining a fair market value; rather, they must conduct a prudent investigation and must independently scrutinize the valuations to make certain they are reasonably justified. See, e.g., Cunningham, 716 F.2d at 1462-63; Shay, 100 F.3d at 1490; Bussian, 223 F.3d at 300-01; Hall Holding, 285 F.3d at 435-37; Bruister, 823 F.3d at 262-64. Specifically, the fiduciaries must (1) investigate the expert's qualifications; (2) provide the expert with complete and accurate information; and (3) make certain that reliance on the expert's advice is reasonably justified under the circumstances. Hall Holding, 285 F.3d at 430. Courts must review the evidence to determine whether fiduciaries thoroughly and scrupulously reviewed expert valuations, as required, or relied on them unthinkingly. Shay, 100 F.3d at 1490; Bussian, 223 F.3d at 300-01; Hall Holding, 285 F.3d at 435-37.

In line with this well-established caselaw, the district court scrutinized Wilmington's actions, weighed the facts, and found that Wilmington did not meet its burden to satisfy the exemption. The court heard witnesses from both sides, including experts, and "focus[ed] on whether the process the trustee used to determine fair market value is consistent with professional norms and its ERISA fiduciary obligations." 241 F. Supp. 3d at 633.

Wilmington and amici ASA fault the district court for its thorough review of Wilmington's decision-making. First, Wilmington attempts to distinguish this well-established caselaw by suggesting that the trustee's intent affects the level of scrutiny applied by the court to these prohibited transactions, a distinction no circuit court has ever endorsed. Compare App. Br. 20 (referencing "bad faith, collusion, or the sorts of performance deficiencies that have led other courts to find prohibited transactions"); ASA Br. 7-8 with, e.g., Hall Holding, 285 F.3d at 442, n.12 (rejecting review based on subjective intent as against great weight of authority). To the contrary, Cunningham made clear that a court considering whether the fiduciary properly determined the fair market value reviews the prudence of the fiduciary's process, not whether he had good intentions. 716 F.2d at 1587; Hall Holding, 285 F.3d at 437.

Second, Wilmington misuses Cunningham to support its theory that the court was too intrusive in its scrutiny and should have simply accepted

Wilmington's reliance on SRR's judgment rather than "second-guessing [the] professional valuation judgments." See, e.g., App. Br. 18, 21. This argument turns Cunningham on its head, as Cunningham held that fiduciaries were required to compare the expert report with information at their disposal and rejected fiduciaries' uncritical reliance on expert opinions. 716 F.2d at 1474. Cunningham held that the fiduciaries did not undertake a prudent investigation because they failed to analyze the assumptions underlying the appraisal. 716 F.2d at 1474. The trustee is required to make "an honest, objective effort to read the valuation, understand it, and question the methods and assumptions that do not make sense." Shay, 100 F.3d 1484, 1491; Bussian, 223 F.3d at 301. An expert report is "a tool, and like all tools, is useful only if used properly." Shay, 100 F.3d at 1490.

The district court here followed long-standing caselaw, which makes clear that merely hiring an adviser does not lessen the court's scrutiny, because an adviser's opinion does not "whitewash" a fiduciary's own actions; as many courts, including Cunningham, have held, "an independent appraisal 'is not a magic wand that fiduciaries may simply wave over a transaction to ensure that their responsibilities are fulfilled.'" See, e.g., Shay, 100 F.3d at 1489-90 (quoting Cunningham, 716 F.2d at 1474). The fiduciary must still evaluate the advice given and "exercise his own judgment" about the transaction. Jenkins v. Yager, 444 F.3d 916, 927-28 (7th Cir. 2006). Expert advice may be a factor when the court

considers whether the fiduciary satisfied its duty, but it does not shield the fiduciary from judicial scrutiny. See Chesemore v. Alliance Holdings, Inc., 886 F. Supp. 2d 1007, 1041-42 (W.D. Wisc. 2012). It was, of course, prudent for Wilmington to hire an appraiser in connection with a transaction involving hundreds of millions of dollars. But its obligation of prudence did not stop with the hiring of the appraiser or permit it to give uncritical deference to the appraiser's opinion. Trustees routinely consult advisers in large transactions. If the mere presence of advisers in these transactions justified unthinking deference, every large transaction would be effectively insulated from judicial review and ERISA's protections for participants and beneficiaries eviscerated.

As the fiduciary, Wilmington – not its appraiser – was ultimately responsible for the determination of whether and at what price to proceed with the transaction. As the party responsible for expending more than $200 million in plan assets, it was expected to act "with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use," 29 U.S.C. § 1104(a)(1)(B), not merely defer to its appraiser's views.

Contrary to Wilmington's argument that the court should have unquestioningly accepted its reliance on SRR, Wilmington bears the burden to prove that its decision to enter into a prohibited transaction met the conditions of a

statutory exemption. <u>See</u> <u>Elmore</u>, 23 F.3d at 864. Applying ERISA's exacting fiduciary standards, the district court must analyze the fiduciary's decisions with scrutiny in order to protect the interests of participants and to ensure compliance with "broadly protective" statutory standards. <u>See</u>, <u>e.g.</u>, <u>Smith v. Sydnor</u>, 184 F.3d 356, 365 (4th Cir. 1999) (adjudication of ERISA violation involves interpretation and application of federal statute, which is within judiciary's, not fiduciary's, expertise); <u>John Hancock Mut. Life Ins. Co. v. Harris Tr. & Sav. Bank</u>, 510 U.S. 86, 96 (1993) ("To help fulfill ERISA's broadly protective purposes, Congress commodiously imposed fiduciary standards on persons whose actions affect the amount of benefits [] participants will receive."); <u>Kenny v. Quigg</u>, 820 F.2d 665, 671 (4th Cir. 1987) (reversing district court that was "unwilling to second-guess" independent fiduciary's valuation of employer stock for ESOP, because court had "an obligation to review the bases for [independent fiduciary's] determinations and recommendation"). Blindly deferring to an adviser's valuation as "fair market value" or "adequate consideration" eviscerates ERISA's prohibitions in areas where strong incentives for abuse and great risk to participants exist.

Wilmington's argument that the court must accept its actions since it relied on SRR infects its brief and ASA's brief. For example, they argue that the district court erred in its decision because it referenced the McLean Report, <u>see</u> App. Br. 27, it used Messina's projections instead of management's projections, <u>see</u> App. Br.

35, or it failed to identify violations of "any specific valuation standards," see App. Br. 22. Wilmington suggests that because SRR stated justifications for its lack of reference to the McLean report and its use of the management projections, and had abided by valuation standards, the court must endorse Wilmington's reliance on SRR's judgment.[2] Again, Wilmington's reliance on SRR does not insulate its own decisions and actions from judicial review; the court is not required to rubberstamp the adviser's valuation as Wilmington did, but must determine whether the trustee prudently and objectively "questioned the methods and assumptions that do not make sense." Shay, 100 F.3d at 1491. Indeed, Wilmington's own expert, Aziz El-Tahch, co-authored a pamphlet highlighting these duties. Brundle I, 241 F. Supp. 3d at 543. The court correctly focused on the trustee's overall efforts to analyze the merits of a $200 million investment, not its adviser's conduct or recommendations. The court appropriately reviewed the trustee's efforts by assessing the facts and weighing the witnesses' credibility. As with any case, this Court then reviews the district court's factual findings and credibility determinations under a "clear error"

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[2] Wilmington cites Cunningham and Eyler v. CIR, 88 F.3d 445 (7th Cir. 1996) to justify ignoring the McLean report, App. Br. 24, but those decisions are inapposite. They faulted a fiduciary for relying on an out-of-date or irrelevant valuation report after failing to question it. Those cases do not stand for the proposition that a fiduciary should ignore or discount all prior valuation reports, but instead require fiduciaries to investigate the relevance, if any, of similar valuations. Cunningham, 716 F.2d at 1469-73; Eyler, 88 F.3d at 454-56.

standard.[3] Hendricks v. Central Reserve Life Ins. Co., 39 F.3d 507, 513 (4th Cir. 1994).

Wilmington concedes that the court must analyze its efforts for "performance deficiencies" and whether the trustee's reliance on an adviser's recommendation is "reasonably justified." App. Br. 20-21. The court did exactly that, and after a trial it found Wilmington's performance severely deficient and its reliance on SRR's opinion unreasonable. These conclusions are perfectly consistent with the review courts should conduct for such transactions, as other

[3] ASA filed an amicus brief criticizing the qualifications of Messina. ASA Br. 10. Messina opined on the trustee's decision to rely on SRR's valuation, the errors in SRR's report rendering such reliance unreasonable, and on the losses caused by those errors. When Messina opined on Wilmington's breach and the loss, he testified as a "financial expert" familiar with the prudent process required for these transactions. Brundle I, 241 F. Supp. 2d at 621. Messina is the Chief Executive Officer of Kirkland Messina, a financial services firm, holds a MBA from the Harvard Business School, has 25 years of experience providing business valuations in ESOP transactions, Brundle I at 621, and was qualified under the relevant standard, Daubert v. Merrill Dow, Pharm, Inc., 509 U.S. 579 (1993); see also Dkt. 204 at 3-4 (noting he is "involved in the purchasing of businesses ranging from $1 million to $100 million"). Wilmington did not appeal Messina's qualification. Courts routinely accept similar financial experts and opinions. See, e.g., First Bankers Trust Services, Inc., No. 12-4450, 2015 WL 5722843, at *2 (D. N.J. Sept. 29, 2015); Henry v. Champlain, 388 F. Supp. 2d 202, 220 (W.D.N.Y. 2003); Perez v. Bruister, 54 F. Supp. 3d 629, 640 (S.D. Miss. 2014). Any concerns about qualified experts or their opinions should be raised in cross-examination. Expert testimony is not evaluated any differently in ESOP cases.

courts require.[4] Indeed, contrary to Wilmington's arguments, as a trustee responsible for a $200 million deal using other people's money, Wilmington, as a prudent investor, needed to look "in-the-weeds" at all aspects of the deal and a court must ensure the trustee fulfilled its duty. See, e.g., App. Br. 45.

II. The District Court Correctly Held That ERISA Prohibited The ESOP From Paying A Control Premium Without Obtaining Effective Control Of Constellis

ERISA prohibits an ESOP from paying more for control of a company than it actually receives. See 29 U.S.C. § 1108(e). This Court defined "control" as "an interest which allows the shareholder to 'unilaterally direct corporate action, select management, decide the amount of distribution, rearrange the corporation's capital structure, and decide whether to liquidate, merge, or sell assets.'" Estate of Godley v. C.I.R., 286 F.3d 210, 215 (4th Cir. 2002) (citation omitted); see also, e.g., Harline, 1992 WL 12151224, at *14; cf. IRS Chief Couns. Adv. 2009-06-012, 29 WL 2200222 (July 24, 2009) (control premium may be taken into account, provided that "[a]ctual control (both in form and in substance) is passed to the purchaser with the sale"). To meet the conditions of the section 408(e) exemption, Wilmington has the burden to prove that a control premium was justified. See,

[4] ASA contorts the caselaw to suggest that all other cases reviewed ESOP transactions only for "glaring defects," a standard found nowhere in ERISA or the relevant cases. ASA Br. 7.

e.g., Harline, 1992 WL 12151224, at *14. The district court found the control premium unwarranted because the ESOP did not, as a matter of fact, acquire effective control even though it acquired 100% of voting stock.

Wilmington argues that the ESOP had effective control because it became a 100% stockholder, and obtained rights, such as the ability to veto certain corporate actions by filing a shareholder derivative lawsuit against the Board. App. Br. 29 n.11, 30 ("recognize the ESOP's 100% ownership stake"), 31. But the court found that the ESOP was only given the power to appoint one of five Board members, was deprived of any mechanism to stop the designation of other members, and had no other powers to control the company's actions. Brundle I, 241 F. Supp. 3d at 626. The court determined that the ESOP's sole means of challenging corporate actions directed by the Sellers and their chosen Board was to file suit, as Constellis's former counsel admitted – the same right that any minority shareholder has. Id. at 626-27. The Plan document gave Wilmington no authority to countermand the Board's instructions when voting on a sale. Id., at 626-27. Accordingly, the court concluded that "the ESOP essentially had no power to control Constellis." Id. at 638-39.

The court found it "extremely unusual" for the selling shareholders to retain the right to appoint a majority of the Board even though the ESOP held 100% of the shares. Brundle I, 241 F. Supp. 3d at 638-39; cf. First Bankers Trust Services,

Inc., No. 12-4450, 2015 WL 5722843, at *14-17 (D. N.J. Sept. 29, 2015) (triable issue of fact as to whether control premium was fair, when alleging ESOP owned 100% of stock but ceded control of Board to selling shareholder). The court additionally found that the other parties to the transaction knew or had reason to know this structure was highly unusual. Brundle I, 241 F. Supp. 3d at 639. According to the district court, although the ESOP owned all the voting stock, the purchase transaction was structured to ensure that ultimate control over the company and its direction was retained by members of the Board selected by the Sellers. Id. at 639. Although Wilmington argues that its role in the Academi transaction demonstrates ESOP control, App. Br. 29-30, the court found as a matter of fact, that the ESOP merely negotiated its interests as a selling shareholder, not as the controlling owner. See App. Br. 31 n.13.

Because the district court found that the ESOP did not obtain rights accorded to a majority shareholder, the mere fact that the ESOP owned 100% of shares does not alone justify a control premium. The district court's analysis of the facts to discern whether the ESOP obtained actual control accords with a leading valuation text, which recognizes that the question of control is complex and requires fact-based analysis. See, e.g., Shannon P. Pratt, Valuing a Business: The Analysis and Appraisal of Closely Held Companies (5th ed. 2008) at 37-38, 65-66 ("Pratt"); e.g., Steiner Corp. v. Benninghoff, 5 F. Supp. 2d 1117 n.7 (D. Nev. 1998) (referring to

Pratt as "one of the leading reference sources in the valuation field"). The valuator must look closely at a number of factors, including elements of control, degree of control, aggregate interest purchased, and rights, obligations, and policies of the company, to decide if a control premium or a minority discount is appropriate. Pratt at 817-18, 1070 ("Control").

Based on its factual findings, the district court correctly held that because Wilmington did not identify any hallmark of effective control acquired by the ESOP, payment of a control premium was unwarranted even though it received 100% of the stock. Brundle I, 241 F. Supp. 3d at 639.

III. The District Court Correctly Held That Wilmington Was Not Entitled To Offset Its Liability For The Loss It Caused By The Amount The ESOP Received In The Later Sale Of The Company

Wilmington committed the ESOP to purchase stock for more than $201.5 million; in exchange, the ESOP should have received stock worth that amount, but instead received stock the court determined was worth less than $172 million. The nearly $30 million difference ($29,773,250.00) between the purchase price and the actual value of the stock is a proper measure of the ESOP's loss. Brundle I, 241 F. Supp. 3d at 649. The district court correctly determined the loss by subtracting the stock's fair market value at the purchase date from the higher price Wilmington caused the ESOP to pay. Id. at 645-49; Brundle II, 258 F. Supp. 3d at 661-62; accord Hall Holding, 285 F.3d at 444. "This is the approach generally used by

courts to compute overpayments" and determine losses. Bruister, 823 F.3d at 265 (citing cases). As the Restatement (Second) of Trusts § 205, cmt. e, states, "[i]f the trustee is authorized to purchase property for the trust, but in breach of trust he pays more than he should pay, he is chargeable with the amount he paid in excess of its value."

In exchange for the purchase price of $201,529.032.77, the ESOP should have received assets worth at least $201,529,032.77, but instead received assets worth almost $30 million less, meaning that it had $30 million less to use for the benefit of the plan and its participants than it should have had. The loss of the overpayment was fixed on the date of the 2013 Purchase, and as of that date, that amount was wholly unavailable for "other, more fruitful investments." Bruister, 823 F.3d at 271. The court rightly treated the amount of the overpayment as the measure of the Plan's losses.

Although the district court applied the standard overpayment measure in assessing losses, Wilmington nevertheless argues that its liability for the ESOP's losses should be offset by $20 million, because the ESOP subsequently received $20 million in the stock sale to Academi that resulted in the transfer of all the ESOP's interest to Academi and the termination of the ESOP. The argument is ill-founded.

The independent, post-transaction sale of the stock to Academi in no way remedied the Plan's overpayment at the time of the original transaction. Academi did not purchase the stock from the ESOP in settlement of the overpayment claim against Wilmington, nor did the Plan and its participants release any of their claims against Wilmington in connection with the 2013 Purchase. The ESOP's loss for the overpayment was fixed at the time of the 2013 Purchase and has never been remedied. Academi was simply purchasing the company for what it was worth to Academi at the time of the purchase, irrespective of whether the Plan had paid too much or too little for the stock in the prior transaction. If the Plan had paid $30 million less for the stock in 2013, or received $30 million more in other assets, it would potentially have been that much richer at the time of the subsequent stock purchase and ESOP termination. In no event, however, did the 2014 Sale remedy, or purport to remedy, the prior overpayment. Academi presumably acquired the stock for the price that it believed best reflected the value of the acquisition to Academi in 2014, regardless of whether the Plan had overpaid or underpaid in 2013.

Thus, the 2014 Sale in no way alters the loss that Wilmington caused when it overpaid for stock in the initial transaction or diminish the fact that the ESOP lost money in the first place. Brundle II, 258 F. Supp. 3d at 662. Had the ESOP paid what Constellis stock was worth in the initial transaction, the ESOP would have

been in a substantially better financial condition than it actually was when it received $20 million in the later stock sale to Academi. The 2014 Sale resulted in the termination of the ESOP (which was originally created to fund hundreds of millions of dollars in employee benefits), a cash payment of $20 million to the ESOP, and a wide variety of large direct and indirect benefits to other parties. Whether or not that transaction was fair or beneficial, on balance, to the Plan's participants is neither at issue in this case, nor relevant to fixing the Plan's losses in connection with the 2013 transaction that is at issue in this case.

Wilmington concedes the subsequent sale was an "arms-length" transaction with Academi and Wilmington, App. Br. 21, 29-30, separate and apart from the purchase transaction. Wilmington also appears not to challenge the many cases that have rejected arguments seeking to offset overpayment losses based on payments in subsequent independent transactions. E.g., Bruister, 823 F.3d at 270-1 (citing Chesemore v. Alliance Holdings, Inc., 948 F. Supp. 2d 928, 943 (W.D. Wisc. 2013)); Henry v. U.S. Trust Co., 569 F.3d 96, 98, 100 n.4 (2d Cir. 2009) (rejecting offsetting for transaction driven by subsequent "economic circumstances"); Neil v. Zell, 767 F. Supp. 2d 933, 941 (N.D. Ill. 2011)); see also Horn v. McQueen, 215 F. Supp. 2d 867, 889-90 (W.D. Ky. 2002).

Instead, Wilmington attempts to distinguish these cases in two ways. First, Wilmington cites to Henry where the Court allowed one offset based on a

subsequent transaction that the parties executed specifically to remedy the overpayment. App. Br. 56. As discussed above, however, here the 2014 Sale was wholly independent of the overpayment in the 2013 Purchase, and was in no way designed to remedy the overpayment. Moreover, Henry, consistent with other courts, expressly disallowed another offset that was independent of the overpayment transaction and driven by subsequent economic circumstances. 569 F.3d at 97. The facts of this case are directly analogous to the disallowed offset in Henry. Accordingly, Wilmington's reliance on Henry fails.

Second, Wilmington argues that the cases precluding such offsets are distinguishable because they involved debt forgiveness and not cash. App. Br. 55. While the facts may be different, the underlying principle in the two lines of cases remains the same – an independent transaction should not offset the losses from the overpayment. Because the subsequent transaction was independent of the overpayment, occurred without reference to the overpayment, and was not used to remedy the overpayment, the district court, consistent with the unanimous caselaw, did not find any valid basis to retrospectively offset losses with proceeds from a completely separate and independent transaction, like the 2014 Sale.

CONCLUSION

The Secretary asks this Court to affirm the district court's conclusions with respect to the questions presented.

Respectfully Submitted,

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Dated: July 23, 2018

/s/ Robin Springberg Parry
Senior Trial Attorney

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I hereby certify that on this 23rd day of July, 2018, I caused this Brief of Amicus Curiae in Support of Appellee to be filed electronically with the Clerk of the Court using the CM/ECF System, which will send notice of such filing to registered CM/ECF users.

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