

Where Leading Plaintiffs' Lawyers Are Leading Now

"Heads Up" is *Of Counsel's* periodic series of interviews with top plaintiffs' lawyers, tapping their perspective on the legal and business issues that loom on the horizon, as well as the predictable impact of significant recent or current cases. The idea is to provide our readers with a sense of what's coming next and prophylactic measures to better manage exposure across a range of issues and industries.

In this issue, we look at the new genus of "mini-Madoff" cases that have implicated leading financial institutions, talk to a retirees' advocate about the alleged abrogation of pension plan commitments by major corporations, and discuss the potential impact of a significant employment reclassification case on franchisers nationwide.

Much-Discussed Pathologies

As of this writing, the government's three-year investigation of insider trading in the hedge fund industry is no doubt the highest-profile regulatory/criminal event affecting the financial services industry since the arrest of Bernie Madoff. That said, there are enough ongoing but less-publicized allegations against the world's leading banks and institutions to keep plaintiffs' bar busy for years to come.

A whole species of mini-Madoff cases has arisen, for example. Steve Berk of Berk Law PLLC in Washington, DC, handled four of them: three against Bank of America and a fourth, *Benson v. JP Morgan Chase Co. Bank, N.A.*, filed by Berk in tandem with Cotchett Pitre & McCarthy. The US District Court for the Northern District Court of California dismissed conspiracy claims against JP Morgan in that case but refused to dismiss charges that Washington

Mutual Inc. (now JP Morgan) aided and abetted fraud.

We spoke to Berk about these cases, which exceeded \$1 billion in claims.

How do you believe the defendants in your cases abetted Ponzi schemes?

Steve Berk: As a threshold matter, the banks knew through inference and circumstantial evidence that they were dealing with illegal activity; the predicate for any Ponzi scheme. As we alleged in *Benson*, they could see that the victims of the scheme thought that they were buying CDs, as their checks had notations that included interest rates, maturity dates, and amounts. Small problem! The illegal entity was not a bank, nor was it licensed to sell securities.

The general pattern is the same in my other cases, although, instead of CDs, the bogus investments used by the con artist and supported by the bank included bridge loan participations, commodities trading, and, wacky as it sounds, paying investors to surf the Internet.

I have been surprised by the flagrant and outrageous nature of these schemes. In *Benson*, the CDs were backed by the Union Trust of Switzerland. Sounds legitimate. But the most cursory review would have revealed that UTS was not a bank, but merely a shell corporation. It did not do business and had no employees.

Another case involved a legitimate, yet modest size, bridge loan that was properly documented with a UCC filing. There was no reason to question the loan itself. But what you could question was that the perpetrator of the scheme repeatedly sold that same loan 50 or 100 times. That's flagrant.

To be sure, you need brains to steal hundreds of millions of dollars! Brains and a willingness to say and do anything to convince investors to join and stay in the game.

In *Benson*, the Ponzi scheme was cooked up by a man named William Wise who has a long history of securities violations that should have appeared on any bank's radar screen. But in many instances, the banks weren't just negligent, they were complicit. We alleged, for example, that a WAMU branch manager advised Wise to obtain a remote deposit facility and the software and hardware to independently wire large amounts of money anywhere in the world. Basically, they set him up as his own unregulated bank.

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Why did these banks think that the overt malfeasances that you're alleging, and the attendant risks, were justified in terms of anticipated business benefit?

Steve Berk: There were, of course, the much discussed cultural pathologies driven by a focus on profit at any risk coupled with the sincere belief that the bubble would never burst. Under such circumstances, there is no perception of risk. Risk does not exist.

Also, internal pressures on bankers cannot be overestimated. When they're forced to compete against the traders in their own organizations, the pressure to generate profits, to not be viewed as second-class citizens, can overwhelm anyone. Bankers are human.

Some of the culpable bankers are by no means Wall Street kingpins. Actually, they're branch managers in places like West Hempstead, Long Island (where one of our Bank of America cases developed). Suddenly they're confronted by the sharpest minds in

the business driving up in a Mercedes. It's easy to be seduced.

How widespread are mini-Madoffs among leading banks? Are we looking at a whole new species of lawsuit? If so, how would you describe the exposure facing institutional defendants?

Steve Berk: I'd have to say they are very widespread, and, yes, it is a new species of lawsuit. I myself got involved in four cases against global banks, so imagine how much more must be out there.

But the type of exposure ahead may be very different. The Supreme Court has made clear that aggrieved investors cannot pursue claims of aiding and abetting liability in securities transactions. Accordingly, our cases were built on historic common law precedent that date back to Blackstone. By simplifying the game, we can make it a more dangerous one for banks to play if, in fact, they've ignored or abetted fraud.

What lessons for banks do these cases underscore?

Steve Berk: The banks know all the lessons already—about compliance, about due diligence, about the internal cultural factors that encourage outright theft. The question is whether it will be worth their while to apply those lessons once the economy rebounds and the profits big enough to dwarf the penalties and judgments. Will they even be able to apply those lessons over the great expanse of their organizations and control their people at so many levels?

I tend to think that criminal penalties will need to be stiffened as a message that both traders on Wall Street and branch managers in Long Island can hear.

Bait and Switch

One of the dramatic impacts of the financial collapse was the precipitous decline in