UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF WISCONSIN

FAYE B. FEINSTEIN, not individually, but as receiver for WML Gryphon Fund LLC,

Plaintiff,

Civil Action No. 11-CV-00058

v.

BRIAN W. BENDER, individually and in his capacity as trustee of the Brian W. Bender Personal Revocable Trust and the Brian W. and Marianne P. Bender Joint Revocable Trust, and MARIANNE P. BENDER, individually and in her capacity as trustee of the Brian W. and Marianne P. Bender Joint Revocable Trust,

Defendants.

DEFENDANTS' CIVIL L.R. 7(h) AND 7(i) EXPEDITED NON-DISPOSITIVE MOTION FOR LEAVE TO FILE A REPLY MEMORANDUM OF LAW IN EXCESS OF THE 15 PAGE LIMIT IN CIVIL L.R. 7(f)

Defendants, Brian W. Bender, individually and in his capacity as trustee of the Brian W. Bender Personal Revocable Trust and the Brian W. and Marianne P. Bender Joint Revocable Trust, and Marianne P. Bender, individually and in her capacity as trustee of the Brian W. and Marianne P. Bender Joint Revocable Trust (collectively, the "Defendants"), by and through their undersigned counsel, hereby move this Court for leave to file a Reply Memorandum of Law in excess of the 15 page limit in Civil L.R. 7(f), and further move the Court to file the Reply Memorandum pursuant to Civil L. R. 7(i). In support of this Motion, Defendants state as follows:

WHD/7820540.1

1. Plaintiff filed a 25 page Complaint, which included 125 numbered paragraphs, and a number of subparagraphs, raising six causes of action against Defendants on January 20, 2011.

2. The Complaint attaches a number of exhibits, and also incorporates by reference the SEC's underlying complaint, and a number of other documents from ancillary proceedings.

3. On March 25, 2011, Defendants filed a Motion to Dismiss Plaintiff's Complaint, along with a Memorandum of Law in Support. The Motion seeks dismissal of all six of Plaintiff's causes of action.

4. Plaintiff filed a 30 page Response In Opposition to Defendants' Motion to Dismiss on April 15, 2011. Plaintiff's Response argues that all six of Plaintiff's causes of action are proper and should not be dismissed.

4. Defendants Reply Memorandum of Law in Support of Their Motion to Dismiss is due May 2, 2011.

5. Defendants respectfully request leave to file a Reply Memorandum of Law that is 18 pages long, which would exceed the 15 page limit set forth in Civil L.R. 7(f) by three pages.

6. Defendants believe the additional pages are necessary in order to fully brief the issues raised by each of the six counts of Plaintiff's Complaint, including issues related to the Receiver's authority and/or standing to bring the causes of action she is attempting to bring against Defendants. Furthermore, Plaintiff's Response Brief is itself detailed, and in order for the Court to have a clear picture of the relevant legal arguments, a somewhat detailed response from Defendants is required. Relatedly, if Defendants' Motion is unsuccessful because of an inability to rebut Plaintiffs' arguments based on page limitations alone, Defendants will incur further and substantial expenses in defending themselves.

7. Defendants' Reply Memorandum of Law is attached hereto as Exhibit A, as required by Civil L.R. 7(i).

WHEREFORE, Defendants respectfully request that the Court grant their Motion for Leave to file a Reply Memorandum of Law in excess of the 15 page limit in Civil L.R. 7(f), and further move the Court to file the Reply Memorandum pursuant to Civil L. R. 7(i)

Date: May 2, 2011.

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Attorneys for Defendants, Brian W. Bender, *individually and in his capacity as trustee of the Brian W. Bender Personal Revocable Trust and the Brian W. and Marianne P. Bender Joint Revocable Trust, and* ***Marianne P. Bender****, individually and in her capacity as trustee of the Brian W. and Marianne P. Bender Joint Revocable Trust*

("Nor does [the proponent] present any caselaw supporting its theory. It is not the job of this court to develop arguments . . . ."); *United States v. Alden*, 527 F.3d 653, 664 (7th Cir. 2008).

And yet, citing two Depression era cases, *McCandless v. Furlaud*, 296 U.S. 140 (1935), and *Texas & Pac. Ry. Co. v. Pottorff*, 291 U.S. 245 (1934), the Receiver argues that she can pursue claw-back claims even though she admits "that none of the counts of the Complaint allege intentional misconduct by [the Benders]." (Resp. Br. at 7.) Those cases are inapposite: neither permits a receiver to pursue claims (1) against an innocent party for (2) funds that were not in the receivership entity's account at the time the receiver was appointed.[3]

The Receiver's problem is that she concedes she is not pursuing claims against the Benders as "relief defendants." Without naming the Benders as "relief defendants," she offers no authority that would allow her to pursue "claw-back" claims against an innocent party, for less-than-principal money, that was not in Gryphon's account when she was appointed. In other words, *McCadless* might be relevant if the Receiver was pursuing "claw-back" claims against Putman, and *Pottorff* might be relevant if the Benders were asking the Receiver to pay them money that is still in Gryphon's account, but since neither of those is happening here, those cases do not allow the Receiver to pursue the Benders as anything other than relief defendants.[4]

The Receiver fails to appreciate the distinction between suits over: (1) money that is in the receivership estate at appointment; and (2) money that is ***not*** in the receivership estate at appointment. That is, she fails to appreciate that she is attempting to bring a "claw-back" claim against the Benders, as opposed to seeking permission *to refuse to pay* the Benders the full

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[3] *McCandless* allowed the receiver to pursue "claw-back" claims against the promoters who had violated several state laws when *the promoters* fraudulently diverted money away from other investors. 296 U.S. at 149, 156, 160-61. Thus, the defendants were not innocent parties, but even as wrongdoers, the receiver had no right to their principal. *Id.* at 164 (the wrongdoers "became accountable . . . for everything that came to them as a result of the conspiracy ***in excess of the consideration furnished on their side***.") (emphasis added). Likewise, in *Pottorff*, the innocent party (the Railway) *sued the receiver* and demanded full payment out of the receivership company's coffers for an amount that it had loaned to the receivership company before the company failed. 291 U.S. at 251. That is, the money at issue was still in the receivership company's coffers at the time the receiver was appointed, and the dispute was whether the innocent party could force the receiver to pay it in full.

[4] Although as explained below, she cannot pursue claims against them as relief defendants either.

amount in their request. This issue goes to the heart of the distinction between this case and *SEC v. Wealth Management LLC*, 628 F.3d 323 (7th Cir. 2010). In *SEC*, the decision only applied to situations "*where investors' assets **are** commingled* . . . ." 628 F.3d at 333 (emphasis added). Here, the Receiver admits that the last payment was made a month before she was appointed. The Receiver fails to cite a single case that would vest the Receiver with the extraordinary authority to pursue claims against (1) an innocent party that (2) has not been named as a relief defendant for (3) money that was not in Gryphon's account when the Receiver was appointed.

In a 2009 amicus brief, the SEC explained the distinction: "The equity of distributing receivership estate assets pro rata, however, has no bearing on whether the receiver may, under equitable principles, claw back principal payments made to innocent investors in order to increase the assets available for distribution. When funds are not in the receivership estate but have been transferred to investors, markedly different equities are implicated that do not arise in the context of the approval of a distribution plan." 2009 WL 6338943 at *24. As such, bringing claims against "innocent investors for the return of the funds they invested would come at great cost to these victims and the receivership estate, and with questionable benefit to all of the victims . . . ." *Id.* at *28.

Moreover, even the fraud allegations the Receiver provides (allegedly having to do with Putman and Fevola) do not give her standing to pursue claims against the Benders, because those allegations merely relate to the "sales step" of a fraud claim. *See Knauer v. Jonathan Roberts Fin. Group, Inc.*, 348 F.3d 230, 233-34 (7th Cir. 2003) (fraudulent inducement to invest actually increases the entity's coffers, so there is not harm until the funds have been embezzled). A receiver only has standing to pursue "embezzlement step" claims. *Id.* There are no allegations of embezzlement here. Indeed, the Receiver trumpets the fact that this was *not* a Ponzi scheme. (Resp. Br. at 17.) Thus, even if Putman was taking kick-backs, he did not embezzle money from the funds. If the Receiver is right, Putman received kick-backs from outsiders in return for

pitching the securities as safe investments used in order to lure investors into adding *more* money to the funds' coffers. As such, the only fraud allegations are "sales step" allegations. Thus, the Receiver does not have standing to pursue "claw-back" claims against the Benders. *See id.*

The Receiver concedes "that none of the counts of the Complaint allege intentional misconduct by Defendants" (Resp. Br. at 7), but argues that if she cannot bring claims against the Benders in this lawsuit, there was no way she could have challenged the payments. That is false. The Receiver *had* options to challenge the payments. She could have filed a Chapter 128 proceeding under the Wisconsin Statutes and brought a state statutory preference claim, or she could have filed for bankruptcy and challenged the transfers as illegal preferences under 11 U.S.C. § 547. Only she knows why, but she did neither. Her time for doing so has expired. However, the Benders do not need to prove the Receiver's motive in choosing her strategy. For the Benders' Motion to succeed, it is sufficient that the Receiver has not cited *any* legal authority that would allow her to pursue these claims. Nor could she: "receivership should not be used as an alternative to bankruptcy," and as such, the Receiver does ***not*** have power to enforce what would amount to a common law "preference." *See, e.g.*, *Eberhard v. Marcu*, 530 F.3d 122, 132 (2d Cir. 2008).

The Benders did not commit a legally cognizable wrong by accepting payments authorized by the Operating Agreement. (*See* Defs.' Mem. of Law Supp. Mot. to Dism. at 4-7, ECF No. 9.)[5] The Receiver does not seriously challenge their interpretation of those provisions, nor does she accuse the Benders of any actual wrongdoing. And she does not offer any authority that would allow her to proceed against the Benders as anything other than relief defendants. Her Complaint should therefore be dismissed.

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[5] Defendants' Memorandum of Law In Support of Their Motion to Dismiss will be referred to as "Br." for the remainder of the Reply.

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B. The Receiver Admits The Benders Are Not Proper Relief Defendants, Meaning She Has No Standing.

The Receiver argues that *Janvey v. Adams*, 588 F.3d 831 (5th Cir. 2009), is inapposite because she has not named the Benders as relief defendants.[6] However, then -- implicitly admitting that she needs a legally cognizable wrong, or to name the Benders as relief defendants -- she unsuccessfully attempts to distinguish *Janvey*. (Resp. Br. at 6-7.) *Janvey* is on point, and demonstrates why, even if she had named the Benders as relief defendants, the Receiver would have no standing to pursue claims for amounts that were paid "***prior to the underlying SEC enforcement action*** . . . ***and the receivership***." *Janvey*, 588 F.3d at 833 (emphasis added).

There is no indication that *Janvey* hinged on whether "the receiver took the easy route." (Resp. Br. at 6.) Moreover, the receiver in *Janvey* did not simply "join[] the investors as relief defendants [and fail to] bring any claims against them." (Resp. Br. at 6.) The receiver *filed separate lawsuits* against the relief defendants (case numbers 09-10761 and 09-10765), and brought claims. Just as the Receiver here is doing, the receiver argued that even though the payments were made pre-receivership, the receiver should nevertheless be allowed to "claw-back" those funds and distribute the proceeds -- which included both principal and interest -- pro rata amongst all of the defrauded investors. *Id.* at 833-34. The court held that the receiver did not have authority to pursue "return of principal" payments that the defendants received. *Id.*

Even though the funds *were* "ill-gotten," the receiver had no authority because he could not show that the defendants lacked a legitimate interest in the "return-of-principal" payments. *Id.* Because a defendant only needs "an 'ownership interest' to preclude [it] from being a proper relief defendant," and because the Investor Defendants received the proceeds through a written agreement with the receivership entity -- meaning a debtor/creditor relationship had been

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[6] Generally speaking, a "relief defendant" did nothing wrong, but may nevertheless "be joined in the lawsuit to aid the recovery of relief." *Janvey*, 588 F.3d at 834. The receiver must plead that the defendant "(1) has received ill-gotten funds, and (2) does not have a legitimate claim to those funds." *Id.* If there is a legitimate claim to the funds, the plaintiff lacks authority to proceed. *Id.*; *CFTC v. Walsh*, 618 F.3d 218, 226 (2d Cir. 2010); *Eberhard*, 530 F.3d at 132-34; *Goodman v. FCC*, 182 F.3d 987, 991-92 (D.C. Cir. 1999).

established before the receivership -- the Investor Defendants could not be "relief defendants." *Id.* at 834-35. As such, the receiver could not pursue a "claw-back" action. *Id.* at 835.

This case is indistinguishable. The Receiver was appointed in the SEC action, and has filed a separate lawsuit to claw-back pre-receivership, "principal only" payments. The Receiver admits that the Benders had a legitimate ownership interest in the payments, and that she cannot name the Benders as relief defendants. (Resp. Br. at 8.) That bars these claims.

Citing *Scholes v. Lehman*, the Receiver argues she has standing. (Resp. Br. at 13-15.) But *Scholes* was a Ponzi scheme case, so its standing analysis has no bearing. In any event, the receiver there was trying to recover from defendants *who had received more money than they paid into the receivership entity* (wrongdoer's ex-wife gave *the company* nothing; investor made $300,000; and charities provided no consideration). 56 F.3d 750, 753, 757-59 (7th Cir. 1995). That is, *Scholes* did not directly address the question in *Janvey* or here -- *i.e.*, whether a receiver has standing to pursue claims against innocent parties for "principal only" payments. And even *Scholes* recognizes that a receiver cannot recover principal. *See id.* at 759 (receiver can only pursue "***the net amount by which the corporations' assets are smaller as a result of the payment to him of his profits***.") (emphasis added).

Scholes is also distinguishable because the receiver was appointed receiver for the wrongdoer and all of the corporations in which the investors invested. Here, Gryphon was initially named as a "relief defendant," meaning the Receiver was inherently adverse to Gryphon: she was planning to pursue claims for *its* funds on WM's behalf. Moreover, *Scholes* involved the wrongdoer "diverting" funds away from the receivership entity for "unauthorized" or "illegal" purposes. As explained above, the Operating Agreement authorized the transfers.

II. THE RECEIVER HAS NO RIGHT TO FUNDS THAT WERE OUT OF GRYPHON'S ACCOUNT PRE-RECEIVERSHIP BECAUSE THE PAYMENTS WERE MADE PURSUANT TO A VALID CONTRACT.

The Receiver boldly claims that even though the Operating Agreement authorized the payments, her authority is not governed by the Operating Agreement. (Resp. Br. at 7.)[7] She cites the Seventh Circuit's decision, but that was only addressing whether investors had contract *claims* against Gryphon, and the holding hinged whether this Court appropriately exercised its discretion *in approving the Receiver's distribution Plan.* The Receiver is not seeking Plan confirmation (*i.e.*, permission on how to distribute money that is still in Gryphon's account). The Receiver is now on the offensive, and is bringing her own claim to recover money that has been out of Gryphon's account since before she was appointed. That means her claim must have some grounding in law or contract. The Receiver argues that her claims are grounded in the Wisconsin Statutes. But even if that were generally true, she fails to cite a case that would allow a receiver to bring back into the receivership estate pre-receivership, "principal only" payments that were authorized by the governing contract's plain terms.

The closest the Receiver comes is citing *Knauer* and *Scholes*, arguing that she can pursue claims that even Gryphon could not pursue, because she is really acting on the investors' behalf. But, *Knauer* holds that a receiver has no standing to pursue "sales step" fraud claims. *Knauer* also explains that, to the extent that a receiver has "extra-statutory" powers, those powers only extend "to the property in [the receiver's] hands . . . ." 348 F.3d at 235-36 (quotation omitted). In any event, the Receiver cites no authority that would allow her to pursue claims that Gryphon's investors could not pursue. Gryphon's investors agreed to be bound by the same

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[7] The Receiver cites two cases, but neither support her position. *SEC v. Wencke*, 622 F.2d 1363 (9th Cir. 1980), dealt with whether the receiver's authority included the authority to stay litigation *against the receivership estate. In re MCGaughey*, 24 F.3d 904 (7th Cir. 1994), dealt with whether to appoint a receiver in a tax collection case.

terms of the Operating Agreement, meaning they would also be barred from challenging "principal only"[8] payments that were made pursuant to the Operating Agreement's plain terms.[9]

As to the voluntary payment doctrine, the Receiver is putting 'the cart before the horse' in claiming her fraud allegation negates it. (Resp. Br. at 11.) The Operating Agreement gave the managing member the discretion to honor the Benders' Redemption Request. Mentioning "fraud" does not make a payment fraudulent. The doctrine prevents a party from making a contract payment and then trumping up fraud claims at a later date. *Putman v. Time Warner Cable of Se. Wis., Ltd. P'ship*, 649 N.W. 2d 626, 631-33 (Wis. 2002); *Total Wall, Inc. v. Wall Solutions Supply, LLC*, No. 09-cv-404-wmc, 2010 U.S. Dist. LEXIS 62283, at *6-7 (W.D. Wis. June 23, 2010). And in any event, the Receiver would have had to have alleged that *the Benders* acted fraudulently to "***induce***[] payment" in order to preclude the Benders from relying on this doctrine. *See Putnam*, 649 N.W.2d at 632 (emphasis added).

The valid contracts between the Benders and Gryphon were executed before the Receiver was appointed.[10] The payments were made pursuant to those contracts, and were received before the Receiver was appointed. Gryphon explicitly acknowledged -- also before the Receiver was appointed -- its contractual obligation: "In accordance with the Operating

[8] Citing *Donell v. Kowell*, 533 F.3d 762 (9th Cir. 2008), the Receiver argues that even if "principal only" payments were required by contract, they could still be voided as fraudulent transfers. (Resp. Br. at 23.) *Donell* actually says that under the UFTA, a receiver can only recover "amounts above [the transferee's] initial investment . . . . Thus, ***the statute . . . allows him to keep the full amount of his original investment*** . . . ." *Id.* at 776 (emphasis added). The Receiver also cites two bankruptcy cases, *In re EBC I, Inc.*, 353 B.R. 631 (Bankr. D. Del. 2006), and *In re Pinto*, 89 B.R. 486 (Bankr. E.D. Pa. 1988), but they are inapposite: they dealt with whether a party could *terminate* a contract with the debtor (and thus deprive the debtor of the contract's value), *not* whether fraudulent conveyance law can void contractually required, "principal only" pre-receivership payments. *EBC*, 356 B.R. at 640; *Pinto*, 89 B.R. at 497-98. Finally, the Receiver cites *CFTC v. Lake Shore Asset Mgmt. Ltd.*, No. 07 C 3598, 2010 WL 960362, at *10 (N.D. Ill. Mar. 15, 2010), and argues that she "may bring [pre-receivership payments] back into the receivership estate . . . ." (Resp. Br. at 23.) *Lake Shore* dealt with plan approval, not a "claw-back" claim. And it did not hold that the receiver could bring pre-receivership payments back into the estate. *Id.* (noting that pre-receivership payment recipients "do not propose that they return their pre-receivership payments so that all of the investors can receive a true proportionate share of their initial investments," but never suggesting they could be forced to.).

[9] The Receiver attempts to distinguish *Javitch*, *Admanco*, *Nick*, *In re All-Star Ins.*, and *Candee*. (Resp. Br. at 9-10.) But her attempt does not explain how the Receiver can undo payments that neither Gryphon nor Gryphon's investors could undo. She also fails to cite a case that would allow her to ignore pre-receivership contracts.

[10] They were also signed before the *post hoc* May 31, 2008 "cutoff," and ***before*** the February 15, 2008 2% letter.

Agreement, an account payable has been created in the Fund financials in your name." (Compl., Ex. B at 11.) Thus, while the Receiver's options differ as to contracts that were *not* fulfilled before her appointment, she cannot pursue "claw-back" claims for obligations that have already been met. *See, e.g., Hays & Co. v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 885 F.2d 1149, 1153 (3d Cir. 1989).

B. The Voidability Rule And The Implied Duty of Good Faith.

The Receiver argues that the Operating Agreement provisions are either void, or precluded by the implied duty of good faith. (Resp. Br. at 12-13.) The Receiver is wrong.

While Wisconsin has a limited voidability rule for contracts that violate the law, the notion that that rule somehow negates terms in a hedge fund's operating agreement is absurd. The Receiver relies on *Solowicz v. Forward Geneva Nat'l, LLC*, 780 N.W.2d 111 (Wis. 2010), but that case provides: "[p]arties also have the freedom to contract as they see fit, which is a well-established principle of law that Wisconsin courts have long recognized." *Id.* at 125. The Receiver also fails to identify what "law" the Operating Agreement supposedly violates. Instead, she relies on her assertion that the terms that all of the investors agreed to somehow violate the law. The Receiver's say-so is not enough to void the Operating Agreement's terms.

As to the implied duty of good faith, the Receiver has not brought a breach of contract claim against the Benders, and the duty of good faith "does not support an independent cause of action for failure to act in good faith under a contract." *See Hauer v. Union State Bank*, 532 N.W.2d 456, 464 (Wis. Ct. App. 1995); *see also Cousins Subs Sys., Inc. v. McKinney*, 59 F. Supp. 2d 816 (E.D. Wis. 1999) (doctrine should not be used to create rights not set forth in the contract). The Receiver fails to cite a case that would allow other investors to rely on Gryphon's actions with the Benders in order to pursue a good faith claim against the Benders. The other case the Receiver relies on, *Cromeens, Holloman, Sibert, Inc. v. AB Volvo*, 349 F.3d 376 (7th Cir. 2003), actually supports the Benders' position. *See id.* at 395-96 ("an implied covenant of

good faith cannot overrule or modify the express terms of a contract."); *M & I Marshall & Ilsley Bank v. Schlueter*, 655 N.W.2d 521, 525 (Wis. Ct. App. 2002) (same).[11]

III. FAILURE TO PLEAD FRAUD WITH SUFFICIENT PARTICULARITY.

The Complaint fails to meet the particularity required by Fed. R. Civ. P. 9(b). The Benders' initial pleading argued that the Receiver failed to meet her 9(b) burden. (Br. at 12-15.) The Receiver responded by re-hashing the allegations in her Complaint. Rather than repeat their initial arguments, the Benders incorporate them by reference here. (*See id.*).

IV. INTENTIONAL FRAUDULENT TRANSFER CLAIM.

A. The Intentional Fraudulent Transfer Claim Is Barred Because The Benders Were Tort Creditors Under The Receiver's Theory.

There cannot have been an intent to hinder, delay, or defraud, because the Benders still have not received all of their principal back. "[I]f a transfer is made for commensurate consideration -- if it is 'fair' in the sense of being one side of an equal exchange -- it is not voidable. For creditors are not disturbed, delayed, hindered, or defrauded if all that happens is the exchange of an existing asset of the debtor for a different asset of equal value." *Scholes*, 56 F.3d at 753. Wis. Stat. § 242.04(2)(h) is in accord.

The Receiver incorporates by reference the SEC's complaint. (Compl. ¶ 8.) And yet, she then proceeds to argue (albeit without support) that the Benders might *not* be tort creditors because this was not a Ponzi scheme and she does not yet have a fraud conviction. (Resp. Br. at 16-17.) This double-speak cannot be countenanced. If there is any doubt in the Receiver's mind as to whether there was fraud, then on what basis is she bringing her fraudulent transfer claims against the Benders? A prerequisite to filing this suit would seem to be an ironclad certainty that there was fraud. If that is in doubt, then the whole house of cards must fall.

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[11] The Receiver also cites *Pottorff*, but that case does not discuss the implied duty of good faith, and in any event, that case would only support the Receiver if the Benders were suing for money in Gryphon's account.

More incredibly, the cases the Receiver relies upon in claiming extraordinary powers *all* involved Ponzi schemes, and it was ***only*** because of the inherently fraudulent nature of a Ponzi scheme that the courts authorized the broad remedies that they did (*e.g.*, relaxing the standing requirements). *See, e.g.*, *Scholes*, 56 F.3d at 753-54. And yet, here, the Receiver's position is that she should have *more* authority than was given in any of those cases *because* this situation did *not* involve a scheme that was as inherently fraudulent as a Ponzi scheme. That position is absurd. This whole argument is an admission that even after two years on the job, and having spent nearly double the amount she is trying to recover from the Benders, the Receiver is still not certain that she will be able to show intentional fraud. This is also an admission that the Receiver cannot meet her heightened pleading requirement under Fed. R. Civ. P. 9(b).

In any event, because the Complaint admits that the Benders are still missing $350,000 from their principal, and because the Receiver's pleadings are admissions that she believes there was fraud, the Benders are tort creditors, meaning the transfers are not voidable. *See Scholes*, 56 F.3d at 753, 755. As such, there was no intent to hinder or delay because, even assuming the Receiver's allegations were correct, the transfer was a trade of an existing asset (75% of the Benders' principal) for a different asset of equal value (release of the Benders' tort claim against Gryphon up to the amount of the principal they received). *See id.* at 753, 755.

Again, this principle is especially important here, because "receivership should not be used as an alternative to bankruptcy," and as such, the Receiver does ***not*** have power to enforce what would amount to a common law "preference." *See, e.g.*, *Eberhard*, 530 F.3d at 132; *B.E.L.T., Inc. v. Wachovia Corp.*, 403 F.3d 474, 478 (7th Cir. 2005); *HBE Leasing Corp. v. Frank*, 48 F.3d 623, 634 (2nd Cir. 1995). The fraud claim should be dismissed.

B. Gryphon's Status As A Relief Defendant Also Precludes These Claims.

Citing *Scholes v. African Enter., Inc.*, 854 F. Supp. 1315 (N.D. Ill. 1994), the Receiver claims that Gryphon's status as a relief defendant does not matter. (Resp. Br. at 17-18.) She

neglects to mention that *none of the receivership entities in that case were relief defendants*. *Id.* at 1317. In *Scholes*, the receiver was a receiver for: (1) the wrongdoer; and (2) the three entities *he* controlled. *Id.* at 1318. The receiver sued charities to recover money that the wrongdoer embezzled from the receivership entities and then gave to the charities. The receiver did not claim that he had been appointed receiver for any of the charities, or for any other relief defendants in whose name the receiver was attempting to bring claims. That shows the Receiver's problem here. The name "relief defendant" inherently creates an adversarial relationship between the receivership entity and the relief defendant: the receiver (on the receivership entity's behalf) will be bringing claims to recoup money from the relief defendant's account. To make *Scholes* on point with this case, then, the receiver there would have had to have: (1) brought claims against the charities; and then (2) brought claims *on behalf of the charities* -- not the receivership entities -- to recover money that the charities paid out to others.

The Receiver has shown no authority that would allow this double leap. WM is the debtor, not Gryphon. The Receiver incorporates by reference the SEC's complaint. The debtor is WM. Gryphon is merely a relief defendant. Wis. Stat. § 242.01(12) defines "transfer" as "every mode . . . of disposing of or parting with an asset or an interest in an asset," and Wis. Stat. § 242.01(2) defines "asset" as "property of a debtor." Therefore, a transfer is only a "transfer" for purposes of fraudulent conveyance law if the *debtor's* property has been transferred. Thus, because WM is the "debtor" in the SEC's complaint, the Receiver can only pursue a claim against the Benders if there was a transfer of *WM's* assets. But, the Complaint alleges that WM caused a transfer of Gryphon's property, not WM's. The Complaint alleges that Gryphon is a creditor of WM. (Compl. ¶ 76.) Nothing in the statute allows the Receiver to have it both ways, or to unwind the transfer of an asset of the creditor, Gryphon.[12]

[12] The Complaint claims that WM "controlled" Gryphon, but it fails to provide any facts sufficient to meet their heightened pleading requirement, and in any event, Wisconsin law has long held that corporations are distinct entities, meaning they are not liable for each others' debts, nor do they have an interest in each other's property.

V. UNJUST ENRICHMENT CLAIM.

Citing only the Complaint, the Receiver argues that the Benders received a benefit. (Resp. Br. at 24.) But the Receiver fails to cite a single case to support her claim that the Benders benefitted by losing money. Without authority, the argument is waived. *See, e.g.*, *Fabriko*, 536 F.3d at 609. In any event, the Receiver is wrong. *See Lawlis v. Thompson*, 405 N.W.2d 317, 320 n.1 (Wis. 1987) ("A loss to the plaintiff without an actual benefit to the defendant is not recoverable as an unjust enrichment."); *B.E.L.T.*, 403 F.3d at 477. The unjust enrichment claim is also barred because the Receiver concedes it cannot go forward if the payments were made pursuant to a valid contract, which, for reasons discussed above, they were. (*See* Resp. Br. at 25); *see, e.g.*, *Arjay Inv. Co. v. Kohlmetz*, 101 N.W.2d 700, 702 (Wis. 1960).

VI. CONSTRUCTIVE FRAUDULENT TRANSFER CLAIM – WIS. STAT. §§ 242.04(1), 242.05(1).

The Receiver claims there was no "reasonably equivalent value," but she only cites cases from outside of this Circuit as support. (Resp. Br. at 21.) Those cases are foreclosed by the Seventh Circuit's analysis in *Scholes*: a defrauded party is a tort creditor, so as long as the party does not receive more than its principal, the transfer was for "reasonably equivalent value." *See* 56 F.3d at 753; *Janvey*, 588 F.3d at 834; *Donell*, 533 F.3d at 772; *B.E.L.T.*, 403 F.3d at 478. According to the Receiver, who incorporated by reference the SEC's Complaint, the investors were defrauded. That means the investors -- including the Benders -- are tort creditors with valid claims, meaning the "principal only" payments cannot be set aside as fraudulent. *See Scholes,* 56 F.3d at 753, 57-58; *Donell*, 533 F.3d at 772.

Citing *Baldi v. Samuel Son & Co.*, 548 F.3d 579 (7th Cir. 2008), the Receiver claims there was insolvency. *Baldi* supports the Benders. The question there was "whether [the entity] was insolvent at the beginning of the transfer period," and the court, rejecting the trustee's apparent attempt to rely on "hindsight," concluded that the entity was *not* insolvent simply because its liabilities exceeded its assets. *Id.* at 581-82. *Baldi* shows the pitfalls in assuming

insolvency based on hindsight alone. *See id.* Hedge funds, like start-ups, require a nuanced approach to the solvency question. Just like the trustee in *Baldi*, the Receiver mistakenly assumes that she can proceed by relying on the fact that Gryphon eventually failed.[13] The Receiver admits that this lawsuit is designed to distribute additional equity to other investors. By definition, then, Gryphon could not have been insolvent because there are no trade creditors who were "hindered, delayed, or defrauded."

VII. UNAUTHORIZED DISTRIBUTIONS CLAIM – WIS. STAT. § 183.0905(3).

The Benders offered three main arguments why the Receiver's unauthorized distribution claim fails. (*See* Br. at 21-23.)[14] Ignoring the Benders' cases, statutes, and principles of statutory construction, and without citing any of her own, the Receiver curiously argues that the Benders "offer no support for any of these arguments . . . ." (Resp. Br. at 25.) The Receiver's word does not make it so. Without offering any *law* to support it, the Receiver concedes that she has no unauthorized distribution claim.[15] Moreover, the Complaint admits that Wis. Stat. § 183.0905(3)'s proportionality requirement only applies "unless otherwise provided in [the] operating agreement." (Compl. ¶ 101.) The distributions were authorized by the Operating Agreement.

VIII. WRONGFUL DISTRIBUTIONS CLAIM – WIS. STAT. § 183.0608.

Citing the plain language of Wis. Stat. § 183.0608(3), the Benders first argued that the statute of limitations for Wis. Stat. § 183.0608 claims is two years. (Br. at 23-24.) The Receiver's response is to assert -- without any law -- that she "has alleged that the limitations period does not bar her action" (Resp. Br. at 28), as though she needs discovery on a question of

[13] It is also worth noting that the admissions in the Complaint bar her insolvency claim. (*See* Br. at 20-21.) The Receiver does not challenge the Benders' argument on this point, so the Benders will not repeat it. (*See id.*)

[14] For brevity's sake, the Benders will not repeat these arguments in full, but the claim fails because: (1) Wis. Stat. § 183.0905 does not explicitly create a cause of action, and Wisconsin does not read a cause of action into statutes; (2) even if Wis. Stat. § 183.0905(3) created *a* cause of action, it only creates a cause of action against Gryphon; and (3) Wis. Stat. § 183.0304 shows that Wis. Stat. § 183.0905 does not create a claim here. (*See* Br. at 21-23.)

law. She then claims the Benders need more than *the statute's plain terms*. (*Id.*) The Receiver offers no law in support; the argument is thus waived. *See Alden*, 527 F.3d at 664. Claims for payments made two years before the Complaint are time-barred. Wis. Stat. § 183.0608(3).

The remainder of the Receiver's wrongful distribution claim is barred because even if the Benders were "members," the payments did not exceed the amount they were entitled to under the Operating Agreement. *See* Wis. Stat. § 183.0608; (Br. at 24.) Without offering any analysis on the relevant portions of the Operating Agreement, the Receiver merely asserts that the payments violated the Operating Agreement. Again, the Receiver's word is not law.[16]

The Receiver cites no authority for her claim that the Benders were "members." Wis. Stat. § 183.0608 only applies to a "member or manager." Under Wis. Stat. § 183.0802, the Benders stopped being "members" of Gryphon when they withdrew (as per terms of the Operating Agreement). Under section 5.3.3, the Benders stopped being "members" *before* they received a payment. Thus, Wis. Stat. § 183.0608 does not apply to them.

IX. AIDING AND ABETTING BREACH OF FIDUCIARY DUTY CLAIM.

Citing *Burbank v. Grease Serv., LLC v. Sokolowski*, 717 N.W.2d 781 (Wis. 2006), the Receiver argues that there is no intent element to an aiding and abetting claim. (Resp. Br. at 29.) However, *Burbank*'s analysis relies on *St. Francis Sav. & Loan Ass'n v. Hearthside Homes, Inc.*, 221 N.W.2d 840 (Wis. 1974). *St. Francis* held that the defendant is not liable unless he or she *intended to cause the wrongdoer's breach. St. Francis*, 221 N.W. 2d at 844 (claim requires an "intention to cause or assist a violation of duty . . . ."). Also, *Burbank* is from 2006. In 2009, the Supreme Court -- citing *Winslow v. Brown*, 371 N.W.2d 417 (Wis. Ct. App. 1985) -- confirmed that there is no claim unless the defendant: "(1) . . . aids another in the commission of an

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[15] The Receiver offers a more robust defense on the dissolution question, but in the interests of brevity, the Benders will stand by the argument in their initial Memorandum. (*See* Br. n.13.)

[16] The Receiver does not address the argument that a payment cannot violate Wis. Stat. § 183.0607 if it is authorized by the Operating Agreement, so the Receiver concedes this point as well. (*See* Br. at 24 n.14.)

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unlawful act; and (2) consciously desires or intends that his conduct will yield such assistance." *Tensfeldt v. Haberman*, 768 N.W.2d 641, ¶ 26 n.12 (Wis. 2009). The naked assertion that the Benders "encouraged" this breach (Compl. ¶ 124) cannot be squared with her admission that "none of the counts of the Complaint allege intentional misconduct by Defendants . . . ." (Resp. Br. at 7.) Thus, the aiding and abetting claim fails. (*See* Br. at 26.)

Moreover, the underlying fiduciary duty is defined by the Operating Agreement. *Gottsacker v. Monnier*, 697 N.W.2d 436, ¶ 29 n.9. The Receiver ignores that and argues that Gryphon violated its fiduciary duty. (Resp. Br. at 30.) But, Gryphon cannot have violated an implied duty by doing what the plain terms of the Operating Agreement gave it permission to do. *See Cromeens*, 349 F.3d at 395-96; *VTR, Inc. v. Goodyear Tire & Rubber Co.*, 303 F. Supp. 773, 778 (S.D.N.Y. 1969). The Operating Agreement gave the managing member sole discretion on redemption requests. (Br. at 5-7.) Thus, the Receiver cannot maintain a breach of an implied duty claim, or a claim against the Benders for "aiding and abetting" that alleged breach.

X. THE *IN PARI DELICTO* DOCTRINE.

Finally, misinterpreting *Knauer* and relying on *Scholes*, the Receiver argues that *in pari delicto* does not bar her claim. (Resp. Br. at 13.)[17] Initially, the Receiver has it backwards: *in pari delicto* is the rule; *Scholes* is the exception. *Knauer*, 348 F.3d at 236. But even if *Scholes* controlled, it is distinguishable. *Scholes*' analysis hinged on the fact that the case involved a Ponzi scheme, not a legitimate investment fund that -- like many -- lost money in the worst economic climate since the Great Depression. In a Ponzi scheme, the court explained, the early distributions were "unauthorized" because the money "should have [instead] been used for the stated purpose of the corporations' sale of interests in the limited partnerships." *Scholes*, 56 F.3d at 754. That is, the wrongdoer should have invested the later investors' money and then paid redemptions based on the actual value of the fund at the time the requests were made, not take

later investors' money and pay it directly to earlier investors. Gryphon was not operating a similar scheme, so *Scholes*' analysis on the equitable *in pari delicto* doctrine does not apply.

In any event, *Knauer*'s (2003) analysis shows the Seventh Circuit's shift from the earlier *Scholes* (1995). The key[18] is that the wrongdoers in *Knauer* controlled JMS and Heartland. That led to the "inescapable conclusion that Heartland and JMS participated in the [fraudulent] scheme and knew of the conversion of Heartland and JMS funds by [the wrongdoers]." 348 F.3d at 233. Thus, the receiver could not proceed because the defendants "derived no benefit," and JMS and Heartland were to blame for the loss. *Id.* at 236. This case is indistinguishable. The Complaint alleges that Putman had sole control over Gryphon and WM. That leads to the "inescapable conclusion that [Gryphon] participated in the allegedly fraudulent scheme and knew of the conversion of [Gryphon] funds by [Putman]." The Receiver admits the Benders did nothing intentionally wrong, so WM and/or Gryphon were to blame for the loss. The Benders have also not benefitted because they are still missing principal.

The receiver in *Knauer* (relying on *Scholes*) attempted the Receiver's argument here. Rejecting it, and affirming the decision on the defendant's 12(b)(6) motion, the court explained:

> The receiver's core argument is that Heartland and JMS should be allowed to pursue claims against the [defendants] because, as a receiver, he is somehow separated from the past crimes of Payne, Danker, Heartland and JMS. While that may be true, the extent of the separation, for purposes of applying standing and *in pari delicto* principles, is an equitable determination. Given the facts here, **we do not see how the fact that Heartland and JMS are represented by a receiver should alone force us to ignore the fact that their nexus to Payne and Danker was far more immediate than that of the [defendants], and deprive the [defendants] of the defense of *in pari delicto*.** The doctrine of *in pari delicto* thus applies to defeat the receiver's claims.

[17] The Receiver lumps her standing discussion in with her *in pari delicto* discussion. They are two separate concepts. As *Knauer* shows, a receiver can have standing, but still lose on *in pari delicto* grounds.

[18] *Knauer*'s facts are complex, but important; the Benders repeat their summary by reference. (Br. at 27.)

Id. at 238 (emphasis added). The equities are even stronger in this case. The defendants in *Knauer* employed -- and therefore had control over -- the wrongdoers. The Benders had *no* control over Putman (or Fevola). Given that, the fact that WM and (arguably) Gryphon are represented by a receiver does not mean the Court must "ignore the fact that [WM's and Gryphon's] nexus to [Putman and Fevola] was far more immediate than that of [the Benders]." *See id.* As such, the Court should not deprive the Benders of the *in pari delicto* defense.

XI. CONCLUSION

For the foregoing reasons, Defendants respectfully request that the Court dismiss the Complaint in its entirety, with prejudice, and award them their costs and attorneys' fees.

Date: May 2, 2011.

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