UNITED STATES DISTRICT COURT
DISTRICT OF MASSACHUSETTS

ARKANSAS TEACHER RETIREMENT SYSTEM, on behalf of itself and all others similarly situated, Plaintiff, v. STATE STREET BANK AND TRUST COMPANY, Defendant.	No. 11-cv-10230 MLW
ARNOLD HENRIQUEZ, MICHAEL T. COHN, WILLIAM R. TAYLOR, RICHARD A. SUTHERLAND, and those similarly situated, Plaintiff, v. STATE STREET BANK AND TRUST COMPANY, STATE STREET GLOBAL MARKETS, LLC and DOES 1-20, Defendants.	No. 11-cv-12049 MLW **FILED UNDER SEAL**
THE ANDOVER COMPANIES EMPLOYEE SAVINGS AND PROFIT SHARING PLAN, on behalf of itself, and JAMES PEHOUSHEK-STANGELAND, and all others similarly situated, Plaintiff, v. STATE STREET BANK AND TRUST COMPANY, Defendant.	No. 12-cv-11698 MLW

MEMORANDUM OF LAW IN SUPPORT OF LABATON SUCHAROW LLP'S
MOTION CONCERNING ISSUES RAISED AT MAY 30 HEARING

INTRODUCTION

The Court-appointed Special Master (the "Master") has filed an Executive Summary, Report & Recommendations, and exhibits (cumulatively, the "Master's Submission") following an investigation of approximately fourteen months' duration. The Report alone is comprised of 377 pages, and the Master's Submission in totality is approximately 10,000 pages. The cost of the Master's investigation, imposed by the Court on the three Customer Class Counsel law firms,[1] has been $3,800,000 to date. Within the costly and heavily disputed, but intricately detailed, Master's Submission, no suggestion whatsoever exists of alleged wrongdoing in the nature of public corruption. There is no such contention in this case. The concept was introduced by the Court *sua sponte*, during the hearing on May 30, 2018. This compels the inference that the Court's injection of this issue into the case was a product either of the Court's own idea untethered to the record, or, perhaps a suggestion by the Master that he did not sufficiently credit to include in his Submission.[2] In either instance, the suggestion conveyed by the Court in the sidebar exchange, and the related questions directed by the Court to the Executive Director (the "Executive Director") of class representative Arkansas Teacher Retirement System ("ATRS"), are the principal bases upon which this motion is premised. The motion secondarily relates to whether the Court's impartiality might reasonably be questioned in passing upon the Firm's challenges to the cost of the Master's proceeding; the manner in which the proceedings have been conducted; the role that the Master has played and continues to play;

[1] Customer Class counsel are Labaton Sucharow LLP ("Labaton"), Lieff Cabraser LLP, and the Thornton Law Firm

[2] Labaton is not aware of any direct evidence that an *ex parte* communication of this nature between the Master and the Court actually occurred. Clearly, it was not the intention of the Court that such communications would occur other than in circumscribed circumstances: In the Court Order of March 8, 2017, the Court directed that the Master communicate with the Court *ex parte* only "with permission," on "particular substantive matters," and that such requests "should be minimized." ECR No. 173 at 4.

and selecting between differing expert views, one of which places responsibility on the Court itself and the other of which diverts it (albeit without support in the existing law) to one of the parties.

28 U.S.C. § 455(a)

Labaton brings this motion pursuant to 28 U.S.C. § 455(a) ("§ 455(a)"), which provides that, "[a]ny justice, judge, or magistrate judge of the United States shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned." For the reasons discussed below, Labaton respectfully requests that the Court consider whether the Court's impartiality in these *de novo* proceedings might reasonably be questioned in light of the *sua sponte* injection of "questions" of public corruption into these proceedings, in the absence of any evidence or suggestion of the same in the Master's Submission.

CONTEXT

As of the May 30 hearing, the context in which the Court was operating at the outset of its *de novo* review of the Master's Submission was as follows: (a) the Court had yet to receive Objections to the Master's Submission; (b) the Court was aware that "many of the [Master's] . . . findings of recommended . . . fact and rulings of law, are very vigorously disputed" (May 30 Tr. at 8) but had not yet been informed of the nature of the disputes;[3] (c) the Court had not yet "studied the Report and Recommendation or the exhibits as deeply as [the Court] will" going forward (*id*. at 10); (d) the Court "ha[d]n't read all the exhibits" (*id*. at 22); and (e) the Court had not reviewed the reports of Labaton's Experts (Lobby Confr Tr. at 6-7).

[3] In the words of liaison counsel for the Customer Class law firms at the May 30 hearing, "you have only seen one side of a very, very hotly disputed story. It looks like you're reading two different books, if you put them side by side." *Id.* at 9.

THE PROCEEDINGS IN OPEN COURT

At the May 30 hearing, the Court questioned the Executive Director in open court, inquiring of him whether he knew a former Arkansas State Senator named Steve Faris (May 30 Tr. at 54); what position Mr. Faris occupied when the Executive Director assumed his role with ATRS (*id*.); whether Mr. Faris had any direct or indirect involvement with ATRS (*id*. at 54-55); whether, on how many occasions, and when the Executive Director and Mr. Faris engaged in conversations about class action lawsuits (*id*. at 55); whether they discussed law firms that might participate "in either monitoring the market for possible class action lawsuits or represent [ATRS]" *(id*. at 55); whether and when they discussed "this State Street case . . . or the aftermath of it" (*id*. at 56); whether, how often, and when they had talked "since the issues arose that prompted the appointment of the Special Master" or "after the issues arose concerning the propriety of the attorney's fees that led to the appointment of the Special Master" (*id*. at 56-57); whether the Executive Director was the one to initiate the latter communication (*id*.); whether the Executive Director discussed Labaton with Mr. Faris (*id*. at 58-59, again at 60); what, if anything, Mr. Faris said about Labaton (*id*. at 59); whether Mr. Faris told the Executive Director that he (Faris) had a role in introducing Labaton to ATRS (*id*. at 59, again at 61); when the two of them had the first such discussion (*id*. at 61); what each of them said in that discussion (*id*. at 61-62); when they had the second conversation on that topic (*id*. at 62); whether the Executive Director had communicated with Mr. Faris after receiving the Master's Report and Recommendation (*id*. at 62); what Mr. Faris said in response to learning that a hearing was occurring the following week in the State Street case (*id*. at 63); whether Mr. Faris's visit to the Executive Director on Memorial Day this year was unusual (*id*.); and whether Mr. Faris had left the state legislature (*id*. at 64). Each response rebutted, rather than supported, any implication that public corruption had occurred.

At the conclusion of the Court's interrogation of the Executive Director, the Court asked whether the Executive Director was aware that Labaton had been accused of misconduct, and whether, if it were to be proven that Labaton had failed to be candid with the Court, the Executive Director agreed that that would constitute misconduct. *Id*. at 72. The Court then asked whether it had occurred to the Executive Director that, "particularly if I find that Labaton engaged in misconduct, that finding could also be harmful to Arkansas Teacher's reputation." *Id*. at 73. The Court also asked whether the Executive Director had "ever heard of a case where there was a 377-page Report and Recommendation regarding the conduct of the attorneys that [the Executive Director] selected." *Id*. at 76. Finally in this regard, the Court stated, "you know that questions have been raised by the Report and Recommendation with Arkansas Teacher, and they're just questions. But to the extent that those issues are litigated in this case, they could be at least embarrassing to [ATRS]." *Id*. at 78.

The Executive Director respectfully pushed back, protesting that "you seem to assume that, you know, how Labaton became associated with ATRS was in some way improper, illegal, or untoward, and I don't think the record shows that. In fact, the record specifically says they [apparently the Master and his attorney] didn't even inquire into that area." *Id*. at 81. The Court denied assuming anything, stating that he was suggesting that "it raises questions." *Id*.

Upon the Court's conclusion of his examination of the Executive Director, Customer Class Liaison Counsel Joan Lukey requested "the opportunity for the public to know right now the nature, just a nugget . . . of what you have characterized as 'misconduct,' because I fear . . . there will be assumptions of nefarious conduct." *Id*. at 82. She then asked for a sidebar to discuss being permitted "to make a brief statement as to the nature of what is at issue . . . ."

A sidebar followed, as to which the transcript is sealed.

THE SIDEBAR

Lukey requested at sidebar that she be allowed to state in open court that "the issue raised by the Special Master is whether a bare referral fee, or forwarding fee, was paid to the attorney who introduced Arkansas, and . . . the issue before the Court is whether the failure to disclose that bare referral fee was improper." Sealed Sidebar Tr. at 3. The Court demurred, stating, ". . . I think it is foreseeable that when the Report becomes public, there are going to be questions about the origin of this relationship and *whether all those millions of dollars stopped with Mr. Chargois.*" *Id*. at 4 (emphasis added). The Court continued, "Mr. Kelly [counsel to the Thornton Law Firm] was a prosecutor, and *Arkansas these days is – ears may perk up.*" *Id*. (emphasis added). When Lukey inquired as to whether the Court was suggesting that there was an impropriety involving Senator Faris with regard to the monies paid, the Court responded, "yes, *those questions occur to me when I read it*" (emphasis added), the latter pronoun presumably referring to the Master's Submission. *Id*.

Lukey strenuously objected, pointing out the total absence of any such contention in the Master's submission, such that "the suggestion that that's at play here shocks me." *Id*. at 5.[4] The Special Master made no such statement or allusion in his 377-page Report. Lukey continued, "[y]ou're suggesting public corruption. Honestly, your Honor, I am appalled that that was even said" (*Id.* at 5). In response to Lukey's subsequent direct questions, the Court denied having already formed the opinion that public corruption had occurred, but stated, "*I've formed the opinion that those are questions that are raised*," *Id*. at 8 (emphasis added).

[4] *See* Exhibit 125 to the Master's Report and Recommendations ("Master's Ex.") at 326:4-327:1 (testimony from the referring attorney that the funds stopped with him, and were paid only to his law firm colleagues, the IRS, and debt services).

THE BASIS FOR THIS MOTION

Rule 53(f)(3) of the Federal Rules of Civil Procedure requires that the Court decide all objections to the Master's recommended findings of fact *de novo*, a requirement that the Court has stated that it will follow in these proceedings as to findings, conclusions of law, and recommendations. May 30 Tr. at 34. The importance of this requirement is particularly pronounced if the Master's role is ambiguous. Here, the Court described the Master as performing a hybrid role, "serving in part as an investigator and in part as the counterpart of a magistrate judge making a report and recommendation." ECF No. 204 at 4, 12. Customer Class Counsel considered the Master to have acted throughout in an adversarial role (May 30 Tr. at 29; Sealed Sidebar Tr. at 9), while the Master disagreed with that assessment. May 30 Tr. at 29. The Master has expressly informed the Court that these proceedings pose an existential risk. In the Master's words, in an *ex parte* communication[5] with the Court, "there could potentially be serious and far-reaching adverse ramifications at least for some of the law firms, and even beyond this investigation for the practice of the Plaintiffs' class action bar and even for courts in class actions." ECF No. 216-1 at 2. Under such circumstances, a *de novo* review that both appears to be, and is, fully impartial is critical.

The Court's significant focus on Mr. Faris at the May 30 hearing, accompanied by the Court's statement that it perceives that questions of public corruption have arisen, raises a legitimate concern as to whether Labaton will receive a truly impartial review. Such a review requires that the Court enter the *de novo* process devoid of bias or predisposition. That millions of dollars paid by Customer Class Counsel have been expended on the Master's investigation without a suggestion of, or a shred of evidence to support, public corruption is telling. In the

[5] The Court made the communication public by appending it to his March 1, 2018 Order. ECF No. 216.

377-page Report, Mr. Faris' name is mentioned only in a brief passage indicating that he suggested to the law firm receiving the referral fee that an introductory call be placed to ATRS' Executive at the time, Paul Doane.[6] Report at 91.[7]

In addition, one or more of the Customer Class Counsel Firms contemplate filing shortly a motion for an accounting regarding all or certain aspects of the $3,800,000 that the Firms have been required to pay for the Master's proceedings to date; clarification as to the nature of the Master's continuing role in these de novo proceedings; and clarification as to whether they are expected to pay for any continuing costs for the Master to act in an adversarial role to them, to which costs they anticipate objecting. Because the Court selected the Master, approved his initial funding and each of his supplemental requests, and bears related responsibilities under FRCP 53(a)(3),[8] the Court is asked to consider whether "his impartiality might reasonably be questioned" in deciding such motions.

ARGUMENT

The concern raised by Labaton in this motion is whether the circumstances of the Court's interjection of a "question" of public corruption, unsupported by the record and therefore a matter of mere speculation, could cause a reasonable person to believe that the Court is not entering the *de novo* review fully impartial.

The governing law is familiar. A judge shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned. 28 USCS § 455(a). In applying § 455(a), the concern "is not [the judge's] actual state of mind at a particular time, but the

[6] The incumbent Executive Director who was examined by the Court at the May 30 hearing was not yet employed by ATRS when the relationship between ATRS and Labaton originated.

[7] Other witnesses remembered this sequence of events somewhat differently. The Special Master credited the recollection of the referring counsel who received the challenged fee division.

[8] "In appointing a master, the court must consider the fairness of imposing the likely expenses on the parties and must protect against unreasonable expense or delay."

existence of facts that would prompt a reasonable question in the mind of a well-informed person about the judge's capacity for impartiality." *In re Bulger*, 710 F.3d 42, 46 (1st Cir. 2013). Thus, the question is

> whether the charge of lack of impartiality is grounded on facts that would create a reasonable doubt concerning the judge's impartiality, not in the mind of the judge himself or even necessarily in the mind of the litigant filing the motion under 28 U.S.C. § 455, but rather in the mind of a reasonable man.

U.S. v. Voccola, 99 F.3d 37, 42 (1st Cir. 1996) (quoting *U.S. v. Cowden*, 545 F.2d 257, 265 (1stCir. 1976)). Even if the judge has the "inner conviction that he or she can decide the case fairly despite the circumstances," recusal is required if there is an appearance of partiality. *In re Martinez Catala*, 129 F.3d 213, 220 (1st Cir. 1997).

"The goal of [§ 455(a)] is to avoid even the appearance of partiality" and to "promote public confidence in the integrity of the judicial process." *Liljeberg v. Health Servs. Acquisition Corp.*, 486 U.S. 847, 860 (1988) (internal quotation omitted). *Liljeberg* is among the seminal cases in which the United States Supreme Court has provided guidance regarding recusal under § 455(a). The Court held that "scienter is not an element of a violation of § 455(a). The judge's lack of knowledge of a disqualifying circumstance may bear on the question of remedy, but it does not eliminate the risk that 'his impartiality might reasonably be questioned' by other persons." *Id*. at 859.

Possible recusal under § 455(a) should be examined under the facts and circumstances of each case. *See, e.g., In re Boston's Children First*, 244 F.3d 164, 171 (1st Cir. 2001) (recognizing "the continuing need for a case-by-case determination of such issues"). In this case,

Labaton is entitled to *de novo* review of the issues addressed in the Master's Submission.[9] *See* Fed. R. Civ. P. 53(f)(3) and (4). The theories propounded by the Master's academic expert Prof. Stephen Gillers are novel and aspirational, but they find no support in the law as it currently exists: As explained by Customer Class Counsels' several experts, whose reports the Court has not yet had the opportunity to read (Lobby Conf. Tr. at 6-7), a perceived[10] deficiency in a client's consent to a fee division under Rule 1.5(e) of the Massachusetts Rules of Professional Conduct("MRPC"), does not convert the analysis into one under MRPC 7.2 ("Advertising"). *E.g.*, Master's Ex. 240 (Report of Prof. Bruce Green) at 14-17; Master's Ex. 241 (Report of Prof. Peter Joy) at 16-27; Master's Ex. 242 (Report of Hal Lieberman) at 17; Master's Ex. 243 (Report of Prof. W. Bradley Wendel) at 15-17. Nor does MRPC 3.3 (candor to the Court) trump the requirement under Fed. R. Civ. P. 54(d)(2) that the Court ask if it wishes the parties to disclose fee divisions (*e.g.*, Master's Ex. 241 at 31-50), any more than a common law fiduciary duty to the class requires Class Counsel to make such a disclosure absent a court order in the face of Fed. R. Civ. P. 23(h). Master's Ex. 234 (Report of Prof. William Rubenstein) at 13-17.

Respectfully, Labaton requests that the Court consider whether a reasonable person could question the Court's ability to be impartial in such a *de novo* review, particularly in light of the following:

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[9] The Master proposes as a remedy for non-disclosure of the fee division that Labaton be required to disgorge $4.1 million, i.e., the same amount as the fee paid to the referring firm, of which 83% would go, not to the class, but to the ERISA lawyers. Only the 17% balance would go to the class. Master's Report at 368-69. The Master makes no recommendation that the recipient of the referral fee be required to disgorge the payment.

[10] According to the expert testimony proffered by Labaton, Labaton's engagement letter with ATRS, which permitted the payment of fees including referral fees, met the requirements of MRPC 1.5(e) as it existed on the date it was entered into. *See* Master's Ex. 241 (Report of Prof. Peter Joy) at 27; Master's Ex. 240 (Report of Prof. Bruce Green) at 19.

First, Prof. Gillers' Supplemental Report, upon which the Master relies, attempts to shift the responsibility for ensuring disclosure to the Court and the class from the Court (*see* FRCP 54(d)(2) and 23(h)) to Labaton as Lead Counsel. Because this was a permissible "bare referral" fee under MRPC 1.5(e), Labaton does not consider that anyone had an obligation to disclose, although the Court certainly had the discretion to order disclosure if it wished under FRCP 54(d)(2). Prof. Gillers advances novel interpretations of the interplay between the Massachusetts Rules of Professional Responsibility and the Federal Rules of Civil Procedure, all without existing case law support. *See, e.g.*, Master's Ex. 253 (March 20, 2018 deposition of Prof. Stephen Gillers) at 144:24-145:1 ("I know of no authority that applies 3.3 to the duty to disclose a fee agreement.");156:20-157:1 (admitting that he knows of no case that requires disclosing a fee division to the class). Class Counsels' experts opine that the responsibility for determining whether fee divisions are occurring is squarely on the Court, pursuant to FRCP 54(d)(2) and 23(h). *See generally* Master's Ex. 234; *see also* Master's Ex. 241 at 31-35. This places the Court in to the position of being required to select between differing expert views, one of which places responsibility on the Court itself and the other of which diverts it (albeit without support in the existing law) to one of the parties.

Second, the existence of the referral fee – a key in the Master's investigation – was disclosed by the Special Master to the Court in an *ex parte* February 28, 2018 letter that the Court subsequently publicly posted. *See* ECF No. 216-1. A reasonable person could ask if the attendant issue, of whether there was an obligation to disclose such fees to the Court, was also the subject of *ex parte* communications. The Court acknowledged on May 30 that it inquired about the existence of referral fees in a different ATRS case several weeks *before* the filing of the Master's Submission as a result of being "educated by this case." May 30 Tr. at 73. Such

"education" was not the product of any public filing or disclosure. The Master has been highly critical of the referral fee throughout the investigation, even though so-called "bare" referral fees are perfectly permissible under Massachusetts' Rules of Professional Conduct. *See* MRPC 1.5(e).[11] If there were *ex parte* communications regarding a central, disputed issue, this could reasonably give rise to a perception that an impartial review would no longer be feasible. *Cf. Edgar v. K.L.*, 93 F.3d 256, 259-60 (7th Cir. 1996) (finding that off-the-record briefings by court-retained experts to the Judge required recusal under, among other provisions, § 455(a), because "[a] thoughtful observer aware of all the facts . . . would conclude that a preview of evidence by a panel of experts who had become partisans carries an unacceptable potential for compromising impartiality.").[12]

Third, the Court's decision to compel the Arkansas-based Executive Director to attend a hearing in Boston on five business days' notice for the purpose of determining whether ATRS should withdraw or be removed as class representative due to a "conflict"[13] – before even hearing or reviewing any of Class Counsel's evidence – reasonably gives rise to an inference that the Court is already predisposed toward finding misconduct on the part of Labaton. Without having seen or heard any of Labaton's evidence and arguments, and before reviewing the complete Report (May 30 Tr. at 22) or the reports of Labaton's Experts (Lobby Confr. Tr. at 6-7), the Court ordered a hearing to examine whether ATRS can remain as class representative, and whether the Customer Class firms should be replaced as class counsel. When counsel for

[11] Massachusetts is one of the minority states that did not adopt the ABA Model Rule.

[12] Even if information learned in such communications were deemed "judicially acquired," which Labaton does not concede, the First Circuit has recognized that § 455(a) "permits disqualification of judges even if the alleged prejudice is the result of judicially acquired information." *United States v. Cepeda Penes*, 577 F.2d 754, 758 (1st Cir. 1978).

[13] The alleged "conflict" is apparently that the Executive Director selected Labaton as counsel, and Labaton has now been accused of – but certainly not proven to have committed – "misconduct." May 30 Tr. at 78.

Labaton raised an issue about the Court's questioning, the Court quoted highly disputed passages from the Report in response. *See, e.g.,* Sealed Sidebar Tr. at 3 (stating as fact the hotly disputed contention that "there was an assiduous effort to keep" the referral relationship "from counsel in the case and others").

Additionally and separately, Labaton requests that the Court consider whether a reasonable person could question the Court's ability to be impartial (a) in determining whether the extraordinary cost burden placed by the Court upon Customer Class Counsel (supplemented twice by the Court without providing Customer Class Counsel an opportunity to review, object, or comment) was reasonable; (b) in determining whether it was reasonable at all to impose these costs on Customer Class Counsel, particularly once the Master's inquiries became adversarial; (c) in deciding whether the Master's role should be curtailed, including with regard to *ex parte* communications with the Court, in this *de novo* stage of the proceedings. In each such instance, the Court will be asked to review a course of action that was set in motion by the Court itself, such that it would be difficult to be impartial in that review even for the most careful and thoughtful jurist; and (d) in selecting between differing expert views, one of which places responsibility on the Court itself and the other of which diverts it (albeit without support in the existing law) to one of the parties.

CONCLUSION

Under § 455(a), it is for the Court to determine whether an "objective, knowledgeable member of the public [could find] a reasonable basis for doubting the judge's impartiality." *In re Boston's Children First*, 244 F.3d at 167. Labaton respectfully requests that the Court undertake such efforts as are necessary for the Court to make that determination. If the Court concludes that § 455(a) compels recusal, Labaton respectfully requests that the Judge recuse himself from this case.

Dated: June 8, 2018

Respectfully submitted,

By: */s/ Joan A. Lukey*

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CERTIFICATE OF SERVICE

I hereby certify that on June 8, 2018, I caused a true and correct copy of the above document, filed conventionally, to be served by electronic mail on counsel for all parties and counsel for the Special Master.

/s/ Joan A. Lukey
Joan A. Lukey