

## ‘Expert’ Tag at Axa Trial Depends on Which Side You’re Sitting

By Greg Saitz February 9, 2016

Phil Goldstein, a well-known activist investor in closed-end funds, testified as a plaintiffs’ expert at the **Axa Equitable** excessive fee trial last week, although defense attorneys and even the judge questioned whether he actually was one.

Goldstein, the straight-talking Brooklyn native who runs Bulldog Investors and who was called to opine on the diligence of the EQ Advisors Trust directors in approving fees, acknowledged that in preparing to testify he gave just a cursory look at materials given to the board during its 15(c) deliberations. Although he read parts of sworn statements given by three independent directors, he didn’t look at the advisory contracts with Axa’s Funds Management Group and merely glanced at the board’s meeting minutes.

“I would probably have to charge a million dollars to go through all the documents,” said Goldstein, whose expert report noted his fee was \$400 an hour.

“So you didn’t do it?” U.S. District Judge Peter Sheridan asked.

It would not have been productive, Goldstein said.

“Based on my experience being on many boards, board minutes do not really tell what happened at board meetings,” Goldstein said at the federal courthouse in Trenton, N.J. “It really gives you no flavor into what the thinking of the board was, who said what. You’re not going to find in the minutes which director was nodding out.”

Ultimately, despite expressing some reservations about Goldstein’s preparation methods, Sheridan allowed him to testify in the non-jury trial. It’s the first excessive fee case since 2009 to reach the trial stage.

“I was concerned he has never really looked at the board minutes and he’s never really been involved in a mutual fund with a subadvisory structure,” Sheridan said. “...But he does have this significant experience.”

Goldstein is an independent director on the boards of two closed-end funds and an interested director on a third. In all, he said he’s served on about 10 fund boards in the past two decades although none were open-end funds.

Goldstein was one of several experts plaintiffs' lawyers presented in their efforts to prove Axa violated Section 36(b) and should repay 12 funds inside the EQ Advisors Trust hundreds of millions of dollars in advisory and administrative fees. The 2011 lawsuit was one of the first to pursue a novel theory that the adviser violated the law because it collected a disproportionate amount of fees while subadvisers did most of the investment management and administrative work.

Defense attorneys dispute Axa's fees were excessive and contend the firm provided plenty of services from compliance to legal to accounting for its cut.

With both sides focusing on the Gartenberg factors, plaintiffs' attorneys brought in Goldstein to dissect the care and conscientiousness of directors in approving Axa's advisory and administrative contracts. He pointed to a statement former independent director Jettie Edwards gave in her deposition in which she disagreed that Axa had delegated day-to-day investment management duties to subadvisers.

"It's shocking...I just don't understand how you can be on the board of these funds and not know the day-to-day investment management is being performed by subadvisers," Goldstein testified. "It's inexplicable to me."

The takeaway, he said under further questioning from **Szaferman Lakind** partner Daniel Sweetser, was that directors can't negotiate or approve a contract – in essence, fulfill their fiduciary duties – unless they know what services are being provided. In later testimony, Goldstein criticized several directors for not being able to explain the cost allocation methods Axa used in determining adviser profitability and for not hiring consultants to help directors figure it out.

One of the main points in the plaintiffs' case is that Axa improperly allocated some \$50 million in costs to FMG, thus driving down the adviser's profit margin. Axa insists the expenses were valid.

Goldstein also testified that he compared the fees paid to FMG and subadvisers and concluded FMG was overpaid because the firm didn't provide investment advice to the funds. FMG was basically a middleman, he said.

"Based on the services provided, FMG's fees should be substantially lower than the subadvisers' because the subadviser is doing all the heavy lifting, the day-to-day work," Goldstein said.

Parts of the former civil engineer's testimony were interspersed with objections from defense attorneys, who have argued since last year that Goldstein's opinions shouldn't be admitted as evidence in the case. In fact, **Milbank** partner Robert Hora objected to the judge even qualifying Goldstein as an expert.

Hora attacked Goldstein's qualifications, questioning him on whether he'd ever published articles or taken or taught any courses on the '40 Act. Goldstein said he had not. And when Goldstein asserted he was familiar with subadvised mutual funds, Hora played a clip from Goldstein's videotaped deposition in the Axa case in which he said he was not familiar with such a structure.

The defense attorney used that tactic repeatedly, even playing snippets of a deposition Goldstein gave in another excessive fee case pending against **The Hartford**. Milbank represents the adviser in that case and Szaferman Lakind represents the plaintiffs.

After Goldstein was asked if he had an opinion about the breakpoints established for FMG and subadvisers during his direct testimony, Hora objected, noting Goldstein wasn't an expert in economies of scale. The judge, who at times seemed as exasperated as Hora with Goldstein's testimony, allowed him to answer certain questions but said of Goldstein, "So far he's picked out one statement out of a deposition, and he's making huge opinions out of this one statement."

Goldstein said it was inexplicable that the EQ board would allow a subadviser breakpoint to kick in at lower asset levels than breakpoints for FMG. "In my opinion, every breakpoint should have some benefit to the fund," he said.

During cross-examination, Goldstein acknowledged he'd never been involved in setting a breakpoint and none of the closed-end funds on which he served as director had them. He also said none of the boards he was on hired consultants to review cost allocation methods, although he faulted EQ Advisors directors for not doing so.

At another point in the cross-examination that lasted less than 30 minutes, Hora suggested Goldstein had not done an analysis of the value of services Axa provided to the EQ Advisors funds, but the witness said he had.

"I'd like to impeach him on that," Hora said before playing a clip of Goldstein's videotaped deposition in which he said he had not done such an analysis.

Hora also elicited testimony from Goldstein that he did not review email correspondence or read depositions from investment and compliance executives at Axa. The defense attorney concluded his questioning by asking whether an investor would care about the adviser/subadviser fee split if the overall fee was competitive.

"He might care," Goldstein testified.

That's when Hora played another section of Goldstein's deposition in the Hartford case. On the video, Goldstein said it made no difference.

"The investor is going to get the same services for the same price no matter how that fee is split," he said on the video.

Plaintiffs' attorneys were scheduled to finish presenting their case last week, and Axa attorneys are scheduled to begin their defense this week. Axa also has appealed an earlier magistrate's ruling that it could not introduce certain regulatory filings the funds made to the Securities and Exchange Commission because it didn't share the documents with plaintiffs in a timely manner.