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SECURITIES AND FIDUCIARY DUTY CASES IN TEXAS

JULY – SEPTEMBER 2024

This quarterly newsletter summarizes recent federal and state court decisions and other developments of interest to practitioners litigating securities and fiduciary duty claims in Texas.

Court rulings, hyperlinked to Westlaw, and other notable events include:

- Fifth Circuit Rulings – The Fifth Circuit issued rulings in three SEC cases this quarter. In ***SEC v. Stanford Int'l Bank, Ltd.***, it vacated a settlement bar order that would have prevented Joint Liquidators appointed by an Antiguan court from pursuing claims against a Swiss bank because the district court did not have *in personam* jurisdiction over the Joint Liquidators and its *in rem* jurisdiction was not a sufficient basis to enter an injunction. In ***Barr v. SEC,*** the Court ruled the SEC did not abuse its discretion in refusing to pay whistleblower awards to two individuals who helped obtain a $38.7 million securities fraud judgment because the company later filed for bankruptcy. In ***SEC v. Stack***, the Court reversed a disgorgement award against an individual for the entire investor loss because it should have been limited to the funds the individual received or benefitted from as required by the Supreme Court's ruling in *Liu v. SEC*.

- Federal District Court Rulings – Among seven cases we summarized, three stand out this quarter. In the long-running ***Alta Mesa*** securities fraud litigation, Judge Hanks granted substantial portions of defendants' motions for summary judgment, leaving for trial only control person liability claims against certain private equity and corporate defendants. In ***Architectural Granite & Marble, LLC v. Pental,*** Judge Lindsay dismissed a whistleblower claim because the former employee lacked evidence that he suffered a material adverse action and the company presented clear and convincing evidence that it would have taken the same actions regardless of the protected activity. In ***State Farm Mut. Auto. Ins. Co. v. Complete Pain Solutions, Inc.***, Judge Hanen denied motions to dismiss RICO and mail fraud claims against a group of doctors who allegedly submitted bills for predetermined, false and/or medically unnecessary treatment to obtain insurance proceeds.

- State Court Rulings – The most notable case this quarter is ***Texas A&M University 12th Man Foundation v. Hines***, filed by Foundation donors who lost their preferred seats when the Foundation solicited new donations to renovate Kyle Field. The Court held the Texas Citizens' Participation Act barred new claims for breach of fiduciary duty and breach of the duties of good faith and fair dealing, ruling that the Foundation's stadium renovation activities were "a matter of public concern." However, the Court also held that claims for breach of contract and promissory estoppel were not barred because the defendants missed the 60-day deadline to raise the TCPA to bar such claims.

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CASE SUMMARIES

I. FEDERAL CASES

A. Fifth Circuit

1. *SEC v. Stanford Int'l Bank, Ltd.*, 112 F.4th 284 (5th Cir. 2024).

This case arises from the SEC's long-running Ponzi scheme litigation against Stanford International Bank, Ltd. (SIBL) and its affiliates. The court-appointed equity receiver settled claims against a third party, Société Générale Private Banking (Suisse) S.A. (SGPB). As part of the settlement, SIBL sought a bar order that "enjoined the world from bringing future Stanford-related claims" against SGPB. The Receiver sought district court approval of the bar order, including barring "Joint Liquidators" appointed by an Antiguan court to retrieve SIBL and Stanford Trust Company Limited assets from pursuing claims. The Joint Liquidators filed objections to the bar order in a related action but did not object in the SEC action for fear of waiving their objections to personal jurisdiction in the SEC action. The trial court told the Joint Liquidators' counsel that if they made any substantive argument at the hearing on the bar order, they would waive any objection to personal jurisdiction. Counsel remained silent, and the trial court entered the bar order. The Joint Liquidators appealed.

The Fifth Circuit vacated the bar order, holding that the trial court's *in rem* jurisdiction over the Stanford receivership estate did not support the bar order's injunction. Instead, *in personam* jurisdiction is required to impose an injunction, which the trial court lacked. The Court held that the trial court's instruction to the Joint Liquidators that they would waive objections to personal jurisdiction if they made substantive objections to the bar order was an impermissible "waiver trap." The Court found the "waive-or-forfeit dilemma" the trial court imposed on the Joint Liquidators did not comport with "traditional notions of fair play and substantial justice." Rather, it "vitiated the Joint Liquidators' voluntariness because either route they chose was tainted by coercion."

Judge Higginson filed a separate concurrence emphasizing that he would have vacated the bar order but remanded the case to the trial court to consider arguments on the merits. Because the case law whether *in rem* jurisdiction is sufficient to enjoin future claims relating to the property is still unsettled, the appellate arguments would have benefited from further development of the case in the trial court.

2. *Barr v. SEC*, 114 F.4th 441 (5th Cir. 2024).

Two whistleblowers petitioned the Fifth Circuit to review an SEC determination that effectively denied them whistleblower awards. The principal issue was whether the SEC was required to pay whistleblower awards on a civil judgment after the Company filed for Chapter 11 – specifically, whether the SEC's motion to appoint a trustee in the bankruptcy action was part of "single enforcement strategy" that transformed the bankruptcy into a "covered judicial or administrative action or related action" under Dodd-Frank's whistleblower provisions. The Court denied the petition and ruled the SEC did not abuse its discretion in refusing to pay whistleblower awards predicated on the bankruptcy case. *Id.* at 452.

Factual and Procedural Background

The whistleblowers, John Barr and John McPherson, gave the SEC information about Life Partners Holdings, Inc., that led to a $38.7 million securities fraud judgment against the company. After the SEC moved for appointment of a receiver, the company filed for bankruptcy protection under Chapter 11. While the bankruptcy action was pending, the SEC posted a Notice of Covered Awards, inviting individuals to apply for whistleblower awards in connection with the successful enforcement action against Life Partners. The SEC preliminarily determined that McPherson but not Barr was entitled to an award of monetary sanctions "collected." The SEC explained, however, that the bankruptcy proceedings *did not* satisfy the statutory requirement for a "covered judicial or administrative action, or a related action" because the bankruptcy proceedings (1) did not arise under the federal securities laws; (2) were not brought by the SEC or DOJ; and (3) were not based on the same information that led to the successful enforcement of the covered action.

In its capacity as an unsecured judgment creditor, the SEC moved for appointment of a trustee in the bankruptcy court. The motion was granted, and the bankruptcy trustee proposed a plan that was ultimately confirmed. As part of that plan, the SEC agreed that if the company dismissed its appeal of the securities fraud action, the SEC would reallocate any amounts collected as a result of the enforcement-action judgment to the company's investors.

The SEC issued its final order regarding the whistleblower awards. It revised the recommendations to grant Barr 5% and McPherson 20% of the "amounts collected or to be collected in connection with" the SEC's enforcement action. In response to McPherson's objections, it noted that (1) it did not "walk away" from the collection of $38.7 million; (2) any collection would have been *de minimis* and dependent on winning the appeal; (3) the whistleblower calculation must be based on the "amount collected" under the statute not a hypothetical collection; and (4) if awards were based on a hypothetical collection amount, it would introduce uncertainty, inconsistency, and delay into the whistleblower award process.

Barr filed his petition for review in the Fifth Circuit, and McPherson filed his in the D.C. Circuit. The D.C. Circuit transferred McPherson's petition to the Fifth Circuit where it was consolidated with Barr's petition.

Court's Analysis and Ruling

By statute, whistleblower-award determinations are committed to the SEC's discretion and may only be set aside if they are found to be "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." *Id.* at 446 (citing 15 U.S.C. §78u-6(f) and quoting *Healthy Gulf v. U.S. Army Corps of Eng'rs*, 81 F.4th 510, 520 (5th Cir. 2023)). Dodd-Frank established a new whistleblower program to motivate people to tell the SEC about securities law violations. If a whistleblower voluntarily provides original information to the SEC that leads to the successful enforcement in a "covered judicial or administrative action" or "related action," the SEC must pay awards to the whistleblower(s) of not less than 10 percent or more than 30 percent "of what has been collected" of the monetary sanctions imposed in the action or related actions. *Id.* at 447 (citing 15 U.S.C.§ 78u-6(b)(1)(A)-(B)).

Applying the plain meaning of the statute, the Court ruled that the bankruptcy case was not a "covered judicial or administrative action" or a "related action" simply because the SEC filed a motion

to appoint the Chapter 11 trustee who then filed the bankruptcy action. First, cases are commenced by the filing of a petition, not a motion to appoint a trustee. *Id.* at 450 (quoting 11 U.S.C. §301(a)). Second, motions to appoint a trustee may only be filed after a bankruptcy action has been commenced. *Id.* (citing 11 U.S.C. §1104(a)). Third, while bankruptcy cases are an aggregation of individual controversies, that does not mean someone other than the SEC or DOJ can file the action to qualify for a whistleblower award. *Id.* ("Petitioners provide no authority explaining why the meaning of 'action brought' should be understood as something other than its ordinary meaning."). Fourth, the words "action" and "proceeding" are not synonyms. The term "proceeding" ordinarily refers to aspects of an already commenced action. *Id.* at 451. Nor was the bankruptcy case a "related action" or a continuation of a "single enforcement strategy" by the SEC. Continuing an action is not the same thing as bringing an action, and the continuation argument does not comport with the ordinary meaning of bringing an action. *Id.* at 451-52.

The Court also rejected McPherson's argument that the SEC should have exercised its discretion to award him a larger amount. While the SEC has authority to exempt whistleblowers from certain rules, McPherson failed to demonstrate that the SEC abused its discretion in declining to exempt McPherson from the statutory limits. *Id.* at 452-53. Given the number of recent cases in which the Supreme Court and the Fifth Circuit have refused to defer to the SEC and other administrative agencies, this ruling that the SEC has some discretion in the area of whistleblower awards is interesting.

3. *SEC v. Stack*, 2024 WL 4199017 (5th Cir. Sept. 16, 2024).

In this long-running civil enforcement action,[1] the Fifth Circuit reversed the trial court's order requiring William Stack to disgorge the entire amount of investor loss ($333,110). The Court cited the Supreme Court's concern about joint and several disgorgement liability in SEC cases and its admonition that it might be "at odds" with traditional equitable principles requiring "individual liability for wrongful profits." *Id.* at *2 (quoting *Liu v. SEC*, 591 U.S. 71, 90 (2020). Noting that $229,500 of the investor funds were wired to Stack's unindicted co-conspirator, the Court remanded the case for the district court to "recalculate a proper disgorgement award plus interest *limited to* the funds that Stack received and benefited from." *Id.* at *4 (emphasis added).

Factual and Procedural Background

Stack was a securities lawyer who represented individuals and entities in the over-the-counter penny stock market. He was broke and was persuaded by William S. Marshall to become the CEO, President, Treasurer, Secretary, and Director of Preston Royalty Corp, a shell corporation that purportedly specialized in financing gold mining operations. Stack raised $333,110 for Preston Royalty from more than 55 investors using a private offering memorandum and a business plan that contained numerous false statements. Stack kept $75,000 for himself for personal expenses and caused the corporation to transfer $16,500 to his then wife. The remaining $229,500 was wired to Marshall's gold mining company.

The SEC and Stack submitted an agreed Partial Judgment enjoining Stack from future violations and barring him from being an officer or director, selling penny stocks, or offering securities law advice. The parties agreed the court would later determine whether to "order disgorgement of ill-gotten gains and/or a civil penalty" and if so, how much. The District Court adopted the magistrate's

[1] *See* FH Newsletter 4Q21, at 4-5; FH Newsletter 1Q23, at 17-18.

recommended disgorgement award of $333,110 plus interest – the full amount of the proceeds obtained from investors. Stack appealed.

Court's Analysis and Ruling

The sole issue on appeal was whether the district court erred in ordering Stack to disgorge the entire amount of the alleged loss. Citing *Liu*, Stack argued that holding him liable for the amount of the investor loss was inconsistent with traditional equitable principles that required "individual liability for wrongful profits." *Id.* at *2.

The SEC argued the district court ordered disgorgement of the entire loss based on Stack's *own violations*. The Fifth Circuit rejected this characterization because (1) the magistrate judge expressly noted that "Stack should be held *jointly liable* for the full amount of money raised," (2) the record showed Stack's involvement in the scheme was limited, (3) the SEC admitted that Stack was not the "true control person" of the company, and (4) unlike the money held by a spouse in *Liu*, Stack and Marshall's finances were not commingled. *Id.* at *3 (citing *SEC v. Blackburn*, 15 F.4th 676 (5th Cir. 2021)). The Court held that disgorgement of the $229,500 in funds Stack transferred from Preston Royalty to Marshall was improper: "Holding Stack liable for funds he did not keep or benefit from does not constitute 'a reasonable approximation of a defendant's unjust enrichment,' as required by *Liu* and our precedent." *Id.* However, the Fifth Circuit directed the district court to consider whether the $16,500 Stack wired to his then-wife should be considered a benefit that Stack enjoyed. *Id.* at *4 (citing *SEC v. Contorinis*, 743 F.3d 296, 302 (2d Cir. 2014) (noting that a defendant could be forced to disgorge profits channeled to friends, family, or clients).

B. District Courts

1. *In re Alta Mesa Res., Inc. Secs. Litig.*, 2024 WL 3760481 (S.D. Tex. Aug. 12, 2024) (Hanks, J.).

In the latest chapter of this long-running securities fraud class action and opt-out case,[2] Judge Hanks granted substantial portions of defendants' motions for summary judgment, leaving for trial only control person claims against certain private equity and other corporate defendants arising from statements made by the CEO of Alta Mesa prior to the SPAC transaction.

Alta Mesa was formed as the result of a de-SPAC acquisition of upstream and midstream companies in Oklahoma's STACK shale play in early 2018. Less than two months after the merger was completed, the Company announced a $3.1 billion write down that constituted over 80% of its value. Twenty months later, the Company filed for bankruptcy, but the securities litigation filed before the bankruptcy continued. Plaintiffs asserted claims under Sections 10(b), 14(a), and 20(a) of the Exchange Act. The district court denied motions to dismiss the securities class action. The class action plaintiffs alleged that defendants inflated reserve and financial projections by using non-standard drilling techniques that departed from industry standards and falsely assured investors that the Company's problems were temporary.

Dismissal of claims relating to Alta Mesa's March 29, 2018 Form 10-K. Plaintiffs alleged five categories of misrepresentations in Alta Mesa's Form 10-K: (1) statements regarding third-party

[2] See 1Q21 Newsletter, at 12-14 and 2Q23 Newsletter, at 8-9.

midstream pipelines or facilities connected to Alta Mesa's gathering, processing, storage, and transportation assets, (2) internal controls, (3) upstream risk factors, (4) midstream risk factors, and (5) disclosure controls. The Court found that Plaintiffs failed to adduce any evidence showing that the statements were false or misleading when made.

Plaintiffs asserted that Alta Mesa's risk disclosures regarding third-party midstream facilities were misleading because they presented events that had already occurred as mere risks. The Court disagreed: "Assuming that risk disclosures can themselves constitute material misrepresentations, Plaintiffs have not presented evidence showing that the third-party midstream facilities disclosure presented as a risk an event that had already transpired when Alta Mesa filed its March 29, 2018 Form 10-K." *Id.* at 6 (citing *Lormand v. US Unwired, Inc.*, 565 F.3d 228, 246–47 (5th Cir. 2009); *see also Carlton v. Cannon*, 184 F. Supp. 3d 428, 492 (S.D. Tex. 2016)).

Plaintiffs alleged the following statement regarding internal controls was not misleading:

> This annual report does not include a report of management's assessment regarding internal control over financial reporting or an attestation report of the company's registered public accounting firm due to a transition period established by rules of the Securities and Exchange Commission for newly public companies. During the most recently completed fiscal quarter, there has been no change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

The Court found the statement was not misleading because – even assuming controls weaknesses existed at the time of the statement – (1) the statement expressly states that the company "had not conducted a comprehensive assessment of [its internal] controls" when it filed its 10-K and (2) there was no evidence that when the statement was made, that there had been any change in Alta Mesa's internal control over financial reporting during the most recently completed fiscal quarter.

The Court noted that "A risk disclosure can be actionably misleading if it frames 'as merely hypothetical' a risk that 'had a near certainty of causing financial disaster to the company.'" *Id.* at *13 (quoting *Karth v. Keryx Biopharmaceuticals, Inc.*, 6 F.4th 123, 138-39 (1st Cir. 2021). The Court, however, found that there was no evidence that the upstream or midstream risks disclosed by the Company had already materialized at the time the statements were made. Thus, these statements were not misleading.

Finally, the Court found that the Company's February 2019 announcement that it had "ineffective internal control over financial reporting" in connection with its $3.1 billion write-down did not constitute evidence that the statement in the March 2018 From 10-K that it had effective "disclosure controls" false or misleading. First, "disclosure controls and procedures" are distinct from "internal control over financial reporting." *Id.* at *17. *Compare* 17 C.F.R. § 240.13a-15(e) (defining "disclosure controls and procedures") *with* 17 C.F.R. § 240.13a-15(f) (defining "internal control over financial reporting"). Second, Plaintiffs failed to cite "evidence linking the $3.1 billion write-down to a deficiency in Alta Mesa's disclosure controls and procedures, and they do not explain exactly what the purported deficiencies in Alta Mesa's disclosure controls and procedures were." *Id.*

Control person liability. The Court noted that "'The precise legal standard' for ascertaining liability under Section 20(a) 'remains somewhat unclear.'" *Id.* at *18 (quoting *Carlton v. Cannon*, 2016

WL 3959164, at *4 (S.D. Tex. July 22, 2016)). The Court held, however, that "in order to create a triable fact issue on Section 20(a) liability, Plaintiffs must prove 'some facts beyond [defendant's] position or title from which it can reasonably be inferred that [defendant] had actual power or control over [a controlled person's] allegedly fraudulent actions[.]" *Id.* (quoting *In re Dynegy, Inc. Sec. Litig.*, 339 F. Supp. 2d 804, 913 (S.D. Tex. 2004)). The Court found that with respect to the majority of alleged violations, there was no evidence that the defendants "had the ability to control the specific transaction or activity upon which a primary violation is based." *Id.* at *19.

The Court, however, found that there was sufficient evidence that certain corporate defendants (a private equity firm, an investment firm, and a producer services firm) worked closely enough with the Company's pre-SPAC CEO to craft public statements for a jury to conclude that control person liability existed:

> [T]here is evidence in the record showing that representatives of HPS, BCE, and ARM worked extensively with Chappelle to craft public statements regarding AMH and Kingfisher before the SPAC transaction, while Chappelle was AMH's CEO. . . . Given the large ownership stakes held by HPS, BCE, and ARM in AMH and Kingfisher, the close relationship between AMH and Kingfisher, and Chappelle's position as AMH's CEO, the Court concludes that a reasonable jury could return a verdict for Plaintiffs on their Section 20(a) claims against HPS, BCE, and ARM for statements made by Chappelle that predate the SPAC transaction.

Id. at *25.

2. *SEC v. Bowen*, 2024 WL 3462359 (N.D. Tex. July 17, 2024) (Scholer, J.).

Judge Scholer denied Bowen's motion to dismiss the SEC's enforcement action involving the unregistered offer and sale of securities. The Court had previously granted a motion to dismiss the original complaint without prejudice based on Bowen's arguments that (1) he was not a maker of the alleged false statements, and (2) the SEC failed to satisfy the heightened pleading standards for fraud and scienter.[3] Based on the allegations in the SEC's amended complaint, however, the Court ruled the SEC plausibly alleged that Bowen "made" false statements in written materials and an investor phone call, and that he was aware of contrary information at the time the alleged false statements were made.

Factual Background

The SEC sued defendants Bowen, Baker, Kim, Cannon Operating Company LLC, and North Texas Minerals L.L.C. for selling unregistered securities, failing to register as brokers, and securities fraud. Bowen was the COO and sales manager of Cannon. The allegations focused on money raised for working interests in four Oklahoma wells. Bowen and Baker allegedly solicited investors and used salespeople paid on commission to find other investors. The offering documents sent to investors were misleading because they (1) misrepresented the actual production and profitability of prior wells, (2) failed to disclose negative information about Baker and Kim, (3) failed to disclose that Bowen had previously been sanctioned for selling unregistered securities, and (4) despite promises in the offering materials, defendants never opened a separate account to hold investor funds but instead deposited

[3] *See* FH Newsletter 3Q23, at 17-18.

them into Cannon's operating account where they were spent to pay the unauthorized (and undisclosed) commissions and excessive management expenses.

In the amended complaint, the SEC added allegations about a July 2018 sales call that Bowen made to "Investor A" about the Mustang 2 well in which he misrepresented the production history and profitability of Cannon's prior wells, stating "all of Canon's prior wells were profitable, had lots of production, and would generate manyfold returns. *Id.* at *5. He also allegedly told Investor A that neither Cannon nor its employees had any history of legal or regulatory problems when he knew that was not correct. Finally, the SEC alleged he did not disclose that investor funds would be used to pay commissions to unregistered salespeople. After the call, Investor A purchased a $30,000 working interest in the Mustang 2 well.

Court Analysis

"Maker" Liability. The Court concluded the SEC plausibly alleged Bowen was a "maker" of statements in the amended complaint based on the allegations that Baker and Bowen were "50/50 partners in Cannon," they "prepared the [Mustang 2 offering materials], and "exchanged drafts with each other and discussed the proposed changes amongst themselves until they were both satisfied with their work product." *Id.* at *4. These allegations were sufficient to suggest that Bowen did more than merely review and approve documents into which he had no input. *Id.* The Court rejected Bowen's argument that this was impermissible group pleading under *Southland*, noting that the SEC had provided "specific factual allegations" about how Bowen was "involve[d] in the formulation of … the entire document." *Southland Sec. Corp. v. INSpire Ins. Sols., Inc.*, 365 F.3d 353, 365 (5th Cir. 2004). In addition, the SEC adequately alleged that Bowen made the allegedly false statements on the call with Investor A.

Duty to Disclose Negative Information. With respect to Bowen's duty to disclose negative information about his co-defendant Baker, as well as his own involvement in the venture, the Court reached an interesting conclusion. The Court ruled that Bowen did not have a duty to disclose Baker's drug and weapons convictions and a cease-and-desist order from the South Carolina Securities Commission because a duty to speak the full truth only arises when a defendant undertakes to say something on a particular subject. The only affirmative representation in the offering materials concerned Baker's "years of experience" in the oil and gas industry. *Id.* at *6 (quoting *SEC v. Mapp*, 240 F. Supp. 3d 569, 580 (E.D. Tex. 2017)). Since the affirmative representation only concerned Baker's years of experience, Bowen was not required to disclose his "unrelated criminal history." *Id.*

The Court reached a different conclusion about Bowen's duty to disclose his own involvement in the venture. While the offering materials contained no reference to Bowen, the Fifth Circuit has stated that a reasonable investor would want to know the true identity of who was leading the company. *Id.* (quoting *SEC v. Blackburn* , 15 F.4th 676, 681 (5th Cir. 2021)). Since the offering materials referred to Baker as part of Cannon's leadership, the Court ruled Bowen had a duty to disclose his own involvement as well.

Scienter. The Court easily concluded the amended complaint alleged scienter for each of the alleged misrepresentations. First, Bowen knew statements about the production and profitability of Cannon's wells were false or misleading because he and Bowen met once or twice a month to discuss Cannon's production numbers and 2016 offering materials used by Bowen described the production declines of two wells in detail. Second, as to commissions paid to unregistered salespeople, the

amended complaint alleged that Bowen oversaw Cannon's sales and marketing efforts, determined the amount of commissions paid on each sale, prepared the Mustang 2 Offering Materials that failed to disclose the commissions, and knew that the commissions violated Section 15(a) because he had previously been charged with securities violations for similar conduct. Third, Bowen knew of his own involvement in the venture and was told of Baker's prior convictions. Finally, Bowen was motivated to commit securities fraud because he received commissions and determined the amount of commissions on each sale.

Claims for unregistered sales of securities. The Court found that the allegations that Bowen prepared and reviewed the Mustang 2 Offering Materials and personally met with at least one investor were sufficient to plausibly allege participant liability. *Id.* at *10. The Court also found that the SEC alleged that Bowen received transaction-based compensation which is the hallmark of the broker dealer. *Id.* at *11. Interestingly, the Court considered the SEC's allegations "holistically" to reach its conclusions.

3. *Hu v. Ask America, LLC*, 2024 WL 3278957 (N.D. Tex. July 1, 2024) (Starr, J.).

In this declaratory judgment action with counterclaims for breach of contract and fraud arising out of an IPO, Judge Starr denied motions to dismiss each of the counterclaims. The Court ruled the counterclaims alleged sufficient factual information to plausibly state a claim for relief.

Vaxxinity, Inc.'s IPO was scheduled to occur on November 11, 2021. The day before the IPO, Mei Mei Hu and Louis Garfield Reese, IV, told Ask America, LLC that they knew an investor, James Chui, who had committed to buy $20 million of shares in the IPO but could not transfer his money from overseas before the closing date. They said that if Ask America would purchase the $20 million in stock, Chui would repurchase it within three months. In addition, Hu and Reese promised to personally cover any investment loss and guarantee Ask America a minimum return on investment of $3.6 million. Ask America bought the shares and entered into a guaranty contract with Hu and Reese.

Hu sued for a declaratory judgment that the guaranty contract was unenforceable and void. Ask American filed counterclaims and cross claims against Hu, Reese, and Vaxxinity for breach of contract, fraud, and violations of the Texas Securities Act. Hu, Reese, and Vaxxinity filed motions to dismiss the counterclaims against them.

In a short opinion, the Court reviewed the elements of each cause of action and the legal standard for motions to dismiss. Without reciting the allegations in detail, it concluded that each counterclaim sufficiently alleged factual matter to plausibly state a claim for relief. With respect to the guaranty contract, the Court ruled the complaint plausibly alleged it was an investment contract for purposes of the Texas Securities Act. *Id.* at *3 (quoting *Life Partners, Inc. v. Arnold*, 464 S.W.3d 660, 681 (Tex. 2015)).

4. *McLeod v. Pershing, LLC*, 2024 WL 3333237 (N.D. Tex. July 8, 2024) (Godbey, J.).

Judge Godbey granted in part and denied in part summary judgment to Pershing, LLC, the clearing firm for Stanford Group Company's brokerage accounts. The decision denying summary judgment on limitations grounds is similar to the Court's earlier ruling in *Sanford v. Pershing, LLC*.[4]

The *McLeod* plaintiffs were originally included in a putative class action styled *Turk v. Pershing, LLC*, Case No. 3:09-CV-2199-N (N.D. Tex) filed on November 18, 2009. The *Turk* plaintiffs stipulated to a narrower class definition on June 25, 2010 that excluded some of the original class members. On May 5, 2016, the *McLeod* plaintiffs filed their complaint in the instant action. Pershing moved for summary judgment on limitations and other grounds discussed below.

Statute of Limitations

Combining New Jersey's discovery rule and *American Pipe* tolling, the Court found plaintiffs' claims were timely.

Pershing claimed plaintiffs' May 5, 2016 complaint was untimely under New Jersey's six-year statute of limitations because plaintiffs became aware or should have become aware of their claims against Pershing more than six years earlier – on or about February 17, 2009 when the SEC announced it had brought a receivership action against the Stanford entities. Further, Pershing's relationship with the Stanford entities was obvious from plaintiffs' account statements. Thus, Pershing argued, plaintiff's claims for fraud and aiding and abetting fraud were untimely.

Plaintiffs made two arguments. Plaintiffs first argued under the discovery rule that their claims did not accrue until November 18, 2009, the date the *Turk* putative class action against Pershing was filed. The SEC's receivership action in February 2009 did not put them on notice of potential claims because it focused solely on Stanford's wrongdoing and presented Pershing as one of the "good guys." Pershing countered that the SEC action against the Stanford entities was sufficient notice for other plaintiffs to become aware of their claims against Pershing since they sued Pershing within two months of the SEC's February 2009 action. The Court found the discovery rule extended the accrual of the statute of limitations to November 18, 2009: "Reasonable minds could differ as to whether other suits predating the *Turk* complaint or any media coverage should have notified Plaintiffs of their potential claims against Pershing. On this evidence, a genuine dispute of material fact exists as to when Plaintiffs discovered, or in the exercise of ordinary diligence would have discovered, that Pershing allegedly caused or contributed to their injuries." *Id.* at *5. However, since November 18, 2009 is still more than six years before the first complaint was filed, Plaintiffs made a second argument to extend the accrual date.

Plaintiffs invoked *American Pipe* tolling, reasoning that their individual claims were tolled from the date the *Turk* class action complaint was filed until June 25, 2010, when the class definition in *Turk* was modified to exclude certain plaintiffs, including the *McLeod* plaintiffs. The Court accepted this argument. While the Supreme Court of New Jersey had not adopted *American Pipe* tolling, the Court noted that the Third Circuit had accepted *American Pipe* tolling and concluded that New Jersey state courts probably would as well. *Id.* at *7 (citing *Aly v. Valeant Pharm. Int'l Inc.*, 1 F.4th 168, 174, 180 (3d

[4] *See* FH Newsletter, 2Q24, at 14-15.

Cir. 2021)). By combining the discovery rule and *American Pipe* tolling, plaintiffs successfully argued their claims did not accrue until June 2016, so their May 5, 2016 complaint was timely.

Holder Claims

Pershing also sought to bar claims relating to any CDs purchased before December 27, 2005. Plaintiffs' theory was that Pershing made misrepresentations prior to this date that were relayed to them and induced them to renew or refrain from renewing their CDs. Pershing argued these were impermissible "holder" claims, i.e., claims based on alleged material misrepresentations or omissions that caused plaintiffs to retain ownership of securities they already owned. Thus, there was no "purchase or sale" as required for federal securities law claims. Holder claims under the federal securities laws are barred under *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 755, 738, n. 9 (1975), but the U.S. Supreme Court did not extend that rule to state common law claims. Noting that no New Jersey court had ruled on the viability of holder claims in the context of common law fraud, the Court declined to extend *Blue Chip Stamps* to New Jersey common law fraud claims. *Id.* at *8. Pershing also argued there was no evidence that it had made any actionable misrepresentations and that evidence of several other elements of fraud was lacking, but the Court ruled that a genuine issue of material fact existed as to all elements of the state fraud claim and denied the motion. *Id.* at *9-10.

Aiding and Abetting Fraud Claims

The Court denied Pershing's a motion for summary judgment on plaintiffs' aiding and abetting claim. This claim requires plaintiffs to show (1) Stanford's fraud against plaintiffs; (2) Pershing's general awareness of its role as part of an overall illegal tortious activity at the time that it provided assistance; and (3) that Pershing knowingly and substantially assisted the underlying fraud. *Id.* at *11.

The Court concluded that genuine issues of material fact on each element precluded summary judgment. First, the Court's prior rulings demonstrated the fraud engaged in by the Stanford entities. Second, Pershing's general awareness was supported by testimony and documents reflecting Pershing's concerns about Stanford, including the amount of revenue coming from CDs, the potential source of Stanford's personal funding, and Stanford's refusal to allow an independent financial audit despite Pershing's repeated requests. While Pershing argued these were mere "red flags" insufficient to demonstrate general awareness, the Court ruled that a juror could find that Pershing derived a financial benefit from the relationship and possessed a general awareness it was participating in improper activities. Finally, Pershing's substantial assistance was demonstrated by providing services to Stanford that were not ministerial or routine, including actively assisting in the recruitment of financial advisers; issuing account statements to investors with Pershing's name at the bottom of the statement; and otherwise lending the credibility of Pershing's name to Stanford's fraudulent scheme.

5. *Architectural Granite & Marble, LLC v. Pental*, 2024 WL 3683713 (N.D. Tex. Aug. 6, 2024) (Lindsay, J.).

Judge Lindsay granted summary judgment dismissing the counterclaim of a former employee who alleged he was fired in retaliation for raising a potential securities law violation with management before the company went public. *Id.* at *1, *35. The Court found the former employee lacked evidence that he suffered a materially adverse action necessary to support a SOX retaliation claim. *Id.* at *17. Further, the Court found that even if the former employee could prove the elements of a SOX

retaliation claim, the company presented clear and convincing evidence that it would have taken the same actions whether the employee engaged in protected activity or not. *Id.* at *35.

Factual Background

Former employee Peter Pental was sued by his former employer Architectural Granite & Marble LLC (AGM) and its parent Select Interior Concepts, Inc. (SIC) (collectively, the "Company") for breaching the confidentiality provisions in his employment agreement when he started a competing business. Pental filed a SOX retaliation counterclaim against the defendants. Pental and his brother sold their company to AGM in 2017, and Pental stayed on as AGM's President. During the summer of 2018, just before SIC went public, Pental and another employee expressed concern that the Company's SEC filings artificially inflated revenues in anticipation of SIC going public. Pental claimed that within a month of raising these accounting concerns, the Company's officers "embarked on a joint campaign and pattern of escalating retaliatory actions" to drive him and the other employee out of the Company.

The evidence showed that Pental filed an HR complaint against Sunil Palakodati and later sent a lengthy email criticizing Palakodati's leadership and business decisions, and blaming him for employee turnover. This led to internal discussions at the Company about a new role for Pental reporting to someone other than Palakodati but remaining at his current salary. Pental resisted the change and eventually sent notice that he intended to terminate his employment for good cause and pursue claims for constructive discharge and retaliation. After his departure, he filed suit. The Company moved for summary judgment on Pentel's SOX retaliation counterclaim.

Applicable Law and Analysis

The elements of a SOX retaliation claim are (1) the employee engaged in protected activity; (2) the employer knew that the employee engaged in the protected activity; (3) the employee suffered an unfavorable personnel action; and (4) the protected activity was a contributing factor in the unfavorable action. *Allen v. Administrative Rev. Bd.*, 514 F.3d 468, 475-76 (5th Cir. 2008). If the employee establishes these four elements, the burden shifts to the employer to prove "by clear and convincing evidence" that it "would have taken the same unfavorable personnel action in the absence of that behavior." *Murray v. UBS Sec., LLC*, 601 U.S. 23, 24 (2024). To rise to the level of prohibited retaliation, the "adverse action" must be "materially adverse," i.e., "an action harmful enough that it well might have dissuaded a reasonable worker from engaging in statutorily protected whistleblowing." *Burlington Northern & Santa Fe Railway Co. v. White*, 548 U.S. 53 (2006). Although it was unclear whether the Fifth Circuit would conclude that constructive discharge qualifies as an adverse employment action in a SOX retaliation claim, the Court assumed it would for purposes of summary judgment.

After reviewing the allegations and evidence, the Court concluded that Pentel's claims of retaliation were not supported by the evidence and amounted to no more than speculation. The Court concluded that, at most, the evidence suggested the cumulative effect of the Company's actions made Mr. Pental subjectively unhappy and frustrated. The Court found that Mr. Pental failed to establish that he suffered a materially adverse action, an essential element of his SOX retaliation claim. Memorandum Opinion and Order, at *31.

In addition, the Court found the evidence consistently showed that the Company attempted to address the dysfunctional relationships between Pental, Palakodati, and the other employee and what would happen if they could not get along. The Court rejected Pentel's theory that the Company intended to fire him for reporting the SIC accounting issues. The Court ruled the Company was entitled to judgment as a matter of law because it showed by clear and convincing evidence that it would have taken the same actions under the circumstances, and it dismissed the SOX retaliation claim with prejudice.

6. *Global Advantech Res. Ltd. v. Hayes*, 2024 WL 4338665 (S.D. Tex. Sept. 27, 2024) (Hoyt, J.).

This litigation arises out of the alleged breach of a non-disclosure agreement between Global Advantech Resources Limited ("GARL") and Alta Mesa Holding, L.P. GARL designed a proprietary water treatment system that reduced costs in oil and gas production. GARL submitted proposals to Alta Mesa and met with Dale Hayes, an Alta Mesa engineer and vice president, who signed a non-disclosure agreement relating to the proposals. Although Alta Mesa claimed it did not intend to use GARL's technology, Hayes later divulged that Alta Mesa had submitted GARL's proposal as part of a project application and additional documents showed other Alta Mesa entities were involved in the application process.

When Alta Mesa filed for bankruptcy, GARL filed suit against Alta Mesa VP Hayes and four defendants somehow related to the project or Alta Mesa. The Court described the petition as a " 'throw-the-book' vilification of the defendants' handling of GARL's confidential information" with eight claims asserted, including fraudulent inducement, common law fraud, constructive fraud, conspiracy, violation of the Texas Securities Act, and other statutory causes of action. Defendants moved to dismiss on various grounds, including the economic loss rule, statute of limitations, and lack of standing to pursue alter ego claims.

The Court acknowledged that "any number of GARL's claims may be dismissed at an appropriate time based on the lack of evidence of lack of jurisdiction." *Id.* at *3. However, the claims could not be dismissed under FRCP 12(b)(6) because the factual allegations were sufficient to state a claim. *Id.* (citing *Bell Atl. Corp. v. Twombly*, 550 U.S. 544 (2007)).

Rejecting defendants' arguments that they should be dismissed because they were not alter egos, the Court stated:

> [T]he entity tracks of the defendants betray their motives. As related entities they are sufficiently tied together to make it impossible for the Court to trace the interest of the individuals and the entities to any degree of certainty. As such, the Court presumes the labyrinthian nature of the relationships between the individuals and entities is of such a nature that it is simply impossible to untangle the network of interests. It is not the province of this Court to unravel the relationships between and among the individuals and entities. Instead, discovery is necessary to unravel [the] kinks. In this respect, the Court's review of the motions is limited to the plaintiff's allegations in the complaint and to any documents proffered and; there, finds disputed facts.

Id. The Court denied all defendants' motions to dismiss.

7. *State Farm Mut. Auto. Ins. Co. v. Complete Pain Solutions, Inc.*, 2024 WL 3488256 (S.D. Tex. July 18, 2024) (Hanen, J.).

State Farm sued doctors and their clinics for submitting false claims to insurance. Defendant Doctors Alj Florence Sparrow and See Loony Chin (collectively "Doctors") worked at Defendant Complete Pain Solutions, PLLC and Defendant MMRI Holdco Rollover LLC (collectively "Clinic") to provide Plaintiff State Farm insureds medical care in connection with injuries allegedly sustained in automobile accidents. 2024 WL 3488256, *1. After a lengthy investigation of nearly 500 individual patients of the Clinic, State Farm concluded that the Doctors and Clinic were submitting bills for predetermined, false and/or medically unnecessary treatment that caused State Farm to mail settlement checks. *Id.* State Farm sued the Doctors, alleging three causes of action: (1) an enterprise violation under RICO, 18 U.S.C. § 1962(c); (2) a separate civil conspiracy violation under RICO, 18 U.S.C. § 1962(d); and (3), a Texas common law claim for "money had and received" (against the Doctors and Clinic). *Id.* at *3-4. Defendants moved for summary judgment on all claims.

Judge Hanen granted Defendants' motion for summary judgment on (1) Plaintiff State Farm's RICO claims against the two individual doctor defendants with respect to nine potential claimants in dispute; and (2) State Farm's common law "money had and received" cause of action against the same individual doctor defendants. The Court denied Defendants' motion for summary judgment on (1) State Farm's RICO claims as to 18 claim numbers against the Doctors and (2) State Farm's "money had and received" claim against the Clinic.

A. Objections to Evidence

Defendants exhaustively objected to State Farm's summary judgment evidence, including purported omissions under the rule of "optional completeness" and undesignated witnesses acting as declarants. The Court determined that these objections were "quite frankly [] not a worthwhile objection at this stage in the proceeding" because it was "more focused on the content of the proof," and the opposing party need only attach any purportedly omitted portion to its reply. *Id.* at *1. The Court, however, agreed with Defendant's criticism of State Farm's broad failure to include pinpoint citations within lengthy exhibits or marshal its own evidence to controvert Defendants' arguments. The Court excoriated State Farm's approach to citing evidence as "at best, unsatisfactory, and at worst shoddy and haphazard." *Id.* at *3. Although "it is not the duty of the Court to search the record for evidence that might establish an issue," the Court admonished that such failure "does not make the exhibit improper—it just makes the brief poorly drafted, and it may ultimately cause that party to lose the motion." *Id.*

B. RICO Claims

State Farm asserted the RICO claims only against the Doctors. State Farm claimed that the Clinic was the enterprise under RICO, and that the Doctors were associated with or employed by the Clinic/enterprise. The Clinic's affairs were conducted through a pattern of racketeering through the creation and presentation of fraudulent bills and other documents for medical services that were either not legitimately performed or were not medically necessary. These purportedly fraudulent documents caused State Farm to mail settlement checks. *Id.* at *5. The Doctors also allegedly conspired to conduct the affairs of the Clinic/enterprise through submitting, or assisting in submitting, fraudulent bills and related documents through the mail, which resulted in State Farm mailing settlement checks. *Id.*

Defendants argued that (1) State Farm lacked standing, primarily because it could not establish causation or reliance; (2) State Farm lacked evidence that the Doctors "controlled" the affairs of the Clinic; (3) State Farm lacked evidence of mail fraud because there was no evidence of fraudulent conduct or intent to deceive; and (4) State Farm lacked evidence of conspiracy under 18 U.S.C. §1962(d).

The Doctors argued that attacked State Farm lacked standing to bring RICO claims because it lacked proof of causation, damages, or reliance. The Court rejected the Doctors' argument that State Farm must prove that it would not have settled the claims but for the Doctors' conduct. Instead, State Farm was only required to show that it would not have paid as much as it did. *Id.* "[R]ather than give the Court a hint of what this controverting evidence might be," State Farm sent the Court on a "treasure hunt." This failure to marshal its evidence would have been fatal, but, without State Farm's assistance, the Court found evidence that raised a fact issue on "the pertinent causation issues regardless as to how they are framed" with respect to 18 of the 27 claim numbers at issue. *Id.* at *7.

The Doctors next argued there was no evidence that they were involved in the affairs of the Clinic. Noting that in the Fifth Circuit, "conduct" and "participate" require evidence of some supervisory involvement in an enterprise to satisfy §1962(c), the Court found sufficient evidence to raise a fact issue as to the Doctors' roles in the alleged enterprise. *Id.* at *8. The Doctors were the sole medical providers that performed the purportedly unnecessary services. Neither Doctor was supervised by Clinic personnel, and both Doctors knew the Clinic was billing for their services. The bills were created using the Doctors' names, and the bills were "key to trigger payment." Each Doctor oversaw their record keeping, and each made their own diagnoses and treatment recommendations. "The doctors' participation here was key. The alleged scheme could not have been successful without them." *Id.*

The Court also refused to hold as a matter of law that no conspiracy under RICO existed. Although RICO civil conspiracy claims routinely fail because the plaintiff fails properly to allege a violation of §1962(c), given the multiple individuals and possible entities involved in the alleged activities, the Court determined there was sufficient evidence to require a decision from the finder of fact. *Id.* at *9.

C. Mail Fraud Claim

The Court found sufficient circumstantial evidence to support a finding that the Doctors acted with fraudulent intent on the mail fraud count. *Id.* at *10. State Farm pointed to evidence that the medical records and bills in over 450 cases were false or indicative of unnecessary treatment. State Farm's expert further opined that over 250 charts contained the same diagnosis, the same prognosis, and the same treatment. The Court also noted some evidence that the co-workers at the Clinic coordinated with various claimants' attorneys as to the care, treatment, and billing of the claimants. State Farm also noted that the Doctors used a similar protocol for which the Clinic was compensated by using bills that purported to seek compensation for fraudulent or unnecessary treatment. *Id.* at *9. This evidence was sufficient to support a finding of fraudulent intent.

D. Money Had and Received Claim

Seeking to defeat the Texas common law "money had and received" claim, Defendants argued that: (1) State Farm's claims were barred by the two-year statute of limitations; (2) the claims are barred because a written contract precluded recovery under this quasi-contractual theory; and (3) there was

no evidence that the "money" at issue belonged to State Farm. *Id.* at *3. The uncontroverted evidence was that neither Doctor received funds directly or indirectly from State Farm. The Doctors were paid either a flat rate based on the procedure or an annual salary by an unrelated limited liability company. *Id.* at *13. The Clinic received funds from State Farm, and it kept all profits. Accordingly, the Court granted summary judgment as to the Doctors but denied summary judgment as to the Clinic. *Id.*

II. STATE CASES

A. Breach of Fiduciary Duty

1. *Texas A&M University 12th Man Foundation v. Hines*, 2024 WL 2972774 (Tex. App. – Beaumont June 13, 2024) (Wright, J.).

This short opinion on Texas procedure will be of keen interest to many Texas A&M football fans, not because the opinion makes new procedural law but because it involves claims against Texas A&M's 12th Man Foundation and donations to renovate Kyle Field. In a six-page opinion, the Court of Appeals ruled that (1) claims for breach of fiduciary duty and breach of the duty of good faith against the Foundation should be dismissed; but (2) claims for breach of contract and promissory estoppel could proceed.

Factual and Procedural Background

The Foundation, previously known as the Aggie Club, is a charitable organization that promotes A&M sports, including financing athletic scholarships. In the 1970s, the Foundation raised money by promising prospective donors they would receive desirable seats at A&M football games and other benefits such as preferred parking. The plaintiffs were some of these donors, and they alleged they were promised the "best available seats" at the stadium for the duration of their endowments which, in some cases, allegedly lasted their lifetimes.

When Texas A&M joined the Southeast Conference in 2011, the University decided to renovate Kyle Field. To raise funds for the renovation, the Foundation solicited new donations and decided to relocate the seats of some previous donors, including those who claimed they had been promised the "best available seats" for the duration of their respective endowments. Many of the displaced donors were unhappy with their new seats. Anticipating this reaction, the Foundation offered to return their original donations. Some accepted, but others sued the Foundation for breach of contract, promissory estoppel, and other causes of action. A flood of procedural maneuvers followed, including the filing of four amended petitions, a class certification motion (denied), and a change of venue.

This appeal addressed the Foundation's motion to dismiss under the Texas Citizens' Participation Act (TCPA) the Fourth Amended Petition, which asserted new claims for breach of fiduciary duty and breach of the duties of good faith and fair dealing.

The Court's Analysis

The TCPA provides a three-step process for dismissal of a case. First, the movant bears the burden to show that the legal action is based on or in response to the movant's exercise of (1) the right of free speech; (2) the right to petition; or (3) the right of association. Second, the burden shifts to the Plaintiff to establish by clear and specific evidence a prima facie case for each essential element

of the claim in question. Third, the burden shifts back to the movant to establish each essential element of an affirmative defense by a preponderance of the evidence. Notably, a motion to dismiss under the TCPA must be timely – filed not later than the 60th day after the date of service of the legal action.

The TCPA defines "exercise of the right of association" as "joining together to collectively express, promote, pursue or defend common interests relating to a governmental proceeding or matter of public concern." Plaintiffs did not dispute that the Foundation met the "right of association" aspect of this test, but they challenged the notion that the lawsuit related to a "matter of public concern." Plaintiffs relied on *McLane Champions, LLC v. Houston Baseball Partners LLC*, 671 S.W.3d 907, 910 (Tex. 2023), but the Court distinguished that case "which involved a purely private party buying a privately-owned sports team from another private party." By contrast, the Foundations' "activities are inextricably linked to a public university that is largely supported by public funds." *Id.* at *4. ("Kyle Field even though built with donations is still owned by A&M.") In short, building a "first class stadium" for a public university made the suit a matter of public concern under the TCPA.

Turning to the Plaintiffs' prima facie case, the Court found the exhibits attached to the Petition failed to show that the Foundation owed a fiduciary duty to Plaintiffs or that a special relationship existed giving rise to a fiduciary duty of care on the part of the Foundation. In particular, the Court noted that officers and directors of a non-profit owe duties to the organization but not to its members. The Court also rejected plaintiffs' novel argument that "Aggie loyalty" and "Aggie core values" created a special relationship that was legally protected.

Although the TCPA barred plaintiffs' new claims for breach of fiduciary duty and breach of the duties of good faith and fair dealing, the Court ruled that Defendants missed the TCPA 60-day deadline with respect to the breach of contract and promissory estoppel claims that were alleged in the original and first amended petitions. Accordingly, the TCPA did not bar those claims.

2. ***Montoya v. State*, 2024 WL 3897468 (Tex. App. – Dallas Aug. 22, 2024) (Miskel, J.).**

The Court affirmed the securities fraud conviction of a pastor who solicited money from his church members to invest in real estate. The pastor pleaded guilty to securities fraud before a jury but claimed on appeal that his plea was not knowing and voluntary due to ineffective assistance of counsel. After reviewing the applicable legal standards and the lack of evidence concerning ineffective assistance of counsel, the Court affirmed the securities fraud conviction. The Court also affirmed the convictions for theft and money laundering.

Factual and Procedural Background

Montoya worked as a pastor in Texas. At some point, he claimed to start making real estate investments. Montoya took money for these alleged investments from church members and others who learned by word of mouth. Investors received brochures and post-dated checks as security for their investments, and their investment contracts were signed before a notary public.

An investigator for the Texas State Securities Board (TSSB) concluded Montoya operated a common enterprise that pooled investors' money with an expectation of profit from real estate investments, house flipping, and construction of new houses. The securities issued by Montoya's

company were not registered, and Montoya was not a registered securities dealer. In addition, the materials Montoya gave to investors contained false statements, including claims that: (1) his company was founded in 2010 when it was not created until 2017; (2) the company was a top real estate development company; and (3) it had five active projects, when only property belonged to Montoya. The TSSB determined that Montoya received nearly $1.4 million from investors, but they could not find that he made any purchases of land, houses, or building supplies. Instead, he placed investor funds in personal accounts, sent wires of $48,000 and $75,000 to a business entity in Brazil, and "structured" many transactions to be paid in cash or in amounts just below $10,000 to avoid bank reporting.

Montoya was indicted for securities fraud, theft, and money laundering. At his jury trial, he pleaded guilty to the securities fraud charge but not guilty to the theft and money laundering charges. The jury found him guilty of all three offenses and recommended he serve 40 years for each offense, to be served concurrently. The judge adopted the jury's sentencing recommendation and ordered Montoya to pay $587,595.51 in restitution.

Montoya appealed his conviction, arguing for the first time that his guilty plea on the securities fraud count was not knowing and voluntary. He claimed the real estate investments forming the basis of the offense were not securities and, as a result, the securities-fraud judgment was void as a matter of law. He claimed he did not understand this, that his attorney did not have sufficient knowledge and experience to provide effective assistance, and that the court did not ensure there was a factual basis for his guilty plea.[5]

Court's Analysis and Ruling on Securities Fraud Conviction

The Court began its analysis by noting that Montoya conflated several different legal standards into a single issue—the requirement that guilty pleas are knowingly and voluntarily made, sufficiency of the evidence, ineffective assistance of counsel, and actual innocence. It emphasized that Montoya *did not* claim that the trial court failed to properly admonish him, that he did not understand the consequences of his plea, that he was coerced into making the plea, or that he was mentally incompetent to do so. The Court therefore construed Montoya's argument as complaining that his guilty pleas was not made voluntarily and knowingly because of ineffective assistance of counsel.

The Court explained the different legal standards that apply when a defendant pleads guilty to a jury and to a court. When a defendant pleads guilty to a jury rather than to the court, article 1.15 of the TEXAS CODE OF CRIMINAL PROCEDURE does not apply and there is no need to introduce evidence showing the defendant's guilt. *Id.* at *3 (citing *Holland v. State*, 761 S.W.2d 307, 313 (Tex. Crim. App. 1988) and other cases). When a defendant pleads guilty to a jury, the court should instruct the jury to return a guilty verdict and decide only the issue of punishment. *Id.* (citing *In re State ex. rel. Tharp*, 393 S.W.3d 751, 757 (Tex. Crim. App. 2012). By contrast, when a defendant waives his right to a jury trial and pleads guilty, the trial court may not render judgment unless the State produces sufficient evidence to support the conviction. *Id.* (citing *Menefee v. State*, 287 S.W.3d 9, 13 (Tex. Crim. App. 2009).

Addressing the ineffective assistance of counsel argument, the Court noted a defendant must show (1) counsel's performance was deficient; and (2) a reasonable probability exists that, but for

[5] Montoya also challenged the sufficiency of evidence to support his theft and money laundering convictions. The court reviewed the evidence presented at trial and affirmed these convictions.

counsel's deficient performance, the result of the proceeding would have been different. *Id.* at *4 (citing *Strickland v. Washington*, 466 U.S. 668, 687, 694 (1984)). The defendant bears the burden of proving both parts of the *Strickland* analysis by a preponderance of the evidence. *Id.* Counsel's performance is considered deficient if it falls below an objective standard of reasonableness, and there is a strong presumption that trial counsel's conduct fell within the wide range of reasonable professional assistance. *Id.* To defeat this presumption, claims must be firmly founded in the record; an appellate court will not speculate in its review. *Id.* Trial counsel should generally be given an opportunity to explain his actions before they are found to be ineffective. *Id.* In the face of an undeveloped record, counsel should be found ineffective *only if* his conduct was so outrageous that no competent attorney would have engaged in it. *Id.*

Because Montoya did not raise the ineffective assistance of counsel argument at the trial court, there was no hearing and no evidence in the record showing (1) what advice trial counsel provided or (2) whether or why Montoya was advised to plead guilty to securities fraud and not the other counts. Based on the record, the court rejected the ineffective assistance of counsel argument because it could not conclude there was no plausible reason for trial counsel's alleged advice.

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