UNITED STATES DISTRICT COURT
DISTRICT OF SOUTH DAKOTA
SOUTHERN DIVISION

THE WATER WORKS BOARD OF THE CITY OF BIRMINGHAM; WASHINGTON SUBURBAN SANITARY COMMISSION EMPLOYEES' RETIREMENT PLAN; ATLANTIC GLOBAL YIELD OPPORTUNITY MASTER FUND, L.P; AND ATLANTIC GLOBAL YIELD OPPORTUNITY FUND, L.P, **Plaintiffs,** **v.** **U.S. BANK NATIONAL ASSOCIATION,** **Defendant.**	**Case No. 4:17-CV-04113-LLP** **DEFENDANT U.S. BANK'S MEMORANDUM OF LAW IN SUPPORT OF MOTION TO DISMISS**

INTRODUCTION

U.S. Bank National Association ("U.S. Bank") is moving to dismiss Plaintiffs' complaint because it seeks to shift a risk of loss to U.S. Bank in violation of express contractual provisions and well-established law. Plaintiffs allege that their investment advisors were controlled by criminals who orchestrated fraudulent bond offerings to steal Plaintiffs' funds. Unable to recover from the guilty parties, Plaintiffs attempt to hold U.S. Bank liable on the ground that, as indenture trustee for the bonds, it had a duty to investigate, detect, and prevent the fraud, but the indenture agreements expressly preclude Plaintiffs from seeking to impose this liability on U.S. Bank. In addition to this bar, Plaintiffs' claims for breach of contract and the implied covenant of good faith and fair dealing also fail because U.S. Bank breached no contractual duties, had no implied duties, and did not cause Plaintiffs' loss. Finally, Plaintiffs' negligence claim fails because U.S. Bank owed Plaintiffs no independent duties outside the indenture contracts.

Plaintiffs' Complaint should be dismissed because it fails to state a claim for relief against U.S. Bank.

FACTS[1]

1. The parties.

Plaintiff The Water Works Board of the City of Birmingham ("Birmingham Water") is an Alabama public corporation. Compl. ¶ 3. Plaintiff Washington Suburban Sanitary Commission Employees' Retirement Plan ("Washington Suburban") is a qualified retirement plan trust with participants in Maryland. *Id*. ¶¶ 1,4.

Plaintiff Atlantic Global Yield Opportunity Master Fund, L.P. is a Cayman Islands limited partnership that is wholly owned by Plaintiff Atlantic Global Yield Opportunity Fund, L.P. a Delaware limited partnership. *Id*. ¶ 5. These limited partnerships (collectively, "Global Yield") are investment vehicles for retirement plans with participants in Nebraska. *Id*. ¶¶ 1, 5.

Defendant U.S. Bank is a national banking association with its principal place of business in Minnesota, with offices in Arizona and Illinois. *Id*. ¶ 6. Plaintiffs do not allege that they paid U.S. Bank for any services, or communicated with U.S. Bank in any way concerning the bonds at issue, before or after they were purchased.

2. Criminals obtain discretionary control over Plaintiffs' funds for the purpose of buying bonds and obtaining the bond proceeds.

For many years, Birmingham Water and Washington Suburban had entrusted their investment funds to Hughes Capital Management LLC ("Hughes"), an SEC registered investment advisor based in Virginia. *Id*. ¶¶ 2, 13-14. Similarly, Global Yield's owners had for many years entrusted their investment funds with a registered investment advisor named Atlantic

[1] For purposes of this Rule 12(b)(6) motion only, the Complaint's well-pleaded factual allegations are accepted as true.

Asset Management LLC ("AAM"). *Id*. ¶¶ 2, 43-44. Birmingham Water and Washington Suburban gave Hughes full discretionary control over their investment funds, and Global Yield gave AAM discretionary control over its investment funds. *Id*. ¶¶ 14, 44.

In March 2014, a group of criminal conspirators began executing a scheme to structure bond sales in a way that would allow them to steal the sale proceeds. *Id.* ¶¶ 2, 11-12. The conspirators, defined by the Complaint as the "Criminal Defendants," included Jason Galanis, the scheme's main architect who has already pleaded guilty to criminal charges, and his associate Hugh Dunkerley. *Id.* ¶¶ 2, 11, 27, 30.

The Criminal Defendants' scheme had several components. First, they convinced the Oglala Sioux Tribe of the Pine Ridge Reservation to issue bonds through a tribal corporation, Wakpamni Lake Community Corporation ("Wakpamni"), with the promise that the proceeds would be used to purchase an annuity contract, and to fund community development projects. *Id.* ¶¶ 1-2, 9, 11-12.

Second, they bought investment advisory companies so they could use their clients' funds to buy the bonds in private placements that they arranged. *Id.* ¶¶ 13-16, 43-44. The Criminal Defendants bought Birmingham Water's and Washington Suburban's investment advisor, Hughes, shortly before using their funds to buy bonds in the first offering in August 2014. *Id.* ¶¶ 13-16. The Criminal Defendants later bought Global Yield's investment advisor, AAM; merged it with Hughes; and used Global Yield's funds to buy bonds in the last offering, in April 2015. *Id.* ¶¶ 43-44.

Third, they acquired control of a New York broker-dealer, Burnham Securities, LLC ("Burnham"), which served as the Tribe's placement agent for the bonds.[2] *Id.* ¶¶ 20, 28, 41. Burnham's principals and representatives in the bond offerings were Galanis and Dunkerley. *Id.* ¶¶ 20, 28; Docket 1-3, at 2.

Finally, the Criminal Defendants structured the bond offerings so that the Tribe would use bond proceeds to buy annuity contracts from an entity named "Wealth Assurance Private Client Corporation." *Id.* ¶¶ 27, 30, 41, 51; Docket 1-6; 1-7; 1-8; 1-9, at 9. Dunkerley created two entities with that same name, one in Florida, and one in the British Virgin Islands. *Id.* ¶¶ 27, 30. Both corporations (collectively, "Wealth Assurance") were created specifically for the fraudulent scheme. *Id.* ¶¶ 2, 27, 30, 41, 45.

Thus, the Criminal Defendants structured the bond deals so that they controlled the seller's agent (Burnham); the buyers' agent (Hughes/AAM); and the annuity provider (Wealth Assurance).

3. U.S. Bank complies with the August 2014 Indenture by disbursing bond proceeds as directed to pay for the annuity Wakpamni bought.

In the first bond offering, which closed on or about August 25, 2014, Wakpamni issued almost $25 million worth of bonds. *Id.* ¶ 15. The Dilworth Paxson law firm acted as Burnham's counsel. *Id.* ¶ 29; Docket 1-3, at 2; 1-4, at 3.Greenberg Traurig acted as Wakpamni's bond counsel. Docket 1-3, at 2; 1-4, at 3. The Criminal Defendants, through Hughes, purchased

[2] A "placement agent," like an underwriter, finds buyers for an issuer, although unlike an underwriter a placement agent does not buy the securities for re-sale. *See* Municipal Securities Rulemaking Board, http://www.msrb.org/Glossary/Definition/PLACEMENT-AGENT.aspx (last visited Oct. 19, 2017).

approximately $4.34 million in bonds for Birmingham Water, and approximately $4.12 million in bonds for Washington Suburban. Compl. ¶¶ 3-4, 15.

U.S. Bank agreed to serve as Indenture Trustee for the first bond issuance pursuant to express terms and conditions set forth in the Indenture dated August 25, 2014. Docket 1-1. One condition was that U.S. Bank would be responsible for performing only those services *expressly* set forth in the Indenture, and that "no implied covenants or obligations shall be read into this Indenture against" U.S. Bank. Docket 1-1, at 41, § 10.1.

Another condition was that U.S. Bank "shall have no responsibility . . . for the security for the Bonds or the use of proceeds of the Bonds . . . disbursed by the Trustee in accordance with this Indenture." *Id*.

The Indenture further provides that U.S. Bank will not be liable for any action "taken by it pursuant to any direction or instruction by which it is governed under this Indenture, including but not limited to investment of funds hereunder." *Id*. § 10.3. Another section similarly provides that, as to documents U.S. Bank "in good faith believe[s] to be genuine and to have been passed or signed by the proper board or person," it has "no duty to make any investigation or inquiry as to any statements contained or matters referred to in any such instrument but may accept and rely upon the same as conclusive evidence of the truth and accuracy of such statements." *Id*. at 43, § 10.9.

Finally, the Indenture provides: "In no event shall [U.S. Bank] be liable for the selection of investments or *for investment losses* incurred thereon." *Id*. at 30, § 5.8.

Before the closing, Wakpamni's President notified U.S. Bank in writing that it was purchasing the annuity investment from "Wealth Assurance Private Client Corporation," and appointing "Private Equity Management, Limited" as its investment manager. Docket 1-8, at 17.

"Private Equity Management" was a fake entity made up by the Criminal Defendants. Compl. ¶ 36.

The Indenture contained several conditions for closing, including two legal opinions, addressed to U.S. Bank, from Burnham's counsel (Dilworth) and Wakpamni's counsel (Greenberg), that the Bonds were valid. Docket 1-1, at 22, § 2.11(c)-(d). Another condition was a "Closing Statement" signed by Wakpamni's President or Vice President setting forth the amounts of proceeds from the bond sales to be used for various purposes, including the annuity purchase. *Id.* § 2.11(f).

The Indenture *required* U.S. Bank to disburse the proceeds as directed by the Closing Statement:

> The proceeds of the 2014 Bonds shall be paid over to the Trustee and deposited by the Trustee in the "Settlement Account", which is hereby established. From the Settlement Account the Trustee shall make the payments, disbursements and deposits as set forth in the Closing Statement required by Section 2.11, including, inter alia, the amount of $22,094,089 for the purchase of the Annuity Investment.

Id. § 2.12.

The agenda for the August 2014 closing assigned responsibility to Dilworth for preparing the Indenture and the Closing Statement. Docket 1-4, at 5. At closing, U.S. Bank received the Closing Statement, duly executed by Wakpamni's president, directing U.S. Bank to disburse approximately $22 million from the bond proceeds to pay for the annuity. Docket 1-5, at 3, 7. The next day, August 26, 2014, Dilworth provided U.S. Bank the "Wiring Coordinates for Wealth Assurance Private Client." Docket 1-7, at 4. U.S. Bank was directed to wire the payment to a J.P. Morgan Chase bank account owned by "Wealth Assurance Private Client." *Id*. at 6. The account address was in Santa Monica, and the bank branch was in Beverly Hills. *Id*. U.S. Bank accurately complied with Dilworth's instructions, and wired the purchase payment to the Wealth Assurance account. *Id*. at 2; Compl. ¶¶ 30-31. The Criminal Defendants owned and controlled

this entity and account, and they misappropriated the purchase payment funds, as they had planned. Compl. ¶¶ 2, 27, 30.

U.S. Bank received $6,500 for its services as Indenture Trustee for the August 2014 bond issuance. Docket 1-5, at 6. For serving as bond counsel, Dilworth received $97,000, and Greenberg received $75,000. *Id*. As placement agent, Burnham received $250,000. *Id*.

Birmingham Water and Washington Suburban allege U.S. Bank had a duty to disregard Dilworth's wire instructions for the August 2014 annuity purchase payment, based on several theories. First, Plaintiffs allege the instructions should have come from Wakpamni, rather than from Dilworth, Compl. ¶¶ 29, 57, but that is not what the Indenture provides. The Indenture provides that *after* U.S. Bank disburses the annuity purchase payment pursuant to the Closing Statement, any *future* disbursements from reserves shall be made pursuant to directions from Wakpamni. Compl. ¶ 24 (quoting § 2.12). The Indenture did not require the annuity payment wire instructions to come from Wakpamni. *Id*.; Docket 1-1, at 22, § 2.12.

Second, Plaintiffs complain that the purchase payment was wired to the "wrong" Wealth Assurance, the one Dunkerley had incorporated in Florida, rather than the one he had incorporated in BVI. Compl. ¶¶ 2, 30, 32, 45-46. But the wire instructions did not identify where the recipient was incorporated, Docket 1-7, and the Complaint does not suggest anyone, other than the Criminal Defendants, knew there were two identically named corporations. Furthermore, the Complaint admits the Criminal Defendants controlled both the Florida and BVI entities, Compl. ¶¶ 2, 27, 30, and it fails to explain what difference it made which entity received the payment.

Third, Plaintiffs complain that Dilworth directed the funds to be sent to Wealth Assurance Private Client Corporation, not "Wealth Assurance AG," but that direction complied

fully with the Indenture. Although a draft "Distribution List" and a "Closing Agenda" had identified the annuity provider as Wealth Assurance AG, the Indenture did not specify an annuity provider, and in connection with the closing Wakpamni's president formally notified U.S. Bank that it was buying the annuity from "Wealth Assurance Private Client Corp."[3] Docket 1-3, at 2; 1-4, at 3; 1-8, at 17. The direction was also consistent with the annuity contract, which identified Wealth Assurance as "part of the Wealth-Assurance Group of companies." Docket 1-6, at 3.

Finally, Plaintiffs allege Dilworth's wire instructions were inconsistent with the annuity contract. Compl. ¶¶ 31-34. U.S. Bank was not a party to the annuity contract, but it received a copy either the day of the closing (according to the Complaint's allegations), or the next day, with the email containing the wire transfer instructions (as shown by Complaint's exhibits). *Compare* Compl. ¶ 27, *with* Docket 1-7, at 4. Among the annuity contract's provisions were that payments must be received at Wealth Assurance's "home office" in BVI; that it was not authorized to do business outside BVI; and that Wakpamni would wire transfer payments to a bank selected by Wealth Assurance with no United States branches. Compl. ¶¶ 31-34. However, Plaintiffs do not identify any provision in the Indenture that U.S. Bank allegedly breached by following Dilworth's wire instructions. *See id.*, ¶¶ 24, 29.

[3] Plaintiffs' table on page 13 of its Complaint is wrong: Wealth Assurance AG was not identified as the annuity provider in a draft indenture; it had been identified as the investment manager, as Plaintiffs acknowledge elsewhere. Compl. ¶ 22 (quoting Docket 1-2, at 22, § 2.11(e)).

4. U.S. Bank complies with the April 2015 Indenture by disbursing bond proceeds as directed to pay for the annuity Wakpamni bought.

The Criminal Defendants orchestrated two more bond offerings: one in October 2014, and another in April 2015. Compl. ¶¶ 41-44. Through AAM, the Criminal Defendants purchased approximately $16.2 million in bonds for Global Yield in the April 2015 offering. *Id.* ¶¶ 43-44.

The April 2015 offering was structured the same way as the August 2014 offering (and the October 2014 offering). *Id*. ¶ 44. Dilworth served as Burnham's counsel, and Greenberg was Wakpamni's. Docket 1-9, at 8. U.S. Bank served as indenture trustee pursuant to an Indenture with, for purposes of this motion, substantially the same material terms as the August 2014 Indenture. Docket 1-11. Again, U.S. Bank complied with the Indenture by disbursing the bond proceeds pursuant to a Closing Statement duly executed by Wakpamni's President. Docket 1-9, at 1, 4. This time, Dilworth put the wire transfer instruction information for the annuity purchase payment in the Closing Statement itself, but they were identical to instructions given in the August 2014 transaction. Docket 1-9, at 9.[4] Again, the Criminal Defendants stole the annuity purchase payment from Wealth Assurance's bank account. Compl. ¶ 2.

As was the case previously, U.S. Bank was not a party to the April 2015 annuity contract. Docket 1-10. Unlike the first annuity contract, however, the April 2015 annuity contract did not specify using a foreign bank. *Id.* at 11, § 5. Like the other Plaintiffs, Global Yield seeks to hold U.S. Bank for its investment loss on a theory that U.S. Bank had a duty not to follow the wire instructions for the annuity purchase payments. Compl. ¶¶ 45-46. Like the other Plaintiffs,

[4] Plaintiffs mistakenly allege the April 2015 Closing Statement directed U.S. Bank to wire the annuity purchase payment to a different bank account from the one specified in the August 2014 closing, Compl. ¶ 45, but actually the wiring instructions were exactly the same. *Compare* Docket 1-7, at 6, *with* Docket 1-9, at 9.

Global Yield does not identify any provision *in the Indenture* that U.S. Bank breached by following the wire instructions. *Id*.

U.S. Bank received $8,500 for its services as Indenture Trustee for the April 2015 bond issuance. Docket 1-9, at 8. For serving as bond counsel, Dilworth received $65,000, and Greenberg received $50,000. *Id*. Burnham again received $250,000 as placement agent. *Id*.

5. The Criminal Defendants make interest payments on the Bonds until their fraud is uncovered.

To avoid detection of their fraud, in fall 2015 the Criminal Defendants funded the first interest payments due on the August and October 2014 bonds. Compl. ¶ 51. In 2016, however, they stopped funding interest payments, their fraud was uncovered, and they were charged with federal crimes. *Id*. ¶ 52.

ARGUMENT

PLAINTIFFS' COMPLAINT SHOULD BE DISMISSED UNDER RULE 12(B)(6) FOR FAILURE TO STATE A CLAIM FOR RELIEF AGAINST U.S. BANK.

1. Rule 12(b)(6) standard.

To survive a motion to dismiss, a complaint must plead facts sufficient to state a claim for relief that is "plausible on its face." *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009). A plausible claim must plead "factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Id.* "Where a complaint pleads facts that are 'merely consistent with' a defendant's liability, it 'stops short of the line between possibility and plausibility of 'entitlement to relief.'" *Id*. (quoting *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 557 (2007)). Determining whether a complaint states a plausible claim for relief is "a context-specific task that requires the reviewing court to draw on its judicial experience and common

sense." *McShane Constr. Co. v. Gotham Ins. Co*., 867 F.3d 923, 928 (8th Cir. 2017) (quoting *Iqbal*, 556 U.S. at 678-79).

In ruling on a Rule 12(b)(6) motion, the court may consider exhibits attached to the complaint, and other documents integral to a claim, such as contracts in a breach of contract action. *Zean v. Fairview Health Servs*., 858 F.3d 520, 526 (8th Cir. 2017). The court accepts as true only specifically pleaded facts, not legal conclusions or conclusory statements. *See, e.g.*, *McShane*, 867 F.3d at 927. To the extent a properly considered document contradicts the complaint's allegations, the document controls. *Zean*, 858 F.2d at 527; *Chicago Dist. Council of Carpenters Welfare Fund v. Caremark, Inc.*, 474 F.3d 463, 466 (7th Cir. 2007).

2. The Indentures' limitation on liability bars Plaintiffs' claims.

Plaintiffs' Complaint is barred by the Indentures' limitation on liability: "In no event shall [U.S. Bank] be liable for the selection of investments or for investment losses incurred thereon." Docket 1-1, at 30, § 5.8; 1-11, at 30, § 5.8. This contractual limitation on damages is enforceable as a matter of law. *See Richland State Bank v. Household Credit Servs.,* 340 F. Supp. 2d 1051, 1057-59 (D.S.D. 2004) (holding that contractual limitation on damages barred contract and negligence claims). Plaintiffs allege that the annuity contracts were "investments" under the Indentures, that the annuities were supposed to fund principal and interest payments on the bonds, and the bonds became worthless because the annuities were fraudulent investments sold by the Criminal Defendants. Compl. ¶¶ 2, 12, 26-27, 48. Thus, Plaintiffs seek to hold U.S. Bank liable for the selection of fraudulent investments and the losses incurred on those investments, precisely what § 5.8 prohibits.

U.S. Bank's express limitation on liability is consistent with the limited, administrative role it played in the bond offerings. U.S. Bank was not retained to conduct any due diligence

investigation or provide any advice concerning the bond offerings or the annuity investments. Yet Plaintiffs seek to hold U.S. Bank liable for approximately $25 million because Wakpamni bought fraudulent investments from criminals. The Indentures bar Plaintiffs from holding U.S. Bank liable for this investment loss, and their complaint should be dismissed. *See Richland State Bank*, 340 F. Supp. 2d at 1057-59.

3. Plaintiffs' Complaint fails to state a breach of contract claim.

Plaintiffs' contract claims are based on alleged breaches of the Indentures, which are the only contracts to which U.S. Bank was a party, and the only contracts to which Plaintiffs claim to have standing to assert a breach. Compl. ¶¶ 54-55, 67. The Indentures are governed by South Dakota law. Docket 1-1, at 50, § 12.11; 1-11, at 51, § 12.11.

To state a breach of contract claim, Plaintiffs were required to plead facts showing (1) an enforceable promise by U.S. Bank; (2) U.S. Bank's breach of that promise; and (3) resulting damages. *See, e.g., Bowes Constr., Inc. v. S. D. Dep't of Transp.*, 793 N.W.2d 36, 43 (S.D. 2010). The complaint must "at minimum, cite the contractual provision allegedly violated." *Gillis v. Principia Corp.*, 832 F.3d 865, 872 n.11 (8th Cir. 2016) (quoting *Cummins Law Office, P.A. v. Norman Graphic Printing Co.*, No. CIV. 11-2061 RHK/FLN, 2012 WL 3430447, at *3 (D. Minn. Aug. 14, 2012)). Interpreting contractual provisions, and determining contractual duties, are issues of law for the court. *Hammonds v. Hartford Fire Ins. Co.*, 501 F.3d 991, 997 (8th Cir. 2007); *Ziegler Furniture & Funeral Home, Inc. v. Cicmanec*, 709 N.W.2d 350, 354 (S.D. 2006).

The Indentures expressly provide that U.S. Bank would be responsible for performing only those services *expressly* set forth in the Indenture, and that "no implied covenants or obligations shall be read into this Indenture against" U.S. Bank. Docket 1-1, at 41, § 10.1; 1-11,

at 41, § 10.1. This provision is consistent with the general rule regarding the duties of a trustee under a corporate bond indenture. Unlike an ordinary trustee, which owes implied common law fiduciary duties to act exclusively for the trust beneficiary's benefit, it is generally accepted that a corporate indenture trustee's duties are ministerial and defined by the indenture agreement. *See, e.g. Elliott Assocs. v. J. Henry Schroeder Bank & Trust Co*., 838 F.2d 66, 71 (2d Cir. 1988); *Harriet & Henderson Yarns, Inc. v. Castle,* 75 F. Supp. 2d 818, 830-32 (W.D. Tenn. 1999) (citing cases from various jurisdictions); *Williams v. Cont'l Stock Transfer & Tr. Co.*, 1 F. Supp. 2d 836, 840 (N.D. Ill. 1998).[5]

A. Plaintiffs fail to state a breach of contract claim based on U.S. Bank's following instructions to pay Wealth Assurance for the annuities.

(1) No breach of promise.

Plaintiffs' allegations center on U.S. Bank's disbursing bond proceeds to Wealth Assurance at each closing to pay for the annuity contracts it executed with Wakpamni. While Plaintiffs offer various after-the-fact critiques about the transfers, they do not and cannot point to *any* breach by U.S. Bank of *any* of its express obligations under the Indentures. For example, Plaintiffs complain that U.S. Bank relied on wire transfer instructions that came from Dilworth, Burnham's counsel, rather than from Wakpamni. Compl. ¶¶ 29, 60. But Plaintiffs cite nothing in the Indenture requiring the wire transfer instructions to have come from Wakpamni, because no such provision exists.

Plaintiffs also complain that U.S. Bank wired the annuity purchase payment to the "wrong entity"— the Wealth Assurance incorporated in Florida, not in BVI, and that U.S. Bank

[5] In some jurisdictions indenture trustees have a duty to avoid conflicts-of-interest, and may owe additional duties after a contractually defined "event of default," *see, e.g., Harriet & Henderson*, 75 F. Supp. 2d at 831, but South Dakota has not adopted these exceptions, and Plaintiffs have not alleged grounds for applying them.

should have conducted an investigation before following the wire transfer instructions. Compl. ¶¶ 2, 20, 30-32, 58, 61. But again, Plaintiffs cite no express duty or promise in the Indentures that U.S. Bank breached by transferring the annuity purchase payment, because none exists. Plaintiffs' failure to plead facts showing the breach of an express promise defeats their contract claim. *See Gillis*, 832 F.3d at 872 n.11.

On the contrary, the Indentures required U.S. Bank to disburse the proceeds as directed by a Closing Statement signed by Wakpamni. §§ 2.11(f), 2.12. In the April 2015 offering, the Closing Statement signed by Wakpamni's president directed U.S. Bank to pay Wealth Assurance, and provided its bank account wire information. Docket 1-9, at 4, 9. In the August 2014 closing, Wakpamni's president notified U.S. Bank that it was buying the annuity from Wealth Assurance, and signed a Closing Statement directing U.S. Bank to pay for the annuity with the bond proceeds. Docket 1-6, at 7; 1-8, at 17. Although Wealth Assurance's wire information came the next day from the attorney for Wakpamni's placement agent, the Indenture did not require the wire information to come from Wakpamni. §§ 2.11(f), 2.12.

Plaintiffs' claim that U.S. Bank had a duty to conduct an investigation before following the wire transfer instructions is not only unsupported by the Indentures, it contradicts them. The Indentures provide that "no implied covenants or obligations shall be read into this Indenture against" U.S. Bank (Docket 1-1, at 41, § 10.1; 1-11, at 41, §10.1); Plaintiffs seek to imply a duty to investigate. The Indentures provide that U.S. Bank "shall have no responsibility . . . [for] the use of proceeds of the Bonds . . . disbursed by the Trustee in accordance with this Indenture" (*id.*); Plaintiffs seek to hold U.S. Bank responsible for the Criminal Defendants' use of bond proceeds that U.S. Bank disbursed in accordance with the Indentures. And the Indentures

specifically provide that U.S. Bank does *not* have the duty to investigate that Plaintiffs seek to impose:

> The Trustee shall be fully protected and shall incur no liability in acting or proceeding in good faith upon any resolution, opinion, notice, telegram, request, requisition, consent, waiver, certificate, statement, affidavit, voucher, bond, or other paper or document which it shall in good faith believe to be genuine and to have been passed or signed by the proper board or person or to have been prepared and furnished pursuant to any of the provisions of this Indenture, and **the Trustee shall be under no duty to make any investigation or inquiry as to any statements contained or matters referred to in any such instrument but may accept and rely upon the same as conclusive evidence of the truth and accuracy of such statements**.

Docket 1-1, at 43, § 10.9; 1-11, at 43, § 10.9 (emphasis added).

(2) No causation of damage.

An essential element of a breach of contract claim is that the breach in fact caused the alleged loss. *See Morris, Inc. v. State, ex rel. State Dep't of Transp*., 806 N.W.2d 894, 903 (S.D. 2011); *McKie v. Huntley*, 620 N.W.2d 599, 603-04 (S.D. 2000). For their contract claim, Plaintiffs allege that U.S. Bank's breach of contract "caused Plaintiffs' bonds to become worthless" (Compl. ¶ 65), but they allege no facts supporting that allegation, and it is not plausible. As Plaintiffs themselves also allege, the bonds became worthless because the Criminal Defendants stole most of the bond proceeds that were used to pay for the annuity contracts. *Id*. ¶ 2. U.S. Bank did not cause the Criminal Defendants to steal the bond proceeds. Nor did U.S. Bank issue a fidelity bond, or guarantee the bonds' repayment, or assume the risk criminals would steal bond proceeds by selling allegedly fraudulent annuities to Wakpamni.

On the contrary, the Indentures expressly provide that U.S. Bank would not be responsible for such risks. Plaintiffs allege that the annuity contracts were "investments" under the Indentures. Compl. ¶¶ 26, 48. The Indentures expressly provide: "In no event shall [U.S.

Bank] be liable for the selection of investments or for investment losses incurred thereon." Docket 1-1, at 30, § 5.8; 1-11, at 30, § 5.8 (emphasis added). This contractual limitation on damages is enforceable as a matter of law. *See Richland State Bank,* 340 F. Supp. 2d at 1057-59. By their own theory, Plaintiffs are seeking to hold U.S. Bank liable "for the selection of investments"—the annuity contracts— and for "investment losses incurred thereon"—the Criminal Defendants' failure to make the annuity payments. The Indentures' express limitation on damages precludes Plaintiffs from recovering the damages they seek.

And, more specifically, Plaintiffs' claim of breach based on U.S. Bank's sending the annuity payments to the "wrong" Wealth Assurance fails to allege a plausible basis for loss causation. This purported breach could not have caused Plaintiffs' loss, because the Criminal Defendants' controlled both Wealth Assurance corporations. Compl. ¶¶ 2, 27, 30. Sending the annuity payment to the "correct" Wealth Assurance, incorporated in BVI, would have led to the same result: the Criminal Defendants having control of the funds. Similarly, the fact U.S. Bank relied on wire instructions for the August 2014 offering that came from Dilworth the day after the closing did not cause Plaintiffs' loss. This is demonstrated by the fact that when the wire instructions were included in the April 2015 Closing Statement, signed by Wakpamni, they were exactly the same, and the Criminal Defendants stole those proceeds as well. Compl. ¶ 47; Docket 1-9, at 9.

B. Plaintiffs fail to state a breach of contract claim based on U.S. Bank's not valuing the annuity contracts.

Plaintiffs also allege U.S. Bank breached the Indentures because the annuity contracts were "investments" under the Indentures, and therefore U.S. Bank was required to value them monthly. Compl. ¶¶ 26, 62. The Indentures define "Investment Securities" by listing various types of investments, including the "Annuity Investment." Docket 1-1, at 11-14; 1-11, at 11-13.

The definition also states that investments shall be valued "as of the end of each month," and specifies how they are to be valued: market-traded securities are to be valued at market price; CDs and bankers acceptances are to be valued at face value plus accrued interest; and all other investments are to be valued by agreement between U.S. Bank and Wakpamni. *Id.*

Plaintiffs seek to hold U.S. Bank liable for their investment losses on the ground U.S. Bank did not value either the August 2014 or April 2015 annuity contract, but they ignore the Indentures' express limitation of liability: "In no event shall [U.S. Bank] be liable for the selection of investments or for investment losses incurred thereon." Docket 1-1, at 30, § 5.8; 1-11, at 30, § 5.8. The valuation provision applies to only "investments." If the annuity contracts were investments, then Plaintiffs cannot hold U.S. Bank liable for their selection, or for losses incurred on them. *See Richland State Bank*, 340 F. Supp. 2d at 1057-59.

Furthermore, Plaintiffs' claim is based on two assumptions, neither of which satisfies *Iqbal.* First, Plaintiffs assume the Indentures required that U.S. Bank perform valuations of the annuity contracts, but they do not. The provision Plaintiffs rely upon merely provides for a "value . . . established by agreement between" Wakpamni and U.S. Bank. Docket 1-1, at 14; 1-11, at 14. It would have been entirely consistent with this provision for Wakpamni to agree with U.S. Bank that Wealth Assurance would value the annuities; the annuity contracts between Wakpamni and Wealth Assurance had their own valuation provision that required a valuation by Wealth Assurance. Docket 1-6, at 12.

Second, Plaintiffs assume that if U.S. Bank had valued the annuity contracts, it would have uncovered the Criminal Defendants' fraud, but they allege no specific facts supporting this causation theory. This allegation is entirely speculative, precisely what *Iqbal's* plausibility requirement prohibits. *See, e.g., Iqbal*, 556 U.S. at 678-79.

C. Plaintiffs fail to state a breach of claim based on U.S. Bank's alleged failure to "alert" the bondholders or issuer.

Plaintiffs' final breach of contract theory is that U.S. Bank failed to "alert" Wakpamni and Plaintiffs, as bondholders, about U.S. Bank's alleged Indenture breaches, and to provide other, unspecified information concerning the possibility that the bond offerings were fraudulent. Compl. ¶ 63. This claim fails because the Indentures contain no such duty to provide such information, and § 10.1 expressly precludes implying such a duty.

Courts have repeatedly rejected claims based on an indenture trustee's alleged duty to provide bondholders information not required by the indenture. For example, in *Lorenz v. CSX Corp.*, 1 F.3d 1406 (3d Cir. 1993), bondholders alleged that the indenture trustee had breached a duty to inform them about potential securities laws violations by the issuer. The bondholders' claims were dismissed under Rule 12(b)(6) because the indenture did not expressly require such notice, and as a matter of law the court could not imply such a duty. *Id*. at 1414-17. Similarly, in *Raymond James & Assocs. v. Bank of New York Trust Co*., Case No. 8:07-CV-239-T-27TBM, 2008 WL 186590 (M.D. Fla. Jan. 18, 2008), the court dismissed under Rule 12(b)(6) a bondholder's claim that the indenture trustee breached a duty to provide it notice of the issuer's prepayment, because the indenture disclaimed any implied duties and did not expressly require such notice. Here, too, the Indentures contain no express duties to provide such information, they expressly disclaim any implied duties, and therefore Plaintiffs' claim fails as a matter of law.

The alleged failure to inform Wakpamni fails to state a claim for an additional reason: lack of causation. Plaintiffs do not identify any information available to U.S. Bank that was not also available to Wakpamni, its bond counsel, or both. U.S. Bank's alleged failure to disclose information to Wakpamni cannot plausibly be the cause of Plaintiffs' damages if Wakpamni had

the same information. Plaintiffs cannot state a claim for breach of contract if the alleged breach did not in fact cause the alleged damages. *See McKie*, 620 N.W.2d at 603-04.

4. Plaintiffs' Complaint fails to state a claim for breach of the implied covenant of good faith and fair dealing.

In a tacit admission that U.S. Bank breached no *express* Indenture covenant by complying with the wire transfer instructions it was provided, Plaintiffs allege that by following them U.S. Bank breached the implied covenant of good faith and fair dealing. Compl. ¶¶ 68-72. Where, as is the case on this motion, there is no factual dispute, applying the implied covenant of good faith and fair dealing is an issue of law. *See Nygaard v. Sioux Valley Hosps. & Health Syst.*, 731 N.W.2d 184, 194 (S.D. 2007) (affirming grant of motion to dismiss); *Farm Credit Servs. of Am. v. Dougan*, 704 N.W.2d 24, 27-28 (S.D. 2005). Plaintiffs' claim fails as a matter of law because they are seeking to modify the Indentures' express provisions, and because the Complaint alleges no facts suggesting U.S. Bank acted in bad faith.

The implied covenant of good faith and fair dealing "prohibits either contracting party from preventing or injuring the other party's right to receive the agreed benefits of the contract." *Nygaard*, 731 N.W.2d at 193 (quoting *Farm Credit*, 704 N.W.2d at 28). "Good faith" means "honesty in fact." *Taylor Equip., Inc. v. John Deere Co.*, 98 F.3d 1028, 1032 (8th Cir. 1996) (quoting *Garrett v. BankWest, Inc.*, 459 N.W.2d 833, 841-42 (S.D. 1990)); *Farm Credit*, 704 N.W.2d at 28.

The implied covenant of good faith and fair dealing cannot be used to "vary the substantive terms of the bargain," or modify a contract's express language, so if "the express language of a contract addresses an issue, then there is no need to construe intent or supply implied terms." *Farm Credit*, 704 N.W.2d at 29 (citation omitted); *Nygaard*, 731 N.W.2d at 194 (quoting *Farm Credit*, 704 N.W.2d at 28). Principles of good faith merely "fill the gap" when a

contract fails to address an issue, by preventing a party from taking "opportunistic advantage in a way that could not have been contemplated at the time of drafting." *Taylor*, 98 F.3d at 1033 (citation omitted); *Farm Credit*, 704 N.W.2d at 28-29 (citation omitted). And because the duties of an indenture trustee are delineated by the express terms of the indenture, it is particularly inappropriate to rely on the implied covenant of good faith and fair dealing to try to establish additional, implied obligations on the part of indenture trustees. *See Lorenz*, 1 F.3d at 1414-17; *Abbate v. Wells Fargo Bank, N.A.*, No. CV 10-6561 DOC (RNBx), 2011 WL 13128742, at *5 (C.D. Cal. Apr. 25, 2011) (dismissing claims).

Plaintiffs' theory is that, before disbursing the bond proceeds to pay for the annuity contracts, U.S. Bank was required to conduct some type of investigation to confirm that Wealth Assurance was a bona fide annuity provider and the annuity contracts were legitimate. *See* Compl. ¶¶ 70-71. But Plaintiffs cannot dispute that the Indentures address U.S. Bank's obligations regarding disbursing the annuity purchase payments, because Plaintiffs base their breach of contract claim (*id*. ¶¶ 56-61) on precisely the same conduct as their implied covenant claim (*id*. ¶¶ 70-71). *See Midwest AG Enters. v. Poet Invs.*, No. 08-4091, 2010 WL 2332717, at *17-18 (D.S.D. June 9, 2010) (granting summary judgment because implied covenant claims are based on same conduct as breach of contract claims).

The Indentures expressly address U.S. Bank's obligations with respect to disbursing bond proceeds to pay for the annuity contracts, and they do not require U.S. Bank to conduct any investigation before doing so. Section 2.12, entitled, "Application of Proceeds of the Bonds; Establishment of Settlement Account," provides as follows:

> The proceeds of the [2014 or 2015] Bonds shall be paid over to the Trustee and deposited by the Trustee in the "Settlement Account", which is hereby established. From the Settlement Account the Trustee shall make the payments, disbursements and

> deposits as set forth in the Closing Statement required by Section 2.11, including, inter alia, the amount of [$22,094,089 or $15,850,000] for the purchase of the Annuity Investment.

Docket 1-1, at 22, § 2.12; 1-11, at 21, § 2.12. Section 10.3 further provides that U.S. Bank shall not be liable for any action "taken by it pursuant to any direction or instruction by which it is governed under this Indenture." Docket 1-1, at 41; 1-11, at 41. Section 5.8 provides that "[i]n no event shall the Trustee be liable for the selection of investments," which Plaintiffs allege include the annuity contracts. Docket 1-1, at 30; 1-11, at 30. And section 10.1 provides that U.S. Bank has no implied obligations. Docket 1-1, at 41; 1-11, at 41.

U.S. Bank did not agree to investigate and confirm Wealth Assurance's legitimacy or the soundness of the annuities before following directions to pay for them. And U.S. Bank was certainly not paid to conduct a due diligence investigation or assume the risk that Wakpamni was being defrauded by criminals and would be unable to repay the bonds. U.S. Bank's obligations in disbursing the payments for the annuity contracts were purely ministerial. Plaintiffs are not seeking to "fill the gaps" by addressing an issue "that could not have been contemplated" at the time of drafting; they are seeking to "vary the substantive terms of the bargain" by imposing additional obligations and risks on U.S. Bank which it did not voluntarily assume and for which it received no compensation. *See Taylor*, 98 F.3d at 1032-33; *Nygaard*, 731 N.W.2d at 194; *Farm Credit*, 704 N.W.2d at 28. Because the Indentures address U.S. Bank's obligations with respect to disbursing the annuity purchase payments, Plaintiffs' implied covenant claim fails as a matter of law. *See Taylor*, 98 F.3d at 1032; *Nygaard,* 731 N.W.2d at 194; *Farm Credit*, 704 N.W.2d at 28-29.

Plaintiffs' claims also fail because they do not state a plausible claim that U.S. Bank acted dishonestly in disbursing the annuity contract payments. *See Taylor,* 98 F.3d at 1033-34 (granting judgment as matter of law for lack of showing of dishonesty). With respect to the

August 2014 offering, Plaintiffs allege U.S. Bank acted in bad faith because the wire transfer information came from one of the Criminal Defendants, Jason Galanis. Compl. ¶ 71. But Plaintiffs allege no facts suggesting U.S. Bank knew Galanis was dishonest in any way. Moreover, Dilworth, bond counsel for the placement agent Burnham, actually sent the wire transfer information to U.S. Bank. Docket 1-7, at 4.[6] Dilworth was responsible for preparing the Closing Statement, which governed U.S. Bank's disbursement of bond proceeds under the Indenture. § 2.12; Docket 1-4, at 5. These facts do not in any way suggest U.S. Bank acted dishonestly in following Dilworth's wire transfer instructions.

With respect to the April 2015 offering, the Indenture expressly required U.S. Bank to disburse the bond proceeds in accordance with the Closing Statement, and the Closing Statement expressly directed U.S. Bank to pay Wealth Assurance for the annuity contract by wire transferring bond proceeds to a specified bank account. § 2.12; Docket 1-9, at 9. U.S. Bank did not act dishonestly by performing its express contractual obligations. *See, e.g., Farm Credit*, 704 N.W.2d at 28-29.

Iqbal requires applying common sense. *McShane*, 867 F.3d at 928 (quoting *Iqbal*, 556 U.S. at 678-79). Claiming that U.S. Bank acted dishonestly by accurately complying with wire transfer instructions to pay for annuity contracts that Wakpamni actually intended to buy defies common sense and does not state a plausible claim for relief.

[6] Dilworth forwarded the information from Galanis, who was identified in the email and draft distribution list as being with Burnham, Dilworth's client. Docket 1-3, at 2; 1-7, at 4.

5. Plaintiffs' Complaint fails to state a claim for negligence.

A negligence claim requires the plaintiff to show the existence of a duty, breach of that duty, proximate and factual causation, and actual injury. *Fisher Sand & Gravel Co. v. S.D. Dep't of Transp.*, 558 N.W.2d 864, 867 (S.D. 1997).Whether a duty exists is a question of law. *Id.*

Plaintiffs' negligence claim fails because it violates the "independent duty" rule, which provides that a party cannot assert a negligence claim unless the defendant owed it "a legal duty which arises independent of the duties under the contract." *Sundt Corp. v. S.D. Dep't of Transp.*, 566 N.W.2d 476, 478 (S.D. 1997) (citing *Fisher)*; *accord Schipporeit v. Khan,* 775 N.W.2d 503, 507-08 (S.D. 2009). Plaintiffs cannot sue U.S. Bank for negligence because, apart from the Indentures, U.S. Bank owed Plaintiffs no duties. *See Schipporeit,* 775 N.W.2d at 507-08 (holding independent rule precludes negligence claim because parties' only relationship was contract defining their duties); *Sundt*, 566 N.W.2d at 479 (holding independent rule precludes negligence claim because there was "no legal duty which existed outside the contract").

Plaintiffs allege that U.S. Bank negligently performed its duties under the Indentures (Compl. ¶ 75), which is exactly what the independent duty rule prohibits. *See, e.g., GSAA Home Equity Trust 2006-2 v. Wells Fargo Bank*, 133 F. Supp. 3d 1203, 1222-24 (D.S.D. 2015). In *GSAA*, this Court, by Judge Lange, dismissed under Rule 12(b)(6) negligence and gross negligence claims that a trust had asserted against the trust servicer for allegedly failing to perform its servicing duties properly and with due care. The Court reasoned the trust was essentially "seeking to enforce obligations the Defendants contractually undertook," and noted the "misconduct and damages alleged in" the negligence and gross negligence counts were "essentially the same." *Id.* at 1222; *see also Abbate*, 2011 WL 13128742, at *5 (dismissing negligence claims because "the duties of indenture trustees arise solely from the terms of the

contract," and that, accordingly, "[p]laintiffs may not recast a suit for breach of those contract duties as a tort suit for negligence") (citation omitted).

Here, too, Plaintiffs' negligence and gross negligence claims are based on the exact same alleged misconduct, and seek the exact same damages, as their breach of contract claim. *Compare* Compl. ¶¶ 56-63, *with* ¶ 75. The independent duty rule precludes Plaintiffs from attempting to re-cast their breach of contract claims as tort claims. *See, e.g., GSAA*, 133 F. Supp. 3d 1203, 1221-22.

Furthermore, even if Plaintiffs could assert a negligence claim, their purported claim would fail *Iqbal*'s facial plausibility standard. This is not a negligence case. U.S. Bank did not send the annuity purchase payments to the wrong account, or send the wrong amounts, or otherwise fail to use ordinary care in following the instructions it was provided. In each offering, U.S. Bank accurately sent the correct amount to the correct account. Unfortunately, criminals orchestrated the bond offerings specifically to steal Plaintiffs' funds, but U.S. Bank was not involved in putting the deals together, did not promote them, and did not agree to conduct any due diligence investigation. Rather, U.S. Bank was paid a relatively modest fee to perform ministerial tasks. Plaintiffs cannot properly rely on a negligence theory to shift their investment loss to U.S. Bank, particularly where the Indentures expressly preclude liability for such losses. *See Richland State Bank*, 340 F. Supp. 2d at 1057-59.

CONCLUSION

U.S. Bank respectfully requests this Court to dismiss Plaintiffs' Complaint for failure to state a claim.

Respectfully submitted this 19th day of October, 2017.

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