

Ninth Circuit: Joins Other Circuits in Holding That Reliance on General Economic Principles Without More Is Not Enough to Plead a Duty-of-Prudence Violation Under *Fifth Third*

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On April 19, 2021, the Ninth Circuit affirmed the dismissal of a putative class action alleging that an employee stock ownership plan (“ESOP”) fiduciary breached his duty of prudence because he knew that the company’s stock price was artificially inflated by undisclosed information concerning the company’s *ex parte* communications with regulators, yet he failed to disclose the information promptly, which would have allowed the company’s stock price to correct and mitigate the harm to the plan participants. [Wilson v. Craver](#), 2021 WL 1523253 (9th Cir. 2021) (Murguia, J.). The court held that plaintiff failed to state a claim for breach of the duty of prudence consistent with the standard announced in *Fifth Third Bancorp v. Dudenhoeffer*, 573 U.S. 409 (2014), because plaintiff offered no context-specific allegations explaining why an earlier disclosure would be so clearly beneficial that a prudent fiduciary could not conclude that it would be more likely to harm the fund than to help it. The court further held that relying on general economic principles (that the longer a fraud is concealed, the greater the harm to the company’s reputation and stock price), without more, was not enough to plead a duty-of-prudence violation, agreeing with the Second, Fifth, Sixth and Eighth Circuits.

The Court Sets Forth the *Fifth Third* Pleading Standard

The court stated that the “sole issue on appeal is whether [p]laintiff plausibly alleged a duty-of-prudence claim under the pleading standard announced in *Fifth Third*[.]” To allege a duty-of-prudence claim against an ESOP fiduciary under the *Fifth Third* pleading standard, “a plaintiff must plausibly allege an alternative action that the defendant could have taken that would have been consistent with the securities laws and that a prudent fiduciary in the same circumstances would not have viewed as more likely to harm the fund than to help it.” Referring to *Fifth Third*, the court explained that this is a context-specific inquiry, focused on the circumstances prevailing at the time that the fiduciary acts.

Plaintiff Claimed the District Court Applied an Impossible Standard

On appeal, plaintiff asserted that the district court applied an “impossible standard” and held that plaintiff “failed to state a duty-of-prudence claim solely because the proposed alternative—a corrective disclosure—would have caused a drop in [the company’s] stock price.” However,

the Ninth Circuit stated that plaintiff “mischaracterizes the district court’s order[]” and clarified that the district court “concluded that [p]laintiff’s [second amended complaint] failed to include context-specific allegations plausibly explaining why a prudent fiduciary in [d]efendants’ position ‘could not have concluded’ that a corrective disclosure would do more harm than good to the Stock Fund.” The court summarized plaintiff’s theory to be that no reasonable fiduciary could conclude that disclosing the truth would do more harm than good because “the longer that corrective disclosure was delayed, the greater the negative price impact would be once disclosure finally occurred[]” and that “the longer [the] fraud went on, the more damage would be done to [the company’s] reputation when the truth emerged.”

Generic Economic Principles Not Enough to Plead Duty-of-Prudence Violations

Citing decisions from the Second, Fifth, Sixth and Eighth Circuits, the court observed that “nearly every court to consider duty-of-prudence claims post *Fifth-Third* has rejected the notion that general economic principles, such as those [p]laintiff relied on, are enough on their own to plead duty-of-prudence violations.” The court pointed out that this “consensus is consistent with *Fifth Third*’s call for context-specific allegations and the Supreme Court’s stated intent to provide some protection from meritless claims.” The court held that “we join our sister circuits in concluding that the recitation of generic economic principles, without more, is not enough to plead a duty-of-prudence violation.” The court further held that “where general economic principles are alleged, the complaint must also include context-specific allegations explaining why an earlier disclosure was so clearly beneficial that a prudent fiduciary could not conclude that it would be more likely to harm the fund than help it.” The court concluded that the “district court did not err in requiring the same.”

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