[redacted]

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IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF UTAH, CENTRAL DIVISION

D. RAY STRONG, as Liquidating Trustee of the Consolidated Legacy Debtors Liquidating Trust, the Castle Arch Opportunity Partners I, LLC Liquidating Trust and the Castle Arch Opportunity Partners II, LLC Liquidating Trust,

Plaintiff,

v.

KIRBY D. COCHRAN; JEFF AUSTIN; AUSTIN CAPITAL SOLUTIONS; WILLIAM H. DAVIDSON; DOUGLAS W. CHILD; CHILD, VAN WAGONER & ASSOCIATES, LLC, fka CHILD VAN WAGONER & BRADSHAW, PLLC; ROBERT CLAWSON; HYBRID ADVISOR GROUP; and JOHN DOES 1-50,

Defendants.

Civil Action No. 2:14-cv-00788-TC

MOTION OF DEFENDANTS [redacted] TO DISMISS THE COMPLAINT PURSUANT TO FEDERAL RULE OF CIVIL PROCEDURE 12(B)(6); AND SUPPORTING MEMORANDUM

Judge Tena Campbell

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RELIEF REQUESTED

Defendant [redacted] move to dismiss the Complaint pursuant to Federal Rule of Civil Procedure 12(b)(6) on the following grounds: (1) Plaintiff fails to meet the heightened pleading standards of Rule 9(b) for his fraud-based claims and the Private Securities Litigation Reform Act for his federal securities fraud claims, which require "all of the essential factual background that would accompany 'the first paragraph of any newspaper story' -- that is, the 'who, what, when, where and how' of the events at issue;" (2) reliance on "group pleading" dooms the Complaint to dismissal by pleading allegations against all "Management" regardless of their position or role, the specific statement made, who they made them to, or the scienter of each particular person; (3) the Complaint fails to allege a particular material misrepresentation or omission by [redacted] and because he is not alleged to have ultimate authority over any vague misstatements, the federal securities law claims fail under the Supreme Court's decision in *Janus*; (4) the Complaint utterly fails to plead the remaining, necessary elements of securities fraud including scienter, reliance and causation; (5) the Complaint fails to allege factual allegations with particularity to support a state or federal claim for control person liability; (6) the Complaint fails to allege a fiduciary relationship, as none exists, foreclosing any claim for a breach of fiduciary duty; (7) the state law claims similarly fail; (8) all the claims are untimely and cannot be revived by an invalid tolling agreement.

INTRODUCTION

After faithfully serving as the Managing Director of Business Development from the

[1] [redacted] previously maintained a "doing business as" bank account registered in such name.

formation of Castle Arch Real Estate Investment Company, LLC ("CAREIC") in April 2004, until his resignation on or about June 2009, [redacted] is forced to defend himself not only for events not within his control, but against claims amounting to no less than double jeopardy for his prior publicly disclosed, statutory disqualification that occurred more than fourteen years prior to the events underlying this present controversy. After being in possession of all the corporate records and investigating the transactions in question for nearly five years, combined with the heightened pleading standards applicable to the claims made by the Plaintiff, it is striking to compare the group pleading of the Complaint to the historical proceedings in the CAREIC bankruptcy matters, which demonstrate the extent to which [redacted] is **not** involved. In the Complaint and those historical pleadings and testimony, much of which were filed by the Plaintiff himself, he is not alleged to have made any misstatements, nor to have had ultimate authority over any such alleged misstatements. That Plaintiff can allege only a remote, if any, link to [redacted] is not surprising especially in light of the fact that, prior to the Complaint, Clawson has never even been held out as a significant employee, officer or director of CAREIC and [redacted] has never even identified him as such or even an insider in the bankruptcy case.

The Complaint fails to satisfy the heightened pleading standards applicable to the fraud and securities fraud claims that require pleading "all of the essential factual background that would accompany 'the first paragraph of any newspaper story' -- that is, the 'who, what, when, where and how' of the events at issue." Importantly, when reviewing judicially noticeable documents filed contemporaneously with this motion, Plaintiff cannot cure this failure.

FACTUAL BACKGROUND AND SUMMARY OF RELEVANT ALLEGATIONS

The following factual allegations are drawn from the Complaint, matters of which a court

may take judicial notice (including SEC filings) and the documents attached or otherwise incorporated by reference. *See Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 322 (2007); *In re Gold Res. Corp. Sec. Litig.*, 776 F.3d 1103, 1108 (10th Cir. 2015).[2]

I. FORMATION AND DOWNFALL OF CAREIC

Castle Arch Real Estate Investment Company, LLC was organized on April 15, 2004 as a California limited liability company "with [Robert] Geringer as president, Cochran as CEO, and CPA Doug Child as CFO along with an advisory board, although the company only really began operating in 2005. Castle Arch's basic starting business model was to acquire raw land with investor money, obtain zoning and other entitlements, and then resell the property for a profit." *In re Castle Arch Real Estate Inv. Co., LLC,* No. 11-35082, 2013 WL 1603319, at *1 (Bankr. D. Utah Apr. 15, 2013); *see also* Compl. ¶¶ 2, 3, 5, 32; *see also* Exhibit 1 attached to the Complaint ¶¶ 36-37 (hereinafter, the "Consolidation Findings").

On **April 2, 2007**, approximately eight months after filing its first quarterly report with the SEC, in the company's first annual report for the 2006 fiscal year,[3] CAREIC began reporting potential problems with its business model and operations:

> **Forecast of Potential Losses on Fresno, California Properties.** "Due to the softening of the residential market in California in 2006, there was an increase in tracts of raw land subject to distressed sales across the state[,] [which] has hindered our ability to profit from the resale of the properties to which we have ownership rights in Fresno County California."
>
> CAREIC had invested $180,409 and $149,145 prior to the "Assignment and the Reassignment" of the Fresno properties to Baillo that were a "**potential conflict of interest**" for Geringer. "During the period between the Assignment and the Reassignment, we reimbursed Mr. Baillio for all deposits and costs incurred by him

[2] The allegations in the Complaint are accepted as true only for purposes of this Motion.
[3] Declaration of Brett G. Evans in Support of Defendants [redacted] Motion to Dismiss the Complaint, Ex. A, Form 10-KSB for Fiscal Year Ended December 31, 2006 ("10-K FY 2006").

in connection with the purchase of the properties[,]… paid other deposit and entitlement costs totaling $210,785 for Firebaugh and $125,145 for Coalinga through December 31, 2006[,] [and]…an additional $1,000,000 to the original sellers of the properties to maintain Mr. Baillio's purchase rights. The Reassignment **did not require us to pay the additional $1,000,000**."

Baillo "failed to pay us and is in default of the Reassignment" and CAREIC determined not to seek judicial enforcement while also not maintaining a termination option under the Reassignment. *See* 10-K FY 2006 at 8-10 (emphasis added).

Weaknesses in Controls and Procedures. Beginning with the quarterly report ended June 30, 2005, CAREIC's "principal executive officer and principal financial officer, with the participation and assistance of our management, concluded that our disclosure controls and procedures…were effective in design and operation [only after implementing] significant changes in our internal controls over financial reporting [that previously] materially affected or are reasonably likely to materially affect our internal controls over financial reporting[,]" including: (1) "separation of incompatible duties and restricted access to cash[;]" (2) "recording of cash[;]" (3) "separation of incompatible duties and restricted access to cash[;]" and (4) "recording of equity." *Id*. at 13-14.

On **April 14, 2008**, any doubt as to CAREIC's failure to execute on one of its first projects was laid to the rest in its second annual report for the 2007 fiscal year (Evans Decl., Ex. Y, Form 10-KSB ("10-K FY 2007")), when classified the deposits as losses and disclosed:

Suspended Project. During the twelve month period ended December 31, 2008 our Board of Directors elected to expense nonrefundable deposits and entitlement costs incurred and previously capitalized relative to properties in Coalinga, Firebaugh, and Imperial, California counties, and Lindale, Texas, totaling $2,161,585. This is in addition to additional related fees and other abandoned property fees totaling $24,701 in 2008 and other write-offs in 2007. Our Board of Director's decision was based on its assessment of the properties' ultimate viability and profitability. These amounts have been recorded in "costs of terminated projects" in our financial statements. *Id*. at 8.

Volatile Real Estate Markets. "The real estate market in the United States became increasingly volatile in 2007. Rising interest rates in 2007 increased the monthly payments on adjustable rate mortgages and property values suffered declines from the demise of the U.S. housing bubble…resulted in a severe credit crunch, and threatened the solvency of a number of marginal private banks and other financial institutions….A decrease in the favorability of the available terms for financing or the ability to obtain financing at all, would have a **negative impact on our profitability** and ability to expand our business…Real estate bubbles are

> invariably followed by severe price decreases that can result in many owners holding mortgage debts higher than the current value of their properties. …**If the bubble breaks or even if housing values decline by 15 to 25%, there would be a decrease in our projected profits and unexpected losses could occur which would negatively impact our operations**." *Id*. at 5. (emphasis added)
>
> **CAREIC's Risky Financial Condition**. CAREIC "**sustained significant operating losses since our inception**…We had no revenues in the year ended December 31, 2007 [as CAREIC still had not consummated its] primary business target of selling property that we have improved through obtaining legal entitlements or other developmental improvements."
>
> CAREIC's "operating selling, general and administrative expenses totaled $10,806,585 during the twelve month period ended December 31, 2007, compared to $5,186,521 during the comparable twelve month period ended December 31, 2006. The increase…is **primarily attributable to increased salaries of our executive officers and additional employees, office costs, professional services and the costs of terminating purchase agreements**, i.e., the forfeiture of deposits."
>
> CAREIC's "decreased cash balance as of December 31, 2007 is l**argely attributable to non-cash common units issued as bonuses to executive officers**, employees for outside professional services….**[A]dditional funding will be necessary** to finance growth and to achieve our strategic objectives… However, if we do not raise sufficient funds in the future, we may not be able to fund expansion, take advantage of future opportunities, meet our existing debt obligations or respond to competitive pressures or unanticipated requirements." *Id*. at 11-12.

With a business model focused "on acquiring and developing real property[,]" CAREIC required additional funding to sustain operations, "because, while property rights had been purchased, the property had not been developed and there was a virtual lack of revenues to fund operations." Consolidation Findings ¶ 37; *see also* Compl. p. 6 fn. 8. Eventually, CAREIC's solvency evaporated as a result of various factors, including but not limited to the global economic crisis generally, the "national decline in real estate market" in particular, an "interruption in the Debtors' ability to solicit Investors as a result of an informational inquiry by the Securities and Exchange Commission in 2009[,]" the "commencement of the 'Longview Action' in the State of New York by the Debtors' FINRA broker-dealer" and a debt collection action by CAREIC's former corporate counsel in June 2010. *See* Bankruptcy Case (hereinafter

defined), Disclosure Statement (hereinafter defined), Dkt. No. 655. On September 9, 2011, a Utah State Court presiding over in the debt collection action by CAREIC's former counsel appointed a receiver (the "Receiver").[4] *Id*. at 25.

II. PRIOR BANKRUPTCY RELATED BANKRUPTCY PLEADINGS

On October 17, 2011, the Receiver for CAREIC filed a Chapter 11 bankruptcy petition in the United States Bankruptcy Court, District of Utah ("Bankruptcy Court"), entitled *In re: Castle Arch Real Estate Company, LLC et al.*, United States Bankruptcy Court for the District of Utah (Bankr. Case No. 11-35082) (the "Bankruptcy Case") and on October 20, 2011, the Receiver also filed Chapter 11 petitions for each of the other Debtors, other than CASV (collectively, these dates are referred to as the "Petition Date"). Compl. ¶ 11.

On May 3, 2012, the Bankruptcy Court entered an Order appointing the Plaintiff as the Chapter 11 Trustee for CAREIC,[5] and in that capacity, the Trustee managed, either directly or indirectly, each of the other Debtors. Compl. ¶ 12.

On December 28, 2012, Plaintiff filed a motion to substantively consolidate,[6] which was supported by a declaration filed on January 29, 2013.[7] *See* Evans Decl., Ex. A ("Decl. ISO Consolidation"). Based thereon, on February 8, 2013, the Bankruptcy Court entered an order substantively consolidating CAOP Managers, CAK, CAS, CASDF and CASV with CAREIC (the "Consolidation Order")[8] and the Consolidation Findings.[9] Compl. ¶¶ 13-14, Exhibit 1

[4] *The Hunt Law Firm v. CAREIC*, Case No. 100700353 (Utah 2nd Dis. Ct.).
[5] Bankruptcy Case, Dkt. 215.
[6] Bankruptcy Case, Dkt. 537.
[7] Bankruptcy Case, Dkt. 578.
[8] Bankruptcy Case, Dkt. 590.
[9] Bankruptcy Case, Dkt. 591.

attached thereto.

On March 27, 2013, the Bankruptcy Court entered an order,[10] which among other items, approved the Disclosure Statement for the Plan of Liquidation (incorporated in the confirmed plan and considered by the Bankruptcy Court in its Confirmation Order, as defined herein).[11] *See* Evans Decl., Ex. B ("Disclosure Statement").

On April 15, 2013, the Bankruptcy Court, after significantly pleading[12] and an evidentiary hearing ("Geringer POC Hearing") that included testimony from several former officers and directors, entered its findings of fact and conclusions of law on defendant Geringer's claim filed against CAREIC in the Bankruptcy Case. *In re Castle Arch Real Estate Inv. Co.*, LLC, No. 11-35082, 2013 WL 1603319 (Bankr. D. Utah Apr. 15, 2013); *see also* Evans Decl., Ex. E ("Geringer Claim Order"). In the Geringer Claim Order, the Bankruptcy Court found the following relevant facts:

> CAREIC "was organized on April 15, 20042 with Geringer as president, Cochran as CEO, and CPA Doug Child as CFO along with an advisory board, although the company only really began operating in 2005." *Id.* at 2.
>
> CAREIC's "Operating Agreement gave Cochran 'full and complete authority, power and discretion to make any and all decisions and to do any and all things which the chief executive officer shall deem to be reasonably required to accomplish the business and objectives of the Company. No Member, other than the chief executive officer, shall have the authority to bind the Company, unless given that authority by the chief executive officer.'" *Id.* at 3.
>
> "Because Geringer was the only one with real estate experience, and at Geringer's own request, Cochran granted Geringer 'the authority to bind the

[10] Bankruptcy Case, Dkt. 652.
[11] Bankruptcy Case, Dkt. 655.
[12] *See* Bankruptcy Case, Dkt. 307 (Objection to Geringer's Proof of Claim), Dkt. 585 (Objection to Geringer's Amended Proof of Claim), Dkt. 604 (Geringer's Response to Objection), Dkt. 612 (Plaintiff's Reply to Geringer's Response), Dkt. 644 (Geringer's Proposed Findings and Conclusions of Law) and Dkt. 645 (Plaintiff's Proposed Findings and Conclusions of Law).

> corporation with regard to any contracts, liabilities, obligations or other matters relating to the operation of [CAREIC] or with regard to the acquisition, disposition or encumbrance of any properties.'" *Id*.

On June 7, 2013, after considering the Disclosure Statement and other pleadings and documents filed in the Bankruptcy Case, the Bankruptcy Court entered its Findings of Fact and Conclusions of Law ("Confirmation Findings")[13] in support of the Order Confirming Chapter 11 Trustee's First Amended Plan of Liquidation Dated February 25, 2013 as Modified (the "Confirmation Order").[14] Compl. ¶ 15.

III. PLAINTIFF DEMANDS [redacted] EXECUTE TOLLING AGREEMENT WITH KNOWLEDGE OF LACK OF REPRESENTATION

On March 7, 2013, Plaintiff and counsel contacted [redacted], **with the "understanding that you are not represented by a lawyer in connection with the Castle Arch matters**[,]" attached a draft Tolling Agreement with the threat of filing a civil suit (Evans Decl., Ex. CC).:

> We are currently preparing a Complaint against you and others…and unless we are able to enter tolling agreements…would expect to file no later than October 15th.
>
> …a Tolling Agreement with you…would allow [us] time to discuss, and hopefully resolve the Trustee's claims without the necessity of filing a Complaint[.]
>
> **I need to hear from you no later than the end of this week**, and we will need to have entered agreements no later than next Monday (10/14). If I do not hear from you, a Complaint will be filed by October 15th.
>
> If you have any questions, please give [Plaintiff's counsel] a call.

On October 12, 2013, five days later and prior to [redacted] responding, Plaintiff and counsel sent a draft complaint to [redacted] and nine other potential parties (or their counsel) informing all of them that four individuals, including "[redacted],…have not returned signed tolling agreements. If we do not receive executed tolling agreements by close of business

[13] Bankruptcy Case, Dkt. 704.
[14] Bankruptcy Case, Dkt. 705.

Monday, our intention is to file the Complaint on Tuesday." Evans Decl., Ex. DD.

On October 14, 2013, the notice and threat to other defendants had its desired outcome – [redacted] was contacted by others out their concern (all or none must sign) and executed the Tolling Agreement. Evans Decl., Ex. EE.

Two days later, on October 16, 2013, counsel to Plaintiff again emailed [redacted] demanding "an additional Tolling Agreement [redacted]" and again, informed [redacted] to contact him if he has "any comments or questions regarding these Tolling Agreements. Otherwise, we'd appreciate having them *signed and returned today or tomorrow*." Evans Decl., Ex. FF (emphasis in original)

[redacted] responded the same day, October 16, 2013, stating "I am not sure I understand either of" the Tolling Agreements and "**I currently have no counsel for advice, so I will seek that now and hope to get back with you next week**." Evans Decl., Ex. FF (emphasis added).

Despite this reasonable request to seek advice of counsel, less than 24 hours later, on October 17, 2013, counsel to [redacted] refused and demanded execution in less than three hours:

> Today is our deadline to file claims absent an agreement tolling the deadline.
> At this time, we have not yet received an executed version of the attached tolling agreement for [redacted] which is an entity that received monies from the Castle Arch entities prior to their bankruptcy.
> Accordingly, **if we do not have executed versions of these agreements back by 5:00 pm (Mountain) tonight, we will be forced to file a lawsuit** against [redacted] seeking to recover the transfers that were made by the debtors to it. *Id.*

IV. LIMITED FACTUAL ALLEGATIONS ABOUT [redacted]

[redacted] was "CAREIC's Managing Director of Business Development, an investor relations contact," and Plaintiff alleges was "a de facto officer and member of CAREIC's Board

from its inception in 2004 until [approximately June 2009]."[15] [redacted] previously maintained a bank account for a dba entitled [redacted] received transfers from Debtors. Compl. ¶¶ 28-29, 303(e).[16] [redacted] was an "Officer, "Management" and a member of the "Board." *Id.* ¶ 31. [redacted] was highly compensated by CAREIC. *Id.* ¶ 154.

[redacted], "[s]ince at least [2001],…has been subject to a 'statutory disqualification' within the meaning of 15 U.S.C. §78c(a)(39)," (*Id.* ¶ 169) and "barred from participating in penny stock offerings and from association with any broker or dealer[.]"[17]

[redacted] "designed," "drafted and oversaw the drafting of the CASDF PPM." *Id.* ¶ 204.

However, these allegations are <u>contradicted by</u>:

Plaintiff has repeatedly declared, argued or relied on testimony that [redacted] was not an officer, director or part of the management team of CAREIC. *See* Decl. ISO Consolidation ¶ 15 (CAREIC and affiliated entities "were managed by a single paid management team. Thus, CAREIC's Board of Directors and Officers also managed the other Debtors and Castle Arch Entities.") (citing Form 10-Ks for fiscal years ending 2005 through 2008); *see also* Disclosure Statement at 7 ("CAREIC was managed by compensated Directors and Officers comprised principally of Kirby D. Cochran ('Cochran'), Robert D. Geringer ('Geringer'), Douglas W. Child ('Child'), and Jeff Austin.");[18] *id*. at 31 (Longview "commenced an action in a New York state

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[15] [redacted] tendered his resignation in mid-June 2009; *see also* Compl., Ex. 5 (last payment occurred on July 28, 2009).

[16] [redacted] previously owned an interest in a failed California corporation, but such entity was formed on May 20, 2011, but shares were tendered to other shareholder in approximately 2012.

[17] *In the Matter of John L. Banach, et al..*, Release No. 189 (Sept. 5, 2001).

[18] Further, Plaintiff listed Insider Equity Interests, but did not list [redacted]'s equity interests on Exhibit D attached to the Disclose Statement. Id. at 6. *Cf*. Evans Decl., <u>Ex. C</u> (listing [redacted] as a holder of preferred interest)

court against **all of the Debtors, Directors and Officers**[,]" but the actual complaint was not filed against [redacted]) (emphasis added);[19] Evans Decl., Ex. F at 44:14-21 (Geringer testifying that officers were Cochran, Child, Geringer, Austin and eventually Davidson). Further, the Board meetings discovered in investigating the unspecified claims do not list [redacted] in attendance. *See* Evans Decl., Ex. I-M.

The relevant PPMs did not list [redacted] as a director, executive officer, promoters and control person or a "significant employee." *See* Evans Decl., Ex. S ("Series E PPM") at 25-29, Ex. T ("CASDF PPM") at 24-27, Ex. U ("CAS PPM") at 20-23. The public filings did not list [redacted] as a director, executive officer, promoters and control person or a "significant employee." *See* 10-K FY 2006 at 12-16, 10-K FY 2007 at 15-19, Evans Decl., Ex. X, Form 10-KSB for Fiscal Year Ended December 31, 2008 ("10-K FY 2008") at 39-43.

While [redacted] may not introduce himself as "statutory disqualified," he has never concealed his prior securities history and in fact, such is available by simply "googling" his name or searching the SEC website. *See supra* fn. 18.

V. UNSPECIFIED, GROUP PLEAD ALLEGATIONS OF MANAGEMENT

[redacted], along with Cochran, Child, Austin, were "Officers" and with Davidson, was a member of the "Board." Compl. ¶ 31.

A. Breaches of Fiduciary Duties Relating to Specific Real Estate Projects

> "CAREIC Management breached their fiduciary duties with respect to the real estate project in Kingman, Arizona by, among other things: (a) using irrational sales assumptions and pro forma metrics that contradicted known data, and failing to

[19] *See* Evans Decl., Ex. D (excerpt of Longview Complaint).

> disclose to investors accurate forecasts;[20] (b) wasting corporate assets (investor money) on an infeasible project without sufficient funding and resources;[21] and (c) engaging in co-mingled and self-dealing transactions that were not disclosed to investors." *Id*. ¶ 31.
>
> "At a minimum, CAREIC Management had a duty to disclose the unrelated debt to investors, and to update the Kingman Pro Forma to account for the additional debt." *Id*. at 64.
>
> As to the Tooele Project, CARIEC Management also breached their fiduciary duties…by: (a) failing to disclose known annexation issues to investors; (b) wasting corporate assets (investor money) to purchase land and water rights…; (c) using irrational sales assumptions and pro forma metrics that contradicted known data…; and (d) encumbering the project with millions of dollars of debt[.]" *Id*. ¶ 61.
>
> As to the Smyrna Project, "CARIEC Management also breached their fiduciary duties… by: (a) ignoring known land and development issues…; (b) using false and improper data to analyze the project's feasibility and profitability; (c) using false and fraudulent estimates for lot demand…; (d) proceeding with lot purchases…despite insufficient funds….; and (e) engaging in self-dealing transactions." *Id*. ¶ 93.

However, these allegations are in hindsight, not supported or contradicted:

The majority of these allegations are no more than a creative attempt to revive untimely securities fraud claims on offerings made more than 10 years prior. For example, the CAK offering occurred during 2006 (*see* FY-2006 at 11), where one must trust was the source of the pro forma, while the loans occurred two years later "in March 2008 and May 2009;" thus, this nothing more than significant hindsight after the fact. Compl. ¶ 61.

The group pleading as to the responsibility of [redacted] (as part of the CAREIC Management) not only contradicts record established in the Bankruptcy Case, the testimony of former officers, directors and managers of CAREIC, but **more importantly, contradicts prior testimony and verified pleadings made by the Plaintiff**. *See* Geringer Claim Order at 3; Geringer POC Hearing at 45:4-18, 436:9-10 (Geringer testimony that responsibilities were solely

[20] Due to "straight line 5% sales price escalator throughout the life of the Kingman Project; and (b) an absorption sales rate of approximately 992 finished lots per year." *Id*. ¶ 45.
[21] Needed to raise an additional $30 million to sustain the Kingman Project.

focused on real estate, including "[f]inding properties, identifying them, doing the due diligence, putting /together the transaction, working with the governmental entities to entitle the property, …interfacing with builders, …and finding builders to buy those properties after they were entitled through the government process."); *id*. at 436:9-11, 437:10-18, 441:11-12 (Plaintiff arguing that Geringer "had full authority to be running these real estate deals for the company."); Evans Decl., Ex. Q, Geringer Complaint ¶ 3 ("Geringer—the President of CAREIC and the person in charge of the Debtors' real estate operations—recklessly moved forward with accelerated investment in raw land long after it was clear that the real estate market was collapsing, and most national production home builders had drastically curtailed, or entirely stopped land purchases."); *id*. ¶ 23 (Geringer empowered by Operating Agreement and quoting Geringer Claim Order); *id*. ¶¶ 33-132 (alleging all such breaches of fiduciary duties to be the responsibility of Geringer); and Evans Decl., Ex. N (Cochran granting real estate authority to Geringer pursuant to CAREIC's Operating Agreement).

B. Lack of Board Oversight and Lack of Officer Diligence

Such allegations that [redacted], as an alleged member of the Board and Officer, lacked oversight and diligence (Comp. ¶¶ 138-143) are unsupported by organization of CAREIC, as previously found in the Geringer Claim Order. The sole power and authority was vested with Cochran. *See* Evans Decl., Ex. R, CAREIC Operating Agreement at § 3.1; Ex. G at 44:14-21 (Hunt testified: "only one functioning board, **and it was a board of advisors for that matter**.").

C. Lack of Internal Control and Reporting Procedures

Allegations that [redacted], as Management, was responsible for the internal controls and reporting procedures or was part of the audit process (Comp. ¶¶ 144-146), is not supported by

the signed certifications filed with the SEC certified by Cochran and Child. *See* Evans Decl., Ex. Z (financial statements, controls and reporting procedures certified by Cochran and Child).

D. Allegations of Material Omissions Related to CAREIC Securities Offerings

Plaintiff alleges that the CAS PPM would use the funds only for the Smyra Project. Compl. ¶¶ 212-215.

"CAREIC Management" ignored multiple reports from Ragan-Smith Engineers prior to acquiring the Smyrna Property, including that: (i) the Smyrna Property was undevelopable because of its geographic features; (ii) "*the maximum number of lots theoretically possible on the entire property was no more than 1,295*" because "only 316.5 [of the 643 acres under contract] were developable;" (iii) property had no sewer services that may require 129.5 acres devoted to septic "reducing *the maximum possible number of lots to 919*;" (iv) annexation to Smyrna which was "unlikely for at least 4-5 years;" (v) "internal analysis…presented it to its Board of Directors" was based on "assumptions [that] were directly contradicted by facts known to CAREIC Management at the time" including that the "project would generate at least 1600 lots for sale (not the 919 that Management's Engineers had advised were possible)." *Id*. ¶¶ 216-217.

However, these allegations are either not supported by the referenced material, misquoted or otherwise offset by relevant cautionary language. For example, Plaintiff misquotes the CAS PPM as it continues to provide that "[w]e have not determined the amount of net proceeds to be used specifically for each of the foregoing purposes. Accordingly, our management will have broad discretion to spend flexibly in applying the net proceeds of this offering." CAS PPM at 33; *see also id*. at 40 ("CAREIC, OUR MANAGING MEMBER, MAY SPEND THE NET PROCEEDS OF THIS OFFERING IN WAYS WITH WHICH YOU MAY

NOT AGREE) (emphasis in original); *id*. at 42 (DISCRETIONARY USE OF PROCEEDS). Further, the Ragan-Smith Engineers information that [redacted] was able to acquire (despite the lack of particularity of factual allegations) tends to support the assumptions in the CAS PPM, or at least, not contradict it. *See* Evans Decl., Ex. BB, Ragan-Smith Engineers Proposal to Town of Smyrna (providing for 1,566 lots).

ARGUMENT

Subject to the applicable heightened pleadings standards, under Rule 12(b)(6) of the Federal Rules of Civil Procedure, a plaintiff must plead "enough facts to state a claim to relief that is plausible on its face." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007). A claim is plausible on its face "when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009). A complaint does not "suffice if it tenders 'naked assertion[s]' devoid of 'further factual enhancement.'" *Id*. at 678 (*quoting Twombly*, 550 U.S. at 557). "'[T]he tenet that a court must accept as true all of the allegations contained in a complaint is inapplicable to legal conclusions. Threadbare recitals of the elements of a cause of action, supported by mere conclusory statements, do not suffice.'" *Bixler v. Foster*, 596 F.3d 751, 756 (10th Cir. 2010). "Further, we 'must consider the complaint in its entirety, as well as other sources,' including 'documents incorporated into the complaint by reference, and matters of which a court may take judicial notice.' I*n re Gold Res. Corp. Sec. Litig.*, 776 F.3d 1103, 1108 (10th Cir. 2015).

I. PLAINTIFF'S FAILURE TO MEET THE APPLICABLE PLEADING STANDARDS REQUIRES DISMISSAL OF THE FRAUD CLAIMS

To plead securities fraud, Plaintiff must plead facts demonstrating "(1) a material misrepresentation or omission by the defendant; (2) scienter; (3) a connection between the

misrepresentation or omission and the purchase or sale of a security; (4) reliance upon the misrepresentation or omission; (5) economic loss; and (6) loss causation." *Stoneridge Inv. Partners, LLC v. Sci.-Atlanta*, 552 U.S. 148, 157 (2008). At a minimum, Rule 9(b) requires that Plaintiff must support his allegations of securities fraud "with all of the essential factual background that would accompany 'the first paragraph of any newspaper story' -- that is, the 'who, what, when, where and how' of the events at issue." *In re Rockefeller Ctr. Props., Inc. Sec. Litig.*, 311 F.3d 198, 216 (3d Cir. 2002) (citations omitted).[22] Under the heightened pleading standards imposed by the Private Securities Litigation Reform Act ("PSLRA"), Plaintiff must: "(1) 'specify **each statement** alleged to have been misleading [and] the reason or reasons why the statement is misleading,' 15 U.S.C. § 78u–4(b)(1); and (2) 'state with particularity facts giving rise to a strong inference that **the defendant** acted with the required state of mind,' § 78u–4(b)(2)." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 321 (U.S. 2007) (emphasis added).

The first subsection requires that a "plaintiff must [] specifically identify each statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if the allegation is made on information and belief, the plaintiff must set forth all information in plaintiff's possession on which the belief is formed."[23] Further, PSLRA "requires the plaintiff to show that the misstatement or loss alleged in the complaint caused the loss incurred by the plaintiff." *Id*. The second subsection, modeled after the Second Circuit's "most stringent

[22] *See also Caprin v. Simon Transportation Servs., Inc.*, 99 F. App'x 150, 158 (10th Cir. 2004) (unpublished)
[23] Private Securities Litigation Reform Act of 1995, S. REP. 104-98, 15, *reprinted in* 1995 U.S.C.C.A.N. 679, 694.

pleading standard," *id*., whereby "in determining whether the pleaded facts give rise to a 'strong' inference of scienter, the court must take into account plausible opposing inferences." *Tellabs*, 551 U.S. at 323, 326. The "court's job is not to scrutinize each allegation in isolation but to assess all the allegations holistically," *id*. at 326:.

> To assess the strength of an inference of scienter, we compare the "inferences urged by the plaintiff[s]" with "competing inferences rationally drawn from the facts alleged." An inference of fraudulent intent must be more than "'reasonable' or 'permissible'—it must be cogent and compelling.'" Thus, the complaint suffices "only if a reasonable person would deem the inference of scienter cogent and at least as compelling as any opposing inference one could draw from the facts alleged."

Anderson v. Spirit Aerosystems Holdings, Inc., 827 F.3d 1229, 1237 (10th Cir. 2016), *as amended* (July 6, 2016) (*quoting Tellabs*, 551 U.S. at 314, 324). The Courts must dismiss a complaint that does not meet these requirements as PSLRA provides no exceptions. *See* 15 U.S.C. § 78u-4(b)(3)(A).

As discussed herein, Complaint's allegation of fraud fails to satisfy the heightened pleading requirements of Rule 9(b) and PSLRA and falls woefully short in pleading the necessary elements for securities fraud. Further, because Plaintiff brings these claims as an assignee, he must allege sufficient facts to show that each of the assignors that assigned are entitled to relief. Here, the Complaint should be dismissed as it "neither identif[ies] the assignors of plaintiffs' claims, nor allege sufficient facts to demonstrate that the assignors would be entitled to relief." *In re TFT-LCD (Flat Panel) Antitrust Litig.*, 787 F. Supp. 2d 1036, 1040 (N.D. Cal. 2011) [antitrust action]). Plaintiff's concealment of the assigning investors is a *prima facie* demonstration of the utter failure of the Complaint to satisfy the applicable pleading standards and requires dismissal – by concealing the assigning investors (and at least one identifiable creditor) conclusively forecloses the Complaint's ability to plead with particularity factual

allegations such as: (i) when the material misrepresentations were made (or misleading statements omitting material facts); (ii) where such misrepresentations or omissions were made to the assigning investors; (iii) the causal nexus between such misrepresentations omissions and the assignors' transactions; (iv) the reliance by the assigning investors; and (v) the loss causation.

A. The "Group Pleading" of the Complaint Dooms It to Dismissal

The Complaint falls woefully short of the requirements of PSLRA and Rule 9(b) by attempting to plead allegations against all defendants regardless of their position or role, the specific statement made, who they made them to, or the scienter of each particular person. By attempting to generally allege against all the defendants, the Plaintiff fails to allege the specifics required: the transactions, the allegedly false statements, who among the defendants allegedly made them, when, where, to whom, the reliance, the loss causation and scienter. Plaintiff has made no attempt to include the kind of detail required to state his claims. This pleading utterly fails to put the defendants on notice of the claims against them, much less provide the details of the serious allegations of fraud contained in the Complaint, and accordingly should be dismissed under Rule 9(b) and the PSLRA. The judicially-created "group pleading" doctrine "is no longer viable in private securities actions after the enactment of the PSLRA"[24] or subsequent to the Supreme Court's decision in *Janus*.[25] *Winer Family Trust v. Queen*, 503 F.3d 319, 337 (3d Cir.

[24] *Janus Capital Grp., Inc. v. First Derivative Traders*, 564 U.S. 135 (2011).

[25] As the Fifth Circuit explained (pre-*Janus*):

> While the PSLRA does not explicitly abolish the doctrine, it was not necessary to do so because Congress never made this judicial creation law to begin with. Even prior to the PSLRA, section 10(b) and Rule 10b–5 required plaintiffs to identify the roles of the individual defendants, and describe their involvement, if any, in preparing the misleading statements…"group pleading" doctrine…cannot withstand the PSLRA's specific requirement that the untrue statements or omissions be set forth with particularity as to "the defendant" and

2007). Prior to the Third Circuit, "[t]he only courts of appeals to have directly addressed the survival of the group pleading doctrine post-PSLRA have abolished the doctrine." *Id.* at 336.[26] In addition to the Third and Fifth Circuit, the Seventh Circuit has abolished the group pleading doctrine,[27] the Second,[28] Fourth,[29] Eighth[30] and Eleventh Circuits[31] appear to have abolished it in whole or in part, while the First and Sixth Circuits have questioned the viability of group

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that scienter be pleaded with regard to "each act or omission" sufficient to give "rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. § 78u–4(b). These PSLRA references to "the defendant" may only reasonably be understood to mean "each defendant" in multiple defendant cases…

Therefore,…the PSLRA requires the plaintiffs to "distinguish among those they sue and enlighten *each defendant* as to his or her particular part in the alleged fraud." As such, corporate officers may not be held responsible for unattributed corporate statements solely on the basis of their titles, even if their general level of day-to-day involvement in the corporation's affairs. *Southland Sec. Corp. v. INSpire Ins. Sols., Inc.*, 365 F.3d 353, 364–65 (5th Cir. 2004).

[26] *Cf. Schwartz v. Celestial Seasonings, Inc.*, 124 F.3d 1246, 1254 (10th Cir. 1997) (pre-PSLRA finding "the identification of corporate insider defendants without matching specific misstatements with specific officers or directors does not violate Rule 9(b)."); *see In re Thornburg Mortg., Inc. Sec. Litig.*, 695 F. Supp. 2d 1165, 1197 (D.N.M. 2010), *on reconsideration in part*, 824 F. Supp. 2d 1214 (D.N.M. 2011), *aff'd sub nom. Slater v. A.G. Edwards & Sons, Inc.*, 719 F.3d 1190 (10th Cir. 2013) ("Tenth Circuit has not addressed the problem of pleading group allegations since Congress passed the PSLRA.").

[27] *See Makor Issues & Rights, Ltd. v. Tellabs Inc.*, 513 F.3d 702, 707–08 (7th Cir. 2008).

[28] *Gavin/Solmonese LLC v. D'Arnaud-Taylor*, 68 F. Supp. 3d 530, 539 (S.D.N.Y. 2014), *aff'd*, 639 F. App'x 664 (2d Cir. 2016) (affirmed based on *Janus* whereby defendants "may not be held liable for alleged misrepresentations made in the POM through the group pleading doctrine").

[29] *Teachers' Ret. Sys. Of LA v. Hunter*, 477 F.3d 162, 184 (4th Cir. 2007) ("a plaintiff must allege facts that support a 'strong inference' that each defendant acted with at least recklessness in making the false statement.").

[30] *In re Hutchinson Tech. Inc. Sec. Litig.*, 502 F. Supp. 2d 884, 901 (D. Minn. 2007), *aff'd sub nom. In re Hutchinson Tech., Inc. Sec. Litig.*, 536 F.3d 952 (8th Cir. 2008) ("hold[ing] that the group-pleading doctrine is inconsistent with the requirements of [PSLRA]." [Even if it were valid,] "it would not apply to Graczyk and Schaefer, whose job titles (vice president of business development and chief technical officer, respectively) do not on their face indicate that they bear any responsibility for contributing to or preparing corporate financial statements.")

[31] *Phillips v. Sci.-Atlanta, Inc.*, 374 F.3d 1015, 1017-18 (11th Cir. 2004) ("hold[ing] that scienter must be found with respect to each defendant and with respect to each alleged violation.").

pleading after the PSLRA but declined to decide the issue.[32]

B. Complaint Fails to Allege a Particular Material Misrepresentation by [redacted]

Plaintiff alleges in their state and federal securities law claims that the Defendants, including [redacted], violated Section 10(b) and Rule 10b-5(b) by making false statements or omissions of material fact in connection with the CAS, CASDF and CAREIC Series E Offerings. These claims fail under the Supreme Court's decision in *Janus*, which establishes that [redacted] did not "make" any of those alleged misstatements.

In *Janus*, the Supreme Court built upon a line of cases that limited the scope of primary liability in Section 10(b) actions. There, the plaintiffs sued Janus Capital Group alleging that it had assisted Janus Investment Fund in the preparation of a prospectus that contained false information. Janus, 564 U.S. at 137-40. The Court rejected the plaintiffs' attempt to impose direct liability on Janus Capital Group, finding that it did not "make" a statement within the meaning of Rule 10b-5(b) because it did not possess "ultimate authority" over the contents of the prospectus. *Id*. at 142.[33] The Supreme Court drew a "clean line" between those who have "ultimate authority" over the contents of statements, and secondary actors who merely provide

[32] *See In re Cabletron Sys., Inc.*, 311 F.3d 11, 40 (1st Cir. 2002); *City of Monroe Employees Ret. Sys. v. Bridgestone Corp*., 399 F.3d 651, 690 (6th Cir. 2005).

[33] The Court articulated the following rule: "For purposes of Rule 10b–5, the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it. Without control, a person or entity can merely suggest what to say, not "make" a statement in its own right. One who prepares or publishes a statement on behalf of another is not its maker. And in the ordinary case, attribution within a statement or implicit from surrounding circumstances is strong evidence that a statement was made by—and only by—the party to whom it is attributed. This rule might best be exemplified by the relationship between a speechwriter and a speaker. Even when a speechwriter drafts a speech, the content is entirely within the control of the person who delivers it. And it is the speaker who takes credit—or blame—for what is ultimately said." *Id*. at 142–43.

"substantial assistance." *Id*. at 143 n. 6. Imposing primary liability on those "without control over the content of a statement" would make any distinction between primary and secondary liability meaningless. *Id*.

Here, Plaintiff provides 37 paragraphs, but not a single statement or omission by [redacted]. Compl. ¶¶ 198-235. The Complaint **does not** allege that [redacted]: (i) controls any of the statements; (ii) signs off on any of CAREIC's SEC filings, (iii) "adopts the [PPMs] as [his] own statement or exercises control over its content[,]"[34] (iv) designs disclosure controls and procedures, internal controls over financial reporting, evaluates their effectiveness or discloses any changes thereof as it relates to the auditor letter, or (v) even control or maintain authority over the acquisition, analysis and reporting of CAREIC's properties and projects. Rather, Plaintiffs resort to impermissible conclusory allegations, which fall short of the bar set by *Janus*, to allege that Management (inclusive of [redacted]) "made, disseminated, approved, and/or allowed false statements or omissions of material fact in connection with investors' purchases…pursuant to the Relevant Securities Offerings." *See* Compl. ¶ 292. Such conclusory allegations are insufficient. *Ashcroft v. Iqbal*, 556 U.S. 662, 686 (2009) ("courts [need not] credit a complaint's conclusory statements without reference to its factual context"); *see Adams v. Kinder-Morgan, Inc.*, 340 F.3d 1083, 1095, 1098, *as amended on denial of reh'g* (Aug. 29, 2003) (PSLRA "strengthened what is required adequately to plead" both falsity and scienter – to allege a material misrepresentation or omission, plaintiff must allege "specific facts that support" his falsity claims.). Nor can Plaintiff survive a motion to dismiss by simply alleging [redacted] was significantly involved or assisted:

[34] *Id*. at 2305 n. 12.

> this assistance, subject to the ultimate control of [CAREIC], does not mean that [redacted] "made" any statements in the [PPMs or SEC filings]. Although [redacted], like a speechwriter, may have assisted [CAREIC] with crafting what [CAREIC] said in the prospectuses, [redacted] itself did not "make" those statements for purposes of Rule 10b–5.

Id. at 148. Further, Plaintiff's conclusory labels, improper in its own right, does not correct the defective pleading as "[n]othing in *Janus* limits its holding to legally independent third parties. The Court's interpretation applies generally, not just to corporate outsiders." *Glickenhaus & Co. v. Household Int'l, Inc.*, 787 F.3d 408, 425 (7th Cir. 2015), *reh'g denied* (July 1, 2015). "*Janus* can't be ignored simply because [redacted] is a corporate insider." *Id*. at 428. In *Glickenhaus*, the Seventh Circuit overturned a jury verdict based on jury instructions that contradicted *Janus* (and mirrored Plaintiff's "approved" allegation) where the "judge instructed the jury that the plaintiffs could prevail on their Rule 10b–5 claim if they proved that the defendant "made, *approved, or furnished information* to be included in a false statement." *Id*. at 425 (emphasis in original); *see also Universal Am. Corp. v. Partners Healthcare Sols. Holdings, L.P.*, 176 F. Supp. 3d 387, 394–95 (D. Del. 2016) (failed to allege sufficient particularity that COO, who allegedly controlled corporation, made material misrepresentations; plaintiff made no individualized allegations regarding COO's authority over any particular statement but instead lumped COO together with other officers, making only vague allegations about COO's participation in preparing certain documents.). Here, David Hunt was the securities attorney drafted the PPMs for CAREIC (as he testified thereto under oath),[35] and as discussed in the

[35] *See* Evans Decl., Ex. G at 173:3-16 (Hunt "drafted substantial portions of" confidential offering memorandum for CAOP I"); 196:11-16 ("I did—my primary focus in securities and I did securities work for them. I drafted a private placement memorandum.").

Factual Background (*see supr*a Facts §§ 4-5), [redacted] was not and could not have any such authority over Hunt (such was solely in the purview of Cochran).[36]

C. Complaint Fails to Plead a Particular Material Omission by [redacted]

Absent a duty to disclose, an omission does not give rise to a cause of action under § 10(b) and Rule 10b–5. *Basic Inc. v. Levinson*, 485 U.S. 224, 238 n. 17 (1988); *see also Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 44–45 (2011).[37] The Court noted that absent some impetus for disclosure apart from section 10(b) and Rule 10b-5, "[e]ven with respect to information that a reasonable investor might consider material, companies can control what they have to disclose under these provisions by controlling what they say to the market." *Id*. An actionable omission claim arises only when disclosure is "necessary ... to make the statements made, in light of the circumstances under which they were made, not misleading." 17 C.F.R. § 240.10b–5(b). "In other words, a duty to provide information exists only where statements were made which were misleading in light of the context surrounding the statements." *Retail Wholesale & Dep't Store Union Local 338 Ret. Fund v. Hewlett–Packard Co.*, 845 F.3d 1268, 1278 (9th Cir. 2017).

First, in addition to other pleading failures related to scienter (*see infra*), the Complaint makes conclusory allegations of what Management knew, or should of known, without any particularity, either to Management collectively, or to [redacted] individually. However, "a duty to

[36] Even assuming otherwise, Plaintiff fails to allege a particular misrepresentation or omission directly attributable to [redacted].

[37] Alternatively, such "a duty may exist 'where the law imposes special obligations, as for accountants, brokers, or other experts, depending on the circumstances of the case.'" *Rudolph v. Arthur Andersen & Co.*, 800 F.2d 1040, 1043 (11th Cir. 1986) (citations omitted); *cf.* Section II *infra* (no fiduciary relationship).

disclose under § 10(b) does not arise from the mere possession of nonpublic market information." *Chiarella v. United States*, 445 U.S. 222, 235 (1980). Rather, "[d]isclosure is required under these provisions only when necessary 'to make ... statements made, in the light of the circumstances under which they were made, not misleading.'" *Matrixx*, 563 U.S. at 44 (*quoting* 17 CFR § 240.10b–5(b)). Here, as discussed *supra*, Plaintiff fails to plead the predicate statement by [redacted] – to prevail on a § 10(b) claim, a plaintiff must show that the defendant made an affirmative statement that was "*misleading* as to a *material* fact." *Basic*, 485 U.S. at 238 (emphasis in original). Here, the claimed omissions (while devoid of particularity), generally amount to silence (or otherwise, not even an omission) – for example: (1) lack of experience (PPMs did not overstate experience, rather the only management member with any detailed real estate experience was Geringer) (*see, e.g.*, CAREIC Series E PPM at 25-29; *cf.* Compl. ¶ 204); (2) breaches of fiduciary duty (while related to pre-offering events) were disclosed (*see, e.g.*, 10-K FY 2008 at 27 (notes payable), 29 (related-party transactions), 41 (no code of ethics), 44-46 (certain relationships and related transactions); (3) devotion of time (*see, e.g.*, CAS PPM at 23 ("management devote only such time to our operations as they, in their sole discretion deem necessary to carry out our operations effectively."), 38 ("success… depends on the continuing contributions of our key personnel" that "devote only as much time to our operations as they, in their sole discretion, deem necessary in carrying or our operations effectively."); (4)" CASDF PPM fails to disclose Kingman Project was infeasible and based on irrational forecasts" Compl. ¶ 224 (*see* CASDF PPM did project or otherwise provide the "Kingman Pro Forma").[38]

[38] Further, Plaintiff faults CAREIC Management for pursuing an infeasible Kingman project due to the necessity of further funding, but then takes issue with CAREIC establishing a vehicle for

D. Plaintiff's May Not Use Scheme Liability as a Backdoor to Liability

Plaintiffs may not circumvent the necessity of pleading a material misrepresentation or omission with particularity by asserting a putative claim for "scheme liability" under Rules 10b-5 (17 C.F.R. § 240.10b-5(c)) or the state securities laws where, as here, the alleged "scheme" does not involve misconduct beyond the alleged misstatements or omissions on which Plaintiff's predicate his claims. Compl. ¶¶ 284, 294. Rather, the nature of the allegation controls:

> Instead we look to the nature of the allegations contained in the complaint, bearing in mind that the *Affiliated Ute* presumption of reliance exists in the first place to aid plaintiffs when reliance on a negative would be practically impossible to prove. Mr. Joseph's complaint essentially alleges that MiniScribe engaged in a pattern of deception which involved manipulating financial data, disseminating false information about the company, concealing the truth about the company's true financial outlook, and hiding the existence of the fraudulent scheme itself. The claims are pled in such a manner as to intertwine affirmative acts with omissions in a strained attempt to recharacterize the alleged wrongdoing….
>
> Any fraudulent scheme requires some degree of concealment, both of the truth and of the scheme itself. We cannot allow the mere fact of this concealment to transform the alleged malfeasance into an omission rather than an affirmative act. To do otherwise would permit the *Affiliated Ut*e presumption to swallow the reliance requirement almost completely.

Joseph v. Wiles, 223 F.3d 1155, 1162-63 (10th Cir. 2000); *see also Pub. Pension Fund Grp. v. KV Pharm. Co.*, 679 F.3d 972, 987 (8th Cir. 2012) (scheme liability claim in securities fraud action must be based on conduct beyond actionable misrepresentations or omissions). Thus, Plaintiff cannot adequately state a claim for "scheme liability" where, as here, the alleged "scheme" does not involve misconduct beyond the alleged misstatements on which Plaintiff's predicate their claim under Rule 10b-5(b).[39]

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funding. Compl. ¶¶ 53-60, 225. Judge Marker appropriately commented on such arguments, "what's sauce for the goose is sauce for the gander." *See* Geringer Claim Order at 20.

[39] *See* also Cal. Corp. Code § 25401 (California does not provide for scheme liability).

E. Complaint Fails to Plead Elements of Securities Fraud

First, the Complaint fails to plead facts (or any particular facts) to create a strong inference of scienter. To plead scienter, plaintiff must allege **particularized facts** that give rise to a "strong inference" that defendants acted with "a mental state embracing intent to deceive, manipulate, or defraud." 15 U.S.C. § 78u-4(b)(2); *Tellabs*, 551 U.S. at 319, 321. In the 10th Circuit, plaintiff may additionally particularized facts that defendant acted recklessly. *In re Zagg, Inc. Sec. Litig.*, 797 F.3d 1194, 1201 (10th Cir. 2015).[40] As to Plaintiff's allegation of an omission, Plaintiff "must show: '(1) the defendant knew of the potentially material fact, and (2) the defendant knew that failure to reveal the potentially material fact would likely mislead investors.'" *Id*. at 1200-01 (citations omitted). Here, Plaintiff conclusory pleads that Management, allegedly inclusive of [redacted], "acted with scienter, either with an actual intent to defraud or in reckless disregard of the truth or falsity of the statements in the above offerings." Compl. ¶¶ 285, 295. This not only fails under PSLRA and Fed. R. Civ. P. 9(b), but amounts to no more than "[g]eneralized or conclusory allegations of fraud [that] will not be sufficient." *Kinder-Morgan*, 340 F.3d at 1098. This lack of particularity **does not** "adequately puts the defendants on notice of the substance of the plaintiffs' claims," but rather, "the range, sources, and level of detail of the facts alleged demonstrate that this complaint is [] frivolous or conclusory and [does not] deserve[] to proceed to the next stage of litigation." *Id*. at 1105.

[40] *Id*. ("Recklessness in the context of securities fraud is a high bar. It is 'defined as conduct that is an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it.' Allegations of conduct that amount to negligence or even gross negligence will not suffice. Rather, it must be 'something akin to conscious disregard.'") (internal citations omitted).

Similarly, the Complaint fails to plead any alleged facts to demonstrate reliance and causation, both essential elements of a private cause of action for securities fraud. *See Stoneridge Inv. Partners*, 552 U.S. at 159. Here, as discussed above, neither scheme liability nor any rebuttable presumption applies as Plaintiff has not identified a prior misleading statement. Again, the Complaint relies on generalized and conclusory statements to such elements, rather than the heightened pleading standards under PSLRA and Fed. R. Civ. P. 9(b). *See Kinder-Morgan*, 340 F.3d at 1098. *See* Compl. ¶¶ 286-87, 296-97 (*e.g.*, "reasonably relied upon the accuracy of Management's representations."). More importantly, and a significant concern for the Court in the prosecution of this case, almost three years after being assigned the claims, **Plaintiff had yet to even interview or communicate with the investors that assigned their claims and cannot plead any such factual allegations in particularity**. *See* Evans Decl., Ex. X at 177:15-25 (Strong confirmed that neither he nor counsel had engaged in "any subsequent outreach to investors" and there was "nothing beyond the plan that has happened."). Thus, "[e]ven if it were the law that the plaintiffs, in the factual context presented here, were entitled to a presumption of reliance as to the information the defendants omitted to disclose, we conclude that the presumption vanished during the presentation of the evidence." *See Cavalier Carpets, Inc. v. Caylor*, 746 F.2d 749, 757 (11th Cir. 1984).

Further, as to the alleged breaches of fiduciary duties, while a noble attempt to revive significantly time-barred securities offerings, these alleged prior breaches, are not "in connection with" the CAS, CASDF and Series E Offerings as such amounts to omissions absent a statement otherwise. To argue otherwise, would imply that the prior offerings (such as CAK) and PPMs offered thereby, were "documents are reasonably calculated to influence investors," in the CAS,

CASDF and Series E offerings. *See S.E.C. v. Wolfson*, 539 F.3d 1249, 1262 (10th Cir. 2008). The same reason applies to the CASDF's alleged omission of the Kingman pro forma as such was not disclosed to investors therein and would necessitate sending CASDF's prospective investors copies of the CAK offering memorandum.[41]

II. COMPLAINT FAILS TO ALLEGE FACTS TO ESTABLISH CONTROL PERSON LIABILITY

"[T]to state a prima facie case of control person liability, the plaintiff must establish (1) a primary violation of the securities laws and (2) 'control' over the primary violator by the alleged controlling person." *Maher v. Durango Metals, Inc.*, 144 F.3d 1302, 1305 (10th Cir. 1998). First, the Complaint fails the first prong to allege a primary violation and should be dismissed. *City of Philadelphia v. Fleming Companies, Inc.*, 264 F.3d 1245, 1271 (10th Cir. 2001). As discussed above, the Complaint fails the first element requiring the successful pleading of a primary violation. *Kinder-Morgan*, 340 F.3d at 1108. The second element "requires that the plaintiffs plead facts from which it can be reasonably be inferred that the individual defendants were control persons. To make this showing, the plaintiffs must point to facts which indicate that the defendants had 'possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise.'" *Id*. (internal citations omitted).[42]

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[41] For similar reasons, the state securities law claims fail. *See, e.g., Wenneman v. Brown*, 49 F. Supp. 2d 1283, 1290 (D. Utah 1999) ("While the Utah Uniform Securities Act, Utah Code Ann. § 61–1–22, is modeled after the Federal Securities Exchange Act of 1934 it contains a more stringent standard for applying primary liability.").

[42] *See also Maher*, 144 F.3d at 1305 ("The SEC's definition of "control" reflects this remedial purpose: "control" is defined as "the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise." 17 C.F.R. § 230.405.").

Here, the Complaint utterly **fails to allege any facts to support that [redacted] controlled CAREIC** as its "Managing Director of Business Development, [serving as] an investor relations contact," or the value "de facto officer and member of CAREIC's Board." Compl. ¶ 28 (*See* Facts § IV). *See Adams*, 340 F.3d at 1108 ("assertion that a person was a member of a corporation's board of directors, without any allegation that the person individually exerted control or influence over the day-to-day operations of the company, does not suffice to support an allegation that the person is a control person."); *id*. at 1109 ("plaintiffs merely refer to his position within the company [as] vice president and the chief financial officer of Kinder–Morgan during the relevant period. [Normally], this would not likely be enough satisfactorily to allege control[;]…however, the two identified, actionable claims of securities fraud relate specifically to official reports of the company's financial performance[,] [where as] chief financial officer, it is reasonable to infer that McKenzie had at least indirect control over the KM's financial reporting."); *Maher*, 144 F.3d at 1305–06 ("court concludes that he has failed to plead sufficient facts establishing COM's control of Durango. Maher has not alleged that COM possessed even the power to control Durango, but rather…by virtue of its agreement with Durango, possessed only the ability to acquire that power."). The same analysis is applicable to the control person liability in Utah, Nevada and California. *See Wenneman*, 49 F. Supp. 2d at 1291 (D. Utah 1999); *Hellum v. Breyer*, 194 Cal. App. 4th 1300, 1315 n. 8 (2011);[43] Nev. Rev. Stat. Ann. § 90.860 ("construe[]…with the related federal laws and regulations.").

[43] *Id*. at 815 ("at the pleading stage, a plaintiff satisfies the control requirement by alleging facts from which an inference can be drawn that the defendant 'had the power to control the general affairs of the entity primarily liable at the time the entity violated the securities laws ... [and] had the requisite power to directly or indirectly control or influence the specific corporate policy which resulted in the primary liability.'").

III. COMPLAINT FAILS TO ALLEGE TO A FIDUCIARY RELATIONSHIP FORECLOSING ANY CLAIM FOR A BREACH OF FIDUCIARY DUTY

The Claim for breach of fiduciary duty is fatally flawed as Complaint neither alleges a fiduciary relationship nor can it. The Complaint fails to allege that [redacted] "exercise[ed] discretionary authority," let alone any "participat[ion] in management" in excess of some "'nominal' officer with no management authority."[44] *See* Facts §§ 4-5. More importantly, Plaintiff cannot establish such a fiduciary relationship – the Bankruptcy Court already decided that the Operating Agreement vests sole management and authority with Cochran (with Geringer responsible for real estate). *See* Geringer Claim Order.[45]

IV. STATE LAW CLAIMS FAIL

First, the common law fraud and negligent claims fails for similar reasons discussed above: (1) Complaint fails to plead elements with particularity under Fed. R. Civ. P. 9(b); (2) allegation that [redacted] made a representation (or otherwise, if he had a duty, omitted a material fact necessary to make a prior statement not misleading); (3) scienter (knew to be false or was reckless) or negligently; (4) to induce a particular investor/assignor to act; (5) investor/assignor reasonably relied and ignorant of falsity;[46] and (6) loss causation. *See Pace v. Parrish*, 247 P.2d 273, 274–75 (Utah 1952) (fraud); *see also Smith v. Frandsen*, 94 P.3d 919, 923 (Utah 2004) (negligent misrepresentation is a species of fraud requiring duty to disclose if an omission).

Second, the civil conspiracy and RICO claims fail as the Complaint fails to plead the

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[44] *GAB Bus. Servs., Inc. v. Lindsey & Newsom Claim Servs., Inc.*, 83 Cal. App. 4th 409, 420–21 (2000), *as modified* (Sept. 14, 2000), *as modified on denial of reh'g* (Sept. 26, 2000) *overruled on other grounds in Reeves v. Hanlon*, 33 Cal. 4th 1140 (2004).
[45] *See, e.g.* Cal. Corp. Code § 17153 (former code vesting "fiduciary duties" of manager-managed LLC with manager).
[46] *Marchese v. Nelson*, 809 F. Supp. 880, 890 (D. Utah 1993) (reliance must be justifiable).

underlying predicate fraud claims. *See Coroles v. Sabey*, 79 P.3d 974, 984 (Utah Ct. App. 2003); *Holbrook v. Master Prot. Corp.*, 883 P.2d 295, 302 (Utah Ct. App. 1994). Further, Plaintiff failed to plead with the necessary particularity as required under Fed. R. Civ. P. 9(b), but instead "plaintiff's allegations of conspiracy are entirely conclusory." *Lochhead v. Alacano*, 697 F. Supp. 406, 415 (D. Utah 1988). "Moreover, the facts set forth in the pleadings must establish not only unlawful conduct, but a pattern of unlawful activity as opposed to an isolated incident." *Holbrook*, 883 P.2d at 302. *See* Compl. ¶¶ 371-75.

Third, the Complaint fails to assert a claim for equitable relief. "It is settled in Utah that the law will not imply an equitable remedy when there is an adequate remedy at law. Moreover, when seeking an equitable remedy, a plaintiff must affirmatively show a lack of an adequate remedy at law on the face of the pleading." *Thorpe v. Washington City*, 243 P.3d 500, 507 (Utah App. 2010) (citations and internal punctuation omitted).

Fourth, the fraudulent transfer claims fail as the Complaint fails to plead factual allegations with the necessary particularity under Fed. R. Civ. P. 9(b), including facts to support fraudulent intent. *See Residential Funding Co., LLC v. Bell State Bank & Trust*, 637 F. App'x 970, 971 (8th Cir. 2016) (unpublished).[47] Further, Plaintiff's fraudulent transfer claims under § 544(b) fail as a matter of law as the limited factual allegations **assert corporate, derivative claims, not those of creditors**. "Under § 544(b), the **Trustee steps into the shoes of a hypothetical creditor** and can assert state law claims to avoid transfers (11 U.S.C. § 550 is used to recover the transfers)." *Rajala v. Gardner*, No. 14-3241, 2016 WL 4547957, at *1 (10th Cir.

[47] *See also All. Shippers Inc. v. Garcia*, No. 15-1895, 2016 WL 5340447, at *1 (2d Cir. Sept. 23, 2016) (unpublished); *see In re McGavin*, 189 F.3d 1215, 1219–20 (10th Cir. 1999).

Aug. 31, 2016) (unpublished) (emphasis added).[48] Here, Plaintiff contends that the relevant entity "made the Transfers to [redacted] as compensation," (Comp. ¶ 46), the gravamen of the wrong alleged is an injury to [CAREIC] (fraudulent transfer of its assets) which resulted incidentally in an injury to plaintiffs (diminution in the value of their ownership interest)." *PacLink Commc'ns Int'l, Inc. v. Superior Court*, 90 Cal. App. 4th 958, 965 (2001) ("constitutes an injury to the company itself[,]" not a creditor).

V. ALL CLAIMS ARE TIME-BARRED AND COMPLAINT SHOULD BE DISMISSED WITH PREJUDICE

All causes of action are time-barred as a reasonable, diligent plaintiff would have discovered the facts constituting the alleged material misrepresentation or omission, conspiracy or scheme or fraudulent transfer on review of the PPMs and public filings referenced in the PPMs, or on or around April 2, 2007 (or no later than April 14, 2008), based on the disclosure in CAREIC's public reporting with the SEC. *See* Facts § I. While the Complaint utterly fails to put [redacted], or any defendant, on notice of the claims brought against him, including not only pleading with the necessary particularity required under Fed. R. Civ. P. 9(b), or the heightened pleading standards of PSLRA for federal securities claims, the Complaint takes it one step further by refusing to identify the assigning investors or even one creditor represented.[49] Plaintiff's concealment of the assigning investors not only documents the Complaint's failure to

[48] "Accordingly, we hold that a party has standing as a creditor under [the UFTA] if the party has a right to payment from the debtor." *Rupp v. Moffo*, 358 P.3d 1060, 1063 (Utah 2015).
[49] "Before asserting applicable state law, however, the trustee "must first show that there is an actual creditor holding an allowable unsecured claim ... who, under [state] law, could avoid the transfers in question…In other words, '[i]f there are not creditors within the terms of section 544(b) against whom the transfer is voidable under the applicable law, the trustee is powerless to act so far as section 544(b) is concerned.'" *Sender v. Simon*, 84 F.3d 1299, 1304 (10th Cir. 1996)

satisfy the required pleading standards, but also impedes efficient resolution of the matter.

Claim	Statute of Limitations	Expiration Date
Breach of Fiduciary Duty	4 years after alleged breach (no tolling) Utah Code Ann. § 78B-2-307(3)	June 15, 2011 (end of employment)[50]
Violation of Utah Securities Law (Utah Code Ann. § 61-1-22)	Earlier of: (i) 2 years after discovery of violation (or when reasonable person would have discovered) or 4 years after the violation occurred. Utah Code Ann. § 61-1-22(7)(a)[51]	April 2, 2009
Violation of California Securities Law (Cal. Corp. Code § 25504)	Earlier of: (i) 2 years after discovery of violation (or when reasonable person would have discovered) or 5 years after the violation occurred. Cal. Corp. Code § 25506(b)	April 2, 2009
Violation of Nevada Securities Law (Nev. Rev. Stat. Ann. § 90.660)	Earlier of: (i) 2 years after discovery of violation (or when reasonable person would have discovered) or 5 years after the violation occurred. Nev. Rev. Stat. Ann. § 90.670	April 2, 2009
Securities Fraud under Section 10(b) and Rule 10b-5 (15 U.S.C.A. § 78j(b); 17 C.F.R. § 240.10b–5(b))	Earlier of: (i) 2 years after discovery of violation (or when reasonable person would have discovered) or 5 years after the violation occurred. 28 U.S.C.A. § 1658(b)	April 2, 2009
Control Person Liability Under Section 20(a) of the Exchange Act of 1934 (15 U.S.C.A. § 78t(a))	Earlier of: (i) 2 years after discovery of violation (or when reasonable person would have discovered) or 5 years after the violation occurred. 28 U.S.C.A. § 1658(b)	April 2, 2009

[50] "Statute of limitations for breach of fiduciary duty…does not" contain a tolling provision. *Allred ex rel. Jensen v. Allred*, 182 P.3d 337, 345 (Utah 2008). *See also* Cal. Civ. Proc. Code § 343 (4 years); *WA Sw. 2, LLC v. First Am. Title Ins. Co.*, 240 Cal. App. 4th 148, 157-158 (2015), *reh'g denied* (Sept. 24, 2015), *review denied* (Nov. 18, 2015) ("Reasonable diligence in such circumstances does not consist of ignoring a private placement memorandum received prior to making an investment…The information and disclosures in the [PPM] put plaintiffs on notice of the falsity of any communications they may have received…delayed discovery rule does not apply… plaintiffs failed in their effort to plead the applicability of the delayed discovery rule.").

[51] Prior version of code (amended to 2/5 years effective May 12, 2009).

Common Law Fraud	3 years Utah Code Ann. § 78B-2-305(3)[52]	April 2, 2010
Negligent Misrepresentation	4 years after alleged misrepresentation or omission (no tolling) Utah Code Ann. § 78B-2-307(3); *see DOIT, Inc. v. Touche, Ross & Co.*, 926 P.2d 835, 842 (Utah 1996)	April 2, 2011[53]
Civil Conspiracy	4 years after alleged occurrence of conspiracy (no tolling) Utah Code Ann. § 78B-2-307(3); *see DOIT*, 926 at 842	April 2, 2011[54]
Utah RICO Violation (Utah Code Ann. § 76-10-1605(1)-(2))	3 years Utah Code Ann. § 76-10-1605(9)	April 2, 2010
Nevada RICO Violation (Nev. Rev. Stat. Ann. § 207.470)	5 years Nev. Rev. Stat. Ann. § 207.520 (West)	April 2, 2012
California RICO Violation[55]	**NO CIVIL ACTION**	
Avoidance of Fraudulent Transfers Under 11 U.S.C. § 544(b) and Utah Code Ann. §§ 25-6-5(1)(a); 25-6-5(1)(b); 25-6-5-6(1) and 25-6-8)	4 years after the transfer made or obligation incurred Utah Code Ann. § 25-6-10(1)	July 28, 2013 (last transfer listed on Exhibit 5 to Complaint)
Recovery of Avoided Transfers Under 11 U.S.C. §§ 550 and 551.	Earlier of (1) one year after the avoidance of the transfer on account of which recovery is sought or (2) the time the case is closed or dismissed. 11 U.S.C.A. § 550(f)	Not applicable if 11 U.S.C. § 544(b) claims are barred. Otherwise, one year after transfers are avoided.

[52] *See also* Cal. Civ. Proc. Code § 338(d) (3 years); *see supra* fn. 50 (discovery rule inapplicable).

[53] *See also* Cal. Civ. Proc. Code § 339 (2 years); *see supra* fn. 50 (discovery rule inapplicable).

[54] In California, "no cause of action exists for conspiracy, per se. Whether or not a cause of action for conspiracy is timely must be determined by reference to the statute of limitations applicable to the underlying cause of action." *Filmservice Labs., Inc. v. Harvey Bernhard Enterprises, Inc.*, 208 Cal. App. 3d 1297, 1309 (Ct. App. 1989).

[55] The Complaint is styled under the assumption that Utah law applies. [redacted] does not concede that Utah law applies to this case and reserves the right to contend that the case be governed by California law and has included citations where the relevant statute of limitations differs. Irrespective of whether Utah or California law applies, the Claims are time-barred.

Constructive Trust	4 years after alleged unlawful conduct (no tolling) Utah Code Ann. § 78B-2-307(3); *see DOIT*, 926 at 842	July 28, 2013[56]
Unjust Enrichment and Disgorgement	4 years after alleged unjust enrichment (no tolling) Utah Code Ann. § 78B-2-307(3); *see DOIT*, 926 at 842	July 28, 2013[57] (last transfer listed on Exhibit 5 to Complaint)

A. Invalidity, Avoidance and Unenforceability of Tolling Agreement

As provided above, any tolling agreement would not revive the statute of limitations. However, in any event, the tolling agreement should be rescinded or found invalid as a result of undue influence/undue advantage, duress or illegality (*See* Facts § III).

> Undue influence…involves an application of excessive strength by a dominant subject against a servient object…the same legal consequences should apply to the results of excessive strength as to the results of undue weakness. Whether from weakness on one side, or strength on the other, or a combination of the two, undue influence occurs whenever there results "that kind of influence or supremacy of one mind over another by which that other is prevented from acting according to his own wish or judgment, and whereby the will of the person is over-borne and he is induced to do or forbear to do an act which he would not do, or would do, if left to act freely." Undue influence involves a type of mismatch which our statute calls unfair advantage…If will has been overcome against judgment, consent may be rescinded. *Odorizzi v. Bloomfield Sch. Dist.*, 246 Cal. App. 2d 123, 132 (Ct. App. 1966)

Further, the coercion and pressure to execute the tolling agreement (and proposing a course of conduct) arguably violates ethics rules making it invalid, such as Rule 4.3 of the Utah Rules of Professional Conduct and Rule 5-100 of the California Rules of Professional Conduct.

[56] *See also* Cal. Civ. Proc. Code § 338(d) (3 years); *see F.D.I.C. v. Dintino*, 167 Cal. App. 4th 333, 348 (2008); *see supra* fn. 50 (discovery rule inapplicable).
[57] *See also* Cal. Civ. Proc. Code § 338(d) (3 years); *see F.D.I.C.*, 167 Cal. App. 4th at 348; *see supra* fn. 50 (discovery rule inapplicable).

CONCLUSION

For the foregoing reasons, [redacted] respectfully request that the Court grant his motion and dismiss the Complaint and grant any such other and further relief as this Court deems just and proper.[58]

EVANS & KOB, PC

DATED: March 31, 2017

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-and-

[redacted]

[58] Based on the limited information [redacted] has on the signatories to the Amended Operating Agreement of CAREIC, he reserves its right to compel arbitration should further details evolve regarding agreements to arbitrate.

CERTIFICATE OF SERVICE

I hereby certify that on March 31, 2017, I electronically filed the foregoing with the Clerk of Court using the CM/ECF system, which sent notification of such filing to the following:

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and I hereby certify that I have mailed the document by United States Mail, first-class postage prepaid, to the following non-CM/ECF participants:

(No manual recipients)

/s/ Brett G. Evans