COMMONWEALTH OF KENTUCKY
COUNTY OF FRANKLIN CIRCUIT COURT
DIVISION II
CASE NO. 21-CI-00645

TIA TAYLOR, *et al.*, as Members and Beneficiaries of Trust Funds of the KENTUCKY RETIREMENT SYSTEMS, Its Pension and Insurance Trusts for the Benefit of Those Trusts — PLAINTIFFS

vs.

THE TIER 3 TRUST PLAINTIFFS' NOTICE OF MOTION AND MOTION FOR STATUS CONFERENCE

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

ELECTRONICALLY FILED

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PLEASE TAKE NOTICE that, on June 20, 2022, at the conclusion of the motion hour docket (9:00 a.m.), or as soon thereafter as counsel may be heard, Plaintiffs Tia Taylor, Ashley Hall-Nagy, Bobby Estes and Jacob Walson (the "Tier 3 Trust Plaintiffs") will, and hereby do, move the Court, before the Honorable Thomas D. Wingate, at Courtroom E of the Franklin County Courthouse, located at 222 St. Clair Street, Frankfort, Kentucky 40601, to set a status conference for a date in June 2022, as it is convenient for the Court, to discuss the further proceedings in this action.[1]

The Tier 3 Trust Plaintiffs expect that the hearing time will exceed ten minutes.

In support of this motion, the Tier 3 Trust Plaintiffs respectfully submit the following memorandum.

[1] A hearing for defendants' motion for status conference was set for June 20, 2022 in the related action, *Commonwealth v. KKR & Co. Inc.*, Case No. 17-CI-1348, now prosecuted by the Attorney General (the "*Mayberry* Action" or the "AG's Action"). On June 13, 2022, based on an agreement of the Attorney General and defendants in that action, the Court set a status conference for July 18, 2022, at 9:30 a.m. The Tier 3 Trust Plaintiffs desire an earlier status conference date in their case. There is no reason for a month-long delay.

THE TIER 3 TRUST PLAINTIFFS' MEMORANDUM IN SUPPORT OF MOTION FOR STATUS CONFERENCE

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I. INTRODUCTION

This breach-of-trust action was brought by Tier 3 KRS members to remedy harm caused by the "Hedge Fund Sellers" and the other Defendants, each of whom participated with or materially assisted the sole Trustee of the KRS trusts — the KRS Board — in one or more breaches of trust.[1] While this case is related to *Commonwealth v. KKR & Co.*, Case No. 17-CI-1348, now prosecuted by the Attorney General (the "AG's case"), it is grounded in a completely different, indeed conflicting, legal theory and thus stands apart from, and is not duplicative of, that case. Specifically, **the complaint in this case alleges that the KRS Board**, **which was by statute the sole Trustee of the KRS trusts**, **is guilty of breaches of trust and that the Defendants knowingly participated with and aided the Trustee in these breaches of trust**. The Attorney General ("AG") does *not* allege that the KRS Board breached the trust; to the contrary, the AG's case is premised on the view that KRS was an innocent victim of breaches of duties owed to KRS. Simply put, allegations that the KRS Board was a **perpetrator**, a primary wrongdoer, are not only different from but indeed incompatible with allegations that KRS was an innocent **victim**.

At this point, the parties await decision on the motions to dismiss that have been fully briefed and taken under submission in January 2022. We are pleased to appear before the Court to discuss the status of the case, but would urge the Court to rule as soon as possible on the motions to dismiss. This submission seeks to assist the Court in "getting up to speed."

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[1] The Tier 3 Trust Plaintiffs also filed a class action on behalf of all Tier 3 members alleging a violation of the RICO statute, which Defendants removed to federal court. The federal court stayed that case pending proceedings in this case. *See Taylor v. KKR & Co., L.P.*, No. 21-0029-KKC, 2022 U.S. Dist. LEXIS 35577, at *14 (E.D. Ky. Mar. 1, 2022).

The Hedge Fund Defendants have filed a paper styled as a "Motion for Status Conference" in the AG's case. It is an effort to recast and reposition the case and their defenses anew. Defendants' self-serving and misleading counter-narrative will have its day in court, but that will come later, at trial. But recognizing that self-serving, false and misleading counter-narratives can do damage if left to fester, we offer our own history and overview of the Tier 3 Trust Plaintiffs' case and offer suggestions as to how to proceed in the related cases.

II. HISTORY OF THE TIER 3 TRUST BENEFICIARIES' CASE

This Tier 3 trust case is not a *tabula rasa*. The first complaint alleging wrongdoing by the Hedge Fund Sellers and others was filed in late 2017 by several Tier 1 members of the KRS (the "*Mayberry* Plaintiffs") as a derivative action (the "*Mayberry* Action") on behalf of KRS. In 2018 Judge Shepherd denied the motions to dismiss that *Mayberry* Complaint, sustaining all the legal claims and the adequacy of the factual allegations as to all Defendants, save one.[2]

The Officer and Trustee Defendants filed an interlocutory appeal and certain other Defendants filed writ proceedings. The Kentucky Supreme Court reversed on the narrow and specific ground that the *Mayberry* Plaintiffs lacked constitutional standing because, as Tier 1 members, their benefits were not impacted by investment returns or plan expenses because they were guaranteed by the Commonwealth through the "inviolable contract."[3]

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[2] *See Mayberry v. KKR & Co. L.P.*, No. 17-CI-1348, slip op. (Ky. Cir. Ct. Franklin Cnty. Nov. 30, 2018) ("Nov. 30, 2018 Order") (attached as Exhibit A).

[3] *Overstreet v. Mayberry*, 603 S.W.3d 244, 266 (Ky. 2020).

When the case was remanded to Judge Shepherd the AG intervened in the *Mayberry* action. Judge Shepherd denied without prejudice the motion of a group of Tier 3 KRS members to intervene as derivative plaintiffs.

Subsequently, the group of Tier 3 KRS members, whose pension benefits are *not* guaranteed (*i.e.*, *not* covered by inviolable contract provisions) and whose pension accounts (and thus ultimate benefits) *are* directly affected by net investment returns, and who thus have the concrete injury required for constitutional standing, filed this *direct* action as a separate action, initiated by the "Tier 3 Complaint."[4]

The Tier 3 Trust Plaintiffs alleged breaches of trust, seeking damages to be paid to the KRS Trusts. The Tier 3 Trust Plaintiffs, Tia Taylor, Ashley Hall-Nagy, Bobby Estes and Jacob Walson are perfect plaintiffs. They are hardworking Kentucky citizens — public employees — whose life savings are in the KRS Trusts and whose accounts and benefits have been damaged/diminished due to the alleged misconduct of the Defendants. The Tier 3 Trust Plaintiffs are represented by the lawyers who originated the *Mayberry* Action, and who crafted the complaint Judge Shepherd upheld and the AG copied.

The Tier 3 Complaint alleges that the sole Trustee (the KRS Board) committed breaches of trust and that the named Defendants participated with or aided the Trustee in connection therewith. The allegations are centered on actions by the KRS Board *as a whole*, not individual KRS trustees acting individually as in the AG's case. These allegations trigger a long-established rule in trust law affording

[4] The allegations in the Tier 3 Trust Plaintiffs' August 19, 2021 Complaint (the "Complaint") are cited as "¶ ___."

trust beneficiaries the right to bring a direct (not derivative) action against the trustee and/or those who participated with the trustee in breaches of trust.

The substantive and factual sufficiency of the core claims now being pursued by the Tier 3 Trust Plaintiffs were upheld 3+ years ago. The factual allegations in the Complaint laid out what a unanimous Kentucky Supreme Court said were "serious allegations of wrongdoing" and Judge Shepherd called "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." December 28, 2020 Order.[5]

According to Judge Shepherd, "any party that breached its fiduciary duties and engaged in reckless conduct, conflicts of interest, or self-dealing should be accountable" and "**principles of equity and public interest require that the factual allegations** … **should be adjudicated on the merits**." Dec. 28, 2020 Order at 16–17. Judge Shepherd observed early on that an "autopsy" should take place. Hundreds of millions — probably billions — in damage caused by the Defendants are at stake.

Every judge that has examined the allegations has reached the same conclusion — "serious wrongdoing" is pleaded.

After months of maneuvering, motions to dismiss the Tier 3 Trust Complaint and the AG's complaint, were fully briefed and submitted for decision several months ago. Most of the issues raised in the motions in both cases involved re-argument of issues on which Judge Shepherd had already ruled adversely to the Defendants. Some new issues,

[5] *See Mayberry v. KKR & Co., L.P.*, No. 17-CI-1348, slip op. at 17 (Ky. Cir. Ct. Franklin Cnty. Dec. 28, 2020) ("Dec. 28, 2020 Order") (attached as Exhibit B).

however, were raised — principally (in this case) the right of the Tier 3 Trust Plaintiffs to bring a direct (not derivative) action (which boils down to who "owns" the claims), and in the AG's case whether the Court had and has subject matter jurisdiction (which argument is an outgrowth of the Tier 1 constitutional standing issue and has no impact on the Tier 3 Trust Plaintiffs' case).

Two things happened while those dismissal motions were pending. First, Judge Shepherd entered summary judgment against the hedge fund defendants in the AG's collateral declaratory-relief action, in a detailed, scholarly and well-reasoned opinion. This judgment voided indemnity clauses contained in the hedge funds' "subscription agreements" and ruled that KRS may only be sued in Kentucky. The Court also ruled that it had personal jurisdiction over certain defendants who opposed summary judgment on jurisdictional grounds.

Second, for some reason, the Defendants began to produce documents to the AG while refusing to produce anything to the Tier 3 Trust Plaintiffs. The Defendants convinced the AG to reverse his prior "open proceedings" posture and agree to an extraordinarily broad and defense-oriented protective order which gives the Defendants the ability to seal and keep secret from the public any document, so long as they say it is a "trade secret", "confidential" or contains "sensitive" information.[6]

[6] The complex and convoluted protective order offered up by the AG and Defendants in the AG's case is inconsistent with Kentucky law and the prior rulings of Judge Shepherd of a presumption of openness and public access to all filings and discovery materials in these cases. *See* Nov. 1, 2021 Order ("The Court will *require* … transparent proceedings and will determine, upon motion and hearing, whether any party seeking a protective order can carry its burden to restrict public access to documents *on a case-by-case basis*."). The Tier 3 Trust Plaintiffs do not agree with the approach in the protective order agreed to by the AG, and reiterate their position in favor of full public access to all discovery materials in this breach-of-trust action. The Tier 3 Trust Plaintiffs have moved for complete public access to all discovery materials in this case, and that no

After Judge Shepherd ruled against the hedge fund Defendants in the AG's declaratory-relief case filed by the AG, and failed to enter the proffered protective order agreed to by the AG, those Defendants mounted an extraordinary attack on his impartiality, claiming he was using these cases to advance his re-election campaign. They sought to have him kicked off all the KRS hedge fund cases, and have all the cases assigned to a retired judge. The Tier 3 Trust Plaintiffs opposed this attack on Judge Shepherd. **But for whatever reason the AG was silent**, **filing no opposition**. As the AG remained silent, Judge Shepherd recused himself, even while disagreeing with the substance of the attack motion. The matter was transferred to this Court.

Due to Defendants' relentless pursuit of technicalities, obfuscations, and attacks on the judiciary, the original *Mayberry/Commonwealth* case is now over four years old, still mired at the motion to dismiss stage and now assigned to a new judge. This case, too, is stuck in the procedural morass Defendants have created. Meanwhile, the KRS pension trusts continue to be horribly under-funded and its plans continue to be in danger of failure. Yet the Defendants remain in possession of their ill-gotten gains — hundreds of millions in fees — they pocketed by looting the KRS trusts, causing its horrendous losses — alleged misconduct the judiciary has said for years now, the "public interest" demands be pursued on the merits, so the perpetrators can be held "accountable."

blanket protective order be entered. *See Taylor v. KKR & Co., L.P.*, No. 21-CI-00645, Memorandum in Support of Motion for Order Directing That No Protective Order Be Entered and That Complete Public Access to All Proceedings Including Discovery Will be Allowed (Ky. Cir. Ct. Franklin Cnty. Aug. 31, 2021) (the Tier 3 Trust Plaintiffs renewed this motion on May 9, 2022). How the AG, who is duty-bound to represent the public, can justify the proposed secrecy in his case remains to be seen.

Hopefully, when this Court gets its arms around these overlapping, competing and conflicting lawsuits, this case — **the case as to which there is no doubt as to its merit** — can finally move forward and be prosecuted on the merits

The question, ultimately, is whether the extremely deep-pocketed group of Defendants, which includes some of the richest men on earth and their Wall Street juggernauts can continue into the indefinite future to delay and thereby frustrate justice.[7]

III. NATURE OF THE TIER 3 TRUST BENEFICIARIES' SUIT

To protect Kentucky's public workers, the Commonwealth created KRS and designated KRS's pension assets as "trust funds" and the KRS Board as the sole Trustee.[8] ¶ 18. The KRS Pension and Insurance Trusts (the "Trusts") are overseen and managed by the Trustee[9] for 390,000 present and former government employees. The Trusts were at one time over-funded with a $2 billion surplus. However, as of 2016–2017, the Trusts were gravely impaired and in danger of failing. The $2 billion surplus was replaced by a

[7] There is also a question as to whether the AG has the political will to aggressively pursue these extremely rich and powerful individuals, who not incidentally happen to be among the largest multi-million-dollar contributors to Senator McConnell's political operation. *See* discussion at pages 33 through 35 below.

[8] KRS 61.515 established the "Kentucky Employees Retirement System," a "retirement system for employees" giving KRS the powers and privileges of a corporation, with bylaws and the power to conduct business, governed by its Board of Trustees/Directors. It also created a fund called the "Kentucky Employees Retirement Fund" and provided that "[a]ll assets received in the fund shall be deemed trust funds to be held and applied solely as provided in KRS 61.510 to 61.705." KRS 78.520 created a "fund" called the "County Employees Retirement Fund" and provided "all assets received in the fund shall be deemed trust funds." KRS 16.510(2) created "a fund" called the "State Police Retirement Fund" and provided "all assets received in the fund shall be deemed Trust funds." Later, KRS 61.701 created and established a trust fund for insurance benefits. According to KRS's "Mission Statement" in its 2016 Annual Report, "members … contribute money into our trust funds."

[9] References to "the Trustee" are to the KRS Board acting in its capacity as sole Trustee for the Trusts.

$30 billion deficit. KRS was the worst-funded public pension plan in the United States. The largest of the KRS Plans — 139% funded at one time — had only 13% of the money it needed to pay the billions of dollars it owed. ¶ 20.

This is a breach-of-trust action by Tier 3 members of KRS, as beneficiaries of KRS's Trusts, seeking to recover losses via equitable relief, including make-whole relief in the form of a money judgment to be paid into those Trusts. The Tier 3 Trust Plaintiffs, as trust beneficiaries, assert their own **direct claims** (*i.e.*, **not derivative claims** on behalf of the Trustee) against Defendants for knowingly participating with the Trustee in a series of breaches of trust.[10] This action is a classic expression of the beneficiaries' right to sue a trustee who commits breach of trust — and third parties who with notice participate in the breach — to vindicate the beneficiaries' direct right and recover losses through a case in equity. These concepts were recognized in American case law nearly a century ago when they were enshrined in the RESTATEMENT (FIRST) OF TRUSTS.[11]

[10] These claims are stated in various ways including knowingly aiding/abetting and conspiring and pursuing a common enterprise with the Trustee (KRS), as well as breaches of fiduciary duties owed to the trust beneficiaries.

[11] *See, e.g.*, RESTATEMENT (FIRST) OF TRUSTS § 205, comment a. ("If the trustee commits a breach of trust, the beneficiary may have the option of pursuing a remedy which will put him in the position in which he was before the trustee committed the breach of trust; or of pursuing a remedy which will give him any profit which the trustee has made by committing the breach of trust; or of pursuing a remedy which will put him in the position in which he would have been if the trustee had not committed the breach of trust."); RESTATEMENT (FIRST) OF TRUSTS § 326 ("A third person who, although not a transferee of trust property, has notice that the trustee is committing a breach of trust and participates therein is liable to the beneficiary for any loss caused by the breach of trust."). Though reorganized and renumbered, the Restatement (Third) carries these rules forward. *See, e.g.*, RESTATEMENT (THIRD) OF TRUSTS §§ 100, 107, and *see esp*. Reporter's Note to § 107, comment f: "Ordinarily … the beneficiary will bring suit against *both* the [wrongdoing] trustee and the third party [who participated in the breach of trust]. However, **it is not necessary to join the trustee in the suit**, **because** … [**t**]**he liability of the third party is to the beneficiaries**, **rather than to the trustee**[.]"

Defendants' central premise, underlying virtually all of their arguments against the Tier 3 Trust Plaintiffs, is that this breach-of-trust action is necessarily a "derivative" case — that Plaintiffs are not real parties in interest entitled to sue directly to vindicate their own rights — and thus (they say) the AG's case swallows up and preempts this case. But Defendants' central premise is wrong. These Tier 3 Trust beneficiary plaintiffs **own** these claims arising from breach of trust by the sole Trustee; the Trustee **does not own** them and the AG has not asserted (and cannot assert) these claims.

The right of trust beneficiaries to pursue claims **directly** against third parties who participated in a culpable trustee's breach of trust has long been recognized in American (including Kentucky) law.[12] This breach-of-trust cause of action comes from the common law of trusts and is personal to (and owned by) the trust beneficiaries. This direct claim is available where the Trustee is alleged to have committed breach of trust and third parties participate therein. And, as explained below, this venerable rule makes perfect sense when one focuses on the fact that **a trust is not a separate entity or legal person**.[13] In the bipartite trust relationship, the *only* actors who can "own" claims are the trustee and the beneficiary — and **the trustee does not** "**own**" (***i.e.***, **hold in trust for his beneficiary**) **a claim against himself for breaching duties owed to the**

[12] *See*, *e.g.*, RESTATEMENT (FIRST) OF TRUSTS § 326 ("A third person who, although not a transferee of trust property, has notice that the trustee is committing a breach of trust and participates therein is liable to the beneficiary for any loss caused by the breach of trust."); RESTATEMENT (SECOND) OF TRUSTS § 326 (same); 76 AM. JUR. 2D TRUSTS § 603 ("a trust beneficiary may sue third persons who, for their own financial gain or advantage, induced the trustee to commit a breach of trust, participated with, aided or abetted the trustee in such a breach of trust, or while knowing of the breach of trust, received and retained trust property from the trustee").

[13] Definitionally, **a** "**trust** … **is a fiduciary relationship with respect to property**[.]" RESTATEMENT (THIRD) OF TRUSTS § 2.

beneficiary.[14] Hence beneficiaries own, and may pursue in their own right, this sub-species of claims, against a trustee who has committed breach of trust and third parties who participated with or aided and abetted the trustee. In connection with such claims, it is not necessary that the beneficiaries ask the trustee to sue the assistors and co-conspirators, nor is it necessary for the beneficiaries to sue the culpable Trustee.[15]

Defendants cite RESTATEMENT (SECOND) OF TRUSTS § 282 for the proposition that a beneficiary cannot sue a third person unless the Trustee "improperly refuses or neglects" to bring the action. But § 282 is inapposite here. It is found in Chapter 9 (*Liabilities of Third Persons*), Topic 1 (*Persons Acting Adversely to the Trustee*). That is not this case. We do not claim that Defendants acted adversely to — **against** — the Trustee; to the contrary, we allege that Defendants participated **with** the Trustee in breach of trust. Thus, this case is covered not by Topic 1 of Chapter 9, but by Topic 3 (*Participation in Breach of Trust*). The correct rule for this very different fact scenario is set out in RESTATEMENT (SECOND) OF TRUSTS § 326:[16]

> A third person who, although not a transferee of trust property, has notice that the trustee is committing a breach of trust and participates

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[14] This distinguishes the facts here, involving a trust, from a corporate shareholder setting where the corporation (unlike a trust) *is* a separate legal person with the legal capacity to retain counsel and bring and defend lawsuits.

[15] *See*, *e.g.*, RESTATEMENT (THIRD) OF TRUSTS §§ 100, 107, and *see esp*. Reporter's Note to § 107, comment f: "Ordinarily … the beneficiary will bring suit against *both* the [wrongdoing] trustee and the third party [who participated in the breach of trust]. However, **it is not necessary to join the trustee in the suit**, **because** … [**t**]**he liability of the third party is to the beneficiaries**, **rather than to the trustee**"; *see also In re Rural/Metro Corp. S'holders Litig.*, 102 A.3d 205, 252–53 (Del. Ch. 2014).

[16] Indeed, Comment a. to § 326 posits a fact pattern not dissimilar to our own:

> "[I]f the trustee purchases through a stockbroker securities which it is a breach of trust for him to purchase and the broker knows that the purchase is in breach of trust, the broker is liable for participation in the breach of trust."

therein is liable to the beneficiary for any loss caused by the breach of trust.

Thus where, as here, the Trustee is alleged to have breached its duties, the trust beneficiaries retain the personal, individual right to sue any third-party participant or assistor directly to recover damages/equitable relief which may be paid into the trust for the benefit of beneficiaries.

Defendants have asserted, incorrectly, that the Plaintiffs are suing derivatively "*on behalf of KRS trusts*." Not so. Defendants have deliberately misquoted the Complaint, representing that it uses the "*on behalf of KRS trusts*" language. But the Complaint does not say the Tier 3 Trust Plaintiffs are suing "on behalf of KRS trusts." To the contrary, the Complaint expressly states: "This action is **not a derivative action** on behalf of KRS or its trusts. This is a **direct action by trust beneficiaries** …." ¶ 16. The "**right of the beneficiaries against the** [**third party**] **is a direct right and not one that is derivative through the trustee**." *City of Atascadero v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 68 Cal. App. 4th 445, 465 (Cal. Ct. App. 1998) (original emphasis removed). Plaintiffs do intend and pray that any money judgment recovered herein be paid *into the Trusts* to restore trust property — but that is a long way from saying they are suing derivatively *on behalf of the Trusts*. As noted above, **a trust is not a legal person**; **a trust cannot sue in its own right; and thus no derivative case may be brought on behalf of a trust**.

Defendants also claim that Tier 3 members of the KRS pension plans and beneficiaries of its Trusts lack constitutional standing. But, their arguments ignore both the status of the Tier 3's as members of a "hybrid" plan with "defined contribution" features whose plan accounts and ultimate benefit payments have already been reduced as a result of the wrongful conduct alleged, and the fact that, without the "inviolable

contract" guarantees enjoyed by Tier 1 members, they are dependent on the survival and adequate funding of the trusts to receive their benefits. The Tier 3 "upside sharing" percentage of annual plan-wide investment returns means that their current pension accounts and final pension amounts (held in the Trusts) are directly affected by investment performance/fees, trust expenses and the Trustee's fiduciary stewardship. Constitutional standing exists under either theory.

This case focuses on **breaches of trust by the KRS Board**, acting as a whole in its role as **sole Trustee** of the KRS Trusts. In contrast, the AG accuses an *ad hoc* subset of individual past or present KRS trustees of breaching fiduciary duties owed *to* KRS. Thus, in this Tier 3 trust case, the KRS Board is viewed as a primary bad actor — a **perpetrator** not sued only because of sovereign immunity — while in the AG's case KRS is viewed as a **victim** of bad conduct by others. **It makes a huge difference whether the trustee is a perpetrator or a victim**. A trustee who is guilty of breach of trust cannot and does not "own" (*i.e.*, hold in trust for beneficiaries) claims for relief arising from his own breach; the beneficiaries own those claims and prosecute them on a *direct* basis. It makes a huge difference whether the third-party Defendants are seen as having "**act**[**ed**] **adversely to the Trustee**," (**the AG's case**) or as having "**participat**[**ed**] **in breach of trust**" with the Trustee (the Tier 3 Trust Plaintiffs' case).[17] The two theories cannot coexist.[18]

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[17] *Compare*, RESTATEMENT (SECOND) OF TRUSTS, Ch. 9, Topic 1 ("Persons Acting Adversely to the Trustee") *with* Ch. 9, Topic 3 ("Participation in Breach of Trust Other Than by Receiving Transfer"). It appears the AG is in effect proceeding under a Topic 1 theory, while we are proceeding under a very different Topic 3 theory.

[18] In this case, the Trustee's bad behavior opens the door for beneficiaries to sue the third-party Defendants for participation in breach of trust. In the AG's case, that same bad behavior forms the basis for Defendants' *in pari delicto* defense.

Another problem with the AG's case stems from his recent unequivocal statement in open court that he does not represent KRS, abandoning prior claims that he represents the interests of KRS. But the KRS Board was and is the sole Trustee — and the Commonwealth cannot stand in for the Trustee just by saying it is so. **KRS, in its role as a "statutorily created agency of state government," undoubtedly is an "arm, branch, or alter ego" of the Commonwealth, and is its agent.**[19] **But the KRS Board in its role as sole Trustee of the KRS trusts is different**. In its role as sole Trustee, the Board was and is charged with "sole interest" and "exclusive purpose" fiduciary duties that cannot be diluted; **the sole Trustee cannot also be the agent of a principal (the Commonwealth) that has different priorities**. That would constitute an impermissible structural conflict of interest.

In this case, Plaintiffs, as trust beneficiaries, assert their own **direct claims** (*i.e.*, **not derivative claims** on behalf of the Trustee) against Defendants for knowingly participating with the Trustee in a series of breaches of trust. It is well-established that trust beneficiaries have the right to sue a trustee who commits breach of trust — and third parties who with notice participate in the breach — to vindicate the beneficiaries' direct right and recover losses through a case in equity. These concepts were recognized in American case law nearly a century ago when they were enshrined in the RESTATEMENT (FIRST) OF TRUSTS.[20]

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[19] *Commonwealth v. Kentucky Retirement Systems*, 396 S.W.3d 833, 837 (Ky. 2013).

[20] *See, e.g.*, RESTATEMENT (FIRST) OF TRUSTS § 205, comment a. ("If the trustee commits a breach of trust, the beneficiary may have the option of pursuing a remedy which will put him in the position in which he was before the trustee committed the breach of trust; or of pursuing a remedy which will give him any profit which the trustee has made by committing the breach of trust; or of pursuing a remedy which will put him in the position in which he would have been if the trustee had not committed the breach

The Defendants portray the case as one that is centered entirely around the decision to invest in the hedge funds. But that is far too narrow a lens. The Trustee committed breaches of trust in at least the following ways:

(a) By approving and allocating 10% of the KRS Trust funds to hedge fund investments all at one time to just three sellers, each with extremely dubious track records of dishonest and illegal behavior and cheating those to whom they owned fiduciary duties;

(b) By permitting certain hedge fund sellers to benefit from improper insider connections with the KRS investment staff;

(c) By agreeing to buy, and buying, the high-fee, high-risk, illiquid hedge fund vehicles, *i.e.*, Black Box hedge funds of funds from the Hedge Fund Sellers in the face of stark warnings that high-risk, illiquid investments would likely lead to disaster;

(d) By agreeing to waive the Hedge Fund Sellers' suitability obligations – really, the meat, bone and gristle of their fiduciary duties – without having any other way to assess suitability, since the KRS investment staff had neither the expertise nor the detailed information about the underlying hedge funds to do the job itself;

(e) By failing and refusing to disclose the amount – or even magnitude – of the total fees paid to the Prisma, PAAMCO and BAAM Black Box funds-of-hedge-funds or to the underlying hedge funds in which they invested in connection with KRS;

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of trust."); RESTATEMENT (FIRST) OF TRUSTS § 326 ("A third person who, although not a transferee of trust property, has notice that the trustee is committing a breach of trust and participates therein is liable to the beneficiary for any loss caused by the breach of trust."). Though reorganized and renumbered, the Restatement (Third) carries these rules forward. *See, e.g.*, RESTATEMENT (THIRD) OF TRUSTS §§ 100, 107, and *see esp*. Reporter's Note to § 107, comment f: "Ordinarily … the beneficiary will bring suit against *both* the [wrongdoing] trustee and the third party [who participated in the breach of trust]. However, it is not necessary to join the trustee in the suit, because … [t]he liability of the third party is to the beneficiaries, rather than to the trustee[.]"

(f) By failing adequately to monitor the hedge fund investments and failing to remove these expensive, risky, illiquid, imprudent investments from the portfolio;

(g) By failing to prevent in advance, or inquire after the fact about, improper under-the-table inducements that the known facts suggest were provided by certain of the hedge funds to certain KRS staffers;

(h) By entering into a "Strategic Partnership" with KKR Prisma and allowing its agents to **sign secret contracts** (**the** "**Advisory Services Agreements**") **giving KKR Prisma** (**and its** "**affiliates**," **explicitly including KKR**) **the right to self-deal with KRS trust assets** while effectively waiving their statutory and other fiduciary duties; and

(i) By covering up their prior wrongdoing via a "fixed" internal review and report — the Calcaterra Report — by a New York law firm retained under dubious circumstances and paid with "public" funds. KRS, its current officials and the AG have concealed this report from KRS's members and the public, refusing repeated requests to disclose it.

The unlawful conduct described in (h) and (i) above is not included in the AG's case. As part of the "Strategic Partnership," KKR Prisma agreed to perform very substantial services for KRS — services for which KKR Prisma would otherwise have charged millions of dollars — purportedly "for free." But the secret Advisory Services Agreements revealed what the actual "consideration" was — "the opportunity for [KKR Prisma] to expand its industry knowledge and develop further business relationships with third parties through the provision of services under this Agreement." In other words, **KKR Prisma was secretly granted the right to use its gatekeeper role in connection with hundreds of millions in trust assets to advance its own**

business interests. And, the current CEO/ED of KRS who was personally implicated in this unlawful conduct then orchestrated the Calcaterra Report whitewash cover up to protect himself and his coconspirators.

IV. DEFENDANTS' PENDING MOTIONS TO DISMISS REHASH ALREADY-REJECTED ARGUMENTS

Defendants filed over a dozen separate motions to dismiss this case, 300 pages of briefs and 1,200-plus pages of other submissions. Those filings, along with defendants' most recent filings in the AG's case, are chock-full of self-serving counter-factual narratives of supposed innocence. But we are at the motion-to-dismiss stage. This Complaint's allegations must be taken as true; and the pleading standard is liberal and minimal. Even so, the Tier 3 Complaint is filled with details of a decade-long scheme with specific acts of wrongdoing by every Defendant pleaded.

Every Defendant attempts to recast the actual allegations detailing the KRS fiasco and their culpable participation as a benign event, due to natural forces — rather than their misconduct. Defendants deny that any of them were involved in any breach of duty or wrongdoing or aided or abetted, conspired or participated in a breach of trust or common enterprise with the culpable Trustee. Defendants deny fault or responsibility for the worst public fund catastrophe in U.S. history, during which they held key fiduciary positions intended to protect the Trusts and from which many of them pocketed millions — even hundreds of millions — of dollars in fees. The Court need only scan ¶¶ 1, 2, 3, 16, 17 and 29 through 79 of this Complaint to "get the gist" of the course of misconduct, conspiracy and common enterprise, the horrible risks taken, the explicit warnings ignored, the grotesque fees imposed, the cover-up/catch-up scheme and the specific involvement of every Defendant and the condemnation of what they did by high-ranking

Commonwealth officials, who have had access to internal information and documents thus far denied Plaintiffs.

The Defendants' motions to dismiss this Complaint regurgitate the same arguments Judge Shepherd rejected over four years ago. It is worthwhile to examine the *specificity* with which Judge Shepherd rejected the arguments Defendants repeat now. The Court found the original *Mayberry* Plaintiffs had alleged:

> … that these defendants acted in bad faith … describing use of 7.75% return rate as "willfully reckless" … describing concealment of KRS's financial condition as "deliberate, willful manipulation" … listing scenarios in which KRS trustees and officers acted "willfully or recklessly" in violation of duties and "did not act in good faith" … explaining that conflicts of interest among trustees and entities made it impossible to use good faith judgment, … explaining that each defendant "knowingly" participated in a civil conspiracy or scheme.

Nov. 30, 2018 Order at 13, 21–22. The Complaint pleads all this and more. As to personal jurisdiction, the Court noted how personal jurisdiction had been pleaded:

> Several executives of Prisma, PAAMCO, and BAAM … Kravis, Roberts, Schwarzman, and Hill — contest personal jurisdiction …. Blackstone and KKR also contest personal jurisdiction ….
>
> … Plaintiff states that each of the out-of-state defendants "participated in a years-long conspiracy, scheme, and common course of concerted conduct and enterprise with in-state Kentucky residents and actors, involving repeated travel into Kentucky by themselves or their agents for business purposes, thus subjecting themselves in the personal jurisdiction of Kentucky courts." Stated another way, the plaintiffs allege that these defendants entered into business arrangements with a Kentucky entity, and through those arrangements, engaged in a pattern of intentional or reckless misrepresentation, which foreseeably caused significant financial losses to KRS … members … to the benefit of these out-of-state defendants. *See* KRS 454.210(a)(4) (providing personal jurisdiction over non-residents that cause tortious injury in the Commonwealth by virtue of their business relationships, persistent courses of conduct, or substantial revenue derived from their Kentucky relationships).

Nov. 30, 2018 Order at 17–19. The same allegations are at ¶¶ 81–96, 152–160.

As to the liability of the Hedge Fund Sellers and their controlling principals and top executive officers, Judge Shepherd stated:

> The "Hedge Fund Seller Defendants" include the entities responsible for the sale and management of the relevant hedge funds, *as well as several top executives of these companies*. These defendants now argue that Plaintiffs fail to identify a fiduciary duty, relying primarily on the contractual nature of the relationship between these defendants and KRS. In other words, … these parties were bound only to the terms of those contacts and there are no allegations that they breached the specific terms of those agreements.
>
> … [T]he Court finds that the [Complaint] contains allegations sufficient to imply a common law fiduciary relationship between the Hedge Fund seller Defendants and KRS *and its members* (referencing "superior knowledge and expertise" of the Hedge Fund Seller Defendants, KRS's dependence on said expertise, and Defendants' knowledge of that dependence). The complaint also contains sufficient allegations of a breach of those fiduciary duties. For example, Plaintiffs reference the massive fees collected by these defendants in breach of the common law fiduciary duty to not charge excessive fees.

Nov. 30, 2018 Order at 26–27. The same allegations are at ¶¶ 122, 125, 133–135, 141–144, 215–220, 279–278.

As to the conspiracy, aiding and abetting and joint enterprise allegations, they were upheld as well:

> … Defendants argue that Plaintiffs fail to allege an agreement among the defendants to do the unlawful or tortious act… the Court finds that Plaintiffs sufficiently pleaded circumstances that could lead a jury to conclude that such an agreement existed. … throughout the Complaint, Plaintiffs repeated their allegation that various defendants "knowingly aided and abetted the breach of duties by Trustees, while participating by committing overt acts, in an ongoing scheme, civil conspiracy, common course of conduct and joint enterprise" in concert with the KRS trustees, by "acting and failing to act as alleged herein."
>
> The actions and inactions included in the Complaint include providing false or misleading information, and otherwise acting in bad faith. The Complaint also details alleged conflicts of interest among the KRS trustees and the other defendants, which could lead to a factfinder to conclude that an agreement, express or implied, existed among these parties.
>
> * * *
>
> … [T]he Court finds that Plaintiffs sufficiently plead their aiding and

> abetting claim .... Plaintiffs also allege that the defendants knowingly provided assistance to the breaching parties by promoting or allowing the use of false or misleading information in an effort to conceal KRS's financial status.
>
> In *Steelvest*, our Supreme Court made clear that "a person who knowingly joins with or aids and abets a fiduciary in an enterprise constituting a breach of the fiduciary relationship becomes jointly and severally liable with the fiduciary for any profits that may accrue." 807 S.W.2d at 485.

Nov. 30, 2018 Order at 27–29. The same allegations are at ¶¶ 56–59, 125, 136, 144, 165, 169–170, 179, 224–228, 267, 352–365, and 380.

Finally, Judge Shepherd summarized the allegations in the *Mayberry* Complaint regarding Defendants' bad faith and willful and/or reckless misconduct, which the Court accepted as true for CR 12.02 purposes there, and should likewise be regarded as true here:

> Plaintiffs allege that these defendants acted in bad faith .... Plaintiffs also allege that these defendants "consistently used, or allowed the use of, outdated, misleading or false estimates and assumptions of the actuarial value of the Trust Funds' actuarial assets and liabilities ..." this constituted "deliberate, willful manipulation to conceal the true financial and actuarial condition and underfunded status of the KRS Plans."
>
> Trustees and Officers willfully or recklessly violated their duties ... and did not act in good faith or in what they honestly believed was in the best interests of KRS, and its Funds when they failed to: (i) adequately safeguard the trust funds under their control; (ii) procure adequate fiduciary insurance; (iii) invest the trust assets prudently, (iv) avoid excessive and/or unreasonable fees and expenses; (v) use realistic estimates and assumptions regarding the actuarial condition and future investment returns of the funds; (vi) adequately match the assets and liability of the funds; (vii) failed to protect and assure KRS' full legal rights, including the right to sue in Kentucky state court, in open proceedings, with a jury trial, if KRS's legal rights were violated by others — especially by sophisticated out-of-state sellers of investment products who might try to limit or eliminate KRS' legal remedies; or (viii) make truthful, complete, accurate disclosure of, or a fair presentation of, the true financial and actuarial condition the KRS Funds and Plans as is detailed in this Complaint.
>
> **These allegations of bad faith and willful and/or reckless misconduct — when accepted as true for purposes of considering**

a CR 12.02 motion — allow Plaintiffs to sue ….

Nov. 30, 2018 Order at 14–15.

V. THIS CASE IS NOT THE SAME AS THE AG'S CASE

Defendants insist that only the AG should be allowed to sue them. Leaving aside the obvious rejoinder that they aren't entitled to hand-pick their preferred plaintiff/opponent — **of course they would like to avoid a two-front war and get rid of all these claims as quickly as possible**. But the two cases, as noted above, arise from completely different, indeed competing, allegations and premises. The central premise of this breach-of-trust case is that the KRS Board, as sole Trustee, is a core wrongdoer who breached its trust duties and that the Defendants participated with and/or aided in these breaches. The AG, who by law is "the chief law officer" and "the legal adviser" to KRS, has *not* alleged that KRS or its Board is committed wrongdoing or is guilty of breach of trust. *This distinction makes a huge difference* in how the respective cases are prosecuted and, quite likely, in their ultimate results. **In this case**, **the KRS Board's wrongdoing provides the legal basis for the beneficiaries to bring a direct action for breach of trust against the Trustee and/or those who participated in the breaches**. **In the AG's case**, **the Board's wrongdoing provides the legal basis for the Defendants' powerful *in pari delicto* defense** (**which is not available to them in this case**).[21]

[21] Thus, the evidence and presentation at trial will be vastly different. We will only have to prove the sole Trustee was guilty of breach of trust, then prove that each Defendant (a) had notice of such breach of trust and (b) participated in it or aided and abetted the Trustee. In contrast, the AG alleges that a group of *individual KRS trustees*, not the KRS Board as a whole acting in its role as sole Trustee, were the central wrongdoers. *See*, *e.g.*, Amended Intervening Complaint ("AIC") ¶ 237, which alleges that "Trustees, by the actions and inactions alleged herein, acted in a willful, wanton or reckless manner and breached their statutory, trust, common law and fiduciary duties to

The separate cases are fundamentally different in other ways.

First, **the parties Plaintiff are not the same**. The AG declined for months to specify his precise role in the litigation — *Parens patriae*? Counsel for KRS? Counsel for the taxpayers? Other? However during a hearing conducted in *Commonwealth v. KKR & Co., L.P.*, Case No. 17-CI-01348, on March 10, 2022, counsel for the AG definitively announced that **he does not represent KRS**. This new development has important implications.[22]

One implication of the AG's announcement is that the "field" that the OAG purports to "occupy" has shrunk. While the AG remains situated to recover damages for and on behalf of the state treasury, he, now having disavowed any representation of KRS, is not in a position to even seek, let alone recover, the "trust damages."[23]

The AG does not and cannot represent the Tier 3 beneficiaries,[24] private parties whose interests are different from and in conflict with the interests of the state treasury,

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… KRS [*i.e.*, the Trustee] …." Thus, the AG will have to demonstrate that the *individual KRS trustees* he has sued are responsible for the harm, then tie each Defendant to the acts or omissions of one or more of these individual KRS trustees. **At trial**, **the evidence**, **argument and jury charge** (**including any comparative fault question**) **will be very different**. These are not small things.

[22] *See* Plaintiffs' Supplemental Submission Regarding New Development filed herein on April 7, 2022, in which we discuss the effects of the AG's announcement that his office does not represent KRS/KPPA, including the substantial probability that the AG will not be able to recover damages to the trust corpus, *i.e.*, "trust damages." Significantly, no party has attempted to dispute this conclusion.

[23] By "trust damages" we mean losses suffered by the KRS trust corpus, which we allege were caused by the sole Trustee's breaches of trust and/or the participation by the third-party defendants in those breaches of trust.

[24] The AG unequivocally stated in a prior hearing in Case No. 17-CI-01348 that it was not acting in a *parens patriae* capacity. Nor could it, for many reasons. How, for example, could the Commonwealth act as *parens patriae* to protect the interests of citizens who have been harmed by an arm of the Commonwealth — and who are already acting to protect their own interests?

i.e., "the Commonwealth, the body politic," to which the AG owes its "primary obligation."[25] The AG cannot and does not represent the distinct interests of the Tier 3 members/beneficiaries. The Tier 3 members/beneficiaries have interests different from — and in some ways in conflict with — the interests of "the Commonwealth, the body politic," to which the AG owes his "primary obligation." *Commonwealth ex rel. Hancock v. Paxton*, 516 S.W.2d 865, 868 (Ky. 1974). The AG cannot represent — or embody — conflicting interests.

And the AG cannot, as a matter of legal metaphysics, represent the Trusts directly as trusts are not legally capable of retaining counsel or bringing suit. This is in part because Trusts such as the KRS Trusts are not separate legal persons, not distinct entities and as such are not entitled to sue in their own name or retain their own counsel. *See, e.g., Raymond Loubier Irrevocable Trust v. Loubier*, 858 F.3d 719, 731 (2d Cir. 2017) ("[t]raditional trusts] have no distinct judicial identity allowing them to sue or to be sued in their own names"). So, it is now clear that the part of the "field" where "trust damages" reside is **not** "occupied" by the AG.[26]

Defendants cannot show that they would be prejudiced by the pendency of the two cases before this Court, which will be in a position to prevent a true double recovery and to manage the cases in an equitable manner.

Second, **the Defendants are different**. The Defendants here are different from those in the AG's suit. This case does not name former KRS trustees because, again,

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[25] *See Commonwealth ex rel. Beshear v. Bevin*, 498 S.W.3d 355, 363 (Ky. 2016).

[26] Even if the AG decided to represent KRS, the field would not be pre-emptively occupied, as the AG is without power to "take" private claims (*i.e.*, the Tier 3 claims) simply so he may take control over those private claims and prosecute them with his own contingent fee counsel. That would be an unconstitutional abuse of sovereign authority.

our focus is on Board action, not actions by individual trustees. This case sues the current CEO/ED of the Trustee, David Eager, whose involvement in the alleged breach of trust and conspiracy and aiding or abetting from 2016 forward is detailed in the Complaint (*see* ¶¶ 11, 180–183), and Adam Tosh, a former Chief Investment Officer of the Trusts, who was intimately and corruptly involved in the Black Box purchases in 2010-2011 as is detailed in the Complaint. *See* ¶¶ 53–55. It sues Michael Rudzik, the Kentucky-based KKR Prisma partner who was placed inside the Trust's operations in violation of KRS's Conflict of Interest rules, where he self-dealt in Trust assets for KKR/Prisma. *See*, *e.g.*, ¶¶ 11, 57, 74–78, 108–124. Finally, it includes as a defendant Ice Miller (fiduciary counsel to the Trustee), against whom Judge Shepherd has upheld the allegations made previously (repeated and expanded on here). *See* Nov. 30, 2018 Order at 19–20, 26–29. The AG has sued 27 defendants. But he did not sue Eager or Tosh. Nor did the AG sue the Trust's "fiduciary counsel," Ice Miller or Rudzik, both insured deep pockets.

Third, the factual allegations of wrongdoing in the two cases while similar are far from identical. The AG's complaint does not plead at all the 2020–21 wrongdoing where the Trustee's CEO/ED Eager corruptly procured and helped write a purported "independent" investigative report in an apparent attempt to exonerate himself and his alleged co-conspirators, wrongdoing alleged in detail here. ¶¶ 79, 180–183, 326–351. Nor does the AG allege the 2015–16 wrongdoing involving current or former officers of the Trustee, *i.e.*, Eager, Peden *et al.*, as well as Cook, Rudzik, and KKR Prisma where the Trustee took a bribe/improper inducement ("free services") disguised as a "Strategic Partnership" with a so-called Advisory Services Agreement to let KKR/Prisma self-deal in Trust assets, in anywhere near the detail pleaded here. ¶¶ 11,

74–79, 123–24, 185–88, 289–325. The AG does not address the Calcaterra cover-up at all.

Fourth, **the AG's case is endangered by an existential threat — the jurisdictional challenge the Court of Appeals has agreed to hear**. The AG chose to intervene in the dismissed *Mayberry* case and take it over by copying the *Mayberry* complaint as his own. The defendants have long insisted there was no existing case to intervene into, because (they argue) the *Mayberry* Plaintiffs never had constitutional standing and thus the Court never acquired subject matter jurisdiction. They now appear poised to succeed. This threat to the AG's case just grew much more ominous with the recent ruling of the Court of Appeal where it will hear and decide the defense claims of lack of jurisdiction. *See KKR & Co., Inc. v. Mayberry*, No. 2021-CA-1307-MR, Order, at 5 (Ky. Ct. App., June 6, 2022). This case-threatening issue is now to be decided by an appellate court and is then subject to further review by the Supreme Court. This sword of Damocles threatening the existence of the AG's case — this existential threat to the AG's case is not going away anytime soon.

Fifth, **the AG's claims are subject to unique defenses**. Even assuming the AG's case is not dismissed for lack of jurisdiction, the two separate actions are subject to *different defenses*. According to the Defense Motions to Dismiss, the AG's claims are subject to unique "Direct Action Defects, Deficiencies, and Defenses" including contract, causation, damages (ripeness), statute of limitations, and imputation of knowledge/conduct, *i.e.*, *in pari delicto* defenses.

None of these unique defenses are available to defeat or diminish the value of the breach-of-trust claims asserted by the Tier 3 trust beneficiary Plaintiffs, who had nothing to do with the operation and mismanagement of the Trusts, the years of false statements

and reassurances by the Trustee, the purchase of the Black Box Hedge Funds, the 2015-2016 turnover of the entire hedge fund portfolio to KKR etc., the contracts entered into by the Trustee which gave away or compromised the Trustee's legal rights and remedies or the decade long underfunding of the Trusts by the State, actions which the Defendants assert were the real causes of the KRS financial fiasco and any damage to its funds, and/or entirely defeat the Trustees' and Commonwealth's direct claims.

Sixth, **the relief sought is not the same**. While the damages sought in the two cases might or might not overlap, they are *different* regarding theory, amount and recoverability, to an extent that could have a huge impact on the value of the respective claims. **It is questionable**, **even doubtful**, **that the AG will be able to reach the** "**trust damages**" **as his case is currently postured**.[27]

KRS, in its role as a "statutorily created agency of state government," is an "arm, branch, or alter ego" of the Commonwealth, and is its agent. The Commonwealth can no doubt stand in for KRS *qua* state agency. But the KRS Board in its role as sole Trustee of the KRS trusts is different; it is charged with "sole interest" and "exclusive purpose" fiduciary duties that cannot be diluted. The Trustee is not the Commonwealth and the Commonwealth is not – and cannot stand in for — the Trustee. Therefore, the AG's announced decision not to represent KRS leaves a gap in his damages case.[28] **The only persons potentially entitled to sue for the** "**trust damages**" **are the trustee and**

[27] By "trust damages" we mean losses suffered by the KRS trust corpus, which we allege were caused by the sole Trustee's breaches of trust and/or the participation by the third-party defendants in those breaches of trust. *See* footnotes 22–24 above.

[28] There may be several reasons for this declination. One may be that the AG is trying to avoid the *in pari delicto* defense. Another may be that the AG's access to the Calcaterra Report prior to filing his Amended Complaint is problematic. But the reason doesn't matter, only the announced decision not to represent KRS does.

the beneficiaries, **and the AG represents neither**. In this situation involving trusts, the Commonwealth as such is an interested outsider.

There may be other differences involving recoveries. A jury may be much less likely to award punitive damages to the culpable conspiring Trustee than to innocent victims, *i.e.*, Tier 3 trust beneficiaries. Judge Shepherd has already held the facts as alleged here may justify punitive damages. Nov. 30, 2018 Order at 32. The presence of a credible punitive damage threat is very important to enhance the settlement value of the claims.

Finally, the two cases seek to put money in different pockets. The Tier 3 Trust Plaintiffs, unlike the AG, have no interest in recovering funds to go into the state treasury, where any recovery by the AG must go. By contrast, the Tier 3 Trust Plaintiffs will seek to have portions of the net recovery allocated to the "upside sharing" element of their plans. The AG, who is required to deposit any recovery in his case in the state treasury, has shown no interest in doing this, and it would likely conflict with the taxpayer interests he represents if he did.

VI. WHAT TO DO NEXT IN THESE CASES

To move forward, the Tier 3 Trust Plaintiffs request that the Court **not sign** the proposed protective order, *i.e.*, the seal-and-secrete order extracted by the Defendants from the AG in his case, open discovery in this case while denying Defendants' motions to dismiss this case, grant the Tier 3 Trust Plaintiffs' pending motion that no protective order be entered in this case, and grant their pending motion for an accounting by the Hedge Fund Defendants of their financial dealings with the KRS Trusts.

The AG's willingness to slow-walk his jurisdictionally dubious case — agreeing to a long continuance of a scheduled status conference — should not impact this separate case as to which there is no jurisdictional defect and which the Tier 3 Trust Plaintiffs are

ready to prosecute now. In fact, in light of the endangered status of the AG's case, the best course of action may be to abate it pending a final resolution of the jurisdictional challenge and allow this case to go forward. If and when the AG's case survives the appellate proceedings, the AG can have access to the discovery produced in this case. The Tier 3 Trust Plaintiffs are ready to prosecute this case now — in the open and on the merits.

The Tier 3 Trust Plaintiffs have served discovery requests — interrogatories and document production requests — on all Defendants. They have all refused to comply. Defendants have refused to produce a single document. Yet they are giving documents to the AG with a promise of secrecy. In light of these circumstances, the Tier 3 Trust Plaintiffs request that Defendants be required to comply with their discovery requests now, while the motions to dismiss are pending, under circumstances that assure maximum public access to all discovery materials in this case.

The Court should direct Defendants (who are fiduciaries to the Trusts and their beneficiaries) to comply with the Tier 3 discovery requests without any assertion of attorney-client privilege or trade secret claims or other devices to evade their disclosure obligations.[29] Looting a trust does not involve "trade secrets" or "sensitive" or

[29] Judge Shepherd has already ruled in the context of denying Ice Miller's Motion to Dismiss that due to the fiduciary nature of KRS's relationships with its members that there is no attorney-client privilege. *See* Nov. 30, 2018 Order at 19–21; *see also Durand v. Hanover Ins. Grp.*, 244 F. Supp. 3d 594 (W.D. Ky. 2016), for a comprehensive discussion of the fiduciary exemption and why for an ERISA litigation, *i.e.*, pension fund fiduciary suits like these breach-of-trust claims there is no attorney-client privilege. This is consistent with a well-established body of law that there is no attorney-client privilege available in well-pleaded litigations involving fiduciaries' breaches. *See*, *e.g.*, *Garner v. Wolfinbarger*, 430 F.2d 1093 (5th Cir. 1970); *Wal-Mart Stores, Inc. v. Ind. Elec. Workers Pension Trust Fund*, 95 A.3d 1264, 1276–78 (Del. 2014); *Nama Holdings, LLC v. Greenberg Traurig LLP*, 133 A.D.3d 46 (N.Y. App. Div. 1st Dep't 2015); *see also The Shareholders' Derivative Claim Exception to the Attorney Client Privilege*, 48 LAW & CONTEMPORARY PROBLEMS NO. 3 at 199 (Duke Univ. 1985); *Riggs Nat'l Bank v. Zimmer*,

"confidential" business information and there is no attorney-client privilege in this type of breach-of-trust suit.

The Calcaterra report (and all drafts) should be made public immediately. Concealing an investigation into wrongdoing at a public fund, paid for with public funds, cannot be justified. Plaintiffs' discovery requests seek production of this report.

In addition to moving for no protective order in this case, the Tier 3 Trust Plaintiffs have also moved for an accounting by the Hedge Fund Sellers. *See Taylor v. KKR & Co., L.P.*, No. 21-CI-00645, Memorandum in Support of the Tier 3 Trust Plaintiffs' Motion for Accounting (Ky. Cir. Ct. Franklin Cnty. Aug. 31, 2021). The motion for an accounting focuses on fees and transparency. The Tier 3 Trust Plaintiffs requested that Prisma/KKR & Co., PAAMCO and Blackstone/BAAM[30] each render and file with the Court a complete accounting of all management fees, performance fees, expenses and other funds paid to itself or any related persons or entities, and all management fees, performance fees, expenses and other funds paid to each of the underlying hedge funds in which it invested KRS funds. In addition, each of them should be required to render a cash-basis accounting of all funds received from KRS, and all funds returned to KRS (whether as return of capital, profits or otherwise). Each should also be made to account for any benefit it received from or related to any of the underlying hedge funds, including but not limited to returns from seeding any such hedge funds.

355 A.3d 79 (Del. 1976); *In re Kipnis Section 3.4 Trusts*, 329 P.3d 1055 (Ariz. Ct. App. Div. 1 2014); RESTATEMENT (THIRD) OF TRUSTS § 82 (2005).

[30] Prisma Capital Partners, L.P., Pacific Alternative Asset Management Company, LLC, and Blackstone Alternative Asset Management, LLC.

KRS consistently understated the fees paid in connection with its hedge fund investments by as much as $25–50 million, or more, each year. The full measure of these fees has never been publicly disclosed or accounted for. Such an accounting is justified simply by the fact that many millions of dollars in public funds have been and will continue to be expended to support this public employee retirement plan; there is, in other words, a need for an accounting independent of any other justification. But it goes beyond that. The fees were so large that they must be viewed as a waste of trust assets, which is perhaps why KRS management has so long kept them hidden. And, the magnitude of the fees, when finally disclosed, will give the lie to the Hedge Fund Sellers' primary defense — that they performed as advertised and expected. This should all be public as well.

VII. DISMISSING OR ATTEMPTING TO EXTINGUISH THESE PRIVATE DAMAGES CLAIMS IN FAVOR OF OR VIA A SETTLEMENT OF THE AG'S CASE WILL RAISE SERIOUS CONSTITUTIONAL ISSUES AND PREVENT FINALITY

The AG has a proper role in attempting to remedy the misconduct Judge Shepherd condemned and said must be pursued "on the merits." He can seek damages for the taxpayers, to be deposited in the State treasury. However, the AG is not an "Angel General" — who descends to adequately represent *every* legal claim of *every* person in Kentucky — in *every* capacity, *to the exclusion of all separate private claims*. To grant such a broad reach to the AG — and/or give his actions such preclusive effect — assures serious constitutional due process problems. These problems will be eliminated by allowing this case to go forward.

Lawsuits by Attorneys General that seek preclusive effect in connection with the claims of others raise significant due process issues. Attempts to prosecute and then

extinguish claims of broad groups of claimants and interests require vigorous *separate* representation of differing claims and interests *at all times during the litigation process*. Not every citizen of the state has the same interests or claims respecting an overlapping set of complex facts unfolding over some 20 years that damaged many individuals and groups. And every citizen has due process rights to litigate claims belonging to him[31] — especially claims involving *property* interests that are unique from or potentially in conflict with claims "for all the people." *See In re Payment Card Interchange Fee and Merchant Discount Antitrust Litig*., 827 F.3d 223 (2d Cir. 2016). The conflicts inherent in the many "hats" worn by the AG are of constitutional dimension if, and to the extent, claim preclusion is sought. *Id*; *see also,* Margaret H. Lemos, *Aggregate Litigation Goes Public: Representative Suits by State Attorneys General*, 126 HARV. L. REV. 486 (2012).[32]

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[31] "[A] cause of action is a species of property protected by the Fourth Amendment Due Process Clause." *Logan v. Zimmerman Brush Co*., 455 U.S. 422, 428 (1982). This is grounded in "our deep rooted historic tradition that everyone should have its own day in court." *Martin v. Wilks*, 400 U.S. 755, 762 (1989). In addition to their constitutional standing and ability as trust beneficiaries to sue, the Plaintiffs have vested property interests in **their** KRS accounts/benefits held in the Trusts.

[32] This scholarly article discusses the conflicts and serious constitutional issues raised when state attorneys general attempt to bring claims that subsume private suits or enter into "global" (*i.e.* state wide) settlements, extinguishing the litigation claims and rights of its citizens – whether they have been asserted individually or not. It suggests that to permit the AG to sue for every person in Kentucky — all claims — direct/derivative or otherwise and/or to extinguish those claims will create a constitutional morass that would plague these litigations for years. *See Satsky v. Paramount Comm'ns*, 7 F.3d 1464, 1470 (10th Cir. 1993) (state settlement of claims of environmental discharge violations which included comprehensive relief and money damages could not bar individual damage suits by impacted owners of private property because they are "purely private interests which the state cannot raise"). In *Engle v. Liggett Group, Inc.*, 945 So.2d 1246, 1261 (Fla. 2006), the Florida Supreme Court wrote:

> We agree with the reasoning of *Satsky* and with the principle that "litigation by a government agency will not preclude a private party from vindicating a wrong that arises from related facts but generates a distinct individual cause of action."

Judge Shepherd has ruled that the AG's suit is in substance, and will be treated as, a class or representative action. He said the AG's suit raises "the same concerns regarding fairness, notice and the opportunity to be heard that are addressed for class actions in CR 23.05. The due process concerns, codified for class actions in CR 23.05, apply with equal force to the compromise or dismissal of any claims in [the AG's] action." *Commonwealth v. KKR & Co. L.P.*, No. 17-CI-01348, slip op., at 1 (Ky. Cir. Ct. Franklin Cnty. Sept. 21, 2021). No secret settlements are permitted under this order.

For present purposes it is sufficient for the Court to be aware of *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591 (1997); *Ortiz v. Fiberboard Corp.*, 527 U.S. 815 (1999); *Payment Card*, 827 F.3d 223; and *In re Literary Works in Electronic Databases*, 654 F.3d 242 (2d Cir. 2011). These cases impose very formidable due process barriers to "global" settlements of representative suits impacting related, overlapping, competing/claims or cases arising from shared facts.

Payment Card voided a $7.2 billion settlement achieved after 10 years of litigation. The settlement had been negotiated with the active involvement of experienced and respected mediators and the two district court judges involved. 400 depositions, 32 days of expert depositions and the production of 80 million pages of documents, had occurred. However, the claims extinguished by the "global" settlement had received "*unitary representation*," from several law firms that had been appointed by the court as "class counsel." That unitary representation was held as a matter of law to be inadequate representation of the competing and conflicting claims settled within the "global" settlement. That unitary representation violated the due process rights of individuals with claims released by that settlement. The settlement was voided on their objection.

What matters at the end of the day is **not the size of overall recovery**, **or even its overall fairness or its allocations — what matters is whether distinct interests and claims were separately and adequately represented throughout**.

> "Adequacy must be determined independently of the general fairness review of the settlement; the fact that the settlement may have overall benefits for all class members is not the 'focus' in the 'determination whether proposed classes are sufficiently cohesive to warrant adjudication.'"
>
> * * *
>
> One aspect of the Settlement agreement that emphatically cannot remedy the inadequate representation is the assistance of judges and mediators in the bargaining process .... even "an intense, protected, adversarial mediation, involving multiple parties" including "highly respected and capable" mediators and associational plaintiffs, does not "compensate for the absence of independent representation." *Literary Works*, 654 F.3d at 252–53. The mission of mediators is to bring together the parties and interests that come to them. It is not their role to advance the strongest arguments in favor of each subset of class members entitled to separate representation, or to voice the interests of a group for which no one else is speaking.

Payment Card, 827 F.3d at 232, 234.

The fact that two lower court judges had actually **participated in the settlement negotiations in Payment Card and approved the settlement allocations** as fair and equitable and that the plaintiffs' lawyers had been diligent and honest and all involved had acted in good faith did not matter. Going forward with the suit with unitary representation and creating a "global" resolution without separate representation and advocacy forced on them all an inherently "*inequitable task*" that doomed the entire decade of litigation and $7.2 billion settlement regardless of that huge recovery and its overall fairness.

This case is high-profile, with many eyes on it. The presence of the Tier 3 Trust Plaintiffs and their counsel in prosecuting these overlapping, but conflicting, claims will

provide an assurance of a no-holds-barred prosecution of the case without any fear of political influence. The process and result here must be — and must be seen as — honest and above-board. To ensure public confidence in the ultimate result, the appearance of impropriety must be guarded against.

The known facts here portend, if nothing else, a serious appearance-of-impropriety issue. Commentators have noted that Steven Schwarzman — who individually is a Defendant in the AG's case (and ours as well) — "is one of the largest financial supporters of Mitchell McConnell and Donald Trump's political machine."[33] **Schwarzman alone gave at least $35 million to Senator McConnell's Senate Leadership Fund during the 2020 cycle**, **and he gave the same McConnell PAC at least $10 million in the first quarter of this year**.[34] And Schwarzman may have donated anonymously (*via* a McConnell-connected "dark money" fund) to Cameron's campaign for AG.[35]

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[33] *See, e.g.*, Peter Castagno, *Landmark Wall Street Scandal Implicates Top Trump & McConnell Donor,* CITIZEN TRUTH (July 23, 2020), *available at* https://citizentruth.org/leaked-fbi-memo-reveals-no-intel-indicating-antifa-involvement-in-sundays-violence/.

[34] *See* https://www.factcheck.org/2022/03/senate-leadership-fund-3/ and https://www.chicagobusiness.com/government/trumps-small-dollar-donors-fuel-19-million-first-quarter-haul.

[35] 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.

Other Defendants, chiefly but not only Henry Kravis, are also mega donors to Republican/McConnell PACs and super-PACs, even if not at Schwarzman's level.[36]

It is no secret that AG Cameron is closely tied to the McConnell political operation. As the Associated Press noted when the AG announced his candidacy for the governorship: "Cameron … has close ties to the Bluegrass State's most powerful Republican — U.S. Senate GOP leader Mitch McConnell — and once served as the senator's legal counsel."[37] AG Cameron's candidacy for the governorship only adds another layer of political intrigue.

That Schwarzman has personally given tens of millions of dollars to the McConnell operation, and that the AG is tied to if not beholden to the McConnell operation, are simple facts. This is not speculation. The dots are there to be connected, which pretty well defines "appearance of impropriety."

This confluence of unimaginable political money and undeniable political self-interest has the potential to create an unbelievable political firestorm. Any suggestion that the AG has cut Schwarzman, Kravis or the other Wall

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[36] Employees at both Blackstone and KKR are huge contributors to McConnell's political operations:

> Boosted by big bundles of Wall Street contributions, Senate Majority leader Mitch McConnell's reelection committee took in more than $3 million during the recent quarter that ended June 30.
>
> The biggest blocks of contributions during the period came from two global financial services firms based in New York: 29 people with Blackstone Group made contributions totaling $95,400; and 14 executives of KKR & Co., are listed as giving a combined $51,000.

Tom Loftus, *Wall Street Firms, Not Kentuckians, Are Leading Mitch McConnell's Campaign Donations*, COURIER JOURNAL, July 17, 2019.

[37] *See* https://apnews.com/article/2022-midterm-elections-covid-health-kentucky-mitch-mcconnell-986c9195d6a147516f7d1bd1bd7c027e.

Street titans any slack in terms of prosecution (including favorable secrecy terms) or settlement has the potential — at a bare minimum — to significantly erode public trust in the process and the outcome.

Indeed, outward appearances even now strongly suggest that the Defendants and the AG are working behind the scenes to arrange a headline grabbing "global" settlement (which will attempt to extinguish this action) without any prosecution on the merits or public disclosure of the evidence of the excessive fees, looting and gross mismanagement of the KRS Trust funds that KRS members, taxpayers and the public are entitled to — and the media will demand, when any such settlement is presented to the Court for review as "fair, just and adequate" and possible approval, as Judge Shepherd has already ruled any settlement by the AG must be.

Potential (likely) public perception of favorable treatment, combined with the previously-discussed constitutional problems that would arise from any attempt to preclude the Tier 3 claims, would be problematic in the extreme. But these problems can largely be obviated by allowing this separate action to go forward, unimpeded by any action of the AG. Doing so will actually make this Court's tasks down the road easier. By assuring vigorous independent representation of separate competing interests now, so that everyone's due process rights are honored now, if there is a global resolution later, then finality can be achieved.

VIII. COUNSEL FOR THE TIER 3 TRUST PLAINTIFFS ARE READY TO PROSECUTE THIS CASE ON THE MERITS NOW AND IN THE OPEN AS THE PUBLIC INTEREST REQUIRES

Why are Defendants providing documents to the AG while withholding them from the Tier 3 Trust Plaintiffs, when the two cases are in the same procedural stages? Why the long delay in the scheduled status conference? We suspect because the AG is going to

attempt a quick, likely cheap but headline-grabbing settlement — without prosecuting the case on the merits, while attempting to extinguish all claims in a "global settlement" and without allowing this court as well as the media, the public, taxpayers, KRS members to ever see the actual evidence of the looting and gross mismanagement that took place at KRS, evidence that must be seen and evaluated by the court to evaluate the fairness of any settlement by the AG, in a public hearing which Judge Shepherd previously ruled will be required.

The AG's case is now under serious threat for lack of jurisdiction — an issue now out of this Court's hands to be decided at some future date by Kentucky's appellate courts. The Tier 3's have in place a team to prosecute this case **now** on the merits without further delay, without any jurisdictional defect and without secrecy. The Tier 3's counsel — and their consultants and experts — are veterans of these types of huge, complex litigations. To uncover the facts and get the accounting expertise needed to uncover the details of the misconduct they alleged in the *Mayberry* Complaint, the Tier 3's counsel long ago reached out to private investigator and forensic accounting firms known for their work in financial fraud litigations. They have been involved in over 100 major financial fraud cases and virtually all of the prior billion-dollar recoveries the Tier 3's counsel have previously been involved in. To create maximum value, the breach of trust claim will also require world-class testifying experts or consultants. Again, the Tier 3's counsel have access to hedge fund, fiduciary duty and pension governance expert(s) with impeccable credentials and mega-case experience.

The Tier 3 counsel have substantial experience in prosecuting mega-cases and recovering billions of dollars — much of it for public pension funds and their trusts including successfully forcing "open proceedings" where discovery materials are made

public. This includes prior suits against some of **the same hedge fund defendants in this action, represented by the same lawyers representing them here**. It was counsel for the Tier 3's that conceived the original allegations of wrongdoing at the request of the *Mayberry* Plaintiffs, spending **months** (over a thousand hours) — developing the case concept and creating the original *Mayberry* complaint. We and our consultants, and experts created virtually **all of the substantive work in the cases before the Court**.

The AG had nothing to do with the origination of the *Mayberry* action. His private counsel have never prosecuted a case of this size and complexity. They abandoned their original clients and switched horses — if not sides — when the going got tough to aggrandize their own economic interests seeking a larger fee by representing a client with interests that conflict with those of their prior clients, taking positions adverse to them. They intervened in the dismissed *Mayberry* case and copied their prior clients' complaint as the AG's complaint.[38] By intervening in the dismissed *Mayberry* action and copying the *Mayberry* complaint as his own, the AG may have blundered his way into dismissal of his case for lack of jurisdiction. The Tier 3s and their counsel — who started the case in the first place and have soldiered on — are ready to keep fighting on the merits to get a substantial recovery for the KRS Trusts, with all the evidence being in the public domain.

The Hedge Fund Sellers are no strangers to being sued for cheating their clients. They have been repeatedly accused of breaching their fiduciary duties and paid billions to settle claims that exposed their predatory tactics. Not surprisingly, the Tier 3's counsel have encountered these folks before — and bested them. For example, in the $7.2 billion

[38] The *Mayberry* plaintiffs have reserved their rights and remedies against these lawyers for their dubious conduct.

Enron class action — the largest such recovery in history — Tier 3 counsel represented the Lead Plaintiff (Regents of the University California Pension Fund) against J.P. Morgan Chase (represented by Simpson Thacher, counsel for KKR here), and Citibank (represented by Paul Weiss, counsel for Blackstone here). After years of scorched-earth defense tactics, they were forced to pay billions. These same lawyers were again bested by the Tier 3's counsel in the *WorldCom* pension-fund "opt-out" litigation — where we represented a group of some 40–50 pension funds individually in a private suit for damages which cost Simpson Thacher's client, J.P. Morgan, hundreds of millions to settle.

In 2007, KKR and Blackstone were sued by the Tier 3's counsels' then firm **on behalf of public pension funds** and others for conspiring to restrain competition and fix prices (keep them low) in "going private" buyouts they engineered, cheating their pension fund clients whose investments included stock in buyout targets. KKR and Blackstone condemned the suit as "preposterous." They tried to keep incriminating e-mails secret. But discovery proved a **conspiracy** alleged, led by KKR and Blackstone to **cheat** in going-private deals by fixing a low price and then dividing the spoils. Once the court ordered key emails made public, KKR and Blackstone settled. The result was a $590 million recovery. Simpson Thacher — counsel for KKR here — represented both the conspirators Blackstone and KKR in the private equity price-fixing case.

In almost all these mega-cases, there have been related suits/prosecutions by government entities — the SEC, FDIC, the DOJ. Where wrongdoers injure large groups of victims, investors and pension systems and their beneficiaries and the like, suits by multiple private parties (direct or representative) **and** by governmental regulators or prosecutors are routine. Having the prosecution of such cases spearheaded by the strongest case on the facts and the law, prosecuted by lawyers who investigated the case

and first pleaded it, and have both the case-specific knowledge and the specialized experience required and a strong supporting team of consultants and experts — with the evidence open to the public — normally achieves the best result.

IX. CONCLUSION

Experience teaches one thing — the sooner Defendants, all fiduciaries to the Tier 3 trust beneficiary Plaintiffs, account for their financial dealings with the KRS Trusts and produce documents that will prove their predatory conduct and self-dealing, the sooner these matters will be resolved, benefiting the "public interest."

Dated: June 13, 2022

Respectfully submitted,

s/ Michelle Ciccarelli Lerach

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The above signature certifies that, on June 13, 2022, the foregoing was served via email in accordance with any notice of electronic service or, in the absence of an electronic notification address, via email or mail as indicated below, to:

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EXHIBIT A

EXHIBIT A

COMMONWEALTH OF KENTUCKY
FRANKLIN CIRCUIT COURT
DIVISION I
CIVIL ACTION NO. 17-CI-1348

JEFFREY C. MAYBERRY, *et al.* **PLAINTIFFS**

v. **OPINION & ORDER**

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

This matter is before the Court on Defendants' Motions to Dismiss. The parties appeared before the Court on August 23, 2018 to argue the matter. At that time, the plaintiffs were represented by Ann Oldfather, Vanessa Cantley, Michelle Lerach, Johnathan Cuneo, and Abe Kucjaz. The following counsel appeared on behalf of the defendants listed: Philip Collier and Jefferey Moad for R.V. Kuhn & Assocs., Inc., James Voytko, and Rebecca Gratsinger ("RVK Defendants"); Robert Brazier and Charles English, Jr. for Cavanaugh MacDonald LLC, Thomas Cavanaugh, Todd Green, and Alisa Bennett ("CavMac Defendants"); Cory Skolnick, Margaret Keeley, and Ana C. Reyes for Ice Miller LLP ("Ice Miller"); Dustin E. Meek and Melissa M. Whitehead for the Government Finance Office Association ("GFOA"); Donald Kelly, Virginia Snell, Jordan White, Brad S. Karp, Lorin L. Reisner, Andrew J. Ehrlich, and Brette Tannenbaum for Blackstone Asset Management LP ("BAAM"), Blackstone Group LP ("Blackstone"), Stephen Schwarzman, and J. Tomilson Hill; Barbara Edelman, Grahmn Morgan, and Barry Barnett for KKR & Co. L.P., Henry Kravis, and George Roberts ("the KKR Defendants"); Barbara Edelman, Grahmn Morgan, and Paul C. Curnin for Prisma Capital Partners LP ("Prisma"), Pacific Alternative Asset Management Co., LLC ("PAAMCO"), Jane Buchan, and Girish Reddy; Glenn Cohen and Lynn Watson for William Cook; David Guarnieri and Kenton Knickmeyer for David Peden; Sean Ragland for Jennifer Elliott; Richard Guarnieri for Bobby Henson and Randy

Overstreet; Mark Guilfoyle for Thomas Elliott; John Dwyer for Tim Longmeyer; Mel Camenisch, Jr. for T. J. Carlson; Kevin Fox for William Thielen; Brent Caldwell and Noel Caldwell for Vince Lang; and Christopher Schaefer and Sarah Bishop for nominal defendant Kentucky Retirement Systems ("KRS"). Plaintiffs Jeffrey Mayberry, Brandy O. Brown, Martha M. Miller, and Ben Wyman were also present.

Also before the Court is the Motion to Defer Ruling on Plaintiffs' Lack of Standing Until Finality of Recent Supreme Court Opinion That Would Compel Dismissal, filed by Defendants Blackstone and BAAM. Defendants PAAMCO, Prisma, the KKR Defendants, the RVK Defendants, Ice Miller, and the GFOA have also joined in this Motion. By Order dated November 14, 2018, the Court permitted Plaintiffs to file a responsive memorandum. Upon receipt of the plaintiffs' memorandum, the matter was taken under submission and is addressed herein in the Court's analysis on standing.

Accordingly, having considered the arguments of counsel and being otherwise sufficiently advised, the Court hereby rules as follows:

BACKGROUND

Plaintiffs are several members of the Kentucky Employees Retirement Systems ("KRS"), suing both derivatively and as taxpayers on behalf of the Commonwealth. They allege that several trustees and officers of the Kentucky Employees Retirement Systems ("KRS") breached various duties owed to its members and ultimately depleted KRS's pension funds by investing in high-risk hedge funds. It is also alleged that certain entities including actuarial and investment advisors, hedge fund sellers, and their executives similarly breached duties owed to KRS and its public employee members and aided and abetted the breaches of the trustees and officers. In addition, all defendants are accused of participating in a joint enterprise or civil conspiracy to breach various

fiduciary duties and enrich certain defendants at the expense of KRS and its public employee members. More specifically, Plaintiffs assert the following causes of action in their First Amended Complaint: Breach of Trust and Fiduciary Duties (Count I); Breaches of Statutory, Fiduciary, and Other Duties (Count II); Joint Enterprise and/or Civil Conspiracy (Count III); Aiding and Abetting Breaches of Statutory, Fiduciary, and Other Duties (Count IV); and Punitive Damages (Count V). Plaintiffs seek monetary damages, as well as declaratory and injunctive relief.

In response, several defendants joined to file a Consolidated Motion to Dismiss, arguing that Plaintiffs lack standing to sue, either derivatively or as taxpayers. In addition, most defendants filed separate motions to dismiss, asserting a variety of defenses, including lack of personal jurisdiction, lack of subject matter jurisdiction, immunity, statutes of limitations, and failure to state a claim. Many, if not all, of these defenses are asserted and briefed by multiple defendants. Accordingly, the Court issued an agenda outlining the various topics for oral argument and will now address each issue in the same order that they were argued on August 23, 2018.

STANDARD OF REVIEW

When a court considers a motion to dismiss under Kentucky Rule of Civil Procedure ("CR") 12.02, "the pleadings should be liberally construed in a light most favorable to the plaintiff and all allegations taken in the complaint to be true." *Gall v. Scroggy*, 725 S.W.2d 867, 869 (Ky. App. 1987) (citation omitted). Thus, the Court should only grant a motion to dismiss when it "appears the pleading party would not be entitled to relief under any set of facts which could be proved in support of his claim." *Mims v. Western-Southern Agency, Inc.*, 226 S.W.3d 833, 835 (Ky. App. 2007) (quoting *James v. Wilson*, 95 S.W.3d 875, 883–84 (Ky. App. 2002)).

ANALYSIS

I. Standing

In their First Amended Complaint, Plaintiffs bring suit as members of KRS "pleading a member/beneficiary derivative action for [KRS] and its trust funds," and as taxpayers bringing a taxpayer action on behalf of the Commonwealth. *See* First Am. Compl. 1. In response, Defendants filed a Consolidated Motion to Dismiss, asserting lack of standing. After oral argument on the various Motions to Dismiss, Defendants BAAM and Blackstone filed a Motion to Defer this Court's ruling on the issue of standing. More specifically, the defendants asked this Court to stay the matter until a recent Kentucky Supreme Court decision, *Commonwealth of Kentucky, Cabinet for Health and Family Services v. Sexton*, 2016-SC-000529 (Ky. Sept. 27, 2018), becomes final. That decision, Defendants allege, makes clear that Plaintiffs lack constitutional standing.

For the reasons set forth below, the Court finds that Plaintiffs have standing to bring this suit, both derivatively and as taxpayers. The Motion to Defer and the Consolidated Motion to Dismiss, as well as the separately filed Motions to Dismiss, will therefore be denied to the extent they argue lack of standing.

a. Plaintiffs allege a concrete injury and satisfy the test for constitutional standing as stated in *Sexton*.

In *Sexton*, the Supreme Court of Kentucky considered "whether the courts of Kentucky can undertake a statutorily created judicial review of an administrative agency's final order when the person appealing that final order does not have a concrete injury." *Sexton*, slip op. 2. It ultimately concluded that "the existence of a plaintiff's standing is a constitutional requirement to prosecute any action in the courts of this Commonwealth," and it formally adopted the *Lujan v. Defenders of Wildlife*, 504 U.S. 555 (1992) test for standing. Under the *Lujan* test, the plaintiff must have

suffered an "injury in fact" which he or she can causally connect to the conduct at issue. *Lujan*, 504 U.S. at 560–61. The injury must be "concrete and particularized" and "either actual or imminent." *Sexton*, slip op. at 2 (quoting *Lujan*, 504 U.S. at 560). The *Sexton* Court further clarified that a case is considered nonjusticiable if the plaintiff lacks an injury in fact, or otherwise lacks constitutional standing.

Applying this test, our Supreme Court found that the plaintiff in *Sexton* lacked a concrete injury and, as a result, lacked constitutional standing. Sexton, a Medicaid beneficiary, sought medical treatment at a hospital, but the relevant managed-care organization would not preauthorize certain services. Due to the life-threatening nature of Sexton's condition, the hospital proceeded with the medical treatment, and the managed-care organization then denied reimbursement. The hospital acted as Sexton's representative to ultimately bring suit in circuit court. On appeal, the Supreme Court characterized Sexton as "the true plaintiff" in the suit and found that Sexton had not been "injured" for purposes of standing. The Court noted that Sexton received the medical treatment that she sought and needed. The hospital, not Sexton, sought reimbursement for those services, and Sexton therefore also lacked a financial interest in the dispute. Thus, the "true injuries" in the case involved losses suffered by the hospital, namely, unreimbursed medical expenses. *Id*. at 22. The remedy—reimbursement—would make the hospital whole but would have no effect on Sexton. In other words, regardless of the outcome of the case, "Sexton would be no better or worse off." *Id*. at 21. The Court therefore found that Sexton lacked the particularized injury necessary to establish standing.

The *Sexton* decision was rendered on September 27, 2018 but is not yet final. Defendants therefore ask this Court to defer ruling on the issue of standing until the decision is final, at which time the Court should apply the same analysis to find that Plaintiffs in the present matter also lack

standing. More specifically, Defendants argue that (1) KRS's financial loss is not a concrete and particularized injury suffered by the individual plaintiffs; (2) even if they have suffered a sufficient injury, Plaintiffs cannot establish causation between that injury and the defendants' conduct; and (3) that injury is unlikely to be redressed by the recovery sought because any damages will be paid to the Commonwealth, rather than directly to KRS.

However, the Court finds the present suit distinguishable from *Sexton*. In the *Sexton* case, an entity (the hospital) sought to enforce the rights of an individual (Sexton). The Court then considered whether that individual—the "true plaintiff"—suffered an injury, and it ultimately concluded that the true injuries were suffered by the entity. Here, however, these individual plaintiffs (KRS members) seek to enforce the rights of an entity (KRS) by bringing a derivative action on behalf of the entity. They also bring this suit as taxpayers seeking to enforce the rights of the Commonwealth. Thus, under *Sexton*, the Court should consider whether *KRS* and the *Commonwealth*—the true plaintiffs—suffered concrete and particularized injuries.

The injury alleged is the depletion of KRS's pension funds, which allegedly resulted from the actions of KRS's trustees, officers, hedge-fund sellers, and advisors, primarily, their breaches of fiduciary duties. While Defendants may argue that this injury is not a concrete and particularized injury suffered by the individual named plaintiffs, it is no doubt a sufficient injury suffered by the true plaintiffs: the Commonwealth and KRS. Plaintiffs have therefore demonstrated a concrete injury that satisfies the *Lujan*/*Sexton* test. These allegations also satisfy the essential element of causation, which requires only that the injury be "fairly traceable" to the alleged misconduct. *See, e.g.*, *Allen v. Wright*, 468 U.S. 737, 751 (1984) (citation omitted).

In addition, the Court finds that these individual plaintiffs have also suffered concrete and particularized injuries. These public employees paid into the defined benefit pension program, as

mandated by statute. They therefore have a vested financial interest in ensuring that the state retirement fund, which secures their retirement, is administered in compliance with the safety net of fiduciary duties designed to protect their financial interests, and those of all similarly situated members. The alleged breaches of those fiduciary duties give rise to a case or controversy in which the plaintiffs have a very real and tangible stake in the outcome. Again, the alleged misconduct of the defendants—the willful and reckless breach of duties, among other things—is alleged to be causally connected to the depletion of the retirement funds in which the plaintiffs have a property interest.

Lastly, the Court disagrees with Defendants' assertion that no redress is available. Defendants claim that the monetary damages sought by Plaintiff cannot redress the alleged injury (depletion of pension funds) because the award must be paid directly to the Commonwealth, after which the General Assembly decides its allocation. In other words, a monetary award does not automatically restore KRS's funds. However, to say that there is no redress available simply because the funds might be paid to the Commonwealth, rather than directly to KRS, is to say that there is no way to ever redress a financial loss suffered by a state agency or public entity. The Court cannot accept that argument. Instead, the Court finds that the relief sought by Plaintiffs can disgorge the defendants of inappropriately-obtained funds and restore, at least in part, the losses suffered by KRS. Plaintiffs have therefore satisfied the third element of the *Lujan* test: redressability. Accordingly, Defendants' Motion to Defer will be denied.

In their Motion to Defer, Defendants Blackstone and BAAM assert that *Sexton* "announced a sea change in Kentucky courts' approach to the determination of standing." Defs. Blackstone and BAAM's Mot. to Defer 1. At most, however, the *Sexton* decision formally adopts the federal standard of *Lujan*—an analysis already informally applied in Kentucky courts—and clarifies that

constitutional standing is a matter of justiciability. *Sexton* does not purport to alter the established derivative and taxpayer standing analyses of Kentucky's courts, and the Court therefore addresses each in turn.

b. Plaintiffs may sue derivatively as members and beneficiaries of KRS and its trust.

Typically, derivative suits arise in the context of dissenting shareholders who must first comply with various statutory requirements prior to bringing suit to enforce the rights of the corporation. *See* KRS 271B.7-400. Defendants now argue that Plaintiffs failed to comply with these statutory requirements. Specifically, Defendants point to the requirement that the shareholders first make a demand upon the board of directors under KRS 271B.7-400(2). Under that statute, the complaining shareholders must allege that the demand was refused or explain why they failed to make such a demand.

However, the Court finds that Defendants' argument fails for two reasons. First, this case is not a typical shareholder derivative suit against a private corporation. Plaintiffs are not shareholders of a private for-profit corporation; instead, they are members of KRS and beneficiaries of KRS's trust by operation of the statutes establishing Kentucky's public pension system. Accordingly, they are not bound by the precise statutorily-mandated procedures set forth for private shareholder derivative suits. Instead, their right to sue stems primarily from KRS 61.645(15), which lists the duties of the trustees and explains under what circumstances a person may sue for failure to perform these duties. *See* KRS 61.645(15)(e), (f). In addition, the Restatement (Third) of Trusts provides that a beneficiary of a trust can sue a third party when the trustee cannot or will not do so, to the detriment of the beneficiary's interest. *See* RESTATEMENT (THIRD) OF TRUSTS § 107(2)(b) (2012); *Osborn v. Griffin*, 865 F.3d 417, 447 (6th Cir. 2017)

(relying on similar provision in the Restatement (Second) of Trusts)). Neither KRS 61.645 nor the Restatement contains a demand requirement.

In addition, even if this Court presumed that a demand requirement existed for these plaintiffs, that requirement was essentially met when the KRS Board expressly declined to bring suit. In the Joint Notice attached to Plaintiffs' response to the Motions to Dismiss, KRS explains why it declined to pursue these claims and its belief that Plaintiffs are acting in the best interests of KRS. For this reason, and the reasons set forth above, the Court will deny the Motions to Dismiss to the extent they allege lack of standing to sue derivatively.

c. Plaintiffs may sue on behalf of the Commonwealth as taxpayers.

In addition to being members of KRS and beneficiaries of its trust, Plaintiffs are also taxpayers. *See* First Am. Comp. ¶ 58. In this suit, they allege that the wrongful conduct of the KRS trustees and officers ultimately resulted in damages to the Commonwealth and its taxpayers, as the trust is funded by public tax dollars. *See id*. ¶¶ 272–73, 275. Prior to bringing this suit, however, they made a written demand on the Attorney General to bring these claims, but the Attorney General also declined to do so. *See id*. ¶ 274.

Though the Attorney General is authorized to bring such claims, his failure to do so does not preclude Plaintiffs from now filing this taxpayer suit. In fact, Kentucky favors taxpayer suits. *See generally Price v. Commonwealth*, 945 S.W.2d 429 (Ky. App. 1996); *Rosenbalm v. Commercial Bank of Middlesboro*, 838 S.W.2d 423 (Ky. App. 1992); *Russman v. Luckett*, 391 S.W.2d 694, 699 (Ky. 1965). Thus, Kentucky courts typically do not impose difficult restrictions upon taxpayers seeking to bring such suits. Instead, a claimant must show only "(1) a wrongful act on the part of a public body or its officers, (2) injury to the complaining taxpayer or to the public body, and (3) a right to seek the relief prayed for." *Price*, 945 S.W.2d at 432–33 (quoting

Rosenbalm, 838 S.W.2d at 427) (internal quotation marks omitted). There is no requirement that the claimant first present their claims to the Attorney General, nor is any statutory authority necessary to bring suit.

With this standard in mind, the Court finds that these Plaintiffs allege sufficient facts to demonstrate taxpayer standing. They allege that the wrongful acts of KRS, a public body, and its trustees and officers ultimately resulted in depleted pension funds and, as a result, damage to the Commonwealth and its taxpayer citizens. *See, e.g.*, ¶¶ 239–43 (charging excessive fees); ¶¶ 251, 255 (making false and misleading statements with the intent to create a false sense of security); ¶¶ 279, 285 (claiming damages, including lost funds and increasing costs). They also allege that they have a right to seek the relief prayed for in the First Amended Complaint. *See, e.g.*, *id*. ¶¶ 272–274. These factual allegations are sufficient to defeat Defendants' Motions to Dismiss to the extent that they allege lack of taxpayer standing.

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 above, 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. Thus, the alleged breach of those duties gives rise to a case or controversy, and Plaintiffs have a very real and tangible stake in the outcome. Their personal financial contributions to the KRS retirement funds, matched by public appropriations that are subject to the fiduciary duties set

forth in statute and case law, give the plaintiffs standing to sue over alleged breaches of fiduciary duties in the administration of those funds. Accordingly, the Court will deny the Motions to Dismiss to the extent they allege lack of standing to sue as taxpayers.

II. Statutes of Limitations and Tolling Doctrines

Defendants argue that Plaintiffs claims are time-barred, at least in part, because a five-year limitation period applies to breach of fiduciary duty and breach of trust claims, while a one-year statute of limitations period applies to conspiracy claims. *See* KRS 413.120(2) (providing that an action upon a liability created by statute must be brought within five years of the accrual of that cause of action, if no other time is fixed by statute); KRS 413.120(6) (allowing five years to bring a personal injury suit); KRS 413.140 (providing a one year statute of limitations for civil conspiracy claims); *Middleton v*. *Sampey*, 522 S.W.3d 875, 878–79 (Ky. App. 2017) (applying five-year statute of limitations to breach of fiduciary duty and breach of trust claims). Plaintiffs initiated this suit on December 27, 2017. Thus, Defendants argue, the Court must dismiss any breach claims and related aiding and abetting claims arising prior to December 27, 2012 and any conspiracy claim arising prior to December 27, 2016. Plaintiffs, on the other hand, argue that (1) KRS 413.160 applies and allows for ten years to file "an action for relief not provided for by statute" (i.e., breach of trust) and (2) regardless, each violation constitutes a new cause of action under *Tibble v*. *Edison International*, 135 S.Ct. 1823 (2015); and (3) tolling doctrines, such as the adverse domination theory and equitable tolling, apply.

The Court finds that there are sufficient allegations to overcome the statute of limitations defenses for purposes of these Motions to Dismiss. For example, the plaintiffs allege that the compensation of the hedge fund sellers was grossly excessive and breached fiduciary duties to the members, and Plaintiffs further allege that the full compensation of some of the defendants has

remained secret and sealed from public disclosure. *See* First Am. Compl. ¶¶ 239–43 (discussing excessive fees). To the extent that the defendants may have received excessive compensation in breach of fiduciary duties, and that compensation has not yet been fully disclosed, the statute of limitations may not have even started to run, since a limitations period cannot run before the plaintiffs were reasonably on notice of the nature and extent of the breach of duty.

Accordingly, Defendants' Motions to Dismiss will be denied to the extent they rely on a statute of limitations defense. However, discovery is necessary to provide the full factual context as to when specific causes of action accrued, and whether any tolling occurred to extend the relevant limitations periods. Accordingly, if necessary and appropriate, the statute of limitations defense may be raised by a motion for summary judgment after completion of factual discovery.

III. Qualified Official Immunity

In their Motions to Dismiss, the individual trustee and officer defendants assert claims of official immunity, both absolute (if sued in their official capacities) and qualified (if sued in their individual capacities). At the time these Motions were filed, it remained unclear whether Plaintiffs intended to sue these defendants in their individual or official capacities. However, in their reply memorandum, Plaintiffs expressly state, "Plaintiffs are bringing claims against Trustees and Officers *in their individual* capacity, with no intent, in fact *disclaiming any intent*, to hold KRS liable for their actions." Pls. Opp. 108. Thus, as explained below, the Court need only consider whether qualified official immunity bars Plaintiffs' claims. By Order entered September 5, 2018, the Court allowed the parties to submit supplemental briefs on this issue.

a. Qualified immunity does not apply to actions taken in bad faith.

The doctrine of official immunity shields public officers and employees from tort liability for acts performed in the exercise of their discretionary functions. *Yanero v. Davis*, 65 S.W.3d

510, 521 (Ky. 2001). It is absolute when asserted by a public officer or employee being sued in his or her official or representative capacity. *Id*. However, when public officers and employees are sued in their individual capacity, they "enjoy only qualified official immunity, which affords protection from damages liability for good faith judgment calls made in a legally uncertain environment." *Id*. at 522. More specifically, "[q]ualified official immunity applies to the negligent performance by a public officer or employee of (1) discretionary acts or functions, *i.e*., those involving the exercise of discretion and judgment, or personal deliberation, decision, and judgment; (2) in good faith; and (3) within the scope of the employee's authority." *Id*. (citations omitted).

In the present suit, however, the actions at issue—as alleged in the First Amended Complaint—do not entitle the KRS trustees and officers to qualified official immunity. For example, Plaintiffs allege that these defendants acted in bad faith. *See, .e.g*. First Am. Compl. ¶ 7 (describing use of 7.75% return rate as "willfully reckless"), ¶ 169 (describing concealment of KRS's financial condition as "deliberate, willfull manipulation"), ¶ 171 (explaining that KRS trustees and Ice Miller failed to pursue training in good faith), ¶ 174 (listing scenarios in which KRS trustees and officers acted "willfully or recklessly" in violation of duties and "did not act in good faith"), ¶ 195 (explaining that conflicts of interest among trustees and entities made it impossible to use good faith judgment), ¶ 239 (explaining that each defendant "knowingly" participated in a civil conspiracy or scheme). The Court must accept these allegations as true when considering the CR 12.02 Motions to Dismiss. Thus, at this time, the allegations are sufficient to overcome the trustees' and officers' Motions to Dismiss to the extent said Motions are based on qualified official immunity.

b. KRS 61.645 serves as a limited waiver of immunity for KRS trustees.

Plaintiffs' allegations also trigger the limited statutory waiver of immunity for KRS trustees, as expressed in KRS 61.645. That statute directs a KRS trustee to discharge his or her duties in good faith, on an informed basis, and "[i]n a manner he [or she] honestly believes to be in the best interest of the Kentucky Retirement Systems." KRS 61.645(15)(a). It further provides that a trustee's action or inaction cannot form the basis for a suit for injunctive relief *unless* "[t]he trustee has breached or failed to perform the duties of the trustee's office in compliance with this section." KRS 61.645(15)(e)(1). Monetary damages, on the other hand, may be sought if "the breach or failure to perform constitutes willful misconduct or wanton or reckless disregard for human rights, safety, or property." KRS 61.645(15)(e)(2). In other words, the General Assembly provided a specific waiver of KRS trustees' immunity (absolute or qualified) in certain circumstances, namely, when a trustee breaches his or her statutorily-defined duties.

In the present suit, Plaintiffs allege that the trustee defendants breached or failed to perform those duties listed in KRS 61.645 and that the breaches constituted willful misconduct or gross negligence. For example, as noted above, Plaintiffs allege that these defendants acted in bad faith, in derogation of their statutory duty to act in good faith, as outlined in KRS 61.645(15)(a). Plaintiffs also allege that these defendants "consistently used, or allowed the use of, outdated, misleading or false estimates and assumptions of the actuarial value of the Trust Funds' actuarial assets and liabilities." First Am. Compl. ¶ 169. According to Plaintiffs' Complaint, this constituted "deliberate, willful manipulation to conceal the true financial and actuarial condition and underfunded status of the KRS Plans." *Id*. Summarizing its claim against the trustee and officer defendants, Plaintiffs explain,

> Trustees and Officers willfully or recklessly violated their duties to KRS and its Funds and the taxpayers of Kentucky and did not act in good faith or in what they

> honestly believed was in the best interests of KRS, and its Funds when they failed to: (i) adequately safeguard the trust funds under their control; (ii) procure adequate fiduciary insurance: (iii) invest the trust assets prudently, (iv) avoid excessive and/or unreasonable fees and expenses; (v) use realistic estimates and assumptions regarding the actuarial condition and future investment returns of the funds; (vi) adequately match the assets and liability of the funds; (vii) failed to protect and assure KRS' full legal rights, including the right to sue in Kentucky state court, in open proceedings, with a jury trial, if KRS's legal rights were violated by others – especially by sophisticated out-of-state sellers of investment products who might try to limit or eliminate KRS' legal remedies or (viii) make truthful, complete, accurate disclosure of, or a fair presentation of, the true financial and actuarial condition the KRS Funds and Plans as is detailed in this Complaint.

Id. ¶ 174. These allegations of bad faith and willful and/or reckless misconduct—when accepted as true for purposes of considering a CR 12.02 motion—allow Plaintiffs to sue the KRS trustees for monetary relief under KRS 61.645(15)(e).

In sum, Plaintiffs sue the trustee and officer defendants in their individual capacity and allege that these defendants acted willfully or in bad faith or were otherwise grossly negligent. Allegations of actions taken in bad faith defeat the trustees' or officers' claims for qualified official immunity in the context of these Motions to Dismiss. In addition, these actions constitute a breach of the trustees' statutory duties listed in KRS 61.645, thereby triggering the limited waiver of immunity contained within that provision and allowing Plaintiffs to seek injunctive relief. Willful misconduct and gross negligence similarly trigger the statute's limited waiver of immunity and allow Plaintiffs to sue for monetary damages.

Likewise, the statute's express authorization for the "purchase of fiduciary liability insurance" under KRS 61.645(2)(e), in combination with the statute's express reference to suits for monetary damages in KRS 61.645(15)(e), may also constitute a limited waiver of any qualified, official, or governmental immunity for the alleged breaches of fiduciary duty, at least to the extent of the insurance coverage. *See Reyes v*. *Hardin Cnty*., 55 S.W.3d 337 (Ky. 2001). Accordingly,

to the extent that any KRS trustee or officer defendants asserts a claim of official immunity, the Motions to Dismiss will be denied without prejudice.

IV. Subject Matter Jurisdiction

Several defendants argue that the Kentucky Claims Commission retains exclusive jurisdiction over these claims under KRS 49.070, thereby depriving this Court of the subject matter jurisdiction necessary to resolve this suit. That statute provides that the Commission "shall have primary and exclusive jurisdiction over all negligence claims for the negligent performance of ministerial acts against the Commonwealth, any of its cabinets, departments, bureaus, or agencies, or any officers, agents, or employees thereof while acting within the scope of their employment." KRS 49.070(2). Such claims cannot be brought in this Court, or any other forum, until the Commission determines that it does not have primary and exclusive jurisdiction. KRS 49.070(5).

In this suit, Plaintiffs' First Amended Complaint does not list a cause of action for negligence against any defendant. Regardless, Defendants assert that Plaintiffs' claims against the KRS trustees and officers are based in negligence and must therefore be presented to the Kentucky Claims Commission. For example, Count II alleges that "[e]ach of the Defendants by their actions and inactions, as alleged herein, acted in a negligent manner and failed to exercise due care and failed to fulfill their statutory and other duties, including their fiduciary duties, to KRS and its Funds and to Kentucky and its taxpayers." First Am. Compl. ¶ 288.

The Court notes, however, that the General Assembly intended to provide a limited waiver of sovereign immunity through KRS 49.070. *See* KRS 49.060; *Yanero*, 65 S.W.3d at 524 (explaining that the Board of Claims Act "represents not a creation of immunity, but rather a limited waiver of immunity to the extent that immunity exists"). Thus, if one is injured by the negligent acts of a state officer, agent, or employee acting within the scope of his or her

employment, that injured party can seek damages against the Commonwealth, something otherwise barred by the doctrine of sovereign immunity. In other words, the statute provides a limited waiver of sovereign immunity to allow for negligence suits against the state itself. However, because it serves as a *waiver* of immunity, it applies only to state agencies that would otherwise be shielded by immunity; it does not shield government agencies, officers, and employees who are not immune from suit. *See Yanero*, 65 S.W.3d at 525.

The Board of Claims (now the Kentucky Claims Commission) was established to allow limited recovery to parties injured by state action by creating a limited waiver of sovereign immunity. Here, however, Plaintiffs have now made clear that they seek damages against the KRS trustees and officers in their *individual* capacity; they do not seek damages from the Commonwealth for the negligent acts of those individuals. *See* Pls.' Opp. 108. Thus, there is no threat to the state treasury and no need to rely on the limited waiver of sovereign immunity contained within KRS 49.070. Stated another way, Plaintiffs' claims for breaches of fiduciary duty against third parties and state employees and officers in their individual capacities do not fall within the jurisdiction of the Kentucky Claims Commission.

Accordingly, the Kentucky Claims Commission is not an available remedy for the breaches of duty asserted by the plaintiffs; therefore, to the extent that Defendants' Motions to Dismiss assert a lack of subject matter jurisdiction (or failure to exhaust administrative remedies), these Motions must be denied.

V. Personal Jurisdiction

Several executives of Prisma, PAAMCO, and BAAM—namely, Kravis, Roberts, Schwarzman, and Hill—contest personal jurisdiction. These individual defendants argue that the First Amended Complaint lacks any specific allegations that trigger Kentucky's long-arm statute.

In addition, they argue that the plaintiffs' allegations do not warrant piercing the corporate veil and holding the individuals liable for the actions of their companies.

Blackstone and KKR also contest personal jurisdiction. For example, Blackstone argues that the First Amended Complaint groups Blackstone and BAAM together, but BAAM was Blackstone's subsidiary and was responsible for marketing and managing the "Henry Clay Fund." As the parent company, Blackstone argues, it cannot be held liable for the actions of BAAM unless Blackstone itself had direct contact with or activity in Kentucky. Because the Complaint lacks any allegations that Blackstone independently engaged in any conduct in Kentucky, it cannot be subject to suit in this Court. Similarly, KKR argues that the Complaint fails to allege with reasonable particularity that KKR had sufficient contacts with Kentucky. Though KKR combined with Prisma in 2017, it argues that that indirect ownership, without more, is insufficient.

The Court finds, however, that the First Amended Complaint contains sufficient allegations to survive the Motions to Dismiss on this issue. For example, Plaintiff states that each of the out-of-state defendants "participated in a years-long conspiracy, scheme, and common course of concerted conduct and enterprise with in-state Kentucky residents and actors, involving repeated travel into Kentucky by themselves or their agents for business purposes, thus subjecting themselves to the personal jurisdiction of Kentucky courts." First Am. Compl. ¶ 294. Stated another way, the plaintiffs allege that these defendants entered into business arrangements with a Kentucky entity and, through those arrangements, engaged in a pattern of intentional or reckless misrepresentation, which foreseeably caused significant financial losses to KRS, a Kentucky entity, and harm to its members, citizens of Kentucky, to the benefit of these out-of-state defendants. *See* KRS 454.210(2)(a)(4) (providing personal jurisdiction over non-residents that cause tortious injury in the Commonwealth by virtue of their business relationships, persistent

courses of conduct, or substantial revenue derived from their Kentucky relationships). Accordingly, the Motions to Dismiss will be denied to the extent they argue lack of personal jurisdiction.

However, facts uncovered in discovery may warrant revisiting of the issue of personal jurisdiction. Accordingly, the above-named defendants—Blackstone, KKR, Kravis, Roberts, Schwarzman, and Hill—will not be deemed to have waived their right to reassert this defense if warranted by facts established in pretrial discovery.

VI. Attorney Client Privilege and Scope of Legal Representation of Ice Miller

Plaintiffs describe Ice Miller as KRS's "fiduciary advisor." *See* First Am. Compl. ¶ 146. By virtue of this relationship and the circumstances surrounding it, Plaintiffs argue, Ice Miller was a fiduciary to KRS. Ice Miller now seeks dismissal of Plaintiffs' First Amended Complaint based primarily on two arguments. First, Ice Miller argues that this suit violates the "anti-assignment rule," which holds that assignment of a legal malpractice claim "is void against public policy." *Coffey By and Through Collins v. Jefferson Cnty. Bd. of Educ.*, 756 S.W.2d 155, 157 (Ky. App. 1988). Because the claims against Ice Miller stem from its attorney-client relationship with KRS, it argues that those claims constitute an assignment of KRS's right to sue Ice Miller for malpractice. Next, Ice Miller argues that Plaintiffs lack the privity necessary to sue Ice Miller directly, as Plaintiffs were not parties to or third-party beneficiaries of the contract between KRS and Ice Miller.

Both arguments can be resolved by this Court's finding that the plaintiffs were, in fact, third-party beneficiaries to the contract. One qualifies as a third-party beneficiary to a contract so long as the contract in question has been "made and entered into directly or primarily for the benefit of such third person." *King v. Nat'l Indus., Inc.*, 512 F.2d 29, 32 (Ky. App. 1975) (quoting *Long*

v. *Reiss*, 160 S.W.2d 558, 674 (Ky. 1942)). Though Ice Miller contracted with KRS to provide legal services, the firm was ultimately retained for the benefit of KRS's *members* and the citizens and taxpayers of the Commonwealth of Kentucky. True, the agency itself was the vehicle through which Ice Miller was retained, but there can be no doubt that the legal advisor was retained to protect the best interests of KRS's members and the Commonwealth's citizens and taxpayers. Simply put, the whole purpose of the engagement of legal counsel was to protect the interests of public employees and retirees. In other words, Ice Miller's work with KRS served the public—namely, the members and beneficiaries of KRS. As a result, the present suit is not an assignment of KRS's malpractice claim, but rather, a lawsuit directly brought by members of KRS, who at a minimum are third-party beneficiaries of Ice Miller's representation.

Furthermore, the Court notes that, regardless of the contractual nature of Ice Miller's relationship with KRS, the Complaint alleges facts sufficient to imply a common law fiduciary relationship. Such a relationship "may exist under a variety of circumstances," but "it exists in all cases where there has been a special confidence reposed in one who in equity and good conscience is bound to act in good faith and with due regard to the interests of the one reposing confidence." *Steelvest, Inc*. *v*. *Scansteel Service Center, Inc*., 807 S.W.2d 476, 485 (Ky. 1992) (quoting *Security Trust Co*. *v*. *Wilson*, 210 S.W.2d 336, 338 (Ky. 1948)). It is not typically born solely out of a "generalized business obligation of good faith and fair dealing." *Ballard v*. *1400 Willow Council of Co-Owners, Inc*., 430 S.W.3d 229, 242 (Ky. 2013). However, when that relationship involves a special trust or reliance on the professional party to use its expertise in serving the client, which is knowingly accepted by the professional, a fiduciary relationship is created.

Here, Plaintiffs allege that Ice Miller, as KRS's professional fiduciary advisor, had unrestricted access to and intimate knowledge of KRS's financial records and data. First Am.

Compl. ¶ 146. According to the Complaint, Ice Miller also "has extensive expertise and experience in fiduciary matters for pension plan trustees including advising on the purchase of fiduciary insurance, conflicts of interest and investments in fund of hedge fund investments." *Id*. ¶ 147. Furthermore, the Complaint implies that Ice Miller knowingly accepted this role as fiduciary advisor. *Id*. ¶ 148 (discussing importance of the professional-client relationship between Ice Miller and KRS). Thus, while the full contours of the attorney-client relationship between KRS (and its members) and Ice Miller have not yet been developed in discovery, the plaintiffs have sufficiently alleged that Ice Miller owed fiduciary duties to them which were breached and resulted in injury. Accordingly, for this reason and those cited above, Ice Miller's Motion to Dismiss will be denied.

VII. Failure to State Claims for Breaches of Fiduciary, Statutory, and Other Duties

a. Trustees and Officers

Several of the trustee and officer defendants argue that Plaintiffs fail to allege specific duties and how those duties were breached. However, as noted above, KRS trustees have a clear duty under KRS 61.645 to act in good faith, on an informed basis, and in the best interests of KRS's beneficiaries. In paragraph 26 of the First Amended Complaint, Plaintiffs reference those duties and that portion of KRS 61.645 that allows one to sue for failure to perform said duties. That paragraph states, in part, "Trustees' and Officers [sic] actions and failures to act were violations of their mandatory duties under Kentucky law," clearly referring to KRS 61.645. The specific breaches—namely, the failure to act in good faith and on an informed basis—and the resulting damages are referenced throughout the Complaint, including but not limited to the following: ¶ 7 (describing use of 7.75% return rate as "willfully reckless"), ¶ 169 (describing concealment of KRS's financial condition as "deliberate, willfully manipulation"), ¶ 171

(explaining that KRS trustees and Ice Miller failed to pursue training in good faith), ¶ 195 (explaining that conflicts of interest among trustees and entities made it impossible to use good faith judgment), ¶ 239 (explaining that each defendant "knowingly" participated in a civil conspiracy or scheme); ¶¶ 279, 285 (claiming damages, including lost funds and increasing costs). In addition, paragraph 74 lists instances in which the trustee and officers "willfully or recklessly violated their duties," including the failure to adequately safeguard trust funds, obtain adequate insurance, invest prudently, avoid unreasonable fees, use realistic estimates, match the assets and liabilities of the funds, and make truthful disclosures of KRS's financial status. These allegations are sufficient to survive the CR 12.02 Motions to Dismiss on this issue.

The trustees, as well as the officers, are also subject to fiduciary duties under the common law. As noted above, a common law fiduciary relationship "exists in all cases where there has been a special confidence reposed in one who in equity and good conscience is bound to act in good faith and with due regard to the interests of the one reposing confidence." *Steelvest*, 807 S.W.2d at 485 (quoting *Security Trust*, 210 S.W.2d at 338). However, the circumstances giving rise to such a relationship "are so varied, it is extremely difficult, if not impossible, to formulate a comprehensive definition of it that would fully and adequately embrace all cases." *Id*. at 489.

In this case, the First Amended Complaint expressly alleges that the trustees had an obligation to protect the trust funds, prudently invest those funds, and to pay benefits to the trust's beneficiaries. *See* First Am. Compl. ¶ 165. The Complaint implies that KRS officers had similar obligations. *See, e.g*., *id*. ¶ 174 (noting that both trustee and officer defendants breached fiduciary duties by failing to perform the listed actions). The Court finds these allegations sufficient to imply a relationship of trust between the Board, the officers, and KRS members, and a duty to act in the best interest of those members. The Complaint also alleges a failure to act in accordance

with that duty and resulting damages. *See, e.g., id.* ¶ 174 (breaches), ¶¶ 279, 285 (damages). In other words, the Complaint sufficiently alleges a fiduciary relationship and breaches of those duties. For these reasons, the Motions to Dismiss of the trustee and officer defendants will be denied to the extent they allege a failure to state a claim for breach of fiduciary, statutory, or other duties.

b. CavMac Defendants

The First Amended Complaint also alleges facts sufficient to imply a common law fiduciary relationship between the CavMac Defendants and KRS's members. For example, Plaintiffs allege that CavMac "represented that it had superior skill, experience and expertise in public pension fund actuarial matters." First Am. Compl. ¶ 139. With this experience and expertise, the CavMac Defendants "provided expert actuarial services to KRS for many years," supplying certification for each year's actuarial estimates and assumptions. *Id.* ¶ 140. The individual CavMac Defendants—Cavanaugh, Green, and Bennett—signed off on these certifications, as well as other related opinions and reports. *Id.* ¶ 141.

These allegations are sufficient to overcome the CavMac Defendants' Motion to Dismiss on this issue. Clearly, the CavMac Defendants had contractual duties concerning the administration of funds held in trust for the plaintiffs, but the Court cannot determine the full scope of such duties, or whether they were fiduciary in nature, until after full discovery on the nature of the relationship between the CavMac Defendants and KRS. Thus, factual discovery may support the CavMac Defendants' assertion that they had no fiduciary relationship; however, at this stage in the proceedings, the Court finds that the First Amended Complaint contains allegations that a duty exists and was breached, and that the breach of duty resulted in damages to the plaintiffs. Accordingly, the plaintiffs' claims against these defendants survive a CR 12.02 Motion to Dismiss.

c. Government Finance Officers Association

GFOA is a nonprofit professional association of state and local finance officers that encourages its members, like KRS, to create financial reports, including Comprehensive Annual Financial Reports. *See* First Am. Compl. ¶ 154. Because KRS created such reports, it repeatedly received GFOA's "Certificate of Achievement" in financial reporting. *See id*. ¶ 157. Plaintiffs now allege that GFOA reviewed these Annual Reports and knew or should have known that the reports contained false or misleading information. *See id*. ¶ 158. Essentially, Plaintiffs argue that the Certificates of Achievement contributed to a false and misleading public perception of KRS's financial status. As a result, Plaintiffs sue GFOA for breaching statutory, fiduciary, or other duties (Count II); participating in a joint enterprise or civil conspiracy (Count III); and aiding and abetting the other defendants' breaches of statutory, fiduciary, and other duties (Count IV). Plaintiffs also attempt to assert a claim of negligent misrepresentation in their reply memorandum; however, the Court finds it inappropriate to amend the pleadings through memoranda and without leave of Court *See generally* CR 15. Regardless, the Court finds that the the First Amended Complaint fails to maintain a cause of action against GFOA for that additional tort, or any other named cause of action, because GFOA owed no duty to Plaintiffs, nor is there any basis but sheer speculation that GFOA's conduct, as alleged by Plaintiffs, had any causal connection to any injury or damages alleged by Plaintiffs.

First, the Court finds that Plaintiffs have failed to allege the breach of any duty owed by GFOA to the plaintiffs. The uncontested facts demonstrate that GFOA is a nonprofit entity that promotes public finance agencies by encouraging financial reporting among these agencies. However, there is no factual assertion that the public or any plaintiff—or *anyone*, for that matter—

has relied on the representations of GFOA (i.e., the Certificates of Achievement) in any material way relevant to the plaintiffs' claims.

In fact, the record is abundantly clear that it would be wholly unreasonable for anyone to assume that GFOA's Certificates are related to KRS's financial solvency, management competency, board competency, investment strategies, or any other material fact relevant to this litigation. GFOA merely promotes financial *reporting* among these agencies; it does not review the financial solvency of the agency. Simply put, GFOA has no regulatory authority or legal oversight responsibilities regarding KRS. Absent some statutory, regulatory, contractual, or other duty to Plaintiffs or the public, GFOA plays merely an advisory role in reviewing financial reports of government agencies.

For example, Plaintiffs' counsel has questioned what might have happened if GFOA had withdrawn its designation for KRS. To answer this question, the Court need look no farther than the description of the GFOA Certificate of Achievement cited in paragraph 157 of the First Amended Complaint:

> The Certificate of Achievement is a prestigious national award recognizing excellence in the preparation of state and local government financial reports and is valid for a period of one year. . . . In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized document. The report must satisfy both generally accepted accounting principles and applicable legal requirements.

From this description, the Court concludes that the only thing a reasonable person would assume from GFOA's hypothetical withdrawal of its Certificate would be that the KRS reports were not "easily readable and efficiently organized." A reasonable person might conclude that KRS needed better editors and graphic designers to put their reports in more readable formats or to make them more understandable to the average reader. If GFOA has withdrawn its certification, no reasonable person would have concluded that KRS was recklessly investing in hedge funds or breaching

fiduciary duties to its members. It would be sheer speculation that the withdrawal of the GFOA seal of approval might have tipped off members or public officials with oversight responsibilities as to the dire financial condition of KRS. It is simply untenable to posit that any reasonable person would rely on GFOA designations to evaluate the financial status of a multi-billion-dollar public agency. The record is undisputed that the GFOA designation is based on the *form* of the reports, not their substance. In these circumstances, there is no breach of any duty to the plaintiffs.

For these same reasons, the Court finds that the First Amended Complaint lacks any facts to supports its claims that GFOA engaged in a civil conspiracy or aided and abetted the other defendants in their alleged breaches. As stated above, GFOA's Certificate of Achievement merely acknowledged the "easily readable and efficiently organized" nature of KRS's Annual Reports, and no reasonable person would rely on that Certificate to validate KRS's financial condition. Furthermore, there is no negligent misrepresentation where GFOA's description of the Certificate of Achievement clearly states that it is awarded based on the format of the agency's financial reporting—not the strength of the agency's financial status.

Accordingly, for the reasons set forth above, the Court will grant GFOA's Motion to Dismiss, thereby dismissing all claims against GFOA.

d. Hedge Fund Sellers

The "Hedge Fund Seller Defendants" include the entities responsible for the sale and management of the relevant hedge funds, as well as several top executives of those companies. These defendants now argue that Plaintiffs fail to identify a fiduciary duty, relying primarily on the contractual nature of the relationship between these defendants and KRS. In other words, they argue that no fiduciary relationship arose from the contracts; instead, these parties were bound

only to the terms of their contracts and there are no allegations that they breached the specific terms of those agreements.

At this time, the Court finds that the First Amended Complaint contains allegations sufficient to imply a common law fiduciary relationship between the Hedge Fund Seller Defendants and KRS and its members. *See, e.g.*, First Am. Compl. ¶ 183 (referencing "superior knowledge and expertise" of the Hedge Fund Seller Defendants, KRS's dependence on said expertise, and Defendants' knowledge of that dependence). The Complaint also contains sufficient allegations of a breach of those fiduciary duties. For example, Plaintiffs reference the massive fees collected by these defendants in breach of the common law fiduciary duty to not charge excessive fees. *See id*. ¶¶ 239–243. After factual discovery is completed, those allegations may be disputed or disproven. At this time, however, without full disclosure of all fees, costs, and other expenses related to the management of these hedge funds, the Court cannot dismiss these defendants.

VIII. Failure to State Claim for Joint Enterprise/Civil Conspiracy

To successfully plead a claim of civil conspiracy, one must allege "an unlawful/corrupt combination or agreement between the alleged conspirators to do by some concerted action an unlawful act." *James v. Wilson*, 95 S.W.3d 875, 897 (Ky. App. 2002). Similarly, a claim of joint enterprise requires

> (1) an agreement, express or implied, among the members of the group; (2) a common purpose to be carried out by the group; (3) a community of pecuniary interest in that purpose, among the members; and (4) an equal right to a voice in the direction of the enterprise, which gives an equal right of control.

Huff v. Rosenberg, 496 S.W.2d 352, 255 (Ky. 1973) (citation omitted). Ultimately, "[a] conspiracy may be shown by circumstantial evidence, by the acts or declarations of the conspirators, or by the

cumulative effect of concerted action of the several parties concerned." *See Addison v. Wilson*, 37 S.W.2d 7, 11 (Ky. 1931) (citation omitted).

In the present suit, Defendants argue that Plaintiffs fail to allege an agreement among the defendants to do the unlawful or tortious act. However, accepting all allegations in the First Amended Complaint as true for purposes of this decision, the Court finds that Plaintiffs sufficiently plead circumstances that could lead a jury to conclude that such an agreement existed. For example, throughout the Complaint, Plaintiffs repeat their allegation that various defendants "knowingly aided and abetted the breach of duties by Trustees, while participating by committing overt acts, in an ongoing scheme, civil conspiracy, common course of conduct and joint enterprise" in concert with the KRS trustees, by "acting and failing to act as alleged herein." First Am. Compl. ¶¶ 93, 106, 138, 145, 153, 159. The actions and inactions included in the Complaint include providing false or misleading information, and otherwise acting in bad faith. *See, e.g., id.* ¶¶ 7, 169. The Complaint also details alleged conflicts of interest among the KRS trustees and the other defendants, which could lead a factfinder to conclude that an agreement, express or implied, existed among these parties. *See, e.g., id.* ¶¶ 62, 69–70. Accordingly, at this time, the Court will deny the Motions to Dismiss to the extent they argue that Plaintiffs failed to sufficiently allege a claim for civil conspiracy and/or joint enterprise.

IX. Failure to State Claim for Aiding & Abetting

A claim of aiding and abetting a breach of fiduciary duty requires the following elements: "(1) the existence and breach of a fiduciary relationship; (2) the defendant gave the breaching party 'substantial assistance or encouragement' in effectuating the breach; and (3) the defendant knew that the party's conduct breached that fiduciary duty." *Insight Ky. Ptnrs II, L.P. v. Preferred Automotive Servs., Inc.*, 514 S.W.3d 537, 546 (Ky. App. 2016) (citing *Miles Farm Supply, LLC v.*

Helena Chem. Co., 595 F.3d 663, 666 (6th Cir. 2010)). In this suit, several Defendants argue that Plaintiffs fail to sufficiently allege that they provided the "substantial assistance" necessary to support these claims.

However, accepting all allegations in the First Amended Complaint as true for purposes of this decision, the Court finds that Plaintiffs sufficiently plead their aiding and abetting claim. First, as explained in more detail above, Plaintiffs allege the existence and breaches of a fiduciary duty. Plaintiffs also allege that the defendants knowingly provided assistance to the breaching parties by promoting or allowing the use of false or misleading information in an effort to conceal KRS's financial status. *See, e.g.*, ¶¶ 105, 134, 136–37, 144, 152, 169. At this time, these allegations are sufficient to overcome the defendants' Motions to Dismiss on this issue.

In addition, at least one defendant argues that aiding and abetting a breach of fiduciary duty is not a separate cause of action in Kentucky, citing *Peoples Bank v. Crowe Chizek and Co., LLC*, 277 S.W.3d 255, 260–61 (Ky. App. 2008). However, this Court finds that *Steelvest, Inc. v. Scansteel Service Center, Inc.*, 807 S.W.2d 476 (Ky. 1992) remains controlling law on this issue. *See Gundaker/Jordan American Holdings, Inc. v. Clark*, 2008 WL 4550540, *4 (E.D.Ky. Oct. 9, 2008) (declining to follow *Peoples Bank* and instead following *Steelvest*).[1] In *Steelvest*, our Supreme Court made clear that "a person who knowingly joins with or aids and abets a fiduciary in an enterprise constituting a breach of the fiduciary relationship becomes jointly and severally liable with the fiduciary for any profits that may accrue." 807 S.W.2d at 485. Thus, aiding and abetting is appropriately pleaded as a separate cause of action, and, for the reasons set forth above, this cause of action survives Defendants' Motions to Dismiss.

[1] At the time of the *Gundaker/Jordan* decision, the *Peoples Bank* decision was not yet final. The Court noted this, explaining that the case "cannot be cited as authority in Kentucky courts." 2008 WL 4550540 at *4. However, this was only one factor in the Court's decision not to follow *Peoples Bank*; the primary reason was the precedential value of the Kentucky Supreme Court's holding in *Steelvest*, which was not addressed by *Peoples Bank*.

X. Economic Loss Rule

In support of their Motion to Dismiss, the CavMac Defendants explain that "all of the CavMac Defendants' actions complained of in this case were conducted pursuant to the terms of its contracts with KRS to perform actuarial services." CavMac Defs.' Mem. 18. Thus, they argue, each of Plaintiffs' claims is barred by the economic loss rule. In response, Plaintiffs insist that that the economic loss rule applies only to claims brought by the purchaser of a defective product for economic losses arising from the malfunction of that product. This Court agrees.

The Kentucky Supreme Court officially adopted the economic loss rule in 2011 in *Giddings & Lewis, Inc. v. Industrial Risk Insurers*, 348 S.W.3d 729 (Ky. 2011). Limiting its ruling to the commercial context, the Court explained that the rule "prevents the commercial purchaser of a product from suing in tort to recover for economic losses arising from the malfunction of the product itself, recognizing that such damages must be recovered, if at all, pursuant to contract law." *Id.* at 733. Other states have expanded this doctrine and applied the economic loss rule to other areas of the law, including construction contracts and real estate transactions. *See generally West Ridge Group LLC v. First Trust Company of Anaga*, 414 Fed. Appx. 112, (10th Cir. 2011) (violations of Real Estate Settlement Procedures Act); *Marion County Public Library v. Charlier Clark & Linard, P.C.*, 929 N.E. 2d 722 (Ind. 2010) (defective design and construction of parking garage); *Flagstaff Affordable Housing Limited Partnership v. Design Alliance, Inc.*, 223 P.3d 664, 673 (Ariz. 2010) (construction defect).

The Kentucky Court of Appeals also expanded the rule in an unpublished decision involving a services contract, specifically, one for construction work. *See Cincinnati Ins. Cos. V. Staggs & Fisher Consulting Engineers, Inc.*, 2013 WL 1003543 (Ky. App. Mar. 15, 2013). However, that case has little precedential value, and Kentucky remains skeptical of the economic

loss doctrine. *See State Farm Mutual Auto. Ins. Co. v. Norcold, Inc.*, 849 F.3d 328, 335 (6th Cir. 2017) (explaining Kentucky's "skepticism" of the rule); *D.W. Wilburn, Inc. v. K. Norman Berry Associates, Architects, PLLC*, 2016 WL 7405774, *6 (Dec. 22, 2016) (explaining that *Staggs & Fisher* has "has no precedential value" and implying that, at most, its ruling is limited to the facts of that case). In fact,

> federal courts applying Kentucky law, both before and after the *Giddings & Lewis* decision, that have addressed the issue of whether the economic loss rule should apply to the provision of services consistently have held that the Kentucky Supreme Court would not apply the economic loss rule to service contracts.

NS Transp. Brokerage Corp. v. Louisville Sealcoat Ventures, LLC, 2015 WL 1020598, *4 (W.D.Ky. Mar. 9, 2015) (citations omitted). This Court declines to now extend the doctrine to such contracts.

This decision is not altered by Defendants' reliance on *Presnell Construction Managers, Inc. v. EH Construction, LLC*, 134 S.W.3d 575 (Ky. 2004). The *Presnell* decision—decided prior to *Giddings & Lewis*—does not mention the economic loss rule; rather, the rule is discussed in Justice Keller's concurring opinion. In fact, federal courts have since "found the absence of any such discussion by the majority indicative of our Supreme Court's unwillingness to expand the economic loss rule beyond products liability cases." *D.W. Wilburn, Inc.*, 2016 WL 7405774, *7 (referencing *Louisville Gas and Elec. Co. v. Continental Field Systems, Inc.*, 420 F.Supp.2d 764 (W.D.Ky. 2005)). As noted above, this Court also declines to extend the economic loss rule to the present suit involving a service contract between a state agency and an actuarial services provider. The CavMac Defendants' Motion to Dismiss will therefore be denied to the extent it relies on this doctrine.

XI. Punitive Damages

As their fifth cause of action, Plaintiffs assert a claim for punitive damages. Some defendants argue that this claim fails as a matter of law because punitive damages are a remedy, rather than a separate cause of action. *See, e.g.*, CavMac Defs.' Mot. to Dismiss 19. The Court agrees that, generally speaking, "a claim for punitive damages is not a separate cause of action, but a remedy potentially available for another cause of action." *Dalton v. Animas Corp.*, 913 F.Supp.2d 370, 378 (W.D. Ky. 2012) (citation omitted); *see also Archey v. AT&T Mobility, LLC*, 2017 WL 6614106, *4 (E.D. Ky. Dec. 26, 2017) (citations omitted). However, as recently as 2017, our Court of Appeals explained, "Unlike the view of the federal courts and the state courts that follow them, Kentucky *does* consider punitive damages a separate claim and not merely an additional remedy along with compensatory damages." *Chesley v. Abbott*, 524 S.W.3d 471, 480 (Ky. App. 2017) (citation omitted). In that case, *Chesley v. Abbott*, the Court examined Kentucky case law, as well as Kentucky's punitive damages statute, KRS 411.186. That statute provides, in pertinent part, "In any civil action where *claims* for punitive damages are included, the jury or judge if jury trial has been waived, shall determine concurrently with all other issues presented, whether punitive damages may be assessed." KRS 411.186(1) (emphasis added). Accordingly, "[i]n Kentucky, a claim for punitive damages, although interrelated, is a separate claim that is extricable from a breach of fiduciary duty judgment and vice versa." *Chesley*, 524 S.W.3d at 480–81. As such, Plaintiffs' punitive damages claim (Count V) survives Defendants' Motions to Dismiss.

Defendants also argue that a claim for punitive damages must fail when the underlying tort is dismissed. However, for the reasons set forth above, Plaintiffs' claims have survived the

Motions to Dismiss (with the exception of GFOA's Motion). Accordingly, the Defendants' motions to dismiss the plaintiffs' claim for punitive damages must be denied.

CONCLUSION

For the reasons set forth above, the Court hereby **GRANTS** the Motion to Dismiss filed by Defendant GFOA, and all claims against GFOA are hereby **DISMISSED**. All remaining Motions to Dismiss are hereby **DENIED**. The Motion to Defer is also **DENIED**.

Furthermore, the parties are **ORDERED** to meet and confer and submit an Agreed Case Management Order within thirty (30) days of the entry of this Order. That Order shall address deadlines for completion of discovery, disclosure of lay and expert witnesses, and filing of dispositive motions, and any other necessary pre-trial deadlines. If the parties cannot agree on the terms of the Order, they shall contact Judicial Assistant Kathryn Marshall at 502-564-8383 to schedule a Case Management Conference with this Court.

SO ORDERED this 30th day of November, 2018.

/s/ HON. PHILLIP J. SHEPHERD
electronically signed
11/30/2018 1:51:29 PM

PHILLIP J. SHEPHERD, JUDGE
Franklin Circuit Court, Division I

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EXHIBIT B

EXHIBIT B

COMMONWEALTH OF KENTUCKY
FRANKLIN CIRCUIT COURT
DIVISION I
CIVIL ACTION NO. 17-CI-01348

JEFFREY C. MAYBERRY, *et al.* **PLAINTIFFS**

v. **ORDER**

KKR & CO. LLP, *et al.* **DEFENDANTS**

This matter is before the Court on remand from the Supreme Court of Kentucky, following its ruling that the Plaintiffs lack constitutional standing to pursue their claims for breach of fiduciary duty and mismanagement of the funds held by Kentucky Retirement Systems for public employee pensions. *Overstreet v. Mayberry,* 603 S.W.3d 244 (Ky. 2020). The Supreme Court of Kentucky remanded the case "with direction to dismiss the complaint." *Id.* at 265. Following this ruling from the Kentucky Supreme Court, the Plaintiffs[1] filed a Motion for Leave to File Second Amended Complaint and Attorney General Daniel Cameron filed a Motion to Intervene on Behalf of the Commonwealth of Kentucky. Upon consideration of all arguments, briefs, papers, and otherwise being sufficiently advised, the Court hereby **DISMISSES** the Complaint filed by the Plaintiffs, **DENIES** Plaintiffs' Motion to file a Second Amended Complaint, and **GRANTS** the Office of the Attorney General's Motion to Intervene, for reasons explained more fully below.

BACKGROUND

This action was filed with this Court on December 27, 2017 by eight individuals (the "Original Plaintiffs"), each being members of the Kentucky Retirement Systems ("KRS"). The

[1] Jeffery C. Mayberry, Hon. Brandy O. Brown, Martha M. Miller, Steve Roberts, Teresa M. Stewart, Ashley Hall-Naqy, Tia Taylor, and Bobby Estes.

Original Plaintiffs are composed of two groups: the "Mayberry Plaintiffs" (Jeffery C. Mayberry, Hon. Brandy O. Brown, Martha Michelle Miller, Steve Roberts, and Teresa Stewart) and the "Wyman Plaintiffs" (Ben Wyman, Jason Lainhart, and Don Coomer). The Original Plaintiffs each began participation in KRS prior to 2014, and thus had defined-benefit retirement plans, meaning that the payments that they will receive each month upon retirement will be fixed amounts. And, the Commonwealth of Kentucky has guaranteed by statute that those members of KRS enrolled prior to 2014 who receive these defined-benefit retirement payments would receive them for their entire lives.

The Original Plaintiffs brought suit against several defendants, including KRS trustees, KRS officers, various investment advisors, and hedge-fund managers, among others, based on a 25-billion-dollar funding deficiency in the KRS asset pool. Original Plaintiffs asserted that Defendants mismanaged KRS retirement assets in several ways, including concealing the declining state of KRS assets. And, the Original Plaintiffs argue that Defendants recklessly sought to rectify the state of KRS retirement assets by investing 1.5 billion dollars in high risk investment vehicles. This further worsened the state of the KRS portfolio: the new investments lost another 100 million dollars by 2018 and accumulated massive fees. KRS itself did not join this action as either a plaintiff or defendant but stated that it supported the Original Plaintiffs' action as being on behalf of KRS on a "derivative basis." The Kentucky Attorney General was notified of the filing of the Original Plaintiffs' complaint, but initially declined to participate in this suit.

Defendants filed a Motion to Dismiss this case in February of 2018. Defendants argued that the Original Plaintiffs lacked standing to bring their claims, in part arguing that the Original Plaintiffs suffered no injury—as defined-benefit retirees, they are guaranteed payment of fixed

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amounts even if KRS were to fail. Further, some Defendants argued that they are immune from the Original Plaintiffs' claims.

On November 30, 2018, this Court entered an Opinion and Order denying Defendants' Motion to Dismiss. Therein, this Court held that the Original Plaintiffs alleged a sufficiently concrete injury to have standing to bring their suit because the true plaintiffs—the Commonwealth and KRS—suffered injury due to Defendants' alleged conduct. The Court also found that the Original Plaintiffs could bring suit derivatively as members and beneficiaries of KRS and as Kentucky taxpayers, and the Attorney General's initial failure to join this action did not prevent them from doing so. Further, the Court held that the factual record was insufficient to determine whether applicable statutes of limitation had been tolled, that sovereign immunity defenses raised by Defendants did not apply, and that the Court had both subject matter jurisdiction over the dispute and personal jurisdiction over the Defendants. Finally, the Court found that the Original Plaintiffs had stated sufficient claims to overcome Defendants' motion to dismiss except as to the Government Finance Officers Association ("GFOA"), whose motion to dismiss was granted due to a failure to sufficiently allege a breach of any duty owed by GFOA to any of the Original Plaintiffs.

The KRS trustee and officer Defendants filed two interlocutory appeals from this Court's 2018 Order, arguing both that the Original Plaintiffs lacked constitutional standing and that they were entitled to sovereign immunity as KRS trustees and officers. In a separate action filed in January of 2019, another group of Defendants sought a writ of prohibition from the Kentucky Court of Appeals; these Defendants requested a determination that this Court lacked subject-matter jurisdiction over the Original Plaintiffs' action. The writ of prohibition was granted by the

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Kentucky Court of Appeals in April of 2019, but later dismissed as moot by the Kentucky Supreme Court.[2]

While this matter proceeded through Kentucky's appellate courts, the doctrine of standing was being modified and restricted in cases before both the Kentucky Supreme Court and the United States Supreme Court. After the filing of this case, the Kentucky Supreme Court rendered its decision in *Commonwealth Cabinet for Health and Family Services, Department of Medicaid Services v. Sexton*, 566 S.W.3d 185 (Ky. 2018) on September 27, 2018. In *Sexton*, the Kentucky Supreme Court adopted the United States Supreme Court's analysis for constitutional standing found in *Lujan v. Defenders of Wildlife*, 504 U.S. 555 (1992). This analysis requires a plaintiff to have suffered an injury in fact that can be causally connected to the alleged conduct, and that all Kentucky courts have a responsibility to ascertain standing to determine whether a cause is justiciable. *Sexton*, 566 S.W.3d at 188.

On June 1, 2020 and shortly before the Kentucky Supreme Court reached its decision in *Overstreet*, the Supreme Court of the United States rendered its decision in *Thole v. U.S. Bank N.A.*, 140. S.Ct. 1615 (2020). The United States Supreme Court held in *Thole* that the Plaintiffs therein lacked standing to bring their action for mismanagement of their pension plans under the Employee Retirement Income Security Act ("ERISA"). *Thole*, 140 S.Ct. at 1618. In short, because standing requires "an injury in fact that is concrete, particularized, and actual or imminent" and the plaintiffs in *Thole* were members of defined-benefit plans rather than defined-contribution plans, the plaintiffs lacked a sufficient injury because they were "legally and contractually entitled to receive those same monthly payments for the rest of their lives." *Id*. at 1619-20. Whether or not

[2] See *Overstreet v. Mayberry*, *Id.* at 265, footnotes 4 and 6.

the plaintiffs won or lost, "they would still receive the same monthly benefits that they are already slated to receive." *Id*. at 1618.

In the present matter, both interlocutory appeals and the writ of prohibition came before the Kentucky Supreme Court for oral argument, and the Supreme Court thereafter rendered its Opinion on July 9, 2020. The Supreme Court held that the Original Plaintiffs lacked standing to pursue this action, since they had a statutorily-declared inviolable contract with the Commonwealth that guaranteed their retirement payments in fixed amounts regardless of KRS mismanagement or failure. *Overstreet v. Mayberry*, 603 S.W.3d 244, 253-54 (Ky. 2020). Further, because they lacked a sufficient personal injury, the Original Plaintiffs were found to lack standing in a derivative capacity on behalf of KRS. *Id*. at 257. The Supreme Court disagreed with analogizing this situation to mismanagement of a trust, since a trust beneficiary has rights in trust assets and KRS members instead had rights to receive their fixed retirement payments. *Id*. at 262. The Supreme Court also held that the Original Plaintiffs lacked standing as taxpayers to pursue their claims on behalf of the Commonwealth. *Id*. at 264-65.

Importantly, the Supreme Court noted that it is the obligation of the Attorney General to bring lawsuits in a derivative capacity on behalf of the Commonwealth. *Id*. at 265. In discussing the role of the Attorney General, the Supreme Court stated that the Attorney General is empowered to bring suits on behalf of the Commonwealth in situations where the Commonwealth is the real party in interest. *Id*. And, the Attorney General has broad discretion to evaluate particular facts and to decide whether or not to bring suit. *Id*. The Supreme Court presumed that the Attorney General must have exercised this discretionary power to decline to pursue this action, as the Office of the Attorney General ("OAG") had not been involved in the suit up to that point. *Id*. at 266.

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Upon determining that the Original Plaintiffs did not have standing to bring their suit, the Supreme Court decided that it did not need to reach the issue of immunity or other issues. *Id*. at 251. Accordingly, the Supreme Court "dismiss[ed] this case" and "remand[ed] this case to the circuit court with direction to dismiss the complaint." *Id*. at 249-51; *Id*. at 266. The Supreme Court's ruling became final on July 30, 2020.

Following entry of the Supreme Court's decision on July 9, 2020, but prior to the decision becoming final on July 30—multiple parties have filed motions attempting to revive this case. The OAG filed its Motion to Intervene on Behalf of the Commonwealth of Kentucky on July 20, 2020. The OAG argues that it has an unconditional right to intervene in this case, and argues in the alternative that the Court should allow it to permissively intervene. Further, the OAG asserts that its Motion is timely, arguing that it filed its Motion less than ten days after the Supreme Court rendered its decision and that the case was stayed pending litigation of the standing issue at the appellate courts.

Also after the Kentucky Supreme Court's ruling but before its finality, Plaintiffs filed their Motion for Leave to File Second Amended Complaint on July 29, 2020. In an effort to allege more particular injuries in response to the Supreme Court's decision, Plaintiffs propose to amend their Complaint in several respects. First, they seek to add an assertion that Plaintiffs' Cost of Living Allowance ("COLA") benefits were eliminated by the legislature in 2013 as a result of the financial condition of KRS. Second, they seek to add a claim that all Plaintiffs hold health insurance coverage—funded in part by mandatory personal contributions from KRS members—which are not protected by any inviolable contract and thus are not guaranteed in the same manner as their defined benefit payments. Third, the Plaintiffs seek to amend their Complaint to add three plaintiffs who were enrolled in KRS after January 1, 2014 and thus are not enrolled in a defined benefit plan

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and whose benefits are not protected by an inviolable-contract statutory provision. Rather, these new Plaintiffs' monthly benefits upon retirement depend upon the performance of KRS assets, and therefore would have their retirement benefits reduced though mismanagement of KRS funds.

ANALYSIS

The Court finds that the Kentucky Supreme Court's ruling requires the dismissal of all claims filed by the original Plaintiffs and that it would be an abuse of discretion to allow those parties to revive their action by filing a Second Amended Complaint after the Supreme Court's ruling directing dismissal of their claims. Nevertheless, this Court further finds that the Kentucky Attorney General has the right to intervene in this action to assert all claims of the Commonwealth, and that his intervention is not precluded by the ruling of the Supreme Court dismissing the private claims asserted by the original Plaintiffs for lack of standing.

I. The Writ of Prohibition Entered by the Court of Appeals is Moot and Therefore No Longer Deprives this Court of Jurisdiction

As a preliminary point, several Defendants assert that the decision in *Overstreet* left the writ of prohibition issued by the Court of Appeals undisturbed. The Court disagrees. Rather, the Kentucky Supreme Court in *Overstreet* clearly stated that the writ of prohibition entered by the Court of Appeals finding that this Court was acting outside of its subject-matter jurisdiction due to a lack of standing by the Original Plaintiffs is no longer in effect. In two footnotes, the Supreme Court states that the writ of prohibition is now moot. Footnote four states that the Supreme Court entered an order simultaneous with its decision that dismissed the writ of prohibition case as moot. *Overstreet*, 603 S.W.3d 244, n.4 (Ky. 2020). Footnote six explicitly states that "[o]ur dismissal of this case renders the Writ Case moot." *Id.* n.6. Further, the writ issued by the Court of Appeals never became final. It was appealed to the Kentucky Supreme Court, where the Court explicitly held that it was no longer in effect. Moreover, the Supreme Court of Kentucky explicitly remanded

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this case to this Court, obviously recognizing the jurisdiction of this Court to rule on matters properly brought before it under the Civil Rules. Accordingly, the Court is not prevented from considering the pending Motion to Amend and Motion to Intervene.

II. Plaintiffs' Motion for Leave to File Second Amended Complaint Is Denied, and the Original Plaintiffs are Dismissed

Upon review of the Supreme Court's ruling in *Overstreet*, the Court denies the Original Plaintiffs' Motion to Amend and therefore dismisses them from this action. Granting leave to amend is largely a matter left to the discretion of the circuit court: "whether a party may amend his complaint is discretionary with the circuit court, and we will not disturb its ruling unless it has abused its discretion." *Kenney v. Hanger Prosthetics & Orthotics, Inc.*, 269 S.W.3d 866, 869-70 (Ky. Ct. App. 2007). When deciding whether to grant leave to amend a complaint, a circuit court "may consider such factors as the failure to cure deficiencies by amendment or the futility of the amendment itself." *Id*. at 869 (*quoting First National Bank of Cincinnati v. Hartman*, 747 S.W.2d 614, 616 (Ky. Ct. App. 1988)). Further, a circuit court should consider whether the proposed amendment "would prejudice the opposing party or would work an injustice." *Id*. (*citing Shah v. American Rubber Corp.*, 655 S.W.2d 489, 493 (Ky. 1983)).

The ruling in *Overstreet* demonstrates that the Supreme Court intended to terminate the complaint brought by the Original Plaintiffs. The Supreme Court opinion does not provide for any post-appellate amendments to the complaint to cure the defects in standing. Again, the United States Supreme Court issued its opinion in *Thole* on June 1, 2020, shortly before the Kentucky Supreme Court rendered its decision in *Overstreet*. The plaintiffs in *Thole*, as members of a defined-benefit retirement plan, lacked a concrete injury in fact based on alleged mismanagement of their pension plans because they were "legally and contractually entitled to receive those same monthly payments for the rest of their lives." *Thole*, 140 S.Ct. at 1619-20. As the PAAMCO

Defendants note in their Objection to Further Proceedings, the Original Plaintiffs submitted a Motion For Leave to Submit New Authorities to the Kentucky Supreme Court in light of *Thole* prior to its decision in *Overstreet*. This was done in an effort to respond to and comply with the recently-rendered *Thole* decision. However, this request was denied by the Kentucky Supreme Court, and it instead rendered its decision adopting the reasoning in *Thole* without further briefing.

The *Overstreet* opinion itself prevents the Original Plaintiffs from continuing in this case. The Kentucky Supreme Court reversed this Court's Opinion and Order and remanded the case "with direction to dismiss the complaint." *Overstreet*, 603 S.W.3d at 249-50, 266. Accordingly, the language of the *Overstreet* opinion as well as the procedural history of this case further reflects a directive by the Supreme Court of Kentucky to disallow the Original Plaintiffs to proceed in this matter by further amending their complaint.

Further, federal caselaw lends support to the idea that it is not beyond the discretion of this Court to disallow the Original Plaintiffs from adding additional plaintiffs or adding additional claims through amendment to ensure that at least some plaintiff in this action has constitutional standing to bring this suit. "Threshold individual standing is a prerequisite to all actions." *Fallick v. Nationwide Mut. Ins. Co.*, 162 F.3d 410, 423 (6th Cir. 1998). In *Lans v. Gateway 2000, Inc.*, the Federal District Court of Washington, D.C. discussed FRCP 15(a)—the federal analogue to Kentucky's CR 15.01—and noted that while there is a general rule permitting free amendment of complaints, the D.C. District Court declined amendment because plaintiffs sought to add a plaintiff who had standing to sue in order to "retroactively create jurisdiction." *Lans v. Gateway 2000, Inc.*, 84 F.Supp.2d 112 (D.D.C. 1999), *aff'd*, 252 F.3d 1320 (Fed. Cir. 2001). In *Summit Office Park v. United States Steel Corp.*, the United States Court of Appeals for the Fifth Circuit determined that if a plaintiff never had standing to assert a claim, then the plaintiff does not have standing to

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substitute new plaintiffs or a new cause of action by amending a complaint. *Summit Office Park v. United States Steel Corp*., 639 F.2d 1278, 1282-83 (5th Cir. 1981).

As for the Original Plaintiffs' request to amend their complaint to state additional claims, the United States Court of Appeals for the Eleventh Circuit declined similar amendment in *Canon Latin America, Inc. v. Lantech (CR), S.A.* There, the plaintiff sought to reopen a case following dismissal on remand to the district court and amend their complaint to include additional claims not included in either their original or first amended complaint. *Canon Latin America, Inc. v. Lantech (CR), S.A.*, 382 Fed.Appx. 797, 798-99 (11th Cir. 2010). The Eleventh Circuit held that it was not an abuse of discretion for the district court to deny the plaintiff's motion to amend its complaint where the claim it sought to amend was not pled at the outset and did not include the claim in its amended complaint. *Id*. The court noted that the plaintiff "could have—and should have—sought amendment to state its claim for damages stemming from breach of the forum selection clause long ago in the litigation."

In the instant case, the Original Plaintiffs could have included each of these claims at the outset of litigation, but they did not do so. Their proposed claims related to deprivation of their COLA benefits and their insurance benefits lacking contractual protection could have been brought at the start of this suit. These harms existed when this suit was brought, but the Original Plaintiffs did not include them in either their original complaint or its first amended complaint. As in *Canon*, the Court exercises its discretion in disallowing amendment to add additional claims.

In sum, the Court declines to allow the Original Plaintiffs to file a Second Amended Complaint for two reasons. First, the Court observes the circumstances surrounding the *Overstreet* opinion and the procedural history of this case reflects an intent by the Kentucky Supreme Court to not allow the Original Plaintiffs to continue. Second, the discretion to permit amendment to a

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complaint lies with a trial court; other trial courts, for persuasive reasons, have declined to permit amendment in cases similar to the one presently before the Court. Accordingly, the Court denies the Original Plaintiff's request to file a Second Amended Complaint to add new parties or claims to allow them to proceed in this action.

III. The Attorney General's Motion to Intervene Is Granted

Notwithstanding the Supreme Court's direction to dismiss the complaint of the Original Plaintiffs, the Court finds that the Supreme Court did not address the other issue now before this Court: whether the Attorney General may file an Intervening Complaint. As noted above, the Supreme Court instructed this Court upon remand to "dismiss the complaint." *Overstreet*, 603 S.W.3d at 249-51, 266. The Supreme Court also stated in its decision that "[b]ecause we find that Plaintiffs lack an injury in fact sufficient to support constitutional standing, we dismiss this case and do not reach the immunity issue." *Id*. at 251. However, the subsequent action of the Attorney General, in filing his motion to intervene, is in no way precluded by the ruling of the Supreme Court.

Instead, the Supreme Court discussed at length the role of the Kentucky Attorney General to pursue lawsuits on behalf of the people of the Commonwealth. As the Supreme Court notes in *Overstreet*, the Attorney General is empowered by KRS 15.020 "to represent the Commonwealth in cases in which the Commonwealth is the real party in interest." *Overstreet*, 603 S.W.3d at 265. The Supreme Court observed that it the Attorney General who performs this role and not individuals such as the Original Plaintiffs. *Id*. The Attorney General "is entrusted with broad discretion in the performance of his duties, which includes evaluating the evidence and other facts to determine whether a particular claim should be brought." *Id*. The Attorney General's "authority necessarily includes the 'broad powers to initiate and defend actions on behalf of the people of the

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Commonwealth.'" *Id.* (*quoting Commonwealth ex rel. Conway v. Thompson*, 300 S.W.3d 152, 173 (Ky. 2009)). "It is the Attorney General's responsibility to file suit to vindicate public rights, as attorney for the people of the State of Kentucky." *Conway*, 300 S.W.3d at 173; *see also Commonwealth ex rel. Beshear v. Commonwealth ex rel. Bevin*, 498 S.W.3d 355, 361 (Ky. 2016) (noting that the Attorney General is empowered to bring suit to vindicate the public interest of the Commonwealth).

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).

In *Hancock v. Terry Elkhorn Mining Co., Inc.*, residents of Johnson County, Kentucky living near two state highways sought to enjoin the defendant mining company and others from driving trucks that violated the roads' weight limits. *Hancock v. Terry Elkhorn Mining Co., Inc.*, 503 S.W.2d 710, 711 (Ky. Ct. App. 1973). In reversing the Johnson Circuit Court, the Kentucky Court of Appeals—then the highest court in the Commonwealth—determined that the Attorney General had the right to intervene in the case. *Id.* at 715. The Court of Appeals observed that KRS

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15.020 obligates the Attorney General to "exercise all common law duties and authority pertaining to the office of the attorney general," and that such common law duties include "protecting the interest of all the people" of Kentucky. *Id*. Further, in discussing CR 24.01 and whether the plaintiffs' interests were protected in the absence of the Attorney General, the Court of Appeals observed that "the individuals who filed this action really had two interests they were seeking to protect." *Id*. While the plaintiffs had personal interests in their homes and property, they also had "a public interest involving their concern over the continued destruction of the state highways by overweight trucks." *Id*. Thus, because the Attorney General is charged with protecting the interests of the population broadly, the Court of Appeals reversed the circuit court and permitted the Attorney General to intervene under CR 24.01. *Id*.

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 not only empowered by KRS 15.020 to appear in cases such as the present case, "[the Attorney General] *shall* also commence all actions or enter his appearance in all 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. Similar to the plaintiffs in *Hancock*, 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 for that reason that the Attorney General has an interest in this action, and in light of *Overstreet* this interest would no longer be adequately pursued without the Attorney General being permitted to intervene.

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As the OAG notes in its Motion to File Intervening Complaint, the conduct of the Defendants in this case is alleged to have caused severe financial damage to the Commonwealth by diminishing the KRS asset pool by several hundred million dollars and further contributing to KRS's 25-billion-dollar shortfall. As the Supreme Court stated in *Conway*, the Attorney General is the attorney for the people of Kentucky, and it is clear that the Commonwealth has an interest in intervening in this case. Thus, the Court finds both that KRS 15.020 grants the Attorney General a statutory right to intervene in this case under CR 24.01(1), and that without his intervention that interests in this case would not be adequately represented. In the alternative, the Court finds that the Attorney General has a sufficiently strong interest to intervene under CR 24.02. The Attorney General filed his Motion prior to the Supreme Court's decision becoming final, and thus his Motion is timely.

The Court notes that the Supreme Court's ruling in this case was based in large part on the U.S. Supreme Court's holding in *Thole*, a decision which had not been rendered at the time of the filing of this action. More importantly, the *Thole* case had not been decided when the OAG originally declined to participate as a plaintiff in this action. At the time former Attorney General Beshear declined to participate in the original litigation, it appeared that the interests of the Commonwealth were adequately represented by highly competent counsel who were aggressively litigating those claims. There was no controlling case law that indicated the original Plaintiffs lacked standing at the time the Attorney General's office originally declined to join in the litigation. This change in circumstances justifies the change in position on the part of the Attorney General.

Moreover, this Court further recognizes that the newly elected Attorney General Cameron should not be bound by the initial decision made by his predecessor—General Beshear—prior to this change in the law of standing. Had this Court originally decided the standing issue on the same

grounds adopted by the Kentucky Supreme Court (denying the named Plaintiffs' standing to sue), it would have been duty-bound to allow the Attorney General to intervene (upon the filing of a motion to intervene prior to finality). The passage of time during the appellate proceedings should make no difference in the Court's ruling on a motion to intervene by the Attorney General, who came forward with the motion to intervene within days of the Supreme Court ruling, and prior to its finality.

The intervening Complaint tendered by the Attorney General mirrors the original claims of the Plaintiffs that allege 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 engaged by the Board to manage these retirement investments. If those allegations are true, thousands of public employees have had their retirement savings depleted by investments that included self-dealing, exorbitant fees, conflicts of interest, and risky non-prudent investment strategies. Moreover, if the claims can be proven, then the state itself is now on the hook for replenishing the staggering losses of public funds that resulted from these alleged breaches of duties.

The ruling in *Thole* holds that retirees whose funds were depleted have no standing, because they are still entitled to their full defined benefit pension; the Commonwealth of Kentucky will simply have to come up with the money to fund these benefits from other sources. Of course, this means that the Commonwealth will have to make up the funds depleted from these alleged breaches of fiduciary duties by one of two methods: raising taxes or cutting services. While such actions may (or may not) make the individual Plaintiffs whole, there can be no question that such remedial actions would inflict a serious financial injury on state government, and the public as a

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whole. This is why the Kentucky Supreme Court went to great pains to specifically point out that the Attorney General has standing to pursue such claims.

Kentucky law has long recognized that "there is no wrong without a remedy". *See Conrett's Ex'r v. Rice*, 187 S.W.2d 544 (Ky. 1945). Here, unless the Court grants the Attorney General's Motion to file the Intervening Complaint, there could be a serious wrong with no remedy. Under the law, the hedge fund managers and officers, directors, and advisors to the Kentucky Retirement Systems, who allegedly breached their fiduciary duties to the public, must be held accountable. Any party that breached its fiduciary duties and engaged in reckless conduct, conflicts of interest, or self-dealing should be accountable under the law. Those breaches of duty are unproven at this early stage of the litigation, but in ruling on the Motion to Intervene, the Court must assume the validity of the claims asserted. These alleged breaches of duty potentially resulted in the depletion of hundreds of millions of dollars of public funds, which the taxpayers of the Commonwealth will be obliged to indemnify.

This Court does not believe that the Kentucky Supreme Court intended its ruling in *Overstreet* to be applied so as to provide a free pass, or "get out of jail free" card, for fiduciaries who breached their duties to the public and the taxpayers. Accordingly, this Court must grant the Attorney General's motion to file an Intervening Complaint. While some or all of the Defendants may have valid defenses on the merits, the Attorney General is entitled to his day in court to prove these allegations.

CONCLUSION

While this case has been ongoing since 2017 and has passed through each appellate level before finding itself again before this Court, the case has not progressed beyond a motion to dismiss. At the motion to dismiss stage, the Court is required to view the allegations in the

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complaint in a light most favorable to the plaintiff. *Gall v. Scroggy*, 725 S.W.2d 867, 869 (Ky. Ct. App. 1987). With that in mind, the Court notes that while the Original Plaintiffs lack standing to pursue their claims by being members of defined benefit plans, each iteration of their Complaint contains allegations of severe misconduct and breaches of fiduciary duties of Defendants related to management of KRS assets. The Kentucky Supreme Court observed as much in *Overstreet*, recognizing that "Plaintiffs allege significant misconduct." *Overstreet*, 603 S.W.3d at 266. Fiduciary duties exist in all circumstances where there is a "special confidence reposed in one who in equity and good conscience is bound to act in good faith and with due regard to the interests of the one reposing confidence."*Steelvest, Inc. v. Scansteel Service Center, Inc.* 807 S.W.2d 476, 485 (Ky. 1991) (*quoting Security Trust Co. v. Wilson*, 210 S.W.2d 336, 338 (Ky. 1948)).

Serious breaches of fiduciary duties have been alleged in this case, and the Court believes that statute, case law, the Civil Rules, as well as principles of equity and public interest, require that the factual allegations in this case—and the defenses asserted by all Defendants—should be adjudicated on the merits and not dismissed on a legal technicality. Because the Attorney General is empowered by statute, the Civil Rules, and the decision of the Kentucky Supreme Court in this case, to intervene in suits such as these, the Court finds that the Attorney General must be allowed to take over this case and pursue these claims on their merits.

Being sufficiently advised, **IT IS ORDERED:**

1. The claims of the Original Plaintiffs adjudicated by final decision of the Kentucky Supreme Court in *Overstreet* are **DISMISSED** for lack of standing;
2. The Motion of the Original Plaintiffs to File a Second Amended Complaint is **DENIED;**

3. The Motion for Leave to File Second Amended Complaint, to the extent that it seeks to add new claims of the Tier 3 movants (Ashley Hall-Naqy, Tia Taylor and Bobby Estes), who seek to join in the claims of the original Plaintiffs and assert related claims on behalf of state employees who are part of the defined contribution, rather than defined benefit, pension program, is **DENIED** without prejudice;
4. The motion of the Attorney General to file the Intervening Complaint is **GRANTED** under CR 24.01 and CR 24.02, and the Intervening Complaint of the Attorney General is hereby **FILED** of record as of this date**.**

So **ORDERED** this the 28th day of December, 2020.

/s/ HON. PHILLIP J. SHEPHERD
electronically signed
12/28/2020 2:27:20 PM ET

PHILLIP J. SHEPHERD, JUDGE
Franklin Circuit Court, Division I

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COMMONWEALTH OF KENTUCKY
COUNTY OF FRANKLIN CIRCUIT COURT
DIVISION II
CASE NO. 21-CI-00645

TIA TAYLOR, *et al.*, as Members and Beneficiaries of Trust Funds of the KENTUCKY RETIREMENT SYSTEMS, Its Pension and Insurance Trusts for the Benefit of Those Trusts — PLAINTIFFS

vs.

[PROPOSED] ORDER GRANTING THE TIER 3 TRUST PLAINTIFFS' MOTION FOR STATUS CONFERENCE AND SETTING STATUS CONFERENCE

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

Having considered the motion of Tia Taylor, Ashley Hall-Nagy, Bobby Estes and Jacob Walson for a status conference, and good cause appearing, the Court grants the motion and orders that this matter shall come before the Court for a status conference on June ____, 2022, at ____:____ __.m., in Courtroom E of the Franklin County Courthouse.

SO ORDERED, this ____ day of June, 2022.

_____
THOMAS D. WINGATE
Judge, Franklin Circuit Court