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Re: In re Countrywide Corporation Shareholders Litigation
C.A. No. 3464-VCN
Date Submitted: September 3, 2008

Dear Counsel:

Five former shareholders of Nominal Defendant Countrywide Corporation object to the proposed settlement of the above-referenced action which was spawned

by Bank of America's acquisition of Countrywide.[1] Although the Complaint asserted a range of claims, the settlement reflects an understanding reached between the Plaintiffs in this action and the Defendants[2] that resulted only in additional disclosures. The transaction has closed.

The Objectors oppose a settlement for a number of reasons; they focus, however, on the derivative claims which they have sought to pursue in the California Litigation.[3] The derivative claims are based on a range of alleged fiduciary duty breaches, and some have speculated that they might have been worth as much as $2 billion. Because the Objectors, as the result of the merger, are no longer shareholders of Countrywide, they fear that they will be deemed to have lost standing to assert those claims. They assert, however, that the value of the derivative claims, now presumably belonging to Bank of America, was not duly

[1] The five Objectors, Arkansas Teacher Retirement System, Fire & Police Pension Association of Colorado, Louisiana Municipal Police Employees' Retirement System, Central Laborers Pension Fund, and Public Employees Retirement System of Mississippi, are plaintiffs in related litigation pending in the United States District Court for the Central District of California (the "California Litigation"). Reference in this letter opinion to the "derivative claims" generally encompasses the derivative claims asserted (or which the Objectors have attempted to assert) in the California Litigation.

[2] The Defendants, in addition to Countrywide, are its directors and Bank of America.

[3] They also object to settlement and release of the direct class claim for no monetary consideration.

considered by Countrywide's board before the merger or by Plaintiffs' counsel in valuing this litigation and in coming to a reasonable settlement. Moreover, they object to the failure of Plaintiffs' counsel to take steps to preserve the derivative claims for the benefit of Countrywide's shareholders in advance of the merger.[4] The questions underpinning the Objectors' theory of the case, perhaps framed too simplistically, are (1) whether the value of the derivative claims was considered by the Countrywide directors before the merger and (2) whether, in the exercise of their fiduciary duties, they should have undertaken efforts to preserve those claims—which Bank of America, as argued, neither wanted nor paid for—for the benefit of Countrywide's shareholders.[5] According to the Objectors, the Countrywide directors would be liable for any recovery on the derivative claims and, thus, it would have been in their self-interest to facilitate a merger that might be expected to allow them to escape any liability.[6]

[4] The release proposed as part of the settlement of this action excludes the derivative claims from its reach.

[5] Among the options, according to the Objectors, would have been an assignment by Countrywide of the derivative claims to a litigation trust for the benefit of its soon-to-be former shareholders or a sale of such claims.

[6] The Court, of course, expresses no view as to the merits of any such argument.

Before the Court is a dispute regarding the scope of discovery to be afforded the Objectors.[7] During a teleconference on July 3, 2008, the scope of discovery into the settlement process resurfaced. In substance, the Court asked counsel to "meet and confer" about the scope of proper discovery. The Objectors then filed broad-based discovery requests which may fairly be deemed as fulsome merits-based discovery. For example, the Objectors seek a Rule 30(b)(6) witness from both parties and nonparties regarding "the [t]he settlement of [this action], including the timing of the settlement and the bases for the decision to settle." Also, the deponents would be asked about "[t]he negotiations leading up to the settlement of [this action], including how they were initiated, how they proceeded, [and] when and how various aspects of the settlement were reached." Documents subpoenaed include "all documents concerning Bank of America's agreement to cause the surviving corporation in the transaction to indemnify and hold harmless present and former officers of Countrywide"; "all notes, memoranda, reports, summaries, and other documents concerning any meeting, including all handwritten notes of such

[7] The Objectors have moved to compel. The Plaintiffs (more specifically, their co-lead counsel), the Countrywide Defendants, Bank of America, one of the law firms representing Countrywide, and one of the investor bankers involved in the transaction have moved for protective orders or to quash various subpoenas.

meetings, and all other documents exchanged, distributed or given in connection with such meetings, concerning: (a) the Transaction . . . ."

The parties have provided the Objectors with the documents produced and the deposition transcripts generated in this action, as well as the various experts' reports.[8]

The scope of discovery in a proceeding involving approval of a settlement agreement is limited by context. If the Objectors are to be granted full-blown discovery, then one of the major incentives to settle—avoiding the expense of further discovery—is lost. On the other hand, there are instances in which unduly limiting the Objectors' opportunity for discovery would frustrate their ability to develop a sufficient factual record regarding propriety of the settlement. It is, however, significant that their task is not to win the case on the merits; instead, it is a less taxing challenge. The question for the Court is whether the settlement is fair, reasonable, and in the best interests of the shareholder class. The burden of

[8] This production is said to have been in excess of 400,000 pages. There is no reason to believe that this production is not sufficient to allow the Objectors to review why the Plaintiffs, within the context of Plaintiffs' theories of the case, committed to the settlement that they did and to evaluate the reasonableness of the settlement in that context.

demonstrating that the settlement is appropriate must be met, not by the Objectors, but by the proponents of the proposed settlement.[9]

An objector's right to discovery has been summarized:

> Although an objector may be permitted to take discovery, his or her discovery rights "are substantially more constrained" than those of party litigants seeking to take advantage of the broad scope of discovery ordinarily permitted outside the settlement context. Nonetheless, upon a showing of good cause, an objector may be allowed a limited right to investigate "the good faith of the parties to the negotiation process." Thus, an objector may be permitted to inquire into how negotiations came about, how they proceeded, and when various elements of the settlement proposal (including provisions regarding attorney's fees) were agreed upon and why. Ordinarily, inquiry may also be made into both the judgment to engage in settlement negotiations at a particular time and the judgment to recommend the particular settlement negotiated. This latter category of objector discovery generally will be limited to review of the court file in the case, all discovery previously taken in the case, and any other pertinent information generally available (and thus available to the class representative and his or her counsel).[10]

The Objectors seek to show good cause (lack of good faith or incompetence) for expanding the scope of discovery by contending that the failure to value and to preserve or otherwise account for the derivative claims demonstrates both bad faith

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[9] *See, e.g.*, *Fins v. Pearlman*, 424 A.2d 305, 308 (Del. 1980).

[10] DONALD J. WOLFE, JR. & MICHAEL A. PITTENGER, CORPORATE AND COMMERCIAL PRACTICE IN THE DELAWARE COURT OF CHANCERY §9.04[g], at 9-18 (2008) (internal quotations and citations omitted); *see Ginsburg v. Phila. Stock Exch., Inc.*, 2007 WL 2982238, at *2 (Del. Ch. Oct. 9, 2007); *In re Amsted Indus., Inc. Litig.*, 521 A.2d 1104, 1108 (Del. Ch. 1986).

and incompetence.[11] The Objectors, however, have been unable to make a showing of bad faith or incompetence. Plaintiffs' counsel did not pursue a relatively novel claim regarding the preservation of derivative claims.[12] Moreover, the operative facts supporting the Objectors' challenges are relatively undisputed; for example, there can be no debate that the Plaintiffs did not achieve a monetary recovery. In short, the traditional requirements for allowing broader discovery by objectors have not been satisfied.

The scope of discovery, however, is committed to the discretion of the Court by Court of Chancery Rule 26(c) and Court of Chancery Rule 45(c). Under these somewhat unusual circumstances, limited additional discovery is appropriate as a matter of efficiency and to avoid needless, and likely unhelpful, speculation.

The Objectors' discovery requests as initially framed were far too expansive under the circumstances, and the Plaintiffs appear to concede as much. By the time

[11] Although Plaintiffs' counsel undoubtedly will seek a fee for their efforts, no fee arrangement has been negotiated with the Defendants. In addition, the Objectors have been careful to note that Plaintiffs' counsel are not "incompetent" in a general sense. Instead, they argue that poor judgment exhibited in this action demonstrates that lack of competence in this action.

[12] Whether the Objectors will be successful in their argument along these lines is not before the Court. Maybe reasonable minds can differ; maybe the settlement is not fair, reasonable, and in the best interest of the shareholder class. Plaintiffs' counsel, however, have not fallen below that negative threshold of incompetence for purposes of this analysis.

this dispute came before the Court, they were emphasizing their need to obtain "information and discovery relating to the value of the derivative claims and, specifically, what efforts, if any, the Delaware plaintiffs made to preserve that value that could be realized through the prosecution of those claims before agreeing to the release that is in this proposed settlement."[13] Under the circumstances of this case, allowing Objectors this narrow discovery is appropriate.

Limited discovery, with a specific purpose, can meet the reasonable needs of the Objectors without unduly burdening any other party. Thus, the competing discovery motions are resolved as follows:

1. Lead Counsel for the Plaintiffs shall confirm to the Objectors whether or not they made any effort to preserve the derivative claims. This was essentially done during the telephonic oral argument on the pending motion.[14]

2. Lead Counsel for the Plaintiffs shall provide Objectors with the projections which they were using as to the valuation of the derivative claims. It is possible that this may include either work product or otherwise privileged material.

[13] Transcript (Aug. 29, 2008) at 5. This inquiry has two components. Inquiry into the value of the derivative claims is akin to merits-based discovery while inquiry into the efforts of Plaintiffs' counsel addresses process-related issues.
[14] Transcript (Aug. 29, 2008) at 37.

Without delving into the role of the attorney-client privilege and the work product doctrine in circumstances such as this, it is sufficient to note: (a) this may be the most reliable source of valuation of the claims that can be brought before the Court to enable it to make a prudent assessment of the best interests of the shareholder class;[15] (b) the information was gathered ultimately for the benefit of the class and the class will benefit from the use of such information in the context of the settlement proceedings; (c) presumably, the Plaintiffs will support their actions regarding the derivative claims by referring to the valuation of such claims and, if they intend to do so, then the basis for their valuation should be available to the Objectors before the settlement hearing; and (d) this is a very narrow intrusion into a collection of documents that otherwise might be protected from discovery.[16]

3. The Countrywide Defendants shall appropriately inform Objectors whether or not, at any time before the merger, the value of the derivative claims was estimated or projected either by them or by anyone acting on their behalf and

[15] One can certainly argue to the contrary that the Objectors, as the most vigorous advocates in favor of the derivative claims, should be able to provide sufficient information to the Court regarding the potential value of those claims.

[16] There is no apparent reason why documents would not meet the Objectors' need for discovery from Plaintiffs.

whether such estimates or projections were provided in any form to any of them.[17] If there are documents evidencing any such estimates or projections, for which no privilege is claimed, such documents will be provided to the Objectors. If a claim of privilege is asserted for any documents in this limited category, it shall be accompanied by a privilege log.

4. For the reasons set forth in the Court's bench ruling of April 11, 2008,[18] Bank of America is not required to respond further to the outstanding discovery requests regarding valuation of the derivative claims.[19]

Otherwise, the scope of the Objectors' discovery request is too broad and too burdensome under the circumstances. Objectors' motion to compel is granted to the extent set forth above; otherwise, it is denied. The motion for a protective order or to quash subpoenas filed by Defendants and certain third parties are granted, except to the extent that the Objectors' competing motion to compel is granted above.

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[17] The Countrywide Defendants have essentially conceded that no such valuation efforts occurred. Transcript (Aug. 29, 2008) at 55. Discovery from Countrywide would appear to be sufficient to meet the needs of the Objectors. Thus, the third-party movants' (i.e., counsel and investment banker) motions to quash will be granted.

[18] Transcript (Apr. 11, 2008) at 43-47.

[19] In light of these conclusions, it is not necessary to address the other challenges to the Objectors' discovery efforts.

IT IS SO ORDERED.

Very truly yours,

/s/ John W. Noble

JWN/cap
cc: Seth D. Rigrodsky, Esquire
Register in Chancery-K