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***Fiduciary Responsibility***

## Court Certifies Class Action of Pension Plans That Invested in JPMorgan Securities Lending

A class action was certified Aug. 4 by the U.S. District Court for the Southern District of New York consisting of private and government pension plans that used the securities lending program of JPMorgan Chase Bank N.A. to invest in the now-defunct Sigma Finance Inc. (*Board of Trustees of the AFTRA Retirement Fund v. JPMorgan Chase Bank N.A.,* S.D.N.Y., No. 09 Civ. 686 (SAS), 8/4/10).

The class certified by Judge Shira A. Scheindlin is made up of at least 76 government and Employee Retirement Income Security Act plans that allegedly lost millions of dollars when Sigma collapsed in September 2008.

The plans alleged in their lawsuit that JPMorgan breached its ERISA and state law-imposed fiduciary duties by investing in Sigma when JPMorgan should have known that it was a poor investment. The plans asserted that their investment agreements with JPMorgan required JPMorgan to invest only in "conservative, high-quality, low-risk" investment vehicles. They claimed that the Sigma investment did not live up to this standard.

JPMorgan objected narrowly to the class certification motion. It argued that of the 76 plans, five of the plans were "direct account holders" that should not be included in the class because they each had the ability to direct their plans' investments, unlike the other plans that were members of collective investment vehicles.

The court was not persuaded by this argument, saying that JPMorgan had "exaggerated" the differences between the direct account holders and other class members. "For purposes of determining liability, it is JPMC's conduct—rather than that of the individual class members—that is the key issue," the court said, adding that it was JPMorgan that selected Sigma as an investment option for its clients.

### Plaintiffs Pleased With Certification

The plans' attorney, Peter H. LeVan Jr. of Barroway Topaz Kessler Meltzer & Check, Radnor, Pa., told BNA Aug. 5, "We are pleased by Judge Scheindlin's thorough and well-reasoned decision to certify a class of all entities that suffered substantial losses as a result of JPMorgan's imprudent and conflict-ridden decision to purchase and hold $490 million of Sigma medium-term notes on behalf of its securities lending clients."

"The class representatives and other class members placed their trust in JPMorgan, both as a custodian bank and as their securities lending agent. JPMorgan breached that trust by failing to act prudently and by placing its own financial interests above those of its clients. JPMorgan imprudently purchased and continued to hold the Sigma notes, even as individuals within JPMorgan itself were warning of Sigma's impending collapse," LeVan said.

He added, "Unbeknownst to class members, JPMorgan also began providing Sigma with repo financing during this period, making hundreds of millions of dollars in fees for itself while subordinating the legal rights of the class members. We look forward to a trial on the merits and fully expect to establish that JPMorgan failed to comply with the important fiduciary obligations it owed to its securities lending clients."

### 'Deck Stacked Against' Defendants

Attorney René E. Thorne of Jackson Lewis, New Orleans, told BNA Aug. 5 that, "Where, as here, you have institutional plaintiffs (i.e., the plans rather than multiple, individual plaintiffs/participants), defendants sometimes face a more difficult battle proving individualized issues to defeat class certification." Thorne was not an attorney in the case, but she frequently represents employers and management in ERISA class actions.

"Although the arguments raised by defendants regarding predominance and superiority were sound, arguably the deck was stacked against them from the beginning. In addition, whenever, as here, the court hangs it hat on cases suggesting that the focus in a breach of fiduciary duty case is on the defendant's, not the plaintiffs', conduct, that focus tends to gut any argument the defendant might make regarding individualized investment behavior by the plaintiffs," she added.

### Consolidated Cases

In early 2009, three separate lawsuits were filed against JPMorgan by an ERISA plan and two government plans. The lawsuits, which were later consolidated, alleged that JPMorgan breached its fiduciary duties under ERISA and state law with respect to its decision to invest in medium-term notes (MTNs) offered by Sigma (85 PBD, 5/6/09; 36 BPR 1153, 5/12/09).

According to the complaints, Sigma is a Delaware corporation organized for the sole purpose of issuing debt securities for its Cayman Islands parent company. The debt securities at issue were secured only by a "floating lien" on the assets of Sigma, which were subject to subordination to the lien interests of Sigma's other creditors.

According to the lawsuits, shortly after JPMorgan purchased a substantial amount of Sigma MTNs, using the cash collateral

held by class members, financial analysts warned that structured investment vehicles (SIVs) like Sigma lacked liquidity in the credit market and that sharp declines in the market value of assets backing many SIVs threatened their viability.

In the summer of 2007, Sigma was the largest of approximately 30 SIVs in the world, according to the complaints. The lawsuits charged that despite these analyst warnings, JPMorgan "buried its head in the sand and refused to heed the warning signs." According to the lawsuits, analyst predictions later proved true when Sigma's creditors seized over $25 billion of its approximately $27 billion of assets in late September and early October 2008. This left Sigma with just under $2 billion as security for approximately $6.2 billion of outstanding MTNs and other secured debt, the lawsuits alleged.

According to the complaints, Sigma was placed into receivership in early October 2008. The lawsuits also alleged that JPMorgan's involvement with Sigma MTNs was not limited to investments on behalf of its pension plan clients. While JPMorgan was investing the plans' money in Sigma MTNs, JPMorgan also earned substantial fees and interest through providing short-term repurchase (repo) financing for Sigma, according to the complaints.

The lawsuits charged that JPMorgan's financial interest as Sigma's "repo financier" was in direct conflict with its fiduciary responsibility to the pension funds.

**Plans Move for Class Certification**

The plans asked the court to certify the following class: "All plans and entities for which JPMorgan Chase Bank, N.A., pursuant to a securities lending agreement, invested cash collateral, either directly or through a collective investment vehicle, in one or more debt securities of Sigma Finance, Inc. and continued to hold those debt securities as of the close of business on September 30, 2008."

JPMorgan objected on narrow grounds to the class certification motion. It argued that five of the class members were direct account holders and that their interests were in conflict with the other class members. These direct account holders retained authority over their accounts and could direct JPMorgan to hold or sell particularly securities. The other potential class members did not have this authority.

The court rejected this argument and found that these direct account holders would not stand in the way of class certification. The court said all the class members, including the direct account holders, were party to standard investment guidelines that required JPMorgan to invest in conservative, high-quality, low-risk investments.

The court also said that JPMorgan uniformly recommended to both direct account holders and the portfolio managers for the other class members that they should hold the 2009 Sigma MTNs. "[T]he overwhelming dominant question is whether the 2009 Sigma MTNs were a prudent investment and the evidence offered to prove or disprove plaintiffs' prudence claims is common to all class members," the court said.

The court added that even if there were slight variations in the class members' investment guidelines and portfolios, this would not take away from the fact that the class members were alleging that the Sigma MTNs were "too risky an investment for *any* securities lending participant by virtue of the basic, low-risk, high-quality structure that a securities lending program entailed."

The plans were represented by Joseph H. Meltzer and Peter H. LeVan Jr. of Barroway Topaz Kessler Meltzer & Check, Radnor, Pa.; Milo Silberstein of Dealy & Silberstein, New York; Gregory M. Nespole of Wolf Haldenstein Adler Freeman, New York; Bradley E. Beckworth and Brad Seidel of Nix Patterson & Roach, Dangerfield, Texas; and David L. Wales of Bernstein Litowitz Berger & Grossman, New York.

JPMorgan was represented by Lewis Richard Clayton and Jonathan H. Hurwitz of Paul Weiss Rifkind Wharton & Garrison, New York.

*By Jo-el J. Meyer*

*The full text of the opinion is at http://op.bna.com/pen.nsf/r?Open=jmer-882jnr.*



ISSN 1523-5718