UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re	Chapter 11
PATRIOT COAL CORPORATION, *et al.*,	Case No. 12-12900 (SCC)
Debtors.	(Jointly Administered)
EASTERN ROYALTY LLC f/k/a EASTERN ROYALTY CORP.,	Adv. Pro. No. 12-01786
Plaintiff,	
v.	**REPORT OF RULE 26(f) MEETING**
BOONE EAST DEVELOPMENT CO., PERFORMANCE COAL CO., AND NEW RIVER ENERGY CORP.,	
Defendants.	

Pursuant to Federal Rule of Civil Procedure 26(f), a telephonic meeting was held on August 16, 2012, and was attended by Antonio J. Perez-Marques, Jonathan D. Martin and Bernard Chen Zhu of Davis Polk & Wardwell LLP for Plaintiff Eastern Royalty LLC f/k/a Eastern Royalty Corp. ("**ERC**" or "**Debtor**"), and by James L. Bromley, Luke A. Barefoot and Emily Weiss of Cleary Gottlieb Steen & Hamilton LLP for Defendants Boone East Development Co., Performance Coal Co., and New River Energy Corp. ("**Defendants**").

The parties jointly submit this report of the meeting in advance of the pre-trial conference scheduled for September 25, 2012.

I. Staging of Discovery and Dispositive Motions

A. Debtor's Position

ERC's Complaint presents a pure question of law: whether the Payment Agreement dated August 31, 2005, executed by ERC and each of the Defendants, is (1) a non-executory contract for purposes of section 365 of the Bankruptcy Code, (2) that is not integrated with (or is severable from) any other agreement, including the Assignment Agreements and the Boone Lease.[1] *See*, *e.g.*, *TVT Records v. Island Def Jam Music Group*, 412 F.3d 82, 89 (2d Cir. 2005) ("If the documents in question reflect no ambiguity as to whether they should be read as a single contract, the question is a matter of law for the court."); *see also Seitz v. Paul T. Freund Corp.*, No. 07-CV-6067L, 2009 U.S. Dist. LEXIS 31939 (W.D.N.Y. Apr. 15, 2009) (ruling, as a matter of law, on whether an agreement is executory for purposes of Section 365).

[1] Capitalized terms not defined herein have the meanings ascribed to them in the Complaint.

Because both aspects of that question can be decided as a matter of law, ERC proposes to file promptly a motion for summary judgment seeking a determination that, based on its plain and unambiguous language, the Payment Agreement is a standalone, fully integrated, and non-executory contract. The Debtor's position is that discovery should be stayed briefly pending a ruling on the motion by the Court. That approach will promote judicial economy, allow for a prompt resolution of the action, avoid wasting the parties' resources, and inflict no prejudice on any party.

Defendants do not dispute that discovery will be completely unnecessary if the contract is unambiguous and can be construed as a matter of law. But Defendants also concede that they have no argument that the contract is unambiguous in their favor. Instead, Defendants contend that the contract is unclear and – because Defendants contend that extrinsic evidence will be "inevitable" – that full blown discovery should commence immediately, without any threshold determination by the Court as to whether the dispute can be resolved on summary judgment without extrinsic evidence. But as the Court is well aware, it is for the Court – not Defendants – to resolve the threshold question of whether a contract is ambiguous and thus whether extrinsic evidence is necessary. *See In re 4Kids Entm't, Inc.*, 463 B.R. 610, 681 (Bankr. S.D.N.Y. 2011) (Chapman, J.). The mere fact that Defendants have advanced a competing interpretation of the contract, or attach different meanings to its provisions, does not render the contract ambiguous. *See id.* That is for the Court to decide in the first instance.

Discovery will be necessary in this action only in the event that the Court identifies an ambiguity in the contract that requires resort to extrinsic evidence. *See id.* (ruling that "*if* ambiguity exists, *then* extrinsic evidence of the parties' intent may be

looked to as an aid to construing the contractual language" (emphasis added)). Indeed, the law is clear that the parties cannot even submit extrinsic evidence to the Court until the Court identifies an ambiguity in the contract. *See In re Lehman Bros. Inc.*, 473 B.R. 34, 55 (S.D.N.Y. 2012) (holding that bankruptcy court erred in considering extrinsic evidence "without first making a preliminary finding that the language of the [contract] was in fact ambiguous"). Defendants' proposal to engage in full discovery that can be placed before the Court on summary judgment calls for a "cart-before-the-horse, result-oriented decision . . . rather than one firmly grounded in the documents themselves." *Id.* at 56.

Apart from being required by the law, it makes practical sense to defer discovery until the Court has had an opportunity to determine whether extrinsic evidence is even necessary and, if so, on which issues. Any discovery taken in advance of that threshold determination by the Court may turn out to be wholly unnecessary. For example, Defendants have already served broad document requests and interrogatories on ERC, and served subpoenas on third parties, seeking information about a Settlement Agreement dated July 5, 2005 between Massey Coal Sales Company, Inc., and COALTRADE LLC (a subsidiary of Peabody Energy Corporation, not Patriot Coal Corporation), which Defendants contend is somehow integrated with the Payment Agreement. Notably, Defendants do not contend that their theory is supported by the plain language of the agreements, but instead wish to explore the theory through burdensome depositions (at least 8 total) and broad document demands. But if the Court agrees with ERC that the Defendants' theory is untenable based on the plain language of the separate contracts

(which, among other things, involve none of the same parties), the fishing expedition that Defendants seek would be a complete waste.

Defendants claim below that they intend to demonstrate that the Payment Agreement "is integrated with the Settlement Agreement and its other exhibits."[2] But they also candidly concede that this argument is not supportable "on the face of the agreements" – i.e., they admit that they cannot prevail as a matter of law on the four corners of the contracts. That concession explains Defendants' eagerness for the Court to conclude immediately (without bothering with full briefing) that resort to extrinsic evidence is "inevitable." But Defendants' only argument that the contracts are ambiguous, and that extrinsic evidence is "inevitable," is that the Settlement Agreement and the Boone Lease each contain integration clauses. But this supposed "ambiguity" arises only when the two contracts are incorrectly read, as Defendants urge, as a single contract. It is clear as a matter of law, as ERC will demonstrate, that the "integration clause" in the Settlement Agreement was intended simply to exclude extrinsic evidence, not to suggest that the separate contracts it contemplated – involving wholly separate and distinct parties – would constitute a single, unified agreement going forward. In fact, ERC will show that Defendants' argument that the Settlement Agreement and the Boone Lease cannot be read together without creating ambiguity actually supports ERC's

[2] This argument belies Defendants' claim that they need discovery into "the complete universe of agreements between the Parties and their affiliates." There is no dispute over the "universe" of potentially relevant agreements. ERC's position is that the Payment Agreement is a standalone, fully integrated, and non-executory contract as a matter of law. Defendants' contrary view is that the Payment Agreement is somehow integrated with the Settlement Agreement and its exhibits, a position that Defendants concede cannot be justified based on the plain language of the contracts. Defendants' request for discovery regarding the "universe" of agreements is just another way of saying that the parties should resort prematurely to extrinsic evidence.

position that, based on their plain language, the two agreements are separate. Finally, ERC will also demonstrate that, even if Defendants' integration argument were correct – which it is not – the Payment Agreement would still be severable as a matter of law and therefore a separate contract for purposes of section 365. For all of these reasons, discovery makes no sense until the Court has resolved the threshold and potentially dispositive legal issues.

Indeed, ERC attached a copy of the Settlement Agreement to the Complaint precisely so that it would be before the Court for an early ruling as a matter of law.[3] ERC is willing to brief such a motion, which can be brought pursuant to either Rule 12(c) or Rule 56, on as short a schedule as Defendants wish. A brief stay of discovery pending a ruling on the motion will cause no prejudice to Defendants. By contrast, ERC and its affiliated debtors would suffer great prejudice in the absence of a stay. Commencing discovery now, especially when it may turn out to be wholly unnecessary, would waste the debtors' limited resources at a time when management and its professional advisors are focused on achieving a successful chapter 11 reorganization. *See*, *e.g.*, *In re Rockefeller Ctr. Props.*, 272 B.R. 524, 531 (Bankr. S.D.N.Y. 2000) (staying discovery where it would be "costly and labor intensive" and would "become irrelevant if the motion for partial summary judgment were decided in favor of" the reorganized debtor).

ERC does not expect that discovery will ever be required, because the Court will be able to rule as a matter of law on the face of the agreements. However, in the event

[3] Defendants advanced their argument regarding the Settlement Agreement only after ERC filed its original motion. Defendants' suggestion below that ERC should have anticipated their argument and included the Settlement Agreement in the original motion is nonsensical, not least of all because even Defendants concede that their argument is not clear on the face of the agreements.

that the Court concludes that extrinsic evidence is necessary to construe a particular provision, discovery should be targeted to that particular issue. Defendants' contrary proposal to engage immediately and prematurely in broad discovery – without the Court's guidance as to the specific issue or issues, if any, that are ambiguous and require extrinsic evidence – will only result in unnecessary burden, expense, and distraction for both parties.

B. Defendants' Position

While ERC's position is predicated on an avoidance of "broad" or far-ranging discovery, the targeted and low-volume discovery that Defendants actually believe is necessary to resolve this case can be completed in approximately 8 weeks. As the Defendants have made clear to ERC from the beginning, full discovery, merits briefing and argument can be readily accomplished by year end. As that discovery is inevitable, the Parties should proceed to complete it promptly, after which ERC's claims can be determined in a single presentation to the Court.

To resolve the central question of whether the Payment Agreement is a stand-alone document or is an integrated part of a larger transaction, discovery is required to ensure that the documents appended to ERC's complaint are the complete universe of agreements between the Parties and their affiliates. Therefore, contrary to ERC's assertion that Defendants admit that discovery will be completely unnecessary if the contract is ambiguous, discovery of the universe of agreements is necessary before any decision regarding ambiguity can be made. The procedural history of this case demonstrates the importance of such discovery. The Debtors initially filed a motion seeking a determination that the Payment Agreement was not executory. That motion contained no mention of the Settlement Agreement, pursuant to which the Payment

Agreement was executed.[4] Only after Defendants raised the importance of the Settlement Agreement did ERC include any reference to it in its complaint. While ERC now urges this Court to determine in isolation whether its selection of the Parties' agreements are ambiguous, in order to effectively make that determination, the Parties must engage in discovery so as to apprise the Court of the universe of agreements at issue. That discovery is all the more critical since at the time the Payment Agreement was negotiated and executed, ERC was an affiliate of Peabody Energy Corporation ("Peabody"), and relevant documents may be in the possession of Peabody or its subsidiaries. Defendants have served a subpoena on Peabody seeking production of such documents.

Beyond the basic identification of all of the relevant agreements, discovery is necessary because the agreements attached to ERC's complaint are ambiguous on their face, such that extrinsic evidence is required to resolve this dispute. *See Cantrell Supply, Inc. v. Liberty Mut. Ins. Co.*, 94 S.W.3d 381, 385 (Ky. 2002); *Jessee v. Aycoth*, 503 S.E.2d 528, 531 (W. Va. 1998).[5] Defendants intend to demonstrate that the Payment Agreement, as an exhibit to the Settlement Agreement, is integrated with the Settlement Agreement and its other exhibits. This question of integration, however, cannot be decided on the face of the agreements since (a) the Payment Agreement contains no integration clause; (b) the Assignment Agreements, to which the Payment Agreement

[4] See Motion for an Order (i) Confirming the Massey Payment Agreement Is Not an Executory Contract, or Alternatively, (ii) Approving Rejection of the Massey Payment Agreement (D.I. 24 in Case No. 12-12900).

[5] The Settlement Agreement and its exhibits contain both a Kentucky choice-of-law clause and West Virginia choice-of-law clauses. See Adv. Compl. Ex. B at 6 ¶ 12; Adv. Compl. Exs. C-E at ¶ 8; Adv. Compl. Ex. F at ¶ 7.

undeniably relate, contain no integration clause; and (c) the only two documents in the agreements appended to ERC's complaint that have integration clauses have clauses that directly conflict with each other. *See Lee Enters., Inc. v. Twentieth Century-Fox Film Corp.*, 303 S.E.2d 702, 703-04 (W. Va. 1983) (reversing lower court's determination that contract was unambiguous because contract contained two conflicting paragraphs and therefore extrinsic evidence was required).

Notwithstanding ERC's suggestion that Defendants' argument is not "supported by the plain language of the agreements," the Settlement Agreement's integration clause states that the Settlement Agreement and all of its exhibits, including the Payment Agreement, "constitute the full and complete understanding, agreement and arrangement of the parties, and is the integrated memorial of their agreement." Adv. Compl. Ex. B at 7 ¶15. ERC focuses instead on the Boone Lease, which just like the Payment Agreement is an exhibit to the Settlement Agreement, and which contains its own integration clause, stating that the Boone Lease "constitutes the sole and entire existing agreement between the parties and expresses all the obligations of and restrictions imposed upon the parties." Adv. Compl. Ex. G at ¶23.7. ERC fails to address these conflicting terms. Nor is this the only term that requires resort to extrinsic evidence. Even if the terms of the Settlement Agreement do not control, because neither the Payment Agreement nor the Assignment Agreements contain integration clauses, no express terms in those documents themselves would permit the Court to determine the question of integration without resort to extrinsic evidence.

Discovery into the intent of the parties in entering into these agreements and the surrounding circumstances is thus inevitable.[6] While ERC proposes to stay that discovery pending the Court's determination on the documents themselves, such a stay is not warranted where only a modest amount of discovery is necessary and that discovery can be completed in a matter of weeks.[7] Defendants believe that the relevant agreements were negotiated and documented by a few company representatives over a few months' time. Therefore, subject to agreement on an overall discovery schedule, Defendants are prepared to agree that each Party shall be limited to serving no more than 10 interrogatories under Rule 34(a)(1). In addition, Defendants are prepared to agree that each Party shall be limited to no more than three depositions pursuant to Rule 30(b)(1) and one deposition pursuant to Rule 30(b)(6). These restrictions mean that any burden associated with discovery will be minimal. Defendants also remain willing to consider additional limitations on discovery. Aside from its proposed stay of discovery pending a motion for summary judgment on the pleadings, ERC has proposed no such restrictions.

Defendants propose the following pre-trial schedule, which Defendants believe permits for expeditious resolution of the case through a single presentation to the Court following completion of the targeted discovery described above:

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[6] *See Steve Marchionda & Assocs. v. Weyerhauser Co.*, 11 F. Supp.2d 268, 272 (W.D.N.Y. 1998) (noting that no discovery had been done yet and that because the contract was ambiguous, "summary judgment is inappropriate at this juncture"); *cf. General Packaging Serv., Inc. v. Colgate-Palmolive Co.*, No. 80 Civ. 1816, 1981 U.S. Dist. LEXIS 12287, at *1 (S.D.N.Y. Apr. 7, 1981) (denying motion to dismiss breach of contract claim because there were "possible ambiguities in crucial terms of the contract" and plaintiff had not yet had the opportunity to conduct discovery).

[7] Defendants intend to provide additional information concerning available documents in their initial disclosures, and they have already served document requests on the Debtors on August 16, 2012, immediately following completion of the Rule 26(f) conference.

Matter	Date
Initial disclosures made pursuant to Rule 26(a)(1)(A)	September 7, 2012
Discovery requests (including any third-party discovery requests) and interrogatories	September 28, 2012
Responses and objections to document requests	October 5, 2012
Responses and objections to interrogatories	October 10, 2012
Completion of the production of documents	October 26, 2012, but parties produce responsive documents on a rolling basis at the earliest possible date
Completion of depositions	November 16, 2012
Opening pre-trial briefs or motions for summary judgment[8]	December 4, 2012
Responsive pre-trial briefs	December 21, 2012
Hearing	To be scheduled by the Court

II. Initial Disclosures

A. Debtor's Position

To avoid unnecessary burden and expense, the Debtor's position is that initial disclosures required by Rule 26(a)(1) should be deferred pending the Court's ruling as a matter of law, for the same reasons merits discovery should be deferred. *See*, *e.g.*, *Flores v. S. Peru Copper Corp.*, 203 F.R.D. 92, 93 (S.D.N.Y. 2001) (staying all discovery, including initial disclosures, pending ruling on dispositive motion). If the Court ever identifies an ambiguity in the parties' agreement, then the parties will be in a better position to identify the individuals and documents that may have relevant extrinsic evidence. If the Court concludes that it can rule as a matter of law, initial disclosures will be irrelevant and unnecessary.

B. Defendants' Position

[8] In the event of a motion for summary judgment, a briefing schedule would be agreed on by the Parties or ordered by the Court.

Defendants will make the initial disclosures called for by Rule 26(a)(1)(A) no later than September 7, 2012. In these initial disclosures, Defendants intend to provide details concerning the documents, electronically stored information ("ESI"), and tangible things in their possession, custody, or control that have been located to date and the search criteria used to locate such items pursuant to Rule 26(a)(1)(A)(ii). This identification of individuals and documents for the initial disclosures is neither burdensome, nor does it depend in any way on whether the document is ambiguous. There is thus no basis to wait for a decision on the contract's ambiguity to make initial disclosures.

III. Electronically Stored Information

Given the disagreement about the scope and timing of discovery, the Parties have not yet discussed the discovery of ESI.

Dated: New York, New York
August 30, 2012

EASTERN ROYALTY LLC f/k/a EASTERN ROYALTY CORP.

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