Filing # 11748442 Electronically Filed 03/25/2014 07:23:13 PM

IN THE CIRCUIT COURT OF THE SEVENTEENTH JUDICIAL CIRCUIT, IN AND FOR BROWARD COUNTY, FLORIDA

CASE NO.: 12-034123 (04)

P&S ASSOCIATES, GENERAL PARTNERSHIP, a Florida limited partnership, *et al.*,

Plaintiffs,

v.

MICHAEL D. SULLIVAN, *et al.*,

Defendants.
_____/

PLAINTIFFS' RESPONSE AND MEMORANDA IN OPPOSITION TO DEFENDANTS VINCENT T. KELLY AND KELCO FOUNDATION'S MOTION TO DISMISS

Plaintiffs P & S Associates, General Partnership ("P&S"), S & P Associates, General Partnership ("S&P") (collectively, the "Partnerships" or "Plaintiffs"), file this Response and Memoranda in Opposition to Defendants Kelco Foundation ("Kelco") and Vincent T. Kelly's ("Father Kelly") (collectively, "Defendants") Motion to Dismiss Plaintiffs' Second Amended Complaint (the "Motion"), and, in support, state as follows:

I. INTRODUCTION

The motion to dismiss should be denied for five reasons: (1) Father Kelly received and benefitted from transfers from P&S to Kelco because he operated Kelco; (2) the doctrine of *in pari delicto* does not bar Plaintiffs' claims because the former Managing General Partner of P&S was acting adversely to P&S, Plaintiffs and Defendants are not at equal fault, and Defendants' conduct is against public policy; (3) Father Kelly is a "broker" under Fla. Stat. § 475.41 because that statute does not only apply to real estate transactions; (4) Plaintiffs have standing to pursue

their claims because they are creditors under Florida law; and (5) Plaintiffs have alleged the existence of a fiduciary duty breached by Defendants because it is alleged that Defendants were partners of P&S and/or S&P.

II. STATEMENT OF FACTS

Defendant Father Kelly abused his position of trust and authority by soliciting individuals or entities in his congregation to invest in the Partnerships in return for kickbacks from the former Managing General Partner of the Partnerships, Michael Sullivan. Sullivan transferred those kickbacks from the Partnerships to Father Kelly's not for profit organization, Kelco, and those funds were then used for the benefit of Father Kelly.

In this manner, Kelly and Kelco received over $750,000 in kickbacks. Father Kelly received these kickbacks and recommended the Partnerships as investments to individuals and entities even though Father Kelly is not registered as investment advisor or broker, and did not comport with any of the minimum standard of care as it relates to the provision of investment advice. The kickbacks received by Kelly and Kelco were among the millions of dollars that Sullivan and his co-conspirators paid themselves in management fees derived from the principal contributions of other Partners, and not from the Partnerships' profits, as required under the Partnership Agreements.[1] It was through the efforts of Father Kelly to solicit additional investors that he was intimately involved in the inappropriate funneling of funds to the Managing Partners and others. The Managing Partners were only able to continuously divert funds from the Partnerships if there was a consistent stream of investors who placed their savings in his hands.

On or about March 10, 2014, Defendants filed the instant Motion seeking to dismiss the Complaint. As set forth below, the Motion should be summarily denied.

[1] *See* Section 5.02 of **Exhibits A and B** to the Complaint (emphasis added).

III. STANDARD OF REVIEW

In reviewing a motion to dismiss, the Court must construe the allegations of the complaint "in the light most favorable to plaintiffs and the trial court must not speculate what the true facts may be or what will be proved ultimately in trial of the cause." *Hitt v. North Broward Hosp. Dist.*, 387 So. 2d 482, 483 (Fla. 4th DCA 1980). The court is confined to consideration of the allegations found in the four corners of the complaint. *Baycon Indus., Inc. v. Shea*, 714 So. 2d 1094, 1095 (Fla. 2d DCA 1998). A motion to dismiss should be denied when a complaint sufficiently states a cause of action. *See Solorzano v. First Union Mortgage Corp.*, 896 So. 2d 847, 849 (Fla. 4th DCA 2005); *see also Fontainebleau Hotel Corp. v. Walters*, 246 So. 2d 563, 565-66 (Fla. 1971) (holding error to dismiss a complaint that contains sufficient allegations to acquaint the defendant with the plaintiff's charge of wrongdoing so that the defendant can intelligently answer the same).

IV. ARGUMENT

A. The Complaint States a Claim Against Father Kelly Because He Caused His Organization, Kelco, to Receive the Kickbacks

Defendants first argue that the Second Amended Complaint must be dismissed as to Father Kelly, because it was Father Kelly's organization, Kelco, that directly received the kickbacks from the Partnerships, but not Father Kelly, individually.

As set forth in the Second Amended Complaint, Father Kelly operated Kelco, caused Kelco to receive the funds from P&S by improperly soliciting individuals or entities to invest in the Partnerships, and Kelly benefitted from the funds that Kelly received: "[t]he Kelco Foundation, which was operated by Father Kelly, received $744,799.08 from P&S in Kickbacks. Kelly Participated in and assisted the Kelco receiving the Kickbacks alleged." Compl. ¶ 31(f). The Complaint further states that Father Kelly participated in all of the wrongdoing at issue, as

described in each substantive count of the Complaint. Accordingly, the Second Amended Complaint contains sufficient allegations which demonstrate Father Kelly was personally involved in the tortious conduct at issue, and states a claim upon which relief can be granted. *See Orlovsky*, 654 So. 2d at 1364 ("A motion to dismiss should not be granted if the pleader sets forth facts in his complaint upon which relief can be granted on any theory.").

Defendants' conclusory argument that Plaintiffs' claims for unjust enrichment, fraudulent transfer, and money had and received require an allegation that Kelly, individually, received the kickbacks is without support.

Moreover, to the extent that Defendant seeks to dismiss the remainder of Plaintiffs' claims for Breach of Fiduciary Duty, Aiding and Abetting a Breach of Fiduciary Duty, Negligence, and Civil Conspiracy on the same grounds, it is unnecessary to allege that an individual personally received a transfer of funds in order to state those claims, and Defendants fail to set forth any law to the contrary.

Finally, under Florida law, a corporate director, such as Father Kelly, can be held liable for torts allegedly committed by a corporation, so long as he personally participates in their commission – which is the case here. *See Roth v. Nautical Eng'g Corp.*, 654 So. 2d 978, 979 (Fla. 4th DCA 1995) ("A corporate officer may be individually liable for torts committed even while acting as the representative of the corporate entity."); *Orlovsky v. Solid Surf, Inc.*, 405 So. 2d 1363, 1364 (Fla. 4th DCA 1981).

B. Plaintiffs' Claims Are Not Barred by the Doctrine of *In Pari Delicto*

Defendants claim that the Second Amended Complaint must be dismissed under the doctrine of *in pari delicto*, or unclean hands, because the transfers at issue came from the Partnerships' accounts. However, Defendants' arguments should be rejected because (1) misconduct associated with the former Managing Partners' making transfers from the

Partnerships' accounts should not be imputed onto the Partnerships; (2) Defendants are not at equal fault with Plaintiffs; (3) applying the doctrine of *in pari delicto* here runs contrary to public policy and (4) the appointment of Margaret Smith, and later Phil Von Kahle, cleansed the Partnerships of any fault.

First, while the transfers at issue were made from P&S and/or S&P by entities controlled by Michael Sullivan and/or Greg Powell, including Michael D. Sullivan & Assoc., Inc. to Defendants, the adverse interest exception prevents the imputation of wrongdoing onto Plaintiffs. It is well established that a principal can only be liable for its agent's conduct when the agent is acting within the scope of his authority. *Roessler v. Novak*, 858 So.2d 1158, 1161 (Fla. 2d DCA 2003). If a corporate agent acts "adversely to the corporation's interests, the knowledge and misconduct of the agent are not imputed to the corporation." *State, Dep't of Ins. v. Blackburn*, 633 So.2d 521, 524 (Fla. 2d DCA 1994); *Seidman & Seidman v. Gee*, 625 So. 2d 1, 2-3 (Fla. 3d DCA 1992). This is because "[w]hen a corporate agent engages in misconduct that is calculated to benefit the agent and to harm the corporation, the agent has effectively ceased to function within the course and scope of the agency relationship with the corporation." *O'Halloran v. PricewaterhouseCoopers LLP*, 969 So.2d 1039 (Fla. 2d DCA 2007); *accord Nerbonne, NV v. Lake Bryan Intern.*, 685 So.2d 1029, 1032 (Fla. 5th DCA 1997) (declining to impute an agent's knowledge onto the principal where the target of the alleged fraud was the principal.).

Here, the Second Amended Complaint unequivocally provides that Sullivan, while acting in breach of his fiduciary duties to the Partnerships and the other partners, caused the Partnerships to transfer substantial funds to Defendants' in violation of the Partnership Agreements. Compl. at ¶¶ 52- 58. As Sullivan did not act to benefit the Partnerships, but instead took action for the purpose of advancing his own interests and the interests of the Defendants

that received kickbacks, his knowledge and conduct cannot reasonably be imputed onto the Partnerships.

Second, the defense of *in pari delicto* does not apply when it would defeat public policy and the defendant's wrongdoing exceeds the plaintiff's. *See Earth Trades, Inc. v. T&G Corp.*, 108 So. 3d 580, 583 (Fla. 2013) ("The defense of *in pari delicto*, however, does not require simply that both parties be to some degree wrongdoers. Rather the parties must participate in the **same** wrong doing. . . [a]nd they must be '**[e]qually at fault**.'") (internal citations omitted) (emphasis added); *see id.* (citing *Kulla v. E.F. Hutton & Co. Inc.*, 426 So. 2d 1055, 1057n.1 (Fla. 3d DCA 1983)); *see also Vista Designs v. Silverman*, 774 So. 2d 884, 886 (Fla. 4th DCA 2001)

In *Earth Trades*, the Florida Supreme Court declined to permit a defendant who was an unlicensed contractor to assert the defense of *in pari delicto*, even though the plaintiff hired that defendant with full knowledge of the its unlicensed status. *Id.* at 586. Since there was a strong public policy against unlicensed contracting to protect the public, and to avoid any detriment for statutory non-compliance the unlicensed contractor simply needed to conform with the law, the Supreme Court rejected the defense. *Id.*

As is in the case of *Earth Trades*, the Defendants' degree of fault vastly outweighs the fault, if any, of the Partnerships because Defendants were soliciting, without a license, individuals or entities to invest in the Partnerships and there could be no wrongdoing by the Partnerships if Defendants simply complied with the law.

Similarly, Defendants' invocation of *in pari delicto* would frustrate public policy because they failed to register with the Florida Office of Financial Registration, as required by Fla. Stat. 517, *et seq.*, or comply with any of the enumerated safeguards established by the administrative regulations promulgated by that office to advance the public policy of protecting the public, and

thus the Partnerships, from the very conduct that Defendants engaged in. The statutes requiring the registration of investment advisors does not prohibit entities from paying unregistered investment advisors commissions, but instead mandates that individuals and entities comply with applicable registration requirements and other regulations. As such, it is clear that the legislature enacted Chapter 517 to prohibit the unregistered provision of investment advice, and placed the onus on investment advisors, and not the entities they dealt with to register and comply with the Florida Office of Financial Regulation's regulations.

Finally, it is improper to permit Defendants to utilize the defense of *in pari delicto*, because the appointment of Margaret Smith and the Conservator prevents the wrong doing at issue from being attributed to the Partnerships. Generally, the appointment of a receiver cleanses a corporation of the taint of its wrong doing, so long as there was at least one honest member of the corporation. *See Freeman v. Dean Witter Reynolds*, 865 So. 2d 543 (Fla. 2d DCA 2003). In this case, many, if not most, of the general partners were not involved in any wrongdoing, the appointment of the Conservator cleanses the Partnerships, and renders the defense of *in pari delicto*, inapplicable. *Id.* (just because a "receiver receives his or her claims from the entities in receivership, a receiver does not always inherit the sins of his predecessors.").

For the foregoing reasons, Plaintiffs claims are not barred by the doctrine of *in pari delicto* as a matter of law.

C. <u>Plaintiffs Have Standing to Pursue Their Negligence Claims</u>

Next, the Defendants allege that Plaintiffs do not have standing to pursue Chapter 517 claims because Chapter 517 purportedly only establishes a duty as it relates to the customers of Defendants. Defendants' arguments misunderstand binding Florida precedent concerning the existence of a duty.

Florida law defines a duty as an "obligation, recognized by the law, requiring the [defendant] to conform to a certain standard of conduct, for the protection of others against unreasonable risks." *Williams v. Davis*, 974 So. 2d 1052, 1055 (Fla. 2007) (internal citations omitted). In determining whether a duty exists in a particular circumstance, "Florida, like other jurisdictions, recognizes that a legal duty will arise whenever a human endeavor creates a generalized and foreseeable risk of harming others." *McCain v. Florida Power Corp.*, 593 So. 2d 500, 503 (Fla. 1992). Thus,

> [w]here a defendant's conduct creates a *foreseeable zone of risk*, the law generally will recognize a duty placed upon defendant either to lessen the risk or see that sufficient precautions are taken to protect others from the harm that the risk poses.

Id. (citing *Kaisner v. Kolb*, 543 So. 2d 732, 735 (Fla. 1989)). In determining the extent of a particular duty, Courts look to the perceived risk that is inherent in a particular action taken, and the reasonable precautions that should be taken to minimize that risk. *Williams v. Davis*, 974 So. 2d at 1061 ("As a consequence, courts must remain alert to the changes in our society that may give rise to the recognition of a duty even where none existed before.").

Here, there is no dispute that Defendants were under a duty to register as investment advisors under § 517.12 and comply with the applicable regulations that relate to the provision of investment advice. The plain language of Fla. Stat. § 517.12 evidences an acknowledgement that the unregulated provision of investment advice can harm corporations as well as customers — which is the case in the instant action. Accordingly, and as alleged in the Second Amended Complaint, Defendants' failure to comply with those statutes foreseeably caused the Partnerships to incur damages, as the addition of new investors to the Partnerships, contributed to the continuing insolvency of the Partnerships and Defendants receipt of illegal commissions. *See* Compl. at ¶¶85-89.

As the Second Amended Complaint clearly provides that the harm to Plaintiffs was the foreseeable result of Defendants' conduct, it contains sufficient allegations to survive a motion to dismiss.

D. Plaintiffs May Pursue a Claim Under Fla. Stat. § 475.41

Defendants argue that Plaintiffs cannot assert a claim under Fla. Stat. § 475.41 because it is entitled "Real Estate Brokers, Sales Associates and Schools," and only requires real estate brokers to operate with a license. Motion at 7. However, Defendants rely on a single 40 year old case (*id*) and they ignore binding law stating that "There is nothing ambiguous about the statute's inclusion of non-real estate transactions under its purview." *Meteor Motors, Inc. v. Thompson Halbach & Associates*, 914 So. 2d 479, 482 (Fla. 4th DCA 2005).

Statute 475.41 (the "Broker Statute") provides:

> Contracts of unlicensed person for commissions invalid.— No contract for a commission or compensation for any act or service enumerated in s. 475.01(3) is valid unless the broker or sales associate has complied with this chapter in regard to issuance and renewal of the license at the time the act or service was performed.

The Fourth District Court of Appeals analysis in *Meteor Motors, Inc. v. Thompson Halbach & Associates*, provides a detailed analysis of the Broker Statute — a case Defendants conveniently forgot to mention in their Motion. 914 So.2d at 481-2. The *Meteor Motors, Inc.* case stands for the proposition that unlicensed individuals cannot receive commissions or referrals for acts as a "broker."

The *Meteor* Court recognized that Chapter 475 includes a broad definition for "broker."[2] A "broker" includes anyone who "takes any part" in procuring purchasers for "business

[2] "Section 475.01(1)(a) defines a 'broker' as including 'a person who, for another, and for a compensation or valuable consideration ... attempts or agrees ... to negotiate the sale, exchange, purchase ... of business enterprises or business opportunities' or who 'takes any part in the procuring of sellers, purchasers, lessors, or lessees of business enterprises or business opportunities.'" *Meteor Motors, Inc.*, 914 So.2d at 482.

enterprises or business opportunities." *Id.* at 483 (citing Fla. Stat. 475.01(1)(a)). In coming to that conclusion, the Fourth District Court of Appeals relied on *Schickedanz Bros. –Riviera Ltd. v. Harris*, where the Supreme Court of Florida found that the definition of a broker is broader than held that Fla. Stat. § 475.01 should not be confined to one who "directly procures a purchaser. . ." 800 So. 2d 608, 611 (Fla. 2001).

Defendants, received a kickbacks, which were fraudulently designated as "charitable contributions", or "management fees" for recommending that individuals or entities invest in the Partnerships, and they are properly designated as "brokers." Because Defendants acted as a broker without a license, they are not entitled to receive a fee or commission without a license to act as a broker under Ch. 475. Accordingly Plaintiffs have set forth a claim pursuant to Fla. Stat. 475.01 against Defendants.

E. Plaintiffs Have Standing to Pursue Their Fraudulent Transfer Claims

Defendants claim that Plaintiffs lack standing to pursue their fraudulent transfer claims because they cannot simultaneously be creditors and debtors. Despite Defendants' contentions, corporations may bring claims "directly against the principals or the recipients of fraudulent transfers of corporate funds to recover assets rightfully belonging to the corporation and taken prior to the receivership." *Freeman v. Dean Witter Reynolds, Inc.*, 865 So. 2d 543, 551 (Fla. 2d DCA 2003) (citing *Scholes v. Lehmann*, 56 F. 3d 750, 754 (7th Cir. 1995); *Schacht v. Brown*, 711 F.2d 1343 (7th Cir. 1983)). "In other words, after a corporation has been placed into a receivership, it becomes a creditor with respect to assets which were fraudulently transferred away." *Sallah ex rel. MRT. LLC v. Worldwide Clearing LLC*, 860 F. Supp. 2d 1329, 1335 (S.D. Fla. 2011) (applying Florida law) (internal citations omitted).

In a similar context, the Forth District Court of Appeal issued an opinion in the matter of *Effective Teleservices, Inc. v. Allerd Charles Smith*, Case Nos. 4D-12-3952 and 4D12-3957,

2014 WL 51686 (Fla. 4th DCA Jan. 8, 2014), which provided that an assignee for the benefit of creditors held the exclusive authority to pursue fraudulent transfer claims on behalf of an assignment estate. The basis for the *Allerd* opinion was that an assignee, like a Conservator, has obtained all assets of the assignor which includes the right to pursue fraudulent transfer claims, and is obligated to distribute all of the assets of the assignor under a priority scheme set forth by statute, subject to court supervision.[3] The Court therefore found that allowing a creditor to pursue a fraudulent transfer claim would undermine the purpose of the assignment and undermine the priorities established under state law. Therefore, Defendants' arguments fail as a matter of law.

Defendants also argue that Plaintiffs lack standing to pursue fraudulent transfer claims because the claims allegedly should be asserted by partners who lost their investments. But Defendants misunderstand the state of Florida jurisprudence. Here, Plaintiffs have standing to pursue claims for fraudulent transfers against those entities who received them, as if they were creditors. *See Freeman*, 865 So. 2d at 551; *Sallah*, 860 F. Supp. 2d at 1335. Accordingly, they have standing to pursue the instant claims as if they were "net losers" in this action.

Because the Second Amended Complaint states that the Partnerships are creditors — and by virtue of the Conservator's appointment, they are in fact creditors — Plaintiffs have standing to pursue the instant claims.

[3] "An assignment for the benefit of creditors is an alternative to bankruptcy and allows a debtor to voluntarily assign its assets to a third party [assignee] in order to liquidate the assets to fully or partially satisfy creditors' claims against the debtor." *Hillsborough Cnty. v. Lanier,* 898 So. 2d 141, 143 (Fla. 2d DCA 2005); *see also* § 727.104(1)(b), Fla. Stat. (2010). The stated intent of Chapter 727 "is to provide a uniform procedure for the administration of insolvent estates, and to ensure full reporting to creditors and equal distribution of assets according to priorities as established under this chapter." § 727.101, Fla. Stat. (2010).

F. DEFENDANTS HAVE SET FORTH A CLAIM FOR BREACH OF FIDUCIARY DUTY

Finally, Defendants argue that Count IX of the Second Amended Complaint should be dismissed because "Plaintiffs curiously neglect to distinguish between non-partner and partner defendants[,]" and did not plead any facts which establish a fiduciary relationship.

Contrary to Defendants' assertion, paragraph 135 of the Second Amended Complaint unequivocally states "Defendants . . . Father Kelly [and] Kelco. . . were partners in the Partnerships or owed fiduciary duties to the Partnerships based on their relationships with the Partnerships." Complaint at ¶ 135. As the Second Amended Complaint alleges that Defendants owed the Partnerships fiduciary duties as partners of the Partnerships, Count IX should not be dismissed.

V. CONCLUSION

WHEREFORE the Plaintiffs request that this Court enter an order denying Defendants Vincent T. Kelly and Kelco, Inc.'s Motion to Dismiss, together with such other and further relief as the Court may deem just and appropriate under the circumstances.

Dated: March 25, 2014

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been served via Electronic Mail and/or First Class U.S. Mail upon *all parties on the service list below* on this 25th day of March, 2014.

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