

**IN THE UNIFIED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION**

MICHAEL J. QUILLING, Receiver for ABC)	
VIATICALS, INC., and Related Entities,)	
)	
Plaintiff,)	Civil Action No.
)	3:07-CV-1153-P
)	
v.)	
)	ECF
ERWIN & JOHNSON, LLP, and)	
CHRISTOPHER R. ERWIN,)	
)	
Defendants.)	

**DEFENDANTS' REPLY
IN SUPPORT OF ITS MOTION TO DISMISS PLAINTIFF'S COMPLAINT
UNDER FEDERAL RULES OF CIVIL PROCEDURE 12(B)(6) AND 9(B);
ALTERNATIVELY, MOTION FOR MORE DEFINITE STATEMENT**

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I. Summary Arguments

Quilling has failed to plead any claim with particularity; thus, to the extent that any claims sound in fraud, they should be dismissed under Rule 9(b). Quilling has also failed to state a plausible claim for relief against Defendants. Accordingly, all claims should be dismissed pursuant to Rule 12(b)(6). Quilling's request for leave to amend should also be denied, because all of his claims are subject to dismissal under Rule 12(b)(6) and his request is subject to procedural deficiencies.

II. To the Extent that Quilling's Claims Sound in Fraud, They Should Therefore be Dismissed for Failure to Plead with Particularity

1. Rule 9(b) Heightened Pleading Standard

This Court has clearly set out the standard for a motion to dismiss for failure to plead a claim which sounds in fraud with particularity. To satisfy the particularity requirement under Rule 9(b), "the complaint must set forth the 'time, place and contents of the false representations, as well as the identity of the person making the representation and what that person obtained thereby.'" (September 26, 2007 Order in *Quilling v. International Fidelity & Surety, Ltd.*, 3:07-CV-00421-P (the "*IFS* Order"), at 5).¹ "In other words, Rule 9(b) requires the 'who, what, when, where, and how to be laid out.'" (*Id.*). Rule 9(b) is read in conjunction with Rule 8(a), which requires only a "short and plain statement of the claim showing that the pleader is entitled to relief." (*Id.*). While Rule 9(b) does not usually apply to these claims, a heightened pleading standard applies to claims sounding in fraud. (*See id.*). "A claim "sounds in fraud" when it relies on the same misrepresentations as those pled in the accompanying fraud claim." (*Id.*).

¹ Defendants refer the Court to page 3 and note 1 of their Reply in support of their motion to dismiss for lack of standing, for a discussion of Quilling's complete failure to cite, mention, address, or distinguish the *IFS* Order. The *IFS* Order also bears directly on Quilling's failure to state a claim and plead with particularity.

2. This Court has Determined that Similar Claims Sound in Fraud

This Court held in the *IFS* Order that, when Quilling asserts claims for fraudulent transfer, aiding and abetting breach of fiduciary duty, and negligence, those claims may sound in fraud if they are predicated on allegations of fraudulent conduct. (*See id.* at 7-8). Quilling's claims appear to be based on his allegations that Defendants acted with the principals of ABC Viaticals, Inc., to make misrepresentations to the investors about the safety and investment of their monies.

Quilling believes that he "does not state any allegations of fraud in his Complaint." (Resp. at 4). However, contrary to Quilling's belief, he makes several allegations of fraud in his Complaint's factual allegations:

- Quilling alleges that Defendants assisted ABC and its principals in "cloak[ing] themselves in legitimacy[.]" (Compl. at ¶ 9).
- Quilling alleges that E&J provided marketing materials touting itself as the "oldest and largest law firm in Ladera Ranch, California," to present a false image of legitimacy to the investors. (*Id.* at ¶ 12).
- Quilling alleges "the representations made to the investors regarding premium escrows were blatantly false and were known by the Defendants to be false." (*Id.* at ¶ 14).
- Quilling alleges: "As further inducement to investors regarding the safety of their investment and the proper performance of their duties, Erwin & Johnson touted the fact that the law firm had malpractice insurance in the amount of at least \$2,000,000 and it provided many of them with a copy of the insurance certificate." (*Id.* at ¶ 17).

Quilling of course makes a claim for "fraudulent" transfer, which certainly involves allegations of fraud, and he requests a constructive trust, which has as the first element the "actual or constructive fraud" of Defendants. *See Burkhart Grob Luft und Raumfahrt*

GmbH & Co. K.G. v. E-Systems, Inc., 257 F.3d 461, 469 (5th Cir. 2001). Finally, all of Quilling’s factual allegations are incorporated into each and every claim.²

Quilling has failed to plead with particularity the alleged fraudulent acts of Defendants. Where his claims incorporate his allegations of Defendants’ supposed assistance in defrauding ABC’s investors, Quilling must specify the statements he believes to be fraudulent, identify the speaker, state when and where the statements were made, and explain why the statements were fraudulent. *ABC Arbitrage Plaintiffs Group v. Tchuruk*, 291 F.3d 336, 349 (5th Cir. 2002). To the extent that any of Quilling’s claims sound in fraud, they have not been pleaded with the requisite level of particularity and should be dismissed.

II. All of Quilling’s Claims Should be Dismissed for Failure to State a Claim

1. None of Quilling’s Claims Has a “Plausible” Basis Against Defendants

“While a complaint attacked by a Rule 12(b)(6) motion to dismiss does not need detailed factual allegations, a plaintiff’s obligation to provide the grounds of his entitle[ment] to relief requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do.” (*IFS Order at 4*) (quoting *Bell Atlantic v. Twombly*, 127 S.Ct. 1955, 1964-65 (2007) (internal quotations and citations omitted)). “Fact allegations must be enough to raise a right to relief above the speculative level.” (*Id.*). “There must be a ‘plausible ground’ on which the claim rests such that is enough fact to raise a reasonable expectation that discovery will reveal evidence in support of the claim.” *Id.* While well-pleaded facts are to be read in the plaintiff’s light, unclear questions of law need not be. *See id.*

² (See Compl. at ¶¶ 21, 26, 30, 35, 40, 43, 45, 47, and 49).

2. *Quilling Fails to State Plausible Claims for Breach of Fiduciary Duty or Aiding or Abetting Breach of Fiduciary Duty*

This claim is being asserted ineluctably for the investors to redress injuries allegedly suffered only by them. Quilling's claims for breach of fiduciary duty and aiding and abetting same should be dismissed for the additional reasons set forth below.

E&J complied with all of its fiduciary duties and obligations to ABC's investors. It adhered to all contractual requirements and common law duties in administering the trusts. E&J was contractually and legally bound to abide by its trustee/escrow agreements with ABC and could not have substituted its judgment if it thought that the trusts would have been better administered in a different manner. *See Estate of Bothwell*, 65 Cal. App. 2d 598, 683 (Cal. 1944). The Court is not bound to accept Quilling's contrary legal conclusions that Defendants breached a fiduciary duty or aided and abetted any such breach. *See Papasan v. Allain*, 478 U.S. 265, 286 (1986) (on a motion to dismiss, courts "are not bound to accept as true a legal conclusion couched as a factual allegation"). And Defendants maintain their position that there has been no damages caused by E&J as all premiums were timely paid and no policy ever lapsed during its tenure. These claims should, therefore, be dismissed. *See Twombly*, 127 S.Ct. at 1968-69.

3. *Quilling Fails to State Plausible Claim for Aiding and Abetting Corporate Waste*

While Quilling cites California law on aiding and abetting an intentional tort, he fails to cite *any* case law supporting his perceived application of the corporate waste claim or that the aiding and abetting standard has ever been applied to a corporate waste claim. Beyond that, Quilling simply ignores the fact that the investors' monies were not ABC's assets. The monies were deposited into trusts, subject to specific written

agreements. Thus, once again, the relief sought by this claim does not belong to Quilling or ABC.

4. *Quilling Fails to State a Plausible Claim for Professional Malpractice*

Quilling also fails to state a plausible claim for professional malpractice claims against Defendants. Quilling cites the same elements as Defendants, those found in *Budd v. Nixen*, 6 Cal.3d 195, 200 (Cal. 1971). Yet, Quilling also cites the elements for a negligence claim, but he fails to state a claim for relief on either claim in his Complaint.

First, there being no duty between ABC or its investors and Mr. Erwin individually, there is no basis for Quilling's claim against Mr. Erwin individually.

Second, as demonstrated in Quilling's Complaint, E&J, through its contractual relationship with ABC, simply owed ABC and its investors a duty to follow the terms of the contracts. E&J at all times abided by all terms, duties, and obligations of its written contracts.

Third, Quilling's claim for professional malpractice also fails because it is based on allegations of intentional – not negligent – conduct. (Resp. at 9) (citing Compl. at ¶¶ 14, 16, 18, 19, and 48).

Fourth, Quilling provides only conclusory statements to support his claims for professional negligence. These conclusory statements do not suffice to state *facts* to survive dismissal of this case. For instance, Quilling fails to plead any damages to ABC. Instead, his Complaint pleads damages to the investors. But without an attorney/client relationship between those that were allegedly harmed (the investors) and the attorneys

(E&J), Quilling's Complaint fails to state a claim for a professional negligence. *See Budd*, 6 Cal. 3d at 200.³

Fifth, Quilling has failed to plead cognizable damages to ABC, to the extent that he believes Texas law applies. Under the "economic loss rule," to recover damages for negligence, a plaintiff must show either a personal injury or property damage, not simply economic harm. *See Express One Int'l Inc. v. Steinbeck*, 53 S.W.3d 895, 898-88 (Tex. App.—Dallas 2001, no pet.). Because Quilling has alleged strictly economic harm, his professional negligence or negligence claims are untenable.

Similarly, Quilling has failed to state a plausible claim for gross negligence. Gross negligence is "the want of even scant care or an extreme departure from the ordinary standard of conduct." *Cooper v. Board of Medical Examiners*, 49 Cal. App. 3d 931, 941 (Cal. Ct. App. 1975). Without negligence, there can be no gross negligence. And no allegations in Quilling's Complaint show that E&J or Mr. Erwin exercised an extreme departure from the ordinary standard of care. Quilling's one-line reference in his response simply will not do.

5. *Quilling Fails to State a Plausible Claim for Fraudulent Transfer*

This Court has explained that "a receiver of an alleged Ponzi scheme may sue under the UFTA to recover funds paid from the entity in receivership." (IFS Order at 12) (citing *Warfield v. Carnie*, No. 04-633, 2007 U.S. Dist. LEXIS 27610, 2007 WL 1112591 (N.D. Tex. Apr. 13, 2007)). Nonetheless, this claim fails here on its face because ABC received "reasonably equivalent value" for its transfers to E&J (namely, the value of E&J's services). Thus, there is no tenable claim for fraudulent transfer. *See, e.g., Annod*

³ Quilling misconstrues Defendants' challenge to his failure to plead damages as a challenge to standing only. While showing a particularized harm to ABC is necessary for standing, alleging harm to ABC is also necessary to state a claim for professional malpractice.

Corp. v. Hamilton & Samuels, 100 Cal. App. 4th 1286, 1294 (Cal. Ct. App. 2002) (“If the debtor received reasonable equivalent value, the inquiry ends there.”).

Further, Quilling has now apparently abandoned the false allegation in his Complaint that Mr. Erwin individually received \$500,000 from ABC. Indeed, he does not even refer to this allegation in his response. Quilling’s new *argument* that Mr. Erwin received the same funds from E&J that E&J received from ABC is absent from Quilling’s *Complaint*. Thus, there is no plausible allegation *in the Complaint* to show that Mr. Erwin individually received fraudulently transferred funds. Because Quilling fails to state a claim upon which relief can be granted, the Court should dismiss Quilling’s fraudulent transfer claim. *See Twombly*, 127 S.Ct. at 1968-69.

6. Quilling Fails to State a Plausible Claim for Breach of Contract

Quilling now clarifies that his breach of contract claim is not against Mr. Erwin individually. (Resp. at 10). Defendants’ motion should thus be granted as to Mr. Erwin individually. Quilling cites the same elements for his breach of contract claim against E&J that Defendants cited. *See Poseidon Development, Inc. v. Woodland Lane Estates, LLC*, 152 Cal. App. 4th 1106, 1112 (Cal. Ct. App. 2007). However, Quilling makes several misstatements about E&J’s contractual duties, as set forth below.

First, Quilling refers to Paragraph 13 of his Complaint and argues that it shows that E&J was required to “establish separate trust accounts or ensure that they were properly funded.” Paragraph 13 does not state this. Rather, Paragraph 13 refers to Article III and paragraph 6.01 of the Trust Agreement. The only portion of the contract cited that required establishment of any account is paragraph 6.01, which required E&J to establish “*a* ‘Policy Premium Payment Account’ into which the Grantor will deposit a

sum certain for the payment of premiums on the Policy . . . Trustee shall timely pay all premiums due and owing under the Policy **at the direction of the Grantor or his designee.**” (Compl. at ¶ 13) (emphasis added). Nothing in Paragraph 13 says that E&J was required to “establish separate trust accounts or ensure that they were properly funded.” Indeed, it says only that E&J was to establish “a” premium payment account and **ABC (as the Grantor) was responsible for funding** it and directing E&J to make payments there from. Quilling’s other references to his Complaint direct the Court to allegations of E&J’s supposed wrongdoing outside of its contractual obligations.⁴ The Court should disregard Quilling’s attempt to state a claim by rewriting the applicable agreements.⁵

Second, ABC *did not perform the contracts*, but rather breached them. (Compl. at ¶ 48). Quilling now attempts to avoid this fact by his legal maneuvering in stating, in a footnote, that ABC did not breach its contracts, the LaMondas’ breached their duties to ABC. Quilling cannot deny that, in dealing E&J, the LaMondas were acting as principals and representatives of ABC. As such, E&J dealt with ABC, not the LaMondas on an individual basis.

7. *Constructive Trust and Disgorgement*

Defendants dispute Quilling’s right to a constructive trust or disgorgement. Quilling’s Complaint fails to state a claim for constructive trust or disgorgement. The party seeking to impose a constructive trust must establish the existence of each of the

⁴ Quilling cites Paragraph 48 in support of his Breach of Contract claim. Paragraph 48 is the bulk of Quilling’s fraudulent transfer claim. Such interspersing and co-mingling of claims further supports Defendants’ contention that Quilling’s fraud allegations underlie some claims in his Complaint.

⁵ In footnote 8, Quilling argues that Defendants breached their common law duty to preserve and maintain trust assets. (Resp. at 11 n.8). Apart from Quilling’s failure to assert the breach of such duty, this does not constitute a breach of *contract*.

following elements: (1) actual or constructive fraud; (2) unjust enrichment of the wrongdoer; and (3) tracing to an identifiable res. *Burkhart Grob Luft*, 257 F.3d at 469. To obtain a constructive trust, the plaintiff must be able to identify a specific asset or fund of money as belonging “in good conscience to the plaintiff.” *Newby v. Enron Corp.*, 188 F. Supp. 2d 684, 703 (S.D. Tex. 2002).

Quilling fails to plead with particularity the “actual or constructive fraud” of either E&J or Mr. Erwin. In fact, he asserts that he has not pleaded fraud at all. (Resp. at 4) (“The Receiver, however, does not state any allegations of fraud in his Complaint.”). Quilling cannot have it both ways; he cannot claim to have not alleged fraud to avoid the heightened pleading requirement of Rule 9(b), yet claim to have pleaded an actual or constructive “fraud.” Moreover, he has failed to identify a specific fund of money as belonging in good conscience to ABC. Thus, this claim should be dismissed.

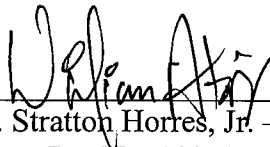
IV. Leave to Amend Should be Denied

Leave to amend does not need to be granted when the amended complaint would not withstand a motion to dismiss for failure to state a claim. *See Sinay v. Lamson & Sessions Co.*, 948 F.2d 1037, 1042 (5th Cir. 1991). Here, several of Quilling’s claims fail to state a claim. Thus, leave to amend should be denied. Leave to amend should also be denied for the reasons more fully stated in Defendants’ reply in support of their motion to dismiss for lack of standing, including (i) that Quilling is capable at asserting proper claims the first time; (ii) his bad faith tactics in failing to voluntarily amend his complaint before filing his responses to Defendants’ motions militates against now granting leave to amend; and (iii) Quilling’s request fails to comply with the applicable Local Rules. *See* N.D. TEX. L. CIV. R. 5.1(c); 7.1(c); 15.1(c). If the Court is inclined to grant Quilling an

opportunity to amend, Defendants request that the Court do so in accordance with Defendants' motion for a more definite statement under Rule 12(e) and with the particularity required by Rule 9(b).

WHEREFORE, PREMISES CONSIDERED, the Court should grant Defendants' Motion to Dismiss Plaintiff's Complaint, enter an Order dismissing the Complaint, and enter judgment for Mr. Erwin and Erwin & Johnson, LLP. To the extent that the Court does not dismiss all claims, the Court should grant Defendants' Motion for More Definite Statement and require that the remaining claims be repleaded in accordance with the Federal Rules of Civil Procedure and applicable state law.

Respectfully submitted,



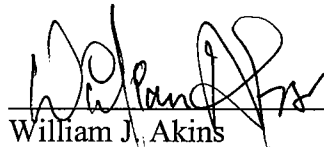
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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing document has been served on this 9th day of November, 2007, to all known counsel of record as required by the Federal Rules of Civil Procedure.



William J. Akins