



# Board of Retirement Regular Meeting

## Sacramento County Employees' Retirement System

---

**Agenda Item 23**

**MEETING DATE:** August 19, 2020

**SUBJECT:** Securities Litigation Claim-Filing Services

**SUBMITTED FOR:** \_\_\_ Consent        X   **Deliberation and Action**      \_\_\_ **Receive and File**

---

### **RECOMMENDATION**

Staff recommends the Board authorize the Chief Executive Officer to approve a multi-year contract with Financial Recovery Technologies (FRT) to provide securities litigation-related services.

### **PURPOSE**

This item supports the Strategic Management Plan by improving effective oversight and management of securities litigation, which is an aspect of the investment program.

### **DISCUSSION**

#### **The Proposed Contract**

SCERS' current contract with FRT ends on August 31, 2020. FRT has proposed a contract extension through December 31, 2023 at a total cost of \$150,000 (i.e., three annual fees of \$45,000 plus a pro-rated fee of \$15,000). FRT will also charge a 20 percent contingency fee for recoveries from antitrust cases, due to the additional complexity of such litigation. However, FRT would deduct its fees by \$15,000 for each year in which FRT's recovery for SCERS falls below a certain threshold (as explained in greater detail below). For the reasons to follow, Staff recommends the Board approve extending FRT's services.

#### **Financial Recovery Technologies**

As an institutional investor, SCERS sometimes experiences investment losses caused by the misconduct of securities issuers and others. SCERS can recover damages for such losses by participating in securities litigation. These recovery opportunities involve varying levels of investor participation, from being an "active" lead plaintiff to being a "passive" claims-filer in settled cases. Historically, SCERS has focused on passive recovery efforts rather than active, a practice the Board recently re-approved in January 2020.

---

FRT is a Massachusetts-based technology company that specializes in passive loss recovery for institutional investors. FRT helps clients identify recovery opportunities and file claims in: (1) U.S.-based settled securities class actions; (2) class actions relating to monopolies and other forms of market manipulation; and (3) non-U.S.-based “group litigation” (similar to U.S.-based class actions).

FRT began providing claims-filing services for SCERS in 2016. Specifically, SCERS entered into a self-renewing contract with FRT in September 2016, which was superseded by a fixed-term one-year contract that began in September 2019. That contract is set to expire on August 31, 2020.

Before FRT, State Street Bank performed claims-filing for SCERS as part of the custodian bank relationship. State Street did not charge SCERS a separate fee for claims-filing, although State Street estimated at the time that approximately \$10,000 of the fees it charges annually was attributable to that service.

From 2016 to July 2020, claims filed by FRT have yielded approximately \$805,000 for SCERS. During that period, SCERS paid FRT approximately \$235,000 in annual and contingency fees, bringing SCERS’ net recovery to approximately \$570,000.

#### Has SCERS Received Value From FRT?

Of course, the fact that SCERS has recovered \$570,000 from FRT filings is not conclusive that SCERS should continue the relationship. After all, if SCERS had continued using State Street as its sole claims-filer, SCERS would still have received a recovery of some amount. Thus, the more pertinent question is whether SCERS has received, and will continue to receive, value from FRT commensurate with the additional expense. Staff believes the answer is “yes,” for the following reasons:

- Recovering investment losses caused by violations of law is an important part of SCERS’ duty of prudent administration. Because that duty is fiduciary in nature, it is appropriate for SCERS to engage a service-provider for whom claims-filing is its core business rather than its secondary or tertiary business. In 2005, Stanford Law Review published an influential article arguing that custodian banks have proven to be inconsistent claims-filers for pension funds. See James D. Cox & Randall S. Thomas, *Letting Billions Slip Through Your Fingers: Empirical Evidence and Legal Implications of the Failure of Financial Institutions to Participate in Securities Class Action Settlements*, 58 Stan. L. Rev. 411 (2005). For that reason, the authors recommended that funds engage an independent third-party claims-filing service as a best practice.
- There is evidence that FRT has a superior system for identifying filing opportunities and maximizing recovery. In 2016, FRT performed an audit of State Street’s claims-filing for SCERS from 2012 to 2015. FRT’s audit uncovered dozens of missed opportunities and sub-optimal recoveries. After identifying those missed opportunities, FRT filed additional and amended claims on SCERS’ behalf. FRT’s efforts resulted in an additional gross recovery of \$325,770, or an additional net recovery of \$244,328 after deducting fees.

- 
- For each year from 2017 to 2019, FRT performed an analysis showing the advantage of its proprietary “aggregate/disaggregate” approach to claims-filing over the “disaggregate only” approach used by State Street. For each claim FRT filed that yielded a recovery, FRT calculated the difference between (1) a hypothetical recovery under State Street’s “disaggregate only” approach versus (2) the actual recovery under FRT’s mixed approach. FRT’s approach yielded a higher level of recovery each year, sometimes significantly so. In addition, FRT agreed to give SCERS a \$15,000 rebate for any year in which the difference in recovery turned out to be less than 10%. SCERS’ recovery in 2019 was too high to qualify for the rebate, but SCERS received the rebate in 2017 and 2018. (This rebate arrangement will remain part of the 2020-2023 proposed contract.)
  - FRT monitors for and files claims in connection with U.S.-based antitrust class actions and non-U.S.-based securities “group litigation.” Those services are expertise- and resource-intensive, which favors SCERS’ continued use of FRT services over the custodian.
  - Staff has found that FRT provides a user-friendly and turnkey solution to managing SCERS’ securities litigation participation. FRT has responsive customer service, a user-friendly online portal, and automatic email notifications about important litigation developments. That combination results in a convenient means for staff to meet its responsibility for monitoring and managing SCERS’ loss recovery efforts.

Prepared By:

/S/

---

Stephen Lau  
General Counsel

Reviewed By:

/S/

---

Eric Stern  
Chief Executive Officer