

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

In the matter of the application of

U.S. BANK NATIONAL ASSOCIATION, THE BANK OF NEW YORK MELLON, THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A., WILMINGTON TRUST, NATIONAL ASSOCIATION, LAW DEBENTURE TRUST COMPANY OF NEW YORK, WELLS FARGO BANK, NATIONAL ASSOCIATION, HSBC BANK USA, N.A., and DEUTSCHE BANK NATIONAL TRUST COMPANY (as Trustees under various Pooling and Servicing Agreements and Indenture Trustees under various Indentures),

Petitioners,

for an order, pursuant to CPLR § 7701, seeking judicial instruction.

Index No. 652382/2014

Assigned to: Friedman, J.

**RESPONDENTS'
MEMORANDUM OF LAW
REGARDING THE SCOPE OF
DISCOVERY UNDER
ARTICLE 77¹**

¹ The Intervenors, Proposed Intervenors, and/or Respondents (collectively, “Respondents”) that join in this brief are: the Federal Home Loan Bank of Boston (“FHLB Boston”); the National Credit Union Administration Board as Liquidating Agent for U.S. Central Federal Credit Union, Western Corporate Federal Credit Union, Members United Corporate Federal Credit Union, Southwest Corporate Federal Credit Union and Constitution Corporate Federal Credit Union (“NCUA”); the QVT Fund V LP, QVT Fund IV LP and Quintessence Fund L.P. (the “QVT Funds”); Ambac Assurance Corporation and The Segregated Account of Ambac Assurance Corporation (“Ambac”); Brevan Howard Credit Catalysts Master Fund Limited and Brevan Howard Credit Value Master Fund (the “DW Funds”); and Triaxx Prime CDO 2006-1, Ltd., Triaxx Prime CDO 2006-2, Ltd., and Triaxx Prime CDO 2007-1, Ltd. (“Triaxx”).

In a hearing on October 29, 2014, the Court stated that it intended to “hear applications for discovery on the return date,” and requested brief submissions “about the scope of discovery and an indication of any disputes,” after the parties had met and conferred about their discovery demands. *See* Doc. No. 102 at 7, 10. Respondents served their initial discovery requests on the Trustees. *See* Exs. A-B.² After a meet and confer, the Trustees rejected the vast majority of Respondents’ requests. *See* Exs. D-E.³ The Trustees’ position is without legal basis, and would deprive the Court of the information necessary for it to fully and fairly evaluate the Trustees’ request for approval of a Settlement affecting thousands of parties and billions of dollars in liability. Respondents should be permitted to pursue the discovery they have propounded, which is consistent with the procedures of an Article 77 proceeding, and is narrowly tailored to provide information “material and necessary” to the declarations that the Trustees seek in their Petition.

A. Parties in Article 77 Proceedings Are Entitled to Full and Complete Discovery of All “Material and Necessary” Information

Unlike other special proceedings in New York, there are no specific limitations on discovery in an Article 77 proceeding. Article 77 is expressly “governed by [A]rticle 31.” CPLR § 408. Under Article 31, “there shall be full disclosure of all matter material and necessary in the prosecution or defense of an action, regardless of the burden of proof.” CPLR § 3101(a); *see also Diamond State Ins. Co. v. Utica First Ins. Co.*, 37 A.D.3d 160, 161 (1st Dep’t 2007) (“New York law requires full disclosure of all material and necessary matter to prosecute or defend an action”). “‘The words ‘material and necessary’ as used in section 3101 must ‘be interpreted liberally to require disclosure, upon request, of any facts bearing on the controversy which will assist preparation for trial by sharpening the issues and reducing delay and prolixity.’” *Kapon v. Koch*, 23 N.Y.3d 32, 38 (2014) (quoting *Allen v. Crowell-Collier Publ. Co.*, 21 N.Y.2d 403, 406 (1968)). Indeed, parties in an Article 77 proceeding “shall be entitled to full and complete discovery with regard to all previous actions taken by . . . Trustees, and shall be entitled to

² Respondents submitted a second set of discovery requests to the Trustees on November 26, 2014. *See* Exs. C-D.

³ Based on this position, the Trustees have offered to produce unredacted expert reports, the Governing Agreements, information provided to the Trustee decision-makers, information provided to their experts, and the identity of individuals with knowledge of information that is material to the Settlement. *See* Ex. H at 1-2.

inspect and/or copy any and all documents and/or things which evidence their administration of trust assets.” *Milea v. Hugunin*, 24 Misc. 3d 1211(A), at *12 (Sup. Ct. Onondaga Cty. 2009).

Justice Kapnick recognized the broad scope of discovery under Article 77 in the Countrywide Article 77 proceeding when she held that “even though it’s an Article 77, I think in order for me to determine whether or not this was fair and reasonable, I think [Petitioners are] going to have to do a lot more production, a lot more discovery.”⁴ Significantly, the Court made these remarks and compelled further discovery *after* the Bank of New York Mellon produced nearly 250,000 pages of documents and had contended that all documents necessary for the parties and the Court to consider the questions presented in their petition had been produced.

The appropriateness of providing Respondents the ordinary scope of discovery under Article 31 of the CPLR is underscored by the fact that the Trustees are seeking a declaration that their acceptance of the Settlement “comports with all applicable duties under the Governing Agreements and any other law” and would exempt them from liability for any breach of those duties in accepting the Settlement. Petition, ¶ 77. Were Respondents, as Trust beneficiaries, to have brought claims challenging the Trustees’ actions, they would be entitled to the full scope of discovery (as the Institutional Investors will soon be pursuing in their many actions against Trustees). It cannot be that the due process rights of Trust beneficiaries to discovery concerning their Trustee’s observance of its duties can be limited or extinguished merely because the Trustee beat its beneficiaries to the courthouse door.

B. Discovery Is “Material and Necessary” To this Case If It Relates to the Relief that the Trustees Seek or the Scope of their Fiduciary Duties

The scope of relevant discovery is determined by the declaration the Trustees seek, including that each Trustee (1) accepted the Settlement “based on a thorough and reasonable investigation of the claims proposed to be released and of the Settlement consideration,” (2) “made its settlement decision in good faith,” (3) “believed that its decision was in the best interests of the beneficiaries of each Accepting Trust,” and (4) complied “with all applicable duties under the Governing Agreements and any other applicable law” in accepting the

⁴ See June 14, 2012 Hr’g Tr. at 59:17-20, *In re the Bank of New York Mellon*, attached hereto as Ex. G.

Settlement. Petition, ¶¶ 74-77. To the extent that the Trustees' conduct is subject to an abuse of discretion standard, discovery is "material and necessary" if it tends to show the Trustees may have acted in bad faith, or, in exercising a power, acted unreasonably, imprudently, or beyond the bounds of reasonable judgment. *See In re Bank of New York Mellon*, 42 Misc. 3d 1237(A), at *15 (Sup. Ct. N.Y. Cty. 2014) (trustee's power to settle "must be exercised with 'reasonable prudence'").⁵

Discovery is also "material and necessary" if it is relevant to establishing the standard of duty governing the Trustees' conduct. In fact, the Court cannot determine the appropriate standard of review *without discovery*. For example, if the Trustees suffer from a conflict of interest, the Court must review the Trustees' conduct not under an abuse of discretion standard, but "with strict scrutiny and with special care . . . to make the determination whether or not the fiduciary duty owed by the trustee has been tainted, affected, controlled, initiated, or consumed by his or he own self-dealing." *Milea*, 24 Misc. 3d 1211(A), at *8. Without discovery, the Court cannot evaluate whether any conflicts exist.⁶

The Trustees themselves have put the standard of duty at issue by relying on report of Daniel Fischel. Fischel (in marked contrast to the experts in the Countrywide Article 77 proceeding) calculates that 98% of the Trusts with timely claims could recover more in a repurchase action than the amount offered by the Settlement, and his only justification for nonetheless recommending that the Trustees accept the Settlement on behalf of these Trusts is that the Trustees have no duty to act, and hence will not bring suit on these claims on behalf of Trust beneficiaries.⁷ But the Trustees concede that if an Event of Default occurs, the Trustees cannot refuse to act, and are required to exercise their discretionary duties (as they may be

⁵ To the extent that the Trustees claim that an adjudication may be subject to an abuse of discretion standard limits the scope of discovery, they incorrectly "conflate[] the standard of review with the standard for discovery." *Mergel v. Prudential Life Ins. Co. of Am.*, No. 09-00039, 2009 WL 2849084, at *1 (S.D.N.Y. Sept. 1, 2009) (rejecting ERISA trustee's argument that because its benefit determination was subject to an abuse of discretion standard, the beneficiary could not obtain discovery into the trustee's alleged conflict of interest).

⁶ If the Trustees are conflicted, the burden of proving the entire fairness of that decision or transaction shifts to the fiduciary. *See Benedict v. Amaducci*, 1993 WL 87937, at *7 (S.D.N.Y. Mar. 22, 1993) (collecting cases).

⁷ The Institutional Investors cannot credibly deny the relevance of Events of Default and conflicts of interest, when they themselves have brought multiple lawsuits against the very same banks that served as Trustees for the JPMorgan Trusts, alleging conflicts of interest and Events of Default on essentially identical Trusts.

required to do in other circumstances). *Id.*, n. 4. Thus, discovery relating to whether an Event of Default occurred is material and necessary, and in fact, critical to determining the Trustees' obligations and standard of conduct.

C. Respondents' Discovery Requests Are Material and Necessary

All of Respondents' discovery requests follow directly from the relief that the Trustees are seeking in this proceeding. Respondents' discovery requests relate to the following issues:

1. The thoroughness and reasonableness of the process undertaken by each Trustee's decision-makers when accepting the Settlement, including what information was or was not presented to the decision-makers;
2. The fairness and reasonableness of the Settlement, including the value of the claims released by the Settlement, that was in the possession of each Trustee when it was considering whether to accept the Settlement;
3. Conflicts of interest faced by each Trustee and each Trustee's reasonableness and good faith in addressing such conflicts;
4. The existence of Events of Default;
5. Each Trustee's knowledge of and involvement in attempts by Certificateholders to form groups to direct any Trustee or attempts to prevent the formation of such groups;
6. Each Trustee's reasonableness and good faith in taking into account the Certificateholders' support or opposition to the Settlement;
7. Each Trustee's reasonableness and good faith in determining that it had no obligation to (i) litigate, (ii) poll Certificateholders, or (iii) avoid impeding formation of groups to direct any Trustee by imposing unreasonable indemnification requests; and
8. Each Trustee's reasonableness and good faith in assessing the timeliness of the released claims.

Each of these discovery requests goes to whether the Trustees conducted a "thorough and reasonable investigation" of the released claims, whether they acted in "good faith" and in the "best interests" of all Certificateholders, and whether the Trustees complied with their fiduciary duties in accepting the Settlement. They should be disclosed without further delay.

D. The Trustees' Objections to This Discovery Are Without Merit

The Trustees advance two fundamentally flawed arguments against Respondents' discovery in their correspondence and in the meet and confer. First, the Trustees suggest that Respondents are attempting to ignore the Trustees' decision-making process and "re-litigate" the underlying issues or "second guess" the Trustees' discretionary decisions. *See generally* Ex. B. This is false. The Respondents' requests are focused on the relief sought by the Trustees in their

petition and whether the Trustees satisfied their duties. As such, the requests are narrowly-tailored to determine whether the Trustees acted reasonably and in good faith, including with regard to their decision-making process, whether the Trustees were subject to conflicts of interest, and whether Events of Default occurred. There is no authority for the proposition that beneficiaries are not entitled to obtain the discovery necessary to determine if, in fact, the Trustees are entitled to the relief they seek in their petition. Indeed, the law is to the contrary. *See, e.g., Kern v. City of Rochester*, 261 A.D.2d 904, 905 (4th Dep't 1999) ("The issues framed by the pleadings determine the scope of discovery in a particular action.") (citations omitted).

Second, the Trustees advance the remarkable view that the only materials relevant to the Court's evaluation of the Trustees' conduct are the "documents considered by each Trustee's committee or other relevant decision maker(s) when determining whether to accept the Settlement." Ex. H at 1. Yet, the Trustees ask for a declaration that they acted properly, not that some committee or decision-maker did. Therefore, whether the Trustees considered all information known to them is relevant to their process for approving the Settlement. It would be an unreasonable exercise of discretion for the Trustees to spoon-feed a "decision-maker" with documents favorable to the Settlement, while withholding information that would lead to a different conclusion. Likewise, it would be unreasonable for the Trustees to limit their investigation in a manner that skewed their understanding of JPMorgan's liability to the Trusts, resulting in the failure to fully inform the decision-makers.⁸ Such issues are material and necessary to evaluating the relief sought by the Trustees, including the declaration that they acted reasonably and in the best interest of Certificateholders, and satisfied "all applicable duties" to the Trusts.

⁸ *See, e.g., In re Korn*, 959 N.Y.S.2d 89, 36 Misc.3d 1224(A), at *6 (Sup. Ct. N.Y. Cty. June 7, 2012) ("In determining whether such a breach of fiduciary duty has occurred, the court must evaluate the fiduciary's actions along with relevant factors that affected or ought to have affected the fiduciary's decisions...."); *see also* Restatement (Third) of Trusts § 50, Comment b ("[T]he court will interpose if the trustee, arbitrarily or without knowledge of or inquiry into relevant circumstances, fails to exercise the discretion.").

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CERTIFICATE OF SERVICE

I, Derek W. Loeser, hereby certify that on December 9, 2014, a true copy of the above document was served on the Parties, through their counsel of record, via ECF.

/s/ Derek W. Loeser _____

Derek W. Loeser