LEGAL UPDATE

Teacher's pet

Europe's pension funds are becoming more involved in class actions worldwide, tempted by law firms offering lucrative yields in return for a share of the winnings.
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Corruption. It's an inconvenient truth that plagues the private and public sector. The World Bank believes it 'impedes investment', highlighting that those countries that can confront corruption tend to attract more investment.

Such has been the focus put on tackling corruption that Transparency International produces an annual Corruptions Perceptions Index (CPI). It focuses on the public sector, but such charts can serve as a good indication of what's going on elsewhere in the countries. The 2018 CPI ranks Denmark as number one in the world for transparency. That's why it came as a shock when one of its major banks was caught up in the one of the biggest money laundering scandals in history.

The extent of the scandal was published in a report in September 2018; what transpired rocked the financial world. Around €200 billion of transactions from thousands of suspicious customers were made through an Estonian branch of the bank over a nine-year period. The fallout from such scandals undeniably has financial implications for the company; at the start of November 2019, Danske shares were trading at a near seven-year low.

Repercussions

When a scandal like this occurs, investor returns suffer, which is why many seek redress. And when many investors are impacted, class actions and multi-claimant cases often make an appearance. As long-term investors, holding a large amount of assets, pension funds often suffer from these corporate scandals.

Grant and Eisenhofer director, Olav Haazen, notes: "They will have purchased the stock or the bond at a price they consider to be good, based on the representations made by the company…when some aspects of that turn out not to be true…the stock price drops. When that happens the assets of the pension fund will drop, because the stock that they hold will be worth less."

Class action and multi-claimant cases in Europe are increasing in popularity, he says, noting that they are shifting somewhat from the United States to other countries in the world. In Europe, he says there are very few precedents in each country but more and more have some experience.

CMS litigation partner, David Bridge, has also seen the "proliferation of collective actions within Europe", particularly the UK in recent years. "This has been driven by a perceived desire at a European level and within certain jurisdictions to provide access to justice for individual claimants, typically affected by mass harm at the hands of corporate defendants and without the financial means to otherwise pursue their claims on an individual basis."

The European Commission (EC) first published proposals for a European-wide collective redress procedure in 2008. "While anxious to avoid importing what some considered to be the excesses of the US class action procedure into European law, a concern remained that claimants, and in particular consumers, should be able to obtain effective and affordance redress both in national and cross-border disputes," Bridge explains.

It was not until June 2013 that the EC published its non-binding recommendation that member states implement systems to facilitate collective redress. In April 2018, it published a proposal for a new European Union

(EU) law, which would introduce the first European-wide approach to consumer class actions.

"The proposed new law seeks to enhance the protection afforded to EU consumers by enabling qualifying entities to launch representative actions on behalf of consumers and introduce stronger sanctioning powers for consumer authorities. It is expected to progress through parliament in 2019/2020," Bridge says.

A new pupil

European pension funds are also taking more interest in class action cases around the world. DRRT managing partner, Alexander Reus, says European pension funds have been "opportunistically looking at these loss recovery opportunities in the United States taking a leading role as lead plaintiffs or in opt-outs".

"The same has occurred outside of the United States where investors must opt-in to litigation to preserve their rights, and the rights of their members, to receive compensation for fraud in the market. We see the trend continuing as loss recovery becomes an important component of fiduciary responsibilities," he adds.

One of these is the UK's Norfolk Pension Fund, a Local Government Pension Scheme that earlier this year acted as the lead plaintiff on a class action against pharmaceutical company, Puma Biotechnology. The company was found liable for securities fraud and because of this its share price was inflated by $4.50 – 15 per cent higher than the price at which its share currently trades at.

At the time, Norfolk Pension Fund investment and actuarial manager, Alex Younger, said the purpose of taking part in the class action was to "enable the fund to maximise returns for the benefit of present and future pensioners, reduce the burden on its sponsoring employer, to advance good governance, and to support the deterrent effect for future misconduct in financial markets".

Bridge also notes that pension funds are, to some extent, tempted by "potentially lucrative returns that they could benefit from by participating in large collective actions in which they have an interest, and their willingness to treat litigation as an investment, backed by professional third-party litigation funders and insurers with deep pockets".

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Prospects and process

If a pension fund is going to seek redress then there needs to be a good chance of winning, but what are the chances? Haazen responds: "Worldwide in these international very large scandals that we litigate, we don't lose those cases. They always get settled but the settlement is always for a very significant amount."

A settlement is quite common, he explains, with many settled out of court, however in some jurisdictions a settlement will still need court approval. Pension funds are also tempted to take action because they get a "ready-made case", says Haazen.

He explains that law firms will have already investigated the case and analysed the data and will know whether it's worth the pension fund participating. "If losses are minor it may not be worth participating," Haazen says.

Cost and time are two other pull factors. "We try to minimise their time commitment," Haazen notes, "so we will select local counsel, we will have already investigated the legal merits of the case and the economics of it, and the factual side of things…and we only advise on cases that are viable". Disclosure – the requirement to submit relevant documents or testify – is also kept to a minimum, he says.

"For pension funds we arrange the funding, we usually fund these cases ourselves, which means we work on a contingent fee, so there are no costs. In some jurisdictions we have to get insurance against adverse costs, that's insurance in case you lose the cases – we pay for that too."

Bridge describes this as the "quid pro quo" for both parties. "Those funders will, in return, be entitled to share in the proceeds of any recovery made by the pension funds, in return for funding the significant costs of the litigation, with the insurers paid for underwriting the risk of liability for adverse costs if unsuccessful.

According to Bridge, sophisticated law firms typically court pension funds with large claims and try to persuade them to issue proceedings, together with other parties, with the promise that the litigation is 'risk free'. A recent example is the case in the UK, against the Royal Bank of Scotland, which settled for a reported €936 million.

"The trend looks set to continue, with the latest investor claim being reported this month (November) to involve a potential action following the high-profile collapse of Woodford Investment Management and its Equity Income Fund," Bridge says. "No doubt pension funds will be approached, if not already, with a view to encouraging them to join a claim. Whilst past performance is no guarantee of future results, trustees may be willing to take the plunge and the courts look set to be busy for the foreseeable future." ■

Notable cases

A round up of some of the most notable cases involving European pension funds

Volkswagen

In 2015, after the US Environment Agency issued a notice of violation of the Clean Air Act against Volkswagen AG (VW) and other affiliates, resulting in a potential fine of up to $18 billion, VW admitted to installing a so-called 'defeat device software' in various models, affecting 11 million vehicles worldwide. This dramatically reduces the nitrogen oxide emissions of diesel cars during the testing, thereby distorting the outcome of official emission tests. DRRT and Grant and Eisenhofer, as part of a law firm consortium, are representing almost 600 institutional investors claiming over €5 billion in damages from VW and Porsche. This group includes at least two-dozen European pension funds, international pension funds and sovereign wealth funds. The model case of the investors is currently pending at the Higher Regional Court of Braunschweig with a collateral case against Porsche pending at the Regional Court of Stuttgart. Various other groups have also filed lawsuits against VW bringing the total damages sought on behalf of investors in the German action to over €8 billion.

Danske Bank

In September 2018, an independent investigation ordered by the bank's board of directors revealed that more than €200 billion in suspicious transactions passed through the Estonia branch from Russian sources. The report found that Danske's senior leadership had known of the problem as far back as 2013, but failed to make appropriate disclosures even after the laundering was confirmed in 2014. Once the scandal came out, Danske's shares dropped from DKK 250.10 on February 27, 2018, to DKK 125.65 on October 24, 2018, losing over $10 billion in market cap as a result. DRRT and Grant and Eisenhofer are representing a group of 230 institutional investors, including many European pension funds, claiming over DKK 5 billion in damages. In March 2019, local counsel filed the first group actions by institutional investors against Danske Bank A/S in the Copenhagen District Court on behalf of 168 institutional investors claiming over DKK 3 billion in damages, which was followed by a second group of 62 institutions in October 2019 seeking an additional DKK 2 billion.

Puma Biotechnology

Norfolk Pension Fund, which served as the lead plaintiff, won a class action against US pharmaceutical company, Puma Biotechnology, in which it was found liable for securities fraud. The jury in the United States District Court for the Central District of California found that Puma, which is listed on the NASDAQ, and its CEO and chairman, Alan H. Auerbach, committed securities fraud and are liable to compensate a class of investors who purchased Puma shares between 22 July 2014 and 13 May 2015 at prices inflated by the defendants' misconduct. The jury found that Puma and Auerbach knowingly misled investors about the effectiveness of a breast-cancer drug called Neratinib, sold commercially under the name Nerlynx. The jury determined that the fraud inflated Puma's share price by $4.50, which is over 15 per cent of the price at which Puma's shares currently trade and which may cost defendants, when all claims are counted, up to $100 million.

Major banks

A number of pension funds have joined a class action that has filed against five banks that unlawfully manipulated the foreign exchange market between 2007 and 2013. The claims are being made against Barclays plc, Citibank, Royal Bank of Scotland plc, JP Morgan and UBS. This legal action follows the European Commission's (EC) ruling on 16 May 2019 that the above banks violated EU competition law. The five banks have now been fined more than $8.5 billion collectively by 11 regulators globally. The EC held that the banks had exchanged commercially sensitive information and trading plans, coordinating their trading strategies via two cartels.