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

THOMAS L. TAYLOR, III, in his capacity as Court-appointed temporary receiver for Breitling Energy Corp. et al., Plaintiff v. ROTHSTEIN KASS P.A. d/b/a ROTHSTEIN KASS & CO. P.C.; ROTHSTEIN KASS & COMPANY, PLLC and BRIAN MATLOCK, Defendants.	§ § § § § § § § § § § § § §	NO. 3:19-cv-01594-D

DEFENDANTS' RENEWED MOTION TO COMPEL DOCUMENT PRODUCTION

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DEFENDANTS' RENEWED MOTION TO COMPEL DOCUMENT PRODUCTION

Pursuant to the Court's June 29, 2020 Order ("June 29 Order," Dkt. #64) Defendants file this Renewed Motion to Compel Document Production as follows.

I. INTRODUCTION

On June 29, 2020, the Court invited Defendants to renew their motion to compel production of Plaintiff's communications with investors ("Investor Communications") if "it appears by the report of the Receiver's damages expert that the damages calculation *does* rely on investors' claims against the Receivership Estate. . . ."[1] June 29 Order, (Dkt. #64) (emphasis in original).

Plaintiff's expert report—served on August 14, 2020— expressly asserts damages based upon "the increased liabilities that were sustained by the Receivership Estate" ("Increased Liability Theory"), measured by total individual investments in the Breitling[2] entities less refunds and/or disbursements to each investor, less the value of any remaining assets held by the Receivership Estate. Limited Investor Communications previously produced only after the Court's order show discussions between the Plaintiff and investors on the nature, timing, and amount of the investors' investments, as well as the returns they received from Breitling. These communications provide information that cannot be discerned from the financial statements and records of the Breitling entities alone. Plaintiff's communications with investors are therefore highly relevant, and the balance of the communications between Plaintiff and investors in Breitling must be produced.

[1] The Court previously denied Defendants' motion to compel such communications and sustained Plaintiff's relevance objection on the grounds that "the Receiver represents that his damages are not based on any of the documents Rothstein Kass seeks." June 29 Order at 2.
[2] "Breitling" refers collectively to Breitling Oil and Gas Corporation, Breitling Royalties Corporation, and Breitling Energy Corporation and the related Crude and Patriot entities.

Defendants therefore renew their Motion to Compel Production of these documents that have been withheld from production.

II. BACKGROUND

On February 28, 2020, Rothstein Kass & Company, PLLC ("Rothstein Kass PLLC") served its First Set of Requests for Production, which included Request No. 31 seeking "[a]ny and all communications between the Receiver and any claimants in *SEC v. Faulkner*, 3:16-cv-01735-D (N.D. Tex.) at any time since June 24, 2016." Despite Plaintiff's concession that he would be seeking damages in part from "fraud victim liabilities," Plaintiff objected and refused to produce relevant Investor Communications. App. at 109, Ex. B.

On April 21, 2020 Rothstein Kass PLLC filed a motion to compel seeking production of communications responsive to its request (Dkt. #39). Pursuant to the Court's April 23, 2020 Order (Dkt. #42), the parties filed a joint report (the "Joint Report") (Dkt. #51) stating their positions. Plaintiff argued that (i) the Investor Communications would not contain relevant information and (ii) production of the documents would constitute an undue burden and would require Plaintiff to expend "hundreds of hours" to complete this process. *See* Joint Report at 7-13 (Dkt. #51). The Court disagreed and ordered the Plaintiff to produce documents responsive to Request No. 31 that had been previously segregated by the Plaintiff or his assistant by June 12, 2020. June 2, 2020 Order ("June 2 Order") (Dkt. #57). Defendants reviewed these Documents and identified additional records referenced in the communications that had not been produced and were responsive. Rothstein Kass requested these responsive records be produced, but after further efforts to meet and confer, Plaintiff again refused. *See* App. at 116-120, Ex. C.

On June 29, 2020, the Court sustained the Plaintiff's relevance objection, noting that the Plaintiff "represents that his damages are not based on any of the documents Rothstein Kass

seeks." June 29 Order at 2 (Dkt #64). The Court stated, however, that expert reports would be forthcoming on August 14, 2020, and that "if it appears by the report of the Receiver's damages experts that the damages calculation *does* rely on investors' claims against the Receivership Estate, then Rothstein Kass may renew its motion prior to the close of discovery." *Id.* As articulated herein, Plaintiff's expert report plainly relies on investor claims as a source of his alleged damages. Rothstein Kass respectfully renews its motion.

III. ARGUMENT

As this Court has held, "the party resisting discovery must show specifically how each discovery request is not relevant or otherwise objectionable" and must "show how the requested discovery is overly broad, unduly burdensome, or oppressive by submitting affidavits or offering evidence revealing the nature of the burden." (citations omitted). *See* April 23, 2020 Order at 2-3 (Dkt. #42). Because Plaintiff's expert report demonstrates Plaintiff's reliance on investor claims as a source of his alleged damages and the Investor Communications contain information related to these investor claims, Plaintiff's relevance and undue burden objections fail.

A. Plaintiff's Expert Report Proves that Investor Communications are Relevant

Relevance is broadly construed. *SEC v. Brady*, 238 F.R.D. 429, 437 (N.D. Tex. 2006). A request for discovery should be considered relevant "if there is 'any possibility' that the information sought may be relevant to the claim or defense of any party." *Merrill v. Waffle House, Inc.*, 227 F.R.D. 467, 470 (N.D.Tex. 2005) (quoting *Sheldon v. Vermonty*, 204 F.R.D. 679, 689 (D. Kan. 2001)).

Plaintiff's expert relies on two damages theories: "(1) the increased liabilities that were sustained by the Receivership Estate" ("Increased Liability Theory") and (2) the

misappropriation or misuse of corporate funds by Faulkner and other individuals. *See* App. at 64-65, Ex. A. Plaintiff's expert describes the Increased Liability Theory as follows:

> "The Increased Liabilities Damages calculation is comprised of the following (1) amounts received by the Breitling entities from investors, less (2) refunds and/or disbursements to investors, less (3) the value of any remaining assets held by the Receivership Estate."

Id. at 65. In other words, Plaintiff's damages theory is based on the amount of money investors invested into Breitling and allegedly lost, minus any returns they received.[3]

While it is undeniable that Plaintiff is seeking damages based on investor claims, he may claim, incorrectly, that those investor claims may be determined solely from the receivership entities' books and records without resort to communications between the Plaintiff and those investors. This position cannot possibly be correct unless the Plaintiff intends to rely solely on records both he and the SEC claim are the basis of a fraud.[4] Specifically, Plaintiff's expert, relies on a data base of bank records reflecting cash deposits and outflows made to various Breitling related bank accounts to determine increased liabilities to investors. To take one

[3] Plaintiff knows this theory is impermissible under the law. Receivership entities do not have standing to pursue damages to investors and may not couch investor damages as "increased liabilities" to a receivership estate to circumvent this standing requirement. *See Reneker v. Offill*, No. 3:08-CV1394-D, 2012 WL 2158733 at *6 (N.D. Tex. June 14, 2012) (Fitzwater, C.J.) ("*Reneker IV*") (holding that investor losses and liabilities to receivership entities were not distinct from one another and were impermissible as damages theory); *Taylor v. Scheef & Stone, LLP et al.*, No. 3:19-CV-2602-D, 2020 WL 4432848, at *10 (N.D. Tex. July 31, 2020) (Fitzwater, C.J.) (citing to *Reneker I* and noting that Thomas L. Taylor may only assert claims for alleged fraudulent conduct directed at the Breitling entities, not investors). Nevertheless, Defendants must obtain the relevant documents to defend against it.

[4] Even if Plaintiff does intend to rely solely on such information, there is no requirement that Defendants be limited in the same manner. The parties may obtain discovery "regarding *any* nonprivileged matter that is relevant to any party's claim or defense…" Fed. R. Civ. P. 26(b)(1) (emphasis added). "Relevant information encompasses 'any matter that bears on, or that reasonably could lead to other matter that could bear on, any issue that is or may be in the case.'" *Merrill*, 227 F.R.D. at 470 (N.D. Tex. 2005) (quoting *Oppenheimer Fund, Inc. v. Sanders*, 437 U.S. 340, 351, 98 S.Ct. 2380, 57 L.Ed.2d 253 (1978)). Plaintiff may not choose to limit the information he relies on and then claim that any other information would be irrelevant.

illustrative example, the Plaintiff's expert asserts increased liabilities associated with investor "Holmes, Carl Dean & Willynda ("H, C, & W") in the amount of $15,625. See App. at 126-134, Ex. F.[5] However, the records relied upon by Plaintiff's expert in fact show that investor H, C, & W made a deposit in the amount of $15,625 on July 30, 2013, made another deposit in the amount of $15,625 on March 3, 2014, and *received an investor refund* in the amount of $32,337.86 on November 18, 2014. *Id.*

While investor H, C, & W appears to have suffered no economic damages at all, Plaintiff is seeking to recover $15,625 from Defendants in connection with this investor. Aside from this error evident on the face of the receivership bank records, the bank records alone do not establish that bank receipts and disbursements—without more—constitute "increased liabilities". The best evidence of any liabilities from investor damages is investor's claims themselves, which are contained in the Investor Communications. Otherwise, Plaintiff would be free to claim any investment into Breitling as damages, even if the investor in question was not pursuing any claims in the Receivership or had otherwise been refunded, like H, C, & W. In the case of investor H, C & W, surely the Plaintiff does not intend to claim damages from a $15,625 liability without seeking to determine whether such a claim is merited.

Plaintiff's expert acknowledges the importance of testing disbursements and receipts reflected in the bank records: "…BRG further tested Veritas' identification of investor deposits and disbursements, which has *a direct impact on BRG's calculation of damages*." App. at 72, Ex. A (emphasis added). Although Plaintiff's expert has conducted his own testing, Plaintiff would deny the Defendants the ability to test whether or not receipts and disbursement in fact give rise to "increased liabilities." Defendants should not be required to accept blindly

[5] Because Plaintiff's expert's appendix that details this information is extremely lengthy, Defendants have excerpted and highlighted a portion of it for the Court's use.

Plaintiff's expert's conclusions without resort to Investor Communications. The Investor Communications previously produced by Plaintiff contain details on (a) the amount investors invested in Breitling properties (b) the date of investment (c) the properties invested in and (d) the amount of money received by investors from these investments. *See* App. at 122-124, Exs. D & E. Such details provide necessary context for investments into Breitling that the bank records may not reflect, including what information the investors relied on in choosing to invest, whether the investors agreed to transfers of their investments, and what documentation the investors received regarding their investment. *See id*.

In fact, the documentation of the investors' interests in the Breitling entities has recently become an issue in the related *SEC v. Faulkner* case. Plaintiff has recently sought to invalidate the royalty interest conveyances that Breitling provided to investors in certain wells "(1) where any asset underlying an offering was purchased with commingled investor funds; (2) where any offering was over-sold; (3) where any asset underlying an offering was over-conveyed; or otherwise when conveyances 'were executed in a "haphazard manner"'. . . ." Receiver's Motion to Invalidate Certain Conveyances in Furtherance of the Court-Approved Plan of Distribution, *SEC v. Faulkner*, 3:16-cv-01735-D at 3 (Dkt. # 559) (internal citations omitted). In attempting to invalidate investors' conveyances, Plaintiff concedes that the basis for some of the Breitling investors' claims—ownership of an interest—is not supported. Bank records alone, as used in Plaintiff's expert's report, would not capture this distinction.

Indeed, Plaintiff's efforts to invalidate conveyances raise another issue with Plaintiff's damages theory that bank records cannot identify: investors' offset of losses through tax breaks. While approving the Plaintiff's distribution plan, the Court in *SEC v. Faulkner* rejected Breitling investors' arguments that royalty and working interest investors should be treated separately

because working interest investors could offset their losses through tax breaks. "As the Receiver clearly explains, to the extent that some Investor Claimants have benefited from tax-related write-offs or deductions to date, the Receiver can take these benefits into account when calculating the Investor Claimants' 'net-out-of-pocket losses.'" *SEC v. Faulkner*, No. 3:16-CV-1735-D, 2020 WL 2042339, at *6 (N.D. Tex. Apr. 28, 2020). But Plaintiffs' expert has not included any tax write-offs or deductions in his damages analysis, even though the basis of Plaintiff's "increased liabilities" theory—the investment into the Breitling entities minus any value received from the Breitling entities—substantially mirrors the "net out-of-pocket losses" definition in the Plaintiff's proposed plan of distribution. *See id.* at *1 ("An Investor Claimant's 'net out-of-pocket loss' would be calculated as the total amount invested in or through the Offering Entities less any amounts, or the value of any assets, received—and retained--with respect to the investment (e.g, payment or assets transferred from a Receivership entity . . .)"). The Breitling bank records cannot capture these tax breaks that can and will affect Investor's claims—but the Investor Communications can illuminate the issue.

Plaintiff cannot continue to pursue damages resulting from investor claims in the Receivership while simultaneously contending that communications about those same claims are irrelevant. *See Merrill*, 227 F.R.D. at 470-471 (if discovery seems relevant, objecting party bears the burden of establishing lack of relevance). Plaintiff's objection should be overruled and he should be required to produce documents responsive to Rothstein Kass's request.

B. Request No. 31 Does Not Impose an Undue Burden on the Plaintiff

Plaintiff cannot support any claim of undue burden. *See SEC. v. Brady,* 238 F.R.D. 429, 437 (N.D. Tex. 2006) (A party objecting because of undue burden must prove the undue burden, usually through an affidavit or other evidentiary proof). Plaintiff's burden, if any, is outweighed

by the importance of the Investor Communications, which contain critical information on Plaintiff's damages theory. *See generally* Fed. R. Civ. P. 26(b)(1) (parties may obtain discovery that is proportional to the needs of the case, considering in part whether "the burden or expense of the proposed discovery outweighs its likely benefit."). Plaintiff may not rely on investor claims for tens of millions of dollars in alleged damages while simultaneously objecting that producing the communications with information on these damages would be unduly burdensome.

Further, after multiple communications, pleadings, and sworn declarations that producing Investor Communications would cost tens of thousands of dollars and take "hundreds of hours," Plaintiff reversed course and stated that he has a usual practice to segregate communications with claimants. *Compare* Joint Report at 12 (Dkt. #51) ("It would potentially take the Receiver and/or his staff literally hundreds of hours to review the files . . . to identify possible communications from investors/potential claimants and segregate and produce those communications.") *and* App. to Joint Report at 46 (Dkt. #52), Decl. of Thomas Taylor III, ¶ 15 (stating review and production of Claimant Communications would take hundreds of hours and approximately cost "tens of thousands of dollars. . . .") *with* App. at 118, Ex. C ("[The Receiver] is unaware of any other responsive documents . . . to the Receiver's knowledge they have produced all investor communications."). Given this newly stated "usual practice" of segregating emails, there will be a minimal burden (and certainly not an "undue" burden), in producing documents responsive to Rothstein Kass's request.

IV. CONCLUSION

For the aforementioned reasons Defendants respectfully request that the Court enter an order requiring the Plaintiff to produce any additional documents in his

possession, custody, or control responsive to Request No. 31 and to supplement his production in the future.

Dated: September 16, 2020

Respectfully submitted,

/s/ Nicolas Morgan

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CERTIFICATE OF SERVICE

This is to certify that a true and correct copy of the foregoing document has been served to all counsel of record in accordance with the Federal Rules of Civil Procedure on September 16, 2020 via ECF notification.

/s/ Nicolas Morgan
NICOLAS MORGAN

Certificate of Conference

Plaintiff opposes this motion. Counsel for Defendants and Edward Snyder, counsel for the Plaintiff, have conferred via telephonic conference on September 11, 2020, during which there was a substantive discussion of every item presented to the Court in this motion and, despite best efforts, the counsel have not been able to resolve those matters presented.

/s/ Nicolas Morgan
NICOLAS MORGAN