

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

MICHAEL J. QUILLING, Receiver	§	
for Megafund Corporation and	§	
Lancorp Financial Group, LLC,	§	
	§	
Plaintiff,	§	Civil Action No. 3:06-CV-0959(BD)
	§	
v.	§	ECF
	§	
GARY McDUFF, Individually and d/b/a	§	Referred to the U.S. Magistrate Judge
SOUTHERN TRUST COMPANY and	§	
FIRST GLOBAL FOUNDATION,	§	
ROBERT REESE, Individually and d/b/a	§	
EXCEL FINANCIAL, INC., and	§	
SHANNON McDUFF, Individually and	§	
d/b/a SECURED CLEARING CORP.,	§	
	§	
Defendants.	§	

**PLAINTIFF’S RESPONSE TO
DEFENDANT GARY McDUFF’S MOTION TO DISMISS**

TO THE HONORABLE JEFF A. KAPLAN, UNITED STATES MAGISTRATE JUDGE:

COMES NOW, Michael J. Quilling, in his capacity as Receiver for Megafund Corporation and Lancorp Financial Group, LLC, (“Plaintiff” or “Receiver”) and responds to the Challenge of Jurisdiction [Dkt. No. 20] filed by Defendant Gary McDuff. The Court has construed Defendant’s challenge as a motion to dismiss for lack of subject matter jurisdiction under Fed. R. Civ. P. 12(b)(1). *Order of August 18, 2006* [Dkt. No. 19]. The Receiver would, therefore, respectfully show unto the Court as follows:

I. INTRODUCTION

It is well-settled that, when a District Court appoints a Receiver in a case where it has subject matter jurisdiction, it maintains that jurisdiction over all ancillary cases later filed by the Receiver. Without question, this Court has subject matter jurisdiction in the SEC's civil action involving numerous questions of federal law. Since the Receiver was appointed in that action, the Court has ancillary subject matter jurisdiction in this case and all others brought on behalf of the Receivership Estate.

II. FACTUAL BACKGROUND

Court Orders Relating to the Receiver's Appointment

1. This case arises out of a lawsuit brought by the Securities and Exchange Commission ("SEC") against numerous defendants involved in a purported investment program. *Securities and Exchange Commission, v. Megafund Corporation, et al.*, Cause No. 3:05-CV-1328-L (N.D. Tex.) (the "SEC case"). The SEC brought that suit against Stanley A. Leitner, Megafund Corporation ("Megafund"), and others for promising high-yield returns to investors and then squandering their money on undisclosed expenditures. *Complaint* [Dkt. No. 1] (3:05-CV-1328).

2. The Court overseeing the SEC case appointed Michael J. Quilling as Receiver for the defendants and relief defendant on July 5, 2005 and he has since continued to function in that capacity. *Order Appointing Temporary Receiver* ("Order Appointing Receiver") [Dkt. No. 9], as amended July 19, 2005 [Dkt. No. 36] (3:05-CV-1328).

3. That Court later expanded the Receivership Estate to include Megafund's largest single contributor, Lancorp Financial Group, LLC, and the funds it managed through Lancorp

Financial Fund Business Trust (collectively, “Lancorp”). *Agreed Order Expanding Receivership and Appointing Receiver* (“Order Expanding Receivership”) [Dkt. No.84], as amended on March 1, 2006 [Dkt. No. 98] (3:05-CV-1328). Michael J. Quilling was appointed Receiver for both entities and he has since continued to function in that capacity. *Id.*

Court Orders Relating to Subject Matter Jurisdiction

4. The Order Appointing Receiver gives this Court exclusive jurisdiction over all cases relating to assets traced to the Megafund Receivership Estate:

This Court hereby takes exclusive jurisdiction and possession of the assets, monies, securities, claims in action, and properties, real and personal, tangible and intangible, of whatever kind and description, wherever situated, of Megafund Corp. [et al.] . . .

* * *

Any actions so authorized to determine disputes relating to Receivership Assets and Receivership Records shall be filed in this Court.

Order Appointing Receiver [Dkt. No. 36] at ¶¶ 1, 5 (3:05-CV-1328) (emphasis added).

5. Similarly, the Order Expanding Receivership gives this Court exclusive jurisdiction over all cases relating to the Lancorp Receivership Estate:

This Court hereby takes exclusive jurisdiction and possession of the assets, monies, securities, claims in action, and properties, real and personal, tangible and intangible, of whatever kind and description, wherever situated, of Lancorp Financial Group, LLC . . . and any entities it controls . . .

* * *

Any actions so authorized to determine disputes relating to Receivership Assets and Receivership Records shall be filed in this Court.

Order Expanding Receivership [Dkt. No.84], as amended on March 1, 2006 [Dkt. No. 98] (3:05-CV-1328).

Defendant's Challenge to this Court's Subject Matter Jurisdiction

6. Following his appointment, the Receiver filed this action against the Defendant for his role in soliciting new investors—including Lancorp—into the Megafund investment program. *Complaint* [Dkt. No. 1] at ¶¶ 11-15. As set forth in the Complaint, the Receiver has identified two transfers totaling \$304,272.58 that Defendant received as compensation from Megafund and Lancorp. *Id.* Bank records clearly show that Defendant (1) kept some of the money in his own accounts, (2) forwarded some to his wife, Shannon McDuff, and a business associate named Robert Reese, and (3) used \$152,401.55 to purchase a home at 1318 Minchen Drive in Deer Park, Texas. *Id.* The Receiver filed this lawsuit to recover those assets as fraudulent transfers or proceeds originating from a *Ponzi* scheme. *Id.*

7. Defendant has now filed a Challenge of Jurisdiction that, among other things, questions this Court's ability to render a judgment on the Receiver's claims. *Respondent's Challenge of Jurisdiction* [Dkt. No. 20]. The Court has construed this pleading as a motion to dismiss for lack of subject matter jurisdiction under Fed. R. Civ. P. 12(b)(1). *Order of Aug. 18, 2006* [Dkt. No. 19].

8. As explained more fully below, Defendant fails to recognize that this Court enjoys ancillary subject matter jurisdiction over all cases relating to the main SEC case. Furthermore, this Court has clearly reserved its own exclusive jurisdiction over all disputes relating to the Receivership Assets of Megafund and Lancorp. Accordingly, Defendant's motion to dismiss is without any legal basis and should be denied.

III. ARGUMENTS AND AUTHORITIES

It is well-settled that, when a federal court appoints a Receiver, it retains ancillary jurisdiction over all suits filed in furtherance of the Receivership Estate. *Quilling v. Cristell*, 2006 WL 316981 at *4 (W.D.N.C. Feb. 9, 2006); *see also Tscherepnin v. Franz*, 485 F.2d 1251, 1255 (7th Cir. 1973); *Haile v. Henderson Nat'l Bank*, 657 F.2d 816, 822 (6th Cir. 1961); *S.E.C. v. Shiv*, 379 F.Supp.2d 609, 615 (S.D.N.Y. 2005); *Missal v. Alexander*, 2000 WL 274230 (D.C. Cir. Feb. 15, 2000); *City of Detroit v. Michigan*, 538 F.Supp. 1169, 1172 (E.D. Mich. 1982). The United States Supreme Court has explained that subject matter jurisdiction flows from the main receivership case into suits later brought by the court appointed Receiver:

When an action or suit is commenced by a receiver . . . to accomplish the ends sought and directed by the suit in which the appointment was made, such action or suit is regarded as ancillary so far as the jurisdiction of the circuit court . . . is concerned; and we have repeatedly held that jurisdiction of these subordinate actions or suits is to be attributed to the jurisdiction on which the main suit rested

Pope v. Louisville, New Albany & Chicago R.R., 173 U.S. 573, 577 (1899) (emphasis added); *see also* 12 Wright, Miller, & Marcus, FED. PRAC. & PROC. §§ 2985 (2d ed. 1997) (“A federal receiver may sue in the court of his or her appointment . . . and such action or suit is regarded as ancillary to the court’s original subject matter jurisdiction”).

There is no doubt that this Court enjoys subject matter jurisdiction in the main case. The SEC brought that action under the Securities Act of 1933 and the Securities Exchange Act of 1934. *See Complaint* [Dkt. No. 1] at ¶¶ 4-5 (3:05-CV-1328). This Court, therefore, enjoys original subject matter jurisdiction in that case. *See* 28 U.S.C. § 1331 (granting district courts original jurisdiction over all actions arising under laws of the United States); 28 U.S.C. § 1345 (granting district courts original jurisdiction over all civil actions commenced by an agency of the United

States); *see also Cristell*, 2006 WL 316981 at *4 (explaining that cases brought under the Securities Act of 1933 and the Securities Exchange Act of 1934 raise “federal question subject matter jurisdiction”).

Since the Receiver was appointed in the SEC case, this Court retains subject matter jurisdiction over every suit brought by him “irrespective of diversity, amount in controversy or any other factor which would normally determine jurisdiction.” *Haile*, 657 F.2d at 822 (describing such jurisdiction as “ancillary subject matter jurisdiction”); *Grassmueck v. Bensky*, 2005 WL 1076533 at *2 (W.D. Wash. May 5, 2005); *see also Gunby v. Armstrong*, 133 F. 417, 426 (5th Cir. 1904) (noting that, once the District Court acquired jurisdiction, “any suits thereafter instituted by the receiver for the collection of the assets . . . were clearly within its cognizance, regardless of the citizenship of the parties or of the amount in controversy”).

This principle is most clearly illustrated in *Quilling v. Cristell*, 2006 WL 316981 (W.D.N.C. Feb. 9, 2006). In that case, the SEC filed a civil suit against Frederick Gilliland in connection with a *Ponzi* scheme he orchestrated to defraud investors. *Id.* at *1. That Court then appointed the Receiver to preserve and protect the Receivership Estate’s assets. *Id.* The Receiver promptly filed an ancillary suit against Marilyn Cristell and the estate of Raymond R. Cristell for receiving \$115,000.00 of investor funds that were fraudulently transferred from the *Ponzi* scheme. *Id.* Cristell responded with a motion to dismiss for, among other things, lack of subject matter jurisdiction. *Id.* The District Court denied the motion, noting that “[s]ubject matter jurisdiction is proper in this case under the principles of ancillary jurisdiction.” *Id.* at *4. It explained that, in raising questions of federal law related to the Securities Act of 1933 and the Securities Exchange Act of 1934, the SEC’s suit invoked the Court’s subject matter jurisdiction over the main case. *Id.* Since the suit against Cristell was furthering the Receivership Estate’s objectives,

the Court ruled that it had “ancillary subject matter jurisdiction” over that case and all others brought by the Receiver. *Id.*

This Court has further underscored its jurisdiction over these cases by issuing numerous orders directing the Receiver to file actions here. The Order Appointing Receiver specifically retains this Court’s “exclusive jurisdiction” over Receivership Assets and explains that all disputes related to those assets “shall be filed in this Court.” *Order Appointing Receiver* [Dkt. No. 36] at ¶¶ 1, 5 (3:05-CV-1328). Later orders expanding the receivership mirror that language. *Order Expanding Receivership* [Dkt. No.84], as amended on March 1, 2006 [Dkt. No. 98] (3:05-CV-1328).

Defendant’s challenge, however, does not address the merits of jurisdiction in the main case or ancillary jurisdiction in this case. Rather, Defendant claims that the United States is really the “UNITED STATES CORPORATION” and jurisdiction cannot be had over him without his implied consent. *Challenge of Jurisdiction* [Dkt. No. 20] at 2. Furthermore, Defendant dismisses federal laws as non-binding “municipal opinions” that cannot form the basis of subject matter jurisdiction over him. *Id.* at 4. The remainder of Defendant’s motion is based on the mistaken idea that the SEC is attempting to put his alter ego, Southern Trust Company, into receivership. *Id.* at 4-6. The Receiver respectfully submits Defendant’s Challenge of Jurisdiction is nothing more than indignant fluff that fails to raise a single, legitimate basis for denying subject matter jurisdiction in this case.

Respectfully submitted,

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ATTORNEYS FOR PLAINTIFF

CERTIFICATE OF SERVICE

On September 12, 2006, a true and correct copy of the above and foregoing was sent by first class mail, with full and proper postage prepaid, to:

Gary McDuff
1314 Minchen Drive
Deer Park, Texas 77536

/s/ Brent J. Rodine
Brent J. Rodine