

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS

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U.S. DISTRICT COURT

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Jury Demanded

~~LABORERS' PENSION FUND, ET AL~~
Plaintiff

v.

~~Hugh B. Arnold, ET AL,~~

DEFENDANT

Laboreers' Pension Fund;
Health and Welfare
Department of the Construction and
General Laborers' District Council
of Chicago and Vicinity; Joseph
Coconato; Charles Cohen; James P.
Connolly; Randy Dalton; Mark Deetjen;
Martin T. Flanagan; Charles J.
Gallagher; Wayne E. Healy; J. Michael
Lazzaretto; David Lorig; Gary Lunds-
berg; Robert J. Madden; Tod Masters;
Liberato Naimoli; Dennis Passarelli;
Scott Pavlis; Frank Riley; Roger
Vignocchi; Sam Vinci; and James
S. Jorgensen

Plaintiffs,

v.

Hugh B. Arnold; and
Arnold & Kadjan, a partnership,

Defendants.

DOCKETED

AUG 25 2000

FIRST AMENDED COMPLAINT

1. Plaintiffs Joseph Coconato, Charles Cohen, James P. Connolly, Randy Dalton, Mark Deetjen, Martin T. Flanagan, Charles J. Gallagher, Wayne E. Healy, J. Michael Lazzaretto, David Lorig, Gary Lundsberg, Robert J. Madden, Tod Masters, Liberato Naimoli, Dennis Passarelli, Scott Pavlis, Frank Riley, Roger Vignocchi, Sam Vinci; and James S. Jorgensen (hereinafter collectively referred to as "Plaintiffs") bring this action on behalf of two employee benefit trusts, seeking redress for violations of the Employee Retirement Income Security Act of 1974, as amended, 29 U.S.C. § 1001 et seq. ("ERISA"), pursuant to 29 U.S.C. § 1132(a)(2) and (3), as well as violations of common law duties to Plaintiffs under Illinois law, in connection with Defendants'

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legal representation of the Laborers' Pension Fund and the Health and Welfare Department of the Construction and General Laborers' District Council of Chicago and Vicinity.

JURISDICTION AND VENUE

2. This Court has jurisdiction over this action pursuant to 29 U.S.C. § 1132(e), 28 U.S.C. § 1331, and 28 U.S.C. § 1367(a).

3. Venue in this District is proper pursuant to 29 U.S.C. § 1132(e)(2) and 28 U.S.C. § 1391(b).

PARTIES

4. Plaintiff Laborers' Pension Fund ("Pension Fund") is an employee pension benefit plan as defined in 29 U.S.C. § 1002(2)(A), and a multiemployer plan as defined in 29 U.S.C. § 1002(37)(A).

5. Plaintiff Health and Welfare Department of the Construction and General Laborers District Council of Chicago and Vicinity ("Welfare Fund") is an employee welfare benefit plan as defined in 29 U.S.C. § 1002(1), and a multiemployer plan as defined in 29 U.S.C. § 1002(37)(A).

6. Plaintiffs Joseph Coconato, Charles Cohen, James P. Connolly, Wayne E. Healy, J. Michael Lazzaretto, Gary Lundsberg, Robert J. Madden, Tod Masters, Dennis Passarelli, Frank Riley, Roger Vignocchi, and Sam Vinci (collectively referred to as "Pension Trustees") are trustees of the Pension Fund. They administer the Pension Fund pursuant to the terms of a Trust Agreement entered into by and between the Construction and General Laborers District Council of Chicago and Vicinity, A.F.L.-C.I.O., and a number of employer associations in the building and construction

industry. Plaintiff Pension Trustees are fiduciaries of the Pension Fund as defined in 29 U.S.C. § 1002(21)(A).

7. Plaintiffs Charles Cohen, James P. Connolly, Randy Dalton, Mark Deetjen, Martin T. Flanagan, Charles J. Gallagher, David Lorig, Liberato Naimoli, Scott Pavlis, Frank Riley, Roger Vignocchi, and Sam Vinci (collectively referred to as "Welfare Trustees") are trustees of the Welfare Fund. They administer the Welfare Fund pursuant to the terms of a Trust Agreement entered into by and between the Construction and General Laborers District Council of Chicago and Vicinity, A.F.L.-C.I.O., and a number of employer associations in the building and construction industry. Plaintiff Welfare Trustees are fiduciaries of the Welfare Fund as defined in 29 U.S.C. § 1002(21)(A).

8. Plaintiff James S. Jorgensen is the Administrator of the Pension Fund and the Welfare Fund. He is a fiduciary of both funds as defined in 29 U.S.C. § 1002(21)(A).

9. The Pension Trustees and Welfare Trustees bring this action in their capacities as trustees, on behalf of the participants and beneficiaries, respectively, of the Pension Fund and the Welfare Fund and on behalf of the respective Funds. Plaintiff Jorgensen brings this action in his capacity as Administrator on behalf of the participants and beneficiaries of the Pension Fund and the Welfare Fund, and on behalf of both Funds.

10. Defendant Hugh B. Arnold ("Arnold") is an attorney whose principal place of business is in Chicago, Illinois, within the Northern District of Illinois. He is a partner in the law firm of Arnold & Kadjan.

11. Defendant Arnold & Kadjan is a partnership engaged in the practice of law. Its principal location is Chicago, Illinois, within the Northern District of Illinois.

STATEMENT OF FACTS

12. More than 1,700 employers participate in the Pension Fund and the Welfare Fund (collectively referred to as "the Funds"). More than 16,500 laborers are receiving, or are entitled to receive, pension, health, disability, or other benefits from the Funds.

Contribution Obligations of Participating Employers

13. Each of the participating employers is a party to a collective bargaining agreement with a union that is affiliated with the Laborers' International Union of North America. Those collective bargaining agreements require each participating employer to contribute to each Fund a specified dollar amount for each hour worked by an employee who is covered by the collective bargaining agreement.

14. The trust agreements described in paragraphs 6 and 7 provide that employers' contributions are due on the date prescribed by their collective bargaining agreements, and that the Trustees may establish a grace period within which such contributions may be remitted to the Funds. Pursuant to that provision the Trustees have established a grace period under which contributions may be remitted to the Funds on or before the 10th day of the second month following the month in which the covered work is performed.

15. The trust agreements further provide that if an employer has not remitted its required contributions by the end of the grace period (hereinafter referred to as the "due date"), the employer incurs liability for liquidated damages equal to 10% of the unpaid contributions, plus interest from the date the contributions were due until they are totally paid. Those trust agreements further provide that if the delinquent account is placed with legal counsel for collection, the employer is also liable for the attorneys' fees incurred by the Funds and collection costs.

16. The collective bargaining agreements described in paragraph 13 contain parallel provisions defining a delinquent employer's liability for liquidated damages, interest, attorneys' fees and other collection costs.

Defendants' Services and Fees to the Funds

17. Beginning no later than 1971, Defendant Arnold served as collections counsel for the Plaintiff Funds. In approximately 1979, Defendant Arnold was given the additional role of co-counsel to the Plaintiff Funds. In approximately 1985, defendant Arnold became the sole counsel to the Plaintiff Funds and served in that capacity until February 19, 1998, when he resigned.

18. Defendants Arnold and Arnold & Kadjan were compensated for their services pertaining to collection of delinquent employer contributions. Their principal compensation for that work was contingent fees calculated as a percentage of all money collected.

19. Arnold stated in an affidavit dated April 8, 1998, that the terms of this contingent fee representation were set forth in a letter that he wrote to Samuel Shapiro (who was then counsel to the Funds) on May 6, 1977. The letter provided for a 15% or 20% contingent fee if no suit was filed; a 25% fee if a suit was filed; and a 33-1/3% fee if trial began, complete trial preparation was done, or an employer defaulted on a note.

20. Arnold's affidavit dated April 8, 1998, stated that he and the Funds "have operated pursuant to" the May 6, 1977, letter "[s]ince 1977."

21. The Funds have located no record that this letter was presented to or approved by the Trustees in 1977 or any later year; that any written contingent fee agreement with Arnold or Arnold & Kadjan was ever proposed by defendants or signed by or on behalf of the Trustees or the Funds; or that the Trustees approved any other

statement of the terms on which defendants were paid a percentage of money they collected from delinquent employers.

22. For the period beginning in or about 1985, and continuing until February 1998, Arnold or Arnold & Kadjan received an annual retainer from each Fund for work as Fund counsel and also billed the Funds for certain matters on an hourly basis. Arnold & Kadjan was paid contingent fees for collection of delinquent contributions, and hourly fees for efforts to collect amounts due from injured participants of the Welfare Fund who received third-party payments for their injuries and were obligated to reimburse the Welfare Fund for benefits it had paid them (herein referred to as "subrogation claims").

23. The total fees paid to Arnold and Arnold & Kadjan, on average, exceeded \$1 million per year for the last three full plan years in which he was Fund counsel – the plan years ending in 1995 through 1997.

Defendants' Practices in Regard to Delinquent Contributions

24. At all times between 1985 and February 1998, the Pension Trustees and the Welfare Trustees (collectively "the Trustees") reasonably relied upon Arnold for legal advice and recommendations relating to the policies and procedures the Funds employed in the collection of delinquent contributions.

25. At all times between 1985 and February 1998, the policies and procedures that were employed on the Funds' behalf in the collection of delinquent contributions were largely, if not entirely, the product of Arnold's practices and his recommendations to the Trustees.

26. In the May 6, 1977, letter and in subsequent conversations with the Trustees, Arnold stated that the contingent fees for collections work were justified because he pursued every delinquency claim diligently – no matter how small or

unlikely to result in recovery – and that his large fees on successful collections were balanced by many hours spent on cases that yielded no fees.

27. These statements were not true and misrepresented the extent of the actual collection efforts that were made by Arnold and by Arnold & Kadjan.

28. Contrary to the representations that Arnold made to the Trustees as justification for the contingent fees, Arnold and Arnold & Kadjan failed to make diligent efforts to collect delinquent contributions in substantial numbers of delinquency cases that were referred to Arnold for collection. Arnold did not tell the Trustees that he was not pursuing those particular delinquency cases nor did he seek or obtain their permission not to pursue those cases diligently.

29. Arnold charged the Funds contingent fees in amounts that were not authorized by the May 6, 1977, letter, without disclosing material facts to the Trustees and without obtaining either written or oral agreement to the additional amounts. Examples of such unauthorized fees include:

- (a) At times employers remitted contributions to Arnold instead of to the Funds on or before the due date for those contributions. Arnold billed the Funds for a contingent percentage of these timely contributions, even though he had collected no delinquency for which a contingent fee could properly be charged under the May 6, 1977, letter.
- (b) Arnold negotiated agreements with employers by which they would pay delinquent contributions over a period of time, and included in those agreements contributions for months that were not delinquent at the time the agreement was signed. Arnold billed the Funds for a

contingent percentage of the entire amount he collected under those installment agreements.

(c) Arnold sometimes filed suit without making any attempts to collect the delinquency prior to litigation. By initiating litigation in this manner, Arnold moved these cases up immediately from a 15% or 20% fee to a higher percentage fee of 25%, thus improperly increasing the amounts he charged to the Funds.

(d) Arnold regularly charged contingent fees at 33-1/3% in cases in which he collected contributions from an employer's general contractor, no matter what stage the case was in when it was resolved, even though fees at that rate were not authorized by his May 6, 1977, letter.

30. Upon Arnold's recommendation, the Trustees delegated to Arnold the authority to exercise discretion in the collection process in two respects: (a) to accept, and set the terms of, installment agreements under which employers agreed to pay their delinquent contributions over periods as long as 24 months, and (b) to accept what Arnold judged to be the maximum amount of the prescribed 10% liquidated damages that could be collected from employers on delinquencies more than five years old. Pursuant to these intentional delegations of authority, Arnold exercised discretion in determining the terms of installment agreements for repayment periods of 24 months or less, and in accepting compromises of amounts claimed as liquidated damages in cases over five years old.

31. In other respects Arnold exercised discretion in the collection process without disclosing his exercise of discretion to the Trustees, and made affirmative misrepresentations denying his exercise of discretion:

- (a) Arnold repeatedly told the Trustees that he never entered into any compromises that accepted less than 100% of the principal contributions owed by an employer.
- (b) Arnold repeatedly told the Trustees that his law firm regularly maintained in its files documentation supporting employer challenges that he or the law firm accepted as satisfactory evidence that the employer owed less than the amount of unpaid principal contributions that had been identified by the Funds' auditors and claimed by the Funds.
- (c) Contrary to the representations described in (a) and (b), Arnold regularly accepted challenges from employers and reduced the principal amounts claimed to be due in contributions, without obtaining Trustee approval or maintaining appropriate documentation justifying those reductions.
- (d) Arnold repeatedly told the Trustees that he never entered into any compromises that accepted less than all of the 10% liquidated damages owed on cases less than five years old.
- (e) Contrary to the representations described in (d), Arnold regularly settled cases without collecting the full 10% liquidated damages owed on delinquent contributions in cases less than five years old.
- (f) Arnold repeatedly told the Trustees that he always included 8% interest on installment agreements, calculated from the date the agreement was signed and continuing until the final payment was due, except in a few cases where a court required the rate of 7%.

- (g) Contrary to the representations described in (f), many of the installment agreements Arnold and his law firm accepted from employers included either no interest or interest at a rate far lower than 7%.
- (h) Arnold also regularly gave the Trustees misinformation when he reported particular settlements to them (for installment periods of 24 months or less) or sought their approval for particular installment periods longer than 24 months, regularly stating that particular agreements included an interest rate of 8%, when they actually did not.

32. Arnold systematically failed to demand and attempt to collect interest from delinquent employers for the period between the original due date of delinquent contributions and the date of payment. In the case of agreements providing for payment in installments, he systematically failed to demand and attempt to collect interest from the original due date until the date the installment agreement was signed.

33. The Trustees asked Arnold about the possibility of recovering interest from delinquent employers from the date that contributions were due until they were paid, or until an installment agreement was signed. Arnold advised the Trustees that attempting to collect such interest generally would not be in the interest of the Funds.

34. Contrary to that advice, it is common practice for multiemployer funds to charge interest to employers who frequently pay late, whose contributions are delinquent for long periods, or who remit contributions only after being sued. ERISA provides for recovery of such interest and courts routinely award it in judgments for delinquent contributions. A practice of not attempting to collect interest on such

delinquent contributions effectively allows delinquent employers to grant themselves interest-free loans from the fund, depriving the fund of the time value of that money and generally encouraging employer delinquencies.

35. Arnold and his law firm failed to demand and attempt to collect reimbursement of the Funds' audit costs from many delinquent employers, although the trust agreements and collective bargaining agreements made delinquent employers liable for those costs.

36. Arnold and his law firm systematically failed to demand and attempt to collect reimbursement of his attorneys' fees and other collection costs from delinquent employers whose accounts were placed with him for collection.

37. The Trustees asked Arnold about the possibility of the Funds recovering his attorneys' fees from delinquent employers, but Arnold told them that he was not aware of any funds that collected attorneys' fees on delinquencies and that the only responsibility of the Funds was to collect the principal contributions and the 10% liquidated damages. He advised against trying to collect attorneys' fees from employers except in cases where a suit was filed.

38. Arnold's statements described in paragraph 37 were false. It is standard practice for multiemployer funds to demand reimbursement of their attorneys' fees and collection costs from delinquent employers. ERISA provides for recovery of such fees and costs, and courts routinely award reasonable fees and costs in judgments for delinquent contributions. Arnold himself obtained attorney's fee awards in isolated cases.

Conflicts of Interest

39. Arnold exercised discretion in entering into compromises of the Welfare Fund's subrogation claims.

40. Arnold negotiated compromises between the Funds and certain participating employers whom he represented in delinquency cases, and between the Funds and certain laborers whom he or Arnold & Kadjan represented in subrogation cases. He acted for both sides of these transactions, with clear conflicts of interest.

41. In the conflict-of-interest cases described in paragraph 40, Arnold failed to collect the full amounts due to the Funds in delinquent contributions and interest, or on subrogation claims, and thus benefited his other clients at the expense of the Funds.

Lawsuit for Files, and Escrow Account for Fees Claimed by Defendants

42. In March 1998, after Arnold resigned as counsel to the Funds, he refused to turn over the Funds' legal files unless the Funds paid his outstanding legal fees. He also refused to turn over records showing time spent and expenses incurred on cases in which he was demanding fees. The Trustees filed a lawsuit on April 6, 1998, against Arnold and Arnold & Kadjan, to obtain the release of files on matters then pending so that the Funds' new counsel would have information they needed to represent the Funds in those matters. The Trustees also sought disclosure of defendants' time and expense records so that they could evaluate whether the claimed fee amounts were reasonable.

43. The lawsuit described in paragraph 42 resulted in an agreement of the parties on April 9, 1998, and an Order was entered approving dismissal of the lawsuit based upon the agreement.

44. Pursuant to the agreed settlement, the Funds placed \$345,000 in an interest-bearing escrow account. That amount represented Arnold's estimate of fees owed on cases pending in litigation, plus the contingent fees that would be earned if every employer then remitting payments under an installment agreement that had

been previously negotiated in a delinquent contribution case paid the full amount that it owed under that agreement, and if the Funds paid contingent fees to Arnold & Kadjan on those collected amounts based upon the percentage fees claimed by defendants.

45. An escrow agreement was signed by the parties, dated May 8, 1998.

46. After the money was placed in the escrow account, Arnold disclosed that defendants had no time and expense records showing the work done on delinquency cases, and disavowed any claim for fees on cases not yet brought to judgment or settlement. As a result of that disavowal, the amount in the escrow account greatly exceeds even the amount of fees that defendants claim are owed by the Funds.

47. The files and documents that defendants subsequently provided to the Funds do not include time and expense records from which the Trustees can determine whether the fee amounts still claimed by defendants are reasonable.

48. In many of the delinquency cases in which defendants had negotiated settlement agreements providing for installment payments that were scheduled to continue after Arnold's resignation as counsel, the delinquent employers have since defaulted on their installment agreements. As a result, the Funds have had to incur additional collection costs, including attorneys' fees, to collect many of those delinquencies.

49. Under the May 8, 1998, escrow agreement the money in the escrow account cannot be released without either a joint direction signed on behalf of Arnold and the Funds, or a court order.

50. Since May 8, 1998, defendants have not agreed to release any part of the escrow account and there has been neither a joint direction nor a court order for release of the money in escrow.

51. As the result of information they learned after obtaining Arnold's files, the Trustees initiated an investigation into his practices. As a result of that investigation, they learned for the first time of the falsity of the representations described in paragraphs 26, 31, 33, and 37, and of the fact that Arnold's actual collection practices were different from what he had repeatedly told the Trustees.

COUNT I

**Claim Against Arnold for
Breach of Fiduciary Duty
in Violation of 29 U.S.C. § 1104(a)(1)(A)**

52. Paragraphs 1 through 41 are incorporated herein by reference as if fully set forth.

53. The Funds' claims against participating employers for delinquent contributions, interest, liquidated damages and attorneys' fees are assets of the Funds.

54. In making discretionary decisions to accept less than the full amount of delinquent contributions, interest, liquidated damages and attorneys' fees that participating employers owed, Arnold acted as a fiduciary with respect to the Funds within the meaning of 29 U.S.C. § 1002(21)(A).

55. In making discretionary decisions to accept employers' agreements to pay their delinquent contributions to the Funds in installments, and in setting the terms for such installment payments, Arnold acted as a fiduciary with respect to the Funds within the meaning of 29 U.S.C. § 1002(21)(A).

56. The Welfare Fund's subrogation claims against participants are assets of the Welfare Fund.

57. In making discretionary decisions to accept less than the full amount of the Welfare Fund's subrogation claims from participants, Arnold acted as a fiduciary with respect to the Welfare Fund within the meaning of 29 U.S.C. § 1002(21)(A).

58. Arnold failed to discharge his fiduciary duties with respect to the Funds solely in the interests of the Funds' participants and beneficiaries, thereby violating 29 U.S.C. § 1104(a)(1)(A), in at least the following respects:

- (a) misrepresenting to the Trustees the terms of settlements he entered into;
- (b) misrepresenting to the Trustees the extent of his collection efforts, in false justification of his large contingent fees that greatly exceeded the value of the legal services provided on many specific cases and in the aggregate;
- (c) misrepresenting to the Trustees the advisability of demanding and attempting to collect interest from delinquent employers for the entire period that contributions were delinquent and unpaid;
- (d) misrepresenting to the Trustees the prospects of obtaining reimbursement of the Funds' attorneys' fees from delinquent employers;
- (e) systematically failing to demand or attempt to collect the full amounts of interest, liquidated damages, and attorneys' fees and other collection costs that were due on delinquent contributions;
- (f) charging or attempting to charge contingent fees in excess of those provided by the only existing description of his contingent fee arrangement;

- (g) failing to make diligent collection efforts in many delinquency cases referred to him for collection;
- (h) causing the Funds to adopt and continue practices that did not maximize the Funds' recovery in delinquency cases or provide incentives for employers to remit contributions when they were due, but instead tended to encourage employers to remit contributions late and thereby enabled defendants to collect large amounts of fees in collections cases; and
- (i) acting on behalf of other parties with interests opposed to the Funds.

COUNT II

Claim Against Arnold for
Breach of Fiduciary Duty
In Violation of 29 U.S.C. § 1104(a)(1)(B)

59. Paragraphs 1 through 38 are incorporated herein by reference as if fully set forth.

60. Arnold failed to exercise his discretionary authority in regard to delinquency collection with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims, thereby violating 29 U.S.C. § 1104(a)(1)(B), in at least the following respects:

- (a) failing to make diligent efforts to collect substantial numbers of delinquency claims that were referred to him for collection;
- (b) systematically failing to demand or attempt to collect the full amounts of interest, liquidated damages, and attorneys' fees and other collection costs that were due on delinquent contributions;

- (c) giving the Trustees inaccurate information and advice on the prospects of obtaining reimbursement of his attorneys' fees from delinquent employers; and
- (d) failing to obtain or maintain adequate documentation of the factual grounds for employer challenges to audits that resulted in reducing the principal amount of contributions claimed by the Funds.

COUNT III

**Claim Against Arnold for
Breach of Fiduciary Duty
in Violation of 29 U.S.C. § 1104(a)(1)(D)**

61. Paragraphs 1 through 38 are incorporated herein by reference as if fully set forth.

62. The trust agreements described in paragraphs 6 and 7 vest in the Trustees the discretionary authority to set the terms upon which claims belonging to the Funds may be compromised and to determine the terms upon which counsel to the Funds will be retained and compensated.

63. Arnold failed to exercise his discretionary authority in regard to delinquency collection in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with ERISA, thereby violating 29 U.S.C. § 1104(a)(1)(D), in at least the following respects:

- (a) accepting settlements from employers that did not include the full interest, liquidated damages, attorneys' fees and other collection costs that were due under the trust agreement, without the knowledge or consent of the Trustees;

- (b) giving the Trustees inaccurate information that deprived them of the opportunity to exercise properly the discretion and authority that the trust agreements gave them in relation to settlements; and
- (c) establishing reporting and billing practices that deprived the Trustees of information they needed to evaluate defendants' performance in collection cases and to determine whether defendants' fees for collections were reasonable.

COUNT IV

Claim Against Arnold as a Fiduciary for Causing the Funds to Engage in Prohibited Transactions In Violation of 29 U.S.C. § 1106(a)(1)(B)

64. Paragraphs 1 through 38 are incorporated herein by reference as if fully set forth.

65. The employers participating in the Funds with whom Arnold entered into settlement agreements on behalf of the Funds were parties in interest within the meaning of ERISA, as defined in 29 U.S.C. § 1002(14)(C).

66. Arnold, acting as a fiduciary as alleged in paragraph 55, caused the Funds to engage in prohibited transactions that violated 29 U.S.C. § 1106(a)(1)(B) by causing the Funds to enter into agreements that improperly extended credit to participating employers, in that the agreements systematically failed to require payment of appropriate amounts of interest, liquidated damages, and/or attorneys' fees on delinquent contributions.

67. The prohibited transactions described in paragraph 66 have not been corrected.

COUNT V

**Claim Against Arnold as a Fiduciary for
Causing the Funds to Engage in Prohibited Transactions
In Violation of 29 U.S.C. § 1106(a)(1)(C)**

68. Paragraphs 1 through 31 are incorporated herein by reference as if fully set forth.

69. As persons providing services to the Funds, Arnold and the law firm Arnold & Kadjan were both parties in interest within the meaning of ERISA, as defined in 29 U.S.C. § 1002(14)(B).

70. Arnold, acting as a fiduciary as alleged in paragraph 55, caused the Funds to engage in prohibited transactions that violated 29 U.S.C. § 1106(a)(1)(C), and that were not exempt under 29 U.S.C. § 1108(b)(2), by causing the Funds to pay more than reasonable compensation for the legal services he and his law firm performed in relation to the collection of delinquent contributions.

71. The prohibited transactions described in paragraph 70 have not been corrected.

COUNT VI

**Claim Against Arnold as a Fiduciary for
Causing the Funds to Engage in Prohibited Transactions
In Violation of 29 U.S.C. § 1106(a)(1)(B) and (D)**

72. Paragraphs 1 through 31 are incorporated herein by reference as if fully set forth.

73. Arnold, acting as a fiduciary as alleged in paragraph 55, caused the Funds to engage in prohibited transactions that violated 29 U.S.C. § 1106(a)(1)(B) and (D) by causing the Funds to enter into agreements that systematically accepted reductions in the amount of contributions claimed by the Funds without complying with the requirements of Prohibited Transaction Class Exemption 76-1 (e.g., without

first making diligent, systematic efforts to collect, without creating or maintaining adequate records of the grounds for accepting employer challenges, and without making a reasonable determination in writing that all or part of the amounts due were uncollectible or could not be collected at reasonable expense).

74. The prohibited transactions described in paragraph 73 have not been corrected.

COUNT VII

Claim Against Arnold as a Fiduciary for Engaging in Prohibited Transactions In Violation of 29 U.S.C. § 1106(b)(1)

75. Paragraphs 1 through 38 are incorporated herein by reference as if fully set forth.

76. Arnold, acting as a fiduciary as alleged in paragraph 55, engaged in prohibited transactions by dealing with the assets of the Funds in his own interest, in violation of 29 U.S.C. § 1106(b)(1), in at least the following respects:

- (a) by exercising discretionary authority as a fiduciary to settle claims for delinquent contributions in such a manner as to influence the amount and timing of his contingent fees from the Funds;
- (b) by systematically failing to demand that employers reimburse the Funds for his law firm's attorneys' fees, in circumstances where demanding full reimbursement of such fees would have created a risk of exposing the unreasonable level of his contingent fees to the Trustees;
- (c) by systematically failing to demand that employers reimburse the Funds for his law firm's attorneys' fees, thus making it easier for Arnold and his law firm to settle cases and collect large amounts of

fees from the Funds without having to invest the time and effort normally required to resolve contested cases;

- (d) by systematically failing to demand or attempt to collect full amounts of interest and liquidated damages due on delinquent contributions, where a change in these aspects of his collection practice could have reduced the volume of employer delinquencies and thus reduced the contingent fees paid to Arnold and Arnold & Kadjan; and
- (e) by causing the Trustees to adopt practices regarding delinquency collection that maximized the number of delinquency cases that would be referred to defendants for collection and thereby increased the fees payable to defendants.

77. The prohibited transactions described in paragraph 76 have not been corrected.

COUNT VIII

Claim Against Arnold as a Fiduciary for Engaging in Prohibited Transactions In Violation of 29 U.S.C. § 1106(b)(2)

78. Paragraphs 1 through 31 and 39 through 41 are incorporated herein by reference as if fully set forth.

79. Arnold, acting as a fiduciary as alleged in paragraphs 55 and 57, engaged in prohibited transactions in violation of 29 U.S.C. § 1106(b)(2), by dealing with the Funds on behalf of parties with opposing interests, namely, by negotiating compromises of claims for delinquent contributions and subrogation claims owed to the Funds by other clients that he or Arnold & Kadjan represented.

80. The prohibited transactions described in paragraph 79 have not been corrected.

COUNT IX

**Claim Against Both Defendants for
Participating in Prohibited Transactions
in Violation of 29 U.S.C. § 1106(a)(1)(C)**

81. Paragraphs 1 through 29 and 69 are incorporated herein by reference as if fully set forth.

82. As the result of Arnold's pattern of misrepresentation to the Trustees regarding material facts pertaining to the activities of Arnold and Arnold & Kadjan in the collection of delinquent contributions from employers, Arnold and Arnold & Kadjan received excessive compensation from the Funds for their collection services.

83. The payment of this excessive compensation to Arnold and to Arnold & Kadjan constituted prohibited transactions in violation of 29 U.S.C. § 1106(a)(1)(C) that were not exempt under 29 U.S.C. § 1108(b)(2).

84. The prohibited transactions described in paragraph 83 have not been corrected.

COUNT X

**Claim Against Both Defendants for
Participating in Prohibited Transactions
in Violation of 29 U.S.C. § 1106(a)(1)(C)**

85. Paragraphs 1 through 38 and 69 are incorporated herein by reference as if fully set forth.

86. As the result of Arnold's pattern of billing for fees that were not properly chargeable under the terms of the 1977 letter, which was the only written description of the contingent fee arrangement, as detailed in paragraph 29, Arnold and Arnold & Kadjan received excessive compensation for their services in the collection of delinquent contributions from certain employers.

87. As the result of defendants' own collection practices and policies that were adopted by the Funds upon Arnold's recommendation, which had the effect of maximizing the volume of delinquent contributions that were referred to defendants for collection, as detailed in paragraphs 31 through 38, Arnold and Arnold & Kadjan received excessive compensation for their services in the collection of delinquent contributions generally.

88. The payment of this excessive compensation to Arnold and to Arnold & Kadjan constituted prohibited transactions in violation of 29 U.S.C. § 1106(a)(1)(C) that were not exempt under 29 U.S.C. § 1108(b)(2).

89. The prohibited transactions described in paragraph 88 have not been corrected.

COUNT XI

Claim Against Both Defendants for Breach of Contract under the Common Law of Illinois

90. Paragraphs 1 through 28 are incorporated herein by reference as if fully set forth.

91. The terms of the contingent fee agreement pursuant to which Arnold and Arnold & Kadjan were paid for their collection efforts on behalf of the Funds were set forth in Arnold's May 6, 1977, letter to Samuel Shapiro, who was then counsel to the Funds.

92. That contingent fee agreement provided for large fees to be paid on successful collections in exchange for Arnold's promise to make diligent collection efforts on all delinquency claims -- no matter how small or unlikely to result in recovery.

93. Neither Arnold nor Arnold & Kadjan performed as required by the terms of the contingent fee agreement. To the contrary, rather than make diligent collection efforts on all delinquency claims, Arnold and his law firm failed to make diligent efforts to collect delinquent contributions in substantial numbers of delinquency cases that were referred to Arnold for collection, without the knowledge or consent of the Trustees.

94. By this failure to diligently pursue collection efforts in a substantial number of the delinquency cases referred to them, Arnold and Arnold & Kadjan breached the terms of the contingent fee agreement.

95. Because Arnold did not perform as required by the contingent fee agreement, he and Arnold & Kadjan were not entitled to the high fees they were paid on successful collections.

COUNT XII

Claim Against Arnold for Fraudulent Misrepresentation under the Common Law of Illinois

96. Paragraphs 1 through 38 are incorporated herein by reference as if fully set forth.

97. Arnold knowingly made false representations to the Trustees about facts material to the collection services he rendered and material to his own compensation for collection work. He also knowingly billed the Funds for payment of contingent fees without telling the Trustees that he was not entitled to the fees he was requesting. Arnold's fraudulent misrepresentations and false billing activities included:

- (a) misrepresenting that he pursued every delinquency claim diligently in false justification of his contingent fee schedule;
- (b) misrepresenting the terms of settlements into which he entered;

- (c) misrepresenting the prospects and advisability of collecting interest from delinquent employers for the entire period between the due date for contributions and the date on which those contributions were fully paid;
- (d) misrepresenting the prospects of obtaining reimbursement for the Funds' attorneys' fees from delinquent employers;
- (e) billing the Funds for a percentage of certain timely payments that employers remitted to Arnold instead of to the Fund, even though Arnold had collected no delinquency for which a contingency fee could properly be charged;
- (f) including contributions that were not delinquent in installment agreements upon which Arnold charged and collected contingent fees for each installment that was paid;
- (g) failing to advise the Trustees that Illinois law required a written agreement fully describing the terms of any arrangement by which he would be compensated by a contingent fee; and
- (h) failing to disclose material facts that the Trustees needed in order to determine whether Arnold's compensation was reasonable.

98. As the Funds' attorney, Arnold was a fiduciary of the Funds under Illinois law and owed his clients a duty to inform them of the material facts described in paragraphs 28 through 29 and 31 through 38 regarding his collection and billing activities. Arnold's failure to make disclosures of those material facts constituted fraudulent misrepresentations under Illinois law applicable to attorneys.

99. By these fraudulent misrepresentations to the Trustees and this failure to make material disclosures, Arnold intended to obtain excessive fees from the Trustees.

100. Because the Trustees justifiably relied on Arnold's fraudulent misrepresentations and on his silence regarding material facts that he failed to disclose, the Funds paid Arnold larger amounts in fees than they otherwise would have paid, and were unable to recover all of the sums that they were entitled to recover from employers as interest, liquidated damages, and attorney's fees. The Funds were damaged thereby.

COUNT XIII

Claim Against Arnold for Undue Influence under the Common Law of Illinois

101. Paragraphs 1 through 38 are incorporated herein by reference as if fully set forth.

102. From approximately 1985 until February 1998, Arnold was sole Counsel to the Funds. In that capacity, Arnold exerted undue influence over his clients and failed to make full and fair disclosure of material facts relating to his practices regarding delinquency collection and compensation for collection work, in at least the following respects:

- (a) Misrepresenting and failing to disclose to the Trustees the possibility of recovering his fees and costs from delinquent employers (a possibility that would have provided a greater net recovery for the Funds and an alternative to Arnold's contingency fee arrangement);
- (b) Misrepresenting the extent of his delinquency collection efforts and his success in collecting amounts owed by employers;

- (c) Failing to disclose to the Trustees the possibility of recovering interest on delinquent contributions beginning on the due date for those contributions (a possibility that could have discouraged delinquencies and thus reduced the volume of collections work and contingent fees);
- (d) failing to advise the Trustees that Illinois law required a written agreement fully describing the terms of any arrangement by which he would be compensated by a contingent fee; and
- (e) failing to disclose material facts that the Trustees needed in order to determine whether Arnold's compensation was reasonable.

103. By his undue influence, Arnold sought to obtain and did obtain the Funds' continued acquiescence in practices that regularly produced fees for Arnold and Arnold & Kadjan that were higher than would have been paid otherwise, and that reduced the Funds' collection of interest, liquidated damages, attorneys' fees and costs from delinquent employers. The Funds were damaged thereby.

COUNT XIV

Claim Against Both Defendants for Breach of Fiduciary Duties Owed by Lawyers to Clients under Illinois Law

104. Paragraphs 1 through 41 are incorporated herein by reference as if fully set forth.

105. As attorneys to the Funds, Arnold and Arnold & Kadjan owed duties of loyalty and honesty to the Funds pursuant to Illinois law. Both defendants breached these fiduciary duties in at least the following respects:

- (a) representing both the Funds and individual employers in delinquency cases, where conflicts of interest existed;

- (b) representing both the Funds and individual participants in subrogation cases, where conflicts of interest existed;
- (c) billing the Funds for contingency fees to which neither Arnold nor Arnold & Kadjan were entitled;
- (d) misrepresenting to the Trustees the terms of settlement agreements;
- (e) failing to demand or attempt to collect the full amount of interest, liquidated damages, and attorneys' fees and collection costs that were due on delinquent contributions;
- (f) giving the Trustees inaccurate advice on the prospects of collecting interest from delinquent employers as required by the trust agreement and collective bargaining agreements;
- (g) giving the Trustees inaccurate advice on the prospects of obtaining reimbursement for the Funds' attorneys' fees from delinquent employers; and
- (h) misrepresenting to the Trustees the extent of efforts by Arnold and Arnold & Kadjan to collect all delinquencies and their degree of success in collecting delinquent contributions and liquidated damages.

106. As a result of defendants' breaches of their fiduciary duties, the Funds paid Arnold and Arnold & Kadjan larger amounts in fees than they otherwise would have paid, were unable to recover all of the sums they were entitled to recover from employers as interest, liquidated damages, attorney's fees and other collection costs, and were damaged thereby.

COUNT XV

**Claim Against Both Defendants for Release
of \$345,000 in Escrowed Fee Amounts**

107. Paragraphs 1 through 51 and 69 are incorporated herein by reference as if fully set forth.

108. Based upon the information that the Trustees have learned since early 1998, as alleged in this Complaint, including Arnold's pattern of misrepresentation in justification of his excessive fees and his breach of contract to make diligent collection efforts in all cases referred to him, defendants are not entitled to any part of the \$345,000 that was deposited in escrow as described in paragraph 44.

109. Under Illinois law, because the employment relationship between the defendant attorneys and their clients, the plaintiff Funds, has been terminated, defendants are entitled to payment only for the fair value of the services they actually rendered to the Funds, and not for any contractually specified fees if such fees exceed the fair value of those services.

110. For the reasons detailed in paragraphs 26 through 29 and 46 through 48, the contingent fees specified in Arnold's May 6, 1977 letter far exceed the fair value of the services actually rendered to the Funds by Arnold and Arnold & Kadjan.

111. Payment of the \$345,000 to defendants would cause them to receive excessive compensation under Illinois law governing attorneys.

112. Payment of the \$345,000 to defendants would also constitute a prohibited transaction under 29 U.S.C. § 1106(a)(1)(C).

113. Plaintiffs are therefore entitled to an order for release of the \$345,000 from escrow, together with all earnings on the account, free of any claim by defendants. In the alternative, plaintiffs are entitled an order requiring Arnold to sign

a joint direction to the escrow agent that all money in the escrow account be released to the Funds.

PRAYER FOR RELIEF

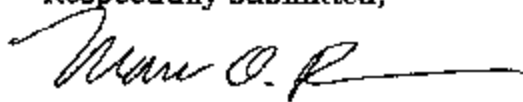
WHEREFORE, plaintiffs pray that judgment be entered on their Complaint, awarding to the Funds:

- (1) the amounts that were paid to defendants as contingent fees in delinquency claims and hourly fees on subrogation claims;
- (2) all losses that resulted to the Funds from defendants' systematic failure to demand or attempt to collect interest, liquidated damages, auditors' fees, and other collection expenses on delinquency claims;
- (3) all losses that resulted to the Funds from defendants' improper representation of an opposing party as well as the Funds in a negotiated settlement of a claim for delinquent contributions or a subrogation claim, including all legal fees paid to defendants in such cases;
- (4) the amounts that were paid to defendants by the Funds as fees for services during the period of defendants' breach of fiduciary duties as described in Count XIV.
- (5) a declaration that the Funds are entitled to the release of all money in the escrow account described in paragraph 44, free of any claim by defendants;
- (6) an order requiring Arnold to sign any joint direction that may be necessary to release the escrow account to the Funds;
- (7) prejudgment interest on the amounts described in paragraphs (1), (2), and (3);

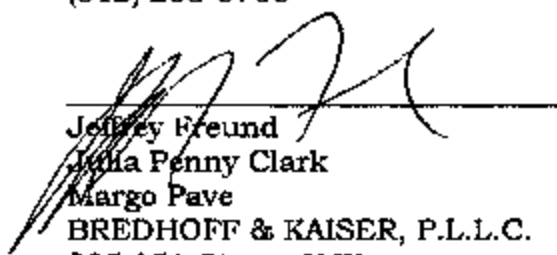
- (8) reimbursement of the Funds' attorneys' fees and other expenses of this action; and
- (9) such other and further relief to which the Funds may be entitled, at law or in equity.

PLAINTIFFS REQUEST A JURY TRIAL ON ALL CLAIMS PROPERLY TRIABLE BY JURY.

Respectfully submitted,



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