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https://missouriindependent.com/2023/04/11/lawsuit-involving-missouri-state-employee-pension-losses-spurs-side-fight-over-budget/

There's a bitter fight underway in Jefferson City between the agency that manages the main retirement fund for state employees and an investment manager it accuses of dirty dealing.

The main arena is a Cole County courtroom, where the Missouri State Employees Retirement System accuses Ontario-based Catalyst Capital Group Inc. of mismanaging $175 million entrusted to its care.

A side arena is the General Assembly, where the agency known best as MOSERS must maintain confidence in its management of the state's pension fund, valued at $8.4 billion when the most recent fiscal year ended June 30.

Although it was filed in late 2020, lawyers are still arguing preliminary matters in the the lawsuit where MOSERS accuses Catalyst of "fraud, deception, willful misconduct, self-dealing and gross mismanagement" resulting in "hundreds of millions of dollars in losses to innocent investors, including MOSERS."

A trial is months, if not more than a year, away.

But the state budget for the coming year will be settled in four weeks and, from the money set aside for future benefits – $718 million for the coming year – lawmakers give MOSERS an allowance, set in the pending budget at $15.6 million, for administration.

Richard McIntosh, lobbyist for Catalyst and a one-time Senate budget analyst, said his review of MOSERS spending shows it has regularly exceeded that allowance by millions of dollars.
McIntosh was hired in November 2020, about a month after the lawsuit was filed.

"I was really on a mission of peace and the more the spending occurred the more questions it raised in our minds," McIntosh said. "It started to become rather apparent that there were extraordinary expenditures made on the legal side."

So far, McIntosh estimates, MOSERS has spent about $5.2 million on legal help in the lawsuit, most of it for nationally known Quinn Emmanuel law firm, which charges in excess of $1,000 an hour for attorney fees.

The legislative language each year sets an amount for "administration of the system, excluding investment expenses."

MOSERS contends the spending McIntosh targets is either one-time costs to update its computerized benefits system or to administer individual retirement accounts for state and higher education employees under its responsibilities separate from the general pension accounts.

The financial statements verify that costs are allocated properly, MOSERS spokeswoman Candy Smith said.

"We are aware of the narrative that Mr. McIntosh is pushing," Smith wrote in an email.

The lawsuit

Last Thursday, for more than 90 minutes, Cole County Circuit Judge Jon Beetem heard arguments on the latest legal wrangle in the lawsuit.

Attorney Dave Grable argued that Catalyst had such a close relationship with a firm named Callidus Capital Corporation that it should produce its internal documents. Catalyst's founder and majority owner, Newton Glassman, was also chairman and CEO of Callidus.

Catalyst purchased shares in Callidus at $14 per share in 2014, partially with funds invested by MOSERS. It also had outstanding loans worth $421 million to Callidus when it faced insolvency in 2019 it was sold for about 56 cents per share to a private investor.

"Defendants did not manage investments honestly, or with anything close to due care," Grable said in court.

MOSERS has not provided The Independent an accounting of returns on its investments in Catalyst and one has not been filed among the public court documents in the case. One aspect of the case is the heavy censoring of public filings and the large number of documents filed under seal.

MOSERS entrusted a total of $75 million with Catalyst via the two funds that held stock and made loans to Callidus. The combined market value of those funds in the latest MOSERS annual report is $16.9 million.

"There were terrific losses in association with these investments as alleged in the complaint and detailed elsewhere," Grable said. "It's MOSERS position that there was a lot of wrongdoing in connection with these Callidus investments."

If MOSERS' attorneys want to subpoena records from Callidus they are free to do so, attorney Alex Barrett, representing Catalyst, said Thursday.

"It is not appropriate for us to go and collect these documents for MOSERS," he said. A major part of the case is that the apparent early success helped persuade MOSERS to subscribe $100 million to a new fund in 2015. Early on in the lawsuit, MOSERS told Beetem it would refuse to fulfill its contractual obligations to provide cash to fulfill that commitment.

In an April 2021 ruling warning MOSERS that he would not provide a court order protecting that decision, Beetem reminded the pension agency that it faced major sanctions under the partnership agreement if it carried through with the threat.

"MOSERS asks the court to protect it from the consequences of its own decision," Beetem wrote.

In the decision, Beetem also cast doubt on many of MOSERS claims about the connections between Catalyst and Callidus.

MOSERS backed down, made the $10 investment and has provided Catalyst $70 million of the $100 million subscription. The fund was listed with a fair market value of $71.4 million on the 2022 annual report.

Over the past five years, Catalyst has received $13.6 million in fees for managing Missouri's investment.

On Thursday, Grable also argued that MOSERS should be allowed to pierce attorney-client privilege for Catalyst because it is a partner in the fund organized as a limited partnership. MOSERS wants to see the advice Catalyst received before investing in Callidus during the initial public offering.

"The Callidus (initial public offering) there, as we've alleged, a lot of different rotten things we say that happened in connection with that, that did violence to the rights of the various limited partners," Grable said.

Catalyst claims those documents are privileged, Grable said.

"When they sought that advice, they were seeking the advice in order to manage the investments of the limited partners," he said. "So they're not allowed to do that."

Chuck Hatfield, also representing Catalyst, said a ruling favoring MOSERS could cut both ways. The argument from Grable was based on Catalyst's duty as a fiduciary to show it was being a prudent investor, he said.

Hatfield spent many years working as chief of staff in the Attorney General's Office, and is entitled to a pension from MOSERS.

"It's kind of strange to me that MOSERS is making the argument that under Missouri, and I guess Ontario, law, beneficiaries of a fiduciary are entitled to all privileged communications, because I'm a beneficiary of MOSERS," Hatfield said.

If he asked for privileged information as a beneficiary, he said, he would be refused "and they should."

Budget fight

The examination of the system's spending grew out of frustration that MOSERS was blocking access to the bills for legal work in the lawsuit, McIntosh said.

McIntosh's associate, John Gaskin, filed a lawsuit when MOSERS claimed they were closed records and Gaskin's motives were suspect as a representative of Catalyst. Circuit Judge Cotton Walker agreed and the case was dropped last year in June.

McIntosh enlisted lawmakers to submit records requests to MOSERS. In each case, MOSERS responded with cost estimates ranging from $122.12 to $196.15. None of the costs have been paid, he said, but Sen. Denny Hoskins, R-Warrensburg, received a packet of records at no cost.

"They fought us tooth and nail on the Sunshine lawsuits," McIntosh said. "So we said, we'll give up on that. State agencies must tell the legislature how much they are spending."

The most significant increase in spending by MOSERS has been on legal services, $5 million over the past two years and budgeted at $3.25 million for the coming year. That kind of expense, McIntosh said, should require justification that the lawsuit will recover at least that amount.

"The legislature should start to ask some really, really, hard questions," McIntosh said. The legal costs are an allowable investment expense, covered by the budgetary exemption, Smith, MOSERS' spokeswoman, wrote. The system has always counted legal costs related to investments as exempt, she wrote in an email to The Independent.

"MOSERS' board actively oversees the system's business, including this litigation and the associated legal expenses," Smith wrote. "The board believes that the legal fees paid for prosecuting its claims against Catalyst in this complex litigation are incurred in the best interest of its members."

Hoskins, a member of the Senate Appropriations Committee, said he agreed to submit records requests because McIntosh convinced him MOSERS was blocking access. Former Rep. David Gregory, who lost the GOP primary for auditor last year, submitted requests that were not filled.
"I am just trying to find out exactly what is going on, if they are overspending their budget authority or not," Hoskins said.

The 11-member Board of Trustees that oversees the system includes four lawmakers, two from the House and two from the Senate, as well as State Treasurer Vivek Malek and Commissioner of Administration Ken Zellers. The governor can appoint two members and people with vested pensions elect the rest.

That is appropriate oversight to keep the budget within the legal limits, Smith wrote.

In fiscal 2022, with complete information available on actual spending by MOSERS from its audited financial statements and proposed 2024 budget, MOSERS actually spent $24.3 million.
The audited financial statement shows just under $7 million for investment-related expenses.

Another $2.8 million was spent administering investment accounts for state and higher education employees and $2.1 million for the new computer hardware and software for administering benefits.

For fiscal 2022, the cap was $12.3 million. If MOSERS' accounting is accepted, it underspent its administrative allowance by $1,822.

McIntosh contends the legal bills should count as administrative expenses, as should costs for buying capital assets. The cost of pursuing the suit should be weighed against the market returns on the same money invested, he said.

By his analysis, MOSERS is overspending its allowance by as much as $6 million.
"You can't play hide the ball and not tell them what you are spending," McIntosh said. "What is not OK is not telling the legislature what you are doing."

Hoskins said he has spoken to McIntosh about the analysis but hasn't drawn any conclusions. If the budget allowance should be increased to reflect what MOSERS actually spends, he said he is open to that.

“I would have to take a look at what that number is and what their reasoning is for why that number should be increased,” Hoskins said.

He did not like being asked to pay to access records, Hoskins added.

“I disagree with state agencies charging legislators to do our jobs,” Hoskins said. “We ultimately are in charge of protecting taxpayer funds and monitoring revenue and expenditures. I would expect they would make every effort to comply without charging for information.”

Charging lawmakers fees for accessing public records they request has become more common as those information requests are formalized as Sunshine Law inquiries. McIntosh, who was the principal staff member for Democratic House Majority Leader Gracia Backer in the mid-1990s, said there should be bipartisan revulsion at the practice.

“It is a complete constitutional abomination,” McIntosh said. “That is not how government works nor should it be how government works.”

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