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Margo Eberlein  
*St. John's University School of Law*

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RECOVERING RETIREMENT SECURITY: AN ANALYSIS OF  
THE LOCKDOWN CLAIMS UNDER ERISA, AS  
ILLUSTRATED BY THE ENRON LITIGATION

MARGO EBERLEIN\*

INTRODUCTION

On December 2, 2001, Enron Corporation (“Enron”) filed for bankruptcy after “the biggest, fastest corporate collapse in American history.”<sup>1</sup> Prior to the bankruptcy, many of Enron’s employees already had lost considerable amounts of money as participants in the Enron 401(k) Savings Plan (the “401(k) Plan”) during the decline in the value of both the 401(k) Plan and in their personal accounts specifically, which were heavily invested in Enron stock.<sup>2</sup> Because of a period of time when changes in the investment allocation of the 401(k) Plan were prohibited, the participants were unable to move their retirement investments out of Enron stock while its value rapidly declined.<sup>3</sup>

A class action was filed in the Southern District of Texas under the Employee Retirement Income Security Act (“ERISA”)<sup>4</sup> on behalf of the Enron employees who were participants in or beneficiaries of the 401(k) Plan (the “Plaintiffs”).<sup>5</sup> Filed on April 8, 2002, *Tittle v. Enron, Corp.*<sup>6</sup> (the “Complaint”) includes allegations that the Enron Corporation; the Administrative Committee in charge of the 401(k) Plan;<sup>7</sup> top executives, such as Kenneth Lay (“Lay”) and Jeffrey Skill-

\* J.D., St. John’s University School of Law, 2004; Cornell University, School of Industrial and Labor Relations, 2001.

1. Kurt Eichenwald, *Enron’s Many Strands: The Company Unravels; Enron Buffed Image to a Shine Even as It Rotted From Within*, N.Y. TIMES, Feb. 10, 2002, at A1.

2. See Michael A. Hiltzik & E. Scott Reckard, *The Enron Inquiry: Enron Chairman Urged Employees to Buy Stock*, L.A. TIMES, Jan. 19, 2002, at A1.

3. See *id.* This period of time is referred to as a lockdown; see also Part I, *infra*.

4. 29 U.S.C. §§ 1001 *et seq.* (2000).

5. See Keller Rohrback L.L.P., *The Case*, at <http://www.enronerisa.com/case.html> (last visited Feb. 1, 2004).

6. See generally First Am. and Consolidated Compl., *Tittle v. Enron Corp.*, No. H-01-3913 (S.D. Tex. Apr. 8, 2002), available at <http://www.enronerisa.com/complaint.html>.

7. Enron assigned the general administration of the 401(k) Plan to the Administrative Committee. The Committee was designated both the plan administrator and the named fiduci-

ing (“Skilling”); and the Northern Trust Company (the 401(k) Plan’s previous plan administrator) breached fiduciary duties under ERISA by misrepresenting Enron’s financial status and encouraging employees to invest their retirement funds in Enron stock.<sup>8</sup> The suit also alleges that the Defendants continued with their earlier decision to prohibit participants from changing the investment allocation of their 401(k) plans (a “lockdown”), despite reconsideration and the decreasing value of Enron stock.<sup>9</sup> This Note will focus on the second allegation; specifically, did the Administrative Committee breach a fiduciary duty under ERISA by deciding not to postpone the lockdown of the Enron 401(k) Plan?

Unfortunately, the Enron lockdown situation is not unique. Similar circumstances involving lockdowns have occurred recently in corporations such as Lucent,<sup>10</sup> International Paper,<sup>11</sup> and Global Crossing.<sup>12</sup> Because of the huge potential for loss, as demonstrated by Enron and other corporations, the issues that arise from lockdown periods must be explored, especially the possibility of relief for participant employees who may lose much of their 401(k) retirement savings during a lockdown. Part I of this Note provides background information on 401(k) plans and lockdowns. Part II describes the situation surrounding Enron and its lockdown to illustrate implica-

ary. See ENRON CORP., ENRON CORP. SAVINGS PLAN, XIII.1 Administration of the Plan: Appointment of Committee, as amended and restated July 1, 1999.

8. See generally First Am. and Consolidated Compl., *supra* note 6.

9. See *id.* This Note will focus solely on the actions and liability of the Administrative Committee because it is the entity that made the decision not to postpone the lockdown. This Note will not discuss the potential liability of the Enron Corporation or top executives, who may possibly be liable for failing to monitor the Administrative Committee or as co-fiduciaries of the Administrative Committee. Moreover, this Note will not discuss Northern Trust Company’s potential liability.

10. See Dennis K. Berman, *Accounting for Enron: All Tied Up: Retirement-Plan Lockdowns at Lucent and Elsewhere Draw Questions*, WALL ST. J., Jan. 21, 2002, at C14. Lucent locked down its 401(k) plan on September 28, 2000, for fifteen days to allow its plan administrator, Fidelity Investments, to “balance the assets” of the plan when Lucent spun off its business communications division Avaya Inc. During the lockdown the value of the shares dropped 19% from \$27.01 to \$21.81. See *id.*

11. See Ellen E. Schultz, ‘Lockdowns’ of 401(k) Plans Draw Scrutiny: Enron Employees’ Losses Suddenly Put Practice in Spotlight, WALL ST. J., Jan. 16, 2002, at C1. International Paper, Inc. locked down its 401(k) plan on November 30, 1999, until January 31, 2000. Forty-three percent of the plan’s assets were invested in company stock. During the lockdown the value of the company’s stock fell 9% to \$47.63. See *id.*

12. See Dennis K. Berman, *Global Crossing Curbed Sales of Staffers’ Shares*, WALL ST. J., Jan. 31, 2002, at A3. Global Crossing locked down its 401(k) plan from December 14, 2001 to January 18, 2002 while it switched plan administrators from Putnam Investments to Fidelity Investments. During the lockdown the value of the company stock dropped 19% from sixty-seven cents to fifty-four cents. See *id.*

tions of the current state of 401(k) regulation. Part III discusses the duties imposed by ERISA, the statute that governs 401(k) plans, as well as the attempts to increase protections for employee participants through changes in the law implemented after the collapse of Enron. Part IV outlines the lockdown claim presented in the Tittle complaint, and finally, Part IV predicts the potential for participant success in lockdown litigation generally, as well as for the Plaintiffs in the Tittle litigation specifically.

### I. 401(K) PLANS AND LOCKDOWNS

In a qualified retirement plan such as a 401(k) plan, both the employee and the employer (on behalf of the employee) make contributions to the participant's individual 401(k) account.<sup>13</sup> These plans offer participants a range of alternative investments to which they may allocate their funds. The funds are held in a trust and accumulate for the benefit of the participants,<sup>14</sup> enabling the employee to save for his or her eventual retirement.<sup>15</sup> 401(k) plans also offer favorable tax consequences to both employers and employees. When an employer makes a contribution to the plan, it receives a deduction for the amount contributed, and the employee does not record any income until the funds are ultimately distributed.<sup>16</sup>

The popularity of 401(k) plans has increased in recent years because the plans provide an opportunity for the employer to offer valuable retirement benefits to employees at a low cost to the employer.<sup>17</sup> Additionally, the portability of 401(k) plans further increases their popularity; when employees switch employers they may carry their 401(k) plan to the new workplace.<sup>18</sup> In 2000, 401(k) plans had

13. See 1 MICHAEL J. CANAN, *QUALIFIED RETIREMENT AND OTHER EMPLOYEE BENEFIT PLANS* § 3.1 (Practitioner ed. 1997).

14. See *id.*

15. See *id.* Normally these funds are distributed to the participant upon retirement. However, the funds may also be distributed to employee participants upon termination of service with the employer. Additionally, the funds may be distributed as a lump sum payment or in installments over the participants' lifetimes depending upon the provisions in a particular plan. See *id.*

16. See *id.* at § 3.1(A).

17. See Donald C. Dahlgren & Paul J. Dauenhauer, *Business Clients: Pensions*, in 2 *LEGAL COMPLIANCE CHECKUPS: BUSINESS CLIENTS* § 16:19 (Robert B. Hughes ed., 2001). Employers have low costs because employees in 401(k) plans fund the plan contributions with reductions in salary, while employees receive the benefit of pre-tax retirement savings. See *id.*

18. See *401(k) Breeds Mobile Work force*, *AUGUSTA CHRON.*, Jan. 28, 2002 (stating that "[t]he portability of 401(k) . . . plans is one of the most favorable features," and "workers can

nearly forty-two million participants<sup>19</sup> and almost \$2 trillion in assets.<sup>20</sup> About one-third of all pension plans are 401(k) plans, which cover approximately 45% of active participants.<sup>21</sup>

Most public companies offer their own stock as an alternative for investment in their 401(k) plans. On average, 40% of the 401(k) plan assets in Fortune 50 corporations are invested in company stock.<sup>22</sup> Employers will often match employees' contributions to their 401(k) plans, and 49% of companies with an employer stock fund mandate that these matches be made with the company's stock.<sup>23</sup> Meanwhile, because the amount of plan assets that may be allocated to employer stock is not restricted in defined contribution plans such as 401(k) plans,<sup>24</sup> there is often a high concentration of plan assets in company stock for this type of pension plan.<sup>25</sup>

Generally participants of a 401(k) plan may freely change the allocation of funds in their accounts.<sup>26</sup> However, when a company changes plan administrators or when a structural change to a 401(k) plan occurs, such as a shift from daily to monthly valuation, a period of time is necessary where participants are prevented from moving their savings among funds in their 401(k) accounts.<sup>27</sup> This period of

move from one job to another without fear of losing their retirement nest eggs"), available at [http://www.augustachronicle.com/stories/012802/bus\\_124-4597.shtml](http://www.augustachronicle.com/stories/012802/bus_124-4597.shtml).

19. See INVESTMENT COMPANY INSTITUTE, 401(K) PLAN PARTICIPANTS: CHARACTERISTICS, CONTRIBUTIONS, AND ACCOUNT ACTIVITY (Spring 2000).

20. See *id.*; see also News Release, Employee Benefits Research Inst., Retirement Data Available to Media (May 2, 2001), at <http://www.ebri.org/prrel/pr562.htm>.

21. See U.S. DEP'T OF LABOR, HIGHLIGHTS FROM FORM 5500 REPORTS, available at <http://www.dol.gov/>.

22. See Bureau of Nat'l Affairs, *Some 401(k) Assets in Company Stock at Higher Level than Enron, Report Says*, 29 PENSION & BENEFITS REP. (BNA) No. 13, Mar. 26, 2002, at 965. A Democratic Policy Committee Report revealed that, of Fortune 50 corporations, "55% of the corporations' plan assets were at least 30% invested in company stock; 38% of the corporations' plan assets were at least 50% invested in company stock; 17% of the corporations' plan assets were at least 70% invested in company stock; and 30% of the plan assets had a higher concentration of company stock than Enron did in 2001." See *id.*

23. See *id.*

24. See *How Sound is Your Retirement Plan?: Lessons From Enron*, FLA. EMP. L. LETTER, May 2002, at 2. In defined benefit plans, an alternative type of pension plan, ERISA requires that no more than 10% of plan assets be allocated to employer stock. See *id.*

25. This high concentration is not unique to Enron. Approximately 95% of Proctor & Gamble's 401(k) is allocated to employer stock, while Coca-Cola's plan is 81% invested in employer stock, and 74% of McDonald's plan is allocated in employer stock. See *id.*

26. See Laura Bruce, *The Push to Reform 401(k) Plans* (Jan. 29, 2002), at <http://www.bankrate.com/brm/news/sav/20020129a.asp?prodtype=grn>. Defined contribution plans like 401(k) plans offer employees control over when to buy or sell most of their plan investments. See *id.*

27. See Schultz, *supra* note 11.

time is commonly referred to as a lockdown.<sup>28</sup> Also called blackouts or quiet periods, these phases occur with great frequency and are both legal and routine.<sup>29</sup> On any given day, ninety-six out of 350,000 company plans that have 401(k) plans are locked down.<sup>30</sup> Secretary of Labor Elaine Chao described lockdowns as follows:

Blackout periods routinely occur when plans change service providers or when companies merge. Such periods are intended to ensure that account balance and participant information are transferred accurately. Blackout periods will vary in length depending on the condition of the records, the size of the plan, and number of investment options. While there are no specific ERISA rules governing blackout periods, plan fiduciaries are obliged to be prudent in designing and implementing blackout periods affecting plan investments.<sup>31</sup>

A total of 74% of 401(k) plans have had lockdown periods.<sup>32</sup> While the entire lockdown transition lasts an average of three or four weeks,<sup>33</sup> the length of lockdown periods ranges from one day to two months.<sup>34</sup> However, the actual transfer of assets between plan administrators takes between twenty-four and seventy-two hours in situations where a lockdown is imposed because of a change in plan administrators.<sup>35</sup>

## II. THE ENRON SCANDAL

Of 21,000 Enron employees, 12,200 participated in the Corporation's 401(k) Plan.<sup>36</sup> Although various options existed for investment,

28. See Berman, *supra* note 10; see also Schultz, *supra* note 11.

29. See Schultz, *supra* note 11.

30. See Berman, *supra* note 10.

31. Maureen Minehan, *Congress, Administration Scrutinize 401(k) Blackout Periods*, 6 COMPENSATION & BENEFITS UPDATE 5 (2002).

32. See Dallas L. Slaisbury et al., EMPLOYEE BENEFITS RESEARCH INST. ISSUE BRIEF NO. 222, *Retirement Confidence Survey 2000* (June 2000) [hereinafter EBRI BRIEF].

33. See Press Release, Am. Soc'y of Pension Admin'rs, *ASPA Releases Results on Lockdown Survey: Lockdown Restrictions Hurt Small Business Retirement Plans* (Feb. 8, 2002), available at [www.aspa.org](http://www.aspa.org). The ASPA received survey responses from retirement plan administrators of 250 firms administering more than 85,000 retirement plans regarding lockdown experiences; the firms were mostly small businesses. See *id.*

34. See EBRI BRIEF, *supra* note 32.

35. See Claire Mencke, *401(k) Sponsors: Go Slow on Reform, Stock Caps Are Resisted*, INVESTOR'S BUS. DAILY, Feb. 26, 2002, at A-11.

36. See *Enron Ex-workers Forlornly View Rubble*, N.H. SUN. NEWS, Dec. 16, 2001, available at <http://www.enronerisa.com/news/news121601.html>; see also Peter Behr & April Witt, *Concerns Grow Amid Conflicts: Officials Seek to Limit Probe, Fallout of Details*, WASH. POST, July 30, 2002, at A1.

most employees allocated much of their money to Enron stock.<sup>37</sup> Additionally, all of Enron's matching contributions were made in the form of Enron stock, which could not be traded or sold until the employee reached age fifty.<sup>38</sup> As a result, prior to the lockdown of the 401(k) Plan, approximately \$1.3 billion (more than two-thirds of the \$2.1 billion fund) was invested in Enron stock.<sup>39</sup>

From October 29, 2001 until November 12, 2001, Enron locked down the 401(k) Plan,<sup>40</sup> preventing employees from changing the allocation of their pension plan funds in that time period. During the lockdown, the stock price dropped 28% from \$13.81 per share to \$9.98 per share.<sup>41</sup> By December 2, 2001, when Enron filed for bankruptcy, the stock price was less than \$1 per share,<sup>42</sup> and the 401(k) plan had lost an estimated \$1.3 billion.<sup>43</sup>

The cause of the Corporation's collapse centers around questionable accounting practices it utilized to report a series of its transactions.<sup>44</sup> Enron manipulated its quarterly and annual financial statements filed with the Securities and Exchange Commission (the "SEC") in order to hide the true nature of the transactions.<sup>45</sup> Meanwhile, starting in 2000, these manipulated transactions provided most of Enron's profits.<sup>46</sup>

The CEO and seventeen officers and directors of Enron signed financial statements that hid the transactions for the year 2000, "declaring [the financial statements] to be a true picture on which inves-

37. See *Enron Ex-workers Forlornly View Rubble*, *supra* note 36.

38. ENRON CORP., ENRON CORP. SAVINGS PLAN, V.16(b) Investment of Accounts: Investment of Company Contribution Accounts, as amended and restated July 1, 1999.

39. See *Enron Ex-workers Forlornly View Rubble*, *supra* note 36. A Democratic Policy Committee Report revealed that nearly one-third of Fortune 50 corporations' 401(k) plans have higher concentrations of employer stock than Enron did last year. See *Some 401(k) Assets in Company Stock at Higher Level than Enron, Report Says*, *supra* note 22.

40. See Albert B. Crenshaw, *Retirees, Workers Assail Enron on 401(k) Freeze; Witnesses Challenge Firm on Length of Halt in Stock Trading*, WASH. POST, Dec. 19, 2001, at E12. These are the dates that Enron maintains the lockdown spanned. However, some dispute exists as to these dates. See *infra* text accompanying notes 63-65.

41. See April Witt & Peter Behr, *Losses, Conflicts Threaten Survival: CFO Fastow Ousted In Probe of Profits*, WASH. POST, July 31, 2002, at E12. These statistics track the dates that Enron maintains the lockdown occurred.

42. See Thomas A. Fogarty, *Enron Officials Discussed Delaying 401(k) Revamp*, USA TODAY, Feb. 5, 2002, at 3B.

43. See C. William Thomas, *The Rise and Fall of Enron: When a Company Looks Too Good To Be True, it Usually Is*, J. ACCOUNTANCY, Apr. 2002, at 41.

44. See *id.*

45. See *id.*

46. See *id.*

tors could rely.”<sup>47</sup> However, Enron’s board members did not carefully monitor the partnerships that occurred during this year as well as prior years—a Senate subcommittee later concluded that they had repeatedly failed to ask pointed questions.<sup>48</sup>

There is evidence that many at Enron were aware of the reporting omissions as well as the precarious financial condition of the Corporation. For example, an in-house lawyer reviewed the questionable transactions in a legal risk memo and concluded that the transactions “might lead one to believe that the financial books at Enron are being manipulated.”<sup>49</sup> At the behest of his superiors, he redrafted the memo to state that he did not know whether the transactions had been manipulated, but feared that this was the case.<sup>50</sup>

But perhaps the most famous example that illustrates the Enron executives’ awareness of the Corporation’s financial condition is the anonymous letter written by Vice President Sherron Watkins to Kenneth Lay on August 15, 2001, the day following Chief Executive Officer Jeffrey Skilling’s resignation.<sup>51</sup> Referring to the disclosure methods used in the transactions, Watkins stated that she was “incredibly nervous that [Enron] will implode in a wave of accounting scandals. Skilling’s abrupt departure will raise suspicions of accounting improprieties and valuation issues. Enron has been very aggressive in its accounting.”<sup>52</sup> This memo demonstrates that top Enron officials were aware of the Corporation’s gross overstatement of earnings and the questionable deals prior to the lockdown of the 401(k) Plan.<sup>53</sup>

Watkins requested a transfer because of her discomfort with these financial practices and was moved to Enron’s human resources department in August.<sup>54</sup> Prior to her meeting with Kenneth Lay, she discussed the allegations in her memo with Cindy Olson, the Executive Vice President of Human Resources and Community Relations

47. *Id.*

48. *See id.*

49. April Witt & Peter Behr, *Dream Job Turns Into a Nightmare: Skilling’s Success Came at High Price*, WASH. POST, July 29, 2002, at A1.

50. *See id.*

51. *See id.*

52. *Id.*; *see also* Thomas, *supra* note 43, at 7.

53. *Seven-page Memo Warned of Enron’s Collapse*, DALLAS MORNING NEWS, Jan. 17, 2002, available at <http://enronerisa.com/news/news011702.html>.

54. *See Retirement Insecurity: 401(k) Crisis at Enron: Hearings Before the Governmental Affairs Comm.*, 107 Cong. 241 (Feb. 5, 2002) [hereinafter *Hearings*] (statement of Cindy Olson, Executive Vice President of Human Resources and Community Relations, Enron).



and a member of the Administrative Committee.<sup>55</sup> Olson then discussed Watson's allegations with Mr. McMahon (the Chief Operating Officer), several other human resources vice presidents at Enron, and Cynthia Barrow (the Senior Director of Benefits), but maintains that she did not inform the rest of the Administrative Committee because she felt that the allegations were hearsay due to the anonymous nature of the memo.<sup>56</sup>

On October 16, 2001, Enron reported a quarterly loss of \$1 billion, characterized the loss as "one-time," and stated that the Corporation was "very confident in [its] strong earnings outlook."<sup>57</sup> On October 22, 2001, Enron announced the beginning of an SEC investigation into its reporting techniques.<sup>58</sup>

On October 29, 2001, Enron imposed the lockdown of its 401(k) Plan in order to change plan administrators from the Northern Trust Company to Hewitt Associates.<sup>59</sup> The Corporation began the search for a new benefits administrator in January 2001, and Enron selected Hewitt in May 2001.<sup>60</sup> About three weeks prior to the lockdown, Enron mailed a brochure to all participants that explained the transition period and outlined its timeframe.<sup>61</sup> Additionally, all Enron employees with e-mail accounts received further reminders in the days preceding the lockdown.<sup>62</sup> Although disagreement exists regarding the exact days the lockdown began and ended, Enron maintains that the lockdown began on the morning of October 29, 2001, and that November 12, 2001 was the last day participants could not make changes to their accounts.<sup>63</sup> During this period Enron's stock price dropped from \$13.81 to \$9.98, or 28%.<sup>64</sup> However, a panel of Enron workers and retirees testified in front of the Senate Commerce Committee that the freeze began on October 17, and several retirees stated they were unable to sell for one month or more.<sup>65</sup>

55. *See id.* at 231, 239 (statement of Cindy Olson).

56. *See id.* at 241-42, 258-59 (statement of Cindy Olson).

57. Witt & Behr, *supra* note 41, at A1; *see also* Thomas, *supra* note 43, at 7.

58. *See* Witt & Behr, *supra* note 41.

59. *See* Minehan, *supra* note 31.

60. *See Hearings, supra* note 54, at 232 (statement of Mikie Rath, Benefits Manager, Enron).

61. *See id.* at 232.

62. *See id.*

63. *See* Crenshaw, *supra* note 40.

64. *See* Witt & Behr, *supra* note 41.

65. *See Crenshaw, supra* note 40. The employees testified before the Senate Committee on December 18, 2001.

Mikie Rath, benefits manager and a member of the Administrative Committee, stated that the Administrative Committee considered postponing the lockdown, but did not because it was not feasible to notify the 20,000 participants in a timely fashion.<sup>66</sup> Also, Rath said that “[a]s the Enron news continued to break . . . the [A]dministrative [C]ommittee again considered stopping the transaction.”<sup>67</sup> Cindy Olson stated that on the advice of counsel and despite concerns to the contrary, that the Committee made the decision to go ahead with the lockdown as planned.<sup>68</sup>

In fact, on October 25, 2001, Enron contacted both Hewitt and Northern Trust to consider delaying the lockdown or halting it altogether.<sup>69</sup> However, later that day both companies were informed that no schedule changes regarding the lockdown would occur.<sup>70</sup>

In a November 8, 2001 report to shareholders and the SEC (issued during the lockdown period), Enron admitted to violating accounting rules in its accounting methods.<sup>71</sup> The Corporation restated its financial statements from 1997 to 2001 to reflect transactions that had been omitted, showing a loss of approximately \$600 million over four years.<sup>72</sup> By November 30, 2001, Enron’s stock price was valued at twenty-six cents per share.<sup>73</sup> Ultimately, Enron filed for bankruptcy on December 2, 2001.<sup>74</sup> In total, the 401(k) Plan had lost an estimated \$1.3 billion during the decline of Enron stock from more than \$80 in January 2001 to less than \$1 when the firm filed for bankruptcy in December 2001.<sup>75</sup>

### III. FIDUCIARY DUTIES IMPOSED BY ERISA

ERISA has no statutory language relating specifically to lockdowns.<sup>76</sup> Therefore, in analyzing lockdown claims generally, and the

66. See *Hearings*, *supra* note 54, at 232, 246 (statement of Mikie Rath).

67. See *id.*

68. See *id.* at 250–51 (statement of Cindy Olson).

69. See *id.* at 236 (statement of Catheryn Graham, Hewitt Associates); see also *id.* at 234 (statement of Joseph Szathmary, Associate, Northern Trust Retirement Consulting).

70. See *id.* at 236 (statement of Catheryn Graham); see also *id.* at 234 (statement of Joseph Szathmary).

71. See Peter Behr & April Witt, *Hidden Debts, Deals Scuttle Last Chance*, WASH. POST, Aug. 1, 2002, at A1.

72. See Thomas, *supra* note 43.

73. See *id.*

74. See *id.*

75. See Fogarty, *supra* note 42.

76. See generally 29 U.S.C. §§ 1001 *et seq.*; Minehan, *supra* note 31.

claims alleged in the Tittle complaint specifically, an application of the general fiduciary standards of ERISA is necessary. The fiduciary duties of ERISA pertinent to these issues include the duties of prudence and loyalty.<sup>77</sup>

In enacting ERISA, Congress declared that “it is desirable in the interests of employees and their beneficiaries . . . that disclosure be made and safeguards be provided with respect to the establishment, operation, and administration” of pension plans, such as 401(k) plans.<sup>78</sup> Therefore, Congress required “the disclosure and reporting to participants . . . in employee benefit plans and their beneficiaries . . . of financial and other information with respect thereto,” and protected participants’ interests “by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and by providing appropriate remedies, sanctions, and ready access to the Federal courts.”<sup>79</sup>

Under ERISA, a person is a fiduciary of a plan when:

- (1) 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;
- (2) 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
- (3) he has any discretionary authority or discretionary responsibility in the administration of such plan.<sup>80</sup>

“This ‘functional’ definition of a fiduciary is extraordinarily broad,” and, therefore, the fiduciaries of a 401(k) plan may include trustees, all individuals with discretionary authority who are active in the plan’s administration, members of the plan’s investment committee, investment advisers, and those who select these individuals.<sup>81</sup> Additionally, anyone specifically designated to carry out fiduciary responsibilities under a 401(k) plan is included as a fiduciary.<sup>82</sup>

77. See 29 U.S.C. § 1104(a) (2000).

78. 29 U.S.C. § 1001(a) (2000).

79. 29 U.S.C. § 1001(b) (2000).

80. 29 U.S.C. § 1002(21)(A) (2000).

81. See Joseph R. Simone & Glenn E. Butash, *Understanding Erisa 2001: An Introduction to Basic Employee Retirement Benefits, Fiduciary Responsibility and Prohibited Transactions Under ERISA*, PLI ORDER No. J0-0042, \*682–83 (2001).

82. 29 U.S.C. § 1105(c)(1)(B) (2000).

“ERISA generally adopts, codifies[,] and expands the common law of trusts in defining the duties of a fiduciary.”<sup>83</sup> Under ERISA, fiduciaries owe participants the duties of prudence and loyalty.<sup>84</sup> ERISA also imposes other fiduciary duties that are irrelevant to the lockdown claims considered in this Note.<sup>85</sup>

The duty of prudence requires that fiduciaries 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 in the conduct of” a similar enterprise.<sup>86</sup> Additionally, the duty of loyalty requires that fiduciaries discharge their duties solely in the interests of participants, for the exclusive purpose of providing benefits to participants.<sup>87</sup>

Some basic fiduciary responsibilities related to lockdowns can be inferred from the duties of prudence and loyalty. First, it is both prudent and loyal for a fiduciary to give advance notice of a lockdown period to plan participants. Additionally, a fiduciary should avoid implementing a lockdown when fluctuations in the value plan alternatives are likely because participants will not be able to change the allocation of their investment in response to the fluctuations. Thus, fiduciaries may violate the duties of prudence and loyalty by failing to adequately notify participants of a lockdown, and by poorly scheduling a lockdown period.

Under ERISA, a fiduciary who breaches the duties imposed by the statute may be personally liable for any loss incurred as a result of the breach.<sup>88</sup> The remedies include equitable and remedial relief such

83. See Simone & Butash, *supra* note 81, at \*684.

84. See *id.*

85. Fiduciaries also have a duty to act in accordance with plan documents. See *id.* Fiduciaries also have a duty to diversify the investments in the plan to minimize the risk of large losses. See 29 U.S.C. § 1104(a)(1)(C) (2000). A fiduciary that delegates any responsibilities to another fiduciary must not only monitor the other’s conduct, but also must terminate the delegation of responsibility if necessary. See Simone & Butash, *supra* note 81, at \*685. Finally, a fiduciary may be liable for a breach of duty by another fiduciary if he participates knowingly in, or undertakes to conceal an act or omission of the other fiduciary, if by failure to carry out his responsibilities under ERISA he enables another fiduciary to commit a breach, or if he has knowledge of a breach by such other fiduciary, unless he makes reasonable efforts under the circumstances to remedy the breach. See 29 U.S.C. § 1105(a) (2000).

86. 29 U.S.C. § 1104(a)(1)(B) (2000).

87. See 29 U.S.C. § 1104(a)(1)(A)(i) (2000); see also Simone & Butash, *supra* note 81, at \*685.

88. See Simone & Butash, *supra* note 81, at \*697.

as injunctions, removal, attorney's fees, and interest.<sup>89</sup> Punitive damages are generally not recoverable under the statute.<sup>90</sup>

Some recent legislative changes enacted after Enron's collapse affect the current regulation of 401(k) plans. Although Congress has failed to pass legislation specific to 401(k) plans,<sup>91</sup> on July 30, 2002, President Bush signed the Sarbanes-Oxley Act into law.<sup>92</sup> This corporate accountability law granted the Department of Labor the power to create regulations requiring thirty days of advance notice to participants before a lockdown begins.<sup>93</sup> The thirty-day notice is the only 401(k) reform that Republicans and Democrats could agree upon.<sup>94</sup> While this legislation and the rules promulgated there represent progress for the protection of employee participants in 401(k) plans, this notice to participants of impending lockdowns mandated by the new regulations was already required by ERISA's duties of prudence and loyalty.<sup>95</sup>

89. *See id.*

90. *See id.*

91. Leigh Strope, *Workers to get 30-day Notice of 401(k) Lockout Periods*, S. FLA. SUN-SENTINEL, Oct. 21, 2002.

92. William Baue, *The Strengths and Inadequacies of the Sarbanes-Oxley Act*, Sept. 27, 2002, at <http://www.socialfunds.com/news/article.cgi/article936.html>. Section 306(b)(1) of the Sarbanes-Oxley Act amended § 101 of ERISA, adding subsection (i), which requires administrators to provide participants with notice prior to a lockdown. Section 306(b)(3) of the Sarbanes-Oxley Act amended § 502(c) of ERISA by adding paragraph (7) creating civil penalties for plan administrators who fail to comply with the notice requirement. *See* U.S. Dep't of Labor Pension and Welfare Benefits Admin., 67 Fed. Reg. 64774, *Civil Penalties Under ERISA Section 502(c)(7) and Conforming Technical Changes on Civil Penalties Under ERISA Sections 502(c)(2), 502(c)(5), and 502(c)(6)* (Oct. 21, 2002).

93. U.S. Dep't of Labor, *News Release: Labor Department Issues Rules on Disclosure of Pension Plan 'Blackout Periods'*, Oct. 18, 2002, at <http://www.dol.gov/opa/media/press/ebsa/EBSA2002605.htm> [hereinafter U.S. Dep't of Labor, *Blackout News Release*].

94. *See* Strope, *supra* note 91.

95. *See supra* Part III. It is the opinion of the Secretary of Labor that Congress must pass additional legislation granting workers the right to diversify their accounts as well as access to better information, including professional investment advice. *See* U.S. Dep't of Labor, *Blackout News Release*, *supra* note 93. On April 11, 2002, the House of Representatives passed a bill allowing workers to diversify their investments in employer stock after three years, requiring quarterly benefit statements that emphasize the importance of diversification, and giving workers access to investment advice from professional advisers. *See* U.S. Dep't of Labor, *News Release: President Takes Action to Protect Pensions and Retirement Security for All Americans*, Oct. 18, 2002, at <http://www.dol.gov/opa/media/press/ebsa/EBSA2002605.htm>. The bill, H.R. 3762, also prohibits executives from selling employer stock during lockdowns. *See* Gov't Fin. Officer's Assoc., *Association Issue Brief: Post-Enron Accounting & Pension Reform Proposals*, June 2002, at <http://www.gfoa.org/flc/briefs/062702/post.enron.06.02.pdf>. Unfortunately, the Senate has failed to pass this legislation as well. *See* U.S. Dep't of Labor, *Blackout News Release*, *supra* note 93.

The interim rules promulgated by the Department of Labor under the Sarbanes-Oxley Act became effective on January 26, 2003. The rules require notice to participants thirty to sixty days prior to the commencement of the lockdown period.<sup>96</sup> The notice must be “written in a manner calculated to be understood by the average plan participant,”<sup>97</sup> and must describe the rights of the participant that will be temporarily suspended during the period as well as the investments subject to the suspension.<sup>98</sup> Additionally, the notice must include the anticipated beginning and ending dates of the lockdown<sup>99</sup> and advise participants to review their current investments in light of the upcoming suspension of trading.<sup>100</sup> Finally, the notice must include the name, address, and telephone number of the plan administrator or one who can answer questions regarding the lockdown.<sup>101</sup>

#### IV. THE COMPLAINT ALLEGATIONS

In the lockdown allegations of the Complaint, Plaintiffs allege that Enron; the Administrative Committee; top executives, such as Lay and Skilling; and the Northern Trust Company (“Defendants”) were and acted as fiduciaries under ERISA.<sup>102</sup>

According to the Complaint, in October 2001 the Defendants breached their fiduciary duties to the participants of the 401(k) Plan by continuing with the lockdown as planned. Defendants allegedly improperly prevented the participants from selling the Enron stock in their individual accounts during a time when the value of Enron stock plummeted.<sup>103</sup> The Complaint alleges that because the Defendants knew some or all of the facts concerning Enron’s precarious financial

96. See 29 C.F.R. § 2520.101-3(b)(2)(i) (2003).

97. 29 C.F.R. § 2520.101-3(b)(1) (2003).

98. See 29 C.F.R. § 2520.101-3(b)(1)(ii) (2003).

99. See 29 C.F.R. § 2520.101-3(b)(1)(iii) (2003).

100. See 29 C.F.R. § 2520.101-3(b)(1)(iv) (2003).

101. See 29 C.F.R. § 2520.101-3(b)(1)(vi) (2003). Additionally, if the plan administrator does not comply with the notice regulations, a second set of rules provides for civil penalties of up to 100 dollars per day per plan participant. See U.S. Dep’t of Labor, *Blackout News Release*, *supra* note 93. The Secretary of Labor will consider the degree and/or willfulness of the failure or refusal to provide notice, computed from the date of the administrator’s failure of the lockdown until the final day of the lockdown. See 29 C.F.R. § 2560.502(c)-7(b)(1).

102. See First Am. and Consolidated Compl., *Tittle v. Enron Corp.*, No. H-01-3913, at 752 (S.D. Tex. Apr. 8, 2002). The pertinent ERISA fiduciary language is found in 29 U.S.C. § 1002(21)(A) (2000). This Note will discuss the allegations against the Administrative Committee only. See *supra* note 9.

103. See First Am. and Consolidated Compl., *Tittle v. Enron Corp.*, No. H-01-3913, at ¶ 753 (S.D. Tex. Apr. 8, 2002).

condition they also knew or should have known that it was imprudent to proceed with the lockdown. Furthermore, the Complaint asserts that the Defendants had a duty to postpone the lockdown, as a loyal and prudent fiduciary would have done in light of this information. As a result of these breaches of duty, Plaintiffs assert that, as participants and beneficiaries of the 401(k) Plan, they lost a great deal of money during the lockdown period.<sup>104</sup>

Additionally, the Complaint asserts that the Defendants had a duty to provide timely and informative notice of the lockdown to participants so they could safeguard their rights by directing the fiduciaries to sell the Enron stock allocated to their individual accounts. In failing to do so, the Defendants allegedly breached their ERISA duties, causing the participants to lose much of their retirement accounts.<sup>105</sup>

Finally, but for these asserted breaches of fiduciary duty, the Complaint asserts that the assets of the plan would have been invested in more profitable alternative investments available under the Plan,<sup>106</sup> and that the Court should restore the losses to the Plan caused by the Defendants' breach of fiduciary duties.<sup>107</sup>

#### V. THE POSSIBILITY OF SUCCESS FOR PARTICIPANTS IN LOCKDOWN LITIGATIONS

The Tittle litigation is illustrative in analyzing the potential for success of lockdown claims against fiduciaries in lawsuits by participants in 401(k) plans. In order for the Tittle Plaintiffs, or other plaintiffs similarly situated, to recover with respect to the lockdown claim against the Administrative Committee, or an entity similar to the Committee,<sup>108</sup> the Committee must first qualify as a fiduciary of the 401(k) plan in terms of the decision to continue with the lockdown. Second, if the Administrative Committee, or a similar entity in other litigations, indeed qualifies as a fiduciary, it must have breached a fiduciary duty under ERISA by making the decision to continue with the lockdown. Stating the issue specifically, did the Enron Adminis-

104. *See id.* at ¶ 758.

105. *See id.* at ¶ 759. While this allegation is related to the lockdown, it does not deal with the issue of Defendant's decision to continue with the lockdown as planned, and will therefore not be discussed in this Note.

106. *See id.* at ¶ 761.

107. *See id.* at ¶ 763.

108. *See supra* note 9.

trative Committee, as a fiduciary of the 401(k) Plan, breach the duties of prudence and loyalty by not postponing the lockdown despite their awareness of the poor financial health of the Corporation?<sup>109</sup>

A. *Was the Administrative Committee a Fiduciary of the Plan with Regard to the Lockdown?*

As discussed above, under ERISA a fiduciary is anyone who exercises discretionary control or authority over plan management or plan assets, has discretionary authority or responsibility for the administration of a 401(k) plan, or provides investment advice to a 401(k) plan for compensation or has the authority or responsibility to do so.<sup>110</sup> Plan trustees, plan administrators, and members of a plan's investment committee may be fiduciaries.<sup>111</sup>

"Despite the ability of an ERISA fiduciary to wear two hats," a fiduciary must "wear the fiduciary hat when making fiduciary decisions."<sup>112</sup> The language of ERISA "plainly indicates that the fiduciary function is not an indivisible one. In other words, a court must ask whether a person [or entity] is a fiduciary with respect to the particular activity at issue."<sup>113</sup>

The named fiduciary of the 401(k) Plan is the Enron Corporation Savings Plan Administrative Committee, the administrator of the plan.<sup>114</sup> In the 401(k) Plan document, Enron placed a fiduciary duty on the Administrative Committee to discharge its duties and responsibilities with respect to the plan solely in the interest of the partici-

109. In the final step, which this Note will not address, the remedies that are available and adequate for a given breach must be considered. Under ERISA, only equitable or remedial relief is available for a breach of fiduciary duty. *See* 29 U.S.C. § 1132(a)(3) (2000); *see also* *Varity Corp. v. Howe*, 516 U.S. 489, 508, 515 (1996).

110. *See* U.S. DEP'T OF LABOR, PENSION AND WELFARE BENEFITS ADMIN., *What You Should Know... About Your Pension Rights*, Jan. 2002, at 45, available at <http://www.dol.gov/ebsa/publications/wyskapr.html>.

111. *See id.*

112. *Bussian v. RJR Nabisco, Inc.*, 223 F.3d 286, 295 (5th Cir. 2000) (citing *Pegram v. Herdrich*, 530 U.S. 211, 225 (2000)).

113. *Coleman v. Nationwide Life Ins. Co.*, 969 F.2d 54, 61 (4th Cir. 1992) ("[T]he inclusion of the phrase 'to the extent' in § 1002(21)(A) means that a party is a fiduciary only as to the activities which bring the person within the definition."); *see also* 29 C.F.R. § 2509.75-8 (2003).

114. *See* ENRON CORP., ENRON CORP. SAVINGS PLAN, XIII.1 Administration of the Plan: Appointment of Committee, as amended and restated July 1, 1999; *see also* First Am. and Consolidated Compl., *Tittle v. Enron Corp.*, No. H-01-3913, at ¶ 44 (S.D. Tex. Apr. 8, 2002). The Complaint alleges that the members of the Administrative Committee include, among others: Cindy Olson, James Prentice, Mary K. Joyce, Sheila Knudsen, Rod Hayslett, Paula Rieker, Tod A. Lindholm, James G. Barnhart, Keith Crane, William J. Gulyassy, and David Shields. *See id.* at ¶¶ 47-60.



pants, for the exclusive purpose of providing benefits to participants; to discharge those duties 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 in the conduct of an enterprise of a like character and with like aims; and to diversify the instruments of the plan so as to minimize the risk of large losses.<sup>115</sup>

Thus, the Administrative Committee was specifically granted fiduciary responsibilities.<sup>116</sup> It had the “authority to control and manage the operation and administration of the plan under section 402 of ERISA.”<sup>117</sup> “Without question, as the persons and entity charged with responsibility for managing the plans and their assets, the members of the Administrative Committee were plan fiduciaries.”<sup>118</sup>

*B. Did the Administrative Committee, as a Fiduciary of the 401(k) Plan, Act Loyally and Prudently in the Decision to Continue with the Lockdown as Planned?*

As discussed above, fiduciaries owe duties of prudence and loyalty to the participants and beneficiaries of a 401(k) plan.<sup>119</sup> At a minimum, ERISA requires fiduciaries to be objective, thorough, and analytical in the decision-making process.<sup>120</sup>

The duty of prudence requires that fiduciaries 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 matter would use in the conduct of” a similar enterprise.<sup>121</sup> “When we apply [the duty of prudence] to the facts of a particular case, we remain mindful of ERISA’s underlying purposes: to protect and strengthen the rights of employees, to enforce strict fiduciary standards, and to encourage the development of private retirement

115. See *Hearings*, *supra* note 54, at 239 (statement of Senator Lieberman).

116. See *id.*

117. Letter from George Miller, Senior Democratic Member, House Committee on Education and the Workforce to Elaine Chao, Secretary of Labor, U.S. Dept. of Labor (Feb. 8, 2002), available at <http://edworkforce.house.gov/democrats/enronlettertochao.html>.

118. Amended Brief of the Secretary of Labor as Amicus Curiae Opposing the Motions to Dismiss, *Tittle v. Enron Corp.*, No. H-01-3913, at 5 (S.D. Tex. filed Apr. 8, 2002), available at <http://www.dol.gov/sol/images/EnronBrief1.fnl.PDF>.

119. See *supra* notes 83–87 and accompanying text.

120. See *Bussian v. RJR Nabisco, Inc.*, 223 F.3d 286, 299 (5th Cir. 2000).

121. 29 U.S.C. § 1104(a)(1)(B) (2000); see also *In re Unisys Sav. Plan Litig.*, 74 F.3d 420, 433–34 (3d Cir. 1996).

plans.”<sup>122</sup> The prudence requirement focuses “on a fiduciary’s conduct in arriving at an investment decision, not on its results, and ask[s] whether a fiduciary employed the appropriate methods to investigate and determine the merits of a particular investment.”<sup>123</sup>

The duty of loyalty requires that fiduciaries discharge their duties solely in the interests of participants, for the exclusive purpose of providing benefits to participants.<sup>124</sup> “[F]iduciaries act consistently with ERISA’s obligations if their decisions are made with an eye single to the interests of the participants and beneficiaries.”<sup>125</sup> They must “keep the interests of beneficiaries foremost in their minds, taking all steps necessary to prevent conflicting interests from entering into the decision-making process.”<sup>126</sup>

To determine if a breach of these fiduciary duties occurred, one must assess what information regarding the financial health of the company the fiduciaries knew, or should have known.

As outlined in Part II, an in-house lawyer reviewing the questionable transactions in a memo determined that one could conclude that Enron’s financial books were being manipulated.<sup>127</sup> He informed his supervisors of his conclusions and then changed them at their request.<sup>128</sup> A vice president of the company, Sherron Watkins, wrote a whistle-blowing memo directly to Kenneth Lay that included predictions of an accounting scandal.<sup>129</sup> Others in the Corporation, including members of the Administrative Committee, were also aware of the allegations in Watkins’ memo.<sup>130</sup> Additionally, the SEC had begun an investigation into the financial practices of the Corporation. Thus, it is clear that information regarding the debatable financial health was available to both the Corporation itself as well as the Administrative

122. *In re Unisys Sav. Plan Litig.*, 74 F.3d at 434.

123. *Id.* The duty of prudence requires that “at the time they engaged in the challenged transactions, [the fiduciaries] employed the appropriate methods to investigate the merits” of the decision. *Bussian*, 223 F.3d at 299 (citations omitted). It requires “prudence, not precience.” *Id.*

124. 29 U.S.C. § 1104(a)(1)(A)(i) (2000); *see also* *Varity Corp. v. Howe*, 516 U.S. 489, 506 (1996). The duty of loyalty, or the obligation of a fiduciary to administer the plan solely in the interests of participants, is the most fundamental duty imposed by ERISA. *See Bussian*, 223 F.3d at 294 (citing *Pegram v. Herdrich*, 530 U.S. 211, 224 (2000)); *see also* *Simone & Butash*, *supra* note 81, at \*685.

125. *Bussian*, 223 F.3d at 298 (citations and quotations omitted).

126. *Id.* at 298 (citations omitted).

127. *See supra* text accompanying note 49.

128. *See supra* text accompanying note 50.

129. *See supra* text accompanying notes 51–53.

130. *See supra* text accompanying notes 55–56.

Committee. As Senator Durbin asked of Mikie Rath during the Senate Governmental Affairs Committee:

But there is something that just does not compute . . . you had to understand that the lockdown period meant that [the participant employees] stood the risk of the value of their 401(k) plummeting during that period of time . . . How could you think [that] you were doing the employees a favor by locking them out of a market when your stock is plummeting . . .?<sup>131</sup>

To Ms. Rath's reply that the Administrative Committee could not predict the value of the stock, Senator Durbin replied,

Do you see this chart over here? Is this a trend line? It looks like one to me. I'm sure you were hoping that things would get better. But I'm a liberal arts lawyer, so I don't know much about this. But I look at that and say, 'Does not look like a good investment.' You must have been aware of the same thing.<sup>132</sup>

Indeed, the Administrative Committee, the entity charged with protecting the participants' interests,<sup>133</sup> considered the possibilities of postponing the lockdown, or halting it altogether.<sup>134</sup>

Furthermore, evidence exists throughout the minutes of the Administrative Committee's meetings that members considered the viability of various investments in Enron's retirement plans. Alternatives available under the 401(k) Plan other than Enron stock were considered and replaced with different investment options.<sup>135</sup> During the meeting on December 9, 1999, Mr. Newgard proposed new guidelines that included performance standards and criteria for investments to guide the Committee in monitoring and replacing the investments of the retirement plans.<sup>136</sup> On February 8, 2001, the Committee discussed the general decline of U.S. stocks, as the

131. *Hearings, supra* note 54, at 251 (statement of Senator Durbin).

132. *See id.*

133. *See supra* text accompanying notes 114–18.

134. *See supra* text accompanying notes 66–68.

135. On October 26, 1999 Jim Newgard summarized the returns from the first three quarters of the year, and an asset allocation study was recommended. Mr. Newgard recommended that the Delaware Fund be replaced with a Vanguard fund, and the board voted to make the change. *See* Cynthia Barrow, Minutes of the Meeting of the Enron Corp. Administrative Committee (Oct. 26, 1999), *available at* <http://edworkforce.house.gov/democrats/enroninfo.html>. On December 9, 1999 the Committee passed a motion to replace an under performing Provident fund with a small cap growth index fund. *See* Cynthia Barrow, Minutes of the Meeting of the Enron Corp. Administrative Committee (Dec. 9, 1999), *available at* <http://edworkforce.house.gov/democrats/enroninfo.html>.

136. *See* Cynthia Barrow, Minutes of the Meeting of the Enron Corp. Administrative Committee (Dec. 9, 1999), *available at* <http://edworkforce.house.gov/democrats/enroninfo.html>.

NASDAQ had its worst year in its thirty-year history,<sup>137</sup> and it was agreed that performance would be reviewed monthly.<sup>138</sup> The Committee was therefore aware of the market's decline, and of its effect on the 401(k) Plan. However, no review of Enron stock is evident until November 1, 2001,<sup>139</sup> after the lockdown had already been implemented. The Committee, after the lockdown had begun, passed Cindy Olson's motion "to hire a reputable firm to advise the Committee on Enron stock."<sup>140</sup> The decision to move forward with the lockdown, or the transfer between Northern Trust to Hewitt Associates, was outlined, and the Committee agreed that it had been prudent to move forward.<sup>141</sup> On December 5, 2001, after the lockdown had been lifted, the Committee determined "that it would be prudent, at [that] time, to have the Enron Stock Fund professionally and externally evaluated by an independent group."<sup>142</sup>

Thus, evidence that adequate information regarding the financial health of the Corporation (and thus the value of Enron stock) existed within the Corporation itself and which the Administrative Committee was aware of. Therefore, it is likely that the fiduciaries of the 401(k) Plan were aware of the precarious position that Enron maintained, and if they were not, they should have been. Additionally, while the Committee actively evaluated some of the alternatives in the 401(k) Plan, they did not discuss the value of Enron stock (which comprised more than 60% of the plan) until after the lockdown had already begun. If it was prudent to examine the Enron Stock Fund after the lockdown on December 5, 2001, it would also have been

137. See Cynthia Barrow, Minutes of the Meeting of the Enron Corp. Administrative Committee (Feb. 8, 2001), available at <http://edworkforce.house.gov/democrats/enroninfo.html>.

138. See *id.*

139. See Cynthia Barrow, Minutes of the Meeting of the Enron Corp. Administrative Committee (Nov. 1, 2001), available at <http://edworkforce.house.gov/democrats/enroninfo.html>. Mikie Rath advised the Committee that it had "no duty to put out cautionary advice on the value/risk of holding Enron stock since the Committee does not act in the capacity of an investment advisor." *Id.*

140. *Id.*

141. *Id.* The members present at this meeting were Paula H. Rieker, Sheila Knudsen, James S. Prentice, and Cindy Olson. Additionally, Cynthia Barrow, Mikie Rath, Sharon Butcher, and Pat Mackin were present, as well as representatives of Hewitt Associates. See *id.*

142. See Chris Rahaim, Minutes of the Meeting of the Enron Corp. Administrative Committee (Dec. 5, 2001), available at <http://edworkforce.house.gov/democrats/enroninfo.html>. Additionally, on October 26, 1999, a special meeting was set up to review the fiduciary duties to Enron's retirement plans. See Barrow, Minutes of the Meeting of the Enron Corp. Administrative Committee (Oct. 26, 1999), *supra* note 135. This meeting, where a review of member duties and responsibilities took place, occurred on March 9, 2000. See Cynthia Barrow, Minutes of the Meeting of the Enron Corp. Administrative Committee Meeting (March 9, 2000), available at <http://edworkforce.house.gov/democrats/enroninfo.html>.

prudent for the Administrative Committee to examine the fund prior to the lockdown.

The Administrative Committee had several options in light of this information regarding the Corporation's declining financial health.<sup>143</sup> First, they could do nothing and continue with the lockdown as planned, which was the chosen path. As shown by the Enron situation, the refusal to postpone a lockdown holds a great probability that a breach of fiduciary duty will occur. Second, the Administrative Committee could have postponed the lockdown period.<sup>144</sup> While this option is less likely to result in a breach of fiduciary duty, it raises several issues.

### 1. The Duty of Impartiality

First, in dealing with participants, fiduciaries such as the Administrative Committee must act impartially.<sup>145</sup> The Committee, in defense of its decision to continue with the lockdown as planned, asserts that current employee participants were likely to receive the information regarding the postponement before retiree participants. This violates the duty of impartiality because current employees would be able to reallocate their assets while retirees would not.<sup>146</sup>

However, while the common law of trusts "requires a trustee to take impartial account of the interests of all beneficiaries,"<sup>147</sup> a trustee also has broad powers to do all acts necessary or desirable to carry out the purposes of the trust.<sup>148</sup> One such purpose of the Enron 401(k)

143. These options stem from the fact that there were no compelling circumstances mandating that the lockdown occur specifically during the planned timeframe.

144. Fiduciaries may violate the duties of prudence and loyalty not only by poorly scheduling a lockdown period, but also by not changing the timing of a well-planned lockdown when information becomes available that the value of the plan assets may fluctuate throughout the planned timeframe.

145. See RESTATEMENT (SECOND) OF TRUSTS, §§ 183, 232 (1959); see also *Varity Corp. v. Howe*, 516 U.S. 489, 514 (1996); *Williams v. WCI Steel Co.*, 37 Fed. Appx. 723, 729 (No. 00-4363) (6th Cir. 2002) ("When there are two or more beneficiaries of a trust, the trustee is under a duty to deal impartially with them.") (quoting RESTATEMENT (SECOND) OF TRUSTS, §§ 183 (1959)).

146. Current employees, but not retirees, would be attending an upcoming all-employee meeting during which the information could be provided to them. See *Hearings*, *supra* note 54, at 246 (statement of Mikie Rath).

147. *Varity Corp.*, 516 U.S. at 514-15.

148. See *Bracken v. Block*, 561 N.E.2d 1273, 1274-75 (Ill. App. Ct. 1990). The fiduciary's "'duty of impartiality . . . ordinarily' gives him 'considerable discretion' in deciding the 'balance' between successive beneficiaries." *Mahoney v. Bd. of Trs.*, 973 F.2d 968, 971 (1st Cir. 1992) (quoting 3A Scott on Trusts § 232 (2001)).

Plan was to provide benefits to participants.<sup>149</sup> It seems that a simple balancing of providing the opportunity to participants to reallocate their assets during the financial decline and the chance that retirees might not receive equal notice of the postponement weighs in favor of postponing the lockdown. Because this has the greatest potential to enable the participants to receive later retirement benefits by moving their investments from the declining Enron stock, this aligns with the purpose to provide benefits to participants.

Additionally, throughout the period when the lockdown was in place, many participants, including retirees, attempted to reallocate their assets despite awareness of the lockdown.<sup>150</sup> Therefore, even if the Administrative Committee postponed the lockdown, and current employee participants were the only class who received it, it is likely that retiree participants would have had the opportunity to reallocate regardless because the decline in the stock would have prompted them to do so.

## 2. Insider Trading

If a fiduciary announces the postponement of a planned lockdown, it is likely that participants will inquire as to the reasons supporting that decision. In the Enron lockdown situation, the information on which the Committee would have based that decision was nonpublic information. Therefore, communicating that information to employees raises insider trading concerns.

Insider trading liability, or the liability of one who trades securities on the basis of material, nonpublic information (“insider” information) is imposed by Rule 10b-5,<sup>151</sup> promulgated under the Securities Exchange Act of 1934.<sup>152</sup> The classical theory of insider trading provides that Rule 10b-5 is violated when one buys or sells securities on the basis of material, nonpublic information if: (1) he owes a duty to the other party in the transaction; and (2) he is an insider of the corporation in whose shares he trades, thus owing a fiduciary duty to the corporation’s shareholders.<sup>153</sup> A person also may be

149. See ENRON CORP., ENRON CORP. SAVINGS PLAN, XV.3 Fiduciary Provisions: Fiduciary Duty, as amended and restated July 1, 1999.

150. See *supra* text accompanying note 65.

151. 17 C.F.R. § 240.10b-5 (2003).

152. 15 U.S.C. § 78j(b) (2000).

153. See George F. Gabel, Jr., *Who May Be Liable Under “Misappropriation Theory” of Imposing Duty to Disclose or Abstain From Trading Under § 10(b) of Securities Exchange Act of 1934 (15 U.S.C.A. § 78j(b)) and SEC Rule 10(b)-5 (17 C.F.R. § 240.10b-5)*, 114 A.L.R. FED. 323,

liable if: (1) he is a tippee who received the material, nonpublic information from an insider of the corporation; and (2) he knows, or should know, that the insider breached a fiduciary duty in disclosing the information to him.<sup>154</sup> These insiders have a duty to abstain from trading securities based on the material, nonpublic information until that information has been disclosed to the public.<sup>155</sup>

The Administrative Committee contends that giving participants the explanation for the lockdown postponement that they would inevitably request would place both the Administrative Committee and the participants in a position to be liable for insider trading because participants would then sell their Enron stock based on material, nonpublic information.

However, for the Administrative Committee and the participants to be liable for insider trading,<sup>156</sup> the Committee must personally benefit from the disclosure of the reasons regarding the lockdown postponement, and must breach a fiduciary duty to the shareholders by disclosing this information.<sup>157</sup> Furthermore, the participants must know (or should know) that this disclosure was a breach, and actually sell their Enron stock based on the information.<sup>158</sup> The Administrative Committee would receive no personal benefit from disclosing the information regarding the reasons behind the lockdown postponement, and, therefore, there would be no liability on the part of the Committee or the participants for insider trading.<sup>159</sup>

If the Enron 401(k) Plan participants asked for an explanation regarding the postponement of the lockdown, the Administrative

§ 2[a] (1993). This classical theory of insider trading is defined by the Supreme Court in *Chiarella v. United States*, 445 U.S. 222 (1980).

154. See Gabel, *supra* note 153.

155. See *Dirks v. S.E.C.*, 463 U.S. 646, 659–63 (1983); see also F. S. Tinio, *Who is an "Insider" Within § 10(b) of the Securities Exchange Act of 1934 (15 U.S.C.A. § 78(j)(b))—and SEC Rule 10b-5 Promulgated Thereunder—Making Unlawful Corporate Insider's Nondisclosure of Information to Seller or Purchaser of Corporation's Stock*, 2 A.L.R. FED. 274, § 2 (1969). While directors, officers, and controlling officers are traditionally recognized as insiders, employees that own securities and have access to nonpublic, material information, including those who acquire stock through 401(k) plans, are subject to the obligations of an insider. See *Dirks*, 463 U.S. at 659–63. This extension comports not only with the public policy of Rule 10b-5 to place investors on an equal footing with insiders, as well as that employees may also be viewed as agents of the stockholders and thus have a duty not to use inside information for personal benefit. See Tinio, *supra*.

156. Or more accurately, for the participants to be subject to the duty to disclose or abstain from trading based on the nonpublic, material information. See *Dirks*, 463 U.S. at 659–63.

157. See *id.*

158. See *id.*

159. See *id.*

Committee would be liable if they lied or misrepresented their reasons, if those reasons were material.<sup>160</sup> Materiality “depends on the significance the reasonable investor would place on the . . . misrepresented information.”<sup>161</sup> Because the participants in the 401(k) Plan would clearly place great significance on information that Enron was in such a precarious state, the reasons behind a postponement decision would be material. Therefore, the Administrative Committee could not lie or misrepresent their reasons for a postponement.

The Administrative Committee could have avoided lying or misrepresenting its material reasons by issuing a “no comment” statement, which is not considered misleading and would not result in liability.<sup>162</sup> Therefore, simply by stating “no comment,” the Administrative Committee could have avoided liability and given the participants the opportunity to change the allocation of their 401(k) plans from the declining Enron stock to a more stable alternative.

In the alternative, the Committee could have announced any explanation they wished to offer the participants of the plan to the public as well to avoid any insider trading liability on behalf of the Administrative Committee or the participants. Insider trading liability does not result from trading based on public information.

### 3. Reliance on Counsel

In a lockdown situation, a fiduciary may assert reliance on counsel as a defense.<sup>163</sup> In the Enron situation, the Administrative Committee claims that because it relied on the advice of counsel in the decision to continue with the lockdown as planned, it cannot be liable for any breach. “Fiduciaries . . . are entitled to rely on the advice they

160. See 17 C.F.R. § 240.10b-5 (2003). The SEC promulgated Rule 10b-5 pursuant to its authority under 15 U.S.C. § 78j (2000). See *Basic, Inc. v. Levinson*, 485 U.S. 224, 230 (1988) (holding that public statements denying merger negotiations which were taking place were misleading as to material facts and in violation of Rule 10b-5). Rule 10b-5 provides:

It shall be unlawful for any person . . . [t]o make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading . . . in connection with the purchase or sale of any security.

See *id.* at 230 n.6.

161. See *Basic*, 485 U.S. at 240. The inquiry for materiality is fact-specific. See *id.*

162. See *In re Carnation Co.*, Exchange Act Release No. 22214, 33 S.E.C. Docket 1025 (1985); *Basic*, 485 U.S. at 239 n.17 (“‘No comment’ statements are generally the functional equivalent of silence,” and absent a duty to disclose, under Rule 10b-5 silence is not misleading.).

163. See *Donovan v. Cunningham*, 716 F.2d 1455, 1474 (5th Cir. 1983) (“ERISA fiduciaries . . . are entitled to rely on the expertise of others.”).



obtain from independent experts.”<sup>164</sup> The use of counsel “may serve the dual purposes of increasing the thoroughness and impartiality of the relevant investigation, and of relieving the fiduciary of any taint of a potential conflict.”<sup>165</sup>

However, fiduciaries may not blindly rely on the advice of counsel.<sup>166</sup> “An independent appraisal is not a magic wand that fiduciaries may simply waive over a transaction to ensure that their responsibilities are fulfilled. It is a tool, and like other tools, is useful only if used properly.”<sup>167</sup> Therefore, mere reliance on the advice of counsel is not a complete defense.<sup>168</sup>

For reliance by a fiduciary on an expert’s opinion to be justifiable, the fiduciary must consider the reputation and experience of the expert, the extensiveness and thoroughness of the investigation by the expert, whether the opinion of the expert is supported by relevant material, and whether assumptions of the expert are appropriate to the decision.<sup>169</sup> “[T]he fiduciary 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.”<sup>170</sup>

Thus, while the Administrative Committee was entitled to request the advice of counsel regarding the possibility of postponing the lockdown, they were not entitled to rely blindly on the opinion rendered by counsel. Although it was possible that not all employee and retired participants would receive notice of the postponement of the lockdown at the same time, it is likely that many participants, including retirees, would have tried to trade during the planned timeframe and, therefore, would have become aware of the postponement. In fact, many participants did attempt to trade throughout the lockdown period, but were unable to do so.<sup>171</sup> Additionally, there is no evidence in the minutes of the Administrative Committee meetings that the Committee considered the many factors that justify reliance on counsel’s opinion, especially whether the lockdown was appropriate in

164. *Bussian v. RJR Nabisco, Inc.*, 223 F.3d 286, 300 (5th Cir. 2000).

165. *Id.*

166. *Id.* at 301.

167. *Cunningham*, 716 F.2d at 1474.

168. *See Bussian*, 223 F.3d at 301 (citing *Donovan v. Mazzola*, 716 F.2d 1226, 1234 (9th Cir. 1983)).

169. *See id.*

170. *Id.* (quoting *Howard v. Shay*, 100 F.3d 1484, 1490 (9th Cir. 1996)).

171. *See supra* text accompanying note 65.

light of Enron's situation.<sup>172</sup> Considering the information available regarding the financial state of the Corporation, it seems it was both disloyal and imprudent to continue with the lockdown as planned because it was not in the best interests of participants, nor would that decision have the greatest likelihood of providing benefits to the participants.

The issues of impartiality, insider trading, and reliance on counsel are not likely to provide a defense for the Administrative Committee or fiduciaries in lockdown claims generally.<sup>173</sup> The decision not to postpone the lockdown was not made with the requisite skill, care, prudence, and diligence required of fiduciaries, and was not solely in the interest of participants for the exclusive purpose of providing benefits. Therefore, it is likely that the court will find that the Administrative Committee breached the duties of prudence and loyalty imposed by ERISA by continuing with the lockdown as planned, despite knowledge of Enron's precarious financial state and the declining value of its stock.<sup>174</sup> These fiduciary duties are among the "highest known to the law,"<sup>175</sup> and such a demanding standard clearly was not satisfied by the Administrative Committee's decision not to postpone the lockdown.

172. See generally ENRON CORP. ADMIN. COMM., Administrative Committee Minutes, available at <http://edworkforce.house.gov/democrats/enroninfo.html>.

173. An additional defense of the Administrative Committee rests in 29 U.S.C. § 1104(c)(1)(B) (2000). Under this Section, no fiduciary shall be liable for any loss, or by reason of any breach, which results from a participant or beneficiary's exercise of control. See 29 U.S.C. § 1104(c)(1)(B) (2000). This qualification has important ramifications for the participants such as the Tittle plaintiffs, who exert control over their 401(k) plans, because they individually choose how to allocate their money across the funds the employer provides. Therefore, the Administrative Committee raised in its defense that because the Enron participants exercise such control, they cannot be liable for the decline of the 401(k) plan because the employees individually directed their investments into Enron stock.

However, because of the inherent nature of a lockdown in removing the participants' control over their accounts, this defense is unavailable to the Administrative Committee. Once the employer initiates the lockdown period, participants can make absolutely no changes in the allocation of their retirement money until the employer terminates the lockdown. Because it is the employer who institutes lockdowns, and it is the employer who terminates the lockdown period, it is the employer, not the participants, who is exerting control over the allocation of the participants' 401(k) accounts. Therefore, if a fiduciary breaches an ERISA duty in instituting a lockdown, they are responsible for the losses that result from the lockdown, even though normally the participants exercise individual control over their accounts.

174. See 29 U.S.C. § 1104 (2000).

175. *Bussian*, 223 F.3d at 294; see also *Sommers Drug Stores Co. Employee Profit Sharing Trust v. Corrigan Enters., Inc.*, 793 F.2d 1456, 1468 (5th Cir. 1986), cert. denied, 479 U.S. 1089 (1987).

## CONCLUSION

Unfortunately, in suits by individuals seeking relief for breach of fiduciary duties under ERISA, equitable relief is the sole remedy available.<sup>176</sup> Therefore, although it is likely that a Court will find that fiduciaries like the Administrative Committee breached their duties of prudence and loyalty in lockdown situations similar to Enron, no compensatory damages are available. Clearly, further changes in ERISA are needed, such as a clear delineation of the fiduciary duties that exist during a lockdown. Hopefully, public discussion of the disastrous effects of Enron for the participants in the 401(k) Plan will bring both greater protections and a more effective remedy in order to prevent such catastrophes in the future.

176. See 29 U.S.C. § 1132(a)(3) (2000); *Varity Corp. v. Howe*, 516 U.S. 489, 508, 515 (1996).