UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

MICHAEL J. QUILLING, Receiver for ABC VIATICALS, INC. and Related Entities,	§	
Plaintiff,	§	
v.	§	**CIVIL ACTION NO.**
INTERNATIONAL FIDELITY & SURETY LIMITED, INTERNATIONAL CONSULTANTS & MANAGEMENT LTD., SURETY MARKETING SOURCE, LLC, KPMG VANUATU, HAWKES LAW, KPMG INTERNATIONAL, BOSWELL, DERMOTT & PAWLETT, LLP, MOHAN & ASSOCIATES, DAVID A. GOLDENBERG, DAG INVESTMENTS, LLC, LPG INVESTMENTS, LLC, WED MARKETING, LLC, GALAX HOLDINGS, LTD, MARK WOLOK, LINDA WOLOK and ARIE KOTLER,	§	**3-07-CV-0421-P**
Defendants.	§	**ECF**

DEFENDANT ARIE KOTLER'S REPLY TO PLAINTIFF'S RESPONSE TO MOTION TO DISMISS PLAINTIFF'S COMPLAINT AND BRIEF IN SUPPORT

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TO THE HONORABLE JORGE A. SOLIS:

Defendant Arie Kotler ("Kotler") files this Reply to the Response by Plaintiff to Kotler's Motion to Dismiss Plaintiff's Complaint and Brief in Support ("Response"), stating as follows:

INTRODUCTION

Plaintiff's Response attempts to transform a Complaint that hardly mentions Kotler at all into one in which Kotler has "joined in" nearly every alleged event. To do so, Plaintiff invokes incorrect or inapplicable pleading standards, resorts to erroneous strategies of imputing the alleged conduct of other defendants to Kotler, or simply repeats his earlier insufficient allegations. Without these contrivances, the Complaint simply fails to allege sufficient claims against Kotler and must be dismissed with prejudice.

ARGUMENT AND AUTHORITIES

I. Plaintiff Attempts to Justify His Complaint Under Incorrect Pleading Standards, Including One Recently Rejected by the United States Supreme Court in *Twombly*.

Plaintiff devotes nearly one third of his Response to arguing -- erroneously -- that Kotler "misstates the pleading standard that applies in this case." (Resp. at 2) He begins this discussion by invoking a standard that has recently been discredited by the United States Supreme Court. (Resp. at 2-4) Citing *Conley v. Gibson*, 355 U.S. 41 (1957), Plaintiff contends that under FED. R. CIV. P. 8, his Complaint should only be dismissed if relief cannot be granted under "any set of facts" that might be proved consistent with Plaintiff's allegations. (Resp. at 2-3) But in *Bell Atlantic Corp. v. Twombly*, 127 S. Ct. 1955 (2007) -- which Kotler cited repeatedly in his Motion and Brief but which appears nowhere in Plaintiff's Response -- the Supreme Court expressly rejected *Conley*'s formulation of pleading requirements, stating that the "any set of facts" language "has earned its retirement." *Id.* at 1968-69. Instead, the Supreme Court has made clear

that a plaintiff must plead "enough *facts* to state a claim to relief that is plausible on its face." *Id.* at 1974 (emphasis added). This requirement applies with even greater force to claims evaluated under FED. R. CIV. P. 9(b). *Dell, Inc. v. This Old Store, Inc.*, No. H-07-0561, 2007 WL 1958609, at *2 (S.D. Tex. July 2, 2007). As explained in Defendant's Motion and Brief, Plaintiff has failed to allege sufficient *facts* against Kotler to meet the *Twombly* pleading standard.

Plaintiff compounds this mistake by erroneously postulating an "even more relaxed" standard for receivers. (Resp. at 2-4) Plaintiff contends that because district courts have "broad powers and wide discretion" to "fashion appropriate relief" in receivership actions, conventional pleading standards do not apply. (*Id.* at 4) But the cases Plaintiff cites apply this principle in support of such procedures as combined hearings or the equitable distribution of funds, and nowhere suggest that basic pleading standards may be relaxed or ignored. *See SEC v. Basic Energy & Affiliated Res., Inc.*, 273 F.3d 657, 668 (6th Cir. 2001) (non-evidentiary hearing); *SEC v. Elliott*, 953 F.2d 1560, 1566 (11th Cir. 1992) (combined hearing).

Plaintiff further contends that "[r]eceivers are also held to a lower pleading standard when stating fraud claims" under FED. R. CIV. P. 9(b) when "the information surrounding the allegations is 'particularly within the knowledge of the defendant.'" (Resp. at 4 (quoting *Cadle Co. v. Schultz*, 779 F. Supp. 392, 396 (N.D. Tex. 1991)) Plaintiff is incorrect to suggest that receivers enjoy their own special pleading standards. The doctrine that Rule 9(b)'s particularity requirements "may be to some extent relaxed" when the necessary information is in the exclusive possession of the defendant is one of general applicability. *See United States ex rel. Willard*, 336 F.3d 375, 385 (5th Cir. 2003) (*qui tam* action).[1] More importantly, Plaintiff cannot avail himself

[1] Where applicable, this "relaxed" standard has only a limited effect. *See Tuchman v. DSC Commc'ns Corp.*, 14 F.3d 1061, 1068 (5th Cir. 1994) (the "relaxed" standard "must not be mistaken for a license to base claims of fraud on speculation and conclusory allegations").

of this "relaxed" pleading standard because he has failed to allege in his Complaint "that the necessary information lies within defendants' control" and to provide "a statement of facts upon which [those] allegations are based." *Naporano Iron & Metal Co. v. Am. Crane Corp.*, 79 F. Supp. 2d 494, 511 n.27 (D.N.J. 1999); *see also Brown v. Coleman Invs., Inc.*, 993 F. Supp. 439, 447 n.41 (M.D. La. 1998).[2] Plaintiff's mistaken reliance on this "relaxed standard" pervades the Response (*see* Resp. at 4-5, 7, 9, 12, 21), yet cannot compensate for his Complaint's lack of sufficient allegations against Kotler.

Finally, Plaintiff is incorrect that Rule 9(b) applies only to the claims he has labeled "fraud." (Resp. at 5-7) Because Plaintiff's claims for fraudulent transfer, aiding and abetting breach of fiduciary duty, and negligence are all predicated on allegations of fraudulent conduct, and thus "sound in fraud," they must meet Rule 9(b)'s particularity requirements. (Mot. at 7-8) Multiple courts – including this Court – have held that Rule 9(b) governs claims under the Uniform Fraudulent Transfer Act. *E.g.*, *Kranz v. Koenig*, 240 F.R.D. 453, 455-56 (D. Minn. 2007) (declining to follow *China Res. Prods. (U.S.A.) Ltd. v. Fayda Int'l, Inc.*, 788 F. Supp. 815 (D. Del. 1992), cited by Plaintiff (Resp. 6-7)); *Quilling v. Stark*, No. 3:05-CV-1976-L, 2006 WL 1683442, at *5 n.4 (N.D. Tex. June 19, 2006). In contending that Rule 9(b) cannot apply to fiduciary duty and negligence claims because the "elements" of those claims do not necessarily require proof of fraud, Plaintiff simply misses the point. (Resp. at 5-6) Where, as here, a

[2] Nor has Plaintiff generally based his allegations, with two exceptions (Compl. ¶ 29), on "information and belief," which is permissible under such circumstances. *Willard*, 336 F.3d at 385.

Plaintiff's Response is similarly deficient. It contains merely the unsupported claim that "only Kotler and the other Defendants know the specific facts and circumstances surrounding these transactions." (Resp. at 5) This statement, like his assertion that "ABC's principles [sic] have invoked their Fifth Amendment rights" (*id.*), is improper because a party may not supplement its complaint by alleging additional facts in its response to a motion to dismiss. 2 JAMES WM. MOORE, ET AL., MOORE'S FEDERAL PRACTICE §12.34[2] (3d ed. 2007). It also lacks any factual basis to explain why this information (which Plaintiff never identifies) is in Kotler's exclusive possession and is unavailable to Plaintiff.

plaintiff has asserted fraudulent conduct *exclusively* in support of such claims, Rule 9(b) should apply. *See Ingalls v. Edgewater Private Equity Fund III, L.P.*, No. Civ.A. H-05-1392, 2005 WL 2647962, at *5 (S.D. Tex. Oct. 17, 2005); *see also Naporano*, 79 F. Supp. 2d at 510 (Rule 9(b) applies to a claim "sounding" in fraud, despite variance between elements of proof for that claim and common law fraud claim).[3]

II. When Viewed Under the Correct Standards, Plaintiff's Allegations Fail to State a Claim Against Kotler and Must Be Dismissed.

Stripped of Plaintiff's distorted pleading standards, the allegations in the Complaint wholly fail to state a claim against Kotler. As Kotler pointed out in his Motion and Brief, the Complaint contains only *four* specific allegations against Kotler himself:

1. Kotler "purported to serve as the managing director and beneficial owner" of IFS and ICM (Compl. ¶ 23);
2. IFS and ICM "exist only on paper" as the "alter egos" of Kotler and two other defendants (*id.* ¶ 24);
3. Plaintiff groups Kotler together with a number of other defendants as the "Bonding Company Defendants" (*id.* ¶ 35); and
4. Kotler and others "owned and controlled" the Bonding Company Defendants (*id.* ¶ 46).

The rest of the Complaint refers to Kotler, if at all, only as one of the "defendants" or "Bonding Company Defendants." These allegations are simply insufficient to state Plaintiff's various claims against Kotler specifically and individually. (Mot. at 8-18)

In an attempt to overcome the paucity of these allegations, Plaintiff resorts to three related, but equally unavailing, tactics to attribute much of the alleged conduct to Kotler. First, Plaintiff repeatedly invokes his allegation that Kotler "purported to serve as managing director and beneficial owner" of IFS and ICM as his basis for imputing the alleged conduct of those

[3] Plaintiff has not alleged lesser conduct such as "mere recklessness or negligent behavior" (Resp. at 6 n.1), and therefore cannot invoke that conduct as a means to avoid Rule 9(b)'s application to these claims.

entities to Kotler. (Resp. at 9, 11-13, 18, 21-22) The primary defect with this tactic is that the Complaint alleges that Galax Holdings, Inc. ("Galax") also served as "the managing director" of IFS and ICM. (Compl. ¶ 23) The Complaint never makes clear *when* Kotler and Galax each allegedly held this position. Because they could not *both* have served as "the" managing director, some or all of the alleged conduct may have occurred during Galax's tenure and thus Plaintiff cannot -- based on this allegation -- attribute these actions of IFS and ICM to Kotler.

Second, Plaintiff defends his pervasive reliance on group pleading by invoking the "presumption" that public statements by a corporation may be attributed to its senior executives. (Resp. at 21-22) To the degree it exists, this presumption is entirely inapplicable. Before the passage of the PSLRA, plaintiffs could plead collective allegations against senior executives based on the presumption "that statements in prospectuses and press releases [were] the collective work of those individuals with direct involvement in the day-to-day affairs of the company." *Coates v. Heartland Wireless Commc'ns, Inc.*, 26 F. Supp. 2d 910, 915 (N.D. Tex. 1998). But none of the misrepresentations alleged in the Complaint appears in such press releases or prospectuses; instead, they are specific inducements to and contracts with ABC. (Compl. ¶¶ 22-30, Ex. 3-6)

Moreover, this "group pleading doctrine" has now been wholly repudiated as inconsistent with the PSLRA and Rule 9(b). *Southland Sec. Corp. v. INSpire Ins. Solutions, Inc.*, 365 F.3d 353, 364-65 (5th Cir. 2004); *Kunzweiler v. Zero.Net, Inc.*, No. CIV .A.3:00-CV-2553-P, 2002 WL 1461732, at *13 n.15 (N.D. Tex. July 3, 2002) (Solis, J.). Indeed, other judges from this Court have specifically disagreed with the "group pleading" analysis in *Zuckerman v. Foxmeyer Health Corp.*, 4 F. Supp. 2d 618 (N.D. Tex. 1998), Plaintiff's lone supporting authority. *E.g.*, *In re Capstead Mortgage Corp. Sec. Litig.*, 258 F. Supp. 2d 533, 561-62 (N.D. Tex. 2003); *Coates*,

26 F. Supp. 2d at 915-16. To satisfy Rule 9(b), Plaintiff cannot merely name every executive who may have "had a hand" in the misrepresentation (Resp. at 22), but rather must "identif[y] . . . the officer or director responsible for making the statement." *In re Capstead Mortgage*, 258 F. Supp. 2d at 562. Plaintiff has not met this requirement.

Third, Plaintiff contends that he has pleaded "sufficient facts to impose alter ego liability on Kotler for the acts of IFS and ICM." (Resp. at 20-21; *see also id.* at 9, 11) But Plaintiff's allegations that IFS and ICM are "fictitious," "exist only on paper," and function as "alter egos" of Kotler, Goldenberg, and Wolok are simply legal conclusions, not objective factual statements. (Compl. ¶¶ 24, 35) Similarly, his claims that these entities lacked "offices, employees, or facilities," had false financial statements, and that Goldenberg and Wolok diverted funds for their own use (Resp. at 20) do not suffice to show the requisite "unity" between the entities ***and Kotler*** to support an alter ego finding. (Mot. at 13-14)[4] Kotler's alleged role as "the managing director and beneficial owner" at some unspecified time is also insufficient to establish an alter ego relationship. (*Id.* at 14)

Thus distilled, the allegations supporting Plaintiff's various claims against Kotler are insufficient as a matter of law:

Fraud. Plaintiff's fraud claim is premised entirely on attributing the alleged actions of other defendants to Kotler, without asserting sufficient allegations against Kolter himself, in violation of FED. R. CIV. P. 9(b). Contrary to Plaintiff's Response, the Complaint does not allege that *Kotler* made the "numerous fraudulent representations to ABC" (Resp. at 11), but rather attributes them to SMS, Goldenberg, Wolok, IFS, and ICM (Compl. ¶¶ 25-26). Plaintiff contends that the exhibits to his Complaint are more than sufficient to establish the substance and

[4] Indeed, Plaintiff ignores the fact that at one point in his Complaint, he alleges that IFS and ICM are the alter egos of Godenberg and Wolok, but not Kotler. (Compl. ¶ 27; Mot. at 13 n.11)

details of these representations (Resp. at 12), but nowhere in any of these exhibits does Kotler's name appear (Compl. Ex. 3-6). Only by improperly relying on the various imputation tactics described above can Plaintiff claim that Kotler was involved in this conduct. (*E.g.*, Resp. at 11 (arguing that "Kotler made" the misrepresentations "as the managing director, beneficial owner, and alter ego" of IFS and ICM)) But even this enterprise would involve making significant inferential leaps, such as Plaintiff's speculation that by virtue of his managing directorship, Kotler "must have known" that the representations were false. (*Id.*) The Complaint also fails to allege where or when the various misrepresentations took place, or to whom they were directed, and otherwise depends on bare legal conclusions. (Mot. at 10-11) Accordingly, Plaintiff has not met the requirements of Rule 9(b).

Aiding and Abetting Breach of Fiduciary Duty. Similarly, the factual allegations supporting Plaintiff's claim for aiding and abetting ABC's breach of fiduciary duty implicate only SMS, Goldenberg, Wolok, IFS, and ICM. (Mot. at 11; Compl. ¶¶ 25-28) Again, Plaintiff argues that Kotler "joined" these activities based on the imputation tactics discussed above. (Resp. at 12-13) The allegations are also impermissibly vague: for example, they do not explain how Kotler "allowed" ABC to make the various misrepresentation, when or where the misrepresentations took place, or to whom they were directed. (Mot. at 11)

Fraudulent Transfer. Despite Plaintiff's belief that his fraudulent transfer claim is "very straightforward," the allegations supporting that claim bear no connection to Kotler himself. (Resp. at 16) The alleged transfers were made to other defendants, not Kotler. (Compl. ¶¶ 26-28) Without allegations of Kotler's involvement, this claim must be dismissed.

Negligence. Plaintiff fails to respond to the fact that many of the allegations in his negligence claim are simply "legal conclusions resting on . . . prior allegations" that do not

reference Kotler, and thus fail to meet the pleading standard under Rule 8 or Rule 9. *Twombly*, 127 S. Ct. at 1970. (Mot. at 11-12) The claim is also barred by the economic loss rule, which Plaintiff misconstrues. (Resp. at 16) While the rule has been applied in the context he describes -- barring recovery of economic losses in tort cases when the loss is the subject of a contract between the parties -- it has *also* been applied to preclude recovery of economic damages where, as here, the parties are "contractual strangers" and there is "no accompanying claim for damages to a person or property." *E.g.*, *Coastal Conduit & Ditching, Inc. v. Noram Energy Corp.*, 29 S.W.3d 282, 285-90 (Tex. App.—Houston [14th Dist.] 2000, no pet.). Accordingly, the negligence claim cannot stand.[5]

Negligent Misrepresentation. Plaintiff essentially ignores Kotler's discussion of this claim. Plaintiff once more relies on Kotler's temporally indeterminate role as "the managing director and beneficial owner" of IFS and ICM to justify his argument that Kotler "ma[de] numerous misrepresentations to ABC." (Resp. at 18) But again, the allegations themselves attribute the statements to other defendants, not to Kotler. The remaining allegations are merely conclusory assertions and "formulaic recitation of the elements," *Twombly*, 127 S. Ct. at 1965, such as ABC's "justifiable reliance" on the alleged misrepresentations, without any factual allegations to show that this reliance was reasonable. (Mot. at 16-17)[6]

III. Despite His Arguments to the Contrary, Plaintiff Lacks Standing to Assert The Fiduciary Duty and Fraudulent Transfer Claims.

Plaintiff cannot assert either his fiduciary duty or fraudulent transfer claims because the claims belong only to the customers and creditors of the receivership entities, not to the entities

[5] Contrary to Plaintiff's belief, Kotler did not "mischaracterize" this claim as one for professional malpractice. (Resp. at 15) Kotler's arguments regarding the malpractice allegations were offered in response to Plaintiff's claim as alleged in the Complaint.

[6] As explained in Kotler's Motion and Brief, because Plaintiff has failed to allege any predicate tort against Kotler, his claim for conspiracy fails as well. (Mot. at 17-18)

themselves. Plaintiff contends that he has standing to bring the fiduciary duty claim on behalf of certain "investor trusts." (Resp. at 13-14) Plaintiff does not argue that ABC owed fiduciary duties to these trusts, however, but rather that the alleged mismanagement of the trusts was one of the means by which ABC breached its duties to the customers. (*Id.* at 13 ("ABC's fiduciary duties to its investors included careful and competent management of their investor trusts"); *accord* Compl. ¶¶ 34-35; Mot. at 19)) Thus, even if Plaintiff could act on behalf of these trusts,[7] the basic fact remains that, as alleged in the Complaint, ABC's fiduciary duties (if any) were owed to its customers and those customers are not receivership entities. (Mot. at 20-21)[8]

With regard to his fraudulent transfer claim, Plaintiff cannot overcome the fact that receivers are precluded from asserting such claims on behalf of the defrauded creditors of a receivership entity. (Mot. at 20-22) Plaintiff premises his fraudulent transfer claim on the recovery of "investor funds." (Compl. ¶ 49 (alleging that ABC "made numerous undisclosed transfers of investor funds," which were made "with the intent to hinder, delay, and defraud creditors")) As alleged, this claim seeks to recover funds belonging to parties that are not receivership entities; it does not, as Plaintiff now asserts, seek "to recover ABC funds." (Resp. at 17) Because this claim purports to enforce a right of the customers, and not ABC, Plaintiff lacks standing to assert it. *E.g.*, *Scholes v. Schroeder*, 744 F. Supp. 1419, 1421-24 (N.D. Ill. 1990).[9]

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[7] This is far from clear. The trusts were defined as "Receivership Assets" in this Court's clarifying order, cited by Plaintiff (Resp. at 13); neither that order nor the original appointment order purports to transform all such assets into receivership entities on whose behalf Plaintiff could sue. (Compl. Ex. 1-2)

[8] Plaintiff also cites this Court's order purporting to authorize him to bring claims on behalf of "constructive trust beneficiaries." (Resp. at 13-14) But Plaintiff ignores the fact that this order, to the extent it purports to authorize Plaintiff to assert claims on behalf of non-receivership entities like ABC's customers, runs afoul of Article III of the United States Constitution. (Mot. at 20)

[9] Because it concerned the recovery of funds belonging to receivership entities, *Scholes v. Lehmann*, 56 F.3d 750, 754-55 (7th Cir. 1995), is distinguishable. To the extent Plaintiff relies on other cases that simply posit a receiver's standing to assert fraudulent transfer claims on behalf of a receivership entity's

IV. This Court Should Not Permit Plaintiff To Amend His Complaint.

In a single, perfunctory paragraph, Plaintiff seeks leave to amend his Complaint if the Court agrees with Kotler that the Complaint is deficient. (Resp. at 8-9) The Court should deny Plaintiff's request and dismiss the Complaint with prejudice. The Fifth Circuit and this Court have repeatedly held that this kind of "general curative amendment request," frequently included "almost as an afterthought" to a response to a motion to dismiss, should not be granted. *E.g.*, *Goldstein v. MCI WorldCom*, 340 F.3d 238, 254-55 (5th Cir. 2003); *McKinney v. Irving Indep. Sch. Dist.*, 309 F.3d 308, 315 (5th Cir. 2002); *In re Capstead Mortgage*, 258 F. Supp. 2d at 566-67. Though Plaintiff has been aware of Kotler's objections to his Complaint and could have attempted to cure those deficiencies by amending the Complaint in response, Plaintiff has instead stood on the sufficiency of his pleadings. *See Goldstein*, 340 F.3d at 255. He has not demonstrated how he would replead the Complaint, provided a proposed amended complaint, or suggested any additional facts not initially pleaded that could cure the defects identified by Kotler. *Id.* Because Plaintiff has not pursued any of the curative steps noted above, and instead taken a "'wait-and-see-what-happens' approach," leave to replead should be denied. *In re Capstead Mortgage*, 258 F. Supp. 2d at 567 (repleading under these circumstances would waste time and resources); *see also Goldstein*, 340 F.3d at 255 n.6 (noting criticism of same tactics as "'wait and see' approach" and "'cat and mouse' . . . gamesmanship") (citations omitted).

CONCLUSION

For the reasons stated above and in his Motion and Brief, Defendant Arie Kotler respectfully prays that this Court dismiss all of Plaintiff's claims against him with prejudice.

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creditors/investors (Resp. at 17), Kotler has already explained that those cases are either distinguishable or simply incorrect (Mot. at 22 n.14).

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on August 21, 2007, I electronically submitted the foregoing document with the clerk of court for the U.S. District Court, Northern District of Texas, using the electronic case files system of the court. The electronic case filing system sent a "Notice of Electronic Filing" to the following individuals who have consented in writing to accept this Notice as service of this document by electronic means:

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I hereby certify that I have served the foregoing document by mailing a copy to the following individual:

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