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IN THE THIRD DISTRICT COURT, SALT LAKE COUNTY
STATE OF UTAH

R. WAYNE KLEIN, AS COURT-APPOINTED RECEIVER FOR FFCF INVESTORS, LLC, ASCENDUS CAPITAL MANAGEMENT, LLC, AND SMITH HOLDINGS, LLC, Plaintiffs, v. PENSON FINANCIAL SERVICES, INC., AND CONSILIUM TRADING COMPANY, LLC, Defendants.	**REPLY MEMORANDUM IN FURTHER SUPPORT OF DEFENDANT PENSON FINANCIAL SERVICES, INC.'S MOTION TO DISMISS THE COMPLAINT** Case No. 100924572 Judge Constandinos Himonas

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Defendant Penson Financial Services, Inc. respectfully submits this reply memorandum in further support of its Motion to Dismiss the Complaint.

ARGUMENT

I. THE COMPLAINT FAILS TO ALLEGE A COGNIZABLE INJURY-IN-FACT TO THE RECEIVERSHIP ENTITIES.

The Receiver faces a problem. Now that the Court has removed the alleged injuries to the Investors from this case (claims for those injuries need to be arbitrated), the Receiver needs to identify a separate and independent injury to the Receivership Entities to support his assertion that he has standing to pursue claims against Penson on behalf of the Receivership Entities.

He contends that he has standing because "Penson's conduct caused the Receivership Entities to suffer damages in the form of the creation of tort creditors to the entities themselves." (Mem. in Opp. to Def.'s Mot. to Dismiss, dated Dec. 5, 2011 ("Opp.") at 3). According to the Receiver, Penson allowed Taylor and Smith's fraudulent scheme to remain undetected and continue longer than it otherwise would have, increasing the liabilities of the Receivership Entities. (Opp. at 7). The Receiver's new "tort creditor" theory of standing fails for several reasons.

First, this theory of standing is not pleaded in the Complaint. Under Utah law, standing must properly be alleged. *See Brown v. Division of Water Rights of Dept. of Natural Resources*, 2010 UT 14, ¶ 14, 228 P.3d 747, 751. Plaintiff can point to no allegations in the Complaint in which this theory is stated, let alone explained.[1] Simply raising this theory in opposition to Penson's Motion fails to satisfy Utah's pleading requirements.[2]

What the Complaint actually *does* allege, is a detailed description of the amounts of funds each of the Investors deposited with Penson and the amount of commissions they paid to Ascendus (Compl. ¶ 84(a)-(p))—which corresponds almost exactly to the damages sought by the Receiver in his Prayer for Relief ("in excess of $7,500,000").

Meridian Asset Mgmt., Inc., 296 B.R. 243 (Bankr. N.D. Fla. 2003) is instructive. In that case, the court observed:

> Here, [the trustee's] complaint has made no allegations that the Bank has injured [the corporate entity] in such a way as to be distinct from specific customers; [the trustee] seeks money damages of $2,300,000 in each Count in its Complaint based on funds embezzled from specific customers. To the extent any claim by the trustee alleged money damages to the injured customer creditors, the trustee would lack standing to assert such a claim. Likewise, while [the trustee] contends it is bringing claims on behalf of the bankruptcy estate, the facts demonstrate that all of the claims relate solely to the funds taken by [the corporate entity] and [the Ponzi scheme operator] from specific customers. [The trustee] is asserting causes of action that clearly run in favor of the defrauded customers and allege no causes of action that are unique to the estate of [the corporate entity].

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[1] In a few scattered, conclusory paragraphs, the Receiver simply alleges that the Receivership Entities were "damage[d]." (Compl. ¶¶ 89, 122, 127). But that is surely not enough: "mere conclusory allegations in a pleading, unsupported by a recitation of relevant surrounding facts, are insufficient to preclude dismissal[.]" *Foster v. Saunders*, No. 20040527-CA, 2005 WL 1356799, at *1 (Utah Ct. App. June 9, 2005) (internal quotation marks omitted).

[2] Under Utah law, "[a] plaintiff cannot amend the complaint by raising novel claims or theories for recovery in a memorandum in opposition to a motion to dismiss[.]" *Holmes Development, LLC v. Cook*, 2002 UT 38, ¶ 31, 48 P.3d 895, 904. As the Utah Supreme Court explained, "such amendment fails to satisfy Utah's pleading requirements." *Id.*

Id. at 257 (citations omitted). Just like in *Meridian,* the Receiver here seeks damages that correspond exactly to the funds deposited by the Investors into their Penson accounts and the commissions they paid to Ascendus. (*Compare* Compl. at 38 *with id.* at ¶ 84(a)-(p)). These claims "clearly run in favor" of the Investors—not the Receivership Entities. *Meridian*, 296 B.R. at 257. The Receiver's "tort creditor" theory is contradicted by the pleading he actually filed.[3]

Second, even if the Receiver had pleaded this "tort creditor" theory (he did not), the Receiver's new theory would fail as a matter of Utah law. The Receiver relies on *Marion v. TDI, Inc.*, 591 F.3d 137 (3d Cir. 2010), but that case is predicated on the principle of "deepening insolvency," a theory that has been rejected in Utah. In *Marion*, the receiver argued that the receivership entity had been injured by third-parties because those third-parties had assisted the Ponzi scheme operator (a principal of the corporation) in taking on additional liability to the defrauded investors. *Marion*, 591 F.3d at 148. The Third Circuit found this theory of injury to be barely sufficient for purposes of conferring standing on the receiver,[4] and emphasized that its

[3] The only allegations that plausibly state a distinct injury to the Receivership Entities are pleaded in support of the Receiver's fraudulent transfer claim (Count II) (which fails for separate reasons explained *infra*); and that amount is just $206,561.97. (Compl. ¶¶ 56-59). The Complaint is otherwise silent regarding any damages suffered by the Receivership Entities. Even if the Court were to rule that the fraudulent transfer claim were somehow viable, at a minimum, the Receiver should be required to replead and to state only those damages for which he has good faith support.

[4] The court expressed reservations about its holding:

> We confess to being less than comfortable with what [the receiver's] theory identifies as the actual harm to [the receivership entity]—essentially the harm of being responsible for the injury caused in the first instance to the investors. That seems to

conclusion was compelled by its interpretation of Pennsylvania law. Specifically, the court explained that in a prior Third Circuit case it had held that a creditors' committee had standing to bring suit on behalf of a corporation against third-parties who allegedly prolonged a Ponzi scheme perpetrated by management because the third-parties had "injured the corporation by deepening its insolvent condition." *Id.*

The Receiver's "deepening insolvency" theory of injury has been rejected by the Utah Court of Appeals. In *Coroles v. Sabey*, 2003 UT App 339, 79 P.3d 974, a group of investors in a corporation called Ganter USA ("Ganter"), brought claims seeking to recover monies they had lost in their investment, alleging that they relied on defendants' materially false statements regarding Ganter USA. *Id.* at ¶¶ 2-3. Ganter assigned certain claims to the plaintiffs. *Id.* at ¶7. In granting defendants' motion to dismiss the assigned claims, the trial court held that "even if the defendants made the alleged misrepresentations and omissions to the plaintiffs, Ganter USA would have been the benefactor and not the victim of these actions. In other words, the Complaint contains no allegations of damage to Ganter USA as a result of these actions." *Id.* at ¶ 11. On appeal, the Utah Court of Appeals affirmed, stating that it "agree[d] with the trial court that Plaintiffs failed to plead damages." *Id.* at ¶ 33.

Significantly, the Court of Appeals rejected plaintiffs' contention that Ganter USA had been injured by the defendants: "We decline Plaintiffs' invitation to recognize 'deepening

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> eliminate the cogency of any distinction between harm to the debtor and harm to the creditors.

Id. at 149.

insolvency,' the only theory of damages that Plaintiffs argue on appeal, as sufficient damages. Although deepening insolvency might harm a corporation's shareholders, it does not, without more, harm the corporation itself."[5] *Id.* Therefore, even assuming, *arguendo*, that the Receiver here had pleaded facts to support his new theory of standing, this theory is foreclosed by binding Utah Court of Appeals precedent. In short, the Receiver cannot bring claims on behalf of the Receivership Entities by alleging that Penson's conduct allowed the Ponzi scheme to continue to exist because, under *Coroles*, this does not harm the corporation itself.[6] *Id.*

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[5] Other courts have similarly rejected the notion that a corporation suffers a cognizable injury where a third-party's conduct allegedly prolongs the life of a Ponzi scheme and, thereby, increases the corporate entities' liabilities to its creditors. *See Askanase v. Fatjo*, No. Civ. A.H-91-3140, 1996 WL 33373364, at *28 (S.D. Tex. Apr. 1, 1996) ("The Court is unpersuaded by the plaintiffs' 'deepening insolvency theory.'") (dismissing corporate receiver's negligence claim for lack of standing); *Feltman v. Prudential Bache Secs.*, 122 B.R. 466, 473-74 (S.D. Fla. 1990) (rejecting argument that trustee had standing to sue third-party broker on behalf of debtor corporation where trustee alleged that debtor engaged in a Ponzi scheme and the broker "aided in artificially extending [the debtor's] life").

[6] In addition to relying upon *Marion*, the Receiver argues that "[c]ourts elsewhere have also recognized that standing exists to pursue third parties for creat[ing] an entity's liabilities owed to tort creditors." (Opp. at 4). But the cases cited by the Receiver in support of this assertion do not compel the conclusion that the Complaint adequately alleges a distinct injury to the Receivership Entities for the same reason *Marion* fails: the theory of injury has been rejected by the Utah Court of Appeals in *Coroles*.

Additionally, each case is distinguishable on its facts. In *Reneker v. Offill*, No. 3:08-CV-1394-D, 2009 WL 3365616, at *3 (N.D. Tex. Oct. 20, 2009), the receiver actually *alleged* in the complaint that the defendant law firm's negligence damaged the receivership entities (their clients) in a specific dollar amount. *Id.* at *2-3. Here, the Receiver fails to allege his new theory of standing. In *Smith v. Arthur Anderson LLP*, 421 F.3d 989 (9th Cir. 2005), a bankruptcy trustee brought claims against one of the debtor's former directors and a group of underwriters. The trustee specifically *alleged* that the defendants' conduct caused the debtor to squander the corporation's assets on unviable business plans and to take on more debt. *Id.* at 995. The Ninth Circuit found that standing was properly pleaded because the "wrongful expenditure of corporate assets qualifies as an injury to the firm[.]" *Id.* at 1003; *see also id.* at 1004 ("We rely *only* on the

Finally, with respect to this "tort creditor" theory, the Court should not lose sight of the procedural posture of this case. These so-called "tort creditors" that have claims against the Receivership Entities have assigned their claims against Penson to the Receiver.[7] Indeed, the Receiver has asserted claims against Penson on behalf of the Investors; and this Court has ruled that those claims have to be arbitrated. For the Receiver to now attempt to use these same Investor allegations as a mechanism to conjure up "injury" to the Receivership Entity is a

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dissipation of assets in reaching the conclusion that [the debtor] was harmed.") (emphasis added). Here, by contrast, the Receiver does not allege that Penson's conduct caused the Receivership Entities to take on loans they could not pay back or waste corporate assets to fund an unrealistic business plan. Rather, the gravamen of the Complaint is that Penson allegedly facilitated a fraudulent scheme that resulted in the loss of Investor funds—not corporate funds. (Compl. ¶ 84(a)-(p)). The Receiver's reliance on *Mosier v. Stonefield Josephson, Inc.*, No. 11-2666 PSG, 2011 WL 5075551 (C.D. Cal. Oct. 25, 2011) fails for similar reasons because the court in *Mosier* relied almost exclusively on the reasoning of the Ninth Circuit in *Smith v. Arthur Anderson LLP*, 421 F.3d 989 (9th Cir. 2005). Finally, in *Warfield v. Alaniz*, 453 F. Supp. 2d 1118 (D. Ariz. 2006), a receiver alleged that the receivership entity was injured when the Ponzi scheme operator "transferred funds to [certain defendants] to further the Ponzi scheme[.]" *Id.* at 1126. Acknowledging that there was "a split in authority regarding this issue," the court concluded that this unauthorized removal of assets—which formed the basis of the receiver's fraudulent transfer claim—harmed the receivership entity. *Id.* 1127. Here, for purposes of the Motion, Penson does not challenge the Receiver's standing to bring the fraudulent transfer claim (Count II) on behalf of the Receivership Entities. Therefore, this part of *Warfield*'s holding is inapposite. The *Warfield* court also held that the receiver could pursue his non-fraudulent transfer claims because, if successful, they would "benefit the receivership estate as a whole rather than any individual creditor." *Id.* The court, however, did not explain what the injury-in-fact was to the receivership entities other than the dissipation of corporate assets. Here, the injury underlying the Receiver's tort-based claims (Counts I, V, and VI) are the funds and commissions paid to Taylor and Smith—not any corporate assets belonging to the Receivership Entities. (Compl. ¶ 84(a)-(p)).

[7] The Receiver has not produced these assignments and they are not available for inspection, so it is unclear exactly what it is that has been assigned. The Complaint simply asserts that the Investors "who had brokerage accounts at Penson have assigned to the Receiver their claims against Penson[.]" (Compl. ¶ 83).

contorted, but transparent, effort to evade the contractual requirement that Investor claims against Penson arising out of these facts must be arbitrated.

In the alternative to his "tort creditor" injury theory, the Receiver argues, in essence, that the standing question is premature. He contends that "the dispute over which party actually suffered the damages is one of causation, and [w]hether Plaintiff can prove causation, and if so, the nature and extent of those losses, is an issue that survives a 12(b)(6) motion." (Opp. at 10 (internal quotation marks omitted)).

The Receiver is wrong. Penson contends that the Receiver has failed to *plead* a cognizable injury-in-fact to the Receivership Entities. That is a pleading issue that must be resolved now; a court may certainly dismiss a claim for failure to plead cognizable damages to a corporation on a motion to dismiss. *See Coroles*, 2003 UT App 339 at ¶ 33 n.18, ("A court can decide something as a matter of law at the dismissal stage of the proceedings, and that is what the trial court did in this case. It concluded that, as a matter of law, the type of damages Plaintiffs had alleged in their complaint were legally insufficient.") (internal citation omitted)). The Court should do the same here.

II. THE *IN PARI DELICTO* DOCTRINE BARS THE RECEIVER FROM ASSERTING COUNTS I, II, V, AND VI AGAINST PENSON.[8]

The Receiver argues that *in pari delicto* is an affirmative defense and dismissal on this ground is not available at this juncture. (Opp. at 11-12). The Receiver is mistaken. Courts

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[8] In his Opposition, the Receiver incorrectly states that, under certain case law cited in its Motion, "Penson concedes that *in pari delicto* does not operate to bar the Receiver's fraudulent transfer claims[.]" (Opp. at 14). To be clear and as stated in the Motion, Penson's position is that *in pari delicto* bars *all* the remaining claims in the Complaint.

frequently adjudicate the *in pari delicto* doctrine based solely on the facts alleged in the complaint. *See, e.g.*, *Knauer v. Jonathon Roberts Fin. Group, Inc*, 348 F.3d 230, 235-38 (7th Cir. 2003); *Terlecky v. Hurd (In re Dublin Secs., Inc.)*, 133 F.3d 377, 381 (6th Cir. 1997); *Hays v. Pearlman*, No. 2:10-CV-1135-DCN, 2010 WL 4510956, at *7 (D.S.C. Nov. 2, 2010); *Knauer v. Jonathon Roberts Fin. Group, Inc.*, 01-1168-C-K/T, 2002 WL 31431484, at *8 (S.D. Ind. Sept. 30, 2002), *aff'd*, 348 F.3d 230 (7th Cir. 2003).

Here, the Complaint is replete with allegations that detail the fraudulent scheme perpetrated by Taylor and Smith, which resulted in significant losses to the Investors. (Compl. ¶¶ 7-35). Significantly, the Complaint states that "[b]oth Taylor and Smith have . . . been charged criminally in connection with their roles in the Ascendus and FFCF schemes." (Compl. ¶ 10). Regarding Penson, the Receiver alleges only that Penson, at the instruction of Taylor, transferred Investors' funds from their accounts to third-parties associated with the Ponzi scheme based on forged letters of authorization. (Compl. ¶¶ 8-9). There is no allegation that Penson directly benefited from the embezzlement of the Investors' funds, a factor that the Seventh Circuit found significant in affirming dismissal on *in pari delicto* grounds. *See Knauer*, 348 F.3d at 237. And there is no allegation (nor could there be) that Penson—unlike Taylor and Smith—is facing criminal charges for its alleged conduct here. *See Collins & Aikman Corp. v. Stockman*, No. 07-265-SLR-LPS, 2010 WL 184074, at *7 (D. Del. Jan. 19, 2010) (applying *in pari delicto* based on complaint's allegations where plaintiff's officers were criminally indicted); *see also Mosier v. Quinney*, No. 2:06-CV-519, 2007 WL 2688245, at *2-3 (D. Utah Sept. 11, 2007) (dismissing claims brought by trustee against third-party that allegedly participated in debtor's

Ponzi scheme on *in pari delicto* grounds where Ponzi scheme operators were subject to criminal prosecution for their roles in fraud and the third-parties were not).[9]

Because the Receiver "admits in his [C]omplaint that the [Receivership Entities'] own actions were instrumental in perpetrating the fraud on the [Investors] choosing to invest in the [Ascendus and FFCF] schemes" and that the Receivership Entities "intentionally defrauded their [I]nvestors," this "establishes conclusively that the [Receivership Entities] were *at least* as culpable as [Penson] in this matter." *In re Dublin Secs.*, 133 F.3d at 380 (emphasis in original) (dismissing trustee's claims based on *in pari delicto* at the motion to dismiss stage); *see also Stockman*, 2010 WL 184074, at *7.

The Receiver purports to appeal to "equity" and contends that the Court should decline to dismiss "on public policy grounds." (Opp. at 13). The Receiver maintains that Penson should not be permitted to "go free to the detriment of the innocent [I]nvestors." (*Id.*). In truth, public policy mandates dismissal. If the Court dismisses this case, as it should, Penson does not "go free." The Court already has ruled that the claims that the Investors assigned to the Receiver must be prosecuted in a FINRA arbitration. There is nothing inequitable or contrary to public policy about allowing these claims to proceed in the contractually agreed-upon forum. *See In re Dublin Secs.*, 133 F.3d at 380 (rejecting trustee's argument that *in pari delicto* should not apply

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[9] Although the court in *Mosier* affirmed the application of the *in pari delicto* doctrine at the summary judgment stage, the procedural posture of that case is irrelevant since, here, the Court must take as true the allegation that Taylor and Smith are subject to criminal charges for their roles in the Ponzi scheme.

for public policy reasons because "the defendants [were] also named as defendants in other actions filed by the creditors[.]").

Next, the Receiver asserts that, under the rationale of *Scholes v. Lehman*, 56 F.3d 750 (7th Cir. 1995), the *in pari delicto* doctrine does not apply here because the appointment of the Receiver removed the wrongdoers (Taylor and Smith) from the Receivership Entities, entitling them to seek damages for the benefit of the Investors. (Opp. at 13-14). In its Motion, Penson argued that *Scholes* did not apply here for at least two reasons. (Mot. at 15-16). The Receiver fails to convincingly rebut either reason.

First, courts—including the Seventh Circuit in *Knauer*—have limited *Scholes* where a receiver asserts tort-based claims. *See, e.g.*, *Knauer*, 348 F.3d at 236; *Hays*, 2010 WL 4510956, at *7; *Myatt v. RHBT Fin. Corp.*, 370 S.C. 391, 395-97 (S.C. Ct. App. 2006). As the Seventh Circuit explained, "the key difference, for purposes of equity, between fraudulent conveyance cases such as *Scholes* and the instant case is the identities of the defendants." *Knauer*, 348 F.3d at 236. The court continued that, where a receiver asserts tort-based claims against third-parties who derived no benefit from the embezzlement of investor funds, *Scholes* "was less pertinent than the general Indiana rule that the receiver stands precisely in the shoes of the corporations for which he has been appointed." *Id.*

This rationale applies with equal force to the Receiver's tort-based claims (Counts I, V, and VI). Penson is not alleged to have benefited whatsoever from the Taylor's and Smith's fraud and breaches of fiduciary duty. This Court should apply the general Utah rule that a corporate receiver "stands merely in the shoes of the corporation" and "any defense which would have been good against the corporation may be asserted against the receiver." *Burningham v. Burke*, 245 P. 977, 985, 986 (Utah 1926). The cases the Receiver cites for the proposition that "the difference between a tort claim and a fraudulent transfer claim is a 'distinction without a difference,'" (Opp. at 14), are inapposite because none of them applies Utah law.

Second, even with respect to the Receiver's fraudulent transfer claim (Count II), the Complaint fails to allege how Penson benefited from Taylor's and Smith's transfer of corporate assets. If anything, the Complaint appears to suggest that Penson merely transferred these corporate assets to other Taylor-controlled entities. (Compl. ¶¶ 9, 84(a)-(p)). And, as explained above, dismissing the fraudulent transfer claim will not be inequitable since the Investor claims—the only claims in the Complaint that purport to assert cognizable injuries—may be pursued by the Receiver in the FINRA arbitration.

III. THE RECEIVER FAILS TO STATE A CLAIM AGAINST PENSON IN COUNTS I, V, AND VI.

A. Utah Law Does Not Recognize A Claim For Aiding And Abetting A Breach Of Fiduciary Duty (Count V).

The Receiver contends that Utah courts recognize a claim for aiding and abetting a breach of fiduciary duty and invokes *Russell/Packard Dev., Inc. v. Carson*, 2003 UT App 316, 78 P.3d 616. But the claims at issue there did *not* include a claim for aiding and abetting breach of fiduciary duty. *See Carson*, 2003 UT App 316 at ¶ 9 (listing claims at issue and *not* listing claim for aiding and abetting a breach of fiduciary duty). That *Carson* is of no help to the Receiver is proved in *Coroles v. Sabey*, 2003 UT App 339, 79 P.3d 974, a decision issued *after Carson*. The Utah Court of Appeals affirmed a trial court's dismissal of this type of claim on other grounds. In so doing, the Court of Appeals remarked, "[s]ince we decide the aiding and abetting breach of fiduciary duty claim on the basis discussed above [*i.e.*, failure to adequately plead damages], we do not need to decide the issue, reached by the trial court, of whether this cause of action is cognizable under Utah law in the first place." *See id.* at ¶ 34 n.19. *Carson* did not recognize this tort.

Even assuming, *arguendo*, that this tort existed under Utah law, it still would fail. In *Coroles*, the Utah Court of Appeals stated that "if this cause of action is cognizable in Utah, it includes damages as an essential element[.]" *Id.* ¶ 34 n.19. Here, as explained above, the Complaint does not allege how Penson's conduct damaged the Receivership Entities.

B. Utah Law Does Not Recognize A Claim For Aiding And Abetting A Fraud (Count VI).

Again relying on *Carson*, the Receiver asserts that Utah courts recognize a claim for aiding and abetting fraud. Wrong. *See Carson* 2003 UT App 316 at ¶ 9 (listing claims at issue and not listing claim for aiding and abetting a fraud). And after *Carson* was decided, the Utah Court of Appeals declined to rule on "whether this cause of action is cognizable under Utah law." *Coroles*, 2003 UT App 339 at ¶ 37 n.20. Again, the only authority on point cited by either side remains the trial court decision in *Coroles*, which holds that this tort is not cognizable in Utah.[10]

[10] Citing *D.D.Z. v. Molerway Freight Lines, Inc.*, 880 P.2d 1 (Utah Ct. App. 1994) and the Restatement of Torts, the Receiver argues "even if the Utah appellate courts have not expressly recognized the tort of aiding and abetting fraud, there is every indication that they would." (Opp. at 23). This argument fails. The court in *D.D.Z.* did not expressly adopt any section of the Restatement of Torts. In dismissing the plaintiff's claim for assault and battery, the court noted

C. The Receiver Fails To State A Claim For Aiding And Abetting A Securities Fraud (Count I) Under The Utah Securities Act.

The Receiver concedes that the Complaint must allege that Penson "materially aided in the fraud." (Opp. at 26).[11] The Receiver contends that Penson acted as much more than a "simple" clearing broker, (Opp. at 25), because Penson allegedly transferred funds between Investor accounts to inflate account values, wired monies from Investor accounts to Taylor-controlled entities, received money from Ascendus to deposit into Investor accounts purportedly to create the illusion that the accounts had earned profits, and reported false account balances to

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that the plaintiff did *not* allege that the defendant—who witnessed plaintiff being sexual assaulted—was "acting in concert with [the assailant], or pursuant to a common design, or that he gave substantial encouragement or assistance to [the assailant's] conduct." *D.D.Z.*, 880 P.2d at 4. Although the court cited the Restatement of Torts, it did not impose secondary liability on the defendant for the simple reason that it dismissed the claim. Indeed, the court did not recognize a claim for aiding and abetting a sexual assault, let alone one for aiding and abetting a fraud.

And, the Restatement of Torts, as the Receiver all but acknowledges, does not carry the force of law. *Grundberg v. Upjohn Co.*, 813 P.2d 89, 95 (Utah 1991). This treatise should not be used to create a tort not recognized by Utah's common law. In *Grundberg*, the Utah Supreme Court was presented with an issue of products liability law addressed in the Restatement of Torts but not by Utah law. The court emphasized that the Restatement "is not binding on our decision in this case except insofar as we explicitly adopt its various doctrinal principles." *Id.* at 95.

[11] In its Motion, Penson argued that the Complaint insufficiently alleged the "material aid" element of the Receiver's claim for aiding and abetting a securities fraud under Section 61-1-22 of the Utah Uniform Securities Act (Count I). (Mot. at 18-20). The Receiver asserts that Penson "misstates the standard under Utah law." (Opp. at 25). The Receiver is mistaken. Penson's contention is that, in interpreting the "material aid" element of this claim, the Court should look to the extensive body of case law regarding when a clearing-firm provides "substantial assistance." (Mot. at 19 (citing *Foley v. Allard*, 427 N.W.2d 647 (Minn. 1988) (construing the Minnesota Securities Act's material aid element)). Tellingly, the Receiver cites no Utah case law holding that the "material aid" standard is distinct from a "substantial assistance" standard.

the Investors. (Compl. ¶¶ 31, 32, 67-72). Of course, transferring funds, wiring monies, and depositing funds are precisely the mundane tasks that clearing firms perform.

The Complaint also candidly alleges that the "Investors signed forms granting Taylor authority to buy and sell securities . . . using funds in their Penson brokerage accounts," that these authorizations "were the basis of Penson allowing Taylor and his traders to make trades in the customer accounts at Penson," and that Penson transferred the Investors' funds "[a]t the instruction of Taylor and Ascendus." (Compl. ¶¶ 8, 14). Courts have dismissed aiding-and-abetting claims at the pleading stage on the basis that clearing firms do not provide substantial assistance to securities fraud under similar circumstances. *See Stander v. Financial Clearing & Services Corp.*, 730 F. Supp. 1282, 1288 (S.D.N.Y. 1990) ("Plaintiff has alleged that by performing its contracted-for services, clearing trades in plaintiff's account and reporting on those transactions, [the clearing broker] was an aider and abettor to Domestic and Czin's activities. Absent some fiduciary duty of [the clearing broker] to plaintiff, which has not been alleged in the amended complaint, such inaction does not make out a claim for aiding and abetting.") (finding that plaintiff failed to sufficiently allege substantial assistance); *see also Cromer Finance Ltd. v. Berger*, 137 F. Supp. 452, 472 (S.D.N.Y. 2001) ("[T]he plaintiffs have still failed to allege substantial assistance under this theory. While the Ponzi scheme may only have been possible because of [the clearing firm's] actions, or inaction, [the clearing firm's] conduct was not a proximate cause of the Ponzi scheme.").

IV. THE FRAUDULENT TRANSFER CLAIMS ARE TIME-BARRED AND, IN ANY EVENT, THE RECEIVER CANNOT RECOVER THE VALUE OF THE CHALLENGED TRANSFERS FROM PENSON.

The Receiver contends that the "equitable doctrine of adverse domination" saves his time-based fraudulent transfer claim. The Receiver's argument fails. The adverse domination theory cannot be applied against unrelated third-parties—like Penson—who were not in control of the organization or responsible for the delay. In *Nasr v. De Leon*, 18 Fed. Appx. 601 (9th Cir. 2001), the Ninth Circuit held that the doctrine was "wholly inapplicable" in that case "because it applies only when a suit is brought against a self-dealing agent of an organization." *Id.* at 605 n.4. That reasoning applies here. Because the Receiver's fraudulent transfer claims are brought against Penson (a third-party that is not alleged to have controlled the Receivership Entities), the adverse domination doctrine is inapplicable.[12]

Moreover, the adverse domination doctrine does not apply here because the four-year limitations period is a statute of repose that cannot be tolled. In *Klein v. Capital One Fin. Corp.*, No. 4:10-CV-00629, 2011 WL 3270438 (D. Idaho July 29, 2011), a case similar to the case at bar, the court dismissed a receiver's fraudulent transfer claim as untimely at the pleading stage

[12] The cases cited by the Receiver in opposition do not change this result. The Utah Court of Appeals case the Receiver cites—*Saunders v. Sharp*, 793 P.2d 927 (Utah Ct. App. 1990)—is inapposite because the issue was whether a receiver for a bank could invoke the doctrine as an exception to a rule of appellate procedure. The case had nothing to do with the application of this doctrine to fraudulent transfer claims. And, the non-binding slip opinion issued by Judge Anthony B. Quinn of this Court is contrary to the rule set forth in *Nasr*. Without citing any authority, Judge Quinn concluded that the adverse domination doctrine tolled claims asserted against a third-party who did not control the corporate entity. Penson respectfully submits that the Court should follow the reasoning of *Nasr* instead. Finally, for similar reasons, the adverse domination theory does not toll the limitation periods applicable to Counts I, V, VI.

relying on Idaho's statute of repose. *Id.* at *6-8. In rejecting the receiver's assertion that the adverse domination doctrine tolled the four-year period, the court reasoned that, because the repose statute "extinguished" the receiver's claims, the claims could not be tolled. *Id.* at *7 ("A claim that has been extinguished cannot be tolled.") (internal quotation marks omitted). So too here. The Utah statute "extinguishes" a fraudulent transfer claim if it is not asserted within four years of the challenged transfer, unless the claim is saved by the one-year statutory discovery rule, which it is not as explained below. Utah Code Ann. § 25-6-10(1)-(2).[13]

[13] Based on the plain language of the statute, which "extinguished" and not merely "barred" a claim, the court in *Capital One* concluded that the four-year time limitation was a statute of repose. *Capital One*, 2011 WL 3270438, at *7-8. The court, therefore, held that "the time limits applicable to the Receiver's fraudulent-transfer claims began to run at the time each allegedly fraudulent transfer took place; not on the date that the Receiver was appointed." *Id.* *8. Based on its plain language, the Utah statute should also be deemed a statute of repose. *Compare* Utah Code Ann. § 25-6-10 ("A claim for relief or cause of action regarding a fraudulent transfer or obligation under this chapter is extinguished unless[.]") *with* Idaho Code § 55-918 ("A cause of action with respect to a fraudulent transfer or obligation under this act is extinguished unless[.]"). This is in accord with the weight of authority holding that the time limitations in the Uniform Fraudulent Transfer Act, which Utah adopted, are statutes of repose rather than statutes of limitation. *See, e.g.*, *Forum Ins. Co. v. Comparet*, 62 Fed. Appx. 151, 152 (9th Cir. 2003) (California); *United States v. Bacon*, 82 F.3d 822, 823-24 (9th Cir. 1996) (Washington); *Warfield v. Alaniz*, 453 F. Supp. 2d 1118, 1130-31 (D. Ariz. 2006) (Arizona); *Duran v. Henderson*, 71 S.W.3d 833, 838 (Tex. App. 2002) (Texas). Accordingly, the time limits on the Receiver's fraudulent transfer claims began to run on the date of the challenged transfers—not the date on which the Receiver was appointed. As explained in the Motion, the Receiver filed the Complaint more than four years after the last challenged transfer and, therefore, his fraudulent transfer claim is extinguished. (Mot. at 22).

Selvage v. J.J. Johnson & Assocs., 910 P.2d 1252 (Utah Ct. App. 1996) is distinguishable. There, the Utah Court of Appeals found that a different subsection of the Utah statute—Section 25-6-10(3)—which relates to insider transfer claims (a claim not asserted here) operated as a statute of limitations not a statute of repose. Furthermore, the policy concerns that animated *Selvage* and the Utah Supreme Court case on which it relied—*Berry v. Beech Aircraft Corp.*, 717 P.2d 670 (Utah 1985)—are not as pronounced here and, therefore, do not outweigh the

The Receiver alternatively argues that his fraudulent transfer claims are not barred because his claims are timely under the one-year discovery rule. (Opp. at 18-19). The Receiver's argument fails. First, the one-year statutory discovery rule does not apply to the extent the Receiver is seeking to avoid constructively fraudulent transfers. (Compl. ¶ 100 (asserting both actual fraudulent transfer and constructive fraudulent transfer claims)); *see also* Utah Code § 25-6-10(2) (containing no statutory discovery rule for constructive fraudulent transfer claims). Moreover, in *Capital One*, the court dismissed a receiver's fraudulent transfer claim as untimely at the pleading stage and rejected the argument that the claim was saved by Idaho's one-year statutory discovery rule. *Id.* at *6-8. The same result should apply here. Because the Receiver did not bring the fraudulent transfer claim within one year of being appointed, his claim is not saved by the one-year discovery rule.

The Receiver next argues that, "[a]t the very least, the question of whether the discovery rule applies in this case is a question of fact which cannot be resolved on a motion to dismiss." (Opp. at 20). Wrong again. Penson bases its statute of limitations defense on the Complaint's allegations. Utah law recognizes that statute of limitation defenses may be adjudicated on a

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competing policies of finality and certainty. As the Utah Supreme Court explained, "a statute of repose may bar the filing of a lawsuit even though the cause of action did not even arise until after it was barred and even though the injured person was diligent in seeking a judicial remedy." *Berry*, 717 P.2d at 672. This concern was acute in *Berry*, a products liability action, because the limitations period there could potentially bar a claim before a consumer was ever injured by a product. Those concerns are not present here because the relevant injury—the transfer—cannot conceivably occur *after* the four-year limitations period. Moreover, the strictness of the limitation period at issue here is tempered by its length (four-years) which is significantly longer than the one-year period that attaches to an insider transfer claim, the claim before the Utah Court of Appeals in *Selvage*.

motion to dismiss under such circumstances. *See Tucker v. State Farm Mut. Auto. Ins. Co.*, 2002 UT 54, ¶ 8, 53 P.3d 947, 950; *see also Capital One*, 2011 WL 3270438, at *6-8 (dismissing a receiver's fraudulent transfer claims as untimely on a motion to dismiss).

Finally, the Receiver argues that the Complaint states a claim to avoid actual fraudulent transfers and a claim to avoid constructive fraudulent transfers under the Utah Uniform Fraudulent Transfer Act ("UFTA") and that "this should end the Court's inquiry." (Opp. at 20-21). We disagree. Even if the Receiver were able to allege that the challenged transfers were voidable, the Receiver would then have to allege that he was entitled to recover the value of these transfers from Penson as a "transferee" under the UFTA's recovery provision. *See* Utah Code § 25-6-9(2).[14] Based on the Receiver's own allegations, Penson acted merely as a

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[14] Section 25-6-9(2) of the UFTA provides that:

> Except as otherwise provided in this section, to the extent a transfer is voidable in an action by a creditor under Subsection 25-6-8(1)(a), the creditor may recover judgment for the value of the asset transferred, as adjusted under Subsection (3), or the amount necessary to satisfy the creditor's claim, whichever is less. The judgement may be entered against:
>
> (a) the first *transferee* of the asset or the person for whose benefit the transfer was made; or
>
> (b) any subsequent *transferee* other than a good faith transferee who took for value or from any subsequent transferee.

Utah Code Ann. § 25-6-9(2) (emphasis added). Because the Receiver does not allege that Penson benefited in any way from the transfers, (Compl. ¶¶ 57-58), Penson cannot be considered a "the person for whose benefit the transfer was made." *See Bonded Fin. Services, Inc. v. European Am. Bank*, 838 F.2d 890 (7th Cir. 1988) ("[T]he 'entity for whose benefit' is different from a transferee, 'immediate' or otherwise. The paradigm 'entity for whose benefit such transfer was made' is a guarantor or debtor—someone who receives the benefit but not the money.") (construing 11 U.S.C. § 550(a)).

conduit—not a "transferee"—of the funds transferred from Ascendus and affiliated entities to the Investors' accounts. The UFTA does not define who is a transferee and is derived from an analogous provision in the federal Bankruptcy Code. *See* 11 U.S.C. § 550(a). Courts, therefore, look to case law construing the federal statute for guidance. *See Williams v. Performance Diesel*, No. 14-00-00063-CV, 2002 WL 596414, at *5 n.12 (Tex. App. Ct. Apr. 18, 2002). Courts—including the Tenth Circuit—have held that "certain entities receiving the debtor's funds are not 'transferees' but rather 'financial conduits.'" *Bailey v. Big Sky Motors, Ltd. (In re Ogden)*, 314 F.3d 1190, 1196 (10th Cir. 2002). "Financial conduits are those entities that do not exercise 'dominion or control' over the funds." *Id.* The critical inquiry is whether the entity has "the right to put the money to one's own purposes," *id.* at 1202 (internal quotation marks omitted), after the disputed transfer occurs. *See Rupp v. Markgraf*, 95 F.3d 936, 940 (10th Cir. 1996).

Applying this test, the U.S. District Court for Colorado held that a broker, which facilitated the conversion of its customers' stocks into cash and preferred stock as part of a stock redemption, was "simply a financial intermediary, not a transferee." *Kaiser Steel Resources, Inc. v. Jacobs*, 110 B.R. 517, 521 (D. Col. 1990); *see also Rupp*, 95 F.3d at 938-39 (finding that bank that received funds and issued cashier's check was financial conduit and not transferee); *First Sec. Mortgage Co. v. Malloy*, 33 F.3d 42, 44 (10th Cir. 1994) (holding that bank which deposited money into a client's business checking account was a financial conduit and not transferee). Similar to the broker in *Kaiser Steel*, Penson is merely a financial conduit. The Complaint alleges that there were fifteen transfers "in which Ascendus or an affiliated entity sent funds to Penson for deposit into customer accounts at Penson." (Compl. ¶ 57). The funds were transferred by check, and each checked "was accepted by Penson and deposited into the accounts of the customers [*i.e.*, Investors] listed on each check." (Compl. ¶ 58). These allegations are completely inconsistent with the notion that Penson had the right to use these funds for its own purposes, and the mere fact that the funds passed through Penson is insufficient to transform it into a "transferee." *Rupp*, 95 F.3d at 941 ("[T]he term 'transferee' must mean something different from 'possessor' or 'holder' or 'agent,' or 'anyone who touches the money.'").

V. **ASSUMING, *ARGUENDO*, THAT THE FRAUDULENT TRANSFER CLAIMS ARE NOT BARRED BY THE *IN PARI DELICTO* DOCTRINE OR THE STATUTE OF LIMITATIONS, THE RECEIVER MUST REPLEAD THEM.**

In its Motion, Penson argued that the Receiver did not adequately allege the damages he was pursuing on behalf of the Receivership Entities. (Mot. 23-24). In response, the Receiver contends that "[a]lleging damages with particularity is not an element of a cause of action for fraudulent transfer[.]" (Opp. at 21). But this does nothing to explain why the damages figure sought in the Prayer for Relief ("in excess of $7,500,000") corresponds almost exactly to the damages allegedly suffered by the Investors. (Compl. ¶¶ 84(a)-(p)). The Receiver fails to put Penson on notice of the damages sought on behalf of the Receivership Entities and, therefore, the Receiver does not satisfy the requirements of Rule 8(a)(2) of the Utah Rules of Civil Procedure. *See Peak Alarm Co., Inc. v. Salt Lake City Corp.*, 2010 UT 22, ¶ 69, 243 P.3d 1221, 1245 (affirming dismissal of claim where plaintiff failed to provide defendant "fair notice of a claim").

VI. **AMENDING THE COMPLAINT WILL LIKELY BE FUTILE.**

The Receiver moves for leave to amend the Complaint. The fact that the Receiver has preemptively made this motion is noteworthy. Indeed, in explaining the basis for the alternative motion, the Receiver all but acknowledges the utter lack of allegations regarding the injury to the Receivership Entities. (*See* Mem. in Support of Alternative Mot. for Leave to Am. Compl., dated Dec. 5, 2011, at 2 ("[T]o the extent the Court would find it helpful for the Receiver to re-plead the claims he is asserting against Penson on behalf of the Receivership Entities directly, the Receiver respectfully requests leave to do so.")).

Amendment in all likelihood will be futile because the damages sought make clear that Counts I, V, and VI cannot be brought on behalf of the Receivership Entities. Count II is time-barred and, even if not, Penson is merely a financial conduit not a "transferee." *See Daniels v. Gamma West Brachytherapy, LLC*, 2009 UT 66, ¶ 58, 221 P.3d 256, 272 (noting that leave to replead may be denied based on the futility of the amendment); *see also Brereton v. Bountiful City Corp.*, 434 F.3d 1213, 1219-20 (10th Cir. 2006) (affirming denial of motion to amend complaint on the basis that amendment would be futile since plaintiff lacked standing to bring claims). But because the Receiver does not attach a copy of the proposed amended Complaint, Penson cannot fully assess its viability. Therefore, Penson does not oppose this motion to replead but reserves its right to challenge the viability of any amended Complaint at the appropriate time.

CONCLUSION

For the foregoing reasons, Penson respectfully requests that this Court grant Penson's motion and dismiss Counts I, II, V, VI with prejudice.

RESPECTFULLY SUBMITTED this 22 day of December, 2011.

HOLLAND & HART LLP

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CERTIFICATE OF SERVICE

I hereby certify that on this 22 day of December, 2011, the foregoing **REPLY MEMORANDUM IN FURTHER SUPPORT OF DEFENDANT PENSON FINANCIAL SERVICES, INC.'S MOTION TO DISMISS THE COMPLAINT** was served, via U.S. Mail, postage prepaid, as follows:

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