UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF KENTUCKY
LOUISVILLE DIVISION
CIVIL ACTION NO. 3:13-CV-00710-TBR

SBAV LP Plaintiff,

v.

PORTER BANCORP, INC.,
J. CHESTER PORTER, and
MARIA L. BOUVETTE Defendants.

MEMORANDUM OPINION AND ORDER

This matter comes before the Court upon Defendant Porter Bancorp, Inc.'s ("Bancorp") objection, (Docket No. 181), to the Court's previously entered order, (Docket No. 179). Plaintiff SBAV LP ("SBAV") has responded, (Docket No. 185), and Bancorp has replied, (Docket No. 189). Fully briefed, this matter stands ripe for adjudication. For the reasons set forth below, the Court will overrule Bancorp's objection and will affirm the Magistrate Judge's order of January 16, 2015.

Factual Background

The instant lawsuit involves SBAV, a limited partnership; Bancorp, a publicly traded bank holding company; PBI Bank, Bancorp's wholly-owned subsidiary; Porter, chairman of the board of Bancorp and PBI; and Bouvette, president and chief executive officer of both companies. Beginning in 2010, Bancorp endeavored to raise $30 million in new capital in compliance with federal and state requirements. For the first wave of fundraising efforts, Bouvette and Porter reached out to Sandler O'Neil & Partners, LP ("Sandler"), a New York investment bank, to identify potential investors. As a result of Sandler's efforts, five investors acquired Bancorp securities as part of a private placement, which closed on June 30, 2010. The private placement yielded $27 million in proceeds. (Docket No. 92-1 at 3.) Neither SBAV nor its controlling investment advisor firm, the Clinton Group, Inc. ("Clinton") participated in this private placement.

Before the private placement closed, however, SBAV and Bancorp were introduced. Between July 1, 2010, and July 23, 2010, SBAV and Bancorp representatives considered a potential investment relationship. As SBAV conducted its due diligence, it engaged in a series of meetings, discussions, and correspondence with various PBI officials. Bancorp also allowed SBAV to access a "virtual due diligence room," which included financial information reflecting the status of accounts as of June 30, 2010. SBAV alleges that Bouvette, Porter, and others described a stable bank that actively targeted problem loans, had adequate reserves against its balances, and enjoyed regulatory approval. (Docket No. 31 at ¶ 25.) According to SBAV, these assurances echoed PBI's SEC filings, including its Annual Report for the Fiscal Year Ended December 31, 2009 ("2009 Form 10-K") and Quarterly Report for the Period Ended March 31, 2010 ("IQ 2010 Form 10-Q"). SBAV understood these documents to confirm Bouvette's and Porter's representations that the Bank had fully complied with certain regulatory restrictions instituted by the Federal Deposit Insurance Corporation (FDIC) and the Kentucky Department of Financial Institutions (KDFI) in early 2010. These restrictions followed bank examinations conducted by the two agencies in September 2009 and November 2009.

Certain provisions of the November 2009 report were included in a Memorandum of Understanding (MOU) that the Bank entered into with the FDIC and the KDFI in April 2010. (*See* Docket No. 148, Motion to Compel, Exhibit A, MOU of April 20, 2010.) According to SBAV, the Bank insisted that it had fully complied with the regulators' concerns that were addressed in the document, which it disclosed to SBAV. These concerns involved various unsatisfactory practice and conditions, including the accuracy of the Bank's loan review, its lending policies, credit relationships, risk on loans and asset classification, and the adequacy of its allowance for loan and lease losses. The Bank also provided SBAV with a draft of its next quarterly progress report; SBAV now contends that this report was "incomplete and misleading." (Docket No. 148, Motion to Compel, at 7, citing Exhibit B, email of Bouvette dated July 16, 2010.)

On July 13, 2010, SBAV's investment manager met with Bouvette, Porter, and other Bancorp executives. Ten days later, SBAV entered into a Letter Agreement with Bancorp, agreeing to invest $5 million on the same terms as the initial investments. (Docket No. 31 at ¶ 28.)

Only one day before SBAV's investment closed, on July 22, 2010, Bancorp allegedly received a comment letter from the Securities and Exchange Commission (SEC) requesting that the company provide various financial data. SBAV did not receive a copy of the letter until one week later, on July 30, 2010. SBAV contends that Defendants actively withheld disclosure of the SEC's comment letter in an effort to close the deal before SBAV could learn of the SEC's ongoing investigation. (Docket No. 31 at ¶ 39-41.) Nevertheless, SBAV made a second investment three months later, on September 27, 2010. (Docket No. 31 at¶ 30.)

PBI's regulatory troubles intensified after the SBAV deal was finalized. The FDIC and the KDFI issued a Joint Examination Report of PBI on January 3, 2011. As a result of the Joint Report, the two agencies issued a Notice of Charges and of Hearing alleging various unsound banking practices and regulatory violations that remained resolved after the MOU was issued in April 2010. (Docket No. 31 at ¶ 44-45.) The agencies entered a Consent Order against the Bank on June 24, 2011, requiring a management review and mandating that the Bank reform its internal and financial controls in order to correct the violations. (Docket No. 31 at ¶¶ 47-62.) PBI also confronted regulatory scrutiny from the Federal Reserve Bank, which imposed a binding agreement on Porter Bancorp that limited its ability to issue dividends or raise capital without approval. (Docket No. 31 at ¶¶ 44, 48.) According to SBAV, the violations identified in the consent order and the Federal Reserve Agreement were also addressed in the MOU—the same issues that the Bank had assured SBAV were being addressed in July 2010.

Although PBI began to implement the mandated reforms, its financial losses increased throughout 2011, totaling over $100 million since the initial investment. (Docket No. 101 at 13.) Its share price plunged from $11.50 per share in July 2010 to less than $1.00 at the time SBAV filed the instant action. (Docket No. 101 at 13.)

In this action, SBAV contends that the financial conditions of Bancorp and PBI were not accurately communicated prior to SBAV'S investment. Specifically, SBAV contends that Defendants misrepresented the adequacy of PBI's financial and disclosure controls; mischaracterized the problem loans within its portfolio and maintained inadequate reserves against losses for non-performing loans; misrepresented the value of the loans and other assets on its books; and misrepresented the degree to which regulators maintained confidence in its financial soundness. (Docket No. 101 at 7.) According to SBAV, Defendants' misrepresentations ultimately caused SBAV to lose its entire $5 million investment. Its Amended Complaint alleges negligent misrepresentation, breach of contract, and violation of Kentucky securities laws in connection with Bancorp's 2010 raise of capital from SBAV. (Docket No. 31.) It seeks to recover damages exceeding $4,500,000.00 in the instant action. (Docket No. 101 at 13.)

Legal Standard

Pursuant to Federal Rule of Civil Procedure 72(a), a district judge "must consider timely objections and modify or set aside any part of the [magistrate judge's non-dispositive] order that is clearly erroneous or is contrary to law." *See also* 28 U.S.C. § 636(b)(1)(A) ("A judge of the court may reconsider any pretrial matter under this subparagraph (A) where it has been shown that the magistrate judge's order is clearly erroneous or contrary to law."); *United States v. Curtis*, 237 F.3d 598, 603 (6th Cir. 2001) ("A district court shall apply a 'clearly erroneous or contrary to law' standard of review for the 'nondispositive' preliminary measures of § 636(b)(1)(A)."). This standard of review is limited in nature. *Massey v. City of Ferndale*, 7 F.3d 506, 509 (6th Cir. 1993).

> Under the clearly erroneous standard, a court reviewing a magistrate judge's order should not ask whether the finding is the best or the only conclusion that can be drawn from the evidence. Further, this standard does not permit the reviewing court to substitute its own conclusion for that of the magistrate judge. Rather, the clearly erroneous standard only requires the reviewing court to determine if there is any evidence to support the magistrate judge's finding and that the finding was reasonable.

Brownlow v. Gen. Motors Corp., No. 3:05-CV-00414, 2007 WL 2712925, at *3 (W.D. Ky. Sept. 13, 2007) (citing *Heights Cmty. Congress v. Hilltop Realty, Inc.*, 774 F.2d 135, 140 (6th Cir. 1985)).

Analysis

The objection now before the Court concerns Magistrate Judge Whalin's order of January 16, 2015, which, in pertinent part, compelled Bancorp to answer interrogatories and respond to requests for information and for production of documents related to bank examinations conducted by the FDIC and the Federal Reserve. Specifically, the conflict arises from Interrogatories 12 and 13 and Document Request Nos. 9 and 10, which provide as follows:

> **INTERROGATORY NO. 12:** Identify all examinations by governmental bodies or regulatory agencies (including the Federal Reserve, FDIC, KDFI, or SEC) conducted on Porter Bancorp or PBI Bank. For each such examination, identify:
>
> - The dates the examination took place, including the date any final examination report was issued;
> - The five people who had the most substantial communications on Your behalf with the examining agency, including a description of each person's role in the examination;
> - The five people from the agency who had the most substantial communications with You, including their roles in the examination;
> - The date, time, place, subject matter, and participants in all communications or interviews related to the examination;
> - The types of documents submitted by You to the examining agency; and
> - The types of documents submitted by You to the examining agency.
>
> **INTERROGATORY NO. 13:** Identify all investigations, enforcement proceedings, or administrative proceedings conducted by governmental bodies or regulatory agencies (including the Federal Reserve, FDIC, KDFI, or SEC) of Porter Bancorp or PBI Bank. For each such investigation, or proceeding, please identify:
>
> - The dates the investigation or proceeding took place, including the date any final order from such investigation or proceeding was issued by the agency;
> - The five people who had the most substantial communications on Your behalf with the agency, including a description of each person's role in the investigation or proceeding;

- The five people from the agency who had the most substantial communications with You, including their role in the investigation or proceeding;
- The date, time, place, subject matter, and participants in all communications related to the investigation or proceeding;
- The types of documents submitted by You to the agency conducting the investigation or proceeding; and
- Any agreements made between You and the agency conducting the investigation or proceeding.

DOCUMENT REQUEST NO. 9: All documents concerning examinations conducted of Porter Bancorp or PBI Bank by any governmental body or regulatory agency, including the Federal Reserve, FDIC, KDFI and SEC, including (a) all communications concerning each examination, (b) all documents or communications submitted by You to the examining agency, and all drafts thereof, (c) all written discovery requests You received in connection with such examinations, and Your objections, response, and agreements regarding such request, and (d) for each examination which has been concluded, (i) any final report, finding, or agreement arising out of the examination, and (ii) all documents concerning compliance with the final report, finding, or agreement.

DOCUMENT REQUEST NO. 10: All documents concerning investigations for enforcement or administrative proceedings taken against Porter Bancorp or PBI Bank by governmental bodies or regulatory agencies, including the Federal Reserve, FDIC, KDFI and SEC, including (a) all communications concerning such investigation or proceedings; (b) all Your submission to the body or agency conducting the investigation or proceedings, and all drafts thereof, (c) all written discovery requests you received in connection with such investigation or proceeding, and Your objections, responses, and agreements regarding such request, (d) any agreements made between You and the agency conducting the investigation or proceeding, and (e) all documents concerning compliance with the investigation or proceeding, including letters, plans, statements, studies, notifications and progress reports.

(Docket No. 148, Exhibit J, Document Requests; Exhibit 5, Interrogatories.)

Magistrate Judge Whalin's order granted SBAV's motion to compel concerning these interrogatories and discovery requests. (*See* Docket No. 79.) In the instant objection, Bancorp asserts three bases for its objection to Judge Whalin's order. First, it contends that Magistrate Judge Whalin erroneously concluded that state law governs questions of privilege in this case rather than the federal

bank examination privilege upon which Bancorp relies. Bancorp next contests the Magistrate Judge's determination that even if the federal bank examination privilege applies, good cause nonetheless requires production. Finally, Bancorp argues that the Order flouts federal regulations designed to afford the FDIC and the Federal Reserve notice of the discovery requests and an opportunity to intervene. The Court will address each of Bancorp's arguments in turn.

I. Does the federal bank examination privilege apply?

Bancorp first objects to the Magistrate Judge's conclusion that state law governs questions of privilege in this case. Bancorp instead points to the federal bank examination privilege, which it contends shields the contested documents from disclosure. This federal privilege emanates from general principles that protect government deliberations. *See Principe v. Crossland Sav., FSB*, 149 F.R.D. 444, 447 (E.D.N.Y. 1993) (explaining that "effective and efficient governmental decision making requires a free flow of ideas among government officials and . . . inhibitions will result if officials know that their communications may be revealed to outsiders.") (internal quotations omitted). Similar objectives inform the bank examination privilege: in an effort to promote candor between federal agencies and the banks they regulate, the privilege protects agency opinions and recommendations and banks' responses thereto. *In re Bankers Trust Co.*, 61 F.3d 465, 471 (6th Cir. 1995). As the Sixth Circuit has noted,

> Bank safety and soundness supervision is an iterative process of comment by the regulators and response by the bank. The success of the supervision therefore depends vitally upon the quality of communications between the regulated banking firm and the bank regulatory agency. . . . Because bank supervision is relatively informal and more or less continuous, so too must be the flow of communication between the bank and the regulatory agency. Bank management must be open and forthcoming in response to the inquiries of bank examiners, and the examiners must in turn be frank in expressing their concerns about the bank. These conditions simply could not be met as well if communications between the bank and its regulators were not privileged.

Id. (quoting *In re Subpoena Served Upon the Comptroller of the Currency, and the Sec'y of the Bd. of Governors of the Fed. Reserve Sys. (In re Subpoena)*, 967 F.2d 630, 634 (D.C. Cir. 1992).

Importantly, no such provision exists under Kentucky law. Instead, Kentucky's bank examination statute provides, in pertinent part:

> (1) Reports of examination, and correspondence that relates to the report of examination, of a bank or trust company shall be considered confidential information. No officer or director of a bank or trust company, employee of the department, or employee of a state or federal regulatory authority shall release any information contained in the examination, except when:
>
> (a) Required in a proper legal proceeding in which a subpoena and protective order ensuring confidentiality has been issued by a court of competent jurisdiction[.]

KRS § 286.3-470(1)(a). Although the statute specifies that bank examination materials are confidential, it does not render them privileged. So long as an adequate protective order has been issued, the materials may be lawfully disclosed pursuant to court order.[1]

At the outset, the Magistrate Judge considered whether the federal bank examination privilege or Kentucky's bank examination statute governed the parties' discovery dispute. The Magistrate Judge looked to Federal Rule of Evidence 501, which addresses whether state or federal law governs claims of privilege raised in the federal courts. Rule 501 generally dictates that federal common law governs claims of privilege in federal court; however, "in a civil case, state law governs privilege regarding a claim or defense for which state law supplies the rule of decision." Fed. R. Evid. 501. *See also Jewell v. Holzer Hosp. Found., Inc.*, 899 F.2d 1507, 1513 (6th Cir. 1990) ("[I]n any civil action, state law governs privilege regarding a claim or defense for which state law supplies the rule of decision.").

Where federal jurisdiction is premised upon diversity and each of the claims arises under Kentucky law, Kentucky law "supplies the rule of decision." *See Erie R.R. Co. v.* Tompkins, 304 U.S. 64

[1] The Court has entered an appropriate protective order in the instant case. (*See* Docket No. 104.) This protective order provides that "information protected from disclosure by statute or regulation or other law" cannot be used or disclosed "for any purpose whatsoever other than the evaluation, prosecution ,defense, appeal, or settlement of this Litigation." At §§ 4(1), 5(a). Designated documents may be shared with only certain persons, many of whom must first agree to the terms of the Protective Order. *Id.* § 5(b). Any confidential materials must be filed under seal, and such materials must be either returned to the party that produced them or certified destroyed at the end of the litigation. *Id.* §§ 6, 16(b). The Court notes that Bancorp allege that the protective order is insufficient, its remedy is to seek modification rather than to refuse production of relevant documents. *See Principe*, 149 F.R.D at 450.

(1983). Adhering to the Rule's plain language, then, the Magistrate Judge determined that Kentucky law governs the matter of privilege, rendering the bank examination documents confidential but not privileged. Accordingly, the Magistrate Judge concluded that because the statutory requirements were satisfied, the Bank was required to produce the requested information.

The Court agrees with the Magistrate Judge's conclusion. District courts within the Sixth Circuit have applied Rule 501's principle—that is, that state law governs privilege where state law supplies the rule of decision—in a broad spectrum of cases. *See, e.g.*, *Jewell.*, 899 F.2d at 1513 ("In a civil case involving claims based on state law, the existence of . . . [the physician-patient] privilege is to be determined in accordance with state, not federal, law"); *Politt v. Mobay Chem. Corp.*, 95 F.R.D. 101, 104 (S.D. Ohio 1982) (applying Rule 501 in a products liability action between diverse parties and determining that Ohio law governed the disputed physician-patient privilege); *Union Planters Nat'l Bank of Memphis v. ABC Records, Inc.*, 82 F.R.D. 472, 473 (W.D. Tenn. 1979) (applying Tennessee substantive law to resolve a question of attorney-client privilege).

Particularly relevant here, district courts have applied Rule 501 when analyzing assertions of the bank examination privilege. Judge Whalin relied upon *Michigan First Credit Union v. Cumis Insurance Society, Inc.*, a diversity case wherein a district court reversed a magistrate judge's application of the bank examination privilege. Like Kentucky, Michigan law renders bank examination reports confidential but not privileged. When a foreign insurance company sought to compel a credit union ("MFCU") to produce its examination reports, the Michigan Office of Financial and Insurance Services ("OFIS") argued against such disclosure. Although the magistrate judge applied the federal bank examination privilege, the district court rejected this reasoning.

> The magistrate judge's ruling that the federal bank examination privilege applies to the [bank examination reports and related documents] is contrary to law. In diversity actions where the plaintiff seeks recovery under state law, as here, the question of privilege is governed by state law, and federal common law does not apply. . . . The magistrate judge's reasoning for granting a protective order under Rule 26(c) was premised in part on the erroneous application of the federal common law bank examination privilege and a resulting undue burden upon OFIS and

> MFCU in distinguishing and disclosing factual materials within the OFIS Reports not covered by the federal privilege. Whether the OFIS Reports and MFCU Replies are privileged documents, however, is a question that must be decided under Michigan law.

Mich. First Credit Union, 2007 WL 789041, at *3 (citations omitted).

Magistrate Judge Moyer also looked to *In re Powell*, wherein a federal bankruptcy court considered an adversarial proceeding raised by a trustee against a bank. 277 B.R. 61, 64 (Bkrtcy. D. Vt. 1998). When the trustee sought the production of various audits and reviews, the bank and the FDIC objected, arguing that these documents were shielded by the federal bank examination privilege. *Id.* The court rejected this argument. Despite the FDIC's involvement in the case, the court held that because state law claims were at issue, the state's law of privilege also applied. *Id.* at 64 (citing Fed. R. Evid. 501).

Bancorp objects to the Magistrate Judge's reasoning upon a number of bases. It first notes that the Federal Reserve's regulations provide that although the KDFI and the FDIC conducted a joint examination that yielded the 2011 report, the FDIC retained ownership of the document. Bancorp therefore contends that because the FDIC owns the documents, federal law must apply. However, the Sixth Circuit has explained that "legal ownership of the document is not determinative" in such cases. *In re Bankers Trust Co.*, 61 F.3d at 469. Federal Rule of Civil Procedure 34(a) permits any party to serve on another party a request to produce designated documents that are "in the possession, custody, or control" of the responding party. Fed. R. Civ. P. 34(a). A party is deemed to possess documents if it has actual possession, custody, or control, or the legal right to demand the documents. *In re Bankers Trust*, 61 F.3d at 469. Accordingly, so long as Bancorp possesses the documents at issue, they fall within Rule 34's scope, even if the federal agency retains ownership or even restricts disclosure. *Id.* (citing *Resolution Trust Corp. v. Deloitte & Touche*, 145 F.R.D. 108, 110 (D. Colo. 1992) ("Rule 34, which focuses on a party's ability to obtain documents on demand . . . is not affected by the [federal agency's] retention of ownership or its unilaterally imposed restrictions on disclosure.")). Any relevant documents in Bancorp's possession are therefore discoverable under Rule 34.

Bancorp further contends that applying state law would undermine the federal interest at play. It submits that the Supreme Court has instructed federal courts to apply uniform standards under circumstances that implicate uniquely federal interests. *See Senior Unsecured Creditors' Comm. of First RepublicBank Corp. v. F.D.I.C.*, 749 F. Supp. 758, 769-70 (N.D. Tex. 1990) (explaining that "the rights and obligations of the FDIC relating to its role as guardian of the deposit insurance fund and as receiver for failed institutions is an area of uniquely federal interest."). Bancorp insists that if the Court finds that Kentucky law governs the disclosure of federal agency records and reports, no uniform federal standard could exist unless the state statute were preempted by the federal common law.

Whatever the merits of Bancorp's preemption argument, the Court cannot say that the Magistrate Judge's rejection of it was contrary to law in light of the precedents cited above—neither of which have been criticized on this ground by any published federal case. This silence is revealing, suggesting that any perceived threats to uniformity have not resulted in the chaos that Bancorp anticipates.

As noted in the Magistrate Judge's order, Bancorp suggests that in the future, the Kentucky Supreme Court may recognize a bank examination privilege similar to the federal common law privilege. Bancorp cited *Tibbs v. Bunnell*, 2012-SC-000603-MR, 2014 WL 4115912 (Ky. Aug. 21, 2014), in which the court interpreted the scope of a federal statutory privilege arising under the Patient Safety and Quality Improvement Act, acknowledging the remarkably broad work product privilege that it created.[2] As Magistrate Judge Moyer noted, however, *Tibbs* is not yet a final opinion and may not be cited as authority in Kentucky courts. What is more, *Tibbs* interpreted a statutory privilege; it did not address federal common law. Leaving those concerns aside, were the Kentucky Supreme Court to confront the question now before this Court, adopting Bancorp's reasoning would effectively abandon the language of the Commonwealth's confidentiality statute. Kentucky's highest court is unlikely to endorse such an outcome. *See Williams v. Vulcan-Hart Corp.*, 136 F.R.D. 457, 460 (W.D. Ky. 1991) ("It has consistently been the expressed policy of the Kentucky Supreme Court to decline to recognize a privilege where it has

[2] The PSQIA specified that its work product privilege applies "[n]otwithstanding any other provision of . . . state . . . law to declare that patient safety work product would be privileged and not 'subject to discovery' in connection with a . . . state . . . civil, criminal or administrative proceeding. . . ." 42 U.S.C. § 299b-22(a)(2).

not been expressed in the general laws of evidence existing in the state or in legislative enactment, except in the most compelling situations.").

For these reasons, Magistrate Judge Moyer's determination that state law governed the privilege analysis was not clearly erroneous. The Court agrees that pursuant to Federal Rule of Evidence 501, Kentucky's confidentiality statute applies; therefore, the Court need not disturb the Magistrate Judge's order as to this point.

II. Would the good cause exception override the federal privilege?

Magistrate Judge Moyer further concluded that even if federal law governed the privilege analysis, good cause would nonetheless overcome Bancorp's assertion, leaving Bancorp obligated to disclose the information at issue. The Court agrees. The bank examination privilege is qualified, rather than absolute: it does not protect purely factual matters, which fall beyond the privilege's scope and must be produced if relevant. *In re Bankers Trust Co*, 61 F.3d at 471 (citing *In re Subpoena*, 967 F.2d at 634; *Schrieber*, 11 F.3d at 220).

Given this fundamental limitation, the Court agrees with the Magistrate Judge that the bank would be required to fully respond to Interrogatories 12 and 13, which seek purely factual information: when the examination and investigation occurred, the identifies of individuals involved with such proceedings, the logistical details of any communications or interviews, and the types of documents that were exchanged between the Bank and the agency. Accordingly, the Court agrees that application of the federal common law bank examination privilege would not defeat discovery of the information sought by these two interrogatories.

Turning to Document Requests 9 and 10, the Magistrate Judge explained that certain communications concerning Bancorp's regulatory examinations likely contained deliberative opinions, which are generally privileged. However, even deliberative opinions are not protected by the privilege if

good cause exists to override it. *Id.* A court weighing the existence of good cause must evaluate at least five factors, including:

> (1) the relevance of the evidence sought to be protected; (2) the availability of other evidence; (3) the "seriousness" of the litigation and the issues involved; (4) the role of the government in the litigation; and (5) the possibility of future timidity by government employees who will be forced to recognize that there secrets are violable.

Id. (citing *Schreiber*, 11 F.3d at 220); *In re Subpoena*, 967 F.2d at 634). Examining each of the factors, the Magistrate Judge concluded that SBAV demonstrated good cause to override the federal common law privilege. Although Bancorp insists that the Magistrate Judge's analysis was flawed on all fronts, the Court must disagree.

The first three factors warrant little discussion. The information that SBAV seeks is certainly relevant; Bancorp itself has repeatedly referenced it, allegedly during negotiations with SBAV and certainly throughout the instant litigation. SBAV emphasizes that it requires specific reports to evaluate the accuracy of Bancorp's previous representations and to determine whether Bancorp withheld material information. Although Bancorp contends that this information may be gleaned from other documents, it fails tospecify which documents would accomplish this. Accordingly, the Magistrate Judge's determination that the information sought was relevant and accessible only through the records sought was sound. *See, e.g.*, *In re Franklin Nat'l Secs. Litig.*, 478 F. Supp. 577, 586 (E.D.N.Y. 1979) ("The Examination Reports provide a unique and objective contemporaneous chronicle of the financial decline of [the bank]; no satisfactory substitute exists."). And while Bancorp takes issue with the contention that the litigation is serious, at the heart of this case are allegations that Bancorp raised large amounts of capital through duplicity and deceit. While the Court makes no judgment as to the merits of SBAV's claims, it cannot be said that they are less than serious.

As to the fourth factor, which concerns the Government's role in the litigation, the Magistrate Judge noted that the lawsuit does not involve an action raised by a federal regulatory agency, nor has such

an agency attempted to intervene in the instant lawsuit in order to assert or protect a fundamental interest. In the following section, the Court will more fully consider Bancorp's argument that SBAV was obligated to notify various federal agencies of its requests for the allegedly protected materials. It will suffice to say here that the Court agrees with the Magistrate Judge's conclusion that SBAV was not so obligated.

Finally, Bancorp contends that this perceived attack on the bank examination privilege will give both examiners and bank employees pause during the frank discussions that the examination process entails, second-guessing their ability to speak candidly. The Court perceives no such chilling effect. All discovery disputes that arise under similar facts implicate the important public interest in confidentiality and candor between regulators and banks. If this factor were always dispositive, the privilege would be absolute rather than qualified; however, under some circumstances, the public's interest in the production of evidence overcomes its interest in preserving candor in bank examinations. *See Wultz v. Bank of China Ltd.* at 9. This is one such case. The Court anticipates that the parties' robust protective order will adequately safeguard forthrightness in their future communications. In light of that restriction, and given the strength of the four factors discussed above, the final factor is not determinative.

Because the Court finds no fault with the Magistrate Judge's analysis regarding the good cause exception, it will overrule Bancorp's objection on this point.

III. Was SBAV required to exhaust administrative remedies?

Finally, Bancorp challenges the Magistrate Judge's conclusion that SBAV was not required to exhaust administrative remedies before resorting to legal process in its effort to obtain the disputed documents. Pursuant to the "Housekeeping Statute" at 5 U.S.C. § 301, the federal agencies involved have promulgated administrative regulations governing the release of non-public information. Taking their name from the Supreme Court decision that validated such administrative procedures, they are known as*Touhy* regulations. *See United States ex rel. Touhy v. Ragen*, 340 U.S. 462 (1951).

Bancorp first points to 12 C.F.R. § 309.6(b)(8)(i), which provides, in pertinent part:

> Third parties seeking disclosure of exempt records or testimony in litigation to which the FDIC is not a party shall submit a request for discretionary disclosure directly to the General Counsel. Such request shall specify the information sought with reasonably particularity and shall be accompanied by a statement with supporting documentation showing in detail the relevance of such exempt information to the litigation, justifying good cause for disclosure, and a commitment to be bound by a protective order. Failure to exhaust such administrative request prior to service of a subpoena or other legal process may, in the General Counsel's discretion, serve as a basis for objection to such subpoena or legal process.

See also 12 C.F.R. § 261.22 (governing other disclosure of confidential supervisory information). Federal regulation imposes comparable procedures for requests for disclosure from the Federal Reserve. *See* 12 C.F.R. § 261.22(b)(1) ("Any person . . . seeking access to confidential supervisory information . . . for use in litigation before a court, board, commission, or agency, shall file a written request with the General Counsel of the Board.").

Although Bancorp maintained that SBAV was obligated to exhaust this administrative process, the Magistrate Judge rejected this conclusion. The Court agrees. In *In re Bankers Trust*, the Sixth Circuit dictated the appropriate course when administrative regulations are at odds with the Federal Rules of Civil Procedure. The court explained that a federal agency's regulation should be enforced if based upon a permissible construction of its enabling statute; however, such statutes generally do not permit agencies to promulgate regulations that directly contravene the Federal Rules. 61 F.3d at 469-70. The court reasoned that Congress did not empower the agency at issue to establish regulations directing a party to deliberately disobey a court order, subpoena, or other judicial mechanism requiring the production of information. Therefore, the court held that regulatory language that requires a party to continually decline to disclose such information "exceeds the congressional delegation of authority and cannot be recognized by this court." *Id.* at 471. Pursuant to *In re Bankers Trust*, the Court is convinced that the discovery order at issue is a legitimate exercise of the Court's Rule 34 jurisdiction.

Moreover, the Court notes that other federal regulations require one who has custody of agency records to notify the agency of any legal process requiring their production. *See* 12 C.F.R. § 309.7(b) (requiring such notice for FDIC documents); 12 C.F.R. § 261.23(a) (imposing the same requirement for Federal Reserve records). The Sixth Circuit also acknowledged that it is "advisable if not necessary for a party in litigation that possesses 'confidential supervisory information' to inform the Federal Reserve of any requests for production so the Federal Reserve will have notice and the opportunity to intervene and protect any interests, arguments, or concerns it may have." *In re Bankers Trust*, 61 F.3d at 470, n.6. Given the Court's limited review here, it need not reach the applicability of such guidance here. However, the Court recognizes the dearth of information on the record concerning whether Bancorp has notified federal regulators of SBAV's requests and the Court's order compelling production. Although Bancorp protests the absence of the FDIC and the Federal Reserve from the instant litigation, the Court agrees with the Magistrate Judge that this absence is not attributable solely to SBAV.

Conclusion and Order

The Court having considered Defendant Porter Bancorp, Inc.'s objections to the Magistrate Judge's order compelling production of bank examination documents, as well as Plaintiff SBAV LP's response thereto, IT IS HEREBY ORDERED that Porter Bancorp, Inc.'s objections, (Docket No. 181), are DENIED. The Magistrate Judge's January 16, 2015, Order is AFFIRMED in its entirety.

Thomas B. Russell

Thomas B. Russell, Senior Judge
United States District Court

March 30, 2015