UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WISCONSIN

SCOTT MacTAGGERT, on behalf of the Extreme Engineering Solutions, Inc. Employee Stock Ownership Plan, and on behalf of a class of all other persons similarly situated,

Case No. 22-CV-371

Plaintiff,

v.

PROFESSIONAL FIDUCIARY SERVICES, LLC, JOHN MICHAEL MAIER, ROBERT S. SCIDMORE, and BRET FARNUM,

Defendants.

DEFENDANTS PROFESSIONAL FIDUCIARY SERVICES, LLC AND JOHN MICHAEL MAIER'S REPLY BRIEF IN SUPPORT OF THEIR MOTION TO DISMISS

INTRODUCTION

In an attempt to distract this Court from his Complaint's fatal flaws, Plaintiff Scott MacTaggert's response to the Trustee Defendants' motion to dismiss primarily consists of irrelevant arguments, and cases that are distinguishable or not binding on this Court. MacTaggert does not have standing to bring this case because he has not alleged any *facts* to demonstrate he has suffered an injury, and he ignores the fact that the value of the ESOP's assets have increased by tens of millions of dollars since the ESOP was created. Nothing in his response brief changes that fact. MacTaggert's failure to allege an injury requires this Court to dismiss his Complaint.

ARGUMENT

I. MACTAGGERT'S COMPLAINT MUST BE DISMISSED FOR LACK OF STANDING.

A. MacTaggert suffered no injury.

MacTaggert's claims against the Defendant Trustees are based on allegations that the Defendant Trustees caused the ESOP to buy shares of Extreme Engineering for more than fair market value, but nowhere in the Complaint does MacTaggert allege facts demonstrating that he suffered an injury as a result of these baseless allegations. Nor could he because the value of Extreme Engineering stock has risen substantially each year since the creation of the ESOP. MacTaggert admits that he has not alleged that the value of the stock has decreased, but he suggests that his failure to allege post-transaction drops in valuation is irrelevant to his injury because the Complaint "makes numerous other allegations of injury." (ECF 41 at 22.) But his "other allegations of injury"—optimistic projections and faulty comparable companies—are not injuries. MacTaggert must allege some predicate fact from which this Court could infer that an injury has occurred and he has not done so.

MacTaggert asks this Court to ignore the cases cited by the Trustee Defendants and instead rely on *Allen*. (ECF 41 at 22 (citing *Allen v. GreatBanc Tr. Co.*, 835 F.3d 670, 678–80 (7th Cir. 2016).) But the plaintiffs in *Allen did* allege that the stock value dropped dramatically (22%) after the ESOP transaction. *Allen*, 835 F.3d at 678. The court held that this allegation suggested that the sale price was too high and was enough for purposes of surviving a motion to dismiss. *Id*. MacTaggert admits he did not make similar allegations in his Complaint.

Here, although MacTaggert claims that the Trustee Defendants "caused the Plan to buy shares of Extreme Engineering for more than fair market value," resulting in losses to the Plan, there are no factual allegations concerning why or how the price paid for the stock was too high, including any allegations about a drop in the value of the stock. Moreover, the "numerous other

allegations of injury" consist entirely of conclusory allegations that repeat the exact same thing: that the ESOP overpaid for Extreme Engineering stock. (*See* Compl. ¶¶ 8, 48, 56, 94.) These allegations are insufficient to plausibly allege a concrete and particularized injury in fact. *See Spokeo Inc. v. Robins*, 578 U.S. 330, 339 (2016).

B. This Court can take judicial notice of the publicly filed Form 5500s.

Relying on *Lysengen v. Argent Tr. Co*., 498 F. Supp. 3d 1011, 1017-18 (C.D. Ill. 2020), MacTaggert misleadingly argues that this Court may not take judicial notice of the publicly filed Form 5500s for their truth. (ECF No. 41 at 16.) But in *Lysengen*, the court explained that a court may take judicial notice of a fact that is indisputable. *Lysengen*, 498 F. Supp. 3d at 1017. At issue in *Lysengen* was a publicly available decision by a lower court finding that the share price was fair and negotiated in an "arm's length" process. *Id*. The court refused to take judicial notice of the lower court's decision for its truth, explaining that because "the state court's determination that the transaction was fair is not a fact and it is disputed, … judicial notice [was] inappropriate." *Id*. at 1018.

Unlike the lower court's decision at issue in *Lysengen*, Form 5500s are annual reports, filed with the U.S. Department of Labor, containing information about a plan's financial condition, investments, and operation, the purpose of which is to provide the IRS and DOL with information about the plan's operation and compliance with government regulations. Falsely completing a Form 5500 can subject a fiduciary to civil and criminal penalties. As such, the contents of a Form 5500 are "not subject to reasonable dispute" and are "capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned," *see Lysengen*, 498 F.Supp. 3d at 101. As such, this Court may take judicial notice of the Form 5500s for their truth. Extreme Engineering's Form 5500s demonstrate that the value of the stock has

increased significantly in the years following the ESOP transaction, it is illogical that this somehow translates into an injury suffered by MacTaggert here.

II. THE COMPLAINT FAILS TO STATE A CLAIM FOR BREACH OF FIDUCIARY DUTY AGAINST THE TRUSTEE DEFENDANTS.

A. MacTaggert fails to state a claim that the Trustee Defendants caused a prohibited transaction in violation of 29 U.S.C. § 1106(a).

Count I fails because MacTaggert has not plausibly alleged that the Trustee Defendants caused a prohibited transaction. Contrary to MacTaggert's assertion, merely reciting the ERISA § 406(a) elements is insufficient to state a claim. Specifically, MacTaggert incorrectly claims that, by simply alleging the § 406(a) elements, he has stated *per se* violations of ERISA and met his pleading burden. (ECF 42 at 8.) The cases MacTaggert relies on to support this argument are inapposite because those cases do not stand for the proposition that simply alleging the elements of the statute is sufficient to state a claim and survive a motion to dismiss.

For instance, in *Leigh v. Engle*, 727 F.2d 113 (7th Cir. 1984), contrary to MacTaggert's assertions, (ECF 42 at 8), the court did not rule that reciting the elements of a claim were sufficient to survive a motion to dismiss. Rather, the court in *Leigh*, reviewing a motion for summary judgment, concluded that even though the investments benefitted the plan, they were not made in the plan's interest. Instead, they were made so the defendants could consolidate corporate control. *Id*. at 118. Similarly, *McMaken v. GreatBanc Trust* Co., No. 17-cv-04983, 2019 WL 1468157 (N.D. Ill. Apr. 3, 2019) also did not involve a motion to dismiss for failure to state a claim; rather, the motion before the court was plaintiffs' motion for leave to amend the complaint. And the language MacTaggert quotes from *McMaken* has nothing to do with alleging a violation of § 406; instead, it relates to the parties' dispute over language in an indemnification agreement. (ECF 42 at 8.) By referring to *per se* liability under § 406, these courts were just reciting the standard elements—they were not applying the pleading standard for a § 406 claim.

Furthermore, the purpose for which MacTaggert cites to these cases is irrelevant because the congressional intent behind the creation of § 406(a) has no bearing on whether MacTaggert has met the minimum pleading standards here. In other words, regardless of whether § 406(a) creates *per se* liability for certain ERISA transactions,[1] plaintiffs are nevertheless required to allege *facts*—*i.e.*, more than just legal conclusions—that allow the court to reasonably infer that defendants are liable for the alleged misconduct. *Ashcroft v. Iqbal*, 556 U.S. 662, 679 (2009). MacTaggert has not done so here.

In a final attempt to save Count I, MacTaggert argues that he is not required to plead around affirmative defenses in his Complaint. (ECF No. 42 at 9.) However, the Trustee Defendants have not yet asserted that an affirmative defense bars his claim because doing so at this stage would be premature. *See Dean v. Nat'l Prod. Workers Union Severance Tr. Plan*, 46 F.4th 535, 549 (7th Cir. 2022). For these reasons, MacTaggert's argument is irrelevant.

Lastly, the Trustee Defendants agree with MacTaggert that their argument in support of dismissal of Count I is simple. That is, beyond alleging the elements of § 406(a), MacTaggert's Complaint includes no *facts* to support his claim that the Trustee Defendants caused the Plan to engage in a prohibited transaction. MacTaggert has not sufficiently pled that the Trustee Defendants' process for reviewing the proposed transaction and determining adequate consideration was flawed or that the Trustee Defendants otherwise caused the ESOP to overpay for Extreme Engineering stock. MacTaggert's Complaint is completely devoid of any facts that would tend to support its claim, including but not limited to facts concerning: (1) the Trustee Defendants' due diligence procedures; (2) the Trustee Defendants' valuation of Extreme

[1] In fact, many courts have declined to read ERISA as a *per se* rule barring all transactions between a plan and a party in interest. *See Albert v. Oshkosh Corp.*, 47 F.4th 570, 584 (7th Cir. 2022).

Engineering; and (3) the Trustee Defendants' process for negotiating the terms of the transaction. Accordingly, Count I must be dismissed for failure to state a claim.

B. MacTaggert has not sufficiently alleged a claim against the Trustee Defendants under 29 U.S.C. § 1104(a).

First, contrary to what MacTaggert suggests, the Trustee Defendants do not contend that they are entitled to a presumption of prudence with respect to MacTaggert's ERISA § 404 claim. Rather, consistent with the court's holding in *Fifth Third Bancorp v. Dudenhoeffer* (as well as *Twombly* and *Iqbal*), the Trustee Defendants contend only that, in determining whether to grant their motion to dismiss, this Court should apply a "careful, context-sensitive scrutiny of a complaint's allegations" to "divide the plausible sheep from the meritless goats." *Id.*, 573 U.S. 409, 425 (2014). Simply put, the Trustee Defendants' point is that MacTaggert's allegations against them are nothing more than meritless goats.

MacTaggert claims he does not need to plead any details concerning the Trustee Defendants' process to support his breach of fiduciary duty claim, relying on *Allen v. GreatBanc Tr. Co.*, 835 F.3d 670 (7th Cir. 2016). However, even in *Allen*, the plaintiffs pled a drop in stock price. Like the present case, *Allen* involved an ESOP transaction in which the plaintiffs alleged breach of fiduciary duty against the plan's fiduciary. The issue before the court was whether the plaintiffs sufficiently pled the elements of breach. *Allen*, 835 F.3d at 678. There, the court explained that "an ERISA plaintiff alleging breach of fiduciary duty does not need to plead details to which she has no access, *as long as the facts alleged tell a plausible story*." *Id.* (emphasis added). The court found that the plaintiffs met that burden by alleging the following facts from which a factfinder could infer that the process was inadequate:

> The plaintiffs met this burden: they alleged that the stock value dropped dramatically after the sale (implying that the sale price was inflated), that the loan came from the employer-seller rather than from an outside entity (indicating that outside funding was not available), and that the interest rate was uncommonly high (implying that the sale was risky, or that the shareholders executed the deal

> in order to siphon money from the Plan to themselves). These facts support an inference that GreatBanc breached its fiduciary duty, either by failing to conduct an adequate inquiry into the proper valuation of the shares or by intentionally facilitating an improper transaction.

Id. at 678–79. In other words, the court in *Allen* held that plaintiffs met their pleading burden by alleging: (1) a drop in stock price; (2) a loan from sellers rather than an outside entity; and (3) an unusually high interest rate. *Id*.

MacTaggert's reliance on *Placht* is similarly misplaced. Though MacTaggert is correct that the court in *Placht* found that the plaintiff sufficiently pled a breach of fiduciary claim, MacTaggert conveniently omits the additional allegations that the court relied on in coming to that determination. Again, in that case, the plaintiff alleged that that "stock valuation decreased from $9,300,000.00 five months after the sale to $8,650,000.00 in 2020." *Placht on behalf of Symbria Inc. Emp. Stock Ownership Plan v. Argent Tr. Co*., No. 21 C 5783, 2022 WL 3226809, at *8 (N.D. Ill. Aug. 10, 2022). Based in part on that allegation, the court held as follows:

> Here, the subject stock was not publicly traded, and Plaintiff asserts that the price paid did not adequately reflect its value and that the ensuing debt, financed by the Selling Shareholders, was excessive; she therefore sufficiently alleges a breach of Argent's duty of prudence, ***particularly considering the decreased valuations as Symbria continued to funnel money into the plan***. *See Allen*, 835 F.3d at 678-79 (holding that ***plaintiff met burden by alleging a drop in stock price***, a loan from sellers rather than an outside entity, and a high interest rate) …

Placht, 2022 WL 3226809, at *8 (emphasis added).

MacTaggert's Complaint contains no such allegations. Instead, as to the element of breach, MacTaggert claims it is enough that he included allegations that the Trustee Defendants breach their fiduciary duty when they "failed to appropriately and independently investigate the fair market value of the stock; failed to act independently and probe the projections and other information provided to it by Extreme Engineering management; and failed to negotiate for the Plan to pay no more than fair market value." (ECF 42 at 10) (citing Compl. ¶¶ 72-81)). MacTaggert is incorrect. Unlike the plaintiffs in *Allen* and *Placht*, MacTaggert has included no

allegations about the value of the stock; no allegations indicating that the interest rate was too high; and no allegations indicating that outside funding was not available to finance the loan. In fact, MacTaggert has not even alleged that the Trustee Defendants actually failed to undertake an investigation into the fair market value of Extreme Engineering stock; rather, MacTaggert alleges only that the Trustee Defendants were "required" to do so. (ECF No. 1 ¶ 77.) Similarly, MacTaggert alleged only that the Trustee Defendants were "required" to act independently on behalf of the Plan. (*Id.* ¶ 78.)

For these same reasons, MacTaggert fails to sufficiently allege that the Trustee Defendants acted in self-interest; received any incentives to provide an inflated valuation; or engaged in conduct that would have been imprudent. To the extent MacTaggert now claims that the indemnification agreement entered into by Extreme Engineering and the Trustee Defendants demonstrates that the Trustee Defendants acted in self-interest, that claim fails for the reasons discussed in the Trustee Defendants' opening brief and *infra*. Accordingly, Count II must be dismissed.

C. Count III must be dismissed because MacTaggert has not overcome the fact that the indemnification agreement between Extreme Engineering and the Trustee Defendants is entirely permissible.

As explained in the Trustee Defendants' opening brief, indemnification agreements that "leave the fiduciary 'fully responsible and liable' for breaches of a fiduciary obligation" are permissible. *Appvion, Inc. Ret. Sav. & Emp. Stock Ownership Plan by & through Lyon v. Buth*, 475 F. Supp. 3d 910, 945 (E.D. Wis. July 27, 2020) (quoting 29 C.F.R. § 2509.75-4). This is particularly true under circumstances in which a fiduciary succeeds in defending itself against breach of fiduciary duty claims:

> We may assume that § 410(a) nullifies any provision indemnifying a pension fiduciary who has been found liable. But Kratville was absolved, not convicted. Making a faithful fiduciary whole hardly "relieves" the fiduciary of responsibility

> or liability. Pension administrators such as Kratville should be praised, not told to write a check for $38,000, when they carry out their responsibilities properly.
>
> …
>
> And fee-shifting rules make it easier for pension plans to engage the services of persons unwilling or unable to bear the costs of legal contests.

Packer Eng'g, Inc. v. Kratville, 965 F.2d 174, 175 (7th Cir. 1992).

Here, alleging only on information and belief, and without quoting language from the indemnification agreement, MacTaggert claims that the indemnification agreement between Extreme Engineering and the Trustee Defendants violates § 410(a) and "does not contain an exemption addressing violation of the per se prohibited transaction rules under ERISA § 406." (ECF No. 42 at 12; ECF No. 1 ¶ 59.) MacTaggert is incorrect. In fact, the indemnification agreement between Extreme Engineering and the Trustee Defendants does *not* relieve the Trustee Defendants of their ERISA responsibilities and is therefore not void as against public policy. *See McMaken on behalf of Chemonics Int'l, Inc. Emp. Stock Ownership Plan v. GreatBanc Tr. Co.*, No. 17-CV-04983, 2019 WL 1468157, at *3 (N.D. Ill. Apr. 3, 2019) (citing *Wells Fargo Bank v. Bourns, Inc.*, 860 F. Supp. 709, 714 (N.D. Cal. 1994)). The indemnification agreement[2] states, in relevant part:

> 5. **Indemnification.** XES, *to the extent permitted by applicable law*, shall indemnify and hold PFS and each of its officers. Directors, principals, shareholders, and employees (individually, including PFS, an "Indemnified Party") harmless against any and all losses, claims, damages or liability, including expenses and reasonable attorneys' fees (collectively, "Losses") to which any Indemnified Party may become subject arising out of or in connection with the performance of PFS's Services *unless such Losses are adjudged by a court of competent jurisdiction to have resulted from the Indemnified Party's breach of fiduciary negligence or willful misconduct, or PFS's material breach of its obligations under this agreement*. For purposes of this agreement, any act or omission of an Indemnified Party will be negligent only if such act or omission represents a material departure from ordinary standards of care. Pursuant to the foregoing indemnification, XES will, upon notice, advance or pay promptly to or on behalf of any Indemnified Party, all reasonable attorneys' fees and other

[2] As a general rule, this Court may consider documents incorporated by reference in the pleadings. *Orgone Cap. III, LLC v. Daubenspeck*, 912 F.3d 1039, 1044 (7th Cir. 2019).

> expenses and disbursements as they are incurred; provided, however, that *PFS will promptly reimburse to XES all amounts paid to an Indemnified Party pursuant to this Agreement in the event that it is adjudged by a court of competent jurisdiction, or determined in any other proceeding mutually agreed to by the parties, that the Indemnified Party has acted in breach of its fiduciary duties or with negligence or willful misconduct with respect to the services performed pursuant to this agreement, or that PFS has materially breached its obligations under this agreement.*

(Declaration of Danielle Marocchi, Ex. 1 at ¶ 5) (italics added). The indemnification agreement further provides that the Trustee Defendants "*will be subject to the duties imposed upon a fiduciary by ERISA*" and that they will exercise their powers in their discretion as an independent fiduciary acting in compliance with applicable legal requirements. (*Id*. at ¶ 1) (emphasis added).

Thus, because the agreement requires the Trustee Defendants to act within the bounds of the duties imposed by ERISA and specifically excludes liability for breach of those duties, breach of fiduciary negligence, and any willful misconduct, the indemnification agreement does not relieve the Trustee Defendants from responsibility or liability under ERISA. As a result, MacTaggert's additional arguments that the agreement is prohibited because it equates to an impermissible indemnification by the plan itself is irrelevant. Nonetheless, courts in *this* jurisdiction have held that indemnification agreements are permissible when entered into by the trustee and the employer, not the plan. *Appvion,* 475 F. Supp. 3d at 945 ("The indemnification provisions contained in the agreements between Appvion and the Trustee Defendants are entirely permissible, as each agreement was entered into between each Trustee Defendant and Appvion, not the Plan.") Accordingly, MacTaggert fails to state a claim under §§ 404 and 410 and Count III must be dismissed.

<u>CONCLUSION</u>

For the foregoing reasons, as well as those set forth in the Trustee Defendants' opening brief, the Trustee Defendants respectfully request this Court dismiss the Complaint in its entirety.

Dated this 21st day of November, 2022.

s/ Danielle E. Marocchi
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