Nest eggs for thousands cracked with heavy bet on one bad stock, lawsuit says

By Mark Davis

September 14, 2017 03:24 PM , Updated September 14, 2017 03:32 PM

Imprudent investing cracked the nest eggs of thousands of employees at Kansas City-based DST Systems Inc., according to a former employee's lawsuit.

DST Systems allowed a money manager it hired to put too much of its employees' retirement assets in one company's stock, the lawsuit said. And that stock — shares of Valeant Pharmaceuticals International Inc. — tanked.

Amid scandal and investigations, Valeant's stock fell from more than $260 a share to less than $15 a share in 15 months. The lawsuit said DST employees saw nearly $400 million disappear from their retirement accounts.

"They couldn't get out of it, and they couldn't control it," said Ted Kapke, an attorney representing the former DST employee who sued.

A DST Systems spokeswoman said the financial services company would not comment for this article. Officials with Ruane, Cunniff & Goldfarb Inc., the money manager, could not be reached.

The incident is a new twist on an old problem that has plagued many employees' 401(k) and similar retirement plans. They suffer stiff losses from a heavy investment in one stock, though that stock usually has been the employer's own shares.

For example, the 401(k) plan at the former Aquila Inc. in Kansas City was stuffed with Aquila shares when the bottom dropped out of the stock's price in 2002. Aquila's employees were locked into the Aquila investment and powerless to move that money into a safer mix of investments.

Similar situations led to big investment losses in employee retirement accounts at Enron. Such events led some Kansas City area companies to allow their employees to sell company shares that were held inside retirement plans.

The DST Systems Inc. 401(k) Profit Sharing Plan has held DST shares, but it was the Valeant investment that spawned an ongoing legal battle.

Early this year, the Valeant losses became the focus of a DST employee lawsuit brought by James DuCharme. He sued on behalf of the plan, what Kapke called a representative action, rather than to recover his personal losses.

Kapke, of Kapke & Willerth LLC in Lee's Summit, said DST was dismissed from the case because DuCharme previously accepted DST's request for an agreement to arbitrate any disputes. Kapke said arbitration doesn't work in representative actions and pension law allows only representative action in such disputes.

Enter Stephanie Ostrander, who filed a new lawsuit this month in U.S. District Court in Kansas City. Ostrander worked for DST Systems' printing and mailing operation, called DST Output. DST sold the business to Broadridge Financial Solutions Inc. in 2016.

Ostrander, Kapke said, had opted out of DST's arbitration agreement. First, she intervened in DuCharme's lawsuit, a point that DST noted in its latest quarterly report to shareholders.

"We intend to defend this case vigorously, and, because the suit is still in its preliminary stages, we are not able to predict whether any loss related to the suit is probable," it said in part. The report to shareholders mentioned a related lawsuit in U.S. District Court in the Southern District of New York and said DST had been dismissed from that case.

Ostrander then filed the new lawsuit in Missouri seeking class-action status to represent participants in the plan since the end of 2011. Like DuCharme, Ostrander seeks damages for the retirement plan rather than for herself individually.

According to the lawsuit, DST relied on Ruane, Cunniff & Goldfarb to manage the profit-sharing portion of DST's combined 401(k) and profit-sharing plan. Each portion was roughly equal in size.

Kapke said the original Valeant investment posed no outsized risk. But Valeant shares soared, hitting their peak in August 2015. At one point, the suit said, Valeant shares came to represent 30 percent of the profit-sharing portion of the plan, or 15 percent of all the retirement plan's assets.

DST and Ruane breached their fiduciary duties to the plan's participants, the lawsuit claimed.

"No prudent fiduciary under like circumstances would have or could have made the same decision to invest so heavily in a single stock," Ostrander's lawsuit said.

Nor did DST or Ruane reduce the exposure to Valeant by selling some shares and reinvesting the proceeds into a mix of holdings. Investment advisers routinely advise clients to rebalance their accounts toward an original investment mix when changing stock prices alter the intended mix.

"DST knew or should have known they needed to rebalance but weren't. They were effectively letting it ride," Kapke said.

The lawsuit further claimed that DST and Ruane each had a conflict of interest.

Ruane also managed and distributed the Sequoia Fund, a mutual fund that had a large investment in Valeant shares, the suit said. Kapke said it tainted Ruane’s judgment in making a large Valeant investment in the profit-sharing portion of the DST plan.

The lawsuit claimed DST had a conflict of interest because the Sequoia Fund was a customer of DST, which provides fund accounting and other services to mutual fund companies.

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