[FILED UNDER SEAL]

No. 18-3310

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

FREDERICK ROZO,

Plaintiff-Appellant,

v.

PRINCIPAL LIFE INSURANCE COMPANY,

Defendant-Appellee,

PRINCIPAL FINANCIAL GROUP, INC.,

Defendant.

Appeal from the United States District Court
for the Southern District of Iowa – Des Moines
(No. 4:14-cv-00463-JAJ)

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INTRODUCTION

If, as Principal urges, this Court follows the Tenth Circuit's reasoning in *Teets v. Great-West Life & Annuity Ins. Co.*, __ F.3d __, 2019 WL 1760113 (10th Cir. Mar. 27, 2019), *revised on reh'g* (Apr. 22, 2019), Rozo wins—easily. *Teets* squarely supports Rozo's position here.

The Tenth Circuit agreed that an employee benefit plan contract is a plan asset (*id.* at *7) and that the service provider changing the interest rates is not a ministerial function (*id.* at *11 n.14). Here, Principal exercised unfettered, unilateral control over the PFIO contract by setting the interest rate that participants earn.

On the critical question of what makes the service provider a fiduciary when it adjusts that rate, the Tenth Circuit was unequivocal: "when the plan or the plan participants cannot reject the service provider's action or terminate the contract *without interference or penalty*, the service provider is a functional fiduciary." *Id.* at *8 (emphasis added). And it further explained that imposing a 12-month delay—just like the one Principal imposed on Rozo's plan and on every plan that offers the PFIO—is a penalty that renders the provider a fiduciary.

Principal is therefore a fiduciary under *Teets*'s reasoning and for the multiple other reasons Rozo's opening brief explained. As discussed below, each of Principal's responses fails.

On Rozo's (alternative) non-fiduciary claim, Principal agrees that fact disputes remain regarding whether it received reasonable compensation under a reasonable contract. That question must be put to the factfinder on remand, under the traditional rule that the defendant bears the burden of establishing affirmative defenses. Each of Principal's attempts to short-circuit that inquiry fails.

Principal argues it needed to know that its conduct actually violated the law. But *Harris Trust v. Salomon*, 530 U.S. 238, 251 (2000), requires knowledge only of the *circumstances* rendering the transaction unlawful, not that the transaction violated ERISA as a matter of law.

Principal also contends that ERISA offers no remedy for its misconduct. The district court did not address this issue, so this Court need not either. But under *Salomon*, Principal must disgorge profits that it wrongfully earned from its use of a plan asset. For ERISA's excessive-compensation bar to mean anything, it must be possible to force parties-in-interest to disgorge excessive profits. And here, Principal does not dispute that it used a plan asset (the PFIO contract) to earn profits. Thus, if the factfinder finds those profits excessive, Principal must disgorge them.

The Court should vacate and remand.

ARGUMENT

I. Because Plans And Participants Lack The Unimpeded Ability To Exit The PFIO, Principal Is A Fiduciary Under The *Teets* Analysis.

Rozo explained that summary judgment on his fiduciary claims was erroneous because there remains at minimum a fact question regarding whether plans (and participants) can exit the PFIO without impediments. Principal's chief authority—the Tenth Circuit's recent decision in *Teets*—confirms Rozo's view. Accordingly, Principal's efforts to resist fiduciary status fail.

A. A Service Provider Like Principal Is A Fiduciary If Plans Or Participants Lack The Unimpeded Ability To Exit The Fund.

Cases from around the country show that a service provider is a fiduciary unless plans have a meaningful opportunity for a costless exit. Opening Br. 20-25.

The Tenth Circuit's recent decision in *Teets* unambiguously supports *Rozo's* position, not Principal's. *Teets* held that obstacles to plans exiting the fund make the service provider a fiduciary in setting the interest rate for participants: "[W]hen the plan or the plan participants cannot reject the service provider's action or terminate the contract without *interference or penalty*, the service provider is a functional fiduciary." 2019 WL 1760113, at *8 (emphasis added); *see also id.*, at *7 (need "unimpeded ability" to exit), *9 (ability to "freely" exit), *11 (fiduciary status "if the service provider can prevent or penalize plans for" exiting).

Principal thus elides a critical aspect of *Teets* and its rule for determining fiduciary status. According to Principal, "an entity becomes a fiduciary only if it has final say over whether a proposed term will govern a participant's funds." Br. 18; *see, e.g.*, Br. 20. But *Teets* makes clear that a service provider *does* have final say if plans or participants cannot terminate the relationship "without interference or penalty." 2019 WL 1760113, at *8. Principal loses under the Tenth Circuit's rule.

B. The Restrictions On Plans' Ability To Exit The PFIO Make Principal A Fiduciary.

Here, two obstacles impede plans' ability to terminate the contract after Principal exercises its unilateral discretion to change the Composite Crediting Rate: the twelve-month delay in exiting after giving notice and the alternative 5% surrender charge. Opening Br. 26-27. It is undisputed that Principal imposed the 12-month waiting period on Rozo's plan (App. 131-132, 225), and that the surrender charge will be imposed should a plan wish to avoid that delay. Neither provision is optional. App. 131-132, 159, 225; App. 249 (Principal witness explaining Principal has "no discretion in waiving [the waiting period or surrender charge]"). Principal's attempts to brush aside these obstacles lack merit.

1. The 12-month waiting period. Teets makes this an easy case, for it held that imposing a 12-month delay definitively leads to fiduciary status: a service provider's "contractual option to delay a plan's ability to receive funds from the [defendant] upon termination of the contract, if exercised, may make it a fiduciary," and whether the provider is in fact a fiduciary turns on whether the waiting period "had been or w[as] certain to be enforced" rather than remaining an "unexercised contractual option." 2019 WL 1760113, at *11-12. The only reason *Teets* found no obstacle was because the court thought there was no evidence that the service provider there actually enforced the waiting period.

But here Principal did enforce the delay. Under *Teets*'s unambiguous reasoning, this delay in "the plan's withdrawal of funds" "'lock[s] [the plan] in' and ma[kes] the service provider a functional fiduciary." *Id.* at *8. That is the end of the matter. Rozo's plan was forced to accept the rate change for 12 months, and that restriction makes Principal a fiduciary.

Principal accuses Rozo of complaining about "Principal's potential exercise of a right it negotiated for in the PFIO contract." Br. 27. But the "potential exercise of a right it negotiated for" means that Principal negotiated for discretionary authority over an aspect of the plan. Principal's argument has been squarely rejected by courts across the country: even when "the service provider's discretionary decision making" is "authorized by contract," ERISA's fiduciary duties still "'cabin'" that discretion. *Teets*, 2019 WL 1760113, at *9 (surveying cases).

Principal distorts *Teets* in arguing that the waiting period is "'a specific contract term'" "'that is the product of an arm's-length negotiation." Br. 27-28 (quoting *Teets*, 2019 WL 1760113, at *7-8). As before, Principal excises the part of

Teets's holding it doesn't like. *Teets* pointed to a "two-step analysis," while Principal quotes only the first step. "First, courts decide whether the service provider's alleged action conformed to a specific term of its contract with the employer plan." 2019 WL 1760113, at *7. But "[s]econd, if the service provider took unilateral action beyond the specific terms of the contract respecting the management of a plan or its assets, the service provider is a fiduciary unless the plan or perhaps the participants . . . have the unimpeded ability to reject the service provider's action or terminate the relationship with the service provider." *Id.*

Expanding the second step, the court emphasized that even when the contract authorizes a "discretionary decision"—here, Principal's unilateral discretion to set the Composite Crediting Rate—the service provider "is 'cabined by ERISA's fiduciary duties' unless plans or participants can freely reject the service provider's choices or terminate the contract." *Id.* at *9. The provider is thus a fiduciary if it exercises its "rights to impose penalties." *Id.* at *11. It is irrelevant that the contract provides those rights; by impeding plan exit, they allow Principal to bind plans to its discretionary rate-setting decision. That makes Principal a fiduciary.

2. *Surrender charge.* Even if Principal didn't impose the waiting period, the plan's only other option would be paying the 5% surrender charge, an obvious "penalty." *Id.* at *8.

Principal argues again that the surrender charge is merely a contractual term that "is no different than any other price term of the contract." Br. 26. The case law again forecloses Principal's argument. The surrender charge here mirrors the "surrender charge" in *Midwest Cmty. Health Serv., Inc. v. Am. United Life Ins. Co.*, 255 F.3d 374, 375 (7th Cir. 2001), and it is exactly the "built-in penalt[y]" that engendered fiduciary status in *Charters v. John Hancock Life Ins. Co.*, 583 F. Supp. 2d 189, 199 (D. Mass. 2008). *See Teets*, 2019 WL 1760113, at *7, 8-9, 12 (approving these cases). Principal cannot evade those decisions.

Knowing the surrender charge makes it a fiduciary under this unequivocal authority, Principal tries to morph the charge into something less problematic. Principal claims the surrender charge is no different from a plan sponsor "pay[ing] a certain amount up front for the right to exit at any time." Br. 27. But this hypothetical gets Principal nowhere, because Rozo's plan actually had to endure the waiting period. Under *Teets*, that delay alone makes Principal a fiduciary.

In any event, an up-front payment provides different incentives for the service provider than does a surrender charge. With a surrender charge, the service provider can favor its own profit whenever it changes the rate, because the plan faces a significant impediment to terminating. But with an up-front payment, the service provider can only impose the most favorable rate changes, because otherwise the plan will freely exit—the plan already paid for the ability to terminate, so it faces no deterrent to terminating after a rate change. Thus, a surrender charge, unlike an up-front payment, locks plans in and subjects them to the service provider's whims. That is exactly why, as *Teets* discusses, cases uniformly hold that termination penalties give rise to fiduciary status. 2019 WL 1760113, at *8-9. The same is true here.[1]

C. Participants' Ability To Exit The PFIO Is Legally Irrelevant, But Regardless They Also Face Impediments To Exiting.

1. Participants' ability to exit the PFIO is legally irrelevant to the fiduciary inquiry; accordingly, the restrictions on plans' ability to terminate their contracts suffice to require reversal. Opening Br. 27-30; *see Teets*, 2019 WL 1760113, at *8 ("when the plan *or* the plan participants cannot reject the service provider's action or terminate the contract" (emphasis added)); *id.* at *7 (plans *and* participants need "unimpeded ability" to exit), *11 (provider is a fiduciary "if the service provider can prevent or penalize *plans* for" exiting (emphasis added)).

Principal maintains that it cannot be a fiduciary if participants are savvy enough to "escape any rate they dislike." Br. 23. Principal is wrong. The basic flaw in Principal's position is that ERISA aims to protect participants, not treat them as market actors on equal footing with service providers or plans. ERISA does not

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[1] Principal also attempts to recharacterize the PFIO as a series of offers that plans can accept or reject. Br. 19-20. That is wrong. Plans are *automatically bound* by Principal's new "offers," and can "reject" them only by waiting 12 months or paying the penalty. App. 131-132, 225, 249.

contemplate participants having to outmaneuver entities who "'affect the amount of benefits retirement plan participants will receive.'" *Teets*, 2019 WL 1760113, at *11 n.14 (quoting *John Hancock Mut. Life Ins. Co. v. Harris Tr. & Sav. Bank*, 510 U.S. 86, 96 (1993)). Rather, recognizing "the lack of . . . adequate safeguards concerning [plans'] operation," Congress imposed its own "safeguards." 29 U.S.C. § 1001(a). It imposed those restrictions on any entity that exercises control over participants' benefits. 29 U.S.C. § 1002(21)(A).

Rozo's point is confirmed by considering the status of service providers selecting the investments available to plan participants. Opening Br. 28-29. It is settled that "[f]iduciary status attaches to the party empowered to make unilateral changes to the investment menu by its contractual arrangement with the plan." *Teets*, 2019 WL 1760113, at *9 (quoting *Rosen v. Prudential Ret. Ins. & Annuity Co.*, 718 F. App'x 3, 5 (2d Cir. 2017)); *Howell v. Motorola, Inc.*, 633 F.3d 552, 567 (7th Cir. 2011). If that provider picked a terrible investment option, the participant could freely choose a different investment from the menu. But that participant's choice would still leave the provider a fiduciary. *See id.*[2]

[2] Principal incorrectly asserts that in the menu-selection cases, the entities had "already been determined to be fiduciaries." Br. 25. On the contrary, the cases examine which decisions are "acts to which fiduciary duties *attach*." *Howell*, 633 F.3d at 567 (emphasis added).

Principal tries to dodge the implications of that straightforward analogy. It blithely explains that it lacked "authority over whether the PFIO was placed on the menu of options." Br. 24. That obviously was not the point of Rozo's analogy to the menu-selection cases. Principal has no response to the unavoidable inference from those decisions: simply because a participant can avoid a service provider's inclusion of a bad investment doesn't mean fiduciary duties haven't attached to that provider. Likewise, even if participants can exit the PFIO if they dislike Principal's chosen interest rate, that capability doesn't forestall Principal's fiduciary status. Principal still exercised control over the PFIO contract, a plan asset.[3]

Principal insists that multiple cases support its position, but it misreads them. Br. 23. Each case turned on the *plan*'s ability to override the provider's decisions. Not one relied on participants' ability to change investments to conclude that otherwise discretionary decisions were not fiduciary in nature. *See Scott v. Aon Hewitt Fin. Advisors*, No. 17 C 679, 2018 WL 1384300, at *8 (N.D. Ill. Mar. 19, 2018) (provider "was not a fiduciary when it negotiated at arm's length with [the *plan*] and did not have [ongoing] control over its compensation"; although "fees were tied to the number of plan participants," whether those participants could

[3] Principal notes that fiduciary duties "run to a plan's participants and beneficiaries, not merely to the plan itself." Br. 22 (citing 29 U.S.C. § 1104(a)(1)). But the definition of fiduciary—*i.e.*, the issue presented here—speaks in terms of being a fiduciary "with respect to a *plan*" and controlling the *plan*'s "assets." 29 U.S.C. § 1002(21)(A).

"approve" provider's decisions was irrelevant); *Patrico v. Voya Fin., Inc.*, No. 16 Civ. 7070, 2017 WL 2684065, at *3 (S.D.N.Y. June 20, 2017) (similar); *Fleming v. Fidelity Mgmt. Tr. Co.*, No. 16 Civ. 10918, 2017 WL 4225624, at *5 (D. Mass. Sept. 22, 2017) (defendant not a fiduciary because "the Delta entities [the *plans*], not Defendants, retained control," because "Delta [did not] lack[] the authority or ability to [overrule Defendants' decision] if it determined that the share classes . . . were unsuitable for Plan participants"); *Chendes v. Xerox HR Solutions*, No. 16-13980, 2017 WL 4698970, at *4-5 (E.D. Mich. Oct. 19, 2017) (defendant lacked ability "to exercise discretion in how much money it received *from the Plans*"; although defendant's compensation "was based on factors [including] the number of participants who used [its] services," fiduciary status turned on *the plans*' arm's-length negotiation).[4]

At bottom, Principal's argument that participants must fend for themselves fundamentally misunderstands ERISA's remedial scheme.

2. In all events, even if participants' unimpeded ability to exit the PFIO could theoretically relieve Principal of fiduciary status, participants do face obstacles to

[4] Principal similarly cannot control how many participants invest in the PFIO. But Principal also has ongoing control over the Composite Crediting Rate, which plans cannot override. None of the defendants in Principal's cases had a comparable power—precisely why they weren't fiduciaries.

withdrawing. Principal's response mischaracterizes the evidentiary record and underscores that, at minimum, material fact disputes remain.

a. The equity wash penalizes participants by making them either (i) continue with a Composite Crediting Rate change they dislike or (ii) pick an investment with a materially higher risk profile. Principal responds that the equity wash "merely narrows the potential destinations for withdrawn money." Br. 30. That reply ignores the importance of risk attributes for an investment. As Principal's amicus explains, an investment's risk profile is a critical factor for retirement savers. ACLI Br. 4-5, 8; *see, e.g.*, Br. 1 ("[t]he PFIO provides a virtually risk-free option"). Yet Principal limits access to other low-risk products through the equity wash.

Nonetheless, Principal asserts there is "no evidence" that the equity wash deters participants from moving their money. Br. 31. But Rozo adduced expert testimony on that very point, creating a genuine fact dispute for trial. App. 451-453; App. 124-126. Put simply, having to shoulder unwanted risk to avoid an unfavorable rate change *is the penalty* that impedes exit. *See id.*[5]

Principal also misstates the summary-judgment evidence in suggesting that participants annually withdrew hundreds of millions of dollars from the PFIO. Br. 31. Rozo objected to that evidence because (among other reasons) Principal's

[5] Principal offers zero support for its suggestion that a participant exiting the PFIO "will likely be looking for a different risk profile." Br. 31-32. As investors age, they become *more*, not *less*, risk-averse. ACLI Br. 4-5.

witness could not even identify where the data came from. App. 121. More importantly, Principal admits that those amounts *include plan-level withdrawals*—which indisputably incurred the waiting period or 5% penalty. App. 121. Principal cannot rely on unreliable, disputed evidence about participant withdrawals to obtain summary judgment.

Principal also notes that Rozo's plan lacked a "competing" investment option, so the equity wash didn't apply. Br. 31. But Principal ignores that it offers the PFIO under only two circumstances: either the plan agrees not to include competing investments at all, or its participants must face the equity wash. *See* Amin Decl., Ex. 5, D. Ct. Dkt. No. 110 at 238 (testimony of Dr. Kopcke). Either way, participants confront the same situation: move to a riskier investment or suffer a negative rate change.

Moreover, Principal doesn't deny that the equity wash prevents participants in other plans within the class from moving money to an investment with the same risk profile as the PFIO, and Principal "[a]dmit[s]" that it "strictly adhered to" the equity wash. App 156. Again, the whole point of the equity wash is to prevent participants from exiting the PFIO, because Principal knows how crucial an investment's risk profile is.

b. The stampede provision impedes exit because it generates a 5% surrender charge on the plan. Opening Br. 31. Principal asserts that the charge is incurred by the plan, not the participants (Br. 29-30), but that makes no sense. Plans don't have their own free-floating money; the nature of a 401(k) plan is that it consists of participant funds. When a plan pays the charge, it comes from the participants.

Principal also argues that the stampede provision has never been imposed. Br. 30. But that flatly ignores record evidence to the contrary. App. 128-131.

Principal's final retort—that paying 5% doesn't actually *stop* anyone from exiting—again misunderstands the relevant inquiry. A "penalty" upon termination still makes the provider a fiduciary, even if the termination goes through. *Teets*, 2019 WL 1760113, at *8.

c. Participants also face practical obstacles. Opening Br. 31-32. Principal cannot avoid those impediments on summary judgment. *Cf. Phones Plus, Inc. v. The Hartford Fin. Servs. Grp., Inc.*, Civ. No. 3:06CV018356(AVC), 2007 WL 3124733, at *4 (D. Conn. Oct. 23, 2007) ("Regardless of whether Phones Plus has the power to make the 'ultimate decision' about Hartford's changes to the fund menu, a reasonable factfinder could still conclude, for example, that the change notification procedures are inadequate or that the time provided in which to make such a decision is unreasonably short, and that as a result Hartford is an ERISA fiduciary.").

Most notably, Principal disputes that participants do not typically move their assets once allocated to a certain investment, saying "[t]his speculative argument lacks evidence." Br. 33. But Principal's own expert testified that 401(k) participants seldom move their assets once they allocate them to a certain investment. App. 252. Principal exploits this inertia—underscoring why ERISA does not treat participants as co-equal market actors to large investment companies, but rather protects participants by imposing fiduciary duties on those who control plan assets.[6]

D. Principal Also Exercises Control Over Its Own Compensation.

Principal's control over its compensation, *i.e.*, its profit from the "spread," also makes it a fiduciary, for largely the same reasons already discussed. Opening Br. 33.[7]

To obtain fiduciary status, Principal need not control every single input that could affect its compensation; what matters is whether it controls "factors that

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[6] Principal also misapprehends Rozo's point about tax penalties on 401(k) withdrawals. Br. 32. These penalties deter participants from escaping the equity wash by withdrawing funds from their 401(k) altogether. That does not mean "*all* entities who offered products or services to 401(k) plans would be fiduciaries." *Id.* Rather, entities who impose transfer restrictions like the equity wash cannot escape fiduciary status by arguing that participants could withdraw their money altogether.

[7] Principal misreads (at 34-35) the Department of Labor's suggestion that "'spread' is not treated as compensation." Amendment to Prohibited Transaction Exemption (PTE) 84-24, 81 Fed. Reg. 21147, 21167 n.62 (Apr. 8, 2016). That treatment was only "[f]or purposes of [that] exemption." As *Teets* explained, "that same regulation states that 'compensation' under § 408(b)(2) includes 'indirect compensation received from any source other than the plan or IRA in connection with the recommended transaction,' which could conceivably include the money [Principal] earns on [PFIO] investments." 2019 WL 1760113, at *14 n.19. And the regulation governing the § 1108(b)(2) exemption that Principal raises explains that "[c]ompensation is anything of monetary value," and "'[i]ndirect' compensation is compensation received from any source other than the covered plan," which can "be

determine the actual amount of its compensation." *F.H. Krear & Co. v. Nineteen Named Trs.*, 810 F.2d 1250, 1259 (2d Cir. 1987). There is no dispute that Principal sets the Composite Crediting Rate, which is the most important "factor" in determining Principal's compensation from the PFIO. Even if plans and participants could freely exit, while they remain invested in the PFIO, Principal's decisions about the Composite Crediting Rate (which are undisputedly discretionary) affect its compensation. That is all that is required. *Am. Fed'n of Unions Local 102 Health & Welfare Fund v. Equitable Life Assurance Soc. of the United States*, 841 F.2d 658, 663 (5th Cir. 1988) (service provider's "rate of compensation was directly linked to his discretionary activities").[8]

Moreover, the fact that Principal fails to disclose the size of its margin means that plans (and participants) lack any meaningful opportunity to reject Principal's decision about its own compensation. Indeed, Principal's compensation is so opaque that even the parties' experts disagreed about the amount of Principal's profits. Therefore, contrary to Principal's contention (Br. 35-36), there is at least a fact issue

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expressed as a monetary amount, formula, [or] percentage of the covered plan's assets." 29 C.F.R. § 2550.408b-2(c)(1)(viii)(B). Finally, Principal waived this argument by never raising it below—indeed, Principal accepted that spread qualified as compensation. Principal Mot. for Summary Judgment (MSJ) 12-13.

[8] This is also true regarding the Composite Crediting Rate that participants earn. While plans and participants remain in the PFIO, it is undisputed that Principal has unilateral control over the Rate.

regarding whether the amount of Principal's spread affects plans' (and participants') choices to stay in the PFIO.[9]

II. The District Court Erred In Granting Summary Judgment To Principal On The "Party-In-Interest" Claim.

Principal concedes that fact disputes remain regarding whether it received more than reasonable compensation under a reasonable contract. (Nor did it seek summary judgment on this basis.) It argues instead that (1) it needed to know not only of the *circumstances* rendering its transactions with the plans illegal, but also that those transactions were illegal *as a matter of law*, (2) this Court should abandon the traditional rule that defendants bear the burden of proving affirmative defenses, and (3) even though ERISA bars parties-in-interest from receiving excessive profits, ERISA offers no remedy to actually recover those profits. Principal's arguments are incorrect.

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[9] Principal concludes its discussion of Rozo's fiduciary claims by alleging that accepting Rozo's position would "[e]ffectively [b]an" guaranteed-benefit policies. Br. 36-39. Principal attacks a strawman. Under *Teets*, Principal becomes a fiduciary by retaining unilateral discretion over the interest rate and then imposing obstacles to exiting the PFIO. 2019 WL 1760113, at *8-11. Principal need not have imposed obstacles to withdrawal. Nor did it need to retain discretion over the interest rate at all—the PFIO contract could have established a non-discretionary formula governing changes in the rate. Nowhere does ERISA "explicitly authorize[]" (Br. 36) service providers to unilaterally reduce participants' benefits, while imposing impediments to terminating the providers' contracts in response. *See also* Opening Br. 34 n.5 (addressing 29 U.S.C. § 1101(b)(2)).

A. Principal Knew Of The *Circumstances* Rendering Its Transactions With The Plans Unlawful—And That Is All That Is Necessary.

Resolution of the party-in-interest claim comes down to the meaning of *Harris Trust v. Salomon*, 530 U.S. 238 (2000). And Principal's argument about *Salomon*'s meaning is wrong.

1. *Salomon* does not say that the party-in-interest must have "knowledge that the [transaction] was unlawful." Br. 41 (capitalization omitted). *Salomon* says that the party-in-interest must have "actual or constructive knowledge of the *circumstances* that rendered the transaction unlawful." 530 U.S. at 251 (emphasis added). That is a crucial difference. A *circumstance* is a "*fact*, *event*, or *condition*, such as a *piece of evidence* that indicates the probability of an event." *Circumstance*, *Black's Law Dictionary* (8th ed. 2004) (emphasis added). Thus, knowledge of the circumstances that rendered the transaction unlawful means knowledge of the facts, events, conditions, or evidence that rendered the transaction unlawful.

Principal's contrary "reading" entirely fails to engage with what *Salomon* actually says. Br. 40-45. Principal's only discussion of *Salomon*'s language is its assertion that *Salomon* "emphasized the importance of 'setting limits' on the potential liability of parties in interest under Section 1106(a)." Br. 41 (quoting *Salomon*, 530 U.S. at 251) (brackets omitted). But again, Principal misstates *Salomon*, pulling two words out of a passage that actually supports *Rozo*:

> The common law of trusts . . . plainly countenances the sort of relief sought . . . here. It also sets limits on restitution actions against defendants other than the principal "wrongdoer." Translated to the instant context, a transferee of ill-gotten plan assets may be held liable, if the transferee (assuming he has purchased for value) knew or should have known of the circumstances that rendered the transaction prohibited.

Salomon, 530 U.S. at 251 (citations omitted). The "limit" is that the party-in-interest must know "of the circumstances that rendered the transaction prohibited." *Id.*

That means Principal is liable if it had actual or constructive knowledge of the *facts, events, conditions, or evidence* ("circumstances") that rendered its compensation *more than reasonable* ("prohibited"). And here, there is no question that Principal possessed all the facts surrounding its compensation.

2. Contrary to Principal's contention (Br. 43-44), § 290 of the Second Restatement of Trusts confirms this reading of *Salomon*. Principal again mischaracterizes what the provision actually says:

> If the trustee . . . transfers trust property to a person who knows the circumstances which make the transaction illegal, the transferee does not hold the property free of the trust, although he had no notice of the trust.
>
> . . . .
>
> *Mistake of law or fact.* The rule stated in this Section is applicable if the transferee knows the circumstances which make the transaction illegal, even though he does not know that as a matter of law it is illegal. The rule is not applicable, however, unless the transferee knows the circumstances which make the transaction illegal.

Restatement (Second) of Trusts § 290 & cmt. b. The Restatement thus confirms *Salomon*'s holding that a party-in-interest must know the facts, not the law.

Nor do Principal's cases counsel a different result. The only appellate decision it cites was decided almost a decade before *Salomon* and did not even address non-fiduciary liability under § 1106(a). *See Diduck v. Kaszycki & Sons Contractors, Inc.*, 974 F.2d 270 (2d Cir. 1992) (addressing claim under § 1104). As a district court in the Second Circuit recently explained: "The Court declines to extend the *Diduck* standard to the context of § [11]06 claims, given its apparent inconsistency with [*Salomon*], which requires knowledge of only the *factual* circumstances underlying the violation of the law." *Haley v. Teachers Ins. & Ann. Assoc. of Am.*, No. 17 Civ. 855 (JPO), 2019 WL 1382648, at *7 (S.D.N.Y. Mar. 27, 2019).

As for Principal's out-of-circuit district-court decisions, they either did not require knowledge of illegality or failed entirely to cite *Salomon*. *See Hans v. Tharaldson*, No. 3:05 Civ. 115, 2011 WL 7179644, at *16-17 (D.N.D. Oct. 31, 2011) (asking whether the defendant "had actual or constructive knowledge of the circumstances rendering the transaction unlawful" and granting summary judgment because the defendant lacked "access to the [relevant] information"); *Carlson v. Principal Life Ins. Co.*, No. 01 Civ. 481 (JFB), 2006 WL 2806543, at *5 (E.D.N.Y. Sept. 28, 2006) (discussing whether "Principal learned of the *circumstances* allegedly rendering the transaction unlawful" (emphasis added)); *Kalan v. Farmers*

& Merchants Tr. Co. of Chambersburg, No. 15 Civ. 1435, 2016 WL 2087360, at *2 (E.D. Penn. June 2, 2016) (acknowledging that *Salomon* requires "actual or constructive knowledge of the circumstances that rendered the transfer wrongful," but finding the complaint's allegations too conclusory); *Mejia v. Verizon Mgmt. Pension Plan*, No. 11 Civ. 3949, 2011 WL 1565336, at *12 (N.D. Ill. May 2, 2012) (conclusory analysis failing to cite *Salomon*). These cases do not help Principal.

3. Among courts that address *Salomon*, the weight of authority supports Rozo. Most recently, the Southern District of New York held that the "non-fiduciary transferee defendant must have knowledge of certain facts underlying the prohibited transaction, but need not have knowledge that the transaction violated ERISA, to be liable under § [11]06(a)." *Haley*, 2019 WL 1382648, at *7. The court arrived at this conclusion by simply reading what *Salomon* actually says. *Id.* at *6 ("the most natural reading of 'actual or constructive knowledge of the circumstances that rendered the transaction unlawful' requires knowledge of the underlying *factual* circumstances relevant to lawfulness, not knowledge of the *legal conclusion* that the transaction was unlawful." (quoting *Salomon*, 530 U.S. at 251)).[10]

[10] *Haley* also explained *Salomon*'s express rejection of Principal's argument that non-fiduciaries should be held to a more lenient standard than fiduciaries. 2019 WL 1382648, at *7 n.6.

And while *Neil v. Zell*, 753 F. Supp. 2d 724, 731 (N.D. Ill. 2010), addressed a fiduciary's liability, it reasoned from *Salomon*'s holding that a non-fiduciary need only know "the details of the transaction," not that the transaction was illegal as a matter of law. This reading, again, comes straight from *Salomon*. *See id.* And it is far more persuasive than Principal's, which simply ignores a crucial part of *Salomon*'s standard.[11]

B. Principal Bears The Burden Of Showing It Meets The Section 1108 Affirmative Defense.

Rozo indisputably carried his burden of showing that Principal knew of the circumstances rendering its transactions with the plans unlawful. Principal thus bears the burden to show that a § 1108 affirmative defense applies. That means Principal will have to prove on remand that it received reasonable compensation under a reasonable contract. 29 U.S.C. § 1108(b)(2).

This circuit and every other to address the issue agree that the defendant bears "[t]he burden of proof" on "whether an exception applies under § 1108." *Fish v. Greatbanc Tr. Co.*, 749 F.3d 671, 685-86 (7th Cir. 2014); *Braden v. Wal-Mart*

[11] Principal falsely asserts that the district court held "in the alternative" that Rozo's claim failed even under Rozo's theory of *Salomon*. Br. 45 (citing App. 051). The court held only that Principal did not know "that the transaction violated ERISA." App. 051 ("The fact that Rozo's expert claims the compensation is unreasonable does not mean Principal thought it was unreasonable."). Principal cannot dispute that it knew "the details of the transaction." *Neil*, 753 F. Supp. 2d at 751. Nor did Principal seek summary judgment on this basis.

Stores, Inc., 588 F.3d 585, 600-01 & n.10 (8th Cir. 2009); *Allen v. GreatBanc Tr. Co.*, 835 F.3d 670, 676 (7th Cir. 2016) (collecting cases).

Principal calls these cases irrelevant because they involved suits against fiduciaries. Br. 45-47. But the cases turn not on fiduciary status, but on the fact that "section [11]08 exemptions are affirmative defenses for pleading [and 'burden of persuasion'] purposes, and so the plaintiff has no duty to negate any or all of them." *Allen*, 835 F.3d at 676. Principal offers no reason that affirmative defenses should function differently under ERISA than under any other area of law. *See Haley*, 2019 1382648, at *4 (rejecting this distinction).

Principal also argues that it, somehow, does not have more information than Rozo about whether a defense under § 1108 applies, undermining *Braden*'s rationale vis-à-vis non-fiduciaries. Br. 47; *see Fish*, 740 F.3d at 685-86. That makes no sense: Principal's alleged exemption is that it received reasonable compensation under a reasonable contract, and Principal does not dispute that it is the *only* entity with full knowledge of its compensation. *See Braden*, 588 F.3d. at 602 ("It would be perverse to require plaintiffs bringing prohibited transaction claims to plead facts that remain in the sole control of the parties who stand accused of wrongdoing."). The reasons underlying the traditional allocation of the burden on affirmative defenses apply with full force here.

C. Principal Does Not Contest That Fact Disputes Remain Regarding Whether It Received Reasonable Compensation Under A Reasonable Contract.

Principal did not seek summary judgment on the basis that it received reasonable compensation under a reasonable contract. Nor does it argue on appeal that this provides an alternative basis to affirm the district court's decision. This question must be litigated at trial on remand.

To be clear, however, Rozo did not waive the argument that the PFIO contract violates DOL Regulation 408b-2, which says a contract is not reasonable under § 1108(b)(2) unless it "permits termination by the plan without penalty to the plan on reasonably short notice." 29 C.F.R. § 2550.408b-2(c)(3). Rozo could not waive his response to an argument that Principal did not make.[12]

Rozo raised the regulation in his opening brief to illustrate the factual disputes that must be litigated on remand. Opening Br. 42-44. Principal agrees that this inquiry involves "inherently factual questions." Br. 50 (citation omitted). It must be resolved at trial.

[12] Regardless, "[a]s the Supreme Court has made clear, it is claims that are deemed waived or forfeited, not arguments." *United States v. Pallares-Galan*, 359 F.3d 1088, 1095 (9th Cir. 2004).

D. ERISA Offers Rozo A Remedy For Principal's Violation.

Finally, Principal argues that, even if it violated the law, Rozo is without a remedy. That is wrong—but because the issue was not adequately presented in the district court, this Court should not address it first.

1. The district court did not address the remedy question, and Principal raised it in one cursory paragraph at the end of its summary-judgment motion. Principal MSJ at 20. The remedy issue is accordingly not adequately developed for appellate review.

For example, although Principal disputes Rozo's ability to obtain *monetary* relief, it has never contested Rozo's ability to obtain *injunctive* relief, which is indisputably "appropriate equitable relief." *See* App. 068. Rozo could thus obtain an injunction barring Principal from enforcing its unlawful penalty and lock-in provisions, regardless of his ability to obtain monetary equitable relief. That alone precludes affirming on Principal's alternative argument on appeal. The proper course is thus to allow the district to address the entire remedy question on remand.

2. In any event, Principal's argument that Rozo cannot obtain monetary equitable relief is wrong. Incredibly, in its four-page discussion of the issue, Principal does not even cite *Salomon*, the controlling Supreme Court decision establishing the remedies available against parties-in-interest.

a. *Salomon* held that when a party-in-interest wrongfully uses a plan asset for its own benefit, "the trustee or beneficiaries may then maintain an action for restitution of the property (if not already disposed of) or disgorgement of proceeds (if already disposed of), and disgorgement of the third person's profits derived therefrom." 530 U.S. at 250. This holding is pellucid: an ERISA plaintiff can obtain disgorgement of the profits that a party-in-interest derives from its use of a plan asset in violation of ERISA.

Interpreting *Salomon* and the equity treatises, *Teets* held the same. Appropriate equitable relief includes the recovery of "profits due from [the defendant's] use of [the plaintiff's] property." 2019 WL 1760113, at *18 (quoting 1 Dan B. Dobbs, *Dobbs Law of Remedies* § 4.3(5) at 608)). The plaintiff simply must identify property that "(1) rightfully belonged to him [*i.e.*, a plan asset] and (2) was used to generate unlawful profits." *Id.* at *21.[13]

Nor does it matter if the defendant has commingled those profits with its general account. A plaintiff may "recover profits produced by the defendant's use of that property [the plan asset], even if he cannot identify a particular *res* containing the profits sought to be recovered." *Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 214 n.2 (2002); *Teets*, 2019 WL 1760113, at *21 ("[T]he profit

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[13] The Tenth Circuit believed that the plaintiff in *Teets* had not identified the plan asset from which the defendant unlawfully derived profits. 2019 WL 1760113, at *21.

generated from the property need not be contained in a specifically identifiable *res.*"); *see also id.* at *19 (collecting authority).

b. In short, an ERISA plaintiff must identify a plan asset that the party-in-interest used to generate unlawful profits. That is precisely what Rozo has done here—Principal used the PFIO Contract (a plan asset) to generate excessive profits in violation of ERISA's prohibited-transaction rules. In the district court's words: "Rozo alleges that 'Principal used the Contract (which is a plan asset) on an ongoing basis . . . and retain[ed] the spread in violation of ERISA § 406(a).'" App. 050. Under *Salomon*, Rozo thus may sue for "disgorgement of [Principal's] profits derived" from its use of the PFIO contract. 530 U.S. at 250.

Principal's position not only contradicts *Salomon*, it would eviscerate ERISA's prohibited-transaction rules. These rules bar parties-in-interest from making unreasonable profits using a plan asset. Opening Br. 35-38. If a plaintiff cannot sue to disgorge such profits, this prohibition has little effect. The Court should not interpret ERISA's prohibitions to be self-defeating. *Cf. Pender v. Bank of Am. Corp.*, 788 F.3d 354, 365 (4th Cir. 2015) ("[i]f [ERISA]'s proscription against decreasing accrued benefits is to have any teeth, the available remedies must be able to reach situations like the one this case presents").

If the Court reaches the issue, it should hold that Rozo may disgorge profits that Principal wrongfully earned from using the PFIO Contract.

CONCLUSION

The Court should vacate and remand.

Dated: April 24, 2019

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I, Peter K. Stris, hereby certify that this document complies with the type-volume limitation of Federal Rule of Appellate Procedure 32(a)(7)(B)(ii) as it contains 6,477 words, excluding the parts of the document exempted by Rule 32(f). I further certify that this document complies with the format, typeface, and type-style requirements of Rules 32(a)(4)-(6).

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CERTIFICATE OF SERVICE

I, Peter K. Stris, hereby certify that on April 24, 2019, I filed the foregoing document under seal with the Clerk of the Court for the United States Court of Appeals for the Eighth Circuit via U.S. first-class mail, as provided in Eighth Circuit Rule 25A(h). I further certify that I have served counsel of record for Appellee via U.S. first-class mail at the following addresses:

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