SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

Theo Chino

Plaintiff-Petitioner,

-against-

The New York State Department of Financial Services and Maria T. Vullo, in her official capacity as Superintendent of the New York State Department of Financial Services.

Defendants-Respondents.

Index No. 101880/2015
Hon. Lucy Billings

MEMORANDUM OF LAW IN OPPOSITION TO PLAINTIFF-PETITIONER'S MOTION FOR LIMITED DISCOVERY

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TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Cases **Page(s)**

STATE STATUTES

STATE REGULATIONS

MISCELLANEOUS AUTHORITIES

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Preliminary Statement

Plaintiff-Petitioner Theo Chino commenced this hybrid Article 78 proceeding, which also includes a declaratory judgment claim, alleging that the New York State Department of Financial Services (DFS) exceeded the scope of its regulatory authority and acted arbitrarily and capriciously in promulgating a regulation that addresses virtual currency business activity in New York—claims that turn exclusively on the application of settled principles of law to undisputed facts. In April 2016, DFS filed a dispositive cross-motion to dismiss these claims for lack of standing and failure to state a cause of action. Ten months later, Chino submits the present application seeking wide-ranging discovery under Section 408 of the New York Civil Practice Law and Rules, and requests that DFS's cross-motion be held in abeyance until that motion is decided. (Pet.'s Not. of Mot. 1–2.) Specifically, Chino seeks (1) testimony from Paul Krugman—the Nobel Prize-winning economist and New York Times columnist—about the economic nature of Bitcoin; (2) an assortment of internal DFS emails and other written documentation spanning a three-year period; and (3) the deposition of the former Superintendent of DFS. (*Id.*)[1]

[1] Chino's discovery requests are made under CPLR § 408—the statutory provision governing discovery in Article 78 proceedings. But in a hybrid Article 78 proceeding and declaratory judgment action, courts must apply the "usual rules relating to discovery to them as if they were separate matters." *Price v. N.Y.C. Bd. of Educ.*, 16 Misc. 3d 543, 550 (Sup. Ct. N.Y. Cnty. 2007) (denying the petitioners' motion for discovery in a hybrid action), *aff'd* 51 A.D.3d 27 (1st Dep't 2008). The distinction between standards makes little difference here, however, because Chino's discovery requests are wholly irrelevant and unnecessary to the Court's determination of all of his claims. *See* CPLR § 3101 (in the context of an action for a declaratory judgment, discovery must be "material and necessary in the prosecution or defense of an action"). Thus, for the reasons set forth in this memorandum, Chino's discovery requests are fatally flawed under either standard.

These facially unreasonable requests must be rejected. None of the items on Chino's wish list is relevant or necessary to any of his claims. Chino's motion amounts to nothing more than a request to embark on a "fishing expedition" in the mere hope of uncovering *something* of possible relevance. But such requests—premised on conjecture and speculation—are legally impermissible. Chino's motion should be denied in its entirety.

ARGUMENT

I. Chino is not entitled to discovery in this hybrid Article 78 proceeding.

Discovery is presumptively improper in Article 78 proceedings, which are designed to facilitate a summary disposition of the legal issues presented. "Article 78 proceedings are indeed designed for the prompt resolution of largely legal issues, rather than for discovery, trials, and 'credibility judgments.'" *Council of N.Y. v. Bloomberg*, 6 N.Y.3d 380, 389 (2006) (citation omitted); *see also Town of Pleasant Valley v. N.Y. State Bd. of Real Prop. Servs.*, 253 A.D.2d 8, 15 (2d Dep't 1999) ("Because discovery tends to prolong a case, and is therefore inconsistent with the summary nature of a special proceeding, discovery is granted only where it is demonstrated that there is need for such relief"); *In the Matter of Kellenberg Mem'l High Sch. v. Section VIII of N.Y. Pub. High Sch. Ath. Ass'n*, 255 A.D.2d 320, 320 (2d Dep't 1998).

Discovery in an Article 78 proceeding is allowed only by leave of the Court. CPLR §§ 408, 7804(a). In determining whether discovery should be granted, courts first consider whether the petitioners have "a need to determine information directly related to the cause of action" and then whether the scope of the request is narrowly tailored to resolve disputed material facts. *Lonray, Inc. v. Newhouse*, 229 A.D.2d 440, 440–41 (2d Dep't 1996); *In re Shore*, 109 A.D.2d 842, 843–44 (2d Dep't 1985) (denying pre-hearing discovery under CPLR § 408 where the movant had not demonstrated "ample need," discovery would be "burdensome" for producing party, and requests were "not readily capable of being produced in a relatively short

period of time"). To direct discovery, the court must deem the information sought to be "material and necessary." *Tivoli Stock LLC v. N.Y.C. Dep't of Hous. Pres. & Dev.*, 14 Misc. 3d 1207(A) (Sup. Ct. N.Y. Cnty. 2006) (citations omitted); *City of Glen Cove Indus. Dev. Agency v. Doxey*, 79 A.D.3d 1038, 1038 (2d Dep't 2010) (upholding denial of the "appellant's cross motion for disclosure as the information sought was not material or necessary to its claims").

Where, as here, the discovery sought is neither material nor necessary to resolve the claims asserted, the petitioner's discovery requests must be denied. *CRP/Extell Parcel I, L.P. v. Cuomo*, 101 A.D.3d 473, 474 (1st Dep't 2012) (denying discovery in Article 78 proceeding that was neither material nor necessary to determine "whether [the respondent's] determinations were affected by an error of law or arbitrary and capricious").

Moreover, a court's assessment of a motion for discovery in an Article 78 proceeding is not divorced from its consideration of the merits of the underlying petition. "[I]t is appropriate for a court to consider whether a petitioner would be entitled to Article 78 relief while considering a request for discovery." *Urquia v. Cuomo*, 18 Misc. 3d 1110(A), 2007 N.Y. Slip Op. 52489(U), at *29 (Sup. Ct. N.Y. Cnty. 2007) (citing *Stapleton Studios LLC v. City of New York*, 7 A.D.3d 273, 275) (1st Dep't 2004)). This is especially so where, as here, the respondent challenges the petitioners' standing to even assert their claims. *See Brown v. N.Y.C. Landmarks Pres. Comm'n*, 32 Misc. 3d 1213(A), 2011 N.Y. Slip. Op. 51273(U), at *2–3 (Sup. Ct. N.Y. Cnty. Jul. 7, 2011)

Consequently, the Court should first consider the merits of Chino's claims before it entertains his discovery requests, and should not delay the hearing on the underlying claims.[2]

[2] In accordance with CPLR § 406, pre-hearing motions in an Article 78 proceeding—including those seeking discovery—"shall be noticed to be heard" on the same date the petition itself is scheduled to be heard, not before. *See* CPLR 406.

A. Chino has failed to demonstrate that the discovery sought is material and necessary to his claims.

Chino's requests for discovery must be denied because he has failed to meet the heavy burden of proving that the information sought is "material and necessary" to his claims. *Allocca v. Kelly*, 44 A.D.3d 308, 309 (1st Dep't 2007); *accord City of Glen Cove Indus. Dev. Agency*, 79 A.D.3d at 1038; *Stapleton Studios, LLC*, 7 A.D.3d at 275.

1. Chino has failed to demonstrate why his request to subpoena Paul Krugman as an expert witness in this litigation is material and necessary to his claims.

Chino argues that Paul Krugman "should be subpoenaed as an expert witness to appear before the Court because there are fundamental differences between the parties as to the economic nature of Bitcoin." (Pet.'s Disc. Br. 11.) This argument has no basis in fact or law.

Chino's claim that DFS cites to Paul Krugman "as an expert source supporting their proposition that Bitcoin is money" (*Id.*) relies on a single citation in DFS's reply papers to a scholarly article written by Paul Krugman over thirty years ago.[3] (*See* DFS Reply Br. 16.) Taken in context, this citation was clearly intended to support the narrow proposition that money has historically been understood to serve as a medium of exchange and a store of value.[4] (*Id.*) In

[3] *See* Paul Krugman, *The Int'l Role of the Dollar: Theory and Prospect in Exchange Rate Theory & Practice* 8.2 (John F. Bilson & Richard C. Marston eds., 1984).

[4] The citation to Mr. Krugman's article was taken from the following passage in DFS's reply brief:

> These terms—"medium of exchange" and "form of digitally stored value"—are commonly used to describe financial products and services. *See, e.g.*, *United States v. Faiella*, 39 F. Supp. 3d 544, 545 (S.D.N.Y. 2014) (observing that "money" in ordinary parlance means "something generally accepted as a medium of exchange, a measure of value, or a means of payment"); Paul Krugman, *The Int'l Role of the Dollar: Theory and Prospect in Exchange Rate Theory & Practice* 8.2 (John F. Bilson & Richard C. Marston eds., 1984) (noting that money generally "serves three functions: it is a medium of exchange, a unit of account, and a store of value"); *see also United States v. E-Gold, Ltd.*, 550 F. Supp. 2d 82, 94 (D.D.C. 2008) (holding that "a 'money transmitting service' includes not only a transmission of actual currency, but also a transmission of the *value* of that currency through some other medium of exchange") (emphasis added).

(DFS's Reply Br. 16.)

plucking this single citation from DFS's reply papers, Chino attempts to transform its meaning into something wildly different, arguing that DFS relies on "Paul Krugman as an expert authority to support the proposition that Bitcoin is money," but gets his "views wrong" because he has "repeatedly argue[d] that Bitcoin is not money because it is not a stable store of value." (Pet.'s Disc. Br. 11.) Consequently, Chino contends, "Paul Krugman should be brought in as an expert witness before the Court to explain this contradiction, and provide an opportunity to explain directly to the Court the economic nature of Bitcoin." (*Id.*)

But DFS did not cite Paul Krugman for his views on Bitcoin. In fact, the sole reference to Mr. Krugman's work in DFS's moving papers is to an article published in 1984—over two decades before Bitcoin was even invented. Moreover, that article was cited as support for the limited (and seemingly uncontroversial) proposition that money is typically understood to serve as a medium of exchange and a store of value—a proposition that neither party disputes here. And while Chino emphasizes that Mr. Krugman finds Bitcoin to be a poor store of value, this is wholly irrelevant because DFS did not cite Mr. Krugman for his opinions about virtual currency.[5]

In sum, Chino has utterly failed to show how Paul Krugman's testimony would be relevant—let alone material and necessary—to his claims. And lacking any legitimate basis or "ample need" for his request, Chino should be denied leave under CPLR § 408 to subpoena him as an expert witness.

[5] Chino makes much of the fact that Paul Krugman considers Bitcoin to be a poor store of value, but this does not speak to whether virtual currencies are properly viewed as a "financial product or service" subject to DFS's regulatory authority, and thus does not run counter to DFS's position in this litigation.

2. Chino has failed to demonstrate why his requested document production is material and necessary to his claims.

Chino also seeks leave from the Court under CPLR § 408 to request that DFS disclose certain internal emails and other written documentation about its internal deliberations leading up to the promulgation of 23 NYCRR Part 200 (the "Regulation"). (Pet.'s Disc. Br. 12–13.) Specifically, Chino requests an order requiring DFS to disclose "all internal emails, emails with third-parties, and other written documentation" in DFS's possession "between January 1, 2013 and September 30, 2015" regarding "the economic nature of Bitcoin and whether it qualifies as a 'financial product or service.'" (*Id.* at 13.)

Chino contends this discovery request is warranted because "the only testimony introduced in the written record during the hearings" on the Regulation "support the notion that Defendants-Respondents did not have the statutory authority to regulate Bitcoin." (*Id.*) Given this alleged lack of supporting testimony, Chino surmises that "the economic nature of Bitcoin must have been discussed either before or after the hearings through email correspondence internally or between the Defendants-Respondents and/or with outside parties." (*Id.* at 12–13) Put differently, Chino argues that document discovery is necessary under CPLR § 408 because—in Chino's view—the testimony at the public hearings on the Regulation did not sufficiently address whether Bitcoin is a "financial product or service," so DFS must have had internal deliberations on the issue through email and other written documents. This baseless argument is rooted in nothing but speculation and conjecture.

As Chino recognizes, parties must seek leave from the court to conduct discovery under CPLR § 408, which will only be granted if the requesting party demonstrates an "ample need" for the disclosure that would likely be material and necessary to a claim or defense in the proceedings. (*See* Pet.'s Disc. Br. 2–3); *see also Tivoli Stock LLC*, 14 Misc. 3d 1207(A). And

here, Chino's requested document discovery would be neither material nor necessary to his claims. Whether DFS acted within the authority conferred to it under the Financial Services Law in promulgating the Regulation is a purely legal question, rendering discovery unnecessary. *See, e.g.*, *Mayfield v. Evans*, 93 A.D.3d 98, 103 (1st Dep't 2012) ("ascertaining whether a regulation is consistent with the statute that it is based on" involves "'the interpretation of statutes and pure questions of law'" (quoting *Matter of Madison-Oneida Bd. of Coop. Educ. Servs. v. Mills*, 4 N.Y.3d 51, 59 (2004))). Similarly, the question of whether certain aspects of the Regulation's design and scope are "arbitrary and capricious" is a purely legal question to which internal DFS communications have no relevance. *See Humane Soc'y of N.Y. v. City of N.Y.*, 188 Misc. 2d 735, 737–38 (Sup. Ct. N.Y. Cnty. 2001) ("judicial review is [] confined to whether there was 'any evidence' to support the agency's rule," so "[m]atters outside the record before the agency, including the motivations or thought processes of the agency's members in approving the rule, are … beyond the scope of review").

3. Chino has failed to demonstrate why his request to depose the former Superintendent of DFS is material and necessary to his claims.

In addition to his requests for Paul Krugman's testimony and wide-ranging documentary discovery, Chino also seeks to depose the former Superintendent of DFS. Without citing to a single case allowing a deposition to be taken in this context,[6] Chino alleges that the former

[6] To support his request to depose the former Superintendent, Chino cites to one case, *IA2 Serv. LLC v. Quinapanta*, 51 Misc. 3d 1222(A), 2016 N.Y. Slip Op. 50779(U) (N.Y. Civ. Ct. 2016). In that case, the court granted leave to the respondent to depose a non-party witness in a consolidated holdover proceeding. *Id.* The *Quinanpanta* court was tasked with determining whether a building was eligible for rent-stabilization, which turned on a disputed question of fact—the number of residential units in the building at issue. *Id.* Given the building's landlord was "in possession of the essential facts bearing on the number of residential units in the premises," the court concluded there was "ample need" for the "vital" information being sought, and granted the respondents' motion to depose him. *Id.* The court's decision in *Quinapanta* does not support Chino's discovery requests: there, the court granted a motion to depose a non-party witness to answer a straightforward question of fact—the number of residential units in a building. Here, Chino moves to depose the former Superintendent to clarify a pure question of law—

Superintendent "has exclusive knowledge not shared with the Plaintiff-Petitioner about the basis of Defendants-Respondents' determination of the economic attributes and nature of Bitcoin" because he was the Superintendent of DFS "at the time of the proposed Regulation and when the Regulation was promulgated." (Pet.'s Disc. Br. 14.) Consequently, Chino reasons, the former Superintendent "was central in making the determination that Bitcoin is a 'financial product or service,'" and "[h]is testimony is relevant and necessary for the determination of the economic nature of Bitcoin." (*Id.* at 14–15) This indefensible request must be denied for numerous reasons.

First, as explained above, discovery is not needed to resolve a purely legal question about DFS's authority to regulate virtual currencies under the Financial Services Law. Second, the former Superintendent's deposition is entirely unnecessary to determine whether certain aspects of the Regulation's design and scope are arbitrary and capricious, and it would be unprecedented to allow the deposition of the former head of an executive agency in this type of proceeding.

Furthermore, Chino's contention that the former Superintendent has "exclusive personal knowledge" about the economic nature of Bitcoin is facially impossible given he is seeking to subpoena Paul Krugman to testify on the exact same issue. (*See* Pet.'s Disc. Br. 11 (requesting to subpoena Mr. Krugman "to explain directly to the Court the economic nature of Bitcoin")). Indeed, the financial or economic nature of Bitcoin and other virtual currencies are observable by anyone, and is plainly not secret knowledge in the exclusive possession of any particular DFS employee. Whether this information is in the former Superintendent's exclusive possession is ultimately irrelevant, however, because Chino has not demonstrated a need for the requested discovery.

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whether DFS acted within its authority under the Financial Services Law when it promulgated the Regulation—by making subjective inquiries into his thoughts, motives, and opinions.

B. The motion should be denied because Chino lacks standing and his claims fail as a matter of law.

Chino's request for discovery in his Article 78 challenge also fails because he is not entitled to any of the relief he seeks as a matter of law. DFS's moving papers demonstrate that Chino lacks standing to challenge DFS's regulatory authority, and his claims otherwise fail to state a cause of action. (*See generally* Resps.' Cross-Mot. Br.; Resps.' Reply Br.) "Where a court determines a petition does not state a cause of action, discovery is properly denied." *Rice v. Belfiore*,15 Misc. 3d 1105(A), 2007 N.Y. Slip. Op. 50511(U), at *25 (Sup. Ct. Westchester Cnty. 2007) (citing *Matter of O'Connor v. Stahl*, 306 A.D.2d 286 (2d Dep't 2003)). Chino's requests for discovery could not save his claims from dismissal, and should therefore be denied.

II. No legitimate grounds exist for holding DFS's cross-motion in abeyance pending resolution of Chino's motion for limited discovery.

Chino requests that DFS's cross-motion to dismiss be held in abeyance pending resolution of his request for limited discovery. There are no legitimate grounds for this request. DFS submitted a dispositive motion in April 2016 seeking to dismiss the petition under Rule 3211(a)(7) and Section 7804 of the CPLR for lack of standing and failure to state a claim upon which relief can be granted. (*See* Resps.' Cross-Mot. Br.) If DFS prevails on that motion, it would fully resolve this litigation. Courts have recognized that mere hope that pre-trial discovery will yield helpful information will not forestall the determination of a motion under CPLR § 3211. *See Cracolici v. Shah*, 127 A.D.3d 413, 413 (1st Dep't 2015). This reasoning holds especially true here given the judiciary's interest in the prompt and efficient resolution of summary proceedings under Article 78.

Although courts have held that motions under CPLR § 3211 may be held in abeyance where the plaintiff argues that limited discovery is needed on the issue of personal jurisdiction, *see, e.g., Goel v. Ramachandran*, 111 A.D.3d 783, 788 (2d Dep't 2013), Chino does not seek to

hold DFS's cross-motion in abeyance on jurisdiction-related issues. (Pet.'s Disc. Br. 14–17.) Instead, he requests it be held in abeyance on the grounds that "there is significant disagreement as to the nature of Bitcoin and whether or not it should be considered a 'financial product or service,' which is "at the heart of the issue in determining whether the cross-motion to dismiss should be granted or denied." (*Id.* at 16) Chino further alleges that "the items being requested are under the exclusive knowledge or control of Defendants-Respondents," and that his "motion for limited discovery will clear up matters that could cause the cross-motion to dismiss to be denied." (*Id.*)

But these arguments do not justify holding DFS's cross-motion in abeyance. DFS's cross-motion to dismiss raises jurisdictional and substantive defects in the petition that are dispositive, and discovery is not needed for the Court to rule fully and fairly on the issues before it. Chino's discovery requests are based in speculation and it is unclear how any of the disclosures sought would clarify any relevant issue in this case. Although the parties disagree on whether Bitcoin and other virtual currencies fall within DFS's regulatory authority, the discovery Chino seeks would not shed light on that issue, nor would it provide him with facts that are "material and necessary" to his claims.

In sum, Chino has failed to show good cause for discovery, and his requests should be denied.

III. Chino has failed to show good cause for leave to serve and file a surreply.

Chino moves, in the alternative, for leave to file a surreply. Surreplies are not permitted under CPLR § 2214 absent a showing of good cause. *See, e.g.*, *Conant v. Alto 53, LLC*, 21 Misc.

3d 1147(A) (Sup. Ct. N.Y. Cnty. 2008). Here, Chino has failed to establish good cause, and his request should be denied.

Chino argues that the filing of a surreply brief is appropriate because DFS raised an argument in its reply memorandum that was not raised in its opening papers. (Pet.'s Disc. Br. 17.) Specifically, Chino argues that "Defendants-Respondents try to argue that anything of a financial nature can be regulated as a 'financial product or service' under FSL § 104(a)(2)." (*Id.*) This is wrong for two reasons.

First, Chino misconstrues the arguments contained in DFS's moving papers. At no point has DFS argued—implicitly or explicitly—that it is authorized to regulate "anything of a financial nature" under the Financial Services Law. To the contrary, DFS has consistently maintained throughout this litigation that it is authorized under the Financial Services Law "to enact rules and regulations pertaining to financial products, services and the providers of such products and services," and that the regulation of "virtual currency products and services … falls comfortably within" that mandate.[7] (Resps.' Cross-Motion Br. 14-15.)

Second, DFS's reply brief does not present any new arguments. It only reiterates the arguments set forth in its opening brief and responds to the arguments made in Chino's opposition. In short, Chino cannot establish good cause for filing a surreply brief by referring to a "newly presented argument" that DFS never actually made. There is no basis for a surreply here, and Chino's motion should be denied.

[7] DFS makes the same argument in its reply brief. (*See* Resps.' Reply Br. 8 ("The regulation of virtual currency business activity is precisely the type of regulation envisioned by the Governor and the Legislature when they empowered DFS to regulate banks, insurance companies, *and other financial services industries*—including financial products and services—in the modern, post-financial-crisis era.").)

CONCLUSION

DFS respectfully submits that Chino's motion for limited discovery must be denied, along with any other relief the Court deems just and proper.

Dated: New York, New York
March 10, 2017

Respectfully submitted,

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