IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF WISCONSIN

FAYE B. FEINSTEIN, NOT INDIVIDUALLY, BUT AS RECEIVER FOR WML GRYPHON FUND LLC,

Plaintiff,

v.

Case No. 11-CV-00057

DENNIS J. LONG, individually and in his capacity as trustee of the Dennis J. Long & Patricia S. Magnette-Long Joint Revocable Living Trust, Dated 5/14/04, and PATRICIA S. MAGNETTE-LONG,

Defendants.

RECEIVER'S RESPONSE IN OPPOSITION TO DEFENDANTS' MOTION TO DISMISS

Plaintiff, Faye B. Feinstein (the "Receiver"), not individually, but as receiver for WML Gryphon Fund LLC, a Wisconsin limited liability company ("Gryphon"), by her attorneys, hereby responds in opposition to Defendants' *Motion to Dismiss Pursuant to Federal Rules of Civil Procedure 9(b), and 12(b)(6)* (Docket No. 6) (the "Motion") and Defendants' *Memorandum of Law* in support of their Motion (Docket No. 7) (cited herein as "Defs. Mem.").

INTRODUCTION

Investors in Gryphon have suffered staggering losses. Remaining investments in Gryphon at the time of the Receiver's appointment in May of 2009 totaled slightly more than $36 million. To date, the Receiver has distributed just over $1.9 million to Gryphon investors. Although she expects to make at least one additional distribution, and possibly others, she nonetheless expects recoveries to be *de minimis* compared to the dollars invested. In accordance with the Receiver's Court-approved plan for the allocation of the assets of the receivership estates (the "Plan") (Case No. 09-cv-506, "Receivership Docket" No. 163), the Receiver's first distribution enabled investors in Gryphon to receive approximately ***8.039% of their net investments***.[1]

The Dennis J. Long & Patricia S. Magnette-Long Joint Revocable Living Trust, Dated 5/14/04 (the "Trust"), invested a total of approximately $4.99 million in Gryphon. Prior to the Receiver's appointment, the Trust received distributions totaling approximately ***$5.3 million, or over 106% of its investment***, making it the *only* investor involved in the receiverships of any of the six Wealth Management funds to have received a profit on its investment. More than 79% of the Trust's investment was returned to it *after* February of 2008, when the fund's managing member, Wealth Management LLC ("WM"), informed investors of serious liquidity concerns, which led to cessation of distributions to all except three preferred investors. From March of 2008 through April of 2009, the Trust received a total of $4,194,253.63 from Gryphon (the "Transfers"). These Transfers alone total more than ***twice*** the total distributions made by the Receiver to date to the remaining 98 Gryphon investors combined. The claim that Defendants are nonetheless "victims" (Defs. Mem. at 17) mocks the scores of Gryphon investors who will never again see most of the money they invested with WM.

The Receiver has brought three lawsuits[2], seeking the return of pre-receivership distributions in the total amount of $5,761,705.56, made to investors who, the Receiver has claimed, received preferred treatment from Gryphon by and through WM. The Receiver alleges that WM, through its principals, back-dated the effective date of these investors' redemption requests, thereby allowing them to jump to the head of the line and receive the lion's share of any funds that Gryphon received from the liquidation of its portfolio investments. The Receiver

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[1] Total cash invested less distributions received prior to May 31, 2008.

[2] One of those suits (Case No. 11-cv-00060) has been settled and dismissed. The captioned action and Case No. 11-cv-00058 remain pending.

is seeking return of those payments in order to equitably distribute the proceeds to all Gryphon investors.

Defendants claim, among other arguments, that they were entitled to be paid first, because once their redemption request had been accepted (albeit retroactive to a date before Defendants actually submitted it), Defendants became "creditors" of Gryphon, and the terms of Gryphon's operating agreement required that they receive distribution on their investments before any non-redeeming investor could receive payment. However, the Seventh Circuit, in affirming this Court's order approving the Plan (Receivership Docket No. 161) (the "Approval Order"), found that affording redeeming investors priority over non-redeeming investors "would impermissibly elevate form over substance", and that "where investors' assets are commingled and recoverable assets …are insufficient to fully repay the investors, 'equality is equity'". *SEC v. Wealth Mgmt. LLC*, 628 F.3d 323, 333 (7th Cir. 2010). The Seventh Circuit went on to confirm "the inequity of giving some investors preference even though all investors' claims were substantially the same". *Id.* at 334. Finally, the Seventh Circuit found that no investor was entitled to priority distribution of Gryphon's limited funds and none were, in that sense, "creditors" under Wisconsin law. *Id.* at 335. The Seventh Circuit thereby affirmed this Court's finding that "*no member was 'entitled to receive a distribution' at the time the requests were made*" and that "*none of the investors* who made requests for redemption *would be considered creditors under the applicable state law*". Approval Order at 8 (emphasis added).

The Receiver seeks the return of millions of dollars distributed from Gryphon solely for Defendants' benefit, at a time when, the Court has held, no investor had a right to priority treatment. As was the case in *Scholes v. Lehmann*, 56 F.3d 750 (7th Cir. 1995), Gryphon could not prevent the dissipation of its assets, controlled as it was by WM through WM's principals, James Putman and Simone Fevola. Appointment of the Receiver provided the mechanism for challenging transfers that otherwise could not be challenged, in order to remedy the harm suffered by Gryphon's other members. *See id.*

Defendants cry that the Receiver's action is an unprecedented assault on capitalism itself: "the Receiver [if successful] will do significant damage to the ability to use limited liability companies for economic development and capital formation" (Defs. Mem. at 1), and she threatens the "fundamental underpinnings of corporate law in Wisconsin" (*id.* at 3). In fact, the Receiver's Complaint is far from novel. Rooted as it is in long-standing legal principles of fraudulent conveyance, abuse of discretion, breach of fiduciary duty, and unjust enrichment, the Complaint embodies the same principle established by the United States Supreme Court nearly 90 years ago and reaffirmed by the Seventh Circuit: among investors in an insolvent fund, "equality is equity." *Cunningham v. Brown*, 265 U.S. 1, 13 (1924) (cited in *Wealth Mgmt.*, 628 F.3d at 333). Transfers of property that violate these principles, even if made under the guise of legal agreements, are routinely challenged by receivers and trustees under the same legal theories alleged by the Receiver in her Complaint.

The Receiver's Complaint alleges facts that, if assumed true (as they must be at this stage), permit this Court to reasonably infer that Defendants are liable for disgorgement of the Transfers. For the reasons further explained below, the Motion should be denied.

ARGUMENT

I. Legal Standard

A. Defendants Inappropriately Contest the Complaint's Factual Allegations and Misinterpret Prior Decisions in the Underlying Receivership Proceeding.[3]

Defendants may not seek dismissal of the Complaint on the ground that they contest factual allegations made in the Complaint or that they believe different or additional facts are pertinent. Contradictory or additional factual allegations may be appropriately considered in asserting affirmative defenses, but not on a motion to dismiss. In considering Defendants' Motion, this Court must assume that all of the factual allegations in the Complaint are true, "even if doubtful in fact." *Bell Atlantic Corp. v. Twombly*, 550 U.S. 440, 555 (2007). The Court should, therefore, disregard all of Defendants' factual assertions that are outside of the Complaint or a document referred to in the Complaint, and any conclusions Defendants draw from the documents attached to the Stippich Declaration, which have been interposed for the improper purpose of detracting from, contesting, or defending against the Receiver's factual allegations. Non-exclusive examples of material not appropriate for a motion to dismiss include: (i) the assertion that, as of February 9, 2008, "there was no indication of any losses on . . . other investments, which constituted 75% of the portfolio" (Defs. Mem. at 5); (ii) statements regarding the Defendants' *perception* of Gryphon's "intentions" (*id.*), and (iii) Defendants' *opinions* as to whether Gryphon's portfolio investments were "stable" or had realized a gain (*id.*).

Furthermore, Defendants take language from the Approval Order and the Seventh Circuit's affirming opinion so out of context as to effectively re-write them. For example,

[3] Defendants relegate to a footnote the argument that the Court may consider the declaration of their counsel and documents attached thereto, without converting their motion to dismiss to one for summary judgment. (Defs. Mem. at 4 n.1.) If this Court does determine to treat the Motion as one for summary judgment, the Receiver requests that she be authorized to resubmit this Response, so that she may have a "reasonable opportunity to present all the material that is pertinent" to such a motion and to her opposition thereto. Fed. R. Civ. P. 12(d).

Defendants ask the Court to believe that the Seventh Circuit "*implicitly held* that investors with redemption requests accepted prior to February 2008 were . . . *creditors* of Gryphon [*i.e.*, in the sense of having a priority right to distributions of Gryphon's assets] for the full amount of the accepted redemption" (*id.* at 22) (emphasis added). Defendants thereby suggest that the court's opinion endorsed Defendants' receipt of their entire equity interest, plus hundreds of thousands of dollars more, while virtually all other investors received far less.

Nowhere does the Seventh Circuit find that Defendants, or any other investors, were entitled to priority distributions while there were liquidity concerns. The Seventh Circuit concurred with this Court that so long as there were insufficient funds to fully satisfy all investors' rights to repayment of their equity, no one was entitled to receive a distribution in excess of limitations imposed by WM. The Seventh Circuit did not address whether WM had appropriately exercised its discretion when, on the eve of imposing those limitations, it back-dated Defendants' redemption request so as to free them from those limitations and allow them to receive a preferred return on their equity to the detriment of other investors.

Defendants also assert that this Court has held that "it is equitable for early redeemers to receive *priority* distributions . . . ." (Defs. Mem. at 11 (emphasis added).) In support, they take out of context language from the Approval Order which, they allege, approves "rewarding" their "diligence" in "pulling their money out early." (Defs. Mem. at 11-12, *citing* Approval Order at 11.) The Court made that observation in approving the Receiver's decision to offset against receivership distributions only those payments received by investors after May 31, 2008. This Court did not condone as "diligence" the decision to back-date the effective time of a redemption request in order to insure that only certain preferred investors were able to "pull their money out early."

B. The Seventh Circuit Uses a "Plausibility" Standard to Determine Whether a Complaint States a Claim.

Federal courts, including the Seventh Circuit, operate "on a notice pleading standard; *Twombly* and its progeny do not change this fact." *Bissessur v. Ind. Univ. Bd. of Trustees*, 581 F.3d 599, 603 (7th Cir. 2009). To survive a motion to dismiss under Fed. R. Civ. P. 12(b)(6), "detailed factual allegations are not required." *Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1951 (2009) (citing *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555 (2007)). A plaintiff must merely plead "sufficient factual matter, accepted as true, to state a claim to relief that is plausible on its face." *Iqbal*, 129 S. Ct. at 1951. A claim has facial plausibility "when the plaintiff pleads factual content that allows the court to draw a *reasonable inference* that the defendant is liable for the misconduct alleged." *Id.* at 1949 (emphasis added). The court gives the plaintiff "the benefit of imagination, so long as the hypotheses are consistent with the complaint." *Bissessur*, 581 F.3d at 602. "[A]ll reasonable inferences [are to be viewed] in the light most favorable to the plaintiff." *Knauer v. Jonathon Roberts Fin. Group, Inc.,* 348 F.3d 230, 231 (7th Cir. 2003).

For the reasons set forth below, the Complaint's detailed allegations provide "fair notice of what [each] claim is and the grounds on which it rests." *Bissessur*, 581 F.3d at 603. Those allegations are more than sufficient to permit this Court to draw reasonable inferences of Defendants' liability as to each Count.

II. <u>The Provisions of the Operating Agreement Do Not Bar the Receiver's Claims</u>.

A. The Receiver is Not Bound by the Terms of the Operating Agreement.

Defendants argue that the Receiver is bound by the provisions of Gryphon's operating agreement (the "Operating Agreement"), and, since Gryphon could not challenge the Transfers thereunder, the Receiver is precluded from doing so. Defendants claim that the Receiver's authority "is governed by state law and constrained by the order" of appointment. (Defs. Mem.

at 13.) In fact, as a receiver appointed by a federal court, the Receiver's authority derives not from state law, but from "the inherent power of a court of equity to fashion effective relief". *SEC v. Wencke,* 622 F.2d 1363, 1369 (9th Cir. 1980); *accord In re McGaughey,* 24 F.3d 904, 907 (7th Cir. 1994).

Defendants do not suggest that the Receiver is acting outside the order of appointment; instead, they argue that, having stepped into Gryphon's shoes, she is bound by the Gryphon Operating Agreement entered into pre-receivership. However, "[t]he rule that a receiver stands precisely in the shoes of the corporation is . . . 'subject to the exception that the receiver so far represents the general creditors that he may avoid transactions in fraud of their rights'". *Knauer v. Jonathon Roberts Fin. Group,* 348 F.3d 230, 236 (7th Cir. 2003) (citing *Scholes v. Lehmann,* 56 F.3d 750 (7th Cir. 1995), as an "example of the application of such an exception"). Here, the Receiver is doing just that: seeking to avoid and recover the Transfers for the benefit of all equity holders.

None of the cases cited by Defendants involves challenges by a receiver to pre-receivership transfers to investors; instead, each of the cited cases arose in the context of a receiver seeking to *enforce* or determine the validity of a pre-receivership agreement, or obtain damages thereunder, and each is therefore inapposite. *See, e.g.*, *Javitch v. First Union Secs., Inc.,* 315 F.3d 619 (6th Cir. 2003) (receiver seeking to recover damages under pre-receivership contract from third party brokers, who were not the recipients of transfers from the receivership entities, was bound by arbitration agreement entered into with broker defendants); *Nick v. Holtz,* 297 N.W. 387 (Wis. 1941) (upon action by receiver seeking determination of validity of chattel mortgage, court upheld determination of lower court that mortgage was valid and enforceable against property of the receivership); *In re All-Star Ins. Corp.,* 332 N.W.2d 828 (Wis. Ct. App.

1983) (receiver of insurance company under state court insurance liquidation proceeding seeking to recover monies allegedly due to insurance company under pre-receivership contracts was bound to remedies afforded by the terms of those same contracts); *Admanco, Inc. v. 700 Stanton Drive, LLC*, 786 N.W.2d 759 (Wis. 2010) (Wisconsin statutory receiver in action to enforce pre-receivership lease and recoup proceeds of letter of credit was bound by the terms of those agreements); *Lank v. New York Stock Exchange,* 548 F.2d 61 (2d Cir. 1977) (receiver appointed for former member of national securities exchange found not to have standing to bring private cause of action seeking to enforce violations of the Securities Exchange Act). Ironically, the court in *Lank* noted that, if the receiver had sought to maximize the pool of assets out of which claims could be satisfied, he could bring actions for fraudulent conveyance, even though the corporation could not.

Defendants' reliance on the "voluntary payment doctrine" is equally inapposite (Defs. Mem. at 15). The two cases cited by Defendants involve parties who voluntarily performed under their contracts and then challenged the validity or legality of their payments. *See Burgess v. Commercial Nat. Bank of Appleton*, 128 N.W. 436 (Wis. 1910) (a promissory note); *Putnam v. Time Warner Cable of Se. Wis., Ltd. P'ship*, 649 N.W.2d 626 (Wis. 2002) (a cable television agreement). Neither involves a receiver seeking to avoid fraudulent transfers made pre-receivership that inequitably preferred the transferees. In fact, in *Burgess*, the court specifically found that there were no allegations of fraud to change the result. "The voluntary payment doctrine provides that . . . 'money paid voluntarily, . . . *and without fraud* . . . cannot be recovered merely on account of ignorance or mistake of the law'". *Putnam,* 649 N.W.2d at 632 (emphasis added). The Receiver's allegations of fraud distinguish this case from those relied upon by Defendants.

Defendants inappropriately rely on this Court's findings regarding the status of pre-receivership agreements entered into by the WM Funds with third-party investment vehicles, *i.e.*, the Brown Investment Fund, L.P ("Brown") (Defs. Mem. at 13). The Court did determine that in attempting to enforce Gryphon's rights as an investor in Brown, the Receiver has only the rights Gryphon had as a limited partner in Brown. However, as "an officer of the Court," her duty to recover avoidable transfers made by the receivership entities is not defined by the Gryphon Operating Agreement; her "duties . . . are outlined in the First Modified Order Appointing Receiver", and her appointment "supplant[ed] the operating or partnership agreements of the WM [F]unds." *SEC v. Wealth Mgmt. LLC,* No. 09-C-506, 2009 WL 3765395, at *3 (E.D. Wis. Nov. 9, 2009).

Here, the Receiver is not seeking to enforce, or obtain the benefits of, or extricate herself from, a pre-receivership contract. To the contrary, she has alleged that to the extent the Transfers were made under the guise of compliance with the Operating Agreement, the Operating Agreement cannot be enforced, and the Transfers should be avoided.

B. If the Discretionary Provisions of the Operating Agreement Authorized WM to Effect Fraudulent Transfers, Those Provisions are Voidable as Against Public Policy.

Contract terms will not be enforced if they contravene public policy. *See Solowicz v. Forward Geneva Nat'l, LLC*, 780 N.W.2d 111, 126 (Wis. 2010); *Watts v. Watts*, 405 N.W.2d 303, 309-10 (Wis. 1987). A contract term contravenes public policy if it allows a party to violate the law. *See Abbott v. Marker*, 722 N.W.2d 162, 165-67 (Wis. 2006) (referral agreements between an attorney and non-attorney are void, both because they contravene the law and because they harm society).

Defendants rely on various sections of the Operating Agreement to suggest that these contract terms gave WM complete "discretion" to back-date Defendants' redemption request and breach its fiduciary duty to treat all Gryphon members equitably. The Receiver is not bound by actions taken by WM in reliance on the terms of the Operating Agreement to the extent it afforded WM "discretion" to violate the law. To the contrary, WM could not make fraudulent or otherwise inequitable or illegal transfers under the guise of absolute discretion. *See Abbott*, 722 N.W.2d at 165-66 (invalidating contract terms that violate the law and thus contravene public policy).

Further, the Receiver disputes Defendants' interpretation that the Operating Agreement effectively authorized WM to back-date redemption requests in order to prefer some investors over others. This dispute is not properly resolved on a motion to dismiss.

C. The Covenant of Good Faith and Fair Dealing Precluded WM From Using its Discretion to Prefer Defendants to the Detriment of Remaining Investors.

"Every contract implies good faith and fair dealing between the parties to it,"; "compliance" in form only, but not in substance, breaches that covenant. *Bozzacchi v. O'Malley*, 566 N.W.2d 494, 495 (Wis. Ct. App. 1997) (internal quotations marks and citation omitted). If one party is granted broad discretion to perform, then it must act reasonably and not arbitrarily. *See, e.g.*, *Cromeens, Holloman, Sibert, Inc. v. Ab Volvo*, 349 F.3d 376, 395 (7th Cir. 2003).

WM breached its duty of good faith and fair dealing to the extent it relied on its discretion to back-date the effective time of Defendants' redemption request. The terms of the Operating Agreement required WM to use its discretion in good faith, reasonably, and not arbitrarily. *See id.* But, WM did precisely the opposite, by providing special treatment to the redemption request of a friend and business associate of James Putman (who controlled WM), ultimately rewarding Defendants with 106.5% of their aggregate investment, while virtually all of Gryphon's other investors received only a fraction of their investments, if that. (Compl., ¶63.) The Receiver is duty-bound to take steps to set aside those transactions. *See Texas & Pac. Ry. Co. v. Pottorff*, 291 U.S. 245, 251 (1934).

III. The Receiver Has Standing to Assert Her Claims on Behalf of Gryphon, and Her Complaint Is Not Barred by the Doctrine of *In Pari Delicto*.

Defendants seek to bar the Receiver's Complaint under the doctrine of *in pari delicto*, on the ground that WM and Gryphon "were the only ones at fault" for investor losses, and that Defendants did nothing wrong except failing to object to WM's decision to back-date their redemption request. (Defs. Mem. at 18.) Defendants urge application of the doctrine by contrasting *Scholes v. Lehmann,* 56 F.3d 750 (7th Cir. 1995), with *Knauer v. Jonathon Roberts Fin. Group, Inc.,* 348 F.3d 230 (7th Cir. 2003), and ask this Court to apply the holding in *Knauer* to facts that actually mirror those in *Scholes*. In fact, *Knauer* acknowledges that, under *Scholes*, the doctrine of *in pari delicto does not bar* "actions brought by corporate receivers, even where the receivership entities were complicit in illegal activities," against defendants who *directly benefitted* from the fraudulent transfers, so long as the complicit party *will not benefit* from its own wrongdoing. *Knauer,* 348 F.3d at 235.

Key to the court's analysis of standing in *Scholes* was that the transferor-corporations were "separate legal entities with rights and duties" apart from the person who controlled them (a man named Douglas) and who had caused them to transfer money to, among others, "an investor . . . whom [the controlling person] wanted to keep happy". *Scholes*, 56 F.3d at 754. The court recognized that the transferor-corporations, as the "robotic tools" of Douglas, had themselves sustained harm from the dissipation of their assets. *Id.* As the court noted, ordinarily, those transferor-corporations, as "the maker[s] of the fraudulent conveyance . . . are bound by it." *Scholes*, 56 F.3d at 754. However, once the receiver took control from Douglas, he "removed the wrongdoer from the scene" and had standing to sue the transferees, on behalf of those corporations, to redress the harm done to them and to seek "return of the moneys – for the benefit not of Douglas but of innocent investors . . . ." *Id.* (citing *McCandless v. Furlaud*, 296 U.S. 140 (1935), and *Texas & Pac. Ry. Co. v. Pottorff*, 291 U.S. 245 (1934)). That the receiver's lawsuits might ultimately benefit investors did not affect the receiver's standing; it was merely a consequence of the fact that "help[ing] a corporation helps those who have claims against its assets." *Id.* In *Knauer*, the Seventh Circuit reaffirmed the key holding of *Scholes*: "[a]s long as an entity is legally distinct from the person who diverted funds from the entity, a receiver for the entity has standing to recover the removed funds," although the person in control of the transferor had the authority *or discretion to authorize the transfer* at the time it was made. *Knauer*, 348 F.3d at 235 (citing *Scholes*).

The allegations of the Complaint fit comfortably into the mold of *Scholes*. Putman founded and controlled WM, and WM was the sole managing member, with control over Gryphon. (Compl., ¶¶3, 24, 33). Based on an agreement between WM and Defendants to treat Defendants' January 2008 redemption request as though it had been submitted, accepted, and become effective during the last quarter of 2007, WM caused Gryphon to funnel millions of dollars of assets to the Defendants, at times when WM had otherwise caused Gryphon to limit or suspend distributions to virtually all other investors (Compl., ¶¶51-63). The Transfers damaged Gryphon by rendering it unable to satisfy its obligations to its investor body as a whole (*see, e.g.*, Compl., ¶¶80-84). Now that Gryphon is free of the control of WM and Putman, the Receiver seeks to remedy the injury to Gryphon by recovering the Transfers from Defendants and redistributing those funds for the ultimate benefit of Gryphon's investors, according to their equitable entitlements under the Plan (*see, e.g.*, Compl., ¶¶82, 91, 105).

Conversely, the receiver in *Knauer* had sued five broker-dealers, whose alleged negligence had purportedly contributed to their agents' ability to use the receivership entities to commit an investment fraud. However, those defendants had not themselves benefitted from any fraudulently obtained funds. The *Knauer* court held that defendants who had received no benefit from the underlying fraud, but were allegedly partly to blame for it, could defend against the complaint on the ground that the entities in receivership had been complicit in the same wrongdoing. *Id.* at 236.

The *Knauer* court distinguished *Scholes* on the ground that the receiver in *Scholes* was, in fact, "seeking to recover the diverted funds from the beneficiaries of the diversions (e.g., the recipients of [the] transfers)." *Id.* Correspondingly, the court found that "[i]f the case before us involved the voiding of a fraudulent conveyance, as in *Scholes* . . . *we would likely apply Scholes*" and the exception in favor of the receiver. *Id*. (emphasis added). Analogously, the Receiver in this action seeks to recover the Transfers directly from Defendants who received the benefit.

IV. <u>Counts I and III State Viable Claims for Recovery of Fraudulent Transfers</u>.

A. A Federal Receiver Has Standing to Bring Fraudulent Conveyance Actions that Pre-Receivership Entities Could Not Bring Themselves.

Defendants mistakenly rely on the assumption that the Receiver's authority is constrained and governed by state law. (Defs. Mem. at 13). However, the "power of a district court to impose a receivership . . . derives from the inherent power of a court of equity to fashion effective relief" (*SEC v. Wencke*, 622 F.2d 1363, 1369 (9th Cir. 1980)), a proposition with which the Seventh Circuit agrees. *In re McGaughey*, 24 F.3d 904, 907 (7th Cir. 1994). The Receiver's authority derives, in turn, from this Court's appointment order, which conferred upon her, among other things, "control of all funds, assets . . . *choses in action* . . . and other property of WM and the WM Funds" (*First Modified Order Appointing Receiver* (Case No. 09-CV-506, Docket No. 14) at 3 (emphasis added); Compl., ¶12) along with the authority to implement "the equitable distribution of WM Funds' assets to their investors" (*id.* at 4; Compl., ¶12).

The assumption underlying Defendants' objection to the Receiver's standing is, therefore, incorrect: a receiver's authority to act on behalf of a receivership estate does, indeed, exceed the power that the pre-receivership entity had to act for itself. That authority includes the "power at the instance of the receiver" to bring back into the receivership estate "moneys fraudulently diverted to the prejudice of creditors." *McCandless v. Furlaud*, 296 U.S. 140, 160-61 (1935). In fact, "[i]t is the duty of the receiver of an insolvent corporation to take steps to set aside transactions which fraudulently or illegally reduce the assets available" for the receivership estate, "*even though the corporation itself was not in a position to do so*." *Texas & Pac. Ry. Co. v. Pottorff*, 291 U.S. 245, 260-61 (1934) (emphasis added).

Defendants insist that the Receiver "asserts a claim on behalf of Gryphon, as a purported creditor of WM, the alleged debtor who made the transfers to the Trust", and allege that in order to state a claim for fraudulent conveyance, the Receiver must establish "(1) that Gryphon is a 'creditor' (2) of a 'debtor' and (3) the debtor has made a transfer of the debtor's assets (4) that is fraudulent as to Gryphon". (Defs. Mem. at 19.) Defendants ask how WM could be the "debtor" for purposes of Wisconsin's fraudulent transfer statutes, if it did not transfer its own assets. (*Id.* 20). The defendants in *Scholes* unsuccessfully made the same argument.

The district court in *Scholes* described the person who had controlled the entities then in receivership (Douglas) as the *transferor* of the receivership entities' funds, which he had caused those entities to pay to (among others) a favored investor. *Scholes v. African Enter., Inc.*, 854 F. Supp. 1315, 1325 (N.D. Ill. 1994). At the same time, however, the district court made clear that the assets Douglas had transferred were *not* legitimately *his property*. *Id.* But, for purposes of the receiver's fraudulent transfer claims, *he was the debtor* who had fraudulently transferred the property of the receivership entities because he effectively treated that entity as his instrument, and its property as his own.

Similarly, the Receiver does not allege, nor need she allege, that WM transferred its own assets; she alleges that WM, the managing member in control of Gryphon, caused Gryphon to fraudulently transfer its assets, under circumstances that injured Gryphon by leaving it unable to equitably distribute its assets to all investors. (Compl., ¶¶77-86.) Like Douglas in the *Scholes* cases, WM (acting through James Putman) treated Gryphon as its instrument, and Gryphon's property as its own, and caused Gryphon to transfer its assets to Defendants. WM is, therefore, in the position of the "debtor" for fraudulent conveyance recovery purposes, and the Receiver, acting on behalf of Gryphon, is the "creditor" injured by WM's actions.

Defendants also argue that "Gryphon cannot be both the creditor bringing the claim and the debtor whose assets have been transferred." (Defs. Mem. at 20.) The defendants in *Scholes* also argued that the entities that made the fraudulent transfers could not then claim to recover them. *Scholes* 56 F.3d at 754. However, the district court and Seventh Circuit held in the *Scholes* cases that a *receiver* for such entities can do just that.

On appeal, the Seventh Circuit in *Scholes* focused on the fact that the injured receivership corporations – as separate legal entities, but under Douglas's control – directly transferred assets to the defendants. The receiver was found to have standing to recover the transfers made by the pre-receivership corporations for equitable distribution to all investors. *Scholes*, 56 F.3d at 754. Although the receiver was, nominally, on both sides of the fraudulent transfer, *i.e.*, representing the corporate entities as transferor(s) and as the parties contesting those transfers (the postreceivership entities), the crucial issue was who controlled them at the time of the transfers, and for what purpose. With Douglas's former "zombies" now "controlled by a receiver whose only object is to maximize the value of the corporations for the benefit of their investors and any creditors, we cannot see an objection to the receiver's bringing suit to recover corporate assets unlawfully dissipated . . . ." *Id.* at 755 (*citing McCandless*, 296 U.S. at 160). Similarly, Gryphon may now, by and through the Receiver, seek recovery of transfers which Gryphon made pre-receivership, when it was acting under the control of WM.

B. Counts I and III Meet or Exceed the Requirements of Fed. R. Civ. P. 9(b).

Under Fed. R Civ. P. 9(b), in alleging fraud, "states of mind may be pleaded generally", *DiLeo v. Ernst & Young*, 901 F.2d 624, 627 (7th Cir. 1990), but the allegations must "sufficiently detail[] the circumstances" surrounding the fraud, by describing the "who, what, when, where, and how" of the matter, *Gen. Elec. Capital Corp. v. Lease Resolution Corp.*, 128 F.3d 1074, 1079 (7th Cir. 1997). However, Fed. R. Civ. P. 9(b) still contemplates the same "simplicity and brevity" as do the other Federal Rules of Civil Procedure. *Id.* at 1079 (quoting Fed. R. Civ. P. 84).

The Complaint explains, step by step, (a) Defendants' disputes with WM and Putman and their demands for reimbursement and for the return of all of their invested funds (*id.* at ¶¶33-40); (b) WM's February 2008 proposal to treat Defendants' full redemption request of a month earlier as though it had been submitted, accepted, and become effective during the last quarter of 2007 and the contrary position taken by WM with respect to virtually all other investors (Compl., ¶¶41-53); (c) Defendants' active consideration and acceptance of that proposal (Compl., ¶46), and (d) how, based on the back-dated redemption request, WM caused Gryphon to funnel millions of dollars to Defendants, at times when WM had otherwise caused Gryphon to limit or suspend distributions to virtually all other investors (Compl., ¶¶51-63). The Complaint cites to specific communications regarding these events among Defendants and WM, which were made of public record, under penalty of perjury, by Defendant Dennis Long himself (Compl., ¶32). Finally, the Complaint describes the nature of the harm to Gryphon and how the requested relief will remedy that harm (Compl., ¶¶82, 83, 91).

The Complaint further alleges, as to Count I, that WM and, therefore, its instrument, Gryphon, knew or should reasonably have known that effecting the transfers described in the Complaint would act to hinder, delay, or defraud Gryphon's investors. (Compl., ¶85-86). Because actual fraudulent intent under Wisconsin's fraudulent transfer statute may be inferred from the existence of certain "badges of fraud," the Complaint (*id.* at ¶87) also identifies the circumstances that constitute those "badges" that give rise to that inference. *See* Wis. Stat. §§242.04(2)(a)-(k); *Freeland v. Enodis Corp.*, 540 F.3d 721, 733 (7th Cir. 2008) (presence of "badges of fraud" creates presumption of transferor's intent to hinder, delay, or defraud (under Indiana's adoption of Uniform Fraudulent Transfer Act, which is identical in all material respects to the Wisconsin statute)).

The factual allegations described above also support Count III (constructive fraudulent conveyance). The remaining elements necessary to Count III are (a) Gryphon's failure to receive reasonably equivalent value in exchange for the $4.2 million it transferred to Defendants, and (b) either (i) the Transfers left Gryphon with assets unreasonably small to continue its business of investing in managed funds and securities (Compl., ¶64) or (ii) Gryphon was insolvent at the times of the Transfers or was rendered insolvent by the Transfers.

As to "reasonably equivalent value," the Complaint alleges that Defendants received the Transfers on account of their equity interests in Gryphon (*see, e.g.*, Compl., ¶¶1, 38). As a matter of law, equity redemptions are merely a distribution of an entity's assets, not an exchange for value. *See, e.g.*, *Buncher Co. v. Official Comm. of Genfarm*, 229 F.3d 245, 252 (3d Cir. 2000) (stock redemptions are treated as dividends to shareholders which return no value to company); *In re Roco Corp.*, 701 F.2d 978, 982 (1st Cir. 1983) (same). Alternatively, the Complaint exposes the gulf between the amounts WM caused Gryphon to pay to Defendants during the 14 months between March 2008 and April 2009 and the value of Defendants' equity interest in Gryphon during that period (Compl., ¶¶54-63). In either case, the Complaint permits the inference that the Transfers were made for less than reasonably equivalent value from Defendants, and further analysis is not appropriate on a motion to dismiss.

The Approval Order has foreclosed Defendants' argument that the full $4.2 million of Transfers were payments on account of an "antecedent debt." (Defs. Mem. at 21-22.) Defendants assume that they enjoyed the priority rights to Gryphon's assets of an unsecured creditor. As noted above, this Court has determined that no investor was entitled to preference as a "creditor" because "all investors' claims were substantively the same." *Wealth Mgmt.*, 628 F.3d at 334.

The Complaint details the financial straits of Gryphon during the period of the Transfers and, in particular, the decline of its two largest portfolio investments, resulting in a substantial write-down and re-valuation of those assets (Compl., ¶¶64-76.) The Complaint describes WM's suspension of redemptions, the termination of Gryphon's investment business, and WM's acknowledgment that Gryphon could not then satisfy redemption requests. (Compl., ¶¶48-52.) Assuming these allegations to be true, they permit the reasonable inference that Gryphon had insufficient assets with which to conduct its investment business and/or was insolvent for the entire period during which the Transfers were made. *See, e.g.*, *Baldi v. Samuel Son & Co., Ltd.*, 548 F.3d 579, 581 (7th Cir. 2008) (showing of entity's insolvency at beginning and end of a period justifies assumption that entity was insolvent at any given point within that period).

Finally, "scienter" is not an element of intentional or constructive fraudulent transfer claims under Wisconsin's enactment of the Uniform Fraudulent Transfer Act, Wis. Stat. §§242.01 *et seq.* ("WFTA"). Defendants' authorities (Defs. Mem. at 12) deal with issues far afield from fraudulent transfer claims and are inapplicable. *See Tricontinental Indus., Ltd. v. PricewaterhouseCoopers LLP*, 475 F.3d 824 (7th Cir. 2007) (claims for securities fraud, negligence, misrepresentation, and common law fraud against accountants); *United States ex rel. Gross v. AIDS Research Alliance-Chicago*, 415 F.3d 601 (7th Cir. 2005) (*qui tam* action under federal False Claims Act). Count I need only allege that the *transferor's* intent – not Defendants' – was to "hinder" or "delay" one or more persons with a right to payment from Gryphon; specific intent to "defraud" is not essential. Wis. Stat. §242.04(1)(a); *see In re Art Unlimited, LLC*, 356 B.R. 700, 707-08 (Bankr. E.D. Wis. 2006) (intent to hinder or delay, even without intent to defraud, satisfies "intent" element under 11 U.S.C. §548(a)(1)(A)); *In re Cohen*, 199 B.R. 716-17 (B.A.P. 9th Cir. 1996) (relevant intent is that of transferor, not recipient (examining language from California's statute that is identical to Wis. Stat. §242.04(1)(a))). As for Count III, a claim of constructive fraudulent transfer under sections 242.04(1)(b) and 242.05(1) of WFTA "requires neither evidence of actual intent to defraud nor a specific misrepresentation by defendants." *Gen. Elec. Capital.*, 128 F.3d at 1079; *Badger State Bank v. Taylor*, 688 N.W.2d 439, 449 (Wis. 2004) ("[t]he transferee's subjective state of mind does not play a role in resolving" a case under Wis. Stat. §242.05(1)).

C. Whether the Transfers Were Made Pursuant to Pre-Receivership Contracts is Irrelevant to the Sufficiency of Counts I and III.

Defendants' insistence that the Transfers were made pursuant to "valid and binding pre-receivership contracts" (Defs. Mem. at 14) (a description the Receiver disputes) begs the issues addressed in the Complaint and misses the point of fraudulent transfer law, which is "equity and restoration" of the estate "to the financial condition it would have enjoyed if the transfer had not occurred." *In re JTS Corp.*, 617 F.3d 1102, 1111-12 (9th Cir. 2010). Avoidance of fraudulent transfers recognizes that it "is more equitable to attempt to distribute all recoverable assets among the defrauded investors . . . than to allow the losses to rest where they fell." *Donell v. Kowell*, 533 F.3d 762, 776 (9th Cir. 2008).

Therefore, "[a] transfer may be fraudulent even if it is made in accordance with the terms of a contract between the parties." *In re EBC I, Inc.*, 356 B.R. 631, 640 (Bankr. D. Del. 2006). Whether a transfer "was legal or not is irrelevant for the purposes of [fraudulent transfer recovery]. Any *otherwise legal* transfer may be avoided . . . if the requirements of [the statute] are otherwise met". *In re Pinto*, 89 B.R. 486, 497-98 (Bankr. E.D. Pa. 1988), *order for new trial rev'd*, No. 87-02493S, 1989 WL 234516 (E.D. Pa. Aug. 25, 1989).

Moreover, an investor's entitlement to assets of the WM Funds is now governed by the Plan. Because the Transfers enabled Defendants to receive more than their equitable share under the Plan, the Receiver may bring that money back into the receivership estate for equitable distribution to all Gryphon investors, so that Defendants will "not recover more than their proportionate share [and will not] profit from the fact that they fortuitously . . . received payments from a [receivership] entity prior to the receivership." *CFTC v. Lake Shore Asset Mgmt. Ltd.*, No. 07 C 3598, 2010 WL 960362, at *10 (N.D. Ill. Mar. 15, 2010).

V. <u>Count II States a Viable Claim of Unjust Enrichment</u>.

To state a claim for unjust enrichment under Wisconsin law, a plaintiff must plead that (1) a benefit was conferred on the defendant; (2) the defendant knew of the benefit, and (3) it is inequitable for the defendant to accept or retain the benefit. *Ramsey v. Ellis*, 484 N.W.2d 331, 333 (Wis. 1992); *Watts v. Watts*, 405 N.W.2d 303, 313 (Wis. 1987); *Lawlis v. Thompson*, 405 N.W.2d 317, 319 (Wis. 1987). The cause of action is "founded upon the premise that the obligation to make restitution arises not from any representation or promise, but rather [from] the circumstances which create a duty to make restitution," and it is that "duty . . . to return the property . . . which is the basis for recovery." *Lawlis*, 405 N.W.2d at 319-20.

A. The Complaint Identifies the Benefit Conferred upon Defendants, Defendants' Awareness of the Benefit, and the Inequity of Permitting Defendants to Retain the Benefit.

Count II properly alleges that "[t]he Transfers conferred a monetary benefit on Defendants." (Compl., ¶93.) Incorporated into Count II are the Receiver's allegations of the number, specific dollar amounts, and the dates of each challenged Transfer. (*Id.*, ¶¶1, 92.)

Count II also alleges that "Defendants were aware of—indeed, *actively sought*—the benefit conferred upon them by the Transfers." (*Id.*, ¶94 (emphasis added).) In support, the Receiver shows that "Defendants submitted a written request to redeem their full Gryphon investment account on January 5, 2008" and that Defendants' public filings show that they understood and agreed to accept the benefits being conferred upon them. (*Id.*, ¶¶43-46.)

Finally, Count II alleges that "[i]t would be unjust and inequitable under the circumstances of the fraudulent conveyances alleged herein . . . to allow Defendants to retain the benefit of the Transfers." (*Id.*, ¶98.) Among other support, the Complaint explains that, "[a]lthough Defendants accounted for only 8.11% of the aggregate Net Cash invested in

Gryphon, Defendants received almost 73% of the $4,600,00 distributed from Gryphon in January and April of 2009," while "[i]nvestors who received no redemption payments after May 31, 2008, have been paid . . . just 8.039% of their Net Cash in Gryphon." (*Id.*, ¶¶60, 62.) The Complaint alleges that, if Defendants are allowed to keep those benefits, they "will have received a significantly greater distribution on their investments than all other investors in Gryphon." (*Id.*, ¶97.) The allegations of Count II provide fair notice of the Receiver's claim and permit the reasonable inference that Defendants are liable under a theory of unjust enrichment.

B. Count II is Not Precluded by Gryphon's Operating Agreement or the Wisconsin Limited Liability Company Act.

Defendants argue that an unjust enrichment claim cannot be brought where a contract governs the relationship between the parties. (Defs. Mem. at 29-30.) Their authorities, however, stand for the much narrower proposition that only where a *valid*, *binding* contract exists between the parties is a claim for unjust enrichment precluded. *See Cont'l Cas. Co. v. Wis. Patients Comp. Fund*, 473 N.W.2d 584, 587 (Wis. Ct. App. 1991) (finding that unjust enrichment does not apply where there is a *valid*, *enforceable* contract); *Powell Co. v. McGarey Group, LLC*, 508 F. Supp. 2d 1202 (N.D. Ga. 2007) (same where both parties *conceded* existence of *valid* contract); *A&V 425 LLC Contracting Co. v. RFD 55th St. LLC*, 830 N.Y.S.2d 637 (N.Y. Sup. Ct. 2007) (fully performed, *valid, enforceable written contract* precluded unjust enrichment claim); *but cf. Arjay Inv. Co. v. Kohlmetz*, 101 N.W.2d 700 (Wis. 1960) (money paid under a *void* contract may be recovered under theory of unjust enrichment).

For the reasons stated elsewhere in this Opposition, the Receiver argues that, as a matter of law, she is not bound by the requirements of the Gryphon Operating Agreement and, to the extent the Transfers were made pursuant to, or were permitted by, the Operating Agreement, they were fraudulently made, in violation of the covenant of good faith and fair dealing implied in all contracts and in violation of public policy. For those reasons, the Operating Agreement is not a valid, enforceable contract that precludes consideration of claims for unjust enrichment.

Finally, Defendants appear to argue that Wisconsin's limited liability company act preempts Count II because it "govern[s] the relationship between the parties." (Defs. Mem. at 30.) But, the opinion cited by Defendants held only that, where a statute expressly provides that a mechanic's lien primes a pre-existing lien up to a certain statutory amount, the mechanic's lien holder may not, under equitable theories, recover more than that amount. *Indus. Credit Co. v. Inland G.M. Diesel, Inc.*, 187 N.W.2d 157, 160 (Wis. 1971) (express statutory remedy provides mechanic's lien claimant with "security and protection," precluding additional recovery for unjust enrichment). Defendants can point to no provision of the Wisconsin act that, like the statute at issue in *Industrial Credit*, expressly provides "security and protection" (*id.*) to an insolvent limited liability company or its receivership estate against a member's receipt of fraudulent transfers of the company's assets far in excess of that member's equitable share or that excludes the equitable remedy of unjust enrichment.

VI. **Counts IV and V State Viable Claims under the Wisconsin Limited Liability Company Act**.

The Complaint alleges two causes of action arising under the Wisconsin Limited Liability Company Act, Wis. Stat. §§183.0102 *et seq.* (the "LLC Act"): receipt of "unauthorized distributions" under LLC Act §183.0905 (Count IV) and receipt of "wrongful distributions" under LLC Act §§183.067 and 183.0608. Defendants' arguments for dismissal of those Counts mostly rehash legal positions previously rejected in the underlying receivership case. None support dismissal.

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A. Count IV – Receipt of Unauthorized Distributions by Defendants

Members of a limited liability company that is "winding up" are entitled to distributions of that company's remaining assets only "in proportion to [the] respective values" of their contributions to the company. (LLC Act, §183.090(3); Compl., ¶108.) Count IV alleges that Defendants received a grossly disproportionate share of Gryphon's assets (Compl., ¶109). The Complaint provides quantitative measurements of the disparity between the assets transferred to the Defendant Trust from Gryphon, as compared to the shares received by investors generally. (*Id.*, ¶¶54-63, incorporated into Count IV at ¶106.)

Defendants do not directly dispute these allegations in attacking Count IV; instead, their sole arguments are that (a) Section 183.0905 of the LLC Act does not apply to distributions unless an LLC has first "formally dissolved" pursuant to Section 183.0901 (Defs. Mem. at 23), and (b) Defendants were priority unsecured creditors of Gryphon as of the time (fictitious, as the Complaint shows) that their redemption request was accepted. (*Id.* at 24.) The second argument has been foreclosed by this Court and the Seventh Circuit, as discussed above in this Opposition (*see* the Introduction and the discussion of Counts I and III (alleging fraudulent transfers)). In any event, in light of the fraudulent back-dating, the operative time to determine Defendant's status is not the falsified effective date, but the date the redemption request was actually accepted. On that date, Defendants were, in fact, members of Gryphon, and not "creditors"

As to the timing of distributions, Defendants read into the LLC Act a requirement not contained in the Act itself. Section 183.0905 does not require a limited liability company to formally dissolve prior to engaging in "winding-up" activities and making distributions; by its terms, it applies to any limited liability company that has wound up. The Section does not even contain a cross-reference to dissolution under Section 183.0901. Defendants cite no authority to the contrary.

Even if dissolution were a prerequisite to the applicability of Section 183.0905, the Complaint alleges facts sufficient to allow the Court to infer that Gryphon was dissolving at the time of the Transfers. A limited liability company dissolves upon "[t]he occurrence of events specified in an operating agreement." LLC Act, §183.0901(1). The Gryphon Operating Agreement provides that dissolution and wind-up will occur "upon the election of [WM] to dissolve [Gryphon]" (Oper. Ag., §13.1.1). The Complaint describes a letter (the "Liquidation Letter") sent by WM to all investors in Gryphon, informing them that WM had suspended all redemptions and placed Gryphon into full liquidation. (Compl., ¶51.) The Liquidation Letter stated that those actions were taken "pursuant to Sections 13.1 & 13.2 of the [Operating Agreement]". (*See* Liquidation Letter, first paragraph, attached to Stippich Decl. as Ex. D.) This Court acknowledged, in the Approval Order, that the WM Funds had already been placed "in liquidation mode" as of the Receiver's Appointment. Approval Order at 2. Further, the election of WM to dissolve under Section 13.1 of the Operating Agreement may have been made well before the date of the Liquidation Letter, a factual issue not determinable on a motion to dismiss. If the Court determines that prior dissolution is a necessary element of Count IV, it may and should draw the inference that Gryphon was in dissolution for the purposes of Count IV, subject to discovery on that issue.

B. Count V – Receipt of Wrongful Distributions by Defendants

Section 183.0608 of the LLC Act imposes personal liability on "a member . . . who . . . assents to a distribution in violation of . . . §183.0607 or of an operating agreement". (Compl., ¶114.) Count V incorporates factual allegations that support the claim that the Transfers were made in violation of the Operating Agreement (*id.*, ¶115) and alleges that the Transfers violated LLC Act §183.0607, which, as this Court has recognized, prohibits distributions which leave a company "unable to pay its debts as they become due in the usual course of business" or that result in a manager "giv[ing] property away without any consideration." *Protective Life Ins. Co. v. B & K Enter. LLC*, No. 08-C-312, 2010 WL 1368660, at *4 (E.D. Wis. Mar. 31, 2010); *see also Buncher Co. v. Official Comm. of Genfarm*, 229 F.3d 245, 252 (3d Cir. 2000) (stock redemptions provide no value to company).

As investors in an insolvent fund, each equity holder had a right to payment of its equitable share of Gryphon's assets. *SEC v. Wealth Mgmt. LLC,* 628 F.3d 323, 333-35 (7th Cir. 2010). WM admitted in February 2008, before it caused Gryphon to make any of the Transfers, that it could not satisfy all of the redemption requests of its members in full (Compl., ¶48). The Complaint therefore alleges that the Transfers also violated Section 183.0607 and, because Defendants assented to the Transfers, they are liable for their return. (*Id.*, ¶119-22, 125.)

Again, Defendants do not directly dispute these allegations in attacking Count V. Instead, they argue that the back-dated acceptance of their redemption request relieved them of "member" status and conferred upon them "creditor" status, and, because LLC Act §183.0608 applies only to "members" of a company, they cannot be liable thereunder. As described above, when the Transfers were made, no investor was entitled to "creditor" status (Approval Order at 8) as they all were investors whose "claims were substantively the same." *Wealth Mgmt.*, 628 F.3d at 334. Further, on the date the redemption request was actually accepted (not the fictitious earlier date inserted by WM), Defendants were, in fact, members.

Finally, Defendants implore the Court to import into Section 183.0608 a gloss on the word *assent* that would insure that Defendants, by definition, could not "assent[] to a distribution" that they did not make. When a word is not defined in a statute, it is to carry "its ordinary meaning". *See, e.g.*, *FCC v. AT&T Inc.*, 131 S. Ct. 1177, 1182 (2011) (internal quotation marks omitted) (relying on dictionary definitions of the word "personal"). The word *assent* means "verbal or nonverbal conduct reasonably interpreted as willingness." Black's Law Dictionary 132 (9th ed. 2009). Accepting the Transfers can certainly "be interpreted as willingness" to take them, but the Complaint alleges more: Defendants actively considered WM's proposal to back-date their redemption request so that they could receive the Transfers, and they chose to accept it. (Compl., ¶¶43-46.)

VII. Count VI States a Viable Claim for Aiding and Abetting Breach of Fiduciary Duty.

To state a claim for aiding and abetting a breach of fiduciary duty under Wisconsin law, a plaintiff must plead that (1) a duty exists and (2) a third-party encouraged and profited from a breach of that duty. *Burbank Grease Serv., LLC v. Sokolowski*, 717 N.W.2d 781, 796 (Wis. 2006).

Count VI of the Complaint specifically alleges the existence of fiduciary duties owed by WM to Gryphon and describes WM's express acknowledgment to all Gryphon investors of its "'*fiduciary duty* to treat all investors fairly and equitably'" and to "'manage [Gryphon] in the best interests of all members'." (Compl., ¶¶127-29 (emphasis added).) As the Complaint also describes, WM violated those admitted duties by back-dating the effectiveness of the redemption requests of a select few investors, including Defendants, thereby permitting them to avoid the severe limitations on redemptions that WM imposed on all other investors, even as it told other investors that it was requiring all to follow the process set forth in the Operating Agreement. (*Id.*, ¶¶41-49, incorporated into Count VI at ¶126.) Finally, Count VI incorporates allegations, based on Defendants' own documents, that Defendants discussed the back-dating with WM, knew that its purpose was to move them to the head of the line for Gryphon's dwindling assets, and actively requested that treatment. (*Id.*, ¶¶43-46, 126.)

Notwithstanding WM's direct acknowledgment to Gryphon's investors of its fiduciary duties, Defendants suggest that a conventional exculpation and indemnification provision in the Operating Agreement absolved WM of those duties. (Defs. Mem. at 27, *citing* Oper. Ag., §8.1.1, attached to Stippich Decl. as Exhibit A).) It does not. First, there is no exculpation under the Operating Agreement for acts of fraud. (Oper. Ag., §8.1.1). Moreover, the provision does not purport to define, limit, or eliminate any fiduciary duties WM may have; it simply provides for a limitation on recoverable damages. (*Id.*, §8.1.1 ("[t]o the extent that . . . [WM] *has duties (including fiduciary duties*) and liabilities relating thereto . . .") (emphasis added).) Finally, the provision limits WM's liability for breaches of duty only where WM acted in "good faith" reliance upon the Operating Agreement. (*Id.).* Whether WM acted in "good faith" with respect to the Transfers is an issue of fact not properly determined on a motion to dismiss. *Leuch v. Egelhoff*, 51 N.W.2d 7, 10 (Wis. 1952) (refusing to determine good faith on demurrer); *Amoco Oil Co. v. Capitol Indem. Corp.*, 291 N.W.2d 883, 890 (Wis. Ct. App. 1980).

VIII. <u>The Complaint Should Not Be Dismissed as to Defendant Magnette-Long</u>.

Defendants concede that Magnette-Long is a beneficiary of the Defendant Trust, and the name of the Trust – the "Dennis J. Long & Patricia S. Magnette-Long Joint Revocable Living Trust, Dated 5/14/04" (Compl. at 1) – would justify that inference in any event. Further, the Complaint describes and attaches the proof of claim and voluminous related documentation filed by Long, as a trustee of the Trust, in James Putman's chapter 7 bankruptcy case. (Compl., ¶32 and Ex. B). A letter from Long to James Putman, attached as part of Exhibit B to the Complaint, notes that *both* Long and Magnette-Long had "'agreed to place a great deal of money in the

Gryphon Fund . . .'" (Compl., ¶40). Moreover, WM regularly addressed communications regarding redemptions from Gryphon, including the Transfers, to both Long and Magnette-Long (*see* Compl., Exhibit B, at 56, 93-95, 97, 99 & 101). The Receiver may seek relief against Magnette-Long as one who benefitted from the Transfers. *See, e.g.*, *Knauer v. Jonathon Roberts Fin. Group, Inc.,* 348 F.3d 230, 236 (7th Cir. 2003).

Finally, both Dennis Long and Patricia Magnette-Long personally executed the redemption request at issue in the Complaint. (Compl., ¶38 & Exhibit B at 57.) Even if she were not a beneficiary, as a trustee of the Trust, Magnette-Long would be liable for avoidable transfers made to the Trust. *See Paloian v. LaSalle Bank, N.A.*, 619 F.3d 688, 691-92 (7th Cir. 2010).

CONCLUSION

The six counts of the Complaint rely on detailed factual allegations, documents originating with the Defendants or filed in the underlying receivership case, and explanations of the Receiver's legal theories, all of which permit the Court reasonably to infer that the Defendants are liable as alleged. The Receiver asks that the Court deny Defendants' Motion.[4]

Respectfully submitted this 12th day of April, 2011.

/s/ Christopher Combest

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[4] Under Fed. R. Civ. P. 15(b), courts should "liberally grant permission to amend pleadings" absent "undue prejudice . . . undue delay, bad faith or dilatory motive on the part of movant." *Sides v. City of Champaign*, 496 F.3d 820, 825 (7th Cir. 2007). Defendants allege no such circumstance which would justify dismissal with prejudice. (Defs. Mem. at 31.) To the extent the Court finds that the Complaint is insufficient, the Receiver asks that the Court grant her leave to file an amended Complaint.