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Panel and Audience Dialogue

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PANEL AND AUDIENCE DIALOGUE

The members of Volume 68 have excerpted questions and answers from the panel and audience dialogue that transpired on the day of the Symposium. In this sampling of the proceedings, Jeanne Cullinan Ray, Michael S. Sirkin, and Norman P. Stein discuss the case of Guidry v. Sheet Metal Workers National Pension Fund and address the principle of anti-alienation, the fiduciary duties of trustees, and the effects of bankruptcy law on pension plans. They conclude that the laws will continue to favor pensioners, but that the issues must still be resolved in the courts. In addition, David George Ball discusses the role and position of pension funds in the financial markets, the concept and effects of economically targeted or social investing, and the government's attraction to the trillion-dollar pension establishment. Mr. Ball concludes that the funds should not be redistributed to allay social and economic problems. Rather, he states that managers must maximize their returns to benefit plan participants and not politicians.*

THE AUDIENCE: Mr. Ball, you seem very enthusiastic about the increased authority of institutional investors. Do you see any downside to their increased influence in the marketplace?

MR. BALL: On the contrary, I do not believe that there was any real representation of pensioners during the 1970s and perhaps the early 1980s. At that time, investors generally spoke with management and, if unsatisfied, the investors withdrew their moneys. That was the Wall Street rule, and there was no economic democracy. The chairs were not being voted; the pensioners were not being represented.

THE AUDIENCE: To follow up on that question, do you believe that pension funds are seeking the same type of performance that other shareholders demand, or do they have more of an interest in long-term performance?

MR. BALL: Again, I think pension funds will have a beneficial effect because the pressure on the chief executive, of course, is earnings. This tends to focus matters on short-term profits. Pension funds have a long horizon because the pension funds are pro-

* Professor of Law, University of Alabama School of Law. Professor Stein participated in the Symposium and Panel and Audience Dialogue.

viding for somebody to retire in thirty-five years, so they can afford to be patient investors.

THE AUDIENCE: Do you think that pension funds will seek a more limited involvement because of the insider trading rules and concerns about fiduciary responsibility?

MR. BALL: As I said in my speech, fund managers are unlikely to put their own people on the board. I think what they will do is drive for independent directors. A separation is very valuable because, after all, directors have their own rules that are going to guide them in board decisions, so I think these concerns would have a beneficial effect. I do not think it is going to be a negative. You cannot be more focused on short-term results than we are at the moment. Thus, the effect is likely to allow management to have more time. The pension funds are not going to dump a new CEO in three months if he has a bad quarter; they are going to give him a chance.

THE AUDIENCE: Thus far pension funds activism has come primarily from public funds. Why do you think that is the case?

MR. BALL: It is true that the leadership has come mostly from the public plans. Public plans, I suppose, are political institutions and have been more willing to be proactive. But as I suggested with TIAA-CREF, with Campbell's Soup, with the big corporations that have joined the councils of institutional investors—General Motors and other large companies—there is going to be a ripple effect. Public plans have provided the leadership, but it is going to ripple through the marketplace. There is some evidence that that is already happening, but it will be slow, occurring over the next ten to fifteen years.

In addition, a lot of the private funds use outside money managers and investment managers. These outside managers are worried about current results and whether they are going to be replaced. They have a lot less incentive or direction other than to make returns. To a large extent, therefore, money managers are taking a secondary seat to the internally managed funds. General Motors, for example, is doing a lot of internal management and they pursue a more long-range goal. I think you will probably see a bigger role as there is more internal management of plans.

The bottom line of this whole thing is that the proxy is an asset, and if you are intelligent in the way you vote your proxy you can add value to your investment. This is not just a rule for public plans, it is equally true for private plans. Private plans are beginning to realize that how they vote their shares effects the value of their investments.

THE AUDIENCE: The concept of social investing is not a new one; it has been around for some time. But many people seemed to believe that social investing and section 404 of ERISA and fiduciary responsibility were contradictions in terms. Do you see that philosophy changing within the Department of Labor?

MR. BALL: You raise a good question, one that is very relevant to the Clinton administration. In the campaign, President Clinton talked about economically targeted investing, which is a form of social investing, where pension plans might be required to invest a part of their portfolio in the infrastructure—bridges, public buildings, sewers, and prisons. He has since retreated from that position because he realized it would constitute a flagrant violation of ERISA.

The fiduciary's duty and sole purpose is to consider only what is in the best interests of the plan participants and beneficiaries, and not what is good for society. It is not going to be reassuring to senior citizens who are collecting their pension check when they suddenly discover that they got less money and the fiduciary says, "Well, you really ought to feel good about this because we used that money for social investing. We put it in for some wonderful things in the community and we built some highways. But you are going to have a little less pension money." Those senior citizens are going to be mad.

The Clinton administration and also Helena Burr, my successor, have backed off, making social investing voluntary. There is no change once it is voluntary. You decide where you will invest. If you find two equal investments and one of them is socially redeeming, that is fine. But you may not use that money for a social or political purpose. Basically, your job is to maximize. You have to remember that the money belongs to the pension plan and not to the politicians.

MR. STEIN: I have a question about economically targeted investments. I agree that it would violate ERISA, but is there an argument that we should require some dedication of assets to certain kinds of infrastructure investments that will improve the committee overall? Pension plans have a lot of money. No pension plan wants to be the single plan to make that investment. Other plans will let you make the investment. You will receive a permanent return on your money, but the plan managers will benefit as well. If you require some assets to be dedicated, however, you might improve the underlying performance of the committee as you improve roads, bridges, highways, and the like.

MR. BALL: Well, maybe I am a little conservative here, but I do not believe that there is room for economically targeted investments. It is very hard to carry social investing over to the individual pension plan just because it is good for society. You may remember our reaction when elderly people were promised improvements in insurance, only to discover that they were going to have to pay for it themselves. It was a political reaction. I think that is the kind of political reaction we would have here. Senior citizens in this country would not accept that.

The experience of social investing is very checkered. For example, the state of Connecticut, my home state, had the brilliance to invest in the coal industry. They put in thirty or forty billion dollars and lost almost everything. That was social investing. What about the fiasco in Kansas where the state and local industry invested 100 million dollars in venture capital in start-up businesses? The business of social investing is very difficult. What helps one group—I sometimes think that this "group" must be the construction industry, and I want to know because down at Renaissance Weekend where President Clinton used to go every year for about twelve years, there were people there from the construction trade, and I wonder if he didn't pick up a little construction industry slant from those weekends and all those people in the industry who talked about the way the roads were falling apart—does not necessarily benefit another.

There is no question that the roads are falling apart, but I do not think you can rebuild them on the backs of the elderly people of this country. However, it's a political issue, and it is a health care issue. The world changes. My view is that the money belongs to the plan and not the politicians. Once you give it to the politicians it is in danger. It is best to never let that happen.

I think there is a real Sutton principal here. Somebody once asked the great bank robber Willie Sutton, "Willie, why did you rob banks"? He said, "I guess that is because that's where the money was," and that is what politicians are doing. It is the Willie Sutton principal in pension plans. Today, the money is in pension plans, and the Willie Suttons are the politicians. They are going where the money is.

THE AUDIENCE: I have a question for Ms. Ray. You talked about the interaction between the Bankruptcy Code and ERISA and the way a participant's benefits are protected from creditors. What about the opposite situation? What happens when a trustee or another named fiduciary commits a fiduciary breach and then declares bankruptcy? Can he or she be sued or would those violations be discharged by the Bankruptcy Code?

MS. RAY: I do not think that the Bankruptcy Code would necessarily discharge those violations. Much of it would depend upon the type of suit and the timing of the final petition of bankruptcy. For the most part, it has not been a serious concern. Once again, I believe that the matter will involve a balancing act, with the Supreme Court resolving the issue as it did in *Patterson v. Shumate*. It is the type of thing where you have two markedly different statutes, each of which is a significant piece of legislation.

MS. STABILE: Let me direct a question to Ms. Ray. In discussing both the *Guidry* case and the *Patterson* case you told us enough about the facts to indicate that the plaintiffs were not particularly sympathetic in either case. I am wondering whether in your view any part of the anti-alienation analysis ought to consider the plaintiff's actions, or if anti-alienation is a principal that is so strong that we should not be concerned at all with the plaintiff's wrongdoing.

MS. RAY: I think a number of people were very surprised by the Supreme Court's decision in *Guidry*. The plaintiff in that case embezzled plan funds, and the Court essentially concluded that there would not be any offset. Prior to ERISA, there were provisions known as "bad boy clauses" that were incorporated into pension plans to allow an employer to defeat employees' ability to collect the benefits to the extent they had their hand in the till or otherwise committed some sort of malfeasance. These acts normally amounted to a misdemeanor, and occasionally, a felony. On that score, I think people believe that *Guidry* is the wrong result. The result is one that, frankly, gives lawyers a bad name. It is the sort of thing which, I think, is a gut reaction. People intuitively think that it is wrong. In *Guidry*, the Court was trying to make a point that this was, indeed, a very precious right in terms of protecting pension plans.

In addition, the case differs from *Patterson* when one looks at the timing of the declaration of bankruptcy for the corporation and the plaintiff's excellent legal counsel, who provided the best possible advice on every point of minutia. I also believe that the plaintiff was not as unappealing a person in terms of good guy/bad guy syndrome or basic fairness. As an ERISA lawyer, I found it very reassuring, I admit, that the Court came down on the side of protecting pension benefits even in such an inappropriate case. I think that they viewed it not just from the standpoint of that particular plaintiff, but also from the standpoint of others who would be relying on this.

MR. STEIN: That was the only issue where, I think, you had plaintiffs' and defendants' ERISA counsel on the same side.

THE AUDIENCE: Carrying that theory a little further, suppose the plaintiff's embezzlement had caused the company to go bankrupt. What would have been the result? Say the money is gone and now the plan is insolvent or the company goes bankrupt. *Guidry* only involved 300-something thousand dollars and the company was able to sustain that loss. Suppose there was insurance or something to cover that. What would you think of the equities if other plan participants could not get the benefit?

MS. RAY: If you are viewing it in terms of sheer equity, it would seem inappropriate to allow this particular pension plan participant to benefit by both embezzling the funds (although, presumably, criminal action would be taken against him) and also collecting his benefits at the same time. That is just a question of pure equity.

As far as measuring what the right rule ought to be, if you are going to have general rules to try to explore, I believe in the long run, in an employer-supported pension plan or a union-sponsored pension plan, it is appropriate to try and protect the plan participant, especially if the participant does not have free accessibility to retrieve the funds.

MR. SIRKIN: In my mind, it has always been illogical to argue that no one can attach a pension plan while it remains financially sound, but that as soon as there is financial trouble someone can levy on it. People cannot secure it; they cannot give their money away. It is illogical to say that bankruptcy law will force a party to relinquish plan funds if they are thrown into bankruptcy. That money is supposed to be there for your future.

MR. STEIN: There is another factor. The government has put the money into the retirement plan. It is not just your money; the government is contributing tax benefits. Thus the person that puts the money there is not the only settlor of that trust. The government has that interest because it wants money to be there for retirement. I do not know if this is worth mentioning, but you asked earlier what would have happened if the plan had gone bankrupt. *Guidry* involved somebody who embezzled from the union. I think you had a plan official who embezzled from the plan.

MS. RAY: As a matter of fact, I think your comments are squarely on point because if, rather than Guidry, the plan had sought the benefit, there might have possibly been, or at least a number of people would say that there would have been, a different result in the sense that there might have been a plan interest.

MR. SIRKIN: In that instance you could set-off against his benefit if the fiduciary breached his duty to the plan. This has been the result in the bulk of the lower court decisions that have dealt with the issue.