No. 24-cv-100-XXX

IN THE UNITED STATES COURT OF APPEALS

FOR THE EIGHTH CIRCUIT

JOHN SMITH,

Plaintiff-Appellant,

v.

HOPSCOTCH CORPORATION; RED ROCK INVESTMENT CO.,

Defendant-Appellees.

On Appeal

from the United States District Court For the District of Minnesota

---

BRIEF FOR DEFENDANT-APPELLEES

Team 3

Counsel for Defendant-Appellees

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Rules

Regulations

JURISDICTIONAL STATEMENT

The United States District Court for the District of Minnesota exercised subject matter jurisdiction over this case under the Employee Retirement Income Securities Act of 1974 (“ERISA”). 29 U.S.C. § 1132(e); 28 U.S.C. § 1331. This Court now has appellate jurisdiction after the lower court entered final judgment. 28 U.S.C. § 1291. FED. R. APP. P. 4(a).

STATEMENT OF ISSUES

I. Whether the district court incorrectly held that there was a plausible breach by Hopscotch and Red Rock of their fiduciary duty of prudence because their prioritization of ESG factors in their investment strategy and management was not in the exclusive interest of Plan participants as required under 29 U.S.C. §§ 1104 and 1105.

II. Whether the district court correctly held that the complaint did not contain sufficient facts to plausibly allege a legally cognizable loss to the plan?

STATEMENT OF CASE

Appellant-Plaintiff John Smith initiated suit against Appellee-Defendants Hopscotch Corporation, sponsor and administrator of the 401(k) defined contribution plan in this case (the “Plan”), and Red Rock Investment Co., the investment manager, for breaches of the fiduciary duties of loyalty and prudence under 29 U.S.C. §§ 1104, 1105. Compl. p. 1, 7–9. In response, the Hopscotch and Red Rock jointly filed a motion to dismiss under Federal Rule of Civil Procedure 12(b)(6), arguing that Mr. Smith failed to properly allege a breach of a fiduciary duty or a resulting loss should such a breach have occurred. Mem. Op. and Order p. 4–5.

The U.S. District Court for the District of Minnesota held a hearing on the motion to dismiss and issued an order granting the motion to dismiss in favor of Hopscotch and Redrock. *Id*. at p. 8. In the order, the court ruled that although it was plausible that Hopscotch and Red Rock breached their fiduciary duty of prudence by considering ESG factors, the case must be dismissed because Mr. Smith failed to allege a loss to the Plan because he did not provide a meaningful benchmark to assess underperformance either in his complaint or when pressed to do so during the hearing. *Id*. at p. 5, 7–8. Mr. Smith subsequently filed a Notice of Appeal. This Court now is being asked to review the lower court's grant of the Motion to Dismiss in favor of Hopscotch and Red Rock.

STATEMENT OF FACTS

Appellee-Defendant Hopscotch Corporation ("Hopscotch") is a social media company incorporated and headquartered in Minnesota that sponsors and administrates a retirement plan (the "Plan) under ERISA. Compl. p. 2. Hopscotch hired Appellee-Defendant Red Rock Investment Co. ("Red Rock") to be the investment manager for the plan, making it the Plan fiduciary. *Id*. at p. 2. Appellant John Smith ("Mr. Smith") was an employee at Hopscotch from 2016 to 2023, and participated in the Plan for the duration of his employment, long enough for the plan to have vested. *Id*. at p. 3.

Beginning in 2018, the Board of Directors of Hopscotch began considering ESG factors in its corporate strategy, particularly to attract and retain teenagers and pre-teens, who are Hopscotch's primary clients. *Id*. As a result, Hopscotch became the number one social media company for teenagers and pre-teens within one year. *Id*. Red Rock managed the Plan, its investment, and did proxy voting, in line with Hopscotch's corporate strategy from the period of February 4, 2018 to the date of the complaint of February 4, 2024 ("the relevant time period"). *Id.* at p. 4.

At the hearing on the motion to dismiss, even when pressed to do so, the court found that Mr. Smith failed to identify comparators in the relevant time period; thus, dismissing the case. Mem. Op. and Order p. 7–8.

SUMMARY OF ARGUMENT

The Employee Retirement Income Security Act (ERISA) is a delicate balancing act between encouraging fiduciaries and companies to create plans such as the one in this case, but also ensuring fair execution of the plan and its rights. Mr. Smith alleges that Hopscotch and Red Rock breached their fiduciary duties of prudence because they chose to select investments and an investment manager (in the case of Hopscotch) using ESG factors. Hopscotch had riveting success with their new corporate strategy of utilizing ESG, as they became the number one social media platform for their target demographic. Mr. Smith is arguing that such a plan should only consider the financial returns to determine whether a fiduciary acted prudently when selecting and managing investments; rather than ever considering long-term benefits such as retirement security or risk mitigation for the future. If fiduciaries were required to have foresight to not be liable, no company would create such plans as the liability would exist in any choice a company or fiduciary would make.

Furthermore, Mr. Smith's allegations about the current papers finding ESG funds underperforming compared to a broader market are not sufficient enough to show that a fund is an imprudent choice. Not only is the research presented in a short-term focus, contrary to the long-term focus typically associated with ESG strategies, but fails to overcome the requirement to demonstrate a breach of duty of prudence. It is not enough to utilize public information to show a fiduciary acted imprudently, because such an argument would ignore the very basis of the ERISA rule, that fiduciaries Hopscotch and Red Rock must act reasonably based on their *expertise* and *experiences,* not just short-term retrospective public data.

Mr. Smith's complaint should also be dismissed because it failed to plead sufficient facts to show a loss to the plan relative to a meaningful benchmark.

Instead, he lobbed bare statements after conclusory allegations and drew no nexus between the few generalized statistics he provided and Hopscotch and Red Rock actual actions. He, in the loosest sense, compared Hopscotch to two of its competitors, stating that the company had slower growth rate than the other two companies. But *what* caused that growth rate, *whether* that rate had increased or decreased over time, and *how* a comparison to two other companies was relevant was entirely absent from his allegations.

In another allegation, Mr. Smith compared certain "energy" and "non-energy" stocks over an incredibly brief period, with the implication that Hopscotch and Red Rock were losing money by mostly avoiding certain specific stocks. But again, facts stating how stocks get categorized into the undefined options of "energy" and "non-energy," which of those stocks Hopscotch and Red Rock specifically avoided, and how much loss was incurred aside from "high" were conspicuously absent. Without such critical details, it is remains unclear what Mr. Smith believed was actually happening in the present case.

Mr. Smith also spent several paragraphs making bare allegations of wrongdoing, as cautioned against in *Iqbal* and *Twombly*. He stated that there were non-ESG options with better results but provided no examples. Proxy voting supposedly caused stock prices to decrease but did not indicate whether the price proceeded to cause a reduction to the plan. Furthermore, it was alleged that climate activism and ESG investments led to lower returns, but Mr. Smith provided zero supporting statements showing why or how much.

Lastly, Mr. Smith referenced a study that showed ESG funds slightly underperformed over a brief period. It is well settled law at the trial level that for such a comparison to be valid, it must be of sufficient duration and severity. The typical minimum being ten years, while Mr. Smith only provided five year data. There is no specific cut off for severity, but Mr. Smith only alleged underperformance by 2.5%—well within the range of disparity that courts dismiss.

Therefore, because ESG considerations were within the fiduciary duties of prudence and loyalty, Hopscotch and Red Rock may consider them without breaching their fiduciary duty. Furthermore, even if there is the plausibility of fiduciary breach, Mr. Smith failed to allege loss related to such a breach.

ARGUMENT

I. Standard of Review

A motion to dismiss by a district court is reviewed *de novo*. *Davis v. Washington Univ. in St. Louis*, 960 F.3d 478, 482 (8th Cir. 2020). The court accepts all allegations in the complaint as true and draws all reasonable inferences in favor of the nonmoving party. If the complaint does not contain sufficient factual matter to state a facially plausible claim for relief, then it should be dismissed. *Id*. (citing *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009)).

II. This Court should reverse the lower court's holding that ESG factor considerations may constitute a breach of duty of prudence as the fiduciary duties of prudence and loyal permit ESG considerations.

Under the Employee Retirement Income Security Act (ERISA), a fiduciary's duty is to act prudently and loyally, making investment decisions that are to the best interest of plan participants. §1104(a)(1)(A) and (B). Recently, the consideration of Environmental, Social, and Governance (ESG) factors has been a pivotal topic as this inclusion impacts the risk profile and performance of investment plans. Studies show that ESG affects a plan's sustainability and outcomes because ESG factors tend to have improved financial performance over long-term and mitigate risks including regulatory or economic changes. Radhika Narula et al., *Impact of ESG on Firm Value: A Conceptual Review of the Literature*, 25, J. Soc. & Econ. Dev. 162, 169–171 (2023) at https://doi.org/10.1007/s40847-023-00267-8 (explaining how ESG practices are catalysts in value creation and risk mitigation).

Under ERISA itself, fiduciaries must strictly adhere to the duties of loyalty and prudence. To establish a breach of fiduciary duty, a plaintiff must demonstrate that "the defendant acted as a fiduciary, breached [their] fiduciary duties, and thereby caused a loss to the Plan." *Meiners v. Wells Fargo & Co.*, 898 F.3d 820, 822 (8th Cir. 2018); *See* 29 U.S.C. § 1109.

A fiduciary's duty of loyalty mandates that fiduciaries act solely in the interest of and for the benefit of participants and beneficiaries and to defray reasonable plan expenses. 29 U.S.C. § 1109. This duty emphasizes the requirement that a fiduciary must act with an eye to the benefiting participants, not to other concerns or interests. *Id.*

Meanwhile, the duty of prudence, under §1104(a)(1)(B), mandates that fiduciaries act "with the care, skill, prudence, and diligence under the circumstances" that a prudent man acting in similar circumstances and knowledge with such matter would use to "conduct of an enterprise of a like character and with like aims." §1104(a)(1)(B). *See Matousek v. MidAmerican Energy Co.*, 51 F.4th 274, 278 (8th Cir. 2022); *Hughes v. Nw. Univ.*, 595 U.S. 170, 172 (2022). This is a process-oriented evaluation, focusing on the fiduciary's conduct at the time of conduct rather than on results that occurred from the fiduciary's lack of hindsight. *Fifth Third Bancorp v. Dudenhoeffer*, 573 U.S. 409, 409–10 (2014); *see Tibble v. Edison Int'l*, 575 U.S. 523, 529 (2015).

ESOP fiduciaries, meanwhile, are held "to the same duty of prudence that applies to ERISA fiduciaries in general." However, ESOP fiduciaries are exempt from the need to diversify funds' assets as the diversification requirement of §1104(a)(1)(C) is not violated through the holding of employer stock. *Fifth Third Bancorp v. Dudenhoeffer*, 573 U.S. 409, 417 (2014).

Hopscotch and Red Rock's decision to integrate ESG considerations show their dual commitment: firstly, for a growth strategy aimed at long term success, secondly, a safeguard to the Plan's assets against long-term risk. This approach not only meets the fiduciary duties outlined in ERISA but also embraces a broader, long-term strategy for risk management.

The recent guidance from the Department of Labor (DOL) in 2021 clarifies the application of ERISA's fiduciary duties with ESG metrics, acknowledging that fiduciaries may integrate ESG considerations into investment decisions. U.S. Dep't Lab., *Final Rule on Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights* (Nov. 22, 2022), https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/fact-sheets/final-rule-on-prudence-and-loyalty-in-selecting-plan-investments-and-exercising-shareholder-rights. The previous 2020 rule had a "chilling affect on appropriate integration of ESG factors in investment decisions." *Id.* The DOL's final rule highlighted that ERISA fiduciaries must make sure that their financial decisions that consider ESG factors tie into return-risk mitigation or financial benefits that a qualified investment professional would deem prudent or material. Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights, 87 Fed. Reg. 73822., 73824 (to be codified at 29 C.F.R. pt. 2550).

The DOL further supported the inclusion of ESG considerations with acknowledgement that prudent management included the fiduciary duty to manage shareholder rights such as proxy voting or other shareholder engagement if they align with the financial interests of the plan, reflecting the same standard or care and diligence required by ERISA. *Id.* at 73825. The 2021 ruling removed parts of the regulation that encouraged abstention as the DOL found that prudent management of shareholder rights could increase the value of the plan's assets; thus the encouragement of abstention did not "adequately protect the interests of plans and their participants and beneficiaries." U.S. Dep't Lab.

Thus, the duties of loyalty and prudence under ERISA provide the framework that fiduciaries must operate in to ensure their actions and factor considerations align with the best interests of plan participants. 29 U.S.C. § 1109 As the investment landscape constantly evolves, a prudent investment and prudent fiduciary can include the incorporation of ESG factors. U.S. Dep't Lab.

A. Mr. Smith failed to present any factual allegations that the appellees' decision in choosing an investment strategy and investments with ESG considerations are an imprudent choice that breached the appellees' fiduciary duty.

Without well-pled factual allegations establishing that the funds are an imprudent choice, no reasonable inference can be drawn that the defendants acted with improper motives. *Meiners v. Wells Fargo & Co.*, 898 F.3d 820, 824 (8th Cir. 2018). To prove imprudence under ERISA, plaintiffs need to present meaningful benchmarks that demonstrate their claim. *Id.* at 822.

Furthermore, this Court holds that mere dissatisfaction with the outcomes from the fiduciary's investments does not suffice as a breach, there must be a clear failure in the fiduciary's decision-making and process, not their outcomes. *Matousek v. MidAmerican Energy Co.*, 51 F.4th 274, 278 (8th Cir. 2022) A plaintiff must assert more than a complaint that returns are too low comparatively, they must move from an inference of imprudence into a plausible imprudence with actual sound comparisons. *Id.*

In *Meiners* the plaintiffs alleged that Wells Fargo offered investment options with funds that were more expensive and that underperformed as compared to the Vanguard funds. 898 F.3d at 821. However, this Court dismissed the claim, emphasizing that only alleging underperformance is insufficient without well-pled facts showing that a fund was an imprudent choice, and that "no inference can be made that defendants acted out of improper motives," thus implying that a single comparison is not sound. *Id.* at 824. Furthermore, while plaintiffs are not required to refute every possible lawful reason for retaining an investment option, they cannot rely on allegations that are "merely consistent with" liability. *Id.* at 822.

As the Eighth Circuit explained in *Meiners*, ERISA plaintiffs often are exposed to extensive information about the funds offered because of ERISA's disclosure requirements. *Id*. However, plaintiffs typically lack the detailed insights into the fiduciary's "methods and actual knowledge" as that knowledge is usually exclusively known by the fiduciary. *Id. See also* 29 U.S.C. § 1104(a)(1)(B). Furthermore, this Court explained that "no authority requires a fiduciary to pick the best performing fund." *Id.* at 823.

In this case, Mr. Smith, similarly to the plaintiffs in *Meiners*, fails to provide meaningful benchmarks to establish imprudence. However, like *Meiners*, where this Court held that the plaintiffs failed to present well-pled factual allegations demonstrating that the funds retained were imprudent, Mr. Smith similarly relies on allegations of underperformance without offering substantive evidence. Mr. Smith's claims solely relied firstly on the argument that the ESG investment options offered by the plan underperformed to similar non-ESG options, citing a study that ESG funds underperformed a broader market by 2.5%. Compl. at p. 5. This is problematic because it amounts to citing better performance in hindsight, just as this Court has warned against. Furthermore, there are other studies that show that ESG do not underperform their conventional counterparts, and that ESG investments even outperform traditional investments in times of crisis, such as with COVID-19 that occurred in the relevant time period of this case. J. Soc. & Econ. Dev. at 170.

Secondly, Mr. Smith alleges that Red Rock's choice of not selecting traditional energy sector investment resulted in missed gains as the energy sector outperformed at this time by 55% non-energy sectors. *Id.* However, like in *Meiners*, where the Court found that the comparison to a similar fund that outperformed the chosen fund by the fiduciary did not demonstrate imprudence, Mr. Smith also fails to substantiate his claim with a meaningful benchmark. Red Rock's choice to forgo traditional energy investments, that at the time of selection may have been the best performing, do not breach their fiduciary duty of prudence. A comparison to like funds that have different strategies regarding investment, which just so happen to perform differently, does not establish that the ESG funds retained by the appellees were imprudent at the time of selection.

B. The appellees' ESG-focused investment strategy and independent evaluation of their investments is reasonable under their fiduciary duty of prudence under ERISA.

Fiduciaries do not breach their duty when they independently evaluate and conclude that ESG investments are prudent additions because the court "must give due regard to the range of reasonable judgments a fiduciary may make based on her experience and expertise." *Hughes v. Nw. Univ.*, 595 U.S. 170, 172–73 (2022). The circumstances surrounding fiduciary decisions must be considered as fiduciaries are often required to make tradeoffs so their decisions must be evaluated within the broader context of their information and their aligning expertise. *Id. See also Fifth Third Bancorp v. Dudenhoeffer*, 573 U. S. 409, 425 (2014). ERISA determinations, therefore, require a careful balancing act between encouraging companies and fiduciaries to create such plans and also the fair execution of the plans and rights in them. *Id.* at 424.

The Supreme Court's decision in *Fifth Third Bancorp* offers a useful framework for analyzing the prudence requirement for fiduciaries when the case involves company-specific strategies. *Id.* In *Fifth Third Bancorp*, plaintiffs claimed that fiduciaries breached their duty of prudence by failing to act on public information that the company's stock was overvalued. *Id.* at 425. However, the Court held that allegations that a fiduciary acted imprudently based solely on public information that is available regarding the value of the stock is implausible without special circumstances. *Id.* Furthermore, fiduciaries are not liable for failing to outsmart the future returns of a market and failing to predict the future performance of a company's stock. *Id.* at 427.

In this case, Mr. Smith argues that fiduciaries should have recognized that ESG investments were underperforming based on public data that non-ESG funds were delivering better short-term returns. Compl. at p. 5. As the Court stated in *Fifth Third Bancorp*, allegations of over- or undervaluation of stock are implausible as a general rule. *Id.* at 425. Thus, just like in *Fifth Third Bancorp*, where fiduciaries were not required to act on public information that could affect their stocks, appellees are not required to act on speculative market predictions much as the current market growth rates for ESG funds. Appellees use ESG-focused investments to align with the broader goals of their Plan.

Therefore, the appellees approach also aligns with the requirements outlined in *Hughes.* The Court held in *Hughes* that fiduciaries need to regularly review existing investments and remove those that are imprudent. 595 U.S. at 174. This duty exists separately from the initial duty to exercise prudence in selecting investments. *Tibble v. Edison Int'l*, 575 U.S. 523, 529 (2015). However, the circumstances surrounding fiduciary decisions must also be considered.

In *Hughes*, the Court emphasized that even in defined-contribution plans, where participants could choose from a menu of options for investments, plan fiduciaries must conduct independent evaluations of the investment to determine their prudence based on the fiduciary's specific expertise. 595 U.S. at 171–172. *See also* 29 U.S.C. § 1104(a)(1)(B). In *Hughes*, the plaintiffs claimed that the respondents breached their duty of prudence by offering overly expensive investment options, similar to *Meiners*. *Id*. However, the Court once again pointed out the importance of the requirement of context-specific inquiries about a fiduciaries' duties and ensuring to give weight to fiduciary's expertise and judgements. *Id.*

ESG funds are specifically designed with long-term growth and risk mitigation in mind. Therefore, the appellees acted prudently by evaluating ESG-focused investment options and finding them suitable based on the information available to the fiduciaries and their expertise, and continuing to find them suitable throughout the relevant time period of this case. While Mr. Smith relies on short-term market data to argue imprudence, a company focusing on younger demographics does not imply neglect of retirees' benefits. Instead, based on the circumstances, it reflects a strategy aligned with long-term sustainability by securing the company's financial health, which, in turn, secures the Plan. Fiduciaries are often put in a challenging position where any decision, whether retaining an investment or removing it prematurely, can expose them to liability. *Fifth Third Bancorp,* U.S. 409 at 423. In this case, appellees reasonably balanced competing considerations and chose the one based on their expertise, thus acting prudently as required in their duties.

By strategizing and prioritizing a ESG factor focused portfolio and asset manager, the appellees were not diverging from their fiduciary duties only to align with contemporary investment trends and participant desires; but rather worked to enhance the long-term economic growth and stability of the Plan, in line with their corporate strategy. By doing so, the appellees aimed to secure the financial futures of beneficiaries in the constantly evolving circumstances of investment management, showcasing their commitment to the participants' retirement security and their benefits.

III. This Court should affirm the lower court's dismissal because Mr. Smith failed to allege comparable alternatives that establish a meaningful benchmark showing loss.

This Court should affirm the decision of the U.S. District Court of Minnesota, which held that the loss element was not sufficiently alleged, warranting dismissal because Mr. Smith's failed to identify suitable comparators that show the relative pecuniary disadvantage of the chosen ESG investments in the complaint and at the hearing on the motion to dismiss. This Court has already addressed similar facts and held that to show loss, a plaintiff must show a "sound basis for comparison—a meaningful benchmark." *Matousek v. MidAmerican Energy Co.*, 51 F.4th 274, 280 (8th Cir. 2022) (quoting *Meiners v. Wells Fargo & Co.*, 898 F.3d 820, 822 (8th Cir. 2018)). Instead of doing so, Mr. Smith levied numerous empty allegations of "negative impact[s]," but never clearly demonstrated how the specific investments Hopscotch and Red Rock chose were inferior to their alternatives. *See* Compl. p. 4–5. Where the complaint provided specific numbers, those fell far short of the minimum values courts consider. *Id*. at

p. 5. Accordingly, without the proper comparators, it is merely possible Mr. Smith suffered a loss, not plausible; therefore, the lower court should be affirmed.

A. Most of Mr. Smith's allegations regarding loss do not specify how the value Mr. Smith got from the Plan was less than what he should have received.

The overwhelming majority of Mr. Smith's allegations regarding loss loosely attribute "negative impacts" to the Hopscotch and Red Rock, without explanation beyond a bare statement. Compl. p. 4–5. Under the federal rules, a plaintiff must provide a "short and plain statement of the claim showing that the pleader is entitled to relief." Fed. R. Civ. P. 8(a)(2). The Supreme Court has clarified this requirement to mean the plaintiff cannot simply make "unadorned, the-defendant-unlawfully-harmed-me accusation[s]." *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (quoting *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555 (2007)). The Court emphasized that although the pleading requirements do not necessitate hyper technicality, a plaintiff also cannot be "armed with nothing more than conclusions." *Id*. at 678–79. Nor should legal conclusions be conflated with factual allegations; they need not be presumed to be true. *Id*.

Furthermore, under ERISA, a "loss" is usually a failure to realize as many gains as a prudent fiduciary might and does not necessarily involve the actual loss of money.[1] *See generally Matousek*, 51 F.4th at 278 (citing *Davis*, 960 F.3d at

[1] In other words, a plaintiff frequently gains money, just at a lower rate than they might expect.

482–484). Accordingly, this Court clarified the pleading standard for ERISA claims under *Iqbal* and *Twombly*: a plaintiff must at minimum plead facts to establish a sound basis for comparison that demonstrates how the defendant inflicted loss upon the plaintiff's funds through an imprudent decision. *Matousek*, 51 F.4th at 280 (quoting *Meiners*, 898 F.3d at 822).

In *Matousek*, the plaintiff alleged that the defendant, who offered company-sponsored retirement plans, (1) paid too much money to a recordkeeping company and (2) kept poorly performing or excessively costly investments. *Matousek*, 51 F.4th at 278–281. Both issues differed because the first issue concerned flat payments to a third party, and the second issue concerned the continuing duty to maintain prudent investments. *Id*. But the common overlap was that both involved the improper usage of the plaintiff's funds. *Id*.

Thus, in both situations, this Court attempted to identify a meaningful benchmark to compare the loss attributable to the defendant's actions. *Id*. In the excessive fees claim, this Court expected specific and comparable plans, but received industry-wide averages. *Id*. at 279–80. This Court rejected this proffer because the direct comparison between what the plan offered, what it cost, and its overall pros and cons could not be fully encapsulated by generalized statistics. *Id*. This Court had previously cautioned against apples to oranges comparisons, stating, "[the investment options] have different aims, different risks, and different potential rewards that cater to different investors," and dismissed such a comparison in *Matousek*. *Davis v. Washington Univ. in St. Louis*, 960 F.3d 478, 485 (8th Cir. 2020).

It is the same for the imprudent investment claim. This Court looked for a meaningful benchmark between the comparators and the funds and companies at issue. *Matousek*, 51 F.4th at 280–81. Securities, investment strategies, risk profile, return objectives, management approaches, and preference for growth and/or value stocks were all looked at by this Court. *Id*. at 281–82. The absence of critical details establishing why a benchmark was analogous to its counterpart, such as the ones mentioned, left this Court without sufficient facts to accept as true and accordingly dismissed the complaint. *Compare id*. *with Gaines v. BDO USA, LLP*, 663 F. Supp. 3d 821 (N.D. Ill. 2023) (finding explanation of similarities in investment targets and twenty comparator funds as sufficient).

1. *The standard this Court applied to the two different circumstances in Matousek should extend to Mr. Smith's claim because of the overlap of alleged improper usage of funds.*

As a preliminary matter, this Court should apply the *Matousek* standard to this case because this case is also about imprudent investments, which essentially equates to the second issue of *Matousek*. This Court did not vary in applying the meaningful benchmark standard, even with fairly different claims, so long as the issue was the improper usage of the individual's funds. In this case, Mr. Smith alleged that Hopscotch and Red Rock made imprudent investments by foregoing non-ESG funds. Compl. p. 4–5. Given the similarities between the cases, *Matousek* should control.

> 2. *Mr. Smith repeatedly failed to meet the Matousek standard by omitting critical details that were relevant for comparison.*

Mr. Smith began the bulk of his allegations of loss in paragraphs 14 and 15, where he compared Hopscotch's growth to Hopscotch's competitors, the first and third largest social media companies, alleging Hopscotch was growing slower. Compl. p. 4. But that allegation was entirely bare. *See id*. He identified no similarities in prospects, strategies, nor company composition. *Id*.

On the contrary, the only real analysis was that Mr. Smith indicated Hopscotch became the most popular among the youngest demographic after only a year of implementing a new ESG-focused strategy. Compl. p. 4. This was a clear positive for not only Hopscotch, but Mr. Smith as the beneficiary of the plan because it demonstrates Hopscotch was successfully employing a long-term growth strategy. Whether a company employs a long-term or short-term growth strategy is one potential aspect for analysis identified in *Matousek*, but it only counters his claim of loss in this case. Without any further information on the first and third largest social media companies' strategies (e.g., were they employing long-term or short-term growth strategies?), the information provided is not an adequate benchmark.

Similarly, in paragraph 23, Mr. Smith alleged that over a two year period, energy "large and mid-cap stocks returned over 55% more than non-[e]nergy" options. Compl. p. 5. This statement is riddled with the lack of analysis cautioned against in *Matousek*. The factual premise of Hopscotch and Red Rock's supposed mistake considered only a brief period,[2] evaluated only certain types of stocks, and categorized stocks into "energy" and "non-energy," without defining said terms. It epitomizes cherry-picking statistics to suit an argument.

Furthermore, at no point did Mr. Smith indicate that the stocks he suggested were actually missed out on by Red Rock. Instead, he alleged that Red Rock forewent "most" energy investments and missed out on achieving "these" high returns for the Plan. *Id*. But the complaint does not say Red Rock forewent *all* energy investments, meaning it is just as possible that Red Rock took advantage of the best investments in the 55% average.[3] Mr. Smith may contend that missing out on "these" high returns makes that argument, but what constitutes a "high return" and to what degree Red Rock diverged from that standard is not articulated, making the statement conclusory.

[2] *See infra* Section III.B.

[3] Mr. Smith provided no assurance that by measuring data with an average, it is not confounded by an outlier or otherwise skewed, which Red Rock may have taken advantage of.

3. Mr. Smith also plainly contravenes the basic pleading requirements of Iqbal and Twombly by supplying bare statements, with no supporting allegations.

Mr. Smith continues in paragraphs 16, 21, and 24 by vacantly alleging something bad occurred without tying it to a loss for the plan. Compl. p. 4–5. For example, Mr. Smith pointed out that each option offered by Plan had a similar non-ESG option with better results but provided no examples of such plan. If no plan is even provided, naturally *Matousek*'s requirement for attribute comparison cannot be met. Likewise, Mr. Smith stated that proxy voting caused stock prices to sharply decline but made no allegation as to whether that stock price decrease led to an actual loss or whether the price increased right back. Common sense dictates that although some people may be hesitant of Red Rock's views, once they realize the consideration of ESG factors is a valid strategy, then the low-priced but high value stocks will be quickly bought up, resuscitating the stock price. And finally, Mr. Smith separately alleged that climate activism and ESG investment led to lower returns but again provided no supporting statements. Each of these statements amounted to nothing more than saying Hopscotch and Red Rock unlawfully harmed him, rendering them of no aid to his argument.

B. Even when Mr. Smith used specific numbers, the values fail to establish a meaningful benchmark because they lack the severity and duration of a legally cognizable loss.

Mr. Smith failed to plead comparators suggesting the ESG options chosen by Hopscotch and Red Rock underperformed by a significant enough margin for a significant enough period of time, rendering the comparisons irrelevant. Courts have been extremely cautious about frustrating the prospect of long-term investments by holding them to the standards of short-term investments. *Smith v. CommonSpirit Health*, 37 F.4th 1160, 1166 (6th Cir. 2022) (citing Charles D. Ellis, *Winning the Loser's Game* 7, 83–87, 119 (4th ed. 2002). Rather than viewing brief underperformance of marginal magnitude as "loss," courts have instead repeatedly held that the relevant benchmark must show "consistent" and "substantial" relative underperformance. *See Smith*, 37 F.4th at 1166 (6th Cir. 2022); *Gonzalez v. Northwell Health, Inc.*, 632 F. Supp. 3d 148, 163 (E.D.N.Y. 2022) (citing *Patterson v. Morgan Stanley*, No. 16-CV-6568 (RJS), 2019 WL 4934834, at *10 (S.D.N.Y. Oct. 7, 2019); *Dorman v. Charles Schwab Corp.*, No. 17-CV-00285 (CW), 2019 WL 580785, at *2, *6 (N.D. Cal. Feb. 8, 2019)). Mr. Smith's allegations show neither.

1. Mr. Smith relied on data focused on relatively brief periods of time, which does not adequately encapsulate the underlying goal or mechanism of a long-term investment.

Mr. Smith's reliance on two benchmarks that narrowly analyzed two and five-year performance data is dissimilar as a benchmark compared to the long-term nature of Hopscotch and Red Rock's investment plan. Retirement plans are intended to develop for decades, and selecting a brief snapshot of low performance is not indicative of the expected performance of the plan. *Compare Smith*, 37 F.4th at 1166 (6th Cir. 2022) (rejecting the mere highlighting of a plan that performed better over five years) *and Schaf v. O-I Glass, Inc.*, 680 F. Supp. 3d 854, 858–860 (N.D. Ohio 2023) (accepting detailed tables showing fundamental underperformance). In fact, courts recognize that prudent fiduciaries frequently retain investments, even as their value naturally fluctuates in the short term, such that they can reap the benefits in the long term. *Gonzalez*, 632 F. Supp. at 163 (citing *White v. Chevron Corp.*, No. 16-CV-0793 (PJH), 2016 WL 4502808, at *17 (N.D. Cal. Aug. 29, 2016)).

The "traditional hallmark" for a comparable benchmark, such that it adequately reflects the nature of a retirement plan, is ten years, with five years being too short. *Bloom v. AllianceBernstein L.P.*, 725 F. Supp. 3d 325 (S.D.N.Y. 2024); *Davis v. Salesforce.com, Inc.*, 2020 WL 5893405, at *4 (N.D. Cal. Oct. 5, 2020); *Gonzalez*, 632 F. Supp. at 163–64; *Laboy v. Bd. of Trustees of Bldg. Serv.*

32 BJ SRSP, 513 F. App'x 78 (2d Cir. 2013) (summary order). Short-term performance can "mask year to year performance and is a poor predictor of future performance," so courts do not use it as a benchmark. *Evans v. Associated Banc-Corp*, No. 21-C-60, 2022 WL 4638092 (E.D. Wis. Sept. 30, 2022).

In the present case, Mr. Smith attempted to establish loss by vaguely referencing a paper[4] that stated ESG funds underperformed when compared to non-ESG funds over a five-year period. Compl. p. 5. As a matter of law, this is insufficient. A single study analyzing a relatively brief period cannot encapsulate the full picture of a multi-decade venture, where even the duration of Mr. Smith's employment was longer than the referenced period at seven years. Compl. p. 3.

Further, Mr. Smith alleged Hopscotch and Red Rock invested in ESG options for as much as six years but again only provided five years of data. Compl. p. 3, 5. That absent year amounts to a little over sixteen percent of the time frame, meaning a significant portion of the data showing the efficacy of the fund is missing. In that missing year, ESG funds may have had better results than non-ESG funds, but Mr. Smith made no contention either way.[5] Instead, Mr. Smith's

[4] Although the Appellant stated that multiple "papers" indicated underperformance, only the details of one paper were provided. Compl. p. 5.

[5] Moreover, in the five years that the paper analyzed, several events with sweeping consequences on the economy occurred that should not be taken out of context, including shutdowns resulting from a global pandemic. See generally Mohamed A K Basuony et al., The effect of COVID-19 pandemic on global stock markets: Return, volatility, and bad state probability dynamics, NAT. LIBR. OF MED. (Sep. 23, 2021), https://pmc.ncbi.nlm.nih.gov/articles/PMC8646943/.

argument presents the same problem as the comparators in *Smith*, where a long-lasting investment was also unsuccessfully shoehorned into a mere five-year analysis.

Mr. Smith repeated the same mistake in paragraph 23 of the complaint, where results from two years were suggested as a comparator. Compl. p. 5. Although those two years indicated high underperformance,[6] the issue is the same. The risk of data being selectively reported to suit an agenda is too great, which is why courts look for consistent underperformance, not just a negative statistic or two.

2. *Mr. Smith did not allege that Hopscotch and Red Rock's funds diverged significantly from his proposed benchmark; therefore,he did not experience legally cognizable loss.*

Even if the relatively brief period of analysis were found to be representative of the overarching prospect of Hopscotch and Red Rock's investments, Mr. Smith only alleged modest underperformance. The value of stocks, by their very nature, fluctuates in the short term. *Lanfear v. Home Depot, Inc.*, 679 F.3d 1267, 1282 (11th Cir. 2012); *see Coburn v. Evercore Tr. Co.*, N.A., 844 F.3d 965, 972 (D.C. Cir. 2016). Thus, rather than permit minor dips in value, which could easily rise later, to satisfy the loss element, courts look for substantial underperformance.

[6] Only assuming, which Hopscotch and Red Rock dispute, that the comparator funds Mr. Smith provided were adequately supported by facts under *Matousek*. *See supra* Section III.A.2.

Gonzalez, 632 F. Supp. at 163–64 (rejecting reduced values ranging from .32% to 2.57%) (citing *Bekker v. Neuberger Berman Grp. LLC*, No. 16 CV 6123-LTS-BCM, 2018 WL 4636841, at *2, *7 (S.D.N.Y. Sept. 27, 2018) (rejecting ten-year underperformance of 4.48%); *Cho v. Prudential Ins. Co. of Am.*, No. 19-CV-19886 (JMV) (SCM), 2021 WL 4438186, at *9 (D.N.J. Sept. 27, 2021) (rejecting ten-year underperformance ranging from 1.19% to 2.86%); *Patterson*, 2019 WL 4934834, at *11 (rejecting ten-year underperformance of .74%). Courts keenly do not inhibit the valid strategy of retaining investments during deficits, unless it is clear the deficit is consistently severe. *Jacobs v. Verizon Commc'ns, Inc.*, No. 16 CIV. 1082 (PGG), 2017 WL 8809714 (S.D.N.Y. Sept. 28, 2017) (accepting plaintiff's claim for ten-years of underperformance by 8.63%).

Mr. Smith provided a study that found ESG funds underperformed compared to non-ESG funds by 2.5%. Compl. p. 5. Once again, this is not a legally cognizable amount of loss and could easily be due to any number of outside factors. Among them are simple market fluctuations, where some stocks temporarily have lower value; it does not necessarily predict how a stock price will change over the long term. Moreover, the lower court correctly joined several other district courts that have found values in the 2%–3% range as too low. Among them was the Court in *Bekker*, which found that 4.48% was too low. The 2.5% loss is far removed from the 8.63% loss in *Jacobs*, meaning the loss is simply too low.

This result is further reinforced by the fact that, as Mr. Smith noted, ESG funds returned an average of 6.3%, meaning that if Hopscotch and Red Rock's investments were perfectly encapsulated by this study,[7] Hopscotch and Red Rock's investments still earned Mr. Smith money. He merely alleged that Hopscotch and Red Rock did not earn him enough money, which a nominal reduction is not sufficient to show loss.

[7] Mr. Smith made no allegation as to whether the study he provided was representative of the returns acquired by Hopscotch and Red Rock, which is itself a *Matousek* issue. *See generally supra* Section III.A.

CONCLUSION

For the reasons stated above, this Court should affirm the judgment of the lower court and dismiss Mr. Smith's complaint for failure to state a claim upon which relief can be granted. The lower court was correct that Mr. Smith failed to provide sufficient benchmarks to establish relative loss. But if this Court disagrees, it should still rule in Hopscotch and Red Rock's favor on the basis that Hopscotch and Red Rock followed the process that a prudent fiduciary acting in similar circumstances and knowledge would have when considering ESG factors.

Respectfully submitted,

/s/ Team 3

Team 3

Attorneys for Appellees

DATED: January 24, 2025