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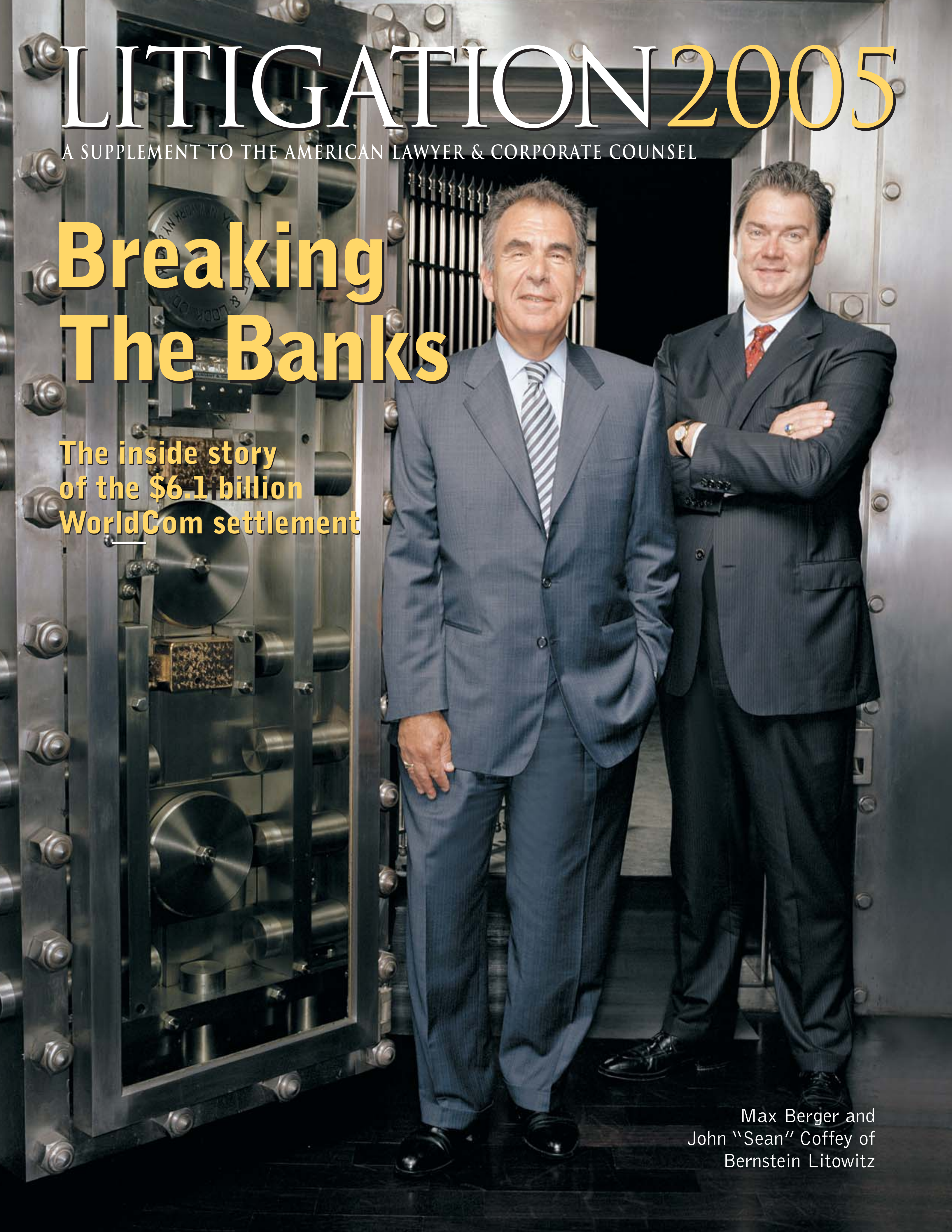
Breaking The Banks

The inside story of the $6.1 billion WorldCom settlement



Max Berger and John "Sean" Coffey of Bernstein Litowitz

Breaking the Banks

When 17 underwriters agreed to pay more than $6 billion to settle a securities class action arising from the WorldCom debacle, it set a new precedent. Only five months later, an Enron class settlement topped $7 billion. Law firms representing banks in such massive cases might want to rethink their strategies.

ON A COLD MORNING LAST MARCH, JOHN "Sean" Coffey was preparing for the biggest trial of his life a few blocks from the federal district courthouse in lower Manhattan. For three years, the 49-year-old former prosecutor had been jousting with the investment banks, directors, and auditor for WorldCom, Inc. He was supposed to start picking a jury the next day.

Coffey and his partner Max Berger at New York's Bernstein Litowitz Berger & Grossmann had already reached settlements with 14 banks. They agreed to pay nearly $3 billion to resolve claims that they had failed to perform adequate due diligence on WorldCom's massive public bond offerings. One of the underwriters, Citigroup, Inc., had also paid more than $1 billion to settle stock fraud claims. JPMorgan Chase & Co. was the lone holdout with deep pockets. Throughout the skirmishing, JPMorgan and its hard-charging counsel at Skadden, Arps, Slate, Meagher & Flom appeared headed for trial. But that morning Berger was locked in settlement talks directly with the client, and Coffey was eager for news from the bargaining table.

Berger's call came at about 11 A.M. Coffey picked up the phone. With a nod to the old *Family Feud* game show, he asked: "Survey says?"

Berger was ebullient: "We got the two, baby."

"The two" was the $2 billion that JPMorgan agreed to pay to settle. As reported by *The Wall Street Journal*, it was 46 percent, or $630 million, more than the bank could have settled for ten months earlier. "They caved!" Coffey and his partners cried.

With the JPMorgan deal, the total amount of settlements topped $6 billion. These recoveries—which are expected to include more than $300 million for lawyers' fees—made it the largest securities class action recovery in history. The record was short-lived, however. In August the class action involving Enron Corp. passed $7 billion in recoveries.

In both cases, Wall Street banks have picked up the bulk of the tab. (The nonbank defendants in WorldCom—Arthur Andersen and former WorldCom directors and officers—contributed only about $126 million.) But those billions in settlement money don't reflect the total impact of these cases. A ruling issued in the WorldCom class action has prodded financial institutions to rethink how they raise capital in the public markets.

The law firms representing banks in such actions might also need to rethink the way they approach the next megacase. In the WorldCom class action, one firm—Skadden—represented 17 underwriters.

BY ANDREW LONGSTRETH
PHOTOGRAPHY BY BEN BAKER

The Bernstein Litowitz team included (from left to right) Max Berger, Steven Singer, J. Erik Sandstedt, Chad Johnson, and John "Sean" Coffey.

The settlement dollars don't reflect the total impact of the case. Rulings issued in the WorldCom class action have prodded financial institutions to rethink their duties to investors in raising capital.

Facing a tireless lead plaintiff that wanted to send a message to Wall Street and a judge who appeared unsympathetic to the defendants, Skadden gave no signs of letting the case go gently—at least not on the plaintiffs' terms. For three years, up to the brink of trial, the firm put on a classic chest-pounding defense, resisting offers to settle.

It was an unusually aggressive gamble for such a high-stakes case. Skadden's clients had originally appeared ready to hang together. But the united front began to crumble when the banks ousted Citigroup, which then proceeded to make its own deal in May 2004. The remaining defendants soldiered on together for another ten months. But two weeks before jury selection, Bank of America Corporation broke away and settled.

Facing a prisoner's dilemma, every bank decided to look out for its own interests. One by one, each settled, until JPMorgan stood alone. And being the last one out came with a hefty price.

What follows is the tale of a remarkable case. At stake were billions of dollars, professional reputations, and the ways of Wall Street.

The WorldCom fraud took years to build but only months to unravel. In March 2002 the company announced that the Securities and Exchange Commission had asked to look at information relating to its financial health. In June, WorldCom announced its intention to restate earnings by a dizzying $3.8 billion. On July 21 the telecom filed for Chapter 11 protection. It was the largest filing ever in terms of total assets, surpassing Enron's by more than $40.5 billion.

This spectacular collapse caught the attention of both plaintiffs lawyers and politicians, an alliance that was the unexpected consequence of congressional reform efforts in the mid-1990s. The Private Securities Litigation Reform Act changed the rules of securities class actions. No longer would an unseemly race to the courthouse decide control of these cases. Instead, judges would select lead plaintiffs based on the size of their potential loss. Congress wanted more institutional investors involved in these suits, as a check on marauding lawyers. In practice, it was an invitation to public employee pension plans to jump into the fray.

The New York State Common Retirement Fund was headed by state comptroller H. Carl McCall, a Democrat, who wanted to become governor. Corporate governance became one of his springboard issues. In July 2002 he was planning an "investors summit" that would assemble the largest pension funds in the country to encourage a new code of conduct on Wall Street. "We want to send a message that if people want to do business with us, they have to show us that their ethical standards are basically above reproach," said McCall. Behind the scenes, the Retirement Fund's general counsel, Kristina Burns, had already invited Bernstein Litowitz and Barrack, Rodos & Bacine to represent the fund in a massive class action against WorldCom.

But who would pay defrauded investors? WorldCom was bankrupt, Arthur Andersen was in a death spiral, Ebbers and the other directors and officers couldn't cover the losses. The potential for a major recovery came only from the investment banks.

The two firms had represented McCall in a class action against Cendant Corporation and its auditor in which they recovered $3.2 billion, at that time the largest settlement in history. Bernstein and Barrack lawyers also contributed generously to McCall's political campaigns, giving a total of $140,000 between 1998 and 2002, according to *Forbes* magazine. Berger, who had handled the Cendant case, brought in his partner Coffey. In four years Coffey, a former Latham & Watkins partner and federal prosecutor, had emerged as a star at Bernstein Litowitz. He had recently represented the Baptist Foundation of Arizona in a case against Arthur Andersen. The case ended after a few weeks of trial when Arthur Andersen coughed up $217 million. For Coffey, who loves a big stage, the WorldCom case was a dream come true.

Suits had already been filed against WorldCom in the Southern District of New York. But the state claims overshadowed the others: McCall's fund claimed more than $300 million in stock losses. So on July 1 Bernstein Litowitz and Barrack, Rodos filed a motion in the Southern District of New York on behalf of the Retirement Fund to become lead plaintiff. In August federal district court judge Denise Cote chose the fund to represent a class of shareholders and a class of bondholders that would later allege nearly $30 billion in losses.

Coffey knew Cote well. She had been his superior in the U.S. attorney's office in Manhattan. He didn't expect any breaks from her, but he didn't mind that she was looking out for any possible "victims" in the case.

But who would pay them? By then WorldCom was essentially judgment-proof. Another key defendant, Arthur Andersen, was in a death spiral after being convicted of obstruction of justice for its role in Enron. (The conviction was later reversed, too late to save Andersen.) Bernard Ebbers and the other directors and officers couldn't cover the losses. The potential for a major recovery came only from the banks.

AROUND THE TIME COFFEY was getting his assignment, Jay Kasner was receiving his. The 49-year-old Skadden partner led a large team of lawyers hired to represent two large syndicates that underwrote more than $15 billion in two bond offerings for WorldCom in May 2000 and May 2001. The latter was the biggest in history. The syndicates included 17 of the most prestigious and successful financial institutions in the world: JPMorgan, Citigroup, Bank of America, Credit Suisse Group, Lehman Brothers Inc., and The Goldman Sachs Group, Inc., among others. They were the kind of clients any lawyer would love to have.

Kasner, who declined to comment for this article, is a Skadden lifer. He's spent 25 years at the firm, where he's helped raise the profile of the securities litigation department. He has a rainmaker's presence—impeccably dressed, articulate, and charming. One of his most prominent recent wins came in 2003. While litigating the WorldCom case, Kasner and his partners scored a major victory for Merrill Lynch & Co., Inc., winning the dismissal of two class actions that alleged massive stock losses had been caused by misleading research in Merrill's analyst reports.

Both allies and foes describe Kasner as tough. "He's an excellent lawyer," says plaintiffs attorney I. Stephen Rabin of New York's Rabin & Peckel, who has faced off against Kasner. "He takes no prisoners. He fights very hard. He's not willing to settle for less than what he thinks his clients are entitled to. He will never admit that there's anything to be said for the other side."

The coleads of each offering, Citigroup and JPMorgan, hired Skadden. It was a high-profile, high-stakes, highly lucrative assignment. The syndicate agreements provided that for any judgment, the individual banks would be liable for the pro rata share of bonds they underwrote. Under the agreement, control of the case (and obligation to pay legal fees) was also distributed on a pro rata basis. That meant that JPMorgan and Citigroup would call the shots.

Citigroup faced the most exposure—more than $50 billion by its own analysis. In addition to the bond claims, it was accused of stock fraud for statements made by its former star analyst Jack Grubman. Because of its unique situation, Citigroup hired additional counsel—Paul, Weiss, Rifkind, Wharton & Garrison. As it happened, Citigroup needed an independent voice.

A TIRELESS LEAD PLAINTIFF, ALAN HEVESI AND HIS STAFF ENTHUSIASTICALLY EMBRACED THE WORLDCOM CASE.

THE TWO SIDES WERE FAR apart from the beginning. According to a defense lawyer and two plaintiffs lawyers, the underwriters' offer was around $35 million. The plaintiffs, meanwhile, were asking for about $10 billion.

Berger suspected that hawks in the underwriters' camp were blocking any reasonable discussion of settlement. But there was good reason to believe that Berger's case itself was unreasonable. It rested on the theory that the underwriters were expected to thoroughly inspect WorldCom's financial health before issuing securities to the public. The law was not clear on the extent of their duty to investigate their client.

But Berger was motivated by a zealous client of his own. In the fall of 2002 McCall lost his bid for governor, and Alan Hevesi was elected as the new state comptroller. Hevesi and his staff enthusiastically embraced the WorldCom action. On his first day as general counsel for the new comptroller, Alan Lebowitz began delving into the details of the case. It would be his number one priority for the next two-and-a-half years. "No brief was submitted without the stamp of our approval," he says.

As repeated settlement talks ordered by Cote failed to make headway, conflict developed within the defendants' camp. According to two lawyers familiar with the matter, the syndicate members had asked Citigroup to pay a premium for its share of the bond claims because it was the only underwriter also charged with stock fraud. Citigroup rejected the idea.

The conflict came to a head around June 2003. In a conversation that would radically change the course of the case, Kasner called Edward Turan, in-house counsel at Citigroup. According to Turan, Kasner made it clear that the syndicate wanted Citigroup out. (Kasner declined to comment.)

"We felt it was the wrong decision," says Turan, who nonetheless says he wasn't surprised by the syndicate's move.

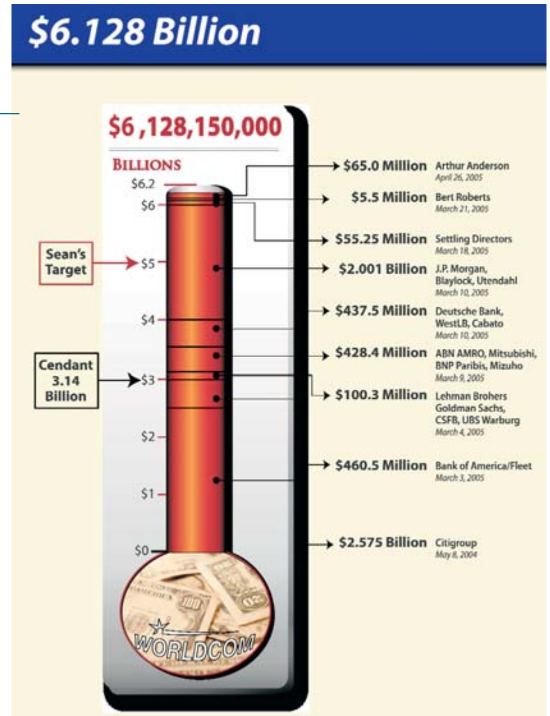
The implications were huge. Kicked out of the syndicate and no longer represented by Skadden, Citigroup, the defendant facing the most exposure, had effectively been unleashed to settle the case.

Lawyers for Paul, Weiss had already been looking for an exit strategy. They had good reason for wanting out. Coffey and company seemed to get everything they wanted in Cote's courtroom. The case was also moving at a breakneck speed, which neutralized the defense strategy of delay. Cote allotted just 60 days of depositions to each side.

Citigroup had a unique agenda among the banks. Its new CEO, Charles Prince, had made cleaning up the company's image a priority. To help do so, Prince and Citigroup general counsel Michael Helfer had lured litigator P.J. Mode to come in-house from the firm now known as Wilmer Cutler Pickering Hale and Dorr, where Helfer had been a partner. One of Mode's main assignments was to work with Brad Karp, Citigroup's relationship partner at Paul, Weiss, to develop a legal strategy for the WorldCom and Enron litigation.

Mode and Karp found leverage within Cote's ruling on class certification for shareholders. Few had been surprised that Cote certified a class for bondholders. But the size of the class she certified for shareholders was dramatic and controversial in its scope. It covered shareholders who bought WorldCom stock over a 38-month period, comprising 793 trading days. The theory was that every purchaser of WorldCom stock during that period relied on the opinion of Jack Grubman. Citigroup appealed the shareholder class certification, and in December 2003 the U.S. Court of Appeals for the Second Circuit granted an interlocutory review.

THIS BERNSTEIN LITOWITZ CHART TRACKS THEIR RISING RECOVERY AS THE DEFENDANTS SETTLED, ONE BY ONE.



The Second Circuit rarely grants such motions, and it presented both sides with an uncertain future. The potential that Cote's ruling would be overturned or altered—thus reducing the class size—worried lawyers for the plaintiffs. A decision against Citigroup, meanwhile, could raise the bank's price of settlement. For Citigroup and the plaintiffs, the Second Circuit argument was the equivalent of a trial date.

Settlement finally began to seem like a real possibility. In early 2004, Paul, Weiss partner Martin London called Berger and asked if they could meet. The offices of Paul, Weiss and Bernstein Litowitz are both located in the UBS Building, across the street from Radio City Music Hall. It was a short trip for London from the twenty-sixth floor to Berger's thirty-

BRAD KARP (LEFT) AND ERIC GOLDSTEIN OF PAUL, WEISS FORGED AN EARLY EXIT STRATEGY FOR THEIR CLIENT CITIGROUP.

eighth floor office. Berger liked what London had to say. "We were dancing around each other," says Berger. "But I came away from that meeting feeling it was possible to get a deal."

Talks continued. On February 4, Coffey and Berger rode the elevator down to London's office. Berger laid out their position: "We understand we have issues in our case, but we have sex appeal in our case, too."

As the date for oral argument drew closer, the discussions turned more serious. On May 6, with four days remaining, New York comptroller Hevesi and Citigroup CEO Prince arrived for a meeting in the jury room of federal district court judge Robert Sweet. Months earlier, Cote had asked Judge Sweet, a former Skadden partner, to assist magistrate judge Michael Dolinger with the negotiations. The gathering felt like a major summit. "I hate the idea of walking out of here without a deal," Sweet told the parties.

For the next four hours, Sweet ushered lawyers from both sides in and out of the jury room. They exchanged numbers until they reached a range of $2.5–2.9 billion. Around 4 P.M., Sweet invited all parties into the room. "The number is $2.65," he announced.

At the conclusion of the negotiations, lawyers for both sides headed back uptown to the UBS Building. Coffey and Berger met Paul, Weiss partners Eric Goldstein and Joyce Huang and associate Susanna Buergel in a Paul, Weiss conference room. Amid boxes of cold pizza and Chinese takeout, they drafted the terms of the settlement. Around 11 P.M., Coffey and Berger left their cell phone numbers with Goldstein and went home. The Paul, Weiss team worked through the night. The next day, Friday, May 7, the plaintiffs team reconvened at Paul, Weiss and executed the agreement, subject to approval from Citigroup's board.

While the Paul, Weiss team was signing papers with the plaintiffs, Kasner was in court arguing discovery issues. He won't comment on whether he knew Citigroup was in negotiations to settle, but he gave no indication that he did. "It seems to me that Kasner . . . had no idea [the talks] were going on," says Berger.

He found out soon enough. On Monday morning, May 10, a black sedan picked up Eric Goldstein, Brad Karp, and Martin London at their homes in Manhattan and headed downtown to give the news to Judge Cote. On their way, Goldstein left a message for Kasner, detailing the settlement.

Kasner was heading to the Second Circuit, apparently believing that Citigroup would be arguing the class certification issue. According to several lawyers involved in the case, Kasner was livid with Paul, Weiss when he finally heard the settlement. He was upset in particular with partner Martin London. Kasner thought that London told him he was only negotiating for the stock claims.

London says he would be "stunned" if Kasner believed he misled him. Kasner declined to comment.

Although the law was not clear on the extent of an underwriter's duty to investigate a client, the case rested on the theory that the underwriters were expected to thoroughly inspect WorldCom's financial health before issuing securities to the public.

THE SETTLEMENT PUT THE syndicate in a difficult spot. When negotiating the deal with Citigroup, the plaintiffs lawyers assigned $1.45 billion of the $2.65 billion to the class of bondholders; the balance would go to the class of shareholders. (Paul, Weiss stayed silent on the division.) The plaintiffs looked at the percentage of bonds that Citigroup underwrote and wanted the same pro rata amount from each of the remaining underwriter defendants. That calculation would later be referred to as the "Citi formula."

Citigroup's settlement deal required that an offer based on that formula be made to all the syndicate members. As reported by *The Wall Street Journal* last spring, if they all had accepted on the same terms, the plaintiffs would have brought in an additional $2.8 billion. The plaintiffs gave syndicate members 45 days to respond. Kasner's clients refused to budge. According to a source close to the negotiations he countered with an offer of $300 million from the entire syndicate, effectively declining to take the Citi deal.

Berger kept at it. On May 27, still within the 45-day window, he again wrote to Kasner, this time offering 12 junior underwriter banks a 25 percent discount off the Citigroup formula. The deal was good for two weeks. The letter went unanswered, says Berger.

Who declined the deals? Kasner won't comment. One in-house lawyer of a syndicate bank, who requested anonymity, downplays Skadden's role. Each bank had its own in-house advisers, says this lawyer, as well as a sophisticated understanding of the risks involved. Indeed, by this time, JPMorgan and Bank of America had brought in additional counsel of their own (Cadwalader, Wickersham & Taft and Kelley Drye & Warren, respectively) to advise on settlement issues and consult with Kasner.

But according to plaintiffs lawyers, Kasner told colleagues that there was no way syndicate members would pay as much as Citigroup. His logic: Citigroup had Grubman and all his baggage. Kasner's clients didn't.

BY THEN OF COURSE THE plaintiffs had their payday. With $2.5 billion already in hand, they could afford a more bullish position. They were in no rush to settle, especially not in Cote's courtroom, where everything was moving their way. Still, at the time, Coffey worried that a serious offer by JPMorgan could undermine the Citi formula. "The dilemma I feared was that JPMorgan would put real money on the table that was in spitting distance of the Citi formula," says Coffey. "How can you turn down $1 billion?" (If JPMorgan settled at the Citi formula, it would have paid around $1.37 billion.)

JUDGE COTE'S RULING WAS THE FIRST SERIOUS ANALYSIS OF THE DUE DILIGENCE DEFENSE IN 40 YEARS, SO IT GOT EVERYONE'S ATTENTION.

That fear never materialized. Much of 2004 was filled with depositions and discovery. Early in the year, the plaintiffs disclosed potentially damaging internal documents at Bank of America, Deutsche Bank AG, and JPMorgan that suggested there had been concern within the banks about WorldCom's credit risk. The plaintiffs were ready to argue that those facts should have been disclosed in underwriting documents or at a minimum spurred more thorough due diligence.

Uncertain if a settlement would ever emerge, both sides did what litigators do: They fought. On several occasions, Coffey wrote letters to Cote, complaining about Skadden's late responses to discovery and deposition matters. The disputes gave rise to the acronym TSBS—typical Skadden bullshit—at Bernstein Litowitz.

Skadden appeared to be spending plenty of resources on the case. In November, when partner Thomas Nolan sent an e-mail to the plaintiffs' legal team, he cc'd more than 50 Skadden attorneys. According to a defense lawyer, Kasner once quipped that Skadden was billing more than $10 million a month. Kasner declined to comment on the figure.

Kasner also seemed to be maintaining his trademark tenacity. In October he deposed Blaine Nye, expert damages witness for the plaintiffs. The questioning appeared to get personal at moments. After a brief break, Kasner asked Nye if he had discussed his testimony with anybody in the interim. After Nye responded that he talked briefly with Bernstein partner Steven Singer, Kasner followed up: "Did you say to him that you're not having as much fun today as you did yesterday?"

"No. In fact, we even said you're a prince," said Nye.

After some more back and forth, Kasner said: "Remember to say that to me when I'm cross-examining you at trial. I appreciate the compliment."

For all the jockeying, Berger kept trying to build a bridge to Kasner. "I said to him regularly, I understand he's in an extraordinary situation. I don't envy him," says Berger. In September he called Kasner and suggested they meet for breakfast. It was a rare one-on-one sit-down between the two lawyers. They discussed the case, their families, and mutual friends. Berger, a highly skilled amateur photographer, talked about an upcoming exhibit featuring his pieces. Afterward, he sent Kasner a book of his work. But the meeting led to nothing. "I never heard from him," says Berger. "One way or the other, which really pissed me off."

Kasner may have been more

focused on summary judgment motions that were soon due to be filed. According to a lawyer familiar with the matter, Judge Sweet tried to nudge Kasner toward settling, suggesting that a summary judgment decision by Cote might not be good for his clients.

But Kasner plowed ahead and filed the motion anyway. According to lawyers in the case, he viewed the submissions as among the finest he'd ever associated with. And they were good. Kasner's adversary Coffey says they're "some of the best work I'd ever seen." In them, the underwriters argued that they were not required to test the reliability of WorldCom's audited financial statements so long as they had "no reasonable ground to believe" that those financial statements were wrong.

The arguments didn't persuade Cote. In denying key parts of the underwriters' summary judgment, she established a tough due diligence standard for investment banks involved in public offerings. In her opinion, Cote wrote: "The underwriter defendants argue that the standard that should apply is whether they had 'clear and direct notice' of an 'accounting' problem. They argue that case law establishes that 'ordinary business events' do not constitute red flags. They are wrong. There is no basis in law to find a requirement that a red flag arises only when there is 'clear and direct' notice of an accounting issue."

"It's the first serious analysis of the due diligence defense in 40–50 years, so it's got everyone's attention," says Kirk Davenport, a prominent securities lawyer at Latham & Watkins, who represents some of Wall Street's biggest banks in bond offerings.

AFTER COTE'S SUMMARY JUDGMENT decision in December, the syndicate started to show cracks. In-house lawyers were evaluating the risks of moving forward, and some wanted out. Richard Posen of Willkie Farr & Gallagher was first to call Berger. Posen said he represented four junior syndicate underwriters: Lehman Brothers, Credit Suisse First Boston, Goldman Sachs, and UBS AG. He wanted to initiate a discussion about the case against his clients.

On January 6, 2005, several weeks after the call by Posen, Coffey received a voice message from David Onorato, an old acquaintance from Georgetown University Law Center. Onorato was coming to New York and wanted to have lunch. He had more on his agenda than hashing over memories of their law review days. Onorato was now an in-house lawyer at Bank of America.

The calls presented Coffey and Berger with a dilemma. Should they engage counsel for the breakaways or force them to bring the entire syndicate to the table? At the time, Berger was traveling through India on a photo shoot. He told Coffey to put off lunch with Onorato until they could work out a plan.

Ultimately, they decided to engage the banks interested in settlement. The question then was, at what price? Coffey and Berger debated what to demand. Berger, the dealmaker, was willing to dip below the Citi formula. Coffey was more zealous. He advocated keeping the Citigroup formula alive by making the remaining defendant banks match it. Coffey, the former Latham partner, understands how big defense firms work. He thought they would advise paying a high price, given that uncertainty is the enemy of Wall Street and that banks rarely take these kinds of cases to trial. He also had future cases in mind: If the other banks got a better deal than Citigroup, it could encourage future defendants to hold out until their deal got sweeter too.

Berger led the negotiations. Posen's clients wanted to beat the Citi formula. So did Bank of America, represented by Gregory Markel of Cadwalader. During one session in a conference room at Bernstein Litowitz, Markel brought in a piece of promotional literature he had picked up in the lobby. The Bernstein Litowitz publication listed the top ten securities class action settlements (several obtained by Bernstein Litowitz). Markel proposed a deal that would be less than the Citi formula but would still make the list of top ten settlements.

AFTER COTE'S SUMMARY JUDGMENT DECISION IN DECEMBER 2004, THE UNDERWRITING SYNDICATE STARTED TO SHOW CRACKS.

While the talks continued, Coffey

CALLS FROM INDIVIDUAL BANKS WILLING TO DISCUSS SETTLEMENT PRESENTED COFFEY AND BERGER WITH A DILEMMA. SHOULD THEY ENGAGE COUNSEL FOR THE BREAKAWAY DEFENDANTS OR FORCE THEM TO BRING THE ENTIRE UNDERWRITING SYNDICATE TO THE TABLE?

headed for Sun Valley, Idaho, where a family he hadn't seen much of was vacationing. He called Berger constantly for updates on the negotiations. For days, the two partners argued about what to accept. During one conversation, Berger told Coffey he thought he could get $420 million, which would be below the Citi formula. Coffey responded jokingly but with a serious message: "If you accept $420 million, I will not be coming back to the firm."

ON THURSDAY, FEBRUARY 24, Coffey was fly-fishing in the Big Wood River with a friend, an investment banker at Citigroup. Berger called with good news: Bank of America agreed to pay $460.5 million, right at the Citi formula. Now, Berger said, if only we can get JPMorgan to pay at the same rate. Coffey had other, bigger thoughts. Back in New York four days later, Coffey told Berger and his partners J. Erik Sandstedt and Steven Singer that he wanted more from JPMorgan. With only a few weeks before trial, he argued, the price of poker had gone up. Coffey was persuasive. Berger and others were on board.

With their strategy set, the plaintiffs team was ready to announce the Bank of America settlement. On Thursday morning, March 3, Coffey and his colleagues sent an e-mail to all the parties in the litigation outlining the deal. Soon after, the New York State Common Retirement Fund issued a press release. That afternoon, the lawyers from both sides went to present the deal to Judge Cote.

After the Bank of America deal was announced, settlement activity kicked into high gear. Fourteen banks were still heading to trial. Berger called Posen—who represented Lehman, Goldman, CSFB, and UBS. Berger told Posen things were moving fast and that he'd better consider taking the Citi deal for his clients. Later that evening, according to a lawyer familiar with the matter, JPMorgan general counsel William McDavid called Alan Lebowitz, general counsel for the pension fund, asking for a meeting between Hevesi and JPMorgan's president, James Dimon. Lebowitz said there would be no meeting until JPMorgan was willing to negotiate in a range acceptable to the plaintiffs.

The next day, Posen's clients settled for $100.3 million, right at the Citi formula. Coffey detected that Posen was frustrated that his clients were being asked to pay so much. Coffey told him that he would be happy with the deal. Coffey expected the remaining settlements to come in above the Citi formula. And, with the exception of two tiny underwriters, they did. As more settlements were announced over the next week, the premiums over the Citi formula grew progressively higher. On Wednesday, March 9, four banks settled for $428 million, one at 5 percent and three at 13 percent above the Citi formula. On Thursday, three more banks settled for $437 million, two at 13 percent and one at 17 percent over the Citi formula. By now, 14 underwriters had settled for a total of around $4 billion. Two small underwriters and JPMorgan were the only ones left standing.

Theirs was not an enviable position.

WITH ONLY A FEW WEEKS BEFORE TRIAL, COFFEY ARGUED, THE PRICE OF POKER HAD GONE UP.

Due to the joint and several liability provisions governing the case, JPMorgan and the other remaining defendants were subject to liability for at least the full amount of their share of bonds. As more defendants had settled, JPMorgan's percentage of potential exposure had increased. Its estimated maximum exposure at this point was $5 billion.

The bank brought in John Callagy of Kelley Drye to object to the settlement. It was a desperate attempt to scuttle the deals and force all the banks to go to trial. At a hearing before Judge Cote on March 10, Callagy argued that the settlement was unfair to JPMorgan partly because it would not be able to seek contributions from settling underwriters if it were found liable at trial.

Judge Cote was skeptical. "It seemed to me we were going from the coalition of the willing to the coalition of the coerced, at least that's your intent," she said at the hearing. Cote denied JPMorgan's objection in a March 14 order. In her opinion, she added a footnote suggesting that JPMorgan might be liable for more than just its share of bonds. By her reasoning, JPMorgan estimated the bank's exposure could rise as high as $13 billion. That rendered going to trial too risky.

On March 14, three days before jury selection in the trial was to begin, JPMorgan's board met to discuss the case. Management recommended settling the case, and the board agreed.

By this point, Kasner appeared to be receding into the background. According to a lawyer familiar with the matter, an intermediary had put JPMorgan co–general counsel Joan Guggenheimer in touch with Berger. A few days before the trial was to begin, the two met over breakfast at the midtown restaurant Brasserie, where they hit it off. They discussed their families and growing up in Queens. In Guggenheimer, Berger found someone he could talk to.

AS THE BANKS RUSHED TO SETTLE BEFORE TRIAL, THE SETTLEMENT FORMULAS GOT PROGRESSIVELY STEEPER, ULTIMATELY RESULTING IN THE UNDERWRITERS PAYING A PREMIUM OF OVER $800 MILLION OVER THE CITI FORMULA.

On March 16 Guggenheimer called Berger and told him he had "his two." That price was 46 percent above the Citi formula the bank could have accepted months earlier. Settlements were also reached with the two smaller underwriters still remaining.

That afternoon, one day before the trial had been set to begin, the parties filed into Judge Cote's courtroom for one last settlement announcement. Afterward, Guggenheimer approached Coffey and offered her congratulations and business card.

"Joan, we should have been smoking the peace pipe a long time ago," said Coffey.

Neither Guggenheimer or JPMorgan will comment on why the bank didn't start smoking that peace pipe earlier. Did they really plan on taking the case to trial? And if they lost, were they really prepared to defend that decision to shareholders? Some lawyers, including Coffey, claim that JPMorgan used Cote's footnote to hide behind a failed legal strategy that never included a realistic exit strategy. (JPMorgan spokesperson says the bank was "pleased with the extraordinary hard work and dedication of our outside counsel, Skadden, Arps," which it continues to use in individual WorldCom-related actions.) The bank's defenders point the finger at Bank of America for breaking up the syndicate and zapping it of any leverage with the plaintiffs. They may have a point, but a strategy based solely on loyalty to the group presents serious problems, as this case showed. Each bank was accountable to its own constituencies. And some decided moving fast was better. They were right. ■