CGR:sec 3025-163

IN THE UNITED STATES DISTRICT COURT FOR THE
CENTRAL DISTRICT OF ILLINOIS
PEORIA DIVISION

DEBRA K. KEACH and PATRICIA A. SAGE, Plaintiffs, vs. U.S. TRUST COMPANY, NA., f/k/a U.S. TRUST COMPANY OF CALIFORNIA, NA., et al., Defendants.	)	Case No. 01-1168

FOSTER AND REGAL RESPONSE TO PLAINTIFFS' SECOND MOTION FOR SUMMARY JUDGMENT

ALLEGED BREACH OF ERISA §404 DUTY OF LOYALTY

Now come the Defendants, Ellen D. Foster, as Executrix of the Estate of Thomas S. Foster, and Melvyn R. Regal, by their attorneys, Charles G. Roth, James W. Springer and Joseph Z. Sudow of Kavanagh, Scully, Sudow, White & Frederick, P.C., and in response to Plaintiffs' Second Motion for Summary Judgment (Breach of ERISA §404 Duty of Loyalty) state as follows:

I. INTRODUCTION

1. Plaintiffs' Second Motion for Summary Judgment against these Defendants argues (without any factual support) that Foster and Regal secured the agreement of U.S.

LAW OFFICES
KAVANAGH, SCULLY, SUDOW, WHITE & FREDERICK, P.C.
301 S. W. ADAMS STREET, SUITE 700
PEORIA, ILLINOIS 61602-1574
TELEPHONE (309) 676-1381
TELECOPIER (309) 676-0324

Trust and Houlihan Lokey Howard & Zukin ("Houlihan Lokey") "not to raise the *Eyler* issue" before the 1995 ESOP transaction.

2. Plaintiffs' motion does not present facts upon which a motion for summary judgment may be granted.

3. Plaintiffs' motion consists essentially of innuendo and extraction of statements out of context.

4. The motion does not indicate that these Defendants failed to discharge any duty as required by ERISA §404(a).

II. MATERIAL FACTS CLAIMED TO BE UNDISPUTED

A. Defendants admit that the following paragraphs contain material facts which are undisputed: 1, 2, 3, 4, 5, 6, 7, 9, 10, 11, 12, 22, 26, 27, 28, 29 and 30.

B. Defendants claim the following paragraphs contain facts which are undisputed but which are not material to Plaintiffs' Motion for Summary Judgment: 13, 14, 15, 16, 17, 18, 19, 20, 21 and 25. Paragraphs 13, 14 and 15 relate to the 1988 ESOP and the 1951 incorporation of Foster & Gallagher, neither of which is material to Plaintiffs' motion. Paragraph 16 relates to Mr. Foster's medical diagnosis and is not material to Plaintiffs' motion. Paragraph 17 relates to a consideration of an initial public offering and is not material to Plaintiffs' motion. Paragraphs 18 and 19 are a letter taken out of context because it does not relate to pre-transaction considerations but rather concerns after the transaction was complete. Further, the letter comes from a third

person, Attorney Sudow, and does not purport to represent the knowledge or belief of either Defendant. Paragraph 20 relates to advice from a third person, Attorney Sudow, but does not relate to any breach of duty and is not material to the basis of Plaintiffs' motion which is an alleged agreement between these Defendants and U.S. Trust and Houlihan Lokey. Paragraph 21 relates to the 1988 ESOP which is not at issue. Plaintiffs make no claim that the *Farnum* case was the basis of any alleged agreement between these Defendants and any others. Paragraph 25 relates to the position of Magna Bank and is not material to Plaintiffs' motion.

C. The following paragraphs are disputed by these Defendants for the reasons given: 8, 23 and 24. As to paragraph 8, it is undisputed that Mr. Foster died on 11 July 1996. Ellen Foster was not Executrix in the 1995 transaction and did not participate in the 1997 transaction. The Thomas Foster estate was closed. In spite of two attempts to reopen Mr. Foster's estate by the Plaintiffs, his estate remains closed and has no assets.

Paragraph 23 is an incomplete and inaccurate statement of the issues in the United States Tax Court opinion, *Eyler v. Commissioner*, 1995 WL 127907 (1995). There was nothing definitive developed from the Internal Revenue Service nor the Department of Labor regarding whether a post-transaction debt should be a factor to consider in pre-transaction value. Norbutas deposition page 59. The district court in *Scott v. Evins*, 802 F.Supp. 411 (N.D.Ala.1992), *aff'd without opinion* 998 F.2d 1022 (11th Cir. 1993), concluded that ESOP acquisition debt does not need to be taken into account into the

stock appraiser's determination of a fair market price of stock acquired by an ESOP to satisfy the adequate consideration requirement. The court in that case stated:

> "The proposed regulations do not state that the valuation must take into account any additional debt placed on the issuer as a result of the transaction. The common stock of Evins exists independently of the debt used to leverage the purchase, whether or not guaranteed by the corporation (as was done here). When the stock was appraised, no such debt existed and was, therefore, properly not taken into account."

In *Eyler, supra*, the court determined that the fiduciary did not conduct a prudent investigation because the fiduciary relied on stock valuation that was out of date and failed to consider other key facts which undermined the financial projections used for the valuations. In fact, in *Eyler* no formal appraisal was ever prepared to value the stock for purposes of the plan's purchase of the shares. Instead, the plan fiduciary relied upon a price range based upon a proposed initial public offering of the stock which in fact never occurred. Judge Evans' Seventh Circuit Court of Appeals opinion does not adopt the language cited by the plaintiff in paragraph 23. In fact he seems to shy away from any reference to a consideration of post-transaction debt as a factor affecting the adequacy of consideration. What is clear is that the Circuit Court of Appeals considered the process and procedure used by the trustee in evaluing the stock, as well as the actual fair market value of the stock sold to the ESOP. Judge Ruwe's opinion in the United States Tax Court is largely considered as *dicta*.

Paragraph 24 appears to offer inadmissible hearsay evidence consisting of a newspaper article regarding the *Eyler* decision and apparently is offered for the truth of

the matter contained therein. It is objectionable and not relevant as the article was not circulated by these Defendants, Foster or Regal.

D. Additional material undisputed facts.

1. Houlihan Lokey, a specialty investment banking firm, on 19 December 1995 issued its opinion letter to U.S. Trust Company that "the consideration to be paid by the ESOP for the company's securities in the transaction; is not greater than adequate consideration for such securities; the transaction is fair and reasonable to the ESOP from a financial point of view, the loan between the ESOP and the company, taken as a whole, is fair and reasonable to the ESOP from a financial point of view; and the interest rate, with respect to such loan, is fair and reasonable to the ESOP from a financial point of view." Exhibit 79 at 1100.

2. That in connection with its opinion, Houlihan Lokey made such reviews, analysis and inquiries as it "have deemed necessary and appropriate under the circumstances." Exhibit 79 at 1099.

3. That among the valuation conclusions of Houlihan Lokey was that the fair market value of the company's equity after consideration of existing debt, future noncash compensation and associated tax benefits is $233,000,000. This equates to a "value per share of $19.81." Exhibit 79 at 1108.

4. That in the opinion of Houlihan Lokey the equity value per share for Foster & Gallagher stock on the day before the December 1995 transaction was $19.81. Exhibit 79 at 1109.

5. That it was the opinion of Houlihan Lokey, on the day before the 1995 transaction, for the purposes of that transaction "the price a willing buyer would pay for the company is after consideration of existing debt, but without regard to the financing associated with the proposed transaction." Exhibit 79 at 1107.

6. That the 20 December 1995 report from the Sonnenschein, Nath & Rosenthal law firm retained as special counsel to U.S. Trust Company contains the opinion that "adequate consideration should look only to the fair market value of the shares immediately before the Shares are purchased and the company incurs the debt used to finance the Trust's purchase and should not be based on the lower fair market value of the Shares immediately after the purchase of the shares due to the debt incurred to finance the purchase." Exhibit 85 at 1365 and 1366.

III. APPLICABLE LAW

A. Section 404 "creates no exclusive duty of maximizing pecuniary benefits." *Foltz v. U.S. News and World Report, Inc.*, 865 F.2d 364 (D.C.Cir.1989).

B. Section 408(e) of ERISA provides an exemption from the prohibited transaction provisions of Section 406(a) and 406(b)(1) and (2) of ERISA where the trust pays no more than adequate consideration for the shares of stock acquired.

C. The United States Department of Labor has issued proposed regulations under ERISA with respect to the determination of fair market value of plan assets other than stock for which there is a generally recognized market. Proposed Regs. 29 CFR

§2510.3-18(b), 53 F.R. 17,632 (17 May 1988). These proposed regulations provide that the requirements of ERISA would not be satisfied unless the value assigned to a plan asset "both (1) reflects the asset's fair market value (as defined in Prop. Regs. 29 CFR §2510.3-18(b)(2)) and (2) results from a determination made by the plan trustee or named fiduciary in good faith."

D. "The proposed regulations do not state that the valuation must take into account any additional debt placed on the issuer as a result of the transaction. The common stock of Evins exists independently of the debt used to leverage the purchase, whether or not guaranteed by the corporation (as was done here). When the stock was appraised, no such debt existed and was therefore properly not taken into account." *Scott v. Evins*, 802 F.Supp. 411 (N.D.Ala. 1992), *aff'd without opinion* 998 F.2d 1022 (11th Cir. 1993).

E. Summary judgment should be granted where "the pleadings, depositions, answers to interrogatories and admissions on file, together with the affidavits, if any, show there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Fed.R.Civ.P. 56(c). The moving party has the responsibility of informing the Court of portions of the record or affidavits that demonstrate the absence of a triable issue. *Celotex Corp.v. Catrett*, 477 U.S. 317, 322 (1986). The moving party may meet its burden of showing an absence of disputed material facts by demonstrating "that there is an absence of evidence to support the non-moving party's case." *Id.* at 325. Any doubt as to the existence of a genuine issue for

trial is resolved against the moving party. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 255 (1986); *Cain v. Lane*, 857 F.2d 1139, 1142 (7th Cir. 1988).

F. If the moving party meets its burden, the non-moving party then has the burden of presenting specific facts to show that there is a genuine issue of material fact. *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 586-87 (1986). Fed.R.Civ.P. 56(e) requires the non-moving party to go beyond the pleadings and produce evidence of a genuine issue for trial. *Celotex*, 477 U.S. at 324. Nevertheless, this Court must "view the record and all inferences drawn from it in the light most favorable to the [non-moving party]." *Holland v. Jefferson Nat. Life Ins. Co.*, 883 F.2d 1307, 1312 (7th Cir. 1989). Summary judgment will be denied where a reasonable jury could return a verdict for the non-moving party. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986); *Hedberg v. Indiana Bell Tel. Co.*, 47 F.3d 928, 931 (7th Cir. 1995).

IV. ARGUMENT

A. The gist of Plaintiffs' Second Motion for Summary Judgment is found at paragraph 61 wherein the Plaintiffs assert that Tom Foster and Mel Regal "knew that the raising of the *Eyler* issue would decrease the sale price of their shares to the ESOP and took care to interview and select a trustee and financial advisor for the ESOP II transaction who would not raise the *Eyler* issue."

B. Plaintiffs present no evidence at all with respect to the knowledge or motivation of Tom Foster other than he knew he had been diagnosed with cancer. With respect to Mel Regal, there is only an inference and no evidence that he interviewed and selected a trustee "who would not raise the *Eyler* issue." There is no evidence from any source of any such promise or guarantee by U.S. Trust Company.

C. Plaintiffs exaggerate their position at paragraph 62 when they allege that U.S. Trust and Houlihan Lokey "compromised the interests of the ESOP and its participants and beneficiaries by agreeing not to raise the *Eyler* issue." There is in fact no evidence to support that assertion and Plaintiffs make no specific factual reference to this allegation.

D. Nor is there any evidence to support the Plaintiffs' conclusion that it would "have been fair to the ESOP participants and beneficiaries for U.S. Trust to have used the *Eyler* issue to negotiate a lower sales price for the shares of F&G." To the contrary, it would have been improper and a violation of its duties to negotiate an improper valuation methodology. The value of the stock must be determined as of the time of the transaction which is before the debt is incurred. The debt is not incurred before the transaction and to have made an evaluation on a date other than the date of the transaction would have been improper. Further, the Plaintiffs present no evidence that U.S. Trust did not properly negotiate the best sales price for the benefit of the ESOP participants.

E. There is a total absence of any evidence that Foster and Regal "sought assurances" from U.S. Trust or Houlihan Lokey before engaging them that either "would

not use the *Eyler* issue in the ESOP II transaction." In fact, the *Eyler dicta* was extensively discussed in the written report of Attorneys Sonnenschein, Nath & Rosenthal (Exhibit 85) and the report of Houlihan Lokey (Exhibit 79).

F. Plaintiffs are overreaching in their interpretation of Norman Goldberg's testimony that the *Eyler* issue was "not a fair issue" on which to negotiate. Plaintiffs' interpretation is that it would have been unfair because U.S. Trust "had promised Foster and Regal not to raise" the issue. There is, of course, no evidence of such promise. A more reasonable reading is that it was unfair in the view of Mr. Goldberg because it was not the correct method of valuation of a stock. As former supervising counsel for the ERISA litigation in the Department of Labor from 1977 to 1985, he should know. The absence of any authority to the contrary from any valuation firm belies the strained interpretation Plaintiffs present here to this Court.

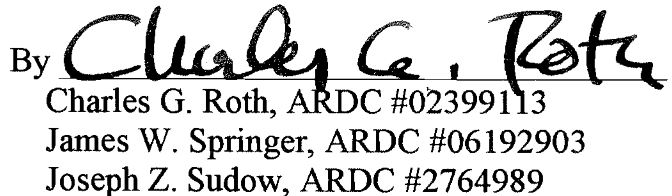
G. Finally, Defendants would have no reason or motive to secure such a promise. Neither U.S. Trust nor Houlihan Lokey could prevent the Department of Labor or the Internal Revenue Service from raising the issue after the transaction. In fact, the government has not raised the issue in spite of repeated invitations by Plaintiffs.

V. CONCLUSION

There is no credible evidence to support Plaintiffs' Motion for Summary Judgment as to these Defendants. In fact, there is no evidence at all regarding the knowledge or intention of Tom Foster on this claimed issue. At best, Plaintiffs can only speculate

regarding the knowledge or intention of Defendant Regal. Plaintiffs fail to present any evidence regarding any purported agreement or promise on behalf of U.S. Trust or Houlihan Lokey to compromise their duties and functions to evaluate and recommend to evaluate the stock. The Plaintiffs' Second Motion for Summary Judgment should be denied.

DEFENDANTS, ELLEN D. FOSTER, as
Executrix of the Estate of Thomas S. Foster,
and Melvyn R. Regal,
by KAVANAGH, SCULLY, SUDOW, WHITE
& FREDERICK, P.C., Their Attorneys

By 
Charles G. Roth, ARDC #02399113
James W. Springer, ARDC #06192903
Joseph Z. Sudow, ARDC #2764989

CERTIFICATE OF SERVICE

The undersigned certifies that a copy of the foregoing document was served upon the following by placing the same in an envelope, postage fully prepaid, and by depositing said envelope in a U.S. Post Office Mail Box in Peoria, Illinois, or by hand delivery, on the 6 day of December, 2002, addressed as follows:

Mr. Dean Rhoads
Sutkowski & Rhoads, Ltd.
124 S.W. Adams St.
Suite 560
Peoria, IL 61602

Mr. Timothy Bertschy
Heyl, Royster, Voelker & Allen
124 S.W. Adams St., Suite 600
Peoria, IL 61602

Ms. Nancy Ross
McDermott, Will & Emery
227 W. Monroe Street
Chicago, IL 60606-5096

Mr. Dean R. Essig
135 Washington Square
Washington, IL 61571

Mr. Bradley M. Jones
Mr. Richard L. Pemberton
Meagher & Geer, P.L.L.P.
4200 Multifoods Tower
33 South Sixth Street
Minneapolis, MN 55402

Mr. Sari Alamuddin
Seyfarth Shaw
55 E. Monroe, Suite 4200
Chicago, IL 60603

Mr. Richard J. Pautler
Thompson Coburn LLP
One Firstar Plaza
34th Floor
St. Louis, MO 63101

Mr. Robert Eccles
O'Melveny & Myers
555 13th St. NW
Washington, DC 20004

Mr. Jeffrey B. Rock
Hasselberg, Rock, Bell & Kuppler
4600 N. Brandywine Drive
Assoc. Bank Bldg. Suite 200
Peoria, IL 61614-5591

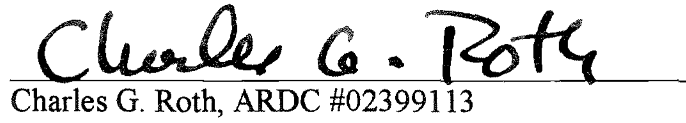
Mr. Stephen D. Gay
Husch & Eppenberger L.L.C.
401 Main Street
Suite 1400
Peoria, IL 61602

Mr. Leland L. Smith
Hinshaw & Culbertson
456 Fulton Street
Suite 298
Peoria, IL 61602-1220

Mr. James C. Bailey
Steptoe & Johnson LLP
1330 Connecticut Avenue NW
Washington, DC 20036

Mr. Roy G. Davis
Davis & Campbell L.L.C.
401 Main Street, Suite 1600
Peoria, Illinois 61602

Mr. Robert Riffle
Elias, Meginnes, Riffle & Seghetti
416 Main Street, Suite 1400
Peoria, Illinois 61602



Charles G. Roth, ARDC #02399113

LAW OFFICES
KAVANAGH, SCULLY, SUDOW, WHITE & FREDERICK, P.C.
301 S. W. ADAMS STREET, SUITE 700
PEORIA, ILLINOIS 61602-1574
TELEPHONE (309) 676-1381
TELECOPIER (309) 676-0324