COMMONWEALTH OF KENTUCKY
COUNTY OF FRANKLIN CIRCUIT COURT
DIVISION I
CASE NO. 17-CI-1348

JEFFREY C. MAYBERRY, *et al.* PLAINTIFFS

MEMORANDUM IN SUPPORT OF THE TIER 3 PLAINTIFFS' MOTION TO INTERVENE

KKR & CO., L.P., *et al.* DEFENDANTS

ELECTRONICALLY FILED

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Tia Taylor, Ashley Hall-Nagy and Bobby Estes (the "Tier 3 Plaintiffs") respectfully submit this memorandum in support of their Motion to Intervene.

I. INTRODUCTION

The world has been turned upside down in this case. In December 2017/January 2018, the original Mayberry Plaintiffs — after months of research and investigation — filed an expertly drafted, 150-page, highly detailed derivative suit for KRS, *i.e.*, the First Amended Complaint ("FAC").[1] Based on then-existing Kentucky and federal law, those plaintiffs had constitutional standing and this Court so held. This Court also upheld the original Mayberry Plaintiffs' prudential standing to sue under KRS § 61.645(15) and common and trust law. Indeed, this Court upheld ***every substantive claim pleaded***, ***including aiding and abetting***, ***conspiracy***, ***common enterprise and direct fiduciary-duty claims against KRS's Advisors and the Hedge Fund Sellers***, ***as well as claims for punitive damages***. Initial discovery served with the FAC (albeit limited in scope, and the only discovery served in this case) produced explosive evidence of wrongdoing — even worse than initially alleged, and was later provided to the Court in the "Companion Memo" and in other filings. The Office of the Attorney General ("OAG"), having refused the *Mayberry* Plaintiffs' request to assert the taxpayers' claims, did nothing to preserve or advance the Commonwealth's claims for three years. However, because "***highly competent***

[1] The *Mayberry* Plaintiffs include five of the original plaintiffs in the *Mayberry* Action: Jeffrey C. Mayberry, Hon. Brandy O. Brown, Martha M. Miller, Steve Roberts, and Teresa M. Stewart.

counsel [were] ***aggressively litigating*** these claims,"[2] the taxpayer claims ***were preserved*** so that the new Attorney General could appropriate them when he intervened on behalf of the Commonwealth.[3] *See* Dec. 28, 2020 Order at 14.[4]

The Supreme Court dismissed the FAC — in the words of this Court — on a "***legal technicality***," and apparently without an opportunity to amend, despite the intervening change in the law concerning Constitutional Standing. *Id*. at 17. The Supreme Court nevertheless acknowledged the FAC alleged "***significant misconduct***." *Overstreet v. Mayberry*, 603 S.W.3d 244, 266 (Ky. 2020). This Court subsequently characterized the FAC as alleging "***extremely serious*** violations of fiduciary and other common law duties on the part of certain KRS Board members and advisors and the defendant hedge fund managers," "***severe misconduct and breaches of fiduciary duties***" involving "***self-dealing***, ***exorbitant fees***, ***conflicts of interest***" causing ***"staggering losses of public funds***." Dec. 28, 2020 Order at 15–17. Because "any party that breached its fiduciary duties and engaged in reckless conduct, conflicts of interest, or self-dealing should be accountable under the law," this Court concluded that "principles of equity and public interest require that ***the factual allegations in***

[2] Unless otherwise noted, all emphases are added.

[3] Because of the experience of the Mayberry Plaintiffs' counsel and performance in this case to date, the Tier 3 Plaintiffs retained them to assure the ***continued*** vigorous representation of KRS's claims in the derivative or representative format. The previously involved local Kentucky counsel have abandoned the prosecution of KRS's claims. They have done nothing to advance the KRS claims since the Supreme Court reversed this Court's standing ruling.

[4] *Mayberry v. KKR & Co., L.P.*, No. 17-CI-1348, slip op. (Ky. Cir. Ct. Franklin Cnty. Dec. 28, 2020) (Shepherd, J.).

this case *...* ***should be adjudicated on the merits***." *See id.* at 16–17; *see also generally* Nov. 30, 2018 Opinion & Order.[5]

Three years have been consumed. Yet these valuable claims, long ago upheld by this Court, are still at the pleadings stage, and all discovery (save that served with the complaint) stayed. Millions of dollars in defense fees have eroded insurance coverages. All to move the needle not at all on the merits, except now to start over.[6] If Defendants are permitted to continue to block these claims for KRS by exploiting technicalities, there will never be a full exploration, let alone adjudication, of these claims on the merits. Rather than honoring the Kentucky maxim that "there is no wrong without a remedy[,]" the KRS derivative lawsuit will assume *Dickensian* dimensions and become a modern-day *Jarnydce v. Jarndyce*[7] — in which Charles Dickens attacked the court system with its endless pettifogging, warning citizens "***suffer any wrongdoing that can be done you rather than come here***." It must not be that the 300,000-plus KRS members — first responders, healthcare providers, social workers and court clerks, all innocent victims of the KRS fiasco — come to hold such a jaded view of this Commonwealth's justice system.

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[5] *Mayberry v. KKR & Co., L.P.*, No. 17-CI-1348, slip op. (Ky. Cir. Ct. Franklin Cnty. Nov. 30, 2018) (Shepherd, J.).

[6] It is a source of some frustration for plaintiffs' complaint to be dismissed without leave to amend for failure to plead something not required when the complaint was filed; regardless, at least the substantive claims pleaded have been sustained and that ground should not need to be replowed.

[7] All the defense lawyers have accomplished since 2017 is to stall meritorious claims, preventing the case from progressing past the motion to dismiss stage, consuming huge legal fees, ***exhausting the KRS directors' and officers' insurance*** coverage (reminiscent of the lawyers in Charles Dickens's *Jarndyce* case, who consumed the entire estate, with their endless pettifogging).

Under applicable accounting rules (FASB5) a lawsuit seeking damages is a ***corporate/trust asset***.[8] KRS is a trust operating in corporate form. Its assets are trust assets — which under law must be used ***exclusively*** for KRS and KRS's beneficiaries. KRS § 61.515. These KRS derivative claims are a "contingent trust asset," that can be realized upon only if those claims are ***provided adequate representation to not only protect — but vigorously advance — the interests of the Tier 3 Plaintiffs, KRS's members and KRS's pension funds***. For that to happen, the Tier 3 Plaintiffs should be permitted to intervene, grab the baton from the initiating plaintiffs and press on.

The Tier 3 Plaintiffs want to intervene to carry forward the prosecution of the previously sustained derivative claims on behalf of KRS to obtain a substantial financial recovery for its pension plans and insurance trusts. Such a recovery will not only remedy the wrong done to KRS by its Trustees, Advisors, and Hedge Fund Sellers, while ameliorating the harm the Tier 3 Plaintiffs' individual retirement accounts have already suffered, but will also help repair KRS's financial condition. If the recovery is large enough, it may restore the KRS funds' sustainability, and greatly reduce and/or even eliminate the threat of the Commonwealth having to honor its inviolable contract obligations. That is the purpose and goal of this lawsuit for KRS; it has always been.

The OAG is now asserting the Commonwealth's claims. Those claims face a discomforting reality — the Commonwealth's historic underfunding of KRS

[8] Daniel Liberto, *Contingent Asset*, INVESTOPEDIA.COM (Dec. 10, 2020), *available at* https://www.investopedia.com/terms/c/contingentasset.asp (last visited Jan. 30, 2021) (citing FASB 5: "A company involved in a lawsuit with the expectation to receive compensation has a contingent asset.").

harmed its finances and influenced its Trustees to take the improvident investment risks central to this case to try to make up for the accumulating financial impact of those funding shortfalls. The OAG's substantive legal claims are largely untested, but they are the same claims the Supreme Court said "***we have never allowed***" under Kentucky law. *Overstreet*, 603 S.W.3d at 263. Because the OAG is now asserting the Commonwealth's claims directly (not derivatively, as did the original Mayberry Plaintiffs) the OAG also faces defenses unique to the Commonwealth's claims — lack of causation and *in pari delicto*. *See Sandoz, Inc. v. Commonwealth*, 405 S.W.3d 506 (Ky. Ct. App. 2012).

The Commonwealth's damages claims are also subject to attack as not "ripe" or "justiciable," since it has not yet paid anything out on its inviolable contract guarantees, and whether it ever will is unknown and contingent upon unknown events. Its claim for future damages directly conflicts with KRS's claims for billions of dollars in "hard," already-suffered damages. *See Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 625–26 (1997).

Finally, any recovery the OAG does obtain in pursuing the Commonwealth's claims must be placed in the State's general fund pursuant to KRS § 48.005(3) to be spent by the Legislature as it sees fit — the same politicians who dealt with KRS's funding issues in the past. Under these circumstances, the OAG's pursuit of the Commonwealth's claims cannot provide adequate representation of the interests of the Tier 3 Plaintiffs, KRS's members or KRS's trust funds, whose interests really are at stake here. Intervention of the Tier 3 Plaintiffs must be permitted to assure separate, adequate representation of these interests.

Accordingly, the Court should permit the Tier 3 Plaintiffs to intervene.

II. OVERVIEW OF ARGUMENT

This Court previously denied the Tier 3 Plaintiffs leave to amend the *Mayberry* FAC without prejudice. Dec. 28, 2020 Order at 18, ¶ 3. They promptly complied with this dispensation, filing a motion for leave to file a Third Amended Complaint ("TAC"). They also filed a separate protective suit, *Taylor v. KKR & Co., L.P.*, No. 21-CI-00020 (Ky. Cir. Ct. Franklin Cnty.), now assigned to this Court. This Court ordered the motion for leave to amend held in abeyance, and directed the Tier 3 Plaintiffs to file a Motion to Intervene. *See* Jan. 12, 2021 Order at 2. The Tier 3 Plaintiffs have so moved and submitted the Complaint in Intervention ("Complaint"), which mirrors claims asserted in the FAC that the *Mayberry* Plaintiffs filed and this Court later sustained across the board.

The Tier 3 Plaintiffs meet all requirements for intervention. Their statutory cause of action under KRS § 61.645 and ability to sue under common and trust law give them a ***right*** to intervene under CR 24.01. So does their claim of an interest in the "***property and transaction***" under litigation (*i.e.*, KRS's pension funds and assets and their own individual KRS retirement accounts), in which Kentucky courts have recognized they have a "property interest," giving them a right to intervene under CR 24.01. Permissive intervention is also proper. Even if their "right" to sue as stated above is conditional, it is clearly permitted because they are asserting claims that not only have a "***question of law or fact in common***" with the original action, but mirror those claims already sustained. CR 24.02.

To the extent the Court exercises its discretion to consider the ***prejudice*** and ***adequacy-of-representation*** factors, they strongly favor intervention. Intervention by KRS plan members with constitutional standing to pursue "***plan-***

wide misconduct" and obtain "***plan-wide relief***" is necessary to salvage the well-pleaded claims already upheld that otherwise will fail due to a "***legal technicality***." Intervention will not prejudice the existing parties; holding Defendants legally responsible for their egregious misconduct in looting the KRS funds is not prejudice, but rather justice, however much delayed.

Intervention by the Tier 3 Plaintiffs ***will benefit KRS***. Otherwise its valuable and substantively sustained derivative claims will be adversely impacted by the imputation of the Trustee's knowledge, acts and misconduct to KRS, which would likely bar the claims if KRS asserted them directly. Intervention will also benefit the Commonwealth and its taxpayers. Assuring the largest possible KRS recovery will lessen the likelihood of the state ever having to pay out on its inviolable contract obligations, reducing or eliminating its future damages. If the competing and conflicting claims can be successfully prosecuted alongside each other, the OAG will benefit from the expertise and experience of the Tier 3 Plaintiffs' counsel, who crafted the claims in the first place and prosecuted them for years to preserve them, and who know more about the facts underlying the KRS fiasco and the history of this case than any other counsel.

The OAG's assertion of the claims on behalf of the Commonwealth is not the assertion of separate claims on behalf of KRS. KRS and the Commonwealth are separate entities. *Commonwealth v. Ky. Ret. Sys.*, 396 S.W.3d 833, 840 (2013). The OAG's claims on behalf of the Commonwealth will face defenses separate from those faced by the KRS derivative claims — both factual and legal. The Commonwealth's past underfunding of the KRS Plans (despite pleas that it comply with its legal obligations, and warnings that its failure to do so would be damaging

to KRS's financial condition) are ***factual*** realities with potentially serious negative ***legal*** consequences for the Commonwealth's legal claims.

The OAG is also required to place any recovery from litigation on the Commonwealth's behalf into the State Treasury general surplus fund (KRS § 48.005(3)). By contrast, ***KRS's damages claims are trust assets that belong solely to KRS and its beneficiaries and, by law, must be used solely for their benefit***. *See* KRS § 61.515(2). The OAG cannot adequately represent the Tier 3 Plaintiffs' and KRS's interests, while at the same time prosecuting the Commonwealth's claims. Because ***separate representation*** is required to assure ***adequate representation*** of those overlapping and conflicting claims, intervention by the Tier 3 Plaintiffs must be permitted.

III. ARGUMENT

A. The Tier 3 Plaintiffs Have Constitutional Standing

Whether viewed as a prerequisite to intervention or an issue to be determined by motion practice, the constitutional standing of the Tier 3 Plaintiffs will have to be determined by the Court, according to both federal and Kentucky Supreme Court precedent. The constitutional standing of the Tier 3 Plaintiffs is beyond fair dispute — indeed, they presented the compelling and controlling authorities on this point, when seeking leave to file the TAC. But we cannot rely upon defense counsel, obsessed as they have been with technicalities, to concede even such an indisputable issue. The Tier 3 Plaintiffs' request to the Defendants to stipulate to their constitutional standing has fallen on deaf ears. We therefore address this issue up front — putting this "legal technicality" to rest once and for all.

1. The Tier 3 Plaintiffs Present Detailed Allegations of Standing

The Complaint alleges facts establishing the constitutional standing of the Tier 3 Plaintiffs to sue on behalf of KRS derivatively. Because of the nature of the Tier 3 Plaintiffs' benefits, and the structure of their accounts within KRS, they have standing under the rationale of *Overstreet, Thole* and a long line of federal ERISA decisions — pre- and post-*Thole*.[9] These authorities hold that ***participants in a contributory pension plan like the Tier 3 Plaintiffs have standing to sue to remedy plan-wide misconduct and recover damages suffered by the Plan*** on behalf of the plan in which they are enrolled. The Tier 3 Plaintiffs are in a Hybrid Cash Balance Plan with individual retirement accounts invested by the KRS Trustees as part of a common investment pool, and their pension entitlement is variable depending upon investment returns, expenses, and the quality of Trustee stewardship. Given these allegations of plan-wide misconduct and losses that have adversely impacted the Tier 3 Plaintiffs, their ***pension benefits have been and will be diminished*** as a result of Defendants' misconduct. Their unguaranteed insurance benefits are at risk of reduction or elimination by the legislature (as they are not, as with the original plaintiffs, part of any "inviolable contract"). Because the KRS funds remain on the brink of failure, ***all benefits*** due to the Tier 3 Plaintiffs — some already "vested" — are at greatly increased risk of loss, as they are simply not guaranteed.

[9] *Overstreet*, 603 S.W.3d at 255–59 (relying on *Thole v. U.S. Bank N.A.*, 140 S. Ct. 1615 (2020), a case arising under the Employee Retirement Income Security Act of 1974 ("ERISA")).

When the Kentucky Supreme Court overruled this Court and ordered dismissal of the *Mayberry* FAC filed by Tier 1/Tier 2 KRS members for lack of constitutional standing, it exempted Tier 3 members — ***none of whom had yet sued*** — from its ruling.[10] Nothing the Supreme Court said addressed the constitutional standing of the Tier 3 members of the KRS Hybrid Cash Balance Plan. The Tier 3 Plaintiffs clearly have standing to sue — which supports their entitlement to intervene under CR 24.01–24.02.

Thole, upon which *Overstreet* relied, involved an ***overfunded*** ERISA ***defined-benefit plan***, with a ***solvent*** plan sponsor, where all benefits were ***guaranteed*** by a federal government agency, and where plaintiffs' benefits ***had not, and would not, be impacted by fiduciary misdeeds causing plan losses, incurring excessive expenses or wasting plan assets past, present or future***. By contrast, the named plaintiff Tier 3 KRS members are in a hybrid cash balance defined-contribution plan where:

- Their pension benefit — even "vested" benefits — are guaranteed by no one.[11]

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[10] *Overstreet*, 603 S.W.3d at 253 n.21, 263: "[T]his case concerns only the ability of beneficiaries of KRS ***defined benefit plans to sue*** for alleged shortfalls in the KRS plan assets because of alleged administrative misconduct." "Plaintiffs' counsel conceded at oral argument that none of the Plaintiffs are members of the KRS 'Hybrid Cash Balance Plan,' which has characteristics of both a defined-benefit plan and a defined-contribution plan. That plan became available to members who began participation with KRS on or after January 1, 2014."

[11] None of the Tier 3 Members' benefits are protected or guaranteed by the State. KRS § 61.692:

> (2)(a) For members who begin participating in the Kentucky Employees Retirement System ***on or after January 1, 2014, the General Assembly reserves the right to amend, suspend, or***

- Their pension benefits are determined by the final financial balance in their individual retirement accounts within the overall common KRS investment pool.

- Their final account balance and pension benefit has already been, and continues to be, impacted up or down by investment returns, expense levels and the quality of KRS's stewardship, which have been lousy, excessive and terrible, respectively for years.

- The Tier 3 Plaintiffs have already suffered economic harm due to excessive hedge fund fees and terrible hedge fund returns as a result of the alleged course of misconduct of the KRS Trustees and Defendants that all but destroyed the finances of the KRS pension plans and insurance trusts.

- Causation is clear. The Tier 3 Plaintiffs have suffered individual harm due to "plan-wide misconduct" which can only be redressed by the financial recovery they seek ***for KRS and its plans***, while praying for the Court to direct a portion of that recovery to be allocated to Tier 3 Members' individual accounts, if KRS fails to behave properly, to assure redressability.[12]

To fully appreciate the devastating impact these ERISA decisions have on Defendants' meritless claims that the Tier 3 Plaintiffs lack constitutional standing, we synthesize below the standing allegations in the Complaint — ***which must be accepted as true*** at this stage — and then discuss in detail the ERISA authorities to show how they support standing for these Tier 3 members to sue on behalf of

> ***reduce the benefits and rights provided under KRS 61.510 to 61.705 if, in its judgment, the welfare of the Commonwealth so demands, except that the amount of benefits the member has accrued at the time of amendment, suspension, or reduction shall not be affected.***

[12] Because KRS assets are held in a "single investment pool," not segregated accounts, ***as a practical matter the Tier 3 Plaintiffs can only be made whole through (1) a recovery for KRS as a whole, with (2) retroactive credits to their individual accounts based on such recovery, as the ERISA authorities cited later provide.***

their plan.[13] The Complaint alleges the Tier 3 Plaintiffs' standing in paragraphs 10–15, 18, 77–79, 82–85, and 86–95:

> Tier 3 members are not in a defined benefit plan with a fixed and guaranteed future pension benefit. The Tier 3 Plan is a Hybrid Cash Balance Plan where the member's actual pension benefit depends on the value of the member's individual account when he/she retires. Tier 3 members have individual retirement accounts within KRS funds and their individual retirement benefit is based on the value of their individual account at the time they retire, the value of which depends on the investment performance of KRS over the years the Tier 3 member works for the Commonwealth. The individual accounts, however, exist as accounting entries, the actual assets are part of the comingled whole of the KRS plans. Thus, if a plan (such as the KERS-NH pension plan) were to be depleted, the assets backing the Tier 3 individual accounts would be gone. Compl. ¶¶ 93, 94.
>
> The Tier 3 Plaintiffs have contributed to and continue to contribute thousands of dollars of their personal funds to help fund KRS's ongoing operations and the KRS pension and insurance trusts that pay and promise to pay them benefits. They are required to contribute between 5–9% of their pay annually. These employee contributions are comingled with KRS's other monies. Compl. ¶ 94.
>
> The contributions of the Tier 3 members into KRS are placed in a common pool — comingled with the contributions of other plan participants which funds are invested and overseen by the Trustees and the advisors. Compl. ¶¶ 11–12, 83, 87, 89–94.
>
> The Tier 3 Plan Hybrid Cash Balance Plan has characteristics of both a defined benefit plan and a defined contribution plan. It resembles a defined contribution plan because it determines the value of benefits for each participant based on individual accounts. However, the assets of the plan remain in the single, comingled investment pool like a traditional defined benefit plan. Their final individual account balance, and thus their pension, depends on the stewardship of KRS's Trustees and KRS's investment returns over the years. Tier

[13] "The Supreme Court has made clear that when considering whether a plaintiff has Article III standing, a federal court must assume *arguendo* the merits of his or her legal claim." *Parker v. Dist. of Columbia*, 478 F.3d 370, 377 (D.C. Cir. 2007). And "[a]t the pleading stage, general factual allegations of injury resulting from the defendant's conduct may suffice, for on a motion to dismiss we 'presum[e] that general allegations embrace those specific facts that are necessary to support the claim.'" *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 561 (1992).

3 members receive a minimum 4% annual return, plus an annual "upside" of 75% of KRS's investment returns over 4% computed on a 5 year basis and credited to their accounts. The "upside" credits of Tier 3 Plan participants have been diminished each year since 2015 as a result of the poor performance and excessive fees attributable to the hedge funds, *i.e.*, the alleged wrongdoing. Compl. ¶¶ 14–15, 93–94.

The damage the T/Os and Defendants' alleged misconduct caused KRS impaired its investment portfolios, causing KRS in 2016 to adopt a much more conservative, cautious "preservationist" investment strategy. This strategy caused diminished returns and curtailed the "upside" to the Tier 3 Plan participants compared to what they would get from a well-managed, well-funded liquid fund. The lost "upside" measures in the many millions of dollars to Tier 3 plan participants and significant individual financial injury to the Tier 3 named Plaintiffs. Compl. ¶¶ 14, 71.

The alleged wrongdoing, *i.e.*, the course of conduct was still raging on inside KRS well into 2016 and the adverse economic impact of that misconduct, *i.e.*, the bad hedge fund investments and their excessive fees continued well into 2018–20. For instance, in fiscal 2016 the BAAM, PAAMCO and PRISMA hedge funds lost, respectively, 1.19%, 7.64% and 8.01%. In 2019, the KERS hedge funds lost 0.54%. On top of the losses were excessive fees. Compl. ¶¶ 94–96.

The poor hedge fund returns, resulting from the wrongful conduct complained of and caused in part by the excessive and wasteful Black Box hedge fund fees, were a drag on KRS returns for each 5-year period ended from 6/30/2015 through 6/30/2019, and thus diminished the amount of "upside sharing interest" the Tier 3 beneficiaries received. Were it not for the defendants' misconduct and waste of plan assets which have been ongoing well through 2018–20, the investment returns of KRS would have been higher, and the upside sharing of these Tier 3 beneficiaries would have been higher and their ultimate pension benefit greater. ***This injury in fact has already occurred***. The *minimum* "drag" for each of the five-year periods mentioned is (Compl. ¶ 96):

fye 6/30/15	fye 6/30/16	fye 6/30/17	fye 6/30/18	fye 6/30/19
3.56%	3.89%	3.54%	2.97%	1.05%

They have been subjected to and suffered individual injury by poor investment returns (the "Black Box" hedge funds) and wasteful expenses that have reduced/lowered

> ***their yearly "upside" credit and their ultimate pension benefits***, all the result of the long ongoing scheme, conspiracy, and common enterprise of the T/Os and Defendants which can be remedied to KRS and its plans. Compl. ¶¶ 10–11.
>
> All the Tier 3 Plaintiffs' personal contributions to KRS face a clear increasing risk, along with loss or curtailment of their benefits, when the KRS funds fail likely as they will in the foreseeable future, benefits they have helped fund via their mandatory contributions.
>
> The Tier 3 Plaintiffs are stuck in the worst funded public retirement funds in the United States, and are ***forced to continue to "contribute" their own earnings into the smoldering remains of what were once fully funded plans***, which the T/Os and Defendants helped destroy and where many of the benefits they are forced to help fund are outside of the inviolable contract protections. Compl. ¶¶ 15–18.
>
> The named Plaintiffs bring this action to expose the wrongdoing of whose who betrayed their trust, and to recover, on behalf of KRS, as much money as possible to repair its prior losses and to improve KRS's current and ongoing financial condition and liquidity, which help protect Plaintiffs' existing and promised, ***but unguaranteed, benefits, as well as the safety of their past, continuing and future personal contributions into the endangered funds***. Compl. ¶¶ 15, 18.

As the KRS "***death spiral***" continues to unfold, the harm/injury to the Tier 3 Plaintiffs continues to accrue. Despite a booming stock market, now at all-time highs, ***the financial condition of KRS continues to deteriorate, further endangering the Tier 3 members' vested, but unprotected, individual retirement accounts***. The Tier 3 Plaintiffs have again been denied any "upside sharing" as KRS achieved overall returns of just 1.2% in the fiscal year ended June 30, 2020. John Cheves, *The Stock Market Is Up Why Did the Ky State Pension System Only Earn a 1.2% Return?*, LEXINGTON HERALD-LEADER, Aug. 20, 2020. These paltry returns in the midst of soaring equity prices are due to the continuing impact of defendants' misconduct which crippled the finances of the KRS funds,

locking some of them into "preservationist" investment programs; because these funds are so illiquid and cash-poor, due to prior mismanagement, bad investments, excessive fees and waste of trust assets, they cannot risk investing in higher return investments available to honest, well-managed and overseen pension funds.

2. ERISA Case Law Establishes the Tier 3 Plaintiffs' Standing

According to *Overstreet*, Kentucky has "adopt[ed] the federal test for constitutional standing." *Overstreet*, 603 S.W.3d at 257 n.46. Since the Tier 1 and Tier 2 plaintiffs' claims were dismissed based on ERISA authorities (*Thole*) and rationales (*Overstreet*), these ERISA cases should be dispositive of the Tier 3 Plaintiffs' constitutional standing. To turn a phrase: if you died by an ERISA sword, you should live — or be resurrected — by ERISA precedents.

A wealth of ERISA case law establishes that ***members in a defined-contribution plan,*** like the Tier 3 Plaintiffs, without guaranteed or fixed benefits, whose individual retirement account balances, *i.e.*, are impacted by excessive fees, bad investments, and trustee/advisor fiduciary and oversight failures, ***have standing to sue to recover damages for the overall plan from which they and all other plan members will benefit***. It does not matter that the named plaintiff has not yet suffered an actual loss or damages — ***diminished benefits suffice***. It is not necessary at the pleadings stage for the alleged harm to be pleaded in detail, much less quantified as the Tier 3 Plaintiffs have done here, alleging thousands of dollars of diminished individual pension accounts. *Boley v. Universal Health Servs., Inc.*, 2020 WL 6381395, at *3 (E.D.

Pa. Oct. 30, 2020) ("Standing allegations need not be crafted with precise detail nor must the plaintiff prove his allegations of injury.").

These ERISA cases demonstrate that, while necessary to sue, constitutional standing is a ***technical*** requirement, the concrete-harm prong of which requires only ***a modest*** individual injury. Once this technical requirement is met the plaintiff may ***sue on behalf of the plan***, ***pursuing litigation challenging plan-wide conduct that*** "***sweeps beyond his individual claim***," ***including misconduct taking place before and/or after that plaintiff's membership in the plan***, ***to achieve a recovery that will make the plan whole***, ***benefiting the plaintiff and all other plan participants***. Once the plaintiff pleads that veritable "***peppercorn***" of injury or harm and seeks a remedy that will help redress his individual loss by making a recovery for the plan, as one judge said, the ***plaintiff has the*** "***ball***" ***and may*** "***play***," *i.e.*, sue for everything — "***plan wide misconduct***" and "***plan wide relief***" "***sweeping beyond his own injury***."[14]

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[14] Both *Thole* and *Overstreet* referred to corporate derivative cases to show that standing was satisfied by a shareholder's obligation to own shares at the outset of and throughout the litigation. Citing *Thole*'s reliance on corporate derivative cases, *Overstreet* said: "The requirement that derivative plaintiffs maintain ownership of their shares ... has constitutional standing implications as well ... [a] '***modest financial stake***' in the outcome of a derivative suit [satisfies] constitutional standing." ***Both*** **Thole** ***and*** **Overstreet** ***cited*** **Gollust v. Mendell**, 501 U.S. 115 (1991), ***where the shareholder plaintiff had but one share***, as best we can determine (no more than $25). Yet this "modest financial slate" created constitutional standing.

We note that this timeless line of jurisprudence allows shareholder suits asserting multi-billion-dollar claims for the corporate entity, even if the shareholder plaintiff has a tiny holding. *Subin v. Goldsmith*, 224 F.2d 753, 761 & n.9 (2d Cir. 1955) (Frank, J.) ("[O]f course it is irrelevant that plaintiff owns but a few shares." "*Cf*. The Code of Maimonides, BK. IV. The Book of the Judges (Transl.

The body of ERISA cases discussed below all involve defined-contribution plans (not defined-benefit plans), which in the past decade have come to dominate the U.S. pension world. (*Thole*-type defined-benefit plans are dinosaurs in the modern pension world). These ERISA cases involve both derivative claims on behalf of the fund and class action claims on behalf of plan members, where under ERISA, ***the recovery goes to the Plan*** — creating the derivative remedy/result as sought by the Tier 3 Plaintiffs. In both types of suits — derivative or class action to benefit the Plan, the derivative or class plaintiff/representative must ***demonstrate individual Article III constitutional standing***. ***Once*** a plan member establishes standing (even if diminished returns are not the only actual loss), ***he can sue for relief*** "***sweeping beyond his own injury***," challenging "***plan wide misconduct***" and ***seeking*** "***plan wide relief***."

All of the ERISA cases discussed below involved ***defined-contribution plans*** where the individual injuries pleaded amidst plan-wide losses pale in comparison to those suffered by the Tier 3 Plaintiffs and KRS. Often, the levels of misconduct by defendants pale as well. Yet Article III standing was present. Given the very serious allegations of wrongdoing, it would be a real failing of justice by this Court if the Tier 3 Plaintiffs were denied ***even the opportunity to pursue***

1949) Ch. XX, Clause 10: 'Think not that the foregoing rules apply only to a case involving a large sum of money to be taken from one (litigant) and given to the other. At all times and in all respects, regard a suit entailing one thousand maneh and one entailing a perutah as of equal importance.'"); *Lewis v. Curtis*, 671 F.2d 779 (3d Cir. 1982) ("The fact that Lewis' investment is comparably small ['a few shares'] is irrelevant."); *Marshall v. Spang & Co.*, 321 F. Supp. 1310 (W.D. Pa. 1971) (owner of 400 shares out of 2.4 million — worth $2,200 — can sue); *Dawson v. Dawson*, 645 S.W.2d 120 (Mo. Ct. App. 1982) ("*de minimis*" stake — 25 shares "***more than adequate***").

relief via a state statute that provides them an express remedy on behalf of the plan. KRS § 61.645.

In *Cassell v. Vanderbilt University*, 2018 WL 5264640 (M.D. Tenn. Oct. 23, 2018) members sued ***on behalf of the Plan*** alleging breach of fiduciary duty, *i.e.*, excessive fees[15] (*id*. at **1–3, 6):

> ... [T]he Court must determine whether Plaintiffs have constitutional standing to bring their claims. As Circuit Judge Sutton recently stated: "***Article III standing is to federal courts as a ball is to soccer***. ***If you have it***, ***you can play***. If you don't, you can just pretend." ...
>
> Courts have recognized that a plaintiff who is injured in his or her own plan assets — and thus has Article III standing — may proceed under Section 1132(a)(2) ***on behalf of the plan or other participants even if the relief sought sweeps beyond his own injury***.
>
> Once an individual has alleged a distinct and palpable injury to himself, he has standing to challenge a practice even if the injury is of a sort ***shared by a large class of possible litigants***.
>
> [***Plaintiffs alleged***] ***an imprudent process that allegedly injured all Plan participants, including Plaintiffs, when a portion of those fees were charged to individual accounts***. Plaintiffs have standing to bring these claims related to administrative, management and record-keeping fees.
>
> ***
>
> If the plaintiffs are successful, any assets recovered from Defendants ***would first be paid into the Plan and then allocated to Plaintiffs' individual accounts as appropriate***.

Once constitutional standing is present, a plan member can pursue plan-wide conduct that predated his entry into the plan, *i.e.*, plan-wide misconduct and

[15] KRS § 61.645(15)(h) ("In discharging his or her administrative duties under this section, a trustee shall strive to administer the retirement system in an efficient and cost-effective manner for the taxpayers of the Commonwealth of Kentucky and shall take all actions available under the law to contain costs for the trusts, including costs for participating employers, members, and retirees.").

relief that "***sweep more broadly than the injury he personally suffered***." *Braden v. Wal-Mart Stores, Inc.*, 588 F.3d 585 (8th Cir. 2009), involved a plan with one million participants and $10 billion in assets. Plaintiffs alleged past excessive fees and expenses of $60 million — and future waste of $20 million per year, suing on behalf of the plan for excessive plan expenses ***that inflicted miniscule charges against plaintiffs' individual account***. Nevertheless, Article III standing was found present and the plaintiff permitted to pursue ***plan-wide relief*** (*id.* at 591–92):

> Article III generally requires injury to the plaintiff's personal legal interests, but that does not mean that a plaintiff with Article III standing may only assert his own rights or redress his own injuries. ***To the contrary***, ***constitutional standing is only a threshold inquiry, and*** "***so long as*** [***Article III***] ***is satisfied***, ***persons to whom Congress has granted a right of action***, ***either expressly or by clear implication***, ***may have standing to seek relief on the basis of the legal rights and interests of others***." ***In such a case***, ***a plaintiff may be able to assert causes of action which are based on conduct that harmed him***, ***but which sweep more broadly than the injury he personally suffered***.
>
> ***
>
> [The district court] concluded that Braden had no standing for ***the period before he began participating in the Plan*** because "[u]nder ERISA, a fiduciary relationship does not exist towards potential participants in a plan and such potential participants have no standing to sue for ... breach of fiduciary duty." It therefore granted appellees' motion to dismiss "all claims occurring prior to October 31, 2003." In reaching this conclusion, the district court mixed two distinct issues. Whether Braden may pursue claims on behalf of the Plan at all is a question of constitutional standing which turns on his personal injury. Whether relief may be had for a certain period of time is a separate question, ***and its answer turns on the cause of action*** **Braden** ***asserts***.
>
> Braden has satisfied the requirements of Article III because he has alleged actual injury to his own Plan account. ***That injury is fairly traceable to appellees' conduct because he has alleged a causal connection between their actions*** — even those taken before his participation in the Plan — and his injury.

> Finally, the injury is likely to be redressed by a favorable judgment. Braden has thus "made out a 'case or controversy' between himself and [appellees] within the meaning of Art. III."

In *Boley*, plan members sued for breach of fiduciary duties — bad investments and excessive fees — which ***reduced*** investment returns, ***negatively impacting*** their retirement accounts. *See* 2020 WL 6381395, at *2–3. They sued "***on behalf of the Plan***." Because the plaintiffs had invested in only a few of the many investment funds offered by the Plan, defendants sought to fracture and restrict the scope of plaintiffs' constitutional standing and defeat their attempt to sue ***for the plan***, ***seeking plan-wide relief*** (*see id.* at **2–3, 6). The Court rejected this attempt to "make standing law more complicated than it needs to be":

> The Fiduciaries argue Ms. Boley, Ms. Sutter, and Ms. Johnson only invested in seven of the Plan's funds during the putative class period and therefore lack standing to bring claims about the remaining funds. They rely on the Supreme Court's recent analysis in *Thole v. U.S. Bank, N.A.* to argue the named participants cannot demonstrate injury with respect to the funds they did not invest in because "[w]in or lose, [p]laintiffs will receive 'not a penny less' (or more)." ***The Employees argue they have alleged injury with respect to each of their claims — which implicate "plan-level conduct" — and may therefore bring their claims on behalf of the Plan. We agree with the Employees and find they have standing***.
>
> The Employees seeking relief under ERISA must demonstrate injury to one's own plan account to have Article III standing. She may show injury through "[***d***]***iminished returns relative to available alternative investments and high fees*** ... ***regardless of whether the plaintiff suffered an actual loss on his investment or simply realized a more modest gain***." ***The Employee may also satisfy this requirement by alleging an injury to a plan's assets unrelated to specific funds, if plan participants are all assessed a portion of the injury. Once an ERISA plaintiff has alleged injury to her own account, she "may seek relief under*** § ***1132***(***a***)(***2***) ***that sweeps beyond*** [***her***] ***own injury***."

***

> [T]he Fiduciaries err in arguing the nature of the plan was "irrelevant" to the [*Thole*] Court's standing analysis. We disagree; ***the Court stated the defined-benefit nature of the plan rather than a defined-contribution plan to be*** "[***o***]***f decisive importance***" because in a defined-benefit plan, participants "receive a fixed payment each month, and the payments do not fluctuate with the value of the plan or because of the plan fiduciaries' good or bad investment decisions" while in a defined-contribution plan, "benefits can turn on the plan fiduciaries' investment decisions." The Fiduciaries further attempt to "***make standing law more complicated than it needs to be***" ***by arguing ERISA plaintiffs are now required to demonstrate standing with respect to each of the funds in a plan, regardless of the claims the plaintiffs bring***. The Supreme Court in *Thole* and the Constitution require plaintiffs demonstrate a concrete stake in the outcome of each of ***their claims*** — the Employees have done so here.
>
> Unlike in *Thole*, Ms. Boley, Ms. Johnson, and Ms. Sutter have demonstrated ***loss to their own accounts with respect to each of their three claims***. They suffered individualized injury for their first claim regarding the imprudence of the suite of Fidelity Freedom Funds because they each invested in at least one of those funds. They further allege injury arising to pursue their latter two claims related to the Plan's allegedly imprudent decision-making processes, ***because at least a portion of the excessive fees or lower returns affected their individual accounts. They sufficiently plead standing for their claims under Thole, as the outcome of each of these claims could affect their returns***.

In *Bekker v. Neuberger Berman Group LLC*, 2018 WL 4636841 (S.D.N.Y. Sept. 27, 2018), a participant in the pension plan which included his "***individual account***" invested in a "***collective trust***" – as is the case with the Tier 3 Plaintiffs – sought to recover ***for the Plan***, alleged excessive fees paid over a 10-year period. The court made clear standing existed ***even if plaintiff's account had positive returns***. ***Diminished returns suffice to provide concrete harm and constitutional standing*** (*id*. at **4–5).

> ***Defendants argue that Plaintiff lacks standing because he has suffered no concrete injury, incurring no personal financial loss, but rather received a positive return*** ....
>
> ***
>
> The Court finds Plaintiff's allegations sufficient in this regard. ***Diminished returns relative to available alternative investments and high fees represent concrete injuries, implicating a financial loss in comparison to what a plaintiff might have received but for the defendant's alleged breach of duty, which can support a cognizable injury regardless of whether the plaintiff suffered an actual loss on his investment or simply realized a more modest gain***.
>
> ... ***In this case, Plaintiff has alleged that the VEF, a fund in which he personally invested, underperformed and was charged improper fees, establishing an injury particularized to him, not merely an injury to the plan. Plaintiff has therefore alleged a sufficiently particularized injury in fact***.

In *Cryer v. Franklin Templeton Resources, Inc.*, 2017 WL 4023149 (N.D. Cal. July 26, 2017), a former plan participant sued over his final pension distribution which he alleged was ***reduced*** due to plan-wide misconduct. The Court found constitutional standing (*id*. at **4–5):

> FRI argues in multiple ways that Plaintiff does not have standing to bring this lawsuit .... First, it argues that he does not have standing to bring claims regarding funds in which he did not invest ... that he lacks standing to pursue claims related to the funds in which he invested that outperformed comparable funds because he was not injured in those instances.
>
> These arguments fail primarily because ... ***the lawsuit seeks to restore value to and is therefore brought on behalf of the Plan***. The Supreme Court has explained that "recovery for a violation of 29 U.S.C. § 1109 for breach of fiduciary ***duty inures to the benefit of the plan as a whole, and not to an individual beneficiary***." ... The potential "liability of the fiduciary is "to make good to such plan any losses to the plan ... and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan." ... ***Accordingly, in determining***

> ***constitutional standing***, ***courts look not to individual funds but*** "***to the nature of the claims and allegations to determine whether the pleaded injury relates to the defendants' management of the Plan as a whole***." …
>
> FRI's arguments are not persuasive because ... any ***recovery is on behalf of the Plan as a whole***. The common focus will be "***on the conduct of Defendants***: whether they breached their fiduciary duties to the Plan as a whole by paying excessive fees, whether they made imprudent investment decisions." ...

After finding statutory standing because a former plan member was still a statutory "participant" under ERISA, the court in *In re: Mutual Funds Investment Litigation*, 529 F.3d 207 (4th Cir. 2008), considered the constitutional standing of former plan members who had cashed out to sue for the plan, alleging their payout ***was diminished*** by fiduciary misconduct. Focusing on the redressability prong of the Article III standing test, the court explained how plan-wide relief redresses the individual injuries of plan members (*id*. at 210, 216–19):

> Because we conclude that the plaintiffs have "***statutory standing***" to bring their claims, we must also now decide whether they have constitutional standing ....
>
> In this case, the first two elements are not at issue: If the plaintiffs' allegations are true, they suffered injury in that their retirement accounts were ***worth less than they would have been absent the breach of duty***, and this injury was caused as the plaintiffs have alleged, by the fiduciaries' misconduct. The defendants contend, however, that the plaintiffs have not satisfied the third element of constitutional standing — ***that their injury be redressable by a favorable decision in this litigation***.
>
> Defendants contend that even if the plaintiffs can prove the merits of their case, ***it is wholly speculative whether any recovery by the plan would pass through to the plaintiffs' individual accounts***.

Of course, a participant suing to recover benefits on behalf of a defined contribution plan for breach of a fiduciary duty is still not entitled to have monetary relief paid directly to him .... ***The recovery is obtained by the plan — even if it is for injury only to a particular individual account — because the aggregation of individual accounts defines the assets of the plan***. ... As the Supreme Court explained, "***fiduciary misconduct need not threaten the solvency of the entire plan to reduce benefits below the amount that participants would otherwise receive***." ***It is sufficient that*** "***a fiduciary breach diminished plan assets payable to all participants and beneficiaries, or only to persons tied to particular individual accounts***."

The defendants' argument that restoration of individual accounts would be speculative following any recovery in these cases thus fails to recognize that in a defined contribution plan, ***it is the plan assets in the individual accounts that are restored*** ....

***

In sum, if we take the plaintiffs' cases as they come to us and therefore accept for now the allegations of the complaints as true — that the defendants breached fiduciary obligations imposed by ERISA section 409(a) ***and those breaches had an adverse impact on the value of the plan assets in the plaintiffs' individual accounts — then the plaintiffs have constitutional standing to bring these claims***.

***

"The benefit in a defined-contribution pension plan is, to repeat, just whatever is in the retirement account when the employee retires or ***whatever would have been there had the plan honored the employee's entitlement, which includes an entitlement to prudent management***." ...

In short, we conclude that participants in defined contribution plans controlled by ERISA have colorable claims against the fiduciaries of their plans when they ***allege that their individual accounts in the plans were diminished by fraud or fiduciary breaches and that the amounts by which their accounts were diminished constitute part of the participants' benefits under the plans. The plaintiffs' claims in this case are for such additional benefits, not damages, and they therefore have standing to sue*** ....

In *Clark v. Duke University*, 2018 WL 1801946 (M.D.N.C. Apr. 13, 2018), pension plan participants who had invested in just a few — but not all — funds available, sued over excessive plan expenses (*id*. at **3–5):

> ... [***T*]*he plaintiffs allege that all funds in the Plan incurred excessive fees and expenses because the defendants breached their fiduciary duties. The plaintiffs allege that these breaches injured them because they assessed a portion of the Plan's higher recordkeeping and service costs that were unrelated to specific funds***.
>
> These allegation and undisputed facts are sufficient at this stage to establishes that the named plaintiffs have Article III standing to pursue their theories of liability. ***The named plaintiffs have alleged actual injury to their individual Plan accounts*** .... That injury is fairly traceable to the defendants' conduct because the plaintiffs have plausibly alleged that the defendants' breaches of fiduciary caused their injury. Finally, a judgment in favor of the named plaintiffs is likely to redress the injury.
>
> The defendants contend that the named plaintiffs only have standing to challenge the 25 funds in which they invested and that they do not have standing to challenge the inclusion of any of the other 375 funds in the Plan because inclusion of those funds in the Plan because inclusion of those funds did not injure them However, courts have recognized that a plaintiff who is inured in his or her own plan assets — and thus has Article III standing — ***may proceed*** ... ***on behalf of the plan or other participants even if the relief sought*** "***sweeps beyond his own injury***."
>
> "***At bottom, the gist of the question of standing is whether*** [***plaintiffs***] ***have such a personal stake in the outcome of the controversy as to assure that concrete adverseness which sharpens the presentation of issues upon which the court so largely depends for illumination***."

In *Taylor v. United Technologies Corp*., 2008 WL 2333120 (D. Conn. June 3, 2008), plan members sued complaining of excessive expenses and bad

investments, including fraud and breach of fiduciary duties, seeking ***to benefit the fund*** (*id*. at *3):

> ***Plaintiffs [allege] imprudent decisions and charges of excessive fees and costs that damaged the Plan as a whole. Because a retirement plan is an "aggregation of its participants' individual accounts," any loss to the Plan causes a loss to Plan's participants***. ... Thus, plaintiffs fulfill standing based on their allegation that defendants breached their fiduciary duties by making decisions ***resulting in impaired returns or unreasonable fee charges and expenses***. "If, but for the breach, the Fund would have earned more than it actually earned, there is a loss for which the breaching fiduciary is liable." *Dardaganis v. Grace Capital, Inc.*, 889 F.2d 1237, 1243 (2d Cir. 1989). Accordingly, the loss to the Plan assets due to excessive fees or impaired returns represents a concrete and actual injury to satisfy standing."

There are many more such cases. *See, e.g., Vaughn v. Bay Envtl. Mgmt.*, 567 F.3d 1021 (9th Cir. 2009) (former plan members who obtained full distribution of benefits have standing to sue to recover plan losses due to fiduciary breaches that "allegedly reduced the amount of their benefits"); *Evans v. Akers*, 534 F.3d 65 (1st Cir. 2008) (same); *Pender v. Bank of Am.*, 788 F.3d 354 (4th Cir. 2015) (same); *Vellali v. Yale Univ.*, 333 F.R.D. 10 (D. Conn. 2019) (class action to recover damages to plan — "plaintiffs have established standing here by alleging an injury in fact to their plan accounts," thus can pursue the full scope of the Plan's losses); *Graden v. Conexant Sys.*, 496 F.3d 291 (3d Cir. 2007) (diminished benefits create standing — damages not required); *Falberg v. Goldman Sachs Grp.*, 2020 WL 3893285 (S.D.N.Y. July 9, 2020) (Plan participant whose account was impacted by excessive fees and bad investments has standing to sue).

The Tier 3 Plaintiffs' Constitutional Standing to sue is beyond fair dispute. The Defendants' refusal to stipulate to the Tier 3 Plaintiffs' Constitutional Standing is just more pursuit of legal technicalities to bar their meritorious claims.

B. Intervention by the Tier 3 Plaintiffs Is Proper Both as a Right and by the Court's Permission

Intervention is controlled by CR 24.01 and 24.02, which provide:

> **CR 24.01 Intervention of right**
> Upon timely application anyone shall be permitted to intervene in an action (a) when a statute confers an unconditional right to intervene, or (b) when the applicant claims an interest relating to the property or transaction which is the subject of the action and is so situated that the disposition of the action may as a practical matter impair or impede the applicant's ability to protect that interest, unless that interest is adequately represented by existing parties.

> **CR 24.02 Permissive Intervention**
> Upon timely application anyone may be permitted to intervene in an action: (a) when a statute confers a conditional right to intervention or (b) when an applicant's claim or defenses and the main action have a question of law or fact in common... In exercising its discretion, the court shall consider whether the intervention will unduly or prejudice the adjudication of the rights of the original parties.

This Court recently laid out the proper application of these rules in permitting the OAG to intervene:

> Our Civil Rules provide for intervention under two mechanisms: intervention as of right and permissive intervention. Under certain circumstances, a court must permit a party to intervene as a matter of right: "[u]pon timely application anyone shall be permitted to intervene in an action: a) when a statute confers an unconditional right to intervene." CR 24.01(1) (emphasis added). In other circumstances, a court has discretion to permit intervention: [u]pon timely application anyone may be permitted to intervene in an action: a) when a statute confers a conditional right to intervene or b) when an applicant's claim or defense and the main action have a question of law or fact in common." CR 24.02 (emphasis added). CR 24.02 "provides trial courts with discretion to allow intervention in cases if the interest of the movant so warrants, even if the asserted

> interest fails to satisfy the dictates of CR 24.01." *A.H. v. W.R.L.*, 482 S.W.3d 372, 375 (Ky. 2016).
>
> ***
>
> The Court finds that the Attorney General has been granted a statutory right to intervene sufficient to satisfy CR 24.01(1). ***The attorney General is*** ... ***empowered by KRS 15.020 to appear in cases such as the present cases, hearings and proceedings*** ... ***in which the Commonwealth has an interest***." However, even if KRS 15.020 did not grant the Attorney General this right, ***the Court in its discretion finds that the Attorney General holds a strong interest in the subject matter of this case in his capacity as the attorney for the Commonwealth to allow him to permissively intervene*** ..., ***the Original Plaintiffs here both have a personal interest in protecting their retirement payments, but also a public interest in ensuring that KRS assets — funded in part by taxpayer dollars — are managed in a prudent fashion. It is this reason that the Attorney General has an interest in this action*** ....

1. Intervention as of Right Is Proper

This Court found the OAG had a right to intervene because KRS § 15.020 authorized him to "***appear in cases***" on behalf of the Commonwealth where it "***has an interest***." Dec. 28, 2020 Order at 13. The Tier 3 Plaintiffs have an ***express statutory right to sue*** for KRS under KRS § 61.645(15), and valid claims under common law and trust as well. *See* Nov. 30, 2018 Opinion & Order at 22–27. If the ***general language*** of KRS § 15.020 gave the OAG a ***right*** to intervene in this case, the specific cause of action in KRS § 61.645(15) should give the Tier 3 Plaintiffs a right to intervene. They have prudential standing by statute to assert the same claims being asserted in the *Mayberry* action.

The Tier 3 Plaintiffs' entitlement to intervene as of right is indeed stronger than the OAG's. Unlike the OAG, the Tier 3 Plaintiffs also "claim ***an interest relating to the property or transaction*** which is the subject matter of the action." CR 24.01. While the Attorney General could make no such claim, this

Court (and the Supreme Court) recognized that KRS beneficiaries and therefore Tier 3 Plaintiffs ***have a property interest in the contributions they have made to KRS over the years***.[16] ***In the case of the Tier 3 Plaintiffs, even their vested benefits are unguaranteed and increasingly at risk of loss***. The Tier 3 Plaintiffs certainly have an interest relating to the property or transaction that is the "subject matter" of the *Mayberry* litigation.

The Tier 3 Plaintiffs also face a risk, as a practical matter, that the dismissal of the KRS derivative claims asserted by the *Mayberry* Plaintiffs for lack of constitutional standing will impair or impede their ability to protect their interests. If those previously pleaded claims upheld by this Court are not asserted, as a practical matter that would not only impede or impair — it would eliminate the Tier 3 Plaintiffs' ability to protect their vested property interests in KRS.

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[16] This Court stated in its November 30, 2018 Opinion & Order (at 10):

> Moreover, under controlling case law, the plaintiffs have a ***property interest*** in the funds administered by KRS. For example, the Kentucky Supreme Court has held that public employees have a ***protected property interest*** in the retirement funds administered by KRS by virtue of their personal contributions to those retirement funds through payroll deductions. *See Commonwealth ex rel. Armstrong v. Collins*, 709 S.W.2d 437, 446–47 (Ky. 1986). As noted, Plaintiffs are public employees who have paid into the pension program to secure their retirement, and they therefore have a ***vested financial interest*** in ensuring that the program is administered in compliance with the very fiduciary duties that are designed to protect the interests of KRS's members.

2. Permissive Intervention Is Proper

The Tier 3 Plaintiffs also satisfy all the requirements for permissive intervention, again more strongly than did the OAG. Permissive intervention is proper when a statute confers "a ***conditional*** right to intervene" or when an "***applicant's claim*** or defense ***and the main action have a question of law or fact in common***." CR 24.02. Both conditions are satisfied here.

If for some reason KRS §61.645(15) is viewed as requiring Tier 3 Plaintiffs to establish certain conditions to proceed (*i.e.* constitutional standing) then KRS § 61.645 confers ***at least a conditional right to intervene***. But fundamentally the Tier 3 ***claims asserted in their Complaint are the same claims asserted in the original*** **Mayberry** ***action***. They are 100% overlapping in terms of the factual allegations and the substantive claims. And, of course, they now also mirror the allegations of the OAG's intervening complaint because the OAG used the *Mayberry* Plaintiffs' allegations.

Permitting these Tier 3 Plaintiffs to intervene will certainly cause no delay in the case. To the contrary, it will finally overcome Defendants' incessant pursuit of technicalities that has delayed it for three years. Nor will their intervention prejudice the rights of the original parties. In fact, the Tier 3 Plaintiffs' intervention will ***save*** the assertion of KRS's derivative claims for which this Court noted the necessity that they be vigorously litigated to protect the public interest. Litigation of these claims will prejudice no one, but it has the potential to greatly benefit KRS and its 300,000-plus members; if the recovery can restore the KRS plans to financial sustainability, it may eliminate the necessity of the Commonwealth's paying out its inviolable contract obligations. This would benefit the

Commonwealth and its taxpayers, at least indirectly, which was the intent of the *Mayberry* Plaintiffs in suing ***derivatively for both KRS and the Commonwealth in the first place. The KRS derivative claims are far stronger than any claims that can be pursued by the Commonwealth***.

3. Intervention Is Proper in Representative Litigation Where Standing Has Been Lost

Mayberry was not an individual lawsuit where the plaintiff quit or was thrown out, leaving only his own rights behind. This is a ***representative lawsuit*** where the original plaintiffs did not assert individual claims seeking damages for themselves, but rather a representative claim seeking damages on behalf of another, *i.e.*, KRS. Nor were the original claims asserted by the *Mayberry* Plaintiffs personal to them in the sense of an automobile accident, breach of contract, or other claim where the harmed party sues and seeks individual relief only for himself. The original *Mayberry* Plaintiffs sought to assert claims – later sustained by this Court — on behalf of KRS. Due to a ***technical*** defect they lost their ability to continue to prosecute the claims (that this Court said they had standing to pursue under ***the existing state of law when the lawsuit was filed***). There is a wealth of authority upholding the right of an applicant to intervene in a representative lawsuit, *i.e.*, a class action or a derivative claim, where the original party suing did not have or has lost his ability to continue, losing standing to assert an otherwise meritorious claim as a representative plaintiff.

As the Court observed in its December 28 Order, "while this matter proceeded through Kentucky's appellate courts, the doctrine of standing was being modified and restricted" in ways that ultimately resulted in dismissal of the

Mayberry Plaintiffs.[17] Under Kentucky standing doctrine as previously understood, the rights and interests of Tier 3 members were represented and protected by the claims as advanced by the *Mayberry* Plaintiffs — who indeed had standing under Kentucky law as it existed when the case was initially filed in December 2017. But that has now changed, and the Tier 3 Plaintiffs should be allowed to step in, as they clearly have standing even in view of the modifications of and restrictions to Kentucky's standing doctrine.[18] Defendants will no doubt assert that Kentucky law embodies in effect a "Catch-22" rule, but they will be utterly unable to articulate how they would be prejudiced by the granting of this motion to intervene (especially now that the Attorney General has been permitted to appear herein) or how denial of the Tier 3 Plaintiffs' request to step into the litigation could possibly be fair and equitable.

The federal cases previously cited by Defendants for the proposition that dismissal of a derivative case for lack of standing by the original derivative plaintiff necessarily precludes amendment or intervention are neither binding nor

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[17] When this case was originally filed, *Sexton* had not been decided and thus Kentucky had not yet adopted the *Lujan*-style "constitutional standing" doctrine on which the *Overstreet* opinion turned. The Mayberry Plaintiffs had standing under pre-*Sexton* standing rules, and in any event the law of standing in Kentucky, as it existed pre-*Sexton* when this case was filed, did not implicate subject matter jurisdiction.

[18] *See, e.g.*, *In re Extreme Networks S'holder Derivative Litig.*, 573 F. Supp. 2d 1228, 1237 (N.D. Cal. 2008) (holding that after original derivative plaintiff lost standing "another qualified shareholder can intervene on the grounds that their rights are no longer represented"); *Malcolm v. Cities Serv. Co.*, 2 F.R.D. 405, 407 (D. Del. 1942) (holding that after original derivative plaintiff lost standing, "[a]ny member of the class, otherwise qualified, may intervene in this suit on the ground that their rights are no longer adequately protected or even represented").

persuasive. The First Circuit very recently referred to this line of cases as "formalistic [in] approach" and observed that the "better reasoned authority" permits amendment in these circumstances.[19] *Yan v. Rewalk Robotics Ltd.*, 973 F.3d 22, 36 (1st Cir. 2020). The First Circuit went on to observe (*id.* at 37):

> We ... see no reason why this permissiveness does not extend to motions seeking to add a named party asserting the exact same claim that is already pleaded in the complaint. *See Allied Int'l, Inc. v. Int'l Longshoremen's Ass'n*, 814 F.2d 32, 34–36 (1st Cir. 1987) (citing the advisory committee's note to the 1966 amendment to Federal Rule of Civil Procedure 15, which states that 'the attitude taken in revised Rule 15(c) toward change of defendants extends by analogy to amendments changing plaintiffs,' and allowing an amendment to substitute the assignee where the original plaintiff had assigned its claims in their entirety, which otherwise would have precluded any recovery).

Derivative cases in particular should not be subjected to the harsh rule Defendants advocate, requiring dismissal without opportunity to cure when the original plaintiff loses standing, as the rights to be vindicated in such a case are those of the company or trust, not the individual plaintiffs (even where, as here, the Tier 3 Plaintiffs have been individually harmed by the complained-of conduct). A rule to the contrary would encourage multiple duplicative actions, as shareholders (or other potential derivative plaintiffs) would conclude that they could not safely rely upon a named derivative plaintiff who might later be held to have lost standing. And that is not the rule. In *Mannato v. Wells*, 2013 WL 12101909 (N.D. Ga. May 6, 2013), the derivative plaintiff died and his estate sold his shares in the company for whose benefit the case had been filed, thus depriving

[19] *Yan* specifically notes disagreement with the "formalistic approach" taken by the Fifth Circuit in *Summit Office Park, Inc. v. United States Steel Corp.*, 639 F.2d 1278, 1282 (5th Cir. 1981), upon which Defendants have relied.

the case of a derivative plaintiff with standing. Counsel for the deceased derivative plaintiff thereafter sought to publish notice to permit another shareholder to step into the case. The court held that such notice should be given because the case otherwise would be dismissed on a non-merits-based technicality that could prejudice the interests of other shareholders who theretofore had been able to rely upon the derivative plaintiff to vindicate the claims of the corporation (*id*. at **2–3):

> [C]ourts have held the notice requirement applies to more than voluntary dismissals under Rule 41(a)(1) and have required notice to nonparty shareholders when a corporate claim has not been adjudicated on the merits and dismissal could preclude a nonparty shareholder from reasserting the claim on behalf of the corporation. ... The cases discussing the requirement of notice to nonparty shareholders, however, teach that a decision, or the circumstances, of a named shareholder class plaintiff that could result in the dismissal of derivative claims requires that notice be given to other shareholders to afford one or more of them to weigh in before dismissal and, in appropriate cases, to allow a substitute plaintiff to prosecute the claims asserted. Notice is especially important where dismissal may result in a later action being barred because the statute of limitations has run.

See also Beaver Assocs. v. Cannon, 59 F.R.D. 508, 511–12 (S.D.N.Y. 1973).

The Second Circuit recently addressed the procedural questions raised when a representative plaintiff loses standing, holding that the "consequences of losing a stake in ongoing litigation are determined not by asking whether the party losing its stake in the litigation has lost its ***standing*** but by asking whether the action has become ***moot***." *Klein v. Qlik Techs., Inc.*, 906 F.3d 215, 221 (2d Cir. 2018) (emphasis in original). The Court explained that the "standing doctrine evaluates a litigant's personal stake as of the outset of litigation [while the] [m]ootness doctrine determines what to do if an intervening circumstance

deprives the plaintiff of a personal stake in the outcome of the lawsuit, at any point during litigation after its initiation." *Id*. (cleaned up). The Second Circuit then elaborated on the policies at stake (*id*. at 222 (quoting *Friends of the Earth, Inc. v. Laidlaw Envtl. Servs. (TOC), Inc.*, 528 U.S. 167, 191 (2000)):

> "Standing doctrine functions to ensure, among other things, that the scarce resources of the federal courts are devoted to those disputes in which the parties have a concrete stake. In contrast, by the time mootness is an issue, the case has been brought and litigated, often ... for years. ... Thus, to abandon the case at an advanced stage may prove more wasteful than frugal." It may also prove prejudicial to non-parties who forewent filing a separate suit on the same issues in reliance on the outcome of the suit already brought. And it may enable defendants to game the judicial system by providing some sort of ephemeral relief to named plaintiffs to avoid the risk of more substantial relief being awarded to other real parties in interest.

Accordingly, under *Yan*, *Klein* and *Mannato*, the Court should permit the Tier 3 Plaintiffs to intervene so that they can continue to prosecute the claims previously asserted by the *Mayberry* Plaintiffs.

C. The Interests of the Tier 3 Plaintiffs, KRS Members and KRS's Trust Funds Cannot Be Adequately Represented by the OAG

1. The OAG Faces a Conflict in Dealing with Any Recovery for KRS

Adequacy of representation issues permeate intervention determinations. Intervention by the Tier 3 Plaintiffs is necessary to assure adequate representation of their own, KRS members' and KRS's interests. While the OAG can prosecute the damages claims of the Commonwealth/taxpayers, the OAG cannot seek or recover damages for, or deliver any recovery to, KRS. ***The OAG is not in a position to make the Tier 3 members whole or provide "plan-wide relief" benefiting KRS***.

The Commonwealth and KRS are separate legal entities, the latter established by statute providing a corporate form, to be overseen by independent Trustees. KRS § 61.515. Under Kentucky's ***statutory scheme***, the respective interests of the Commonwealth and KRS are separate, not aligned and in some regards conflicting. The OAG appears for (and only for) the Commonwealth and seeks a recovery ***for the Commonwealth***, not for KRS. The OAG has always sought to represent the Commonwealth and seeks to recover its — not KRS's — damages. Compare paragraph 1 of the OAG's intervening complaint and paragraph 1 of the FAC, and the respective prayers for relief, wherein the ***OAG deliberately cut out the language about damages incurred by KRS***.

Whenever the Attorney General "***has entered his appearance in a legal action on behalf of the Commonwealth of Kentucky*** ... and a disposition of that action has resulted in the recovery of funds or assets ... by judgment or settlement, ... ***those funds shall be deposited in the State Treasury and the funds or assets administered and disbursed by the Office of the Controller***." KRS § 48.005(3); *see also* KRS 15.020. Those monies must go into the "***general fund surplus account***" (KRS § 48.005(4)) and thus become available to elected officials — some of whom are hostile to public employee unions/pensions funds, favor other priorities, like tax cuts, and at a minimum face other fiscal pressures demanding state funding. Their predecessors hardly distinguished themselves in allocating public funds to KRS to assure its financial stability. Monies to pay general obligations of the Commonwealth are not protected and segregated ***trust funds*** recovered on behalf of KRS. Any net recovery on the KRS derivative damages claims asserted on behalf of KRS will be

an ***asset of KRS*** — "***trust funds to be held and applied solely***" for the benefit of KRS and its members. *See* Compl. ¶¶ 222–223; KRS § 61.515. Those litigating the derivative claims — the Tier 3 derivative plaintiffs ***and*** their lawyers — have fiduciary duties to KRS to ***maximize the value,*** **i.e.**, ***recovery for the KRS funds and its beneficiaries***, ***not the Commonwealth's*** "***surplus account***." The OAG has no discretion to disobey KRS §§ 48.005(3) or 61.515.

The OAG may assume that, because KRS is a state agency, it automatically has the exclusive power to represent KRS. That assumption is incorrect. It has no such exclusive power. KRS is a separate legal entity, which is distinct from the Commonwealth. *See, e.g.*, *Ky. Ret. Sys.*, 396 S.W.3d at 840; KRS § 61.515. KRS's board is "granted the powers and privileges of a corporation," including the power "[t]o conduct the business and promote the purposes for which it was formed." KRS § 61.645(2). ***Derivative suits exist to protect the assets of corporate entities like KRS from loss or damage due to failures of their fiduciaries or those who assist or conspire with them to damage the corporate entity***. *See* Ex. B at 4–7.[20] And the Legislature made sure that such remedy would exist to protect KRS by expressly authorizing members of KRS to sue to recover damages on behalf of KRS. *See* KRS § 61.645(15)(e)–(f). Both Houses of the Kentucky Legislature unequivocally endorsed the merits and importance of the prosecution of these derivative claims, and how private

[20] A true and correct copy of the Law Professors' *Amicus Curiae* Brief, filed in the Supreme Court on June 12, 2019 in *Overstreet*, is attached as Exhibit B. A true and correct copy of the Kentucky Legislature's *Amicus Curiae* Brief, filed in the Supreme Court on June 12, 2019 in *Overstreet*, is attached as Exhibit A.

enforcement of those claims under KRS § 61.645(15) was consistent with the Legislature's intent and the public interest. *See* Ex. A at 1–2, 11–12.[21]

Nowhere is the OAG expressly given the power to represent KRS in litigation — certainly not to the preclusion of other authorized causes of action. KRS § 61.645(11) provides in part that "[t]he Attorney General ***may*** act as ... attorney for the board, and the board may contract for legal services, notwithstanding the limitations of KRS Chapter 12 or 13B." However, in light of KRS § 48.005, KRS cannot hire the OAG, who is already pursuing money damages for the Commonwealth, because the OAG is hopelessly conflicted. Any money he may recover on the Commonwealth's claims must go to the general fund surplus account, not to KRS, and the Commonwealth's and KRS's claims face factual, damage and legal-defense conflicts that preclude concurrent representation by the OAG.

The Tier 3 Plaintiffs have not disputed the right of the OAG to intervene. They do, however, object to any attempt to take over or influence the prosecution of the KRS derivative claims. KRS's assets (including its legal claims for damages) are separate from the Commonwealth and belong to KRS, not the taxpayers; they are trust funds to be used exclusively for KRS trust purposes. KRS and the Commonwealth may have a common interest in creating as big a pot as possible, but have conflicting interests as to how to divide that pot. And they have many other conflicts as well.[22]

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[21] *See also* Thomas E. Rutledge, *Who Will Watch the Watchers? Derivative Actions in Non-Profit Corporations*, 103 K.Y.L.J. ONLINE 4 (Apr. 22, 2015).

[22] The chart below outlines some of these different, conflicting interests.

Commonwealth	KRS
Primary interests are future funding and protection of the Commonwealth in connection with potential payments under the inviolable contract protections.	Primary interests are recovering damages now including losses in and for past years.
Recovery goes to the State Treasury, specifically, the "general fund surplus account," under KRS § 48.005 (4).	Recovery goes to (and should be appropriately split among) the KRS trust accounts, including the insurance trust(s). *See* KRS §§ 61.515, 61.570, 61.701. This result flows from the "use or be sued" language in KRS § 61.645(2)(a). (Commonwealth's interests — because of the inviolable contract issues — would be in all recoveries going toward pension trust funding, directly or indirectly, not to insurance trusts — and not to past year accounts to benefit the Tier 3 members.)
Commonwealth's interests are different from both Tier 3 members, and Tier 1 and 2 members.	Tier 3 members have an interest in adding to past years' excess pension fund returns, to increase their sharing interests, and to insurance trust. Tier 1 and 2 interests do not conflict with these interests, but Commonwealth's interests do.
Attorney General is not the attorney for KRS unless the KRS Board requests that the Attorney General represent KRS. KRS § 61.645 (11).	Attorney General may act as attorney for the board, but the board can also contract for outside legal services (so the Attorney General is not the exclusive attorney for KRS). KRS § 61.645 (11).
Intervening Complaint ¶ 1: "damages for losses incurred ***by the Commonwealth***."	*Mayberry* FAC ¶ 1: "damages for the losses incurred ***by KRS***."
Intervening Complaint, Prayer ¶ 2: "Determining and awarding the ***Commonwealth of Kentucky*** the compensatory damages sustained as a result of the violations set forth above."	*Mayberry* FAC, Prayer ¶ 4: "Determining and awarding to ***KRS and its Pension Funds and the Commonwealth of Kentucky*** the damages sustained by them as a result of the violations set forth above."

2. The Commonwealth's Direct Claims Involve Conflicting Fact Patterns and Are Subject to Unique Defenses Not Applicable to the KRS Claims Asserted Derivatively

The factual and legal differences between the Commonwealth and KRS's competing claims are, as a practical matter, disabling to any attempt by the OAG to simultaneously prosecute both the Commonwealth's and KRS's claims. In permitting the OAG to intervene on behalf of the Commonwealth, this Court noted that the Defendants have ***potential defenses which they are entitled to pursue***. Given the procedural history of this case thus far, one can be sure they will do so — vigorously.

As the OAG's claims are tested by motion practice, and any surviving claims are prosecuted, unique defenses will occupy the OAG. Countering them will be a challenge requiring the OAG to ***focus on defending the Commonwealth's past conduct*** to avoid *in pari delicto*. He will face damage causation defenses and also have to establish that any damages claims by the Commonwealth are "***ripe,***" *i.e.*, represent actual damages presenting a "***justiciable***" claim, as opposed to future speculative damages, contingent on unknown events that may never occur and may be obviated by a large-enough recovery in the KRS derivative case. Given the Supreme Court's enthusiasm for standing, ripeness and justiciability and an appellate decision (*Sandoz*, 405 S.W.3d at 506) explicitly recognizing the *in pari delicto* defense to the Commonwealth in a suit by the OAG, these issues cannot be ignored.

We already know the Tier 3 Plaintiffs have powerful breach of fiduciary duty, breach of trust, aiding and abetting, common enterprise and conspiracy claims including ***direct*** breach of fiduciary duty claims against the advisors and

hedge fund sellers, that can yield punitive damages. *See* Nov. 30, 2018 Order. However, it is not yet established that those types of legal theories are available to the Commonwealth in a ***direct action*** prosecuted by the OAG. KRS is positioned differently than the Commonwealth. ***KRS had fiduciary and trust relationships with Defendants and they owed KRS substantial legal duties***. Whether those same duties are owed to the Commonwealth has yet to be determined.[23] While the Commonwealth no doubt has viable claims against the Trustees/Officers as defaulting state officials, they are not going to be the source of any recovery.[24] ***There are no cases that we — or the Supreme Court — found where the State, on behalf of taxpayers, has successfully pursued third parties using the fiduciary duty, aiding/abetting, common enterprise, and conspiracy theories available to KRS***.

While the Supreme Court stated the OAG had statutory authority "to initiate actions on behalf of the Commonwealth" it did not say what those claims were or that they were substantively viable. The Supreme Court's hostility to private enforcement does not translate into a full-throated endorsement of the merits of the taxpayers claims, only a call on the OAG to "***evaluate***" the facts and determine

[23] The Hedge Fund Sellers and others argued they owed the State no fiduciary duty during the 2018 Motion to Dismiss proceeding.

[24] ***They don't have any money***. Their inadequate insurance coverage has been exhausted, consumed by defenses fees. Suing them is symbolic — but it's a "dry hole." The Tier 3 Complaint continues to allege the Trustees' wrongful conduct, but has dropped them as defendants. Perhaps the OAG will again mimic our decision to drop them as defendants, as continuing to sue them may expose the OAG to an interlocutory appeal that will delay the OAG's case as it delayed the *Mayberry* Plaintiffs.

if "***a particular claim should be brought***." As to what substantive claims exist the Court's language is disquieting (*Overstreet*, 603 S.W.3d at 263–64):

> While Kentucky courts have historically permitted taxpayer claims in certain circumstances as a matter of equity, ***we have never allowed a suit like this***.
>
> First, taxpayers in Kentucky, on behalf of themselves, have been permitted to sue ***government bodies or their agents*** to challenge the propriety of city, county, or state tax or expenditure of public funds. Indeed, Plaintiffs cite only to cases ***against government entities*** in which taxpayers seek to enjoin the imposition of an illegal tax or expenditure of public funds or to compel compliance with certain statutory or constitutional requirements attached thereto. Only in two cases cited by Plaintiffs do taxpayers seek any form of monetary relief; and in both cases, county taxpayers were ***permitted to sue local government officials*** to recover salaries illegally paid to them in excess of a county fiscal court order.
>
> By contrast, under this direct-taxpayer theory of standing, ***Plaintiffs seek damages from private third parties and KRS officials in their individual capacities for tort damages allegedly sustained to all Kentucky taxpayers***. ***Plaintiffs do not cite***, ***and we cannot find***, ***any Kentucky cases permitting such a novel theory of standing***.

Nor did the Supreme Court state that the Commonwealth had suffered damages "***ripe***" for adjudication, presenting a "***justiciable***" claim. While not required to show Constitutional Standing like private litigants, State Attorneys General face different doctrines when suing for their states — "***ripeness***" or "***justiciability***." "A claim is not ripe for adjudication if it rests upon contingent events that may not occur as anticipated or indeed may not occur at all ... [it is] too

speculative whether the problem Texas presents will ever need solving." *Texas v. United States*, 523 U.S. 296, 300, 302 (1998).[25]

What ***actual*** damage — what current "***justiciable***" damage claim ***"ripe"*** for adjudication has the Commonwealth suffered? It has not yet been called upon to pay anything to KRS or any KRS member or anyone else based on its inviolable contract obligations. While the Commonwealth has made financial contributions into KRS – those contributions (even if mismanaged or wasted by the Trustees) ***were required by law, were known to be inadequate and contributed to KRS's financial downfall***. How those legally deficient payments (which impaired KRS's finances and induced the risky Black Box investments that pushed KRS over the edge) damaged the Commonwealth remains to be determined.

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[25] *See also, e.g., Connecticut v. Duncan*, 612 F.3d 107, 112 (2d Cir. 2010) ("Ripeness is a justiciability doctrine [to avoid] premature adjudication."); *Alabama v. Ctrs. for Medicare & Medicaid Servs.*, 674 F.3d 1241, 1245 (11th Cir. 2012) (state claim dismissed as unripe — where ruling on merits would be required "contingent future events that may or may not occur as anticipated or indeed may not occur at all."); *South Carolina v. United States*, 912 F.3d 720, 730 (4th Cir. 2019) (like standing, the ripeness doctrine originates in the case or controversy constraint of Article III ... [a]nalyzing ripeness is similar to determining whether a party has standing."); *Utah v. U.S. Dep't of Interior*, 210 F.3d 1193, 1195-96 (10th Cir. 2000) ("[T]his suit is nonjusticiable both because the state lacks standing to bring this case and because the issue is not yet ripe for adjudication."; State of Utah will suffer no significant hardship because the state can do no more than presently allege that if the lease is approved and the facility developed, it may detrimentally impact the environment. The State's claimed harms are contingent, not certain or immediate"); *Texas v. United States*, 134 Fed. Cl. 8, 17 (Fed. Ct. Cl. 2017) ("Ripeness is a doctrine of justiciability ... a claim is not ripe ... when it is contingent upon future events that may or may not occur"... "if a claim is not yet ripe ... it should generally be dismissed without prejudice."); *South Dakota v. Mineta*, 278 F. Supp. 2d 1025, 1028-29 (2003) ("[R]ipeness combines the constitutional and the prudential" ... ripeness is peculiarly a question of timing and is governed by the situation at the time of review, rather than the situation at the time of the events."); *Wyoming v. Hoffman*, 423 F. Supp. 450 (D. Wy. 1976) ("No injury has occurred. The officials only support a problematic injury to the State of Wyoming.").

There is no doubt that the Commonwealth is facing the prospect of huge damages ***in the future*** if some of KRS's funds fail and it cannot honor those of its pension obligations subject to inviolable contract protection. ***But this has not happened yet***. It may never happen if the Tier 3s are permitted to intervene, carry on the ***meritorious claims pleaded by the*** **Mayberry** ***Plaintiffs*** and effectuate a large enough recovery for KRS to restore it to financial sustainability.[26]

Concurrent pursuit of past "hard" damages and future "soft" damages by common representation creates a disabling conflict. The Supreme Court in *Amchem Products* noted "these factual differences" translate into "significant legal differences" and mandated that claims of current damage and future damage claimants, which ***are fundamentally different***, ***require separate representation to insure adequate representation***. *See* 521 U.S. at 609. The conflict in *Amchem* which prevented single representation of the currently injured victims and those with likely future injuries was – as is the case here — "for the currently injured [*i.e.* KRS] the critical goal is generous immediate payments" while the future injury plaintiffs [*i.e.* Commonwealth] wants a "fund for the future." *See id.* at 626. That reasoning compels that the Tier 3 Plaintiffs be permitted intervention to assure separate ***adequate*** representation of their own, KRS's members and KRS's interests.

[26] This Court seemed to recognize the inherently contingent nature of the Commonwealth's damages claims, stating the Commonwealth "***will*** simply have to come up with the money to fund those benefits" ***if KRS fails*** and such failure "***would*** inflict serious injury on the state government," which potentially "the taxpayers of the Commonwealth ***will be*** obligated to indemnify." Dec. 28, 2020 Order at 15–16.

Whether or not the Commonwealth suffered any "ripe" damages, it still faces the serious and unavoidable factual issue of just whose fault it is that KRS has been so badly damaged? The Defendants have argued and will continue to argue, that the primary reason KRS failed was not their misdeeds but rather that the State for many years ***deliberately underfunded KRS despite formal requests for more funds, pleas for the Commonwealth to comply with its legal obligations and protests that what they were doing was endangering the financial future of the funds***.[27] Is the Commonwealth itself responsible for – at least in substantial part – the financial collapse of KRS because its legislative and executive departments deliberately underfunded KRS by hundreds of millions of dollars in violation of state law? The facts are not going to be in dispute.

> "For many years, Kentucky governors and legislators knowingly failed to put enough money in the state pension fund at the Kentucky Retirement Systems." John Cheves, *Top Issues Facing Kentucky Lawmakers in 2013*, LEXINGTON HERALD-LEADER, Jan. 5, 2013.

- **How did we get into such a big mess?**

"For the past 20 years or so, the state did not put in nearly enough money.

[27] The Defendants have been asserting an "it's the State's fault" defense from the outset. *See* RVK Motion to Dismiss ("For 12 out of the last 17 years, the state has appropriated less money than requested by the Board of Trustees to adequately fund the annual required contribution."). KKR's counsel argued "It[']s been under-funded for twelve [of] the last 17 years quoting state officials" — "We should own up to the fact that we've underfunded KRS for 12 years."

> For most plans over that time, governors did not propose, and the legislature did not appropriate, as much into the plans as was needed. These governors and legislatures were frequently struggling to fund schools and other needs ...."
>
> "Also, in the 1990s when the pension plans were fully funded, the General Assembly approved benefit increases without funding them — including an expensive cost of living benefit increase for Kentucky Retirement System members in place between 1996 and 2012." Tom Loftus, *Kentucky Pension Crisis: How did we get into such a big mess?*, COURIER JOURNAL, Aug. 29, 2017.

- "**How did this happen?**

> "It has been widely reported that the failure of the Governor and General Assembly to adequately fund the full employer's contribution to the pension systems contributed to the underfunding crisis." Kentucky Chamber of Commerce, 2015–2016.

These under-funding problems persist. John Cheves, *Beshear's Budget Would Mean Tens of Millions Less than Expected for KY Pension Funds*, LEXINGTON HERALD-LEADER, Jan. 31, 2020. The Commonwealth simply refuses to adequately fund KRS, using it as a "piggybank" to fund other political priorities.

One could (and Defendants certainly will) argue that the Commonwealth's elected officials benefitted, at least for their own political purposes, when they

diverted funds due to KRS and failed to make the legally required annual contributions to fund other priorities they favored, while denying KRS the funds it needed, and which had they been paid in a timely manner would arguably have avoided KRS's current situation. To those who advance this narrative the state is like a selfish parent that starves its child to near death and then sues the doctors who failed to save it with a long-shot "speculative" treatment. Skillful trial lawyers that they are, defense counsel will not let these facts go unexploited.

Based on this factual reality the Defendants will assert that the Commonwealth is subject ***to unique causation and*** **in pari delicto** ***defenses***. In *Sandoz*, 405 S.W.3d 506, the court overruled two jury verdicts and ***took away*** a multi-hundred-million-dollar recovery for the Commonwealth (which included punitive damages) in a suit brought by the OAG against drug companies who ***conspired*** to cheat and lie about drug prices ("AWP") to obtain and profit from higher reimbursements from state programs. However, the miscreant drug companies proved state officials' "***knowledge that [the drug prices] were inflated***" and the Court of Appeals said this was "***the real crux of this case,***" concluding (*id*. at 511–12):

> States across the nation were aware that pharmaceutical companies were reporting bloated AWPs. Further, ***the Commonwealth itself commissioned a private study of AWP and discovered that AWP was significantly inflated*** .... ***Despite this information, the Commonwealth chose not to implement the suggested reimbursement reductions*** .... ***Clearly, the Commonwealth was aware that AWPs were not the actual prices paid for generic drugs. In light of this fact, it is wholly untenable for the Commonwealth to now claim millions of dollars in compensatory damages for harm***

> ***caused by the false or fraudulent reporting of AWPs to price publishers***.
>
> ***Because the Commonwealth was fully aware of the practices in the industry with respect to AWP, there can be no causation of damages. Frankly, it is appalling that the Commonwealth had actual knowledge of this "shell game" method of pricing employed by the drug companies, the wholesalers, and the pharmacists. However, even more appalling is the fact that, in spite of that knowledge, it acquiesced, billed accordingly, and now seeks reimbursement by way of compensatory and punitive damages***.
>
> ***The Commonwealth was entirely complicit*** in this system of pricing ... basic equitable principles also prohibit the Commonwealth from recovering. In situations such as the present one, where a party's actions are *in pari delicto* with the tortfeasor, recovery is barred by the principles of equity. ... Here, the Commonwealth's actions were *in pari delicto* with the drug companies and other players in the Medicaid reimbursement scheme — a scheme in which the Commonwealth systematically participated by submitting those same figures to the federal government as true and accurate.

Given this opinion, the Defendants will pursue the causation and *in pari delicto* defenses *Sandoz* recognizes because of the State's knowledge and deliberate underfunding of KRS and diverting funds due KRS to the other priorities they favored. ***These defenses are especially dangerous since the Commonwealth's claims are being asserted directly by the OAG for the Commonwealth and not derivatively by innocent taxpayers as the Plaintiffs attempted***.

We must briefly digress into the intricacies of derivative actions to explore the issue of "***imputation***." Derivative litigation exists because of the need to protect the rights of legal entities and their innocent members/shareholders damaged by fiduciary misconduct by insiders and third parties who assist them. The entity cannot sue directly as the conduct and knowledge of the entity's

governing officials — Trustees/Officers — are imputed to the entity under agency principles and bar its claims against third parties, who were aiding and abetting the insiders' misconduct, conspiring with and/or pursuing a common enterprise with them. By permitting innocent stockholders/members to assert the claims ***derivatively*** — independently from the wrongdoers who control or influence the derivative entity and were participants in the wrongdoing — the derivative plaintiffs avoid ***imputation*** and any *in pari delicto* defense. ***Kentucky follows the non-imputation doctrine***. *See Wilson v. Paine*, 288 S.W.3d 284 (Ky. 2009). In *Wilson*, the Supreme Court denied imputation of the knowledge of corporate insiders to time-bar a corporate claim asserted "derivatively" on behalf of the insolvent entity, the bankruptcy trustee (*see id.* at 287–88):

> The doctrine of adverse domination has not heretofore been considered by this Court, but has been widely applied by federal courts in cases involving corporate causes of action against directors and officers.
>
> The doctrine is rooted in the long-established principles of agency law. Adverse domination is premised on the notion that knowledge is not imputed if the agent is acting in a manner adverse to the interests of the principal. This rule is consistent with Kentucky agency law. ... Thus, "[t]he knowledge of the agent is the knowledge of the corporation he serves when the knowledge relates to some matter over which the agent has control and with which his duties are connected and when they relate to matters over which he has authority ...." … In the corporate context, the corporation is the principal and the board of directors as a whole is the agent. ***When the board of directors is accused of breaching its duty to the corporation, it necessarily is accused of acting adversely to the principal's interests***.

The non-imputation doctrine bars wrongdoing corporate Directors/Trustees and those who aid and abet or conspire with or pursue a common enterprise with them from using the complicit acts and knowledge of the

Trustees or Directors to defeat claims asserted in a ***representative manner***, ***i.e.***, ***derivatively***, via an *in pari delicto* defense or otherwise. While an *in pari delicto* defense for third-party service providers to ***for-profit*** corporations is recognized in a minority of jurisdictions when they are only accused of negligence, *i.e.*, malpractice, ***nowhere is the defense available to fiduciaries or to third-party active wrongdoers who aided and abetted***, ***conspired with or pursued a common enterprise with the Trustees***. *See* ***Stewart v. Wilmington Trust***, 112 A.3d 271, 319 (Del. Ch. 2015) ("Delaware law ***sets aside*** **in pari delicto** ***when a receivership trustee or derivative plaintiff*** seeks to sue the corporation's fiduciaries for breach of their fiduciary duties"; therefore, "claims against [banks and auditors] for aiding and abetting breaches of fiduciary duty" are not barred by *in pari delicto*.), *aff'd* 126 A.3d 1115 (Del. 2015); ***Am. Int'l Grp., Inc. v. Greenberg***, 965 A.2d 763, 828 n.246 (Del. Ch. 2009), *aff'd* 11 A.3d 228 (Del. 2011) ("[A]lthough the behavior of faithless fiduciaries is imputed to the corporation when the corporation faces liability to innocent third-parties ... [,] [***t***]***his of course, has never prevented the corporation*** [***itself***] ***from recovering against those faithless fiduciaries in a derivative suit***"); ***Official Comm. of Unsecured Creditors v. Pricewaterhousecoopers, LLP***, 989 A.2d 313 (Pa. 2010) (Misconduct of insiders not imputed to corporation; *in pari delicto* defense not available if third party acts in bad faith); ***NCP Litig. Trust v. KPMG, LLP***, 187 N.J. 353 (2006) (same, even if third party is only negligent); ***FDIC v. O'Melveny & Myers***, 61 F.3d 17 (9th Cir. 1995) (same); ***Merrimack Coll. v. KPMG LLP***, 480 Mass. 614 (2018) (same, with widespread

and informative discussion of imputation). ***Imputation will not apply to KRS's claims, so long as they are asserted derivatively***.[28]

Unlike these authorities protecting the innocent corporate/trust victim and its shareholders/members from imputation of their disloyal fiduciary's knowledge or misdeeds ***where the claims are asserted derivatively or in a representative capacity, like it or not***, Kentucky law appears to permit the assertion of the *in para delicto* defense, ***even where the defendants were intentional wrongdoers***, at ***least where the claim is asserted directly by the Commonwealth and not derivatively for it by innocent taxpayers***, as the *Mayberry* Plaintiffs tried to do until they were blocked by the Supreme Court.

Fortunately for the claims asserted by the Tier 3 Plaintiffs on behalf of KRS, the State's underfunding was but one factor contributing to the damage to KRS resulting in its financial collapse. The Hedge Fund Sellers' and KRS Advisors' breaches of their ***direct fiduciary duties and their active misconduct were key causes as well***. "***But the greater the funding gap the more the state [fund] became a mark for Wall Street's more aggressive sharks***." Gary Rivlin, *How a Gang of Hedge Funders Strip-Mined Kentucky's*

[28] *In pari delicto* is inapplicable to KRS's claims for other reasons as well. KRS is a non-profit entity whose members, unlike equity shareholders, do not "benefit" from the fraudulent behavior of the for-profit corporate board. Also, because the Tier 3 Complaint successfully alleges ***direct breach of fiduciary duty claims against the Advisors and Hedge Fund Sellers***, those "fiduciary" Defendants cannot assert an *in pari delicto* defense. *In pari delicto* is a harsh defense shielding wrongdoers and is subject to policy considerations that sharply limit its use. Unfortunately, the policy considerations do not appear to protect the Commonwealth under *Sandoz*.

Public Pensions, THE INTERCEPT, Oct. 21, 2018. Because breach of fiduciary duty is the equivalent of fraud and given Kentucky's liberal damages rules, the Tier 3 Plaintiffs should be able to recover ***all the damage the defendants' combined misconduct — as they acted jointly — that was a substantial factor in causing harm to KRS***. The Tier 3 Plaintiffs certainly intend to try. *Steelvest, Inc. v. Scansteel Serv. Ctr., Inc.*, 807 S.W.2d 476 (Ky. 1991).[29]

3. The Public Interest and Public Appearances Will Benefit from Separate Representation of KRS's and the Commonwealth's Claims

In inviting the OAG's intervention to prosecute the Commonwealth/taxpayer claims, the Supreme Court in *Overstreet* alluded favorably to the fee limits which would apply to outside counsel hired by the OAG (*i.e.* $125 per hour for partners, $100 per hour for associates). *See Overstreet*, 603 S.W.3d at 265–66; *see also* KRS §§ 15.100(3), 45A.700(1). If the OAG does retain outside counsel at such parsimonious rates they will face a phalanx of the best lawyers available, from Kentucky to Wall Street with ***unlimited litigation budgets*** – charging (in the case of Paul Weiss, *e.g.*, Blackstone's counsel) average partner and associate rates ***of $1,400 and $860 per hour respectively***. However appealing the unrealistic fee limits imposed on the AG might be to some whether the OAG can find and retain high-powered, experienced, complex-case

[29] While Kentucky's apportionment statute restricts joint and several liability for tort cases, due to the non-profit nature of KRS, the deliberate nature of the third parties' wrongdoing, non-tort theories of recovery and public policy considerations, the Tier 3 Plaintiffs believe statutory appointment will not be required as to the KRS claims. But even if it is, they believe proper prosecution of the claims would result in the vast bulk of KRS's damages being attributed to the Advisors and Hedge Fund Sellers.

plaintiffs' counsel under such terms, willing to fund the millions of dollars of costs necessary to vigorously pursue a no-holds-barred prosecution remains to be seen.

By contrast the Tier 3 Plaintiffs' counsel operates under ***no such restrictions***. They have been retained on a contingency percentage of recovery basis providing a powerful free-market incentive to fund and relentlessly pursue the largest possible recovery no matter what. In ***reliance*** upon these contractual fee provisions, counsel have carried on for three full years so far the vigorous prosecution of the derivative claims, ***which appears to have saved both the OAG's claims for the Commonwealth and the KRS claims*** — assuming intervention is granted. The Tier 3 Plaintiffs' counsel are well-funded and experienced — having litigated against, and obtained multi-billion-dollar recoveries from, Wall Street banks (represented by the same Wall Street lawyers who represent them here). Due to preliminary discovery, they already know a great deal about what went on inside KRS as this fiasco unfolded over the past decade and everything about how this case has unfolded to date — a Herculean learning curve for newcomers to climb (not to mention the initial several-months-long initial investigation that formed that basis of the original complaint in this matter). They also have retained accounting, pension fund, financial and fiduciary experts who have done substantial work. They have prepared extensive discovery to serve on KRS, its Trustees and Officers, the Defendants and third parties, as soon as the state of the case permits. They are committed to continue, as demonstrated by their pursuit of these claims to date, and ready to go forward ***now***.

The Tier 3 Plaintiffs have offered to the OAG their willingness for their counsel to work with the OAG, share their experience, expertise, financial

resources, and work over the past three years — and to co-prosecute the case[30] ***so long as the KRS claims and the Commonwealth's claims are kept separate, KRS's recovery goes to KRS and the Commonwealth's recovery goes to the State general fund. No response to the offer was received. In the absence of co-prosecution of the claims, they will have to go forward separately and, inevitably in conflict.***

If the Court wants to be certain the KRS claims are prosecuted on the merits — as the public interest and equity demand — the Tier 3 Plaintiffs should be permitted to intervene to represent the KRS claims derivatively and, if the OAG is willing co-prosecute those claims alongside to assure the level of prosecution of the overlapping, but conflicting, KRS and Commonwealth/taxpayers claims necessary to assure the largest overall recovery to be divided per mutual agreement or, if needed, by Court order.

This case is high-profile, with many eyes on it. The presence of the Tier 3 Plaintiffs and their counsel in prosecuting these overlapping, but conflicting, claims will also provide an assurance of a no-holds-barred prosecution of the case without any fear of political influence. Given the corruption that has infested KRS (and the Commonwealth as a whole that some claim) for many years, the process and result here must also be respected as honest and above-board. Not only must vigorous prosecution of the KRS claims be assured, the appearance of impropriety must be guarded against. Some of the wealthy defendants are among the largest donors to Republican causes and candidates in the country. Defendant Stephen A.

[30] Stephanie Bernstein, *Public-Private Co-Enforcement Litig.*, UNIV. OF FLA. LAW SCHOLARSHIP REPOSITORY, Dec. 2019.

Schwarzman in particular has donated tens of millions of dollars during the 2019-20 cycle, including at least $35 million to the McConnell-related Senate Leadership Fund, and very possibly to "dark money" groups. The *Lexington Herald-Leader* reported on May 6, 2019:

> An independent "dark money" group from Washington reports spending $350,000 to influence the May 21 Republican primary in Kentucky's attorney general race — more money than either candidate has in his own campaign.
>
> The Judicial Crisis Network is promoting Daniel Cameron, former legal counsel to U.S. Senate Republican Leader Mitch McConnell of Kentucky, in his contest against state Sen. Wil Schroder of Wilder.

John Cheves, *'Dark Money' Group Spending Big for McConnell Protégé in KY Attorney General Primary*, LEXINGTON HERALD-LEADER, May 6, 2019.

We do not at this point know whether Mr. Schwarzman or any of the other defendants were involved, and we make no such accusation other than to note the possibility of a conflict, or the appearance of a conflict, of a political nature in the event of settlement or dismissal of claims by the OAG — a problem that would be ameliorated, if not entirely avoided, through the intervention of the Tier 3 Plaintiffs to assure vigorous, unaffected co-prosecution of these claims.

IV. CONCLUSION

Because the OAG's damages claim for the Commonwealth may not be "ripe" or "justiciable" and faces unique causation and *in pari delicto* defenses, the Tier 3s may well be the "last ones standing" – the only ones with Constitutional Standing, ripe and justiciable claims for past "hard" damages for KRS and its funds by pursuing "plan wide conduct" and obtaining "plan wide relief" – to make KRS whole and protect their pension entitlements and cash contributions to the KRS

Plans. Ironically, the intervention of the Tier 3 Plaintiffs may "save" the Commonwealth's claims. The wrong that must not go un-remedied is the ***financial damage to KRS***, ***which has already occurred*** — as opposed to the Commonwealth's damages, which Defendants will argue are unripe, speculative and contingent on future events, barred by causation and *in pari delicto* defenses. If the Tier 3s are successful, the Commonwealth may never have to honor its inviolable contract obligation above and beyond its normal contributions.

For the reasons set forth above, in the Complaint and in Exhibits A and B, the Tier 3 Plaintiffs respectfully urge the Court to grant their motion to intervene, order the Complaint filed, direct the defendants to respond in 20 days and order discovery ***to proceed immediately***.

Dated: February 1, 2021

Respectfully submitted,

s/ Michelle Ciccarelli Lerach

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EXHIBIT A

EXHIBIT A

COMMONWEALTH OF KENTUCKY
SUPREME COURT
CASE NO. 2019-SC-232

JEFFERY C. MAYBERRY, ET AL.		APPELLANTS
v.	On Appeal from the Kentucky Court of Appeals Case Nos. 2019-CA-000043-OA and 2019-CA-000079-OA (consolidated)	
HON. PHILLIP J. SHEPHERD, JUDGE, FRANKLIN CIRCUIT COURT		APPELLEE
and		
PRISMA CAPITAL PARTNERS, ET AL.		APPELLEES/ REAL PARTIES IN INTEREST

BRIEF ON BEHALF OF *AMICUS CURIAE* OF KENTUCKY SENATE PRESIDENT ROBERT STIVERS, KENTUCKY SENATE MINORITY LEADER MORGAN MCGARVEY, KENTUCKY HOUSE SPEAKER DAVID OSBORNE, AND KENTUCKY HOUSE MINORITY LEADER ROCKY ADKINS FOR APPELLANTS

CERTIFICATE OF SERVICE

My signature below certifies that a true copy of this AMICUS CURIAE BRIEF was served on this 12th day of June, 2019: BY REGULAR U.S. MAIL, postage prepaid, to Clerk of the Franklin Circuit Court, 214 St. Clair Street, P. O. Box 378, Frankfort, Kentucky 40601; Clerk of the Kentucky Court of Appeals, 360 Democrat Drive, Frankfort, Kentucky 40601; and Hon. Phillip J. Shepherd, Franklin Circuit Judge, 48th Judicial Circuit, 214 St. Clair Street, P. O. Box 378, Frankfort, Kentucky 40601; and BY ELECTRONIC SERVICE as specified pursuant to CR 5.02 to the persons further listed below:

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STATEMENT OF POINTS AND AUTHORITIES

STATEMENT OF INTEREST OF *AMICI*

The *amici* are elected leaders of Kentucky's legislative branch of government: Senate President Robert Stivers and Senate Minority Leader Morgan McGarvey; House Speaker David Osborne and House Minority Leader Rocky Adkins. The Commonwealth has a vital interest in ensuring the financial health and viability of its public pension plans; more broadly, the Commonwealth has a vital interest in ensuring that means exist to challenge fiduciary misconduct (and related wrongdoing) involving Kentucky's public pension plans, consistent with the statutory structure that the executive and legislative branches have built. When, as here, the Kentucky Retirement System (KRS) — the Commonwealth's statutorily-designated entity — is unable or unwilling to challenge fiduciary misconduct, KRS's members and beneficiaries must be able to do so on KRS's behalf, consistent with longstanding derivative litigation principles. The Court of Appeals' opinion wrongly thwarts those vital interests, misapplies derivative standing principles, and effectively forecloses challenges to fiduciary misconduct involving KRS. We therefore submit this amicus brief in support of Appellants. We have no individual interest, financial or otherwise, in this litigation.

SUMMARY OF ARGUMENT

It is for the executive and legislative branches to define the scope of any public employee pension plan. Public policy likewise is a legislative judgment. As relevant here, it is for the legislature to allow KRS's members and beneficiaries to challenge fiduciary breaches through derivative lawsuits *on KRS's behalf* when KRS cannot do so itself. The legislature has expressly allowed derivative suits challenging trustees' fiduciary breaches. And it has implicitly allowed derivative suits with respect to others' fiduciary breaches by (1) imposing strict fiduciary standards on officers, employees and others, and (2) passing and repeatedly amending legislation

creating statutes many decades after (and with presumed knowledge that) courts allowed derivative lawsuits as an equitable vehicle to prevent wrongdoing — all without seeking to rein in or alter those common law rules.

This Court — like courts around the nation — has long allowed derivative litigation on behalf of an entity when that entity cannot, or will not, challenge wrongdoing on its own. For purposes of standing, the derivative plaintiff must show injury to the entity — the "true plaintiff," — not individual injury. That is the lesson of *Commonwealth, Cabinet for Health & Family Services v. Sexton*, 566 S.W.3d 185 (Ky. 2018).

The court of appeals misapplied *Sexton*, requiring the Appellants here to show individual injury in order to have standing. Derivative plaintiffs almost never suffer individual injury, nor need they show that injury, because the very nature of derivative litigation is to remedy injury to the entity they represent. Moreover, the appeals court's decision ignores and contradicts the legislative judgments contained in the statutes creating and regulating KRS, ignores KRS's statement in the record that it cannot pursue the litigation that Appellants have undertaken on its behalf, and threatens to create mischief for all future corporate and derivative litigation.

ARGUMENT

I. THE EXECUTIVE AND LEGISLATIVE BRANCHES ENVISIONED ALLOWING KRS'S MEMBERS AND BENEFICIARIES TO CHALLENGE FIDUCIARY BREACHES.

It is for the executive and legislative branches of government — the legislature (by enacting laws) and the executive (by signing and enforcing laws) — to decide whether and how to provide a public pension plan for state and local workers. Section 27 of the Constitution of Kentucky creates three distinct branches of government, and Section 28 precludes one branch from exercising any power belonging to the other branches. Under that constitutional separation

of powers, this Court has "recognize[d] that the legislature makes the laws." *Jones v. Commonwealth*, 319 S.W.3d 295, 299 (Ky. 2010) (brackets added). Public policy likewise is a legislative judgment to be gleaned from the legislature's actions. *See Nelson Steel Corp. v. McDaniel*, 898 S.W.2d 66, 68 (Ky. 1995) ("The public policy must be evidenced by a constitutional or statutory provision.") (quoting *Brockmeyer v. Dun & Bradstreet*, 335 N.W.2d 834, 840 (Wisc. 1983)); *Pyles v. Russell*, 36 S.W.3d 365, 368 (Ky. 2000) ("The enunciation of public policy is the domain of the General Assembly."); *Schork v. Huber*, 648 S.W.2d 861, 863 (Ky. 1983) (same); *Fann v. McGuffey*, 534 S.W.2d 770, 779 (1975) ("the legislative branch of government has the prerogative of declaring public policy").

A. The Statutory Scheme Expressly Permits Beneficiaries to Challenge Fiduciary Breaches in a Derivative Action.

KRS 61.645(15)(e)-(f) expressly allows people to sue to recover "damages suffered by [KRS]" if they can prove by clear and convincing evidence that trustees breached their duties of office by reckless or willful misconduct.

Kentucky's legislature requires KRS's trustees to perform their duties "[i]n good faith, KRS 61.645(15)(a)(1), "[o]n an informed basis," KRS 61.645(15)(a)(2), and "in a manner [that they] honestly believe[e] to be in the best interest of" KRS. KRS 61.645(15)(a)(3) (all brackets added).

The statutory scheme — consistent with longstanding equitable principles, *see* § I.B — then recognizes (and partially alters) derivative claims against trustees for breaches of that duty. KRS 61.645(15)(e) specifically provides when those claims against trustees will fail:

> (e) Any action taken as a trustee, or any failure to take any action as a trustee, shall not be the basis for monetary damages or injunctive relief unless:
>
> 1. The trustee has breached or failed to perform the duties of the trustee's office in compliance with this section; and

> 2. In the case of an action for monetary damages, the breach or failure to perform constitutes willful misconduct or wanton or reckless disregard for human rights, safety, or property.

In other words — converting the textual negative to a positive, — a trustee's actions or inactions *may* warrant relief if the trustee breached or failed to perform statutory duties, and *may* warrant monetary damages if the trustee's breach constituted willful misconduct, or wanton or reckless disregard.

Having thus described trustees' duties, and the standard for imposing liability for their breach, the legislature provided for derivative actions as follows:

> A person[1] bringing an action for monetary damages under this section shall have the burden of proving by clear and convincing evidence the provisions of paragraph (e)1. and 2. of this subsection, and the burden of proving that the breach or failure to perform was the legal cause of damages suffered *by the Kentucky Retirement Systems.*

KRS 61.645(15)(f) (emphasis added). That statutory section clearly creates a right of action, otherwise the provisions governing "an action ... under this section" would be meaningless. *See Brooks v. Meyers,* 279 S.W.2d 764, 766-67 (Ky. 1955) ("a [s]tatute should be construed, if possible," to give effect and meaning to each part of it); *see also Hardin County Fiscal Court v. Hardin County Board of Health,* 899 S.W.2d 859, 861-62 (Ky. App. 1995) (same).

Nor can there be any question that this statutory section provides for derivative litigation: the recovery is for "damages *suffered by the Kentucky Retirement Systems.*" *See* KRS 61.645(15)(f) (emphasis added). This then is a recovery *for* KRS brought by someone *other than those in control,* which is the very definition of a derivative action. *See Ross v. Bernhard,* 396 U.S. 531, 534 (1970) ("The remedy made available in equity was the derivative suit, viewed in

[1] For purposes of KRS 61.150-61.705, the term "person" is defined as "a natural person." KRS 61.510(30). KRS thus is not a "person" for purposes of KRS 61.645(15)(f), meaning that only individuals ("natural persons") may bring an action for monetary damages "suffered by [KRS]" under that section.

this country as a suit to enforce a *corporate* cause of action against officers, directors, and third parties.") (emphasis in original); *see also* Thomas E. Rutledge, *Who Will Watch the Watchers?: Derivative Actions in Nonprofit Corporations* [*Watch the Watchers*], 103 KY. L. J. ONLINE 31 (2014–15).

While KRS 61.645 *provides* for derivative actions, it does not *create* them, as detailed in § I.B. *See also Watch the Watchers*, 103 KY. L. J. ONLINE at 31 n.5 ("The first Kentucky statute recognizing the right to bring some form of derivative action was not adopted until 1946, significantly subsequent to the first appearance of the 'derivative action' in Kentucky law."). Rather, Kentucky statutes providing explicitly for derivative actions either codify or supplement the common law, as described in § I.B. That common law has long allowed derivative actions alleging breach of fiduciary duties.[2] Consistent with that common law, KRS 61.650(1)(c) imposes strict fiduciary duties on any KRS "trustee, officer, employee, or other fiduciary." KRS 61.645(15)(e) and (f) then modify the standards for obtaining monetary damages from trustees, while leaving intact common law derivative action standards and remedies against all others.[3] *See Watch the Watchers*, 103 KY. L. J. ONLINE at 32 ("equity will provide the rules applicable when the organizational statute does not specify the rules governing derivative actions").

B. Legislation Enacted in the Face of Longstanding Legal Principles Allowing for Representative Lawsuits Implicitly Codifies Those Principles.

As the Appellants have argued [App. Br. at 25-29], Kentucky's courts have long recognized representative or derivative standing. Over a century ago, this Court described the

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[2] The Appellants' First Amended Complaint fully alleged how each defendant had fiduciary duties to KRS and its members, and the trial court properly — for CR 12.02(b) purposes — deemed those allegations true.

[3] While the statute is silent about why it modifies derivate action standards for trustees, but not for other fiduciaries, it might simply recognize the need to induce people to serve as unpaid volunteers. Those volunteering to serve as trustees are assured that they bear no personal financial risk from fiduciary breaches absent "willful misconduct or wanton or reckless disregard ..." KRS 61.545(15)(e)(2).

doctrine's provenance: "exceptions to the general rule that the acts of the directors are the acts of the corporation, and cannot be interfered with by the courts at the complaint of stockholders" are "as well established perhaps as the rule itself." *Pittsburg, C., C. & St. L. Ry. Co. v. Dodd*, 72 S.W. 822, 827 (1903). Equity allows courts to permit minority shareholders' suits seeking to hold corporate directors accountable for wrongdoing. *Id.* Were it not for derivative litigation, stakeholders would have no means to prevent directors and majority stakeholders from committing wrongs. *See id.* at 828 (rejecting alternatives that would effectively "turn over to a possible wrongdoer the adjudication of his own case").[4] And, as one commentator has noted, Kentucky's courts have recognized the doctrine (even if not by name) for nearly 150 years. *See Watch the Watchers*, 103 KY. L. J. ONLINE at 35-37 (citing *Jones v. Johnson*, 73 Ky. (10 Bush) 649, 660 (Ky. 1874), *Collier v. Deering Camp Ground Ass'n,* 66 S.W. 183, 183 (Ky. 1902), *Dodd*, 72 S.W. 822, and *Reinecke v. Bailey*, 112 S.W. 569, 570 (Ky. 1908)).

The derivative action — initially a court-created equitable action — thus affords standing to an entity's members who have not been individually injured, even though the entity as a whole has been. *See, generally, Watch the Watchers*, 103 KY. L. J. ONLINE 31. The entity's members may sue on the entity's behalf, thereby holding those in charge accountable for breaches of their fiduciary duties. *See Barrett v. S. Conn. Gas Co.*, 374 A.2d 1051, 1055 (Conn. 1977) ("If the duties of care and loyalty which directors owe to their corporations could be enforced only in suits by the corporation, many wrongs done by directors would never be remedied."); *Ross v. Bernhard*, 396 U.S. 531, 534 (1970) ("The remedy made available in equity was the derivative

[4] Nor must a derivative plaintiff bring individual claims along with the derivative claim (although Dodd did). *See Sahni v. Hock*, 369 S.W.3d 39, 47 (Ky. Ct. App. 2010), *abrogated on other grounds*, 436 S.W.3d 189 (Ky. 2013) (dismissing individual claims because alleged injury was mere diminution in stock value (which is an injury derivative of the corporation's injury), but allowing derivative claims on the corporation's behalf). Simply put, individual injury is not required for, nor an element of, a derivative claim. Derivative actions exist because — regardless of individual injury — the individual has a real stake in protecting the interest of the business entity. *Watch the Watchers*, 103 KY. L. J. ONLINE at 38-39.

suit, viewed in this country as a suit to enforce a *corporate* cause of action against officers, directors, and third parties.") (emphasis in original).

As discussed above, Kentucky's courts had allowed derivative lawsuits for more than fifty years before KRS's creation, and more than one hundred years since the latest statutory amendments. *See Pittsburg, C., C. & St. L. Ry. Co. v. Dodd*, 72 S.W. 822, 827 (1903). Had the legislature intended to bar KRS members and beneficiaries from filing derivative lawsuits alleging wrongdoing by those in charge of KRS, it presumably "would have so specified in language explicitly ..." *McDaniel*, 898 S.W.2d at 69. It did no such thing. On the contrary, it explicitly provided *for* derivative lawsuits against trustees. *See* § I.A (citing KRS 61.645(15)(e) and (f)). And it imposed strict fiduciary duties upon any KRS "trustee, officer, employee, or other fiduciary," knowing that the common law allowed derivative actions for breach of those fiduciary duties. KRS 61.650(1)(c).

A legislature is presumed to act with knowledge of existing judicial decisions, and the laws it passes are presumed to be in harmony with those decisions unless the legislature provides to the contrary. The legislature created KRS more than sixty years ago, *see* 1956 Ky. Acts, ch. 110, sec. 28, and has amended the governing statute dozens of times.[5] At no time has it sought

[5] *See* 2017 Ky. Acts ch. 12, sec. 3, effective March 10, 2017; 2013 Ky. Acts ch. 120, sec. 65, effective July 1, 2013; 2012 Ky. Acts ch. 75, sec. 8, effective April 11, 2012; 2010 Ky. Acts ch. 127, sec. 1, effective July 15, 2010; 2009 Ky. Acts ch. 77, sec. 19, effective June 25, 2009; 2008 (1st Extra. Sess.) Ky. Acts ch. 1, sec. 21, effective June 27, 2008; 2004 Ky. Acts ch. 36, sec. 23, effective July 13, 2004; 2003 Ky. Acts ch. 169, sec. 10, effective March 31, 2003; 2002 Ky. Acts ch. 52, sec. 11, effective July 15, 2002; 2000 Ky. Acts ch. 385, sec. 23, effective July 14, 2000; 1998 Ky. Acts ch. 105, sec. 15, effective July 15, 1998; ch. 154, sec. 59, effective July 15, 1998; and ch. 246, sec. 2, effective July 15, 1998; 1996 Ky. Acts ch. 167, sec. 17, effective July 15, 1996; and ch. 318, sec. 29, effective July 15, 1996; 1994 Ky. Acts ch. 406, sec. 3, effective July 15, 1994; and ch. 485, sec. 21, effective July 15, 1994; 1992 Ky. Acts ch. 240, sec. 40, effective July 14, 1992; and ch. 437, sec. 1, effective July 14, 1992; 1990 Ky. Acts ch. 299, sec. 1, effective July 13, 1990; ch. 489, sec. 6, effective July 13, 1990; and ch. 496,sec. 39, effective July 13, 1990; 1988 Ky. Acts ch. 349, sec. 24, effective July 15, 1988; and ch. 351, sec. 3, effective July 15, 1988; 1986 Ky. Acts ch. 90, sec. 20, effective July 15, 1986; 1984 Ky. Acts ch. 232, sec. 2, effective July 13, 1984; 1982 Ky. Acts ch. 448, sec. 65, effective July 15, 1982; 1980 Ky. Acts ch. 186, sec. 13, effective July 15, 1980; and ch. 246, sec. 8, effective July 15, 1980; 1978 Ky. Acts ch. 110, sec. 100, effective January 1, 1979; 1976 Ky. Acts ch. 321, secs. 29 and 40; 1974 Ky. Acts ch. 128, sec. 26; 1972 Ky. Acts ch. 116, sec. 48; 1962 Ky. Acts ch. 58, sec. 19; 1960 Ky. Acts ch. 165, Part II, sec. 14; 1956 (1st Extra. Sess.) Ky. Acts ch. 7, Art. XV, sec. 1.

to constrain or limit derivative or representative claims by KRS members or beneficiaries, except as provided in KRS 61.645(15)(e) and (f) (which, as detailed in § I.A, expressly authorizes derivative actions against trustees without supplanting derivative claims against any others).

McDaniel, 898 S.W.2d 866, provides the guiding principle and applies fully here. *McDaniel* was the fourth in a series of cases developing this Court's "wrongful discharge" jurisprudence. The first three had established a cause of action for wrongful discharge when an employee "was fired for filing or pursuing a worker's compensation claim," but not for fraternizing with a fellow-employee, in purported violation of the right to "freedom of association." *McDaniel*, 898 S.W.2d at 868-69 (characterizing *Pari-Mutual Clerks' Union v. Ky. Jockey Club*, 551 S.W.2d 801 (Ky. 1977), *Firestone Textile Co. Div. v. Meadows*, 666 S.W.2d 730 (Ky. 1983), and *Grzyb v. Evans*, 700 S.W.2d 399 (Ky. 1985)).

McDaniel followed those three cases. There, the employee sought an expansion of *Firestone*, arguing that statutory changes reflected additional "public policy" limits on the at-will employment doctrine. *McDaniel*, 898 S.W.2d at 68-70. This Court disagreed. It found centrally important that the statutory amendments came *after* the *Firestone* decision:

> If the legislative purpose was to expand upon the cause of action as stated in the text of the *Firestone* opinion, we assume the General Assembly would have so specified in language explicitly stating the broader coverage it intended to provide. Presumably the General Assembly was aware of the *Firestone* case and enacted the statute in language intended to codify the decision, not to expand it.

McDaniel, 898 S.W.2d at 69. *See also Tenney v. Brandhove*, 341 U.S. 367, 376 (1951) (holding that federal civil rights statutes did not silently abrogate common law immunities existing at the time of enactment); *Imbler v. Pachtman*, 424 U.S. 409, 418 (1976) ("immunities 'well -grounded in history and reason' had not been abrogated 'by covert inclusion in the general language' of" the applicable statute) (characterizing *Tenney*). Thus, the legislature must be presumed to act

with knowledge of common law derivative actions when it crafted KRS's fiduciary duty statutes.

Analogous principles govern representative lawsuits by a trust's beneficiaries on the trust's behalf.[6] While Kentucky's courts have not reached the issue, the Sixth Circuit, applying Kentucky law in *Osborn v. Griffin*, 865 F.3d 417 (6th Cir. 2017), predicted that this Court would adopt the "correct rule set out in the Restatement of Trusts," permitting a trust beneficiary to bring claims on behalf of the trust when the trustee refuses or neglects to act. *Id.* at 447. *Osborn* is consistent with Kentucky's long history involving derivative actions, consistent with the Restatement of Torts, and consistent with law throughout the nation. *See Tzolis v. Wolff*, 10 N.Y.3d 100 (2008) (noting that derivative lawsuits date back to at least 1832). Courts, using their equitable powers, allow a trust's beneficiary to sue a third party when "the trustee is unable, unavailable, unsuitable, or improperly failing to protect the beneficiary's interest." Restatement (Third) of Trusts (2012), § 107(2)(b). *See Bowen v. United States Postal Service*, 459 U.S. 212, 243 (1983) (recognizing rule); *see also Wolf v. Mitchell, Silberberg & Knupp*, 76 Cal. App. 4th 1030, 1037 (Cal. App. 1999) (same); *City of Dubuque v. Iowa Tr.*, 519 N.W.2d 786, 790 (Iowa 1994) (same); *Garcia v. Suda*, 94 Va. Cir. 246 (Va. Cir. 2016) (same).

Had the legislature intended to bar KRS members, as beneficiaries of the pension fund,[7]

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[6] These Appellants did not seek any individual damages in the trial court; indeed, they disclaimed any individual relief. *See., e.g.*, First Amended Complaint, ¶ 33 (complaint "does not assert any harm to KRS members or beneficiaries individually and it does not seek any relief for them individually"). Rather, the Appellants sued for the benefit of the pension fund in which they are stakeholders. In doing so, they invoked two doctrines: (1) equitable standing applicable to suits brought by equity holders on behalf of business entities (the "derivative action"); and (2) the doctrine that permits trust beneficiaries to sue on behalf of a trust when the trustee fails to act (the "beneficiary action").

[7] KRS is unquestionably a trust. By statute, the funds administered by the KRS Board are "deemed trust funds." KRS 61.515(2) (referring to the Kentucky Employees Retirement Fund); KRS 16.510 (State Police Retirement Fund); KRS 78.520 (County Employees Retirement Fund); 61.701 (insurance trust fund). And the legislature has repeatedly said that the KRS Board "shall be the trustee" of the funds at issue. KRS 61.650 (referring to all four funds); KRS 16.642 (State Police Retirement Fund); KRS 78.790 (County Employees Retirement Fund). The court of appeals' conclusion [Opinion at 18] that KRS is not a trust because it is not governed by the Uniform Trust Act, KRS 386B.1-010, ignores that other statutes — they ones that do apply to KRS — all deem KRS to be a trust.

from filing suit against KRS trustees, it likewise "would have so specified in language explicitly ..." *McDaniel*, 898 S.W.2d at 69. It did no such thing. Rather, it explicitly authorized them to sue the trustees on the trust's behalf. *See* § I.A (citing KRS 61.645(15)(e) and (f)).[8]

II. THE COURT OF APPEALS' DECISION MISAPPLIES STANDING LAW, IGNORES KRS'S EXPRESS AGREEMENT THAT IT CANNOT FILE THIS LAWSUIT, AND UNDERMINES THE EXECUTIVE AND LEGISLATIVE BRANCHES' LEGISLATIVE SCHEME.

Commonwealth, Cabinet for Health & Family Services v. Sexton, 566 S.W.3d 185 (Ky. 2018), adopted formally for Kentucky law the federal test for analyzing constitutional standing.[9] *Id.* at 196 (following *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 560-61 (1992)). *Sexton* held that, in representative litigation, constitutional standing required analysis through the lens of the "true plaintiff" — the person or entity being represented in the lawsuit. This was rooted in Kentucky's constitutional requirement that courts hear only "justiciable causes." Sexton, 566 S.W.3d at 192 (emphasis omitted). Thus, to satisfy constitutional standing in a representative lawsuit, the "true plaintiff" must establish *Lujan*'s three elements: injury, causation, and redressability.

The Court then analyzed whether the true plaintiff — Sexton — had standing, and found that she did not, because she suffered no injury (having received the medical care that she sought, for which the representative plaintiff — the hospital — sought payment). *Id.* at 197 ("We emphasize the crucial determinative fact — because Sexton, not [the hospital], is the true

[8] Allowing members and beneficiaries to file *derivative* lawsuits will not flood the courts with minor disputes about the amount or timing of retirees' benefits. On the contrary, those individual claims are resolved through the normal administrative process. They thus differ fundamentally from a derivative lawsuit filed *on behalf of* KRS — a lawsuit authorized by statute and with a long lineage in the case law. Moreover, by definition, because a derivative lawsuit is filed on behalf of the entity, not the individual, it seeks no individual relief. Nothing in this brief is intended to discuss when, if, or how KRS's members and beneficiaries can assert individual claims.

[9] The Court made clear that it had applied *Lujan* informally in earlier cases.

plaintiff ..., we must examine the standing requirement through the lens of Sexton's, not [the hospital's], purported satisfaction.")

Here, the Court of Appeals got *Sexton* backwards. Rather than assessing whether the true plaintiff (KRS) had standing, it asked whether the representative plaintiffs (the Appellants) had standing.[10] That simply isn't the *Sexton* inquiry. Nor is it consistent with *Sahni*, 369 S.W.3d at 47, which dismissed individual claims for lack of injury, but allowed derivative claims on the corporation's behalf. Simply put, the appeals court either misunderstood *Sexton*, misunderstood the difference between individual and representative claims (and the law governing them), or both. Its decision cannot be permitted to stand, without doing great mischief as detailed in Appellants' brief.

Moreover, KRS agrees that it cannot and will not file this lawsuit, nor engage in the protracted litigation that it requires, despite the case's substantive merit. In its Joint Notice (attached as Ex. 3 to Appellant's Brief), KRS agrees that the Appellants' claims "have merit, ... and ... could have a significant impact on the financial well-being of KRS and its member employees and retirees." [Joint Notice at 2.] Despite that, KRS "will not pursue the claims asserted" ... "would not have been in a position to pursue these claims" had the Appellants brought them to KRS before filing suit, and thus "believes that it is in the best interest of KRS for Named Plaintiffs to continue their pursuit of these claims on a derivative basis on KRS's behalf." [Joint Notice 1-2.]

In other words, by KRS's own admission, it cannot protect its members from its trustees' and others' wrongdoing. If these Appellants, on KRS's behalf, cannot do so, then no one can (and the trustees' and others' wrongdoing will escape free from all scrutiny). But that is

[10] The appeals court relied solely on *Bacigalupo v. Kohlhepp*, 240 S.W.3d 155, 158 (Ky. App. 2007), for its conclusion that the Appellants must have individual standing here. [*See* Opinion at 12-13.] But *Bacigalupo* involved the continuous ownership rule, which has no bearing on this case.

precisely why courts have fashioned, in equity, the derivative lawsuit. *Watch the Watchers*, 103 KY. L.J. ONLINE 31. No one other than these plaintiffs — as beneficiaries of the KRS trust, and derivatively on behalf of KRS's members — can challenge that wrongdoing. The appeals court's decision runs afoul of that underlying equitable notion: derivative claims are a mechanism to prevent a failure of justice, allowing stakeholders (like these Appellants) to assert claims when those in charge (like KRS) cannot or will not do so.

The appeals court's decision also undermines the legislative scheme. As described in § I, the executive and legislative branches are empowered to create, and sculpt the contours of, Kentucky's public pension plans. They have done so, and the legislature — acting within its power to promote and define public policy — has expressly authorized KRS's members and beneficiaries to file suit against wrongdoing by KRS's trustees.[11] And it has implicitly authorized KRS's members to file suit against wrongdoing by other KRS fiduciaries, by expressly imposing strict fiduciary duties on them, and by legislating in the face of, and without altering the content of, longstanding derivative lawsuit principles.

CONCLUSION

For these reasons, and those contained in the Appellants' and *amici*'s briefs, the Court should reverse the decision below, vacate the writ of prohibition, reinstate the trial court's Opinion and Order (denying, in large part, dismissal motions), and allow the trial court to conduct further consistent proceedings.

[11] That statutory provision answers questions about prudential standing. But that grant would be meaningless if, as the court of appeals wrongly held, KRS's beneficiaries who suffered no individual injury lacked constitutional standing to assert derivative claims.

Dated: June 12, 2019

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EXHIBIT B

EXHIBIT B

COMMONWEALTH OF KENTUCKY
SUPREME COURT
CASE NO. 2019-SC-232

PRISMA CAPITAL PARTNERS, ET AL.		PETITIONERS/ APPELLEES
v.	On Appeal from the Kentucky Court of Appeals Case Nos. 2019-CA-000043-OA and 2019-CA-000079-OA (consolidated)	
HON. PHILLIP J. SHEPHERD, JUDGE, FRANKLIN CIRCUIT COURT		RESPONDENT/ APPELLEE
JEFFERY C. MAYBERRY, et al.		REAL PARTIES IN INTEREST/ APPELLANTS

AMICUS CURIAE BRIEF ON BEHALF OF LAW PROFESSORS AND FACULTY SUPPORTING APPELLANTS

CERTIFICATE OF SERVICE

My signature below certifies that a true copy of this AMICUS BRIEF, was served on this 12th day of June, 2019: BY REGULAR U.S. MAIL, postage prepaid, to Clerk of the Franklin Circuit Court, 214 St. Clair Street, P. O. Box 378, Frankfort, Kentucky 40601; Clerk of the Kentucky Court of Appeals, 360 Democrat Drive, Frankfort, Kentucky 40601; and Hon. Phillip J. Shepherd, Franklin Circuit Judge, 48th Judicial Circuit, 214 St. Clair Street, P. O. Box 378, Frankfort, Kentucky 40601; and BY ELECTRONIC SERVICE as specified pursuant to CR 5.02 to the persons further listed below:

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STATEMENT OF POINTS AND AUTHORITIES

I. PURPOSE AND INTEREST OF *AMICUS CURIAE*

We Professors Mary J. Davis, Dennis R. Honabach, Lawrence A. Hamermesh, Jonathon C. Lipson, and Robert B. Thompson, are Professors and faculty members at various Kentucky and other law schools. We respectfully submit this brief as amicus curiae in the appeal of *Prisma Capital Partners, et al. v. Hon. Phillip Shepherd, et al.* This amicus brief sets forth our views regarding the detrimental impact of the Court of Appeals' opinion to the future of derivative litigation in Kentucky. To that extent, we submit this amicus brief in support of Appellants. We have no interest, financial or otherwise, in this litigation.

Amici have considerable familiarity with the history and importance of representative and derivative litigation as a means of remedying wrongs under business organization law. It is black letter law in Kentucky and nationally that in order to institute and maintain a derivative action, a Plaintiff must demonstrate two basic requirements: (1) constitutional standing, *i.e.*, injury, causation, and redressability, on the part of the entity being represented ("Constitutional Standing"); and (2) that the plaintiff had and continues to have, at all times in the litigation, a proper interest in entity she seeks to represent ("Representative Interest"). In its opinion below, the Kentucky Court of Appeals added a third, untenable requirement – that the plaintiff show a personal injury directly to herself in addition to an injury to the represented entity. That third requirement is a fundamental misunderstanding and misapplication of centuries of law on derivative actions.

Constitutional Standing under Kentucky law was closely examined in *Commonwealth Cabinet for Health & Family Services v. Sexton*, 566 S.W.3d 185 (Ky. 2018) . There, this Court formally adopted, after years of Kentucky Courts informally following, the federal *Lujan* test for

analyzing Kentucky constitutional standing, thus requiring a showing of: (1) injury; (2) causation; and (3) redressability.[1] Crucially, *Sexton* held that in representative litigation, constitutional standing must be analyzed from the lens of the "true plaintiff," *i.e.*, the entity being represented in the lawsuit, not the named representative plaintiff. Thus, to satisfy constitutional standing in a derivative lawsuit, the showing of injury required by *Lujan* relates only to the injury of the entity, not any direct injury on the part of the individual, representative plaintiff.

The requirement of a Representative Interest is set forth in *Bacigalupo v. Kohlhepp.*[2] There, the court explained that the plaintiff shareholder in a corporate derivative action must remain a shareholder at all times in the litigation to maintain the lawsuit. The plaintiff in *Bacigalupo* lost his ownership shares during the pending litigation consequent to a merger effective in accordance with Kentucky law. Because the plaintiff no longer had a Representative Interest, the suit was dismissed.

Here, the Court of Appeals confused these two issues, finding that the individual plaintiffs must show not only *Lujan* standing for the entity they represent, but also for themselves. In other words, the Court of Appeals found that the individual plaintiffs must show a personal injury in addition to an injury to the entity they seek to represent. This is likely because of the confusing use of the word "standing" to describe the Representative Interest requirement. *See* Court of Appeals Opinion at 13, *citing Bacigalupo.*[3] Regardless of the reasoning behind the Court of Appeals' mistake, by requiring individual injury on the part of the derivative plaintiffs

[1] *Lujan v. Defs. of Wildlife*, 504 U.S. 555, 560 (1992)

[2] 240 S.W.3d 155 (Ky. App. 2007).

[3] The use of the word "standing" in the context of the Representative Interest requirement is a reference to the notion of "prudential standing," rather than constitutional standing. It is not the function of this brief to examine the tortured history of prudential standing or its place in the current legal framework. Suffice it to say, in the recent *Lexmark Int'l v. Static Control Components, Inc.* case, the U.S. Supreme Court described the term "prudential standing" as "misleading," a "misnomer," an "inapt" label, and a "a doctrine not derived from Article III." 572 U.S. 118, 126-27 & n.3 (2014).

in a derivative action, the Court of Appeals drastically changed Kentucky law in a way that severely limits the availability of representative litigation in Kentucky. Individuals that bring derivative lawsuits typically cannot establish an individual injury and, if they could, they would likely assert their own individual claims rather than bring derivative claims. If representative litigation is no longer viable under Kentucky law, future wrongdoing that injures entities controlled by the wrongdoers will go unchecked and unremedied.

Moreover, the Court of Appeals' ruling pushes Kentucky out of line with the vast majority of jurisdictions that allow representative litigation. This Court should vacate the Court of Appeals' writ of prohibition, preserve the viability of representative litigation in Kentucky, and underscore that in representative litigation, constitutional standing under Kentucky law is analyzed through *only* the lens of the "true plaintiff."

II. ARGUMENT

In the action below, Plaintiffs did not seek any individual damages; they affirmatively disclaimed any individual relief. *See., e.g.*, First Amended Complaint, ¶ 33 (complaint "does not assert any harm to KRS members or beneficiaries individually and it does not seek any relief for them individually"). Plaintiffs brought suit for the benefit of the Kentucky Employee Retirement System pension fund in which they are stakeholders. To do so, Plaintiffs invoked two well-established procedural doctrines. First, Plaintiffs invoked equitable standing principles applicable to derivative cases brought by stakeholders on behalf of business or other entities (most commonly, the shareholder derivative action). Second, Plaintiffs invoked the doctrine that permits trust beneficiaries to bring suit on behalf of a trust when the trustee fails to act. Both procedural doctrines are widely accepted under American and Kentucky jurisprudence.

A. Courts created representative litigation through their equitable powers to hold those in charge of entities accountable for their wrongdoing.

The history of derivative actions is important because it shows that the Court of Appeals' opinion here takes the entire reason derivative actions arose and fundamentally turns it on its head. Derivative actions arose in order to permit individual stakeholders of an organization to pursue a remedy for injury to the organization when those governing the organization cannot or will not pursue such a remedy.[4] In other words, contrary to the logic of the Court of Appeals, derivative actions arose precisely because the individual constituent ***was not personally injured***. In those situations, constituents need the ability to bring suit on behalf of the entity to hold those in control accountable to their fiduciary duties.[5] Courts created derivative standing with their equitable powers to assure that a procedural mechanism existed to police entity leaders that committed wrongdoing to the detriment of the entity.[6] Courts have recognized derivative standing in this country since at least 1832,[7] and it is firmly entrenched in the jurisprudence throughout the country.

Courts also used their equitable powers to create the rule that a beneficiary of a trust can bring suit against a third party when "the trustee is unable, unavailable, unsuitable, or improperly

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[4] *See, e.g.*, Thomas E. Rutledge, *Who Will Watch the Watchers?: Derivative Actions in Nonprofit Corporations*, 103 KY. L. J. ONLINE 31, 33-34 (2014–2015).

[5] *See Barrett v. S. Conn. Gas Co.*, 374 A.2d 1051, 1055 (Conn. 1977) ("If the duties of care and loyalty which directors owe to their corporations could be enforced only in suits by the corporation, many wrongs done by directors would never be remedied.").

[6] *See, e.g.*, *Tzolis v. Wolff*, 884 N.E.2d 1005, 1006 (2008) ("[The derivative action] was not created by statute, but by case law."); *Ross v. Bernhard*, 396 U.S. 531, 534 (1970) ("The remedy made available in equity was the derivative suit, viewed in this country as a suit to enforce a *corporate* cause of action against officers, directors, and third parties.") (emphasis in original).

[7] *Tzolis*, 884 N.E.2d at 1006 (2008) ("[t]he derivative suit has been part of the general corporate law of this state at least since 1832," and that "[i]t was not created by statute, but by case law").

failing to protect the beneficiary's interest."[8] The United States Supreme Court [9] and numerous other jurisdictions also recognize this rule.[10]

Thus, in a derivative action, the representative plaintiff's constitutional standing is derived from that of the entity.[11] "This is so because a representative steps into the shoes of the entity and brings a suit belonging to the entity."[12] Whether the representative herself has suffered injury is irrelevant to determining standing in a derivative action.

B. Kentucky law on representative actions historically mirrors the country's jurisprudence on representative actions.

The history of derivative actions in Kentucky is quite similar to the history of derivative actions across the country. Over a century ago, the then Court of Appeals articulated Kentucky law on derivative standing:

> The first question naturally presented is the right of minority stockholders of a corporation to maintain suit on its behalf. Generally, such a suit cannot be so maintained...*But there are admitted exceptions* to the general rule that the acts of the directors are the acts of the corporation, and cannot be interfered with by the courts at the complaint of stockholders, *which are as well established perhaps as the rule itself.*[13]

The Court stated that it may use its equitable powers to allow a minority shareholder to bring suit and hold the directors of a corporation accountable for wrongdoing.[14] Absent derivative

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[8] See RESTATEMENT (THIRD) OF TRUSTS § 107(2)(b) (AM. LAW INST. 2012). This rule was previously incorporated in the RESTATEMENT OF TRUSTS § 282 (AM. LAW INST. 1935), and RESTATEMENT (SECOND) OF TRUSTS § 282 (AM. LAW INST. 1957).

[9] *Bowen v. United States Postal Service*, 459 U.S. 212, 243 (1983).

[10] See, e.g., *Wolf v. Mitchell, Silberberg & Knupp*, 76 Cal. App. 4th 1030, 1037 (Cal. Ct. App. 1999); *City of Dubuque v. Iowa Tr.*, 519 N.W.2d 786, 790 (Iowa 1994); *Garcia v. Suda*, 94 Va. Cir. 246 (Va. Cir. 2016).

[11] *Roth v. Scopia Capital Mgmt. LP*, 16CV6182LTSHBP, 2017 WL 3242326, at *4 (S.D.N.Y. July 28, 2017)(citing *Donoghue v. Bulldog Inv. Gen. Pshp.*, 696 F.3d 170, 179 (2d Cir. 2012)).

[12] *Id.* (citing *Phillips v. Tobin*, 548 F.2d 408, 411 (2d Cir. 1976)).

[13] *Pittsburg, C., C. & St. L. Ry. Co. v. Dodd*, 72 S.W. 822, 827 (Ky. 1903) (emphasis added).

[14] *Id.*

litigation, there would be no procedural vehicle to prevent directors and majority stakeholders from committing wrongs to the corporation.[15]

The fact that individual injury on the party of the representative plaintiff is not required has been borne out by subsequent case law. In *Sahni v. Hock*,[16] a plaintiff brought individual claims and a shareholder derivative claim. The court dismissed plaintiff's individual claims because her alleged injury was merely diminution in value of stock, which is not a direct personal injury sufficient to sustain a direct cause of action.[17] Rather, diminution in value of stock is an injury that is derivative of the corporation's injury.[18] Despite lacking a direct injury to sustain a direct cause of action, the court allowed plaintiff to pursue her derivative claims on behalf of the corporation because the corporation had allegedly been injured.[19] Thus, Kentucky law is clear that individual injury is not required. Derivative actions exist because, regardless of whether or not the individual constituent has been injured, the individual still has a real stake in protecting the interest of the business entity of which she is a part.[20]

With regard to lawsuits brought by beneficiaries on behalf of trusts, while Kentucky courts have not yet opined on the issue, the Sixth Circuit, applying Kentucky law in *Osborn v. Griffin*,[21] predicted that this Court would likely adopt the "correct rule set out in the Restatement

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[15] *See id.* at 828 ("To close the doors of the courts to a single stockholder in such a case upon the theory that the majority must rule, and that, having embarked in a common enterprise with them, he must abide the judgment of the majority, would be to turn over to a possible wrongdoer the adjudication of his own case. In such an unequal struggle between duty and interest, it would more frequently happen that 'duty would be overborne in the conflict.'").

[16] 369 S.W.3d 39 (Ky. Ct. App. 2010), *abrogated on other grounds*, 436 S.W.3d 189 (Ky. 2013).

[17] *Id.* at 47.

[18] *Id.*; *see also Turner v. Andrew*, 413 S.W.3d 272 (Ky. 2013) (lost profits suffered by LLC were not suffered by LLC's sole member); *Gross v. Adcomm, Inc.*, 478 S.W.3d 396, 400 (Ky. Ct. App. 2015); *Watkins v. Stock Yards Bank & Tr. Co.*, 2011-CA-000228-MR, 2012 WL 2470692, at *5 (Ky. Ct. App. June 29, 2012), opinion not to be published (Aug. 21, 2013).

[19] *Id.*

[20] *See, e.g.*, Rutledge, *Who Will Watch the Watchers, supra* at 38-39.

[21] 865 F.3d 417 (6th Cir. 2017).

of Trusts," presently articulated in § 107(2)(b) of the Restatement (Third) of Trusts, [22] permitting a trust beneficiary to bring claims on behalf of the trust when the trustee refuses or neglects to act.[23] The Sixth Circuit reasoned this Court had relied on the Restatement of Trusts in many instances in fashioning Kentucky jurisprudence, and would likely do so with respect to this issue.[24] In *Osborn* , the Sixth Circuit held that the beneficiaries of a family trust had representative standing to sue certain of its trustees and a related business entity, and affirmed the trial court's judgment in their favor. Nothing in Kentucky law suggests that Kentucky would not adopt the majority rule that provides beneficiaries standing to sue on behalf of trusts.

C. ***Sexton* did not change Kentucky law on standing in representative lawsuits.**

Although the Court of Appeals places considerable reliance on the *Sexton* opinion, the reality is that *Sexton* did not change Kentucky law, and certainly did not change Kentucky law on derivative standing. Rather, *Sexton* reaffirmed that the only Constitutional Standing analysis in a representative action is the standing of the entity or person being represented, not the standing of the individual seeking to represent them.

Sexton is a representative lawsuit in which a hospital brought claims for reimbursement for medical treatment, purportedly as a representative of a patient (Sexton) who actually received the treatment. The issue before the Court was the status of constitutional standing in Kentucky jurisprudence.[25] In reaching its opinion, this Court formally adopted the three-part *Lujan* test for constitutional standing: (1) injury; (2) causation; (3) redressability.[26] However, the Court recognized that Kentucky courts had already judicially created a standing requirement similar to

[22] The court considered § 282 of the RESTATEMENT (SECOND) OF TRUSTS (AM. LAW INST. 1959) , which does not differ in substance from the more recent iteration in § 107 of the RESTATEMENT (THIRD) OF TRUSTS (AM. LAW INST. 2012).

[23] *Id.* at 447.

[24] *Id.*

[25] *Sexton*, 566 S.W.3d at 188.

[26] *Id.* at 195.

federal constitutional standing rooted in the Kentucky Constitution's limit on the courts' judicial power to hear only justiciable causes.[27] To determine if a case is "justiciable," the Court previously used the three elements of the *Lujan* test.[28] Thus, "[t]o provide clarity to Kentucky's standing doctrine, [the Court] formally adopt[ed] the *Lujan* test as the constitutional standing doctrine in Kentucky as a predicate for bringing suit in Kentucky's courts."[29] It is clear that adopting the *Lujan* test was not meant to change general standing principles as they already existed under Kentucky law.

The Court then analyzed constitutional standing in the context of a representative lawsuit. The Court explained that Sexton, the individual that the named plaintiff sought to represent, was the "true plaintiff," so her status was determinative for purposes of the standing inquiry:

> We emphasize the crucial determinative fact — because Sexton, not [the hospital], is the true plaintiff in this case, we must examine the standing requirement through the lens of Sexton's, not [the hospital's], purported satisfaction.[30]

The Court held that the hospital lacked standing to bring the reimbursement claim because Sexton (the true plaintiff) "has not and will not suffer an 'injury' in this case" because she already received the medical treatment and would not be called on to pay for those services.[31]

Sexton's holding is consistent with the history of representative actions in Kentucky and across the country. Representative lawsuits are meant to remedy injury to the represented entity. For constitutional standing purposes, therefore, injury to the entity, *i.e.* the "true plaintiff," is all that matters. *Sexton* did not in any way limit representative actions under Kentucky law, which has never required individual injury to bring a representative lawsuit. Rather, *Sexton* makes it clear that it is the

[27] *See id.* at 194 ("Kentucky courts have seemingly created a judicially—as opposed to constitutionally—imposed standing requirement.").
[28] *Id.* at 195-96.
[29] *Id.* at 196.
[30] *Id.* at 197.
[31] *Id.*

status of the represented entity, not the individual plaintiff, that must be considered in deciding Constitutional Standing.

D. The Court of Appeals' Opinion Misapplies *Sexton* and the Representative Interest requirement in a Manner That Sharply Limits the Viability of Representative Lawsuits in Kentucky.

Despite the clear language of *Sexton*, the Court of Appeals held below that ***both*** the entity being represented and the individual purporting to represent it must show the three elements of *Lujan* standing, including personal injury to the named representative plaintiff. If allowed to stand, the Court of Appeals' opinion essentially precludes litigants from bringing derivative lawsuits in Kentucky.

The Court of Appeals relied on *Bacigalupo v. Kohlhepp*[32] for the proposition that an individual bringing a representative claim must also show individual injury to establish "standing." That analysis, however, is a misreading of *Bacigalupo*, a case that did not involve Constitutional Standing. Rather, as explained above, *Bacigalupo* involved the Representative Interest rule, which requires a derivative plaintiff to own shares in an entity at all material times to maintain the derivative lawsuit.[33] There, the plaintiff's shares were cancelled during the pendency of the lawsuit due to a corporate merger. As a result, the plaintiff could not satisfy the Representative Interest rule and her suit was dismissed.[34] Of course, the Representative Interest rule makes sense – if the named plaintiff no longer has an interested in the entity she seeks to represent, she should no longer be able to maintain a lawsuit on behalf of that entity.

The confusion for the Court of Appeals here seems to arise from the *Bacigalupo* court's use of the word "standing" to refer to the Representative Interest requirement. The court in

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[32] 240 S.W.3d 155 (Ky. App. 2007).
[33] *Id.* at 157.
[34] *Id.* at 158.

Bacigalupo indicated that the plaintiff must maintain "standing" via maintaining a Representative Interest in the entity to continue the lawsuit.[35] In this context, the use of the word "standing," which is in reference to the old rules of "prudential standing," has nothing to do with Constitutional Standing.[36] Once this fundamental misunderstanding of the use of "standing" to apply to the Representative Interest requirement is understood, it is clear that *Bacigalupo* has nothing to do with the issues before this Court because the plaintiffs here have been and remain KRS members or beneficiaries at all relevant times.

In fact, the *Sexton* Court made clear that it was not adopting any prudential standing principles from federal jurisprudence to change Kentucky law. It cannot be the case that a pre-*Sexton* opinion on the Representative Interest requirement suddenly deprives a party of constitutional standing post-*Sexton.* Even *Bacigalupo* never required the plaintiff to show that it had individual injury. On the other hand, cases like *Sahni* illustrate that a representative plaintiff who lacks individual injury is clearly able to bring a representative claim under Kentucky law.[37] Perhaps most importantly, *Sexton* itself stated in no uncertain terms that it is the entity, not the representative, that must be examined with respect to the three elements of *Lujan* standing.

At bottom, Kentucky law has never required an individual plaintiff bringing a representative lawsuit to also establish individual injury to maintain standing. And for good reason. In a traditional shareholder derivative suit, an individual likely cannot establish personal

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[35] *Id.*

[36] *In re Facebook IPO Derivative Litig.*, 797 F.3d 148, 156 (2d Cir. 2015)("Failure to satisfy the contemporaneous ownership requirement of Rule 23.1 does not, of course, raise a jurisdictional issue under Article III. Rather, it means that the putative derivative plaintiff does not have standing to represent the interests of the nominal defendant in a derivative capacity."). Prudential standing does not require a plaintiff to have an individual injury before it can assert a representative claim. *See Dismas Charities, Inc. v. U.S. Dept. of Justice*, 401 F.3d 666, 674 (6th Cir. 2005).

[37] 369 S.W.3d at 47.

injury because the shareholder's injury is typically an unrealized loss, *i.e.*, devaluation of unsold stock.[38] Likewise, a beneficiary bringing suit on behalf of a trust likely could not show individual injury to confer standing because the beneficiary has no legal title to the corpus of the trust.[39] If these individuals could establish personal injuries, they would seek redress for those injuries to their direct benefit, not redress of the entity's injury which only inures to their benefit indirectly.

Here, the Court of Appeals misapplied and misinterpreted clear law on derivative actions. In doing so, it created a new and unworkable standard for standing in derivative lawsuits that sharply limits, if not does away with, the viability of representative lawsuits in Kentucky, which are generally available in all other state and federal courts. The Court should not allow Kentucky courts to become an outlier jurisdiction that limits or discourages representative lawsuits.

III. CONCLUSION

For the foregoing reasons, and the reasons stated in the Appellants' briefs, this Court should vacate the Court of Appeals' writ of prohibition entered April 23, 2019, and reinstate the Circuit Court's November 18, 2018 Opinion and Order denying (in principal part) the Defendants' motions to dismiss.

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[38] Devaluation of unsold stock is not sufficient to establish a personal injury. *See Sahni*, 369 S.W.3d at 47; *see also Turner v. Andrew*, 413 S.W.3d 272, 277 (Ky. 2013).

[39] *Pillsbury v. Karmgard*, 22 Cal. App. 4th 743, 753 (Cal. Ct. App. 1994); *Saks v. Damon Raike & Co.*, 7 Cal. App. 4th 419, 427 (Cal. Ct. App. 1992).

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