

ORIGINAL

IN THE UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

U. S. DISTRICT COURT NORTHERN DISTRICT OF TEXAS
FILED
JUL 10 2000
NANCY DOHERTY, CLERK
By _____ Deputy

MICHAEL J. QUILLING, as Receiver
for Howe Financial Trust, MVP
Network, Inc. d/b/a MVP Trust,
and TREDs Financial Trust

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Plaintiff,

NO. 3-99-CV-2699-M

VS.

JAMES W. CONWAY, ET AL.

Defendants.

**FINDINGS AND RECOMMENDATION OF THE
UNITED STATES MAGISTRATE JUDGE**

Defendants James W. Conway and James W. Conway, P.S.C. have filed a motion to dismiss for lack of personal jurisdiction.¹ The motion has been referred to United States Magistrate Judge Jeff Kaplan for recommendation pursuant to 28 U.S.C. § 636(b).

I.

This case arises out of a lawsuit brought the Securities and Exchange Commission against 46 defendants and 13 "Relief Defendants" involving the sale of non-existent "prime bank" securities. *Securities and Exchange Commission v. Funding Resource Group, et al.*, No. 3-98-CV-2689-M. In that case, the SEC alleges that defendants raised more than \$14 million from unwitting investors by making false representations about the use and safety of investor proceeds and the expected rate of return on their investment. (Def. Am. Reply, App. at 2, ¶ 1). The SEC seeks injunctive relief and civil penalties against the defendants who actively participated in the

¹ Defendants also move to dismiss this case for failure to state a claim upon which relief can be granted. The Court need not address this aspect of the motion in view of the resolution of the jurisdictional issue.

fraud. (*Id.* at 29-33). The “Relief Defendants” were sued to recover all monies allegedly paid to them in furtherance of this scheme. (*Id.*, App. at 2-3, ¶ 2). MVP Network, Inc. d/b/a MVP Trust is a named defendant in the *Funding Resource* litigation. (*Id.*, App. at 3-4, ¶ 9). Howe Financial Trust and TREDIS Financial Trust are “Relief Defendants.” (*Id.*, App. at 5 ¶¶ 20-21).

On November 13, 1998, the district court appointed Michael J. Quilling as Receiver for all defendants and “Relief Defendants” in the *Funding Resource* case. (Rcvr. Response, Exh. 1).

As Receiver, Quilling was authorized to:

take custody, possession and control of any and all assets, monies, securities and properties, real and personal, tangible and intangible, of whatever kind and description, and wherever situated, belonging to [the named defendants] (hereinafter referred to as “Receivership Assets”), as well as any documents relating to the Receivership Assets.

(*Id.*, Exh. 1 at 2-3, ¶ B). The Receiver was further empowered “to institute, prosecute, compromise or adjust such actions or proceedings in state or federal court as may in his judgment be necessary or proper for the collection, preservation and maintenance of the Receivership Assets.” (*Id.*, Exh. 1 at 6-7, ¶ L).

On November 29, 1999, the Receiver filed this action against John W. Conway, a Kentucky attorney, and his law firm, John W. Conway, P.S.C. The complaint alleges that Conway acted as a lawyer and an escrow agent for Howe Financial Trust with respect to certain high interest loans made to Hammersmith Trust, LLC. (Complaint ¶¶ 7-8). The monies involved in these transactions came from 11 different investment groups, including MVP Network, Inc. d/b/a MVP Trust and TREDIS Financial Trust. (*Id.* ¶ 8). Hammersmith subsequently defaulted on the loans causing investors to lose more than \$2.7 million. (*Id.* ¶ 15). According to the Receiver, Conway should have known that the high interest loans made to Hammersmith were

“blatantly illegal and constitute[] a nonsensical transaction.” (*Id.* ¶ 13). He now sues Conway and his law firm for professional negligence, breach of contract, negligent misrepresentation, and aiding and abetting corporate waste. (*Id.* ¶¶ 16-28).

Defendants move to dismiss this case because they lack sufficient minimum contacts with the State of Texas to support the exercise of general or specific jurisdiction over them. The Receiver tacitly concedes this point. Nevertheless, he maintains that personal jurisdiction is proper under 28 U.S.C. §§ 1692 and 754. The issues have been briefed by the parties and the motion is ripe for determination.

II.

The exercise of personal jurisdiction over a defendant must always comport with the requirements of due process. When a federal court sitting in diversity attempts to exercise extraterritorial jurisdiction over a nonresident defendant, these requirements are met where the defendant has minimum contacts with the forum state. *Busch v. Buchman, Buchman & O'Brien, Law Firm*, 11 F.3d 1255, 1258 (5th Cir. 1994), citing *International Shoe Co. v. State of Washington, Office of Unemployment Compensation and Placement*, 326 U.S. 310, 315, 66 S.Ct. 154, 158, 90 L.Ed. 95 (1945); see also *Driver v. Helms*, 74 F.R.D. 382, 390 (D.R.I. 1977), *aff'd in relevant part and rev'd in part*, 577 F.2d 147 (1st Cir. 1978), *rev'd*, 100 S.Ct. 774 (1980). However, the due process analysis is different when personal jurisdiction is predicated on a federal statute that allows for nationwide service of process. In such cases, Congress has effectively provided for the national exercise of personal jurisdiction over a defendant based on his contacts with the United States. *Driver*, 74 F.R.D. at 390. Thus, “while the Due Process Clause must be satisfied if a forum is to acquire personal jurisdiction over a defendant, sovereignty defines the scope of the due process test.” *Busch*, 11 F.3d at 1258.

A.

The lawsuit brought by the Receiver against defendants is authorized by 28 U.S.C. § 1692.

That statute provides:

In proceedings in a district court where a receiver is appointed for property, real, personal, or mixed, situated in different districts, process may issue and be executed in any such district as if the property lay wholly within one district, but orders affecting the property shall be entered of record in each of such districts.

28 U.S.C. § 1692. Thus, the territorial jurisdiction of a receivership court extends to any district where property of the receivership estate may be located. *See Securities and Exchange Commission v. Vision Communications, Inc.*, 74 F.3d 287, 290 (D.C.Cir. 1996); *Haile v. Henderson National Bank*, 657 F.2d 816, 823 (6th Cir. 1981), *cert. denied*, 102 S.Ct. 1450 (1982). There is no question that James W. Conway and his law firm are residents of the United States. By this lawsuit, the Receiver seeks to recover property that belongs to the receivership estate. The Court therefore concludes that defendants have sufficient minimum contacts with this forum to satisfy the requirements of due process. *See Busch*, 11 F.3d at 1258.

B.

However, this does not resolve the jurisdictional issue raised by defendants. A federal district court cannot exercise personal jurisdiction over a nonresident defendant under 28 U.S.C. § 1692 unless the Receiver complies with the requirements of 28 U.S.C. § 754. That statute provides, in relevant part:

A receiver appointed in any civil action or proceeding involving property, real, personal or mixed, situated in different districts shall, upon giving bond as required by the court, be vested with complete jurisdiction and control of all such property with the right to take possession thereof.

* * * *

Such receiver shall, within ten days after the entry of his order of appointment, file copies of the complaint and such order of appointment in the district court for each district in which property is located. The failure to file such copies in any district shall divest the receiver of jurisdiction and control over all such property in that district.

28 U.S.C. § 754. Quilling was appointed as Receiver for Howe Financial Trust, MVP Network, Inc. d/b/a MVP Trust, and TREDIS Financial Trust on November 13, 1998. However, he did not immediately file a copy of the complaint in the *Funding Resource* case and his order of appointment in the United States District Court for the Western District of Kentucky. In fact, the Receiver did not file the necessary documents until March 2, 2000-- 31 days after defendants filed their motion to dismiss for lack of personal jurisdiction.² The question is whether the Receiver's admittedly tardy compliance with section 754 is sufficient to confer personal jurisdiction over defendants in this district.

Not surprisingly, there is paucity of authority on this issue. The few reported decisions on point have used different standards in analyzing the filing requirements of section 754. Some courts hold that late filing under this statute is excused unless the defendant demonstrates prejudice. See *Securities and Exchange Commission v. American Capital Investments, Inc.*, 98 F.3d 1133, 1142 (9th Cir. 1996), *cert. denied*, 117 S.Ct. 1468 (1997), *citing United States v. Arizona Fuels Corp.*, 739 F.2d 455, 460 (9th Cir. 1984); *Securities and Exchange Commission v. Equity Service Corp.*, 632 F.2d 1092, 1094-95 (3d Cir. 1980). Other courts insist that the language of the statute be strictly construed and that "late filing cannot establish jurisdiction

² Quilling obtained an order reappointing him as Receiver in the *Funding Resource* litigation on February 23, 2000. He filed a copy of this order and the underlying complaint in the Western District of Kentucky within ten days thereafter.

retroactively." *See Vision Communications*, 74 F.3d at 291. Courts that follow this later approach suggest that the only proper way for a receiver to acquire personal jurisdiction is to obtain an order of reappointment, thereby restarting the ten-day clock. *See id.*

The Court need not decide which of these approaches is legally correct because the Receiver has failed to establish personal jurisdiction over defendants under either standard. Under a strict construction of section 754, personal jurisdiction must exist at the time service of process is made. *Id.*; *see Prejean v. Sonatrach, Inc.*, 652 F.2d 1260, 1270 n.21 (5th Cir. 1981). Here, the Receiver neither alleged nor proved an adequate basis for jurisdiction over defendants at the time suit was filed.³ Of course, this does not preclude the Receiver from amending his complaint and obtaining new service if defendants later become amenable to personal jurisdiction during the pendency of the litigation. *See Prejean*, 652 F.2d at 1270 n.21. However, there is no evidence that the Receiver ever obtained new service upon defendants after he complied with the requirements of section 754.⁴

Even if the Receiver's late compliance with the statute is excusable, defendants clearly have been prejudiced by this delay. Under Kentucky law:

[A] civil action, whether brought in tort or contract, arising out of any act or omission in rendering, or failing to render, professional services for others shall be brought within one (1) year from the date of the occurrence or from the date when the cause of action was, or reasonably should have been discovered by the party injured.

³ The Receiver did not assert jurisdiction under 28 U.S.C. §§ 1692 and 754 until he filed his amended complaint on April 24, 2000. (Am. Complaint ¶ 3).

⁴ Nor does the amended complaint confer personal jurisdiction over defendants *post hoc*. An amendment that seeks to enlarge federal jurisdiction cannot relate back to the date of the original filing. *Lamb v. United States Postal Service*, 852 F.2d 845, 847 (5th Cir. 1988); *USM Corp. V. GKN Fasteners, Ltd.*, 578 F.2d 21, 22 (1st Cir. 1978).

KY. REV. STAT. ANN. § 413.245 (1980). All of the claims against defendants arise out of their alleged professional negligence. (Complaint ¶¶ 7-14; Am. Complaint ¶¶ 7-14). The Receiver states that he discovered the fraudulent nature of the loan transactions, the illegitimacy of Hammersmith, and the negligence of Conway in early December, 1998. (Complaint ¶ 15; Am. Complaint ¶ 15). Yet he waited until March 2, 2000 to file the documents necessary to acquire personal jurisdiction over defendants. This was almost three months after the statute of limitations expired. There is little doubt that defendants would be prejudiced if they are forced to defend a claim that is barred by limitations.

C.

Without a federal statute authorizing nationwide service of process, the Court cannot exercise personal jurisdiction over defendants unless they have sufficient minimum contacts with the State of Texas. The Receiver has offered no evidence or argument to suggest that such contacts exist. Consequently, this case must be dismissed.

RECOMMENDATION

Defendants' motion to dismiss for lack of personal jurisdiction should be granted. All claims against James W. Conway and James W. Conway, P.S.C. should be dismissed without prejudice.

DATED: July 10, 2000.


JEFF KAPLAN
UNITED STATES MAGISTRATE JUDGE