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David M. Walker, Comptroller General
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Dear David,

I recently read an extract in *Business* Week and then read the entire book Backfire which is the story of last spring's Hewlett Packard ("HP") Compaq proxy fight. I learned that the DOL enforcement problem that I have called to your attention is far broader and more serious than I had originally thought. Notwithstanding that ERISA plans probably were the largest shareholder in both companies and that, therefore, its requirements would be of pivotal significance, ERISA is not even mentioned in the index or in the text. What has happened is that awareness of the existence of ERISA and its conflict of interest prohibitions has disappeared from the market place. I spoke about DOL's problem of enforcement in testimony before Congress last week, a copy of which is on my web site. http://www.ragm.com.

Let me put this in a broader context. The last ten years has seen conflict of interest become the law of the land in the financial community, alas. This was epitomized in the repeal of Glass Steagle. In recent weeks we have all witnessed the scrambling between Wall Street, the Attorney General of New York and the SEC to recreate some kind of protection for investors against Wall Street research and underwriter conflicts of interest. The HP proxy case presents another, if less publicized, kind of conflict of interest — that between the investment management branch of a financial conglomerate and its investment banking operations. My own brief review of the literature reveals no more recent scholarship on the question of fiduciary obligations under ERISA than Betty Krikorian's *Fiduciary Standards in Pension and Trust Fund Management*, published by Butterworth in 1989, 2nd edition in 1994. I am told that there have been no significant cases decided since Bierworth and Engel in the early 1980s. Indeed, I don't recall the Department of Labor bringing conflict of interest enforcement actions since the abortive effort in Carter Hawley Hale and Bank of America in 1984. [I attach a copy of the draft complaint prepared by PWBA, approved by the Solicitor of Labor, but vetoed by the White House as being too activist.] The result of this seems to be that ERISA's prohibition against conflict of interest – the "exclusive benefit rule" – has simply disappeared. It has de facto been repealed. It seems simply to have dropped out of the lexicon of commercial practice. How otherwise can one explain the blatant per se violation of the statute by high level executives in the HP merger, which normally would evoke the risk of the drastic remedies provided in ERISA?

That ERISA's "exclusive benefit" requirement is no longer taken into account is the only explanation that I can have for the parties' conduct in the Hewlett Packard proxy contest. This literally was the largest proxy contest for many years with huge stakes involving financially competent and professionally advised parties. Apparently the applicability of ERISA never occurred to William Hewlett's lawyers; the need to consider ERISA was not brought before the learned Delaware Chancellor and he saw no reason, on his own motion, to require that it be included in the case. Hence the published opinion simply reflects the state of jurisprudence as if ERISA did not exist.

A few extracts from Backfire give unique flavor because they make clear that the parties have no idea that they are clearly breaking a law and that this breach may have serious consequences for them. Let me quote a few of them with interpretive comments:

"Later, Hewlett Packard handed the *bank* a one million dollar contract to investigate how other institutions were voting including an extra one million if Hewlett Packard won the proxy fight." (p. 232) It is plainly impossible to prove that the *bank*, an ERISA fiduciary, was acting for "the *exclusive*…benefit" of HP plan participants when it was being paid by one of the parties in the deal.

"At that point, Griswold [CEO of Deutsche Asset Management ("DAM"), the *bank*, above] slipped through the Chinese wall and asked Barr [Chief Investment Officer of Deutsch Bank Global Investment arm] on the investment side to set up a meeting with HP." [p. 232] This is a per se violation of ERISA, the search by a fiduciary for "consideration" other than the "exclusive benefit" of plan participants.

During the conference call on the day of the vote when DAM was successfully importuned to change its vote the following questions were asked:

"Do we know what the advisors for HP are getting now? I mean, they – I didn't want to ask the question because I was afraid it might be us, but…."

"I believe the answer is we are one of the advisors," Barr answered.

"Isn't there some sort of performance fee associated with that as well?", the unidentified speaker continued. "I have no way of knowing and I'm not even going to ask the question," Barr answered. [p. 235-236] Clearly, DAM knew they were violating some law.

"A few days later Fiorina [CEO of HP] called Griswold to thank him for arranging the meeting with the investment side of the house. "Thanks for going to bat for us," she said, according to trial proceedings. "You know, I'd like to thank you personally. Look forward to doing business with you in the future." Three days later Thornton advised Griswold to erase the message, which he did." [p. 237] Both HP and Deutsche knew that intervention by the investment banking side of Deutsche as a paid consultant to HP– a per se violation of ERISA – was critical to the victorious result.

These simple extracts illumine the extent to which non compliance – possibly utter ignorance - with ERISA has become the law of the land.

It seems particularly important now that investor confidence in America has been virtually destroyed by the much publicized conflicts between research and investment banking that the de facto repeal of ERISA be addressed promptly and effectively. Enron plan participants famously lost $1 billion, in some measure because their trustees took no appropriate action on their behalf. ERISA must be enforced if credibility is to be returned to the public stock market.

I don't think the statute of limitations has run with respect to remedial actions in connection with the HP Compaq merger. Can anything be done to encourage DOL (EBSA) to act within the time limits?

Your friend,

Bob Monks
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