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Memorandum

TO: BATA

DATE: August 17, 2012

FR: Executive Director

W. I. 1254

RE: State Attorneys General Settlement with JP Morgan Chase & Co.

Background

On July 7, 2011 twenty five State Attorneys General (“AGs”), including the California Attorney General entered into a settlement agreement (“Settlement Agreement”) with JP Morgan Chase & Co. (“JPMC”). The Settlement Agreement provides for a \$92,000,000 total payment by JPMC of which \$65,500,000 currently is in an escrow fund to be used to make payments to certain JPMC swap counterparties and other municipal entities. Last month BATA received notice from the claims administrator managing the escrow fund that BATA is eligible to receive a portion of that fund, as further described below. The remaining moneys are to be used for entities covered under agreements with the Securities and Exchange Commission and the Office of the Comptroller of the Currency, as well as for enforcement purposes by the AGs. To date BATA has not received notices of eligibility to participate in any other part of the settlement.

The Settlement Agreement resulted from an investigation of the AGs into violations of antitrust laws, state consumer protection laws and false claims statutes. In that investigation the AGs found evidence of illegal price fixing and/or price manipulation in the sale of interest rate swaps and other derivative products primarily during the period from 2001 through at least 2005. BATA purchased two interest rate swaps in 2005 from JP Morgan Chase Bank, N.A. a subsidiary of JPMC, and is therefore eligible to participate in the settlement. JPMC has not admitted the allegations of wrongful conduct.

The investigation resulting in the Settlement Agreement is part of a broader ongoing investigation conducted by the AGs into the municipal bond derivatives industry. The AGs have entered into a number of settlement agreements with other financial institutions. The California State Attorney General’s office has informed us that BATA is not eligible under the terms of those agreements to participate in those settlements.

BATA was informed of its opportunity to participate in the AGs’ settlement with JPMC last month, and must indicate its intention to do so by August 23, 2012, per rules set by the claims administrator in charge of disbursing settlement funds.

Although this issue is related to litigation, the opportunity for BATA participate in the AGs' settlement does not fall within one of the Brown Act litigation closed session provisions. Given staff's recommendation below to proceed with the settlement, we are discussing this item in open session.

BATA's Portion of the AGs' settlement

If BATA elects to participate in the settlement, BATA will receive \$604,757.82 ("BATA's Settlement") and release JPMC from any further liability related to these claims. BATA would also give up its right to sue JPMC for claims for damages related to the conduct covered by the Settlement Agreement, whether by suing JPMC on its own, or by suing in or participating as part of a settlement class in another action against JPMC underway in the United States District Court, Southern District of New York. That case is titled *In re Municipal Derivatives Antitrust Litigation*.

The named plaintiffs in *In re Municipal Derivatives Antitrust Litigation* have reached a settlement with JPMC pursuant to which JPMC has agreed to pay a settlement amount of up to \$44,575,000 (\$44.6 million, rounded up for convenience) for the benefit of a proposed settlement class, which would include BATA. That settlement has not yet been approved by the court.

As noted above, BATA's Settlement is \$604,757.82. The amount is being paid from a fund of \$65.5 million, the entire amount of which has been allocated to eligible municipal entities. We have been advised that none of the \$65.5 million is allocated to notice and administration costs, taxes and expenses, attorneys' fees and costs and distribution costs ("Ancillary Costs"). In the *In re Municipal Derivatives Antitrust Litigation* class action settlement, up to \$44.6 million will be used to make payments to class members. It will also be used for Ancillary Costs. Lead counsel in the *In re Municipal Derivatives Antitrust Litigation* have not yet proposed a plan for distributing up to \$44.6 million or determined what part of the \$44.6 million will be allocated to make payments to class members.

Although BATA's allocated share of any recovery resulting from the *In re Municipal Derivatives Antitrust Litigation* class action settlement pertaining to JPMC, should it be approved by the court, may be greater or less than BATA's Settlement under the AG's Settlement Agreement, it could likely be less if the Ancillary Costs are paid.

How BATA's Settlement was calculated

BATA's Settlement was based on a formula developed by the AGs with the assistance of an independent economic expert. The Settlement Agreement provides that the AGs have the right to adopt a formula they deem appropriate for payments from the settlement fund.

The formula uses an overcharge methodology established by the AGs that takes into account the estimated overcharge percentage assigned for the general type(s) of swaps BATA entered into

with JPMC in a particular time period. It defines dollar overcharge (which is used in estimating the overcharge percentage) as the difference between (1) the amount of estimated profit attributed to BATA's swaps, and (2) the estimated profit JPMC would have earned absent the alleged conduct. BATA's share equals the percentage that BATA's estimated dollar overcharge is to the total overcharge for all eligible to participate in the \$65.5 million multiplied by the settlement fund.

As noted above, by participating in the AGs' settlement, BATA is giving up its right to pursue a different formula for recovery against JPMC. BATA could pursue a different formula only if it decided not to participate in the AGs' settlement and instead brought its own action or participated in the *In re Municipal Derivatives Antitrust Litigation* class action suit.

Staff's Recommendation

Staff recommends accepting this settlement. The alternatives are: (1) declining to participate and instead be part of the *In re Municipal Derivatives Antitrust Litigation* under which we think it is likely that BATA will receive less than \$600,000 in the proposed settlement up for judicial approval later this year; or (2) to sue JPMC on our own, with an uncertain outcome and likely at considerable expense.

We have also consulted with the California Attorney General's office and been informed that this settlement does not compromise any possible claim by BATA against JPMC in the LIBOR investigations that are now underway. We do not know whether JPMC was involved in LIBOR rate manipulation. We will not know the extent or duration of manipulations of LIBOR rates for some time. Various State Attorneys General are investigating that matter now and we will provide additional information relevant to BATA's swaps to you as we become informed of developments.

As an additional penalty for the alleged misconduct, we have suspended JPMC's investment banking unit, JP Morgan Securities LLC from serving as a senior managing underwriter of BATA bonds for a one-year period beginning August 14, 2012.



Steve Heminger

SH:aw