

Hunter v. Citibank, N.A.

NO. C 09-02079 JW

**UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF
CALIFORNIA, SAN JOSE DIVISION**

2010 U.S. Dist. LEXIS 61912

February 3, 2010, Decided

February 3, 2010, Filed

OPINION**ORDER GRANTING IN PART AND DENYING IN
PART DEFENDANTS' VARIOUS MOTIONS TO
DISMISS**

Presently before the Court are (1) Defendant United Western Bank's ("UWB") Motion to Dismiss Amended Complaint,¹ (2) Defendant Citibank's Motion to Dismiss,² (3) Cordell Defendants' Motion to Dismiss the Complaint;³ (4) Defendant Silicon Valley Law Group's ("SVLG") Motion to Dismiss Plaintiffs' Complaint,⁴ (5) Defendant Jordan Burt LLP's ("Jordan Burt") Motion [*5] to Dismiss Plaintiffs' Amended Complaint,⁵ and (6) Defendants Kutak Rock LLP and Joseph O. Kavan's (collectively, "Kutak Rock") Motion to Dismiss Amended Complaint and Motion to Strike.⁶ The Court finds it appropriate to take the Motions under submission without oral argument. See Civ. L.R. 7-1(b). Based on the papers submitted to date, the Court GRANTS Defendants UWB and Citibank's Motions with leave to amend, DENIES Cordell Defendants' Motion, and GRANTS in part and DENIES in part Lawyer Defendants' Motions.

1 (hereafter, "UWB's Motion," Docket Item No. 131.)

2 (hereafter, "Citibank's Motion," Docket Item No. 132.)

3 (hereafter, "Cordell's Motion," Docket Item No. 168.)

4 (hereafter, "SVLG's Motion," Docket Item No. 136.)

5 (hereafter, "Jordan Burt's Motion," Docket Item No. 190.)

6 (hereafter, "Kutak Rock's Motion," Docket Item No. 195.) Defendants SVLG, Jordan Burt, and Kutak Rock are collectively referred to in this Order as "Lawyer Defendants."

A. Background

In an Amended Complaint filed May 14, 2009,⁷ Plaintiffs allege as follows:

Qualified Intermediaries ("QIs") were established for the purpose of holding funds in trust during the process of carrying out a property exchange pursuant to [*6] 26 C.F.R. § 1.1031(k)-1 ("1031 Exchange"). (AC PP 40-41.) 1031 Exchanges permit deferred capital gains tax for like-kind transfers of property if the seller does not take possession or control of sale proceeds at any time prior to completing the property exchange. (Id.)

In 2005, Edward Okun ("Okun") purchased six QIs and formed a parent corporation, the 1031 Tax Group, as to the other six QIs. (AC P 2.) He gained access to the Exchange Funds held in trust in each QI and appropriated most of those funds to his own use. (Id.) Okun concealed his theft by using incoming deposits of new Exchange Funds to fund older escrows at the various QIs. (Id.) Okun operated a Ponzi scheme which was exposed when the real estate market cooled, and the infusion of new funds slowed, imposing a de facto audit. (Id.) On May 14, 2007, the QIs filed for Chapter 11 bankruptcy, and a Trustee was appointed on October 26, 2007. (Id.) On March 19, 2009, a jury convicted Okun on twenty-three counts. (Id. P 5.)

Plaintiffs executed Exchange Agreements with their respective QIs, which provided that Exchange Funds deposited with each QI upon the sale of relinquished property would be held in trust on deposit in an insured [*7] bank or national de-

pository institution, and used solely to fund the purchase of replacement property identified by the specific depositor. (AC P 6.) Okun's looting of funds created deficits in the trust account at each QI. (Id.) Okun's plan required the participation of banks, "hard money" lenders, and lawyers who actively assisted Okun in committing these crimes, aiding and abetting his breach of fiduciary duties owed to Plaintiffs. (Id. P 5.)

7 (hereafter, "AC," Docket Item No. 3.)

On the basis of the allegations outlined above, Plaintiffs allege eight causes of action: (1) Conversion; (2) Aiding and Abetting a Conversion; (3) Breach of Fiduciary Duty; (4) Aiding and Abetting a Breach of Fiduciary Duty; (5) Aiding and Abetting Fraud; (6) Conspiracy to Convert Exchange Funds and Commit Fraud; (7) Intentional Interference with Contract; (8) Breach of Contract; (9) Negligence; and (10) Negligent Supervision.

B. Standards

Pursuant to Federal Rule of Civil Procedure 12(b)(6), a complaint may be dismissed against a defendant for failure to state a claim upon which relief may be granted against that defendant. Dismissal may be based on either the lack of a cognizable legal theory or the absence [*8] of sufficient facts alleged under a cognizable legal theory. *Balistreri v. Pacifica Police Dept.*, 901 F.2d 696, 699 (9th Cir. 1990); *Robertson v. Dean Witter Reynolds, Inc.*, 749 F.2d 530, 533-34 (9th Cir. 1984). For purposes of evaluating a motion to dismiss, the court "must presume all factual allegations of the complaint to be true and draw all reasonable inferences in favor of the nonmoving party." *Usher v. City of Los Angeles*, 828 F.2d 556, 561 (9th Cir. 1987). Any existing ambiguities must be resolved in favor of the pleading. *Walling v. Beverly Enters.*, 476 F.2d 393, 396 (9th Cir. 1973).

However, mere conclusions couched in factual allegations are not sufficient to state a cause of action. *Papasan v. Allain*, 478 U.S. 265, 286, 106 S. Ct. 2932, 92 L. Ed. 2d 209 (1986); see also *McGlinchy v. Shell Chem. Co.*, 845 F.2d 802, 810 (9th Cir. 1988). The complaint must plead "enough facts to state a claim for relief that is plausible on its face." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570, 127 S. Ct. 1955, 167 L. Ed. 2d 929 (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*, 129 S. Ct.

1937, 1949, 173 L. Ed. 2d 868 (2009). [*9] Thus, "for a complaint to survive a motion to dismiss, the non-conclusory 'factual content,' and reasonable inferences from that content, must be plausibly suggestive of a claim entitling the plaintiff to relief." *Moss v. U.S. Secret Serv.*, 572 F.3d 962, 969 (9th Cir. 2009). Courts may dismiss a case without leave to amend if the plaintiff is unable to cure the defect by amendment. *Lopez v. Smith*, 203 F.3d 1122, 1129 (9th Cir. 2000).

C. Bank and Hard Money Lender Defendants' Motions

1. Defendants UWB and Citibank's Motions to Dismiss

Defendants UWB and Citibank move to dismiss the Amended Complaint, *inter alia*, on the ground that UCC Article 4A provides the exclusive source of any remedies for claims arising out of unauthorized funds transfers. (UWB's Motion at 8; Citibank's Motion at 4.)

a. Colorado and New York Statutory Provisions Adopting UCC Article 4A

As a preliminary matter, the Court considers which state law governs Plaintiffs' claims against the Defendant banks.

"In a diversity case, the district court must apply the choice-of-law rules of the state in which it sits." *Abogados v. AT&T, Inc.*, 223 F.3d 932, 934 (9th Cir. 2000) (citing *Klaxon Co. v. Stentor Elec. Mfg. Co.*, 313 U.S. 487, 496, 61 S. Ct. 1020, 85 L. Ed. 1477 (1941)). [*10] "California applies a three-step 'governmental interest' analysis to choice-of-law questions." *Id.* The parties do not dispute that under the governmental interest test, Colorado law applies to Plaintiffs' claims against UWB, * and New York law applies to Plaintiffs' claims against Citibank. "

8 (See UWB's Motion at 8 n.1; Opposition to UWB's Motion to Dismiss Amended Complaint at 5-9, hereafter, "UWB's Opp'n," Docket Item No. 236.)

9 (See Citibank's Motion at 5 n.2; Opposition to Citibank's Motion to Dismiss at 5-12, hereafter, "Citibank's Opp'n," Docket Item No. 211.)

Colorado and New York have both adopted Article 4A of the UCC, which governs electronic funds transfers. See *Colo. Rev. Stat. Ann.* § 4-4.5-202; *N.Y. U.C.C. art. 4-A*. The applicable provisions of both states define a "funds transfer" as "the series of transactions, beginning with the originator's payment order, made for the purpose of making payment to the beneficiary of the order. The term includes any payment order issued by the originator's bank or an intermediary bank intended to carry out

the originator's payment order." Colo. Rev. Stat. Ann. § 4-4.5-104(a); N.Y. U.C.C. § 4-A-104.

Both states' provisions governing "authorized [*11] and verified payment orders" provide:

(a) A payment order received by the receiving bank is the authorized order of the person identified as sender if that person authorized the order or is otherwise bound by it under the law of agency.

(b) If a bank and its customer have agreed that the authenticity of payment orders issued to the bank in the name of the customer as sender will be verified pursuant to a security procedure, a payment order received by the receiving bank is effective as the order of the customer, whether or not authorized, if (i) the security procedure is a commercially reasonable method of providing security against unauthorized payment orders, and (ii) the bank proves that it accepted the payment order in good faith and in compliance with the security procedure and any written agreement or instruction of the customer restricting acceptance of payment orders issued in the name of the customer.

Colo. Rev. Stat. Ann. § 4-4.5-202;
N.Y. U.C.C. § 4-A-202.

Finally, both states have adopted the provision of Article 4A which imposes a one-year notice requirement on claims that a bank is not entitled to retain a payment order:

If a receiving bank has received payment from its customer [*12] with respect to a payment order issued in the name of the customer as sender and accepted by the bank, and the customer received notification reasonably identifying the order, the customer is precluded from asserting that the bank is not entitled to retain the payment unless the customer notifies the bank of the customer's objection to the payment within one year after the notification was received by the customer.

Colo. Rev. Stat. Ann. § 4-4.5-505;
N.Y. U.C.C. § 4-A-505.

b. Preemption of Common Law Claims

Since the Colorado and New York state legislatures have both adopted UCC Article 4A, the issue becomes whether that Article preempts common law claims involving funds transfers.

Under Colorado law, a UCC provision preempts a common law cause of action "whenever both the code and the common law would provide a means of recovery for the same loss." *Clancy Sys. Int'l, Inc. v. Salazar*, 177 P.3d 1235, 1237 (Colo. 2008). Colorado law allows "the code to abrogate common law rules without requiring unequivocal, explicit reference to the common law in each statutory section that effects a modification." *Id.*

Similarly, New York courts have recognized that UCC Article 4A preempts some common law [*13] claims arising out of electronic funds transfers. In *Aleo Int'l, Ltd. V. Citibank, N.A.*, the court stated:

The Comment to UCC 4-A-102 states that the provisions of article 4-A "are intended to be the exclusive means of determining the rights, duties and liabilities of the affected parties in any situation covered by particular provisions of the article. Consequently, resort to principles of law or equity outside of Article 4A is not appropriate to create rights, duties and liabilities inconsistent with those stated in this Article."

160 Misc. 2d 950, 612 N.Y.S.2d 540, 541 (N.Y. Supr. 1994) (quoting the Official Comment to UCC § 4A-102 (N.Y. U.C.C. § 4-A-102)); see also *ReAmerica, S.A. v. Wells Fargo Bank Int'l*, 577 F.3d 102, 106 (2d Cir. 2009) ("Article 4A 'precludes common law claims when such claims would impose liability inconsistent with the rights and liabilities expressly created by Article 4-A.'").

The policy underlying UCC Article 4A supports broad preemption of related common law causes of action. The Court of Appeals of New York stated:

National uniformity in the treatment of electronic fund transfers is an important goal, as are speed, efficiency, certainty (i.e., to enable participants in fund [*14] transfers to have better understanding of their rights and liabilities), and finality. Establishing finality in electronic fund wire transactions was considered a singularly important policy goal.

Banque Worms v. BankAmerica Int'l, 77 N.Y.2d 362, 372, 570 N.E.2d 189, 568 N.Y.S.2d 541 (N.Y. 1991). The Supreme Court of California has described the underlying policy goals of UCC Article 4A in similar terms:¹⁰

[UCC Article 4A] provide[s] a detailed scheme for analyzing the rights, duties and liabilities of banks and their customers in connection with the authorization and verification of payment orders. Analysis of a funds transfer under these sections results in a determination of whether or not the funds transfer was "authorized," and provides a very specific scheme for allocation of loss.

Zengen, Inc. v. Comerica Bank, 41 Cal. 4th 239, 251-52, 59 Cal. Rptr. 3d 240, 158 P.3d 800 (Cal. 2007). The Zengen court went on to quote extensively from the UCC Comment to section 4A-102, which states in pertinent part:

In the drafting of Article 4A, a deliberate decision was made to write on a clean slate and to treat a funds transfer as a unique method of payment to be governed by unique rules that address the particular issues raised by this method of payment. A deliberate [*15] decision was also made to use precise and detailed rules to assign responsibility, define behavioral norms, allocate risks and establish limits on liability, rather than to rely on broadly stated, flexible principles. In the drafting of these rules, a critical consideration was that the various parties to funds transfers need to be able to predict risk with certainty, to insure against risk, to adjust operational and security procedures, and to price funds transfer services appropriately. This consideration is particularly important given the very large amounts of money that are involved in funds transfers.

Funds transfers involve competing interests--those of the banks that provide funds transfer services and the commercial and financial organizations that use the services, as well as the public interest. These competing interests were represented in the drafting process and they were thoroughly considered. The rules that emerged represent a careful and delicate balancing of those interests and are intended to be the exclusive means of de-

termining the rights, duties and liabilities of the affected parties in any situation covered by particular provisions of the Article.

Id.

10 While the [*16] Court recognizes that California law does not govern the issue of whether UCC Article 4A preempts Plaintiffs' common law claims here, the Court relies on Zengen only to the extent that it provides a useful analysis of the policy considerations underlying Article 4A.

Article 4A's displacement of common law causes of action, however, is not complete. "The exclusivity of Article 4-A is deliberately restricted to 'any situation covered by particular provisions of the Article.' Conversely, situations not covered are not the exclusive province of the Article." *Sheerbonnet, Ltd. v. American Express Bank, Ltd.*, 951 F. Supp. 403, 407-08 (S.D.N.Y. 1996).

c. Application of Article 4A

At issue is whether the situation presented here is covered by the particular provisions of Article 4A.

Here, in relation to their claims against Defendant UWB, Plaintiffs allege in pertinent part:

Investment Exchange Group ("IXG"), a QI for 1031 exchanges, deposited, \$ 75 million in exchange funds at UWB. In August 2006, IXG informed Judy Thornton, an institutional sales employee at UWB who had researched 1031 exchanges and investigated the proper protocol for treatment of QI funds by a bank, that Okun was acquiring [*17] shares of IXG and would transfer the IXG exchange funds on deposit to the 1031 Tax Group account at Wachovia. (AC PP 100, 102.) UWB agreed to this proposal, notwithstanding the fact that UWB knew that IXG held exchange funds in trust for the benefit of each QI exchanger in accounts established at UWB, that IXG's duties to the IXG exchanges were non-delegable, and that IXG, as Trustee, could transfer exchange funds only to an exchanger holding an exchange account at IXG. (Id. P 102.)

Beginning in August 2006, after the sale of IXG shares to Okun's 1031 Tax Group, UWB began transferring exchange

funds from IXG accounts at UWB to accounts at other financial institutions owned by entities other than IXG. (AC P 103.) Included were transfers of over \$ 80,000,000 from the IXG Omnibus Custodial Account held at UWB to 1031 Tax Group's pooled account at Wachovia where the money then disappeared. (Id.)

Pursuant to its Anti-Money Laundering Program, UWB monitored the transfers of exchange funds out of the IXG Omnibus Custodial Account to ensure the wire transfers to third parties were not suspicious. (AC P 104.) In August 2006, UWB designated IXG as a "high risk account," but nevertheless approved [*18] multiple wire transfers from IXG to the 1031 Tax Group. (Id. P 105.) UWB approved these transfers knowing that they were not used to close escrows of any of the known exchangers doing business at IXG. (Id. P 106.) These transfers substantially depleted the account. (Id.)

With regard to their claims against Defendant Citibank, Plaintiffs allege in pertinent part:

Security 1031 Services, LLC ("SOS") was a QI that deposited its funds at Citibank. (AC P 44.) Citibank knew that SOS was under a legal duty to act as a fiduciary to each exchanger doing business at SOS. Citibank also knew that SOS's deposits at Citibank were the legal property of each exchanger to be held in trust, subject to the obligations provided by the Exchange Agreements executed with SOS. (Id.) Citibank knew that exchange funds could not be loaned, borrowed, or used for any purpose other than funding the replacement property identified by the QI exchanger client. (Id.)

Okun acquired SOS on November 15, 2005. (AC P 47.) In late January and February 2006, Okun ordered Todd Pajonas, the former owner of SOS and newly named President of AEC Exchange Company, LLC ("AEC"), another of Okun's recently acquired QIs, to transfer SOS [*19] exchange funds on deposit at Citibank to Bank of America to close AEC escrows. (Id. PP 50-51.) The SOS exchange funds were then disbursed to wait-

ing AEC exchangers in order to conceal Okun's past looting of AEC exchange funds. (Id. P 52.) Citibank knew that these transfers contravened the terms of Exchange Agreements and the rights of SOS QI exchangers with accounts held at Citibank, but nonetheless cooperated in this transfer willingly. (Id.)

The gravamen of Plaintiffs' Complaint is that both UWB and Citibank allowed Okun to transfer exchange funds in a manner that violated the Exchange Agreements between the QIs and their exchanger clients. Knowing that the requested wire transfers violated those Exchange Agreements, and otherwise had at least the appearance of impropriety, Plaintiffs essentially contend that the Defendant banks should have further investigated the circumstances of the transfers and refused to execute them. Refusing to execute a wire transfer because of a belief or suspicion that it would violate the Exchange Agreement or constitute a breach of fiduciary duty amounts to a determination that the wire transfer was unauthorized. Thus, the Court finds that the circumstances [*20] that gave rise to Plaintiffs' claims against UWB and Citibank fall under the purview of UCC Article 4A.

Plaintiffs contend that the situation here is not covered under Article 4A on the grounds that (1) Article 4A only establishes the duties and liabilities of the parties to a funds transfer, and thus its provisions do not apply to Plaintiffs who are third parties, and (2) Plaintiffs do not allege that the funds transfers were not authorized, but instead contend that the banks' failure to intervene, despite the fact that the QI owner requested the transactions, should subject them to liability. ¹¹ The Court finds both contentions unpersuasive.

11 (UWB's Opp'n at 7; Citibank's Opp'n at 10.)

First, although Article 4A does not explicitly place any rights or obligations on third parties, it does squarely define the bank's liability stemming from an unauthorized funds transfer. Article 4A encourages quick and inexpensive wire transfers, and in turn facilitates the voluminous daily financial transactions upon which the nation's economy depends, by setting out a definite set of requirements for banks to adhere to when engaging in such wire transfers. Subjecting banks to liability to third parties [*21] in spite of their adherence to the provisions of Article 4A would severely undermine the important policy goals underlying its enactment. Furthermore, none of the cases that Plaintiffs cite hold that Article 4A does not preclude common law claims brought by non-parties to the wire transfer. For example, Plaintiffs rely on Ban-

que Worms for the proposition that Article 4A "define[s] the rights and liabilities of all parties involved in [a wire transfer]." (See Citibank's Opp'n at 7.) By defining the respective duties and liabilities of the parties to the transaction, however, Article 4A will inherently also affect the rights of third parties to bring suit based on claims arising out of the transaction.

Second, merely labeling the transaction "authorized" does not remove it from Article 4A's purview. In fact, Plaintiffs' admission that IXG "was an 'authorized person' to submit wire instructions to [UWB]" appears to preclude rather than establish UWB's liability for executing the requested wire transfers. (UWB's Opp'n at 7.) Given the broad policy goals enunciated by the drafters of Article 4A in its Official Comments, the Court declines to take the narrow view that Section 202 is only [*22] intended to specifically address situations in which one party claims a transaction was unauthorized. Were that the case, a litigant would only have to plead that the transaction was in fact authorized to avoid coverage under Article 4A.

Accordingly, the Court finds that UCC Section 4A covers the facts as alleged in Plaintiffs' Complaint, and thus Plaintiffs' common law claims are preempted.

d. Sufficiency of Plaintiffs' Claim Under Article 4A

Upon review, the Court finds that Plaintiffs do not allege any facts that would establish liability under Article 4A, such as an unauthorized wire transfer or the lack of commercially reasonable security measures. Furthermore, Plaintiffs have not alleged that they notified the receiving bank of any objection to the payment within one year of receiving notification of the transfer, as required under Section 505. Thus, the Court finds that Plaintiffs have not alleged sufficient facts to state a claim under UCC Article 4A.

Accordingly, the Court GRANTS Defendants' Motions to Dismiss with leave to amend.

2. Cordell Defendants' Motion to Dismiss

The Cordell Defendants¹² move to dismiss on the ground that all Plaintiffs' claims against them are barred by [*23] an injunction order of the United States Bankruptcy Court for the Southern District of New York ("Bankruptcy Court"). (Cordell's Motion at 6.)

¹² The Cordell Defendants are Cordell Funding, LLLP, Cordell Consultants, Inc., Cordell Money Purchase Plan, Cordell Consultants New York, LLC, and Robin Rodriguez. Plaintiffs allege that Cordell is a "hard money" lender, specializing in asset based lending, where higher rates of interest

are charged relative to loans based on cash flow. (AC P 138.)

On December 1, 2008, the Bankruptcy Court approved a Settlement Agreement between the Cordell Defendants and the chapter 11 trustee and issued a channelling injunction which provided, in pertinent part:

[A]ll persons or entities, who have held, hold or may hold claims against or interests in the estates of the 1031 Debtors and [Investment Properties of America LLC ("IPofA")] Debtors are permanently enjoined from (i) commencing, conducting or continuing in any manner, directly or indirectly, and suit, action, cause of action or other proceeding of any kind . . . against or affecting the Cordell Parties or the Collateral on account of or respecting any claim, interest, obligation, debt, right, cause of [*24] action, remedy or liability discharged, released, to be released, governed by or relating to the Settlement Agreement that is based upon or derivative of any claim or cause of action that could have been asserted against the Cordell Parties by, or injury to, the estates of the 1031 Debtors and/or the IPofA Debtors.¹³

¹³ (December 1, 2008 Bankruptcy Court Order P 2, Cordell Defendants' Request for Judicial Notice in Support of Motion to Dismiss the Complaint, Ex. A, Docket Item No. 169.) Since the Bankruptcy Court Order is "capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned," the Court GRANTS Cordell Defendants' Request for Judicial Notice as to that document. See Fed. R. Evid. 201(b).

Under the express terms of the injunction, only actions that are based upon or derivative of claims that could have been asserted by the Debtors are barred. Thus, the issue becomes whether the Trustee could have asserted Plaintiffs' claims against the Cordell Defendants for damages due to their loss of exchange funds.

"It is well settled that a bankruptcy trustee has no standing generally to sue third parties on behalf of the estate's creditors, [*25] but may only assert claims held by the bankrupt corporation itself." *Smith v. Arthur Andersen LLP*, 421 F.3d 989, 1002-03 (9th Cir. 2005) (in-

ternal citations omitted). The Ninth Circuit has explained that:

Although the line between "claims of the debtor," which a trustee has statutory authority to assert, and "claims of creditors," which Caplin bars the trustee from pursuing, is not always clear, the focus of the inquiry is on whether the Trustee is seeking to redress injuries to the debtor itself caused by the defendants' alleged conduct. If the debtor suffered an injury, the trustee has standing to pursue a claim seeking to rectify such injury. But, "[w]hen a third party has injured not the bankrupt corporation itself but a creditor of that corporation, the trustee in bankruptcy cannot bring suit against the third party."

Id.

Similarly, Bankruptcy Judge Glenn recognized these basic principles of bankruptcy law when he found, in an order dismissing the complaint in an adversary proceeding filed by the Trustee against Citibank, that:

[T]he Trustee does not have constitutional standing to recover damages for injuries that are particular to creditors. Specifically, the Trustee does not have [*26] constitutional standing to recover . . . money lost by the 1031 Debtor's exchange participants who were waiting to complete their 1031 exchange transactions when Okun looted funds from the Citibank bank accounts.

....

[T]he Trustee has constitutional standing to recover funds belonging to the 1031 Debtors that Citibank allegedly aided and abetted Okun in looting, to the extent this alleged injury is separate from the injury to the creditors. For example, even if the exchange participants own the claims against Citibank for loss of their Exchange Deposits, the Debtors have constitutional standing to assert claims against Citibank to the extent the looted funds belonged to the Debtors as a result of revenue earned from exchange transactions.¹⁴

14 (Opinion and Order Granting Motion to Dismiss with Leave to Amend at 20, 24, Request for Judicial Notice in Support of Plaintiffs' Opposition to Cordell's Motion to Dismiss, Ex. 2, Docket Item No. 217.) Since the Bankruptcy Court Order is "capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned," the Court GRANTS Plaintiffs' Request for Judicial Notice as to that document. See Fed. R. Evid. 201(b). [*27] For the same reason, the Court GRANTS Defendants Kutak Rock, LLP and Joseph O. Kavan's Request for Judicial Notice. (Docket Item No. 250.)

Here, Plaintiffs allege in pertinent part:

Over the course of thirteen months, Cordell made five separate loans to Okun and Okun Entities, and ultimately loaned them more than \$ 50,000,000. (AC P 140.) The Cordell loans to Okun formed a large part of the Cordell loan portfolio, and these loans assisted Okun and his co-conspirators in perpetuating Okun's Ponzi scheme. (Id.) Okun's purpose was to withdraw equity from real estate through refinancing in order to make payments owed to pending QI exchangers. Okun's intention was communicated to Cordell, which assisted Okun in effectuating this purpose for Cordell's own individual advantage and significant financial gain. (Id.)

The Court finds the reasoning that Judge Glenn applied to find that the Trustee could not bring an action to recover from Citibank for the loss of their exchange funds applies with equal force to a hypothetical Trustee suit against the Cordell Defendants. Although the Trustee has standing to bring a claim against the Cordell Defendants for aiding abetting Okun's looting of exchange [*28] funds to the extent that he seeks to recover revenue the QIs would have earned as a result of the transactions, the Trustee cannot bring suit to recover the lost exchange funds. Thus, the Court finds that the claims against the Cordell Defendants seeking to recover the lost exchange funds belong exclusively to the exchanger Plaintiffs, and are not barred by the channeling injunction.

The Cordell Defendants contend that allowing the Plaintiffs to proceed with their claims would upset the final orders of the Bankruptcy Court and potentially call into question the enforceability of all injunctions entered into under the Reorganization Plan.¹⁵ The Cordell Defendants further present the Trustee's testimony from the Bankruptcy Court's proceedings that in entering into the channeling injunction, they did not intend to leave themselves open to "lawsuits with individual exchangers."¹⁶ However, the Court finds that the plain language of the Settlement Agreement and Bankruptcy Court Order do not give the channeling injunction as broad a scope as the Cordell Defendants would like to give it. Specifically, the Order does not bar the exchangers' direct claims. The Cordell Defendants could have [*29] bargained for a Rule 23 bar Order that would have precluded a class action complaint like the one that Plaintiffs now bring against them, as did the Wave I Settling Defendants,¹⁷ but they did not do so.

15 (Reply in Further Support of Cordell Defendants' Motion to Dismiss Plaintiffs' Complaint at 3-4, hereafter, "Cordell's Reply," Docket Item No. 254.)

16 (Cordell's Reply at 5 (quoting December 1, 2009 Bankruptcy Court Hearing Transcript at 22:12-18, Cordell Defendant's Request for Judicial Notice in Support of Reply in Further Support of Motion to Dismiss, Ex. D, Docket Item No. 255).) Since the Bankruptcy Court Hearing Transcript is "capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned," the Court GRANTS Plaintiffs' Request for Judicial Notice as to that document. See Fed. R. Evid. 201(b).

17 The Wave I Settling Defendants are a group of defendants that entered into Settlement Agreements with plaintiffs in the related case of In re: Edward H. Okun Internal Revenue Service Tax Deferred Exchange Litigation. On October 8, 2009, the Court entered a Final Approval Order of Wave I Settlements. (See [*30] C 07-2795 JW, Docket Item No. 304.)

Accordingly, the Court DENIES the Cordell Defendants' Motion to Dismiss on the ground that Plaintiffs' claims against them are barred by the Bankruptcy Court's channeling injunction order. However, nothing in this Order is intended to bar the Cordell Defendants from later challenging the merits of Plaintiffs' claims based on evidence as to the nature of the funds at issue.

D. Lawyer Defendants' Motions

1. Statutes of Limitations

Lawyer Defendants move to dismiss Plaintiffs' claims on the ground that they are time-barred. (See Kutak Rock's Motion at 8-11; SVLG's Motion at 4-8; Jordan Burt's Motion at 5-8.) Plaintiffs contend that their claims are timely, and that the statutes of limitations of California, Florida, and Nebraska variously apply.¹⁸

18 (See Opposition to Kutak Rock's and Joseph Kavan's (i) Motion to Dismiss Amended Complaint for Lack of Subject Matter Jurisdiction and for Failure to State a Claim upon Which Relief may be Granted and (ii) Motion to Strike at 19, hereafter, "Opp'n Re Kutak Rock," Docket Item No. 238; Plaintiffs' Opposition [to] Defendant Jordan Burt's Motion to Dismiss at 3-5, hereafter, "Opp'n Re Jordan Burt," Docket Item No. [*31] 230; Plaintiffs' Opposition to Defendant Silicon Valley Law Group's Motion to Dismiss at 10-12, hereafter, "Opp'n Re SVLG," Docket Item No. 228.)

a. Choice of Law

As a preliminary matter, the Court considers which state law governs Plaintiffs' claims against the Lawyer Defendants.

California applies the "governmental interest" approach to conflict of law issues. *Abogados*, 223 F.3d at 934. "Where the conflict concerns a statute of limitations, the governmental interest approach generally leads California courts to apply California law." *Deutsch v. Turner Corp.*, 324 F.3d 692, 716 (9th Cir. 2003). "California's interest in applying its own law is strongest when its statute of limitations is shorter than that of the foreign state, because a state has a substantial interest in preventing the prosecution in its courts of claims which it deems to be 'stale.' Hence, subject to rare exceptions, the forum will dismiss a claim that is barred by its statute of limitations." *Id.* at 717.

In California, "[a]n action against an attorney for a wrongful act or omission, other than for actual fraud, arising in the performance of professional services shall be commenced within one year after the plaintiff [*32] discovers, or through the use of reasonable diligence should have discovered, the facts constituting the wrongful act or omission, or four years from the date of the wrongful act or omission, whichever occurs first." Cal. Civ. Proc. Code § 340.6(a). In analyzing the time at which a statute of limitations commences running, the relevant question is "whether the plaintiff has information of circumstances sufficient to put a reasonable person on inquiry, or has the opportunity to obtain knowledge from sources open to his or her investigation." *McGee v. Weinberg*, 97 Cal. App. 3d 798, 803, 159 Cal. Rptr. 86 (Cal. Ct. App. 1979).

Plaintiffs contend that California's limitations period applies to their claims against Defendant Silicon Valley Law Group, that Florida's limitations period applies to claims against Defendant Jordan Burt LLP, and that Nebraska's limitations period applies to claims against Defendants Kutak Rock LLP and Joseph Kavan. Florida and Nebraska's limitations periods conflict with California's because the former are two years and California's is one year.¹⁹ Under these circumstances, where California's limitations period is shorter, the Court finds that California's statute of limitations [*33] applies.²⁰

19 See Fla. Stat § 95.11(4)(a) (two years); Neb. Rev. Stat § 25-222 (two years).

20 Plaintiffs contend that the Court should apply Florida and Nebraska's statutes of limitations because Plaintiffs contend that California's statute of limitations was not enacted to prevent litigation of stale claims, but to protect California lawyers. (See Opp'n Re Jordan Burt at 3-4.) Plaintiffs rely on Restatement (Second) of Conflict of Laws § 142, comment "f," which states:

[W]here the forum has a short statute of limitations whose primary purpose is not to protect the local courts against stale evidence but rather to insure that a specified claim involving either local persons or local events should be brought in a brief space of time . . . the forum *might* refrain from applying its local statute to *bar* a similar action involving only foreign persons and foreign events on the ground that local policy does not require otherwise.

(emphasis added).

The Court rejects Plaintiffs' contention because the case relied on by Plaintiffs states merely that protection of California lawyers was "*one of the Legislature's purposes*" in enacting the California statute. See *Samuels v. Mix*, 22 Cal. 4th 1, 15-16, 91 Cal. Rptr. 2d 273, 989 P.2d 701 (Cal. 1999) [*34] (emphasis added). Furthermore, comment "f" to the Restatement only provides that a court has discretion to choose the foreign law where the forum's statute would *bar* a claim. To the contrary, the Court finds that Plaintiffs' claims are *not* barred by California's statute of limitations.

b. Application of California's Statute of Limitations

Lawyer Defendants contend that the statute of limitations period started running, at the latest, when Okun's businesses filed for bankruptcy on May 14, 2007 because Plaintiffs lost their exchange funds at that time. (See Kutak Rock Motion at 9-10.) Plaintiffs contend that they could not have discovered facts regarding the legal advice rendered by the Lawyer Defendants prior to March and April of 2009, at which time Plaintiffs gained access to many privileged documents pursuant to a Common Interest Agreement and Class/Trustee Agreement with the bankruptcy Trustee.²¹

21 (See Opp'n Re SVLG at 12; Declaration of Robert L. Brace in Support of Plaintiffs' Opposition to Defendant Silicon Valley Law Group's Motion to Dismiss PP 3-9, hereafter, "Brace Decl.," Docket Item No. 228.)

A statute of limitations may be tolled if the plaintiff did not have information [*35] of circumstances sufficient to put a reasonable person on inquiry, or did not have the opportunity to obtain knowledge from sources open to his or her investigation. See *McGee*, 97 Cal. App. 3d at 803. The question of whether a plaintiff discovered, or should have discovered through reasonable diligence, information sufficient to put a reasonable person on notice is generally a question of fact. See *Bank of Am. Nat'l Trust and Sav. Ass'n v. Allstate Ins. Co.*, 29 F. Supp. 2d 1129, 1135 (C.D. Cal. 1998). However, a "statute-of-limitations defense may be raised in a motion to dismiss when the running of the statute is apparent from the face of the complaint." *Vernon v. Heckler*, 811 F.2d 1274, 1278 (9th Cir. 1987).

Here, Plaintiffs allege as follows:

Plaintiffs have only recently discovered the facts alleged after actively and prudently investigating the causes of their losses. The initial bankruptcies filed by Okun for the qualified intermediaries were intended by Okun to delay discovery of losses by Plaintiffs. Okun fraudulently promised to obtain loans to complete outstanding 1031 Exchange transactions pending at the seven QIs. These purported loans did not exist, but caused delay in the [*36] appointment of a Trustee. Plaintiffs were further hampered in obtaining case information, including accurate and timely account information, due to the pending criminal trial of Okun. After Okun's conviction on March 19, 2009, Plaintiffs gained access to true and correct

information from Okun and other witnesses who have helped to develop the facts contained in the First Amended Complaint.

(AC P 38.) Based on these allegations, the Court finds that it is not apparent from the face of the First Amended Complaint when Plaintiffs discovered, or should have discovered, the facts constituting the alleged wrongful acts. Rather, Plaintiffs' allegations indicate that they were not able to discover, "through the use of reasonable diligence[,] . . . the facts constituting the wrongful act." See Cal. Civ. Proc. Code § 340.6(a).

Although Defendant Silicon Valley Law Group contends that the bankruptcy was a "storm warning" that should have put Plaintiffs on notice of their claims, no Defendant has provided the Court with, and the Court is not aware of any, controlling precedent for this proposition. (See SVLG Motion at 7-8.) Lawyer Defendants' point to the fact that Plaintiff Hunter filed suit against [*37] Okun on May 30, 2007 and contend that she should have been on notice of her claims from at least that point in time.²² However, that suit pertained to Okun's alleged wrongdoing; it is at best unclear whether the allegations in that action would put Plaintiff Hunter on notice of any potential wrongdoing by Lawyer Defendants. Thus, the Court finds that Plaintiffs' claims against Lawyer Defendants are not barred by the applicable statute of limitations.

22 (See Kutak Rock Motion at 10; Defendant Kutak Rock's Request for Judicial Notice, Ex. 1, Complaint in *Hunter v. Okun*, No. 5:07-CV-02795 (N.D. Cal.), Docket Item No. 196.) The Court GRANTS Kutak Rock's RJN because the subject documents are "capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned." Fed. R. Evid. 201(b).

Accordingly, Lawyer Defendants' Motions are DENIED as to this ground.

2. Plaintiffs' Standing Based on a Duty Owed to Plaintiffs

Lawyer Defendants move to dismiss Plaintiffs' Third, Fourth, Eighth, Ninth and Tenth Causes of Action for breach of fiduciary duty, aiding and abetting a breach of fiduciary duty,²³ breach of contract,²⁴ negligence, and negligent supervision [*38] on the grounds that (1) the QIs were not trusts, and, even if they were, the mere fact that Lawyer Defendants represented the trusts did not create a duty owed by Lawyer Defendants to Plaintiffs as beneficiaries of the trusts; and (2) Plaintiffs have not

sufficiently alleged that they were third party beneficiaries of the legal services agreements between Lawyer Defendants and the QIs. (See Kutak Rock's Motion at 13-17; SVLG's Motion at 8-12; Jordan Burt's Motion at 8-11.) The Court addresses each ground in turn.²⁵

23 Since Lawyer Defendants move on the ground of lack of duty, the Court finds that this ground is inapplicable to the Fourth Cause of Action for aiding and abetting a breach of fiduciary duty. A claim of aiding and abetting does not require a duty directly owed to Plaintiffs by Lawyer Defendants; rather, it focuses on Lawyer Defendants' intent in assisting another in breaching *their* duty. See, e.g., *Austin B. v. Escondido Union School Dist.*, 149 Cal. App. 4th 860, 879, 57 Cal. Rptr. 3d 454 (Cal. Ct. App. 2007). The Court addresses Plaintiffs' aiding and abetting claims below, in Section D.4.

24 The Eighth Cause of Action for breach of contract is alleged only against Defendant SVLG and is based [*39] on an allegation that Plaintiffs are intended beneficiaries of SVLG's legal services agreement with 1031 Advance (a qualified intermediary). (See AC P 255-57.)

25 Lawyer Defendants also contend that Plaintiffs lack standing because they cannot adequately allege a causal link between Lawyer Defendants and the alleged injury. (See Kutak Rock's Motion at 11-12; SVLG's Motion at 8-12; Jordan Burt's Motion at 8-11.) However, in light of the Court's disposition of the standing issue based on duty, the Court does not reach Lawyer Defendants' ground as to causation.

a. Duty Arising from Plaintiffs' Status as Trust Beneficiaries

At issue is whether the QIs were trusts, and, if so, whether the fact that Lawyer Defendants represented the trustees created a duty owed by the Lawyer Defendants to Plaintiffs as beneficiaries of the trusts.

As a preliminary matter, the Court determines the applicable law. Plaintiffs contend that the laws of California, Florida, Massachusetts, Virginia, and New York apply to its claims.²⁶ (See, e.g., *Opp'n Re Jordan Burt* at 5-7; *Opp'n Re Kutak Rock* at 16-18.) However, as demonstrated below, the Court finds that the laws of these jurisdictions are not in conflict on the [*40] relevant substantive issues of law. Since the laws of the various foreign jurisdictions do not conflict with California law, the Court applies California law. See *Paulsen v. CNF Inc.*, 559 F.3d 1061, 1080-81 (9th Cir. 2009).²⁷

26 Plaintiffs contend that "New York law applies to the torts at SOS [a qualified intermedi-

ary]" because Kutak Rock allegedly provided legal assistance to Okun in acquiring SOS." (See Opp'n Re Kutak Rock at 11, 19.) However, since the First Amended Complaint alleges that Defendant Kutak Rock represented Okun, not SOS, and that SOS was in fact the adverse party in the transaction in which Kutak represented Okun, the Court finds no reason, based on the allegations, to include New York law in its choice of law analysis. (See AC PP 167-170.)

27 Indeed, in the remaining sections of this Order, the Court finds that the laws of the foreign jurisdictions do not conflict with California law, and thus, the Court applies California law in considering Lawyer Defendants' grounds for dismissal.

An attorney engaged by a trustee owes no fiduciary duty to the trust beneficiaries. See *Berg & Berg Enters., LLC v. Sherwood Partners, Inc.*, 131 Cal. App. 4th 802, 827 n.11, 32 Cal. Rptr. 3d 325 (Cal. Ct. App. 2005); [*41] *Spinner v. Nutt*, 417 Mass. 549, 631 N.E.2d 542, 544-46 (Mass. 1994); *Dotson v. Lillard*, NO. 135209, 1994 WL 1031449, *3 (Va. Cir. Ct. 1994); *Silver Dunes Condominium of Destin, Inc. v. Beggs and Lane*, 763 So. 2d 1274, 1276-77 (Fla. Dist. Ct. App. 2000). Thus, generally, the beneficiaries of a trust do not have standing to assert malpractice claims against an attorney hired by the fiduciary. *Borissoff v. Taylor & Faust*, 33 Cal. 4th 523, 530, 15 Cal. Rptr. 3d 735, 93 P.3d 337 (Cal. 2004); *Spinner*, 631 N.E.2d at 544-46; *Dotson*, 1994 WL 1031449, at *3; *Silver Dunes*, 763 So. 2d at 1276-77. However, trust beneficiaries have standing to sue the fiduciary's attorney if they were intended third party beneficiaries of the contract to provide legal services. *Borissoff*, 33 Cal. 4th at 530; *Spinner*, 631 N.E.2d at 544-46; *Copenhaver v. Rogers*, 238 Va. 361, 384 S.E.2d 593, 596-97, 6 Va. Law Rep. 499 (Va. 1989); *Dotson*, 1994 WL 1031449, at *3; *Silver Dunes*, 763 So. 2d at 1276-77.

Here, Plaintiffs allege as follows:

Lawyers, serving as counsel to fiduciaries, owe a fiduciary duty to the beneficiaries of the trust. Lawyer Defendants, serving as counsel to the QIs, breached their fiduciary duties of loyalty, care and fair dealing owed to the QI exchanger clients. Lawyer Defendants assisted [*42] Okun and the seven QIs in breaching their fiduciary duties. Each Lawyer Defendant owed a legal duty of care to the QI exchangers, which arose out of their respective affirmative acts in assuming such duty, or which arose by operation of law

from the fiduciary nature of their relationship with Okun and the QIs that he controlled.

Defendant SVLG entered into a written contract with 1031 Advance [a qualified intermediary] to provide competent legal advice concerning the potential sale of 1031 Advance to Okun. 1031 Advance retained SVLG for the intended benefit of Plaintiffs, as lawful fiduciary to the exchange funds on deposit at 1031 Advance and to each QI exchanger. SVLG breached the terms of its contract of engagement by providing grossly negligent advice and counsel, advising Dashiell [an owner of 1031 Advance] to sell 1031 Advance to Okun and to transfer the exchange funds to Okun's 1031 Tax Group. Plaintiffs were intended third party beneficiaries of the contract between 1031 Advance and SVLG.

Lawyer Defendants retained and used the services of individual lawyers to perform services as employees, agents and servants without adequately training and supervising them about conflicts [*43] of interest, and specific duties of loyalty, care and acting for the exclusive benefit of the client, which duties were owed to the beneficiaries of a trust, and the trust itself, when providing legal representation to the corporate trustee of a trust.

The Hunter Plaintiffs have standing to assert tort claims on behalf of themselves directly against Defendant Kutak Rock because the fiduciary duties Kutak owed to the QIs, as trustees of the Exchange Funds, ran directly to Plaintiffs as beneficiaries. Kutak owed duties of competence, loyalty, fair dealing, and full disclosure to the QIs and to the Exchangers, not to Okun. In fact, Kutak's duties to Exchangers and to the QIs created an irreconcilable conflict of interest in the firm's representation of Okun.

(AC PP 175-76, 240-44, 254-62.)

Assuming that QIs are trusts, Plaintiffs appear to base their standing in part on the fact that they were beneficiaries of the trusts that retained Lawyer Defendants. To the extent that Plaintiffs rely on their status as trust beneficiaries as the basis for their standing to sue

Lawyer Defendants, the Court finds, as a matter of law, that basis is insufficient to confer standing on Plaintiffs. Rather, [*44] Plaintiffs must allege something more--that they were intended third party beneficiaries of the legal services agreements between Lawyer Defendants and the QIs. Thus, the issue becomes whether Plaintiffs have sufficiently pleaded that they were in fact intended third party beneficiaries.

b. Duty Arising from Plaintiffs' Status as Third Party Beneficiaries

At issue is whether Plaintiffs were intended third party beneficiaries of the legal services agreements between Lawyer Defendants and their clients (*i.e.*, Okun and the QIs), and if so, whether Plaintiffs have standing to sue Lawyer Defendants on that basis.

A claim of professional malpractice against an attorney requires the establishment of a duty between the attorney and the plaintiff. See *Moore v. Anderson Zeigler Disharoon Gallagher & Gray*, 109 Cal. App. 4th 1287, 1294, 135 Cal. Rptr. 2d 888 (Cal. Ct. App. 2003); *Lorraine v. Grover, Ciment, Weinstein & Stauber, P.A.*, 467 So. 2d 315, 317 (Fla. Dist. Ct. App. 1985); *Bank of Am. v. Musselman*, 240 F. Supp. 2d 547, 553-54 (E.D. Va. 2003); *Miller v. Mooney*, 431 Mass. 57, 725 N.E.2d 545, 549 (Mass. 2000). Although a lawyer owes a duty of professional care to his client, the lawyer owes "no such duty to [third parties] in the [*45] absence of any showing that the legal advice was foreseeably transmitted to or relied upon by [the third parties] or that [the third parties] were intended beneficiaries of a transaction to which the advice pertained." *Goodman v. Kennedy*, 18 Cal. 3d 335, 336, 134 Cal. Rptr. 375, 556 P.2d 737 (Cal. 1976); see also *Horowitz v. Laske*, 855 So. 2d 169, 173 (Fla. Dist. Ct. App. 2003); *Bank of Am.*, 240 F. Supp. 2d at 554; *Miller*, 725 N.E.2d at 549.

To establish that a duty was owed to a third party beneficiary of a legal services agreement, the third party must show that the parties entered into the agreement with the intent to benefit the third party. *Zenith Ins. Co. v. Cozen O'Connor*, 148 Cal. App. 4th 998, 1008, 55 Cal. Rptr. 3d 911 (Cal. Ct. App. 2007); *B.L.M. v. Sabo & Deitsch*, 55 Cal. App. 4th 823, 832, 64 Cal. Rptr. 2d 335 (Cal. Ct. App. 1997); see *Silver Dunes*, 763 So.2d at 1276 (Fla. Dist. Ct. App. 2000); *Rosenstone v. Satchell*, 560 So. 2d 1229, 1229-30 (Fla. Dist. Ct. App. 1990); *Bank of Am.*, 240 F. Supp. 2d at 553; *Miller*, 725 N.E.2d at 549.²⁸ The mere fact that a third party stood to benefit from legal services to the attorney's client is not sufficient. *Zenith Ins. Co.*, 148 Cal. App. 4th at 1008; see also *B.L.M.*, 55 Cal. App. 4th at 832; *Bank of Am.*, 240 F. Supp. 2d at 554; [*46] *Silver Dunes*, 763 So. 2d at 1277; *Miller*, 725 N.E.2d at 549-50. Additionally, where a potential conflict of interest exists between the attorney's

client and the party claiming third party beneficiary status, courts will not find such status. *Zenith Ins. Co.*, 148 Cal. App. 4th at 1009; *Silver Dunes*, 763 So.2d at 1277; *Miller*, 725 N.E.2d at 550.

28 Although some Florida courts have framed the analysis as whether the *client* intended to benefit the third party and the attorney was *aware* that the third party was an intended beneficiary, other Florida courts have stated that the *parties* to the contract must clearly express an intent to benefit the third party. Compare *Rosenstone*, 560 So. 2d at 1229-30 with *Federal Ins. Co. v. Bonded Lightning Protection Sys., Inc.*, No. 07-80767-CIV, 2008 U.S. Dist. LEXIS 97952, 2008 WL 5111260, at *7 (S.D. Fla. Dec. 3, 2008).

The Court analyzes the allegations as to each Lawyer Defendant in turn.

i. Defendant Kutak Rock

As to Defendant Kutak Rock, Plaintiffs allege as follows:

In January of 2005, Defendants Joseph O. Kavan and Kutak Rock (collectively, 'Kutak') began providing extensive legal representation to [Investment Properties of America]. Kutak understood IPofA to be in the business [*47] of acquiring real property and then selling partial interests in the real estate to buyers seeking to purchase real estate to complete 1031 exchanges. Kutak understood that IPofA was owned and controlled by Okun.

In August of 2005, Okun engaged Kutak to perform legal work regarding the financing of Okun's purchase of AEC [a qualified intermediary], including review of the AEC acquisition loan from Defendant Boulder Capital. Kutak was informed that 'Okun was considering using AEC client funds as a loan.' Nevertheless, Kutak agreed to act as counsel for IPofA and Okun in documenting the loans.

In September of 2005, Kutak was retained as counsel for AEC in employment matters--specifically, to assist in the termination of Dowdall, the former owner of AEC whom Okun hired to serve as president of AEC after it was acquired by Okun. Kutak assisted Okun in concealing his improper borrowing from the AEC exchange funds by carrying out the Okun-directed termination of Dowdall. Kutak,

as counsel for AEC, became a fiduciary to the AEC exchangers, as beneficiaries of the trust. Thus, Kutak owed fiduciary duties directly to the exchangers. Kutak breached its fiduciary duties, which included the duties [*48] of full disclosure, loyalty, and fair dealing. Instead, Kutak actively concealed the prior \$ 33.1 million in loans from Dowdall and from the exchangers to its own financial gain.

In November of 2005, Kutak assisted Okun by negotiating and preparing the documentation for Okun's purchase of SOS [a qualified intermediary]. In December of 2005, Okun formed the 1031 Tax Group to act as the holding company for the qualified intermediaries acquired by Okun. Kutak represented the 1031 Tax Group in corporate matters and in the integration of newly acquired qualified intermediaries.

The Hunter Plaintiffs have standing to assert tort claims on behalf of themselves directly against Kutak because the fiduciary duties Kutak owed to the QIs, as trustees of the Exchange Funds, ran directly to Plaintiffs as beneficiaries. Kutak owed duties of competence, loyalty, fair dealing, and full disclosure to the QIs and to the Exchangers, not to Okun. In fact, Kutak's duties to Exchangers and to the QIs created an irreconcilable conflict of interest in the firm's representation of Okun.

(AC PP 156-76.)

Based on the above allegations, the Court finds that Plaintiffs have not pleaded sufficient factual allegations [*49] to show that they were intended third party beneficiaries of the legal services contract between Defendant Kutak Rock and any of its clients--Okun, 1031 Tax Group, IPofA, or AEC. Of the alleged clients, only AEC was a qualified intermediary, and Defendant Kutak Rock represented it only with regard to the firing of its president.²⁹ Plaintiffs do not allege that Defendant Kutak Rock and AEC expressly intended that representation to benefit Plaintiffs as clients of AEC. Likewise, the Amended Complaint does not attach the retention agreement or allege that the retention agreement expressly states that Plaintiffs were intended beneficiaries of the representation. To the contrary, Plaintiffs allege that Defendant Kutak Rock assisted Okun in acting *adverse* to Plaintiffs' interests.

29 The Amended Complaint describes the 1031 Tax Group not as a qualified intermediary, but as a "holding company for the multiple QIs acquired by Okun." (See AC P 171.) However, even if the 1031 Tax Group could itself be considered a qualified intermediary, it would not change the Court's analysis.

Accordingly, the Court GRANTS Defendant Kutak Rock's Motion as to the Third, Ninth and Tenth Causes of Action. Since [*50] Plaintiffs' allegations cut directly against the notion that Plaintiffs were intended beneficiaries, any amendment would be futile. Thus, Plaintiffs' Third, Ninth and Tenth Causes of Action against Defendants Kutak Rock and Kavan are DISMISSED with prejudice.

ii. Defendant Jordan Burt

As to Defendant Jordan Burt, Plaintiffs allege as follows:

Richard Simring was a partner at Jordan Burt throughout the period of January 1, 2000 to December 31, 2006. On May 11, 2006, IPofA signed the first of two engagement letters with Jordan Burt. The engagement concerned IPofA's potential acquisition of First Montauk Securities Corp.

In November and December of 2006, Simring, while still a partner at Jordan Burt, acted as counsel to Okun, IPofA, and Okun's QIs. On November 29, 2006, Simring informed Hcctor (IPofA's in-house counsel at that time) that Jordan Burt was counsel to Okun, personally, and to 'all of Ed's companies,' which included the QIs.

On December 1, 2006, Simring and Jordan Burt sent Okun an engagement letter that stated: 'Thank you for selecting Jordan Burt LLP to represent you, in your individual capacity, with regard to potential litigation matters, including potential litigation involving [*51] Todd Pajonas.' Todd Pajonas was employed by the 1031 Tax Group and was the president of SOS and AEC. On December 18, 2006, with counsel and assistance from Jordan Burt, Okun, through his 1031 Tax Group, acquired ownership of 1031 Advance [a qualified intermediary].

Starting on January 1, 2007, Simring became 'of counsel' at Jordan Burt and general counsel to Okun Holdings, which was owned and controlled by Okun and which 'held' the 1031 Tax Group (which in turn ostensibly owned the various qualified intermediaries acquired, owned and controlled by Okun).

(AC PP 193-214.)

Based on the above allegations, the Court finds that Plaintiffs have not pleaded sufficient facts to show that they were intended third party beneficiaries of the legal services contract between Defendant Jordan Burt and any of its clients--Okun, IPofA, or Okun's QIs. Plaintiffs have not attached any of the retention agreements to the Amended Complaint or alleged that the retention agreements expressly state that Plaintiffs were intended beneficiaries of the representation. In fact, the allegations are that neither Defendant Jordan Burt nor its clients had any intention of entering into the contracts to benefit Plaintiffs.

Accordingly, [*52] the Court GRANTS Defendant Jordan Burt's Motion as to the Third, Ninth and Tenth Causes of Action. Since Plaintiffs' allegations cut directly against the notion that Plaintiffs were intended beneficiaries, any amendment would be futile. Thus, Plaintiffs' Third, Ninth and Tenth Causes of Action against Defendant Jordan Burt are DISMISSED with prejudice.

iii. Defendant Silicon Valley Law Group

As to Defendant Silicon Valley Law Group, Plaintiffs allege as follows:

In December of 2006, Okun acquired 1031 Advance, a California qualified intermediary owned by Dashiell, Allred, and others. Dashiell, Allred, and 1031 Advance were represented in the sale transaction by Michael Schacter and James Chapman, lawyers at Defendant Silicon Valley Law Group. Dashiell understood that, upon completion of the sale transaction, Okun intended to make further loans to himself or other entities he owned and controlled, from exchange funds held by 1031 Advance. Dashiell and Allred communicated these facts to SVLG.

Dashiell requested advice from SVLG, for the **intended benefit** of 1031 Advance Exchangers, as to whether the

proposed sale of 1031 Advance to Okun was lawful or prudent. Despite SVLG's knowledge that [*53] Okun intended to misappropriate the exchange funds held by 1031 Advance to his own use and for his own purposes, SVLG failed to counsel Dashiell to reject the sale of 1031 Advance to Okun. Instead, SVLG approved the proposed sale and inserted clauses into the Purchase and Sale Agreement regarding the total sum that Okun could 'borrow' from exchange funds. The sale was completed on December 18, 2006.

SVLG knew that 1031 Advance was a trustee and as such, owed fiduciary duties of loyalty and care to its clients. Defendant SVLG entered into a written contract with 1031 Advance to provide competent legal advice concerning the potential sale of 1031 Advance to Okun. 1031 Advance retained SVLG for the **intended benefit** of Plaintiffs, as lawful fiduciary to the exchange funds on deposit at 1031 Advance and to each QI exchanger. SVLG breached the terms of its contract of engagement by providing grossly negligent advice and counsel, advising Dashiell to sell 1031 Advance to Okun and to transfer the exchange funds to Okun's 1031 Tax Group. Plaintiffs were **intended third party beneficiaries** of the contract between 1031 Advance and SVLG.

(AC PP 215-21, 255-56 (emphasis added).)

Based on the above [*54] allegations, the Court finds that Plaintiffs have not pleaded sufficient facts to show that they were intended third party beneficiaries of the legal services contract between Defendant SVLG and 1031 Advance. Although Plaintiffs conclusorily allege that 1031 Advance intended to benefit them, they have not alleged that Defendant SVLG knew of, much less intended, the same. Rather, the allegations are that Defendant SVLG knowingly acted directly *adverse* to Plaintiffs' interest. Additionally, the retention agreement between SVLG and 1031 Advance does not express any intent by the parties to enter into the agreement for the benefit of Plaintiffs. (See Brace Decl., Ex. 4.)³⁰

³⁰ In deciding a motion to dismiss, a court may consider documents referenced in the complaint whose authenticity no party questions. See *Branch v. Tunnell*, 14 F.3d 449, 453-54 (9th Cir.

1994), overruled on other grounds by Galbraith v. County of Santa Clara, 307 F.3d 1119 (9th Cir. 2002).

Accordingly, the Court GRANTS Defendant Silicon Valley Law Group's Motion as to the Third,³¹ Eighth, Ninth and Tenth Causes of Action. Since Plaintiffs' allegations cut directly against the notion that Plaintiffs were intended beneficiaries, [*55] any amendment would be futile. Thus, Plaintiffs' Third, Eighth, Ninth and Tenth Causes of Action against Defendant SVLG are DISMISSED with prejudice.

31 Plaintiffs concede that dismissal of the Third Cause of Action is appropriate as to Defendant SVLG. (See Opp'n Re SVLG at 27.)

3. First Cause of Action for Conversion

Defendants Kutak Rock and Jordan Burt move to dismiss Plaintiffs' claim for conversion on the ground that Plaintiffs have not adequately pleaded facts constituting conversion.³² (Kutak Rock's Motion at 23-24; Jordan Burt's Motion at 13-14.)

32 Plaintiffs' conversion claim is not alleged against Defendant Silicon Valley Law Group. (See AC at 64.)

The elements of a conversion claim are: (1) the plaintiff's ownership or right to possession of the property; (2) the defendant's conversion by a wrongful act or disposition of property rights; and (3) damages. *Burlesci v. Petersen*, 68 Cal. App. 4th 1062, 1065, 80 Cal. Rptr. 2d 704 (Cal. Ct. App. 1998); see also *Mayo v. Allen*, 973 So. 2d 1257, 1258-59 (Fla. Dist. Ct. App. 2008); *Cahaly v. Benistar Property Exchange Trust Co., Inc.*, 68 Mass. App. Ct. 668, 864 N.E.2d 548, 559 (Mass. App. Ct. 2007); *Simmons v. Miller*, 261 Va. 561, 544 S.E.2d 666, 679 (Va. 2001). One who receives stolen money [*56] in good faith and for good consideration will not be liable for conversion. See *Kelley Kar Co. v. Maryland Cas. Co.*, 142 Cal. App. 2d 263, 264, 298 P.2d 590 (Cal. Ct. App. 1956) (citing *State Nat'l Bank v. United States*, 114 U.S. 401, 5 S. Ct. 888, 29 L. Ed. 149, 20 Ct. Cl. 537 (1885)); c.f. *Swim v. Wilson*, 90 Cal. 126, 130-31, 27 P. 33 (Cal. 1891); *Federal Ins. Co. v. Smith*, 63 Fed. Appx. 630 (4th Cir. 2003) (applying Virginia law).

Here, Plaintiffs allege as follows:

Lawyer Defendants exercised dominion and control over exchange funds without the Exchangers' consent, and contrary to the use of these funds as articulated in each exchange agreement. The converted exchange funds were deposited as a spe-

cific and identifiable sum that Plaintiffs were entitled to recover in a period no more than 180 days after deposit with the QIs.

During the exchange process, legal title to exchange funds (the proceeds from selling the real property) is transferred to the QI. However, the QI's clients retain full equitable interest and rights to the sums on deposit, but for the use and benefit of the money during the exchange period. IRC § 1031 prohibits [*57] the seller of property from taking possession or control of sale proceeds at any time prior to completion of the 1031 transaction.

Defendant Kutak Rock was motivated by pecuniary gain and collected over \$ 1,000,000 in fees in 2005 and 2006 from Okun and the entities he owned and controlled. The bulk of payments for these services can be traced back to stolen exchange funds. Kutak knew that Okun's cash came from usurious bank loans or exchange funds.

On November 22, 2006, Simring emailed his partners at Defendant Jordan Burt, stating that Okun's business "is essentially an unregulated Ponzi scheme." In November and December of 2006, Simring, while still a partner at Jordan Burt, acted as counsel for Okun, IPofA, and Okun's QIs. On January 1, 2007, Simring became 'of counsel' at Jordan Burt and general counsel of Okun Holdings with promised compensation in excess of \$ 800,000 per year. Simring's willingness to advance Okun's interests at the expense of the QIs and the exchangers while a partner at Jordan Burt was based, in part, on Okun's promise to pay him an exorbitant salary after he became 'of counsel' at Jordan Burt and general counsel of Okun Holdings.

(AC PP 41, 43, 174, 200, 202, [*58] 214, 235.)

Based on the allegations above, the Court finds that Plaintiffs have adequately pleaded a claim for conversion. Plaintiffs allege that they had equitable ownership of the exchange funds, a right to possess the funds (180 days from date of deposit at the latest), and that Defendants Kutak Rock and Jordan Burt wrongfully exercised

control over those funds by way of collecting legal fees from Okun and his entities with knowledge that Okun was using exchange funds to pay them. Plaintiffs do not allege that Defendants Kutak Rock and Jordan Burt received the money in good faith. The fact that Plaintiffs were not entitled to the funds until the property exchange was completed or 180 days after deposit, whichever came first, does not preclude a cause of action for conversion. See Cahaly, 864 N.E.2d at 559. Thus, the Court finds that the allegations are sufficient to state a claim for conversion.³³

33 However, to the extent that Lawyer Defendants were paid fees prior to any of Plaintiffs (or the putative class members) depositing any money with the QIs, such payments could not constitute conversion of Plaintiffs' property.

Accordingly, the Court DENIES Lawyer Defendants' Motions to [*59] Dismiss Plaintiffs' First Cause of Action for conversion.

4. Fourth and Fifth Causes of Action for Aiding and Abetting

Lawyer Defendants move to dismiss the Fourth and Fifth Causes of Action for aiding and abetting breach of fiduciary duty and aiding and abetting fraud on the grounds that (1) Plaintiffs fail to allege sufficient facts to support their claims, and (2) Plaintiffs failed to obtain a pre-filing court order required under California law in order to assert claims of aiding and abetting against Lawyer Defendants. (See SVLG's Motion at 12-14; Kutak Rock's Motion at 21-23; Jordan Burt's Motion at 11-13.)

a. Sufficiency of Allegations

A plaintiff may state a claim for aiding and abetting an intentional tort if (1) the defendant knew that the primary tortfeasor's conduct constitutes a breach of duty, and (2) the defendant gave substantial assistance or encouragement to the other to so act. See Austin, 149 Cal. App. 4th at 879; Spinner, 631 N.E.2d at 546; Hogan v. Provident Life and Accident Ins. Co., 665 F. Supp. 2d 1273, 2009 WL 3367327, at *10 (M.D. 2009); Avalon-Bay Communities, Inc. v. Willden, No. 1:08-cv-777, 2009 U.S. Dist. LEXIS 69118, 2009 WL 2431571, at *11 (E.D. Va. Aug. 7, 2009).

Here, [*60] Plaintiffs allege as follows:

Okun and the 7 QIs owed fiduciary duties to the QI Exchangers. Lawyer Defendants knew that Okun and the QIs he controlled engaged in material breaches of their fiduciary duties owed to the QI Exchangers. Lawyer Defendants assisted

Okun and the 7 QIs in breaching their fiduciary duties.

Okun and the 7 QIs that he controlled offered exchange agreements for signature by Exchangers, knowing that they contained false promises. Lawyer Defendants knew that the exchange agreements contained false promises, but nonetheless willfully assisted Okun and the QIs in making these false promises for the sole and exclusive purpose of assisting Okun in perpetrating his Ponzi scheme, and with the intent of economic gain for each Lawyer Defendant.

In August and September of 2005, Defendant Kutak Rock was informed that 'Okun was considering using AEC client funds as a loan.' Kutak knew that such 'loans' would not be proper without consent from AEC's clients. Kutak nevertheless drafted the documents for such loans from AEC to Okun personally and to Okun-controlled entities. In that same time frame, Kutak also provided legal assistance to Okun and AEC in terminating Dowdall in [*61] order to assist Okun in concealing his illegal activity. Kutak's own legal research confirmed that Okun's actions constituted a breach of fiduciary duty. Kutak assisted Okun in breaching his fiduciary duties.

On November 22, 2006, Simring emailed his partners at Defendant Jordan Burt, stating that Okun's business 'is essentially an unregulated Ponzi scheme.' Simring and Jordan Burt continued to represent Okun through at least the end of 2006. In December of 2006, Simring and Jordan Burt provided counsel to the 1031 Tax Group in its efforts to acquire 1031 Advance, knowing that 1031 Advance would serve as a further source of funds for Okun's scheme. Simring also convinced Dashiell [an owner of 1031 Advance] to eliminate all borrowing limitations from the 1031 Tax Group Purchase Agreement.

Despite Defendant SVLG's knowledge that Okun intended to misappropriate the exchange funds held by 1031 Advance to his own use and for his own purposes, SVLG failed to counsel Dashiell to reject the sale of 1031 Advance to Okun.

Instead, SVLG approved the proposed sale and inserted clauses into the Purchase and Sale Agreement regarding the total sum that Okun could 'borrow' from exchange funds.

(AC PP [*62] 159-74, 200-18, 243-47.)

Based on the above allegations, the Court finds that Plaintiffs have pleaded facts sufficient to state claims for aiding and abetting. Plaintiffs allege that Lawyer Defendants knew that Okun and his QIs were defrauding and breaching their duties to the clients of the QIs, including Plaintiffs. Plaintiffs also allege in detail the manner in which Lawyer Defendants provided substantial assistance to Okun and his QIs in breaching their duties and committing fraud. Thus, the Court finds that Plaintiffs' claims for aiding and abetting are sufficiently alleged.

Accordingly, the Court DENIES Lawyer Defendants' Motions to Dismiss Plaintiffs' Fourth and Fifth Causes of Action for aiding and abetting intentional torts.

b. Pre-filing Court Order

At issue is whether Plaintiffs were required to obtain a pre-filing court order under California law prior to asserting claims for aiding and abetting against Lawyer Defendants.³⁴

34 Only Defendant Silicon Valley Law Group moves on this ground. (See SVLG's Motion at 13-14.)

California Civil Code § 1714.10(a) states:

No cause of action against an attorney for a civil conspiracy with his or her client arising from any attempt to contest [*63] or compromise a claim or dispute, and which is based upon the attorney's representation of the client, shall be included in a complaint or other pleading unless the court enters an order allowing the pleading that includes the claim for civil conspiracy to be filed after the court determines that the party seeking to file the pleading has established that there is a reasonable probability that the party will prevail in the action.

Claims for aiding and abetting fall within section 1714.10. *Berg & Berg Enters.*, 131 Cal. App. 4th at 823 n.10. Section 1714.10 does not apply where the claims are based on allegations that the attorney "participated in a breach of duty owed by the [attorney's] client and did

so for his or her own personal financial advantage." *Id.* at 826; Cal. Civ. Code § 1714.10(c)(2).

Based on the allegations above (see Section D.4.a), the Court finds that Plaintiffs' claims of aiding and abetting do not fall within section 1714.10(a) because they are premised on the notion that Lawyer Defendants assisted Okun and his QIs in breaching their duties to Plaintiffs. In assisting Okun, Lawyer Defendants were allegedly motivated by personal financial gain. Thus, the Court finds [*64] that Plaintiffs' claims for aiding and abetting are not barred for failure to obtain a pre-filing court order under section 1714.

Accordingly, the Court DENIES Defendant SVLG's Motion to Dismiss on this ground.

E. Conclusion

In sum, the Court ORDERS as follows:

(1) Defendants UWB and Citibank's Motions to Dismiss are GRANTED with leave to amend.

(2) The Cordell Defendants' Motion to Dismiss is DENIED without prejudice.

(3) The Lawyer Defendants' Motions to Dismiss are GRANTED in part and DENIED in part as follows:³⁵

(a) The Lawyer Defendants' Motions as to the Third, Eighth, Ninth and Tenth Causes of Action as alleged against Defendants Kutak Rock LLP, Joseph Kavan, Jordan Burt LLP, and Silicon Valley Law Group are GRANTED with prejudice;

(b) The Lawyer Defendants' Motions to Dismiss as to all other causes of action are DENIED.

35 The Court DENIES Defendant Jordan Burt's request to strike Plaintiffs' prayer for certain consequential damages, punitive damages, and attorney fees because Defendant Jordan Burt has not stated grounds warranting the requested relief. (See Jordan Burt Motion at 16.)

In addition, since the grounds for dismissal raised by Lawyer Defendants are also raised in Defendants [*65] Foley & Lardner LLP and Stephen Burr's Motion to Dismiss currently set for hearing on March 22, 2010,³⁶ the Court finds that its disposition of Lawyer Defendants' Motions applies equally to the issues raised in the Foley's Motion. Accordingly, the Court GRANTS in part and DENIES in part the Foley Defendants' Motion as articulated above in the Lawyer Defendants' Motions.

36 (Docket Item No. 192.)

On or before **March 3, 2010**, Plaintiffs shall file a Second Amended Complaint consistent with the terms of this Order. In light of this Order, the Court finds that it is premature to conduct a Case Management Conference at this time. Accordingly, the February 8, 2010 Conference is VACATED. The Court will set a new conference date in its Order addressing Defendants' anticipated motions to dismiss the amended complaint, if necessary.³⁷

37 In light of this Order, Defendants Kutak Rock's Motion to Continue hearing is DENIED as moot. (Docket Item No. 262.)

Finally, because a Second Amended Complaint is forth coming, the Boulder Defendants and Roy S. Macdowell, Jr.'s Motion to Dismiss is DENIED as moot.³⁸ (Docket Item No. 176.)

38 The Court notes that the Boulder Defendants' Motion raises important personal [*66] jurisdiction issues. Accordingly, Plaintiffs' amended complaint shall clearly state factual allegations to support the Court's jurisdiction over these Defendants.

Dated: February 3, 2010

/s/ James Ware

JAMES WARE

United States District Judge