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

HOWELL FAMILY TRUST DTD 01/27/2004, (LARRY E. HOWELL, TRUSTEE and SHERRY R. HOWELL, TRUSTEE),	§	
Plaintiff,	§	
v.	§	CIVIL ACTION NO. 3:18-CV-02864-M
HOLLIS M. GREENLAW, TODD ETTER, MICHAEL K. WILSON, UDF LAND GENPAR, L.P., UDF LAND GP, LLC, UMTH LAND DEVELOPMENT, L.P., UMT SERVICES, INC., and UMT HOLDINGS, L.P.,	§	
Defendants,	§	
UNITED DEVELOPMENT FUNDING LAND OPPORTUNITY FUND, L.P.,	§	
Nominal Defendant.	§	

ORDER

Before the Court is the Motion to Dismiss, filed by Defendants UDF Land GenPar, L.P. ("GenPar"), UDF Land GP, LLC ("UDF Land"), UMTH Land Development, L.P. ("UMTH"), UMT Holdings, L.P. ("UMT Holdings"), and UMT Services, Inc. ("UMT Services") (together, "UDF Entity Defendants") (ECF No. 30), and the Motion to Dismiss, filed by Defendants Hollis Greenlaw, Todd Etter, and Michael Wilson (together, the "Individual Defendants") (ECF No. 31). For the reasons stated below, the Motions are DENIED.

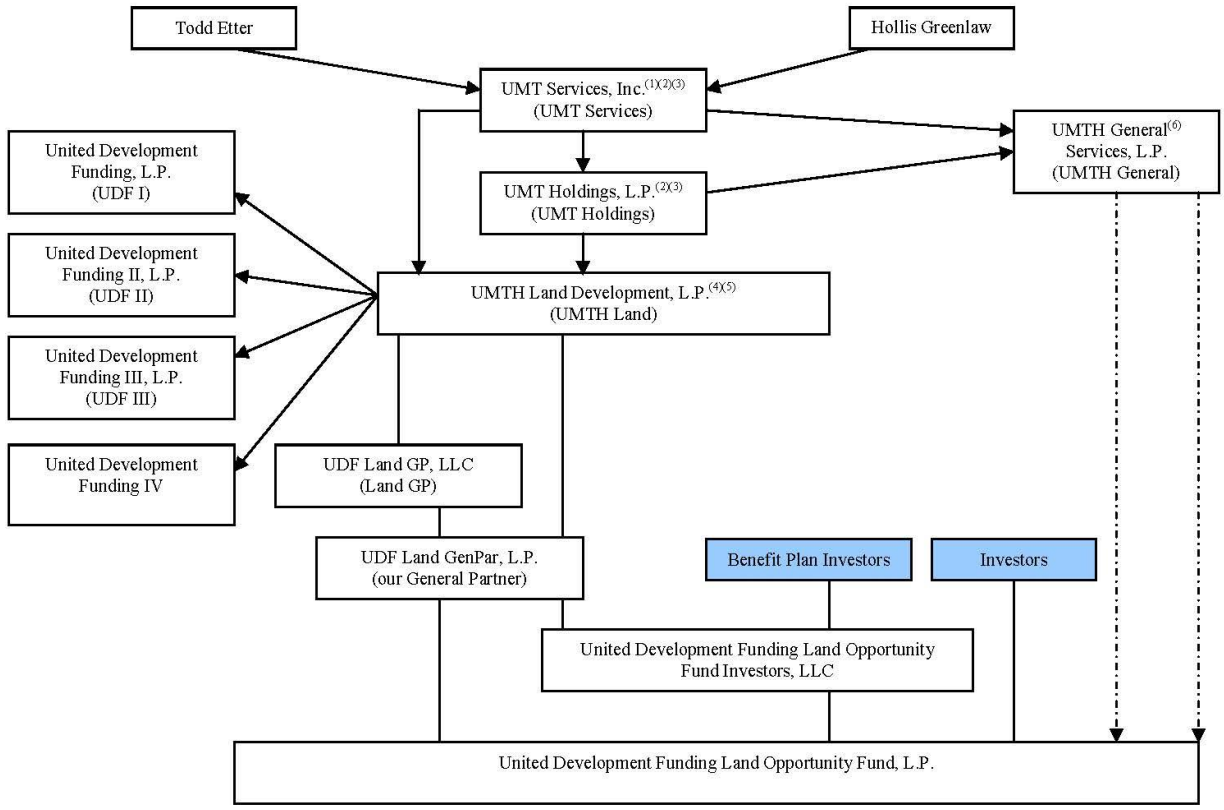
I. Background

This is a shareholder derivative action brought by Plaintiff on behalf of Nominal Defendant United Development Funding Land Opportunity Fund, LP ("LOF"). The following allegations are taken from Plaintiff's Verified Derivative Complaint (ECF No. 1).

LOF is part of the United Development Funding ("UDF") family of investment funds. (ECF No. 1 ¶ 26). UDF was founded in 2003 by Greenlaw and Etter "with the aim of starting one or more investment funds to loan money to developers of residential real estate, with rates above those offered by commercial lenders." (*Id.*). UDF established a number of funds, including UDF I, II, III, IV, V, and LOF, that each raised money from investors. (*Id.*). LOF was formed to invest in "finished lots, 'paper' lots, land to be developed into residential home lots, model and finished new inventory, and other residential real property and dwellings, loans secured by properties, loans provided to entities recently filing for Chapter 11 bankruptcy protection and other real estate opportunities." (*Id*. ¶ 17).

GenPar is the general partner of LOF. (*Id.* ¶ 14). UDF Land is the general partner of GenPar, and UMTH holds 100% of the limited partnership interests in GenPar. (*Id.* ¶¶ 1, 14). UDF Land is owned by UMTH. (*Id*.). UMTH also serves as the asset manager for other UDF funds, including UDF I, II, III, and IV. (*Id.* ¶¶ 14, 29). UMT Holdings holds 99.9% of the limited partnership interests in UMTH. (*Id.* ¶¶ 29, 46). UMT Services is the general partner of UMT Holdings and UMTH and holds 0.1% of the limited partnership interests in UMTH. (*Id.* ¶ 29). Etter, Greenlaw, and Wilson are directors of UMT Services, and Etter and Greenlaw each own 50% of UMT Services. (*Id*. ¶¶ 1, 11–13, 29). Etter, Greenlaw, and Wilson hold 30%, 30%, and 10.09% of the limited partnership interests in UMT Holdings, respectively. (*Id.* ¶ 29). In

the Complaint, Plaintiff includes the following organizational chart from LOF's Offering Memorandum, which summarizes the relationships between the various UDF entities:



(*Id.* ¶ 14).

GenPar and its affiliates, including UMTH, manage LOF's day-to-day business and identify and make investments on behalf of LOF. (*Id.*). Plaintiff contends that "the investment and management decisions made by GenPar with respect to LOF are directed by LOF's Investment Committee, which oversees the investment activities of the [UDF] programs managed by UMTH." (*Id.* ¶ 18; *see also id.* ¶ 52 (The Investment Committee "made all of the investment, loan underwriting and impairment decisions for UDF III, IV, and LOF."). Greenlaw is the President and CEO of UMTH and Chairman of the LOF Investment Committee; Etter is the Chairman of UMT Services and a member of the LOF Investment Committee; and Wilson is a board member of UMT Services and a member of the LOF Investment Committee. (*Id.* ¶ 20).

In December 2007, UDF III and CTMGT, LLC, an unaffiliated Texas limited liability company, executed a $25 million secured promissory note with a maturity date of December 21, 2010. (*Id.* ¶ 38). The CTMGT Note was amended numerous times, and in December 2014, it was a $65.7 million note with a maturity date of July 1, 2015. (*Id.* ¶ 38). The interest rate on the CTMGT Note is 16.25%. (*Id.* ¶ 38).

Plaintiff alleges that UDF III's offering model relied on the expectation that it would make regular distributions to its investors. (*Id.* ¶ 35). Plaintiff states that "[a]t times, UDF III's monthly distributions to investors exceeded the payments UDF III received from its developer borrowers during the same period," and that "[b]y 2011, UDF III, at times, did not have sufficient monthly cash flow to cover its distributions." (*Id.* ¶¶ 35–36).

According to the Complaint, "[i]n July 2011, Defendants, knowing that UDF III's financial condition was precarious, that it could not pay distributions to its investors and that UDF III would not be able to fully repay any loan from LOF, caused LOF to enter into a loan participation agreement with UDF III pursuant to which LOF purchased a participation interest in [the CTMGT Note]." (*Id.* ¶ 39). Plaintiff alleges that Defendants intended "to loot LOF in order to bail out UDF III" and hid this intention from LOF's limited partners. (*Id.* ¶ 39; *see also id.* ¶ 52 ("Defendants each knew, or should have known, that the transactions between LOF and UDF III and the payment of distributions to UDF III investors using LOF funds were contrary to LOF's stated business purposes to the detriment of LOF. Defendants knew, based on their control of UDF III, that the CTMGT Note would be largely uncollectable.").

Plaintiff asserts that UDF III's quarterly SEC filings from November 14, 2011, to November 14, 2014, reflected the amount of LOF's participation interest in the CTMGT Note. (*Id.* ¶¶ 40–42). Plaintiff alleges that "[s]ubsequently, UDF III stopped reporting financials." (*Id.*

¶ 43). The 4Q 2016 letter to LOF partners signed by Greenlaw, Etter, and Wilson as the Board of Directors of UMT Services stated that the CTMGT Note remained unpaid and that "management is evaluating this loan as part of the financial statement preparation process and experts [sic] to be able to provide a more accurate update once Eisner Amper LLP completes its audit of the Fund's financial statements." (*Id.*). Since the 4Q 2016 letter, LOF's limited partners have not received any information about the financial condition of LOF or the status of the CTMGT Note. (*Id.* ¶ 44). Plaintiff states that "[o]n information and belief, only $8.5 million of the CTMGT Note was repaid to LOF, leaving approximately $13 million in default." (*Id.* ¶ 45).

Plaintiff asserts claims for breach of fiduciary duty and unjust enrichment against all of the Defendants and a claim for aiding and abetting a breach of fiduciary duty against the UDF Entity Defendants. (*Id.* ¶¶ 72–83). Plaintiff states that it did not make a demand on any of the Defendants before filing its Complaint, arguing that demand would have been futile. (*Id.* ¶ 71).

On January 11, 2019, the UDF Entity Defendants moved to dismiss Plaintiff's claims against them, arguing that (1) Plaintiff lacks standing because the Complaint fails to allege facts demonstrating that a demand on LOF's general partner would have been futile, (2) limitations bars Plaintiff's claims, and (3) Plaintiff fails to state a claim for breach of fiduciary duty, aiding and abetting, and unjust enrichment. (ECF Nos. 31 and 32). The same day, the Individual Defendants moved to dismiss Plaintiff's claims against them, arguing that (1) limitations bars Plaintiff's claims, and (2) Plaintiff fails to state a claim for breach of fiduciary duty and unjust enrichment. (ECF No. 30). The motions are ripe for review.

II. Legal Standard

To survive a Rule 12(b)(6) motion to dismiss, the plaintiff must have pleaded "a short and plain statement of the claim showing that the pleader is entitled to relief." Fed. R. Civ. P.

8(a)(2). In analyzing a motion to dismiss for failure to state a claim under Rule 12(b)(6), the Court accepts all well-pleaded facts as true and views them in the light most favorable to the plaintiff. *Thompson v. City of Waco*, 764 F.3d 500, 502 (5th Cir. 2014); *In re Katrina Canal Breaches Litig.*, 495 F.3d 191, 205 (5th Cir. 2007). The Court will not, however, "accept as true conclusory allegations, unwarranted factual inferences, or legal conclusions." *Great Lakes Dredge & Dock Co. LLC v. La. State*, 624 F.3d 201, 210 (5th Cir. 2010).

III. Analysis

A. Demand Futility

A derivative shareholder's claim allows an individual stockholder to bring "suit to enforce a *corporate* cause of action against officers, directors, and third parties." *Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 95 (1991) (emphasis in original) (internal quotation omitted). "Devised as a suit in equity, the purpose of the derivative action [is] to place in the hands of the individual shareholder a means to protect the interests of the corporation from the misfeasance and malfeasance of faithless directors and managers." *Id.* (internal quotation omitted).

This derivative right, however, is not absolute. Before a shareholder can act on behalf of the corporation in this manner, he or she must demonstrate "that the corporation itself had refused to proceed after suitable demand, unless excused by extraordinary conditions." *Id.* at 95–96 (internal quotation omitted). This precondition is codified at Federal Rule of Civil Procedure 23.1:

> The complaint must be verified and must: . . . (3) state with particularity: (A) any effort by the plaintiff to obtain the desired action from the directors or comparable authority and, if necessary, from the shareholders or members; and (B) the reasons for not obtaining the action or not making the effort.

Fed. R. Civ P. 23.1(b)(3). The obligation to make a demand is governed by state law. *Kamen*, 500 U.S. at 108–09. Here, the parties agreed that Delaware law applies. (ECF No. 32 at 5–6; ECF No. 38 at 8–9).

Under Delaware law, a limited partner may bring a derivative action "in the right of a limited partnership to recover a judgment in its favor if general partners with authority to do so have refused to bring the action or if an effort to cause those general partners to bring the action is not likely to succeed." 6 Del. C. § 17–1001. In determining futility, Delaware courts apply the *Aronson* test, which asks "whether, under the particularized facts alleged, a reasonable doubt is created that: (1) the [general partners] are disinterested and independent [or] (2) the challenged transaction was otherwise the product of a valid exercise of business judgment." *Aronson v. Lewis*, 473 A.2d 805, 814 (Del. 1984), *overruled on other grounds by Brehm v. Eisner*, 746 A.2d 244, 256 (Del. 2000) (holding that "[t]hese prongs are in the disjunctive. Therefore, if either prong is satisfied, demand is excused").

Plaintiff claims that it would have been futile to make a demand on GenPar, because GenPar was beholden to and controlled by Greenlaw, Etter, Wilson, and the other UDF Entity Defendants, who were interested in the CTMGT Note. (ECF No. 38 at 9–14).

1. Control of GenPar by the Individual Defendants and the Other UDF Entity Defendants

"An entity general partner is beholden to its owner for purposes of demand futility." *Refco Grp. Ltd., LLC v. Cantor Fitzgerald, L.P.*, Civ. No. 1654, 2014 WL 2610608, at *16 (S.D.N.Y. June 10, 2014) (discussing and applying Delaware law); *see also Gerber v. EPE Holdings, LLC*, Civ. No. 3543, 2013 WL 209658, at *13 (Del. Ch. Jan. 18, 2013) (excusing demand on the general partner because the general partner was "control[led] and dominat[ed]" by an individual and "[t]he action that [the plaintiff] would have sought, had he made demand,

would have been directed at" entities owned by the individual); *Brinckerhoff v. Enbridge Energy Co., Inc.*, Civ. No. 5526, 2011 WL 4599654 (Del. Ch. Sept. 30, 2011) (finding that it would have been futile for plaintiff to demand that the general partner sue the entity that "indirectly own[ed] 100%" of the general partner); *Dean v. Dick*, Civ. No. 16566, 1999 WL 413400, at *3 (Del. Ch. June 10, 1999) (finding "it very persuasive that where the general partner is 100% owned by one person, and the general partner would be required to bring suit against that person, there is at least *some* doubt as to the disinterest of that person") (emphasis in original).

The Court finds that Plaintiff has pleaded sufficiently that GenPar is controlled by and beholden to Defendants for purposes of demand futility. (*See* ECF No. ¶¶ 1, 14); *see also Refco Grp. Ltd.*, 2014 WL 2610608, at *16 (finding that the plaintiff adequately pleaded that an individual dominated the general partner because "[a]s one moves up the chain of entities from [the general partner] toward [the individual] . . . each entity is either managed by the next entity or beholden to it by virtue of being wholly owned").

The UDF Entity Defendants contend that Delaware courts have rejected the argument that demand on a board of directors would be futile where the directors would have to sue themselves. (ECF No. 43 at 1–2). But Plaintiff is not arguing that GenPar cannot be expected to sue itself. Rather, it is arguing that GenPar cannot be expected to sue the Individual Defendants and the other UDF Entity Defendants. "This is an argument that [GenPar is] 'dominated' by or 'beholden to' an interested party." *In re Harbinger Capital Partners Funds Inv'r Litig.*, Civ. No. 1244, 2013 WL 5441754, at *18 (S.D.N.Y. Sept. 30, 2013) (applying Delaware law), *opinion vacated in part on reconsideration on other grounds*, Civ. No. 1244, 2013 WL 7121186 (S.D.N.Y. Dec. 16, 2013).

2. The Individual Defendants and UDF Entity Defendants' Interest in the CTMGT Note

Disinterested "means that directors can neither appear on both sides of a transaction nor expect to derive any personal financial benefit from it in the sense of self-dealing, as opposed to a benefit which devolves upon the corporation or all stockholders generally . . . ." *Aronson*, 473 A.2d at 812.

Plaintiff alleges that "LOF was used by Defendants as part of their Ponzi scheme in which they looted various UDF funds, including [UDF IV, UDF V, and LOF], in order to pay distributions to [UDF III] investors, without disclosing the actual purpose of the fund transfers and without regard to the harm to the funds, such as LOF, to which they owed fiduciary duties." (ECF No. 1 ¶ 4). Plaintiff specifically contends that in order to pay UDF III investors, Defendants caused LOF to purchase the participation interest in the CTMGT Note, knowing that LOF would not be repaid. (*Id.* ¶¶ 7, 39, 52). Plaintiff also alleges that the Individual Defendants "had a strong incentive to prop up UDF III and thus conceal the fact that UDF III was struggling financially and could not make distribution payments to UDF III investors out of its own funds." (*Id.* ¶ 54). Plaintiff contends that if such knowledge became public, "prospective investors would have become reluctant to invest." (*Id.*).

The UDF Entity Defendants argue that Defendants could not have appeared on both sides of the transaction between UDF III and CTMGT, because CTMGT is not affiliated with any Defendant. (ECF No. 43 at 2–3). However, the thrust of Plaintiff's argument is not that Defendants appeared on both sides of the transaction between UDF III and CTMGT, but rather that Defendants appeared on both sides of the transaction between UDF III and LOF, in which UDF III (which is owned and controlled by Defendants) caused LOF (which is also owned and controlled by Defendants) to purchase the participation interest in the CTMGT Note.

The Court finds that Plaintiff has pleaded sufficiently that there is a reasonable doubt that Defendants are disinterested and independent. As such, demand is excused.[1]

B. Statute of Limitations

Defendants argue that Plaintiff's claims are barred by the applicable statute of limitations. (ECF No. 32 at 14–17; ECF No. 30 at 6–9). The parties agree that Texas law applies, and that the limitations for Plaintiff's breach of fiduciary duty and aiding and abetting claims is four years and the limitations for its unjust enrichment claim is two years. (ECF No. 38 at 18–19; ECF No. 32 at 14; ECF No. 30 at 10). Defendants argue that Plaintiff's causes of action accrued in July 2011 when LOF and UDF III entered into the participation agreement. (ECF No. 30 at 10–11; ECF No. 32 at 15–17).

Plaintiff responds that the discovery rule applies to toll limitations of its claims. (ECF No. 38 at 19). Plaintiff states that it "had no basis to know or suspect facts giving rise to its claims until after the issuance of the 4Q 2016 Letter to Partners in early 2017," and that the "Letter's absence of information speaks volumes about collectability and is the first clue that the CTMGT Note was failing or uncollectable." (*Id.*). Defendants respond that Plaintiff failed to affirmatively plead facts in its Complaint to allow Plaintiff to invoke the discovery rule.[2] (ECF No. 43 at 7).

[1] The Court need not address the second prong of *Aronson*, *see Dean*, 1999 WL 413400, at *3, or Plaintiff's arguments that demand futility was shown by these facts: (1) Greenlaw and Etter's alleged failure to respond to a demand in *Evans v. Greenlaw, et. al*, Case No. 3:16-cv-0635 (N.D. Tex. 2016), (2) Defendants' alleged denial of similar allegations in *United Development Funding, L.P. v. Bass*, Cause No. 17-06253-B (County Court of Dallas Cty, Tex. 2018), and (3) the SEC suit and consent judgment against Greenlaw and Etter. (ECF No. 1 ¶¶ 56–58; *see also* ECF No. 38 at 15–16).

[2] Defendants also argue that Plaintiff "affirmatively exclude[s] any discovery rule exception by pleading that the CMTGT [sic] Note and each extension were disclosed in public SEC filings." (ECF No. 30 at 11; ECF No. 32 at 15–17). The Court disagrees. The fact that the CTMGT Note itself was public does not mean that Plaintiff knew or should have known that LOF's participation interest in the CTMGT Note allegedly resulted in an injury to LOF.

The discovery rule applies if the alleged injury is inherently undiscoverable and the evidence of injury is objectively verifiable. *See S.V. v. R.V.*, 933 S.W.2d 1, 6 (Tex. 1996). An injury is inherently undiscoverable if "the wrong and the injury were unknown to the plaintiff because of their very nature and not because of any fault of the plaintiff." *Id*. at 7. This does not mean that an injury need be "absolutely impossible to discover, else suit would never be filed . . . ." *Id*. at 7. The Fifth Circuit has held that the discovery rule need not be specifically pleaded in federal court, and that "it is enough that the plaintiff plead sufficient facts to put the defense on notice of the theories on which the complaint is based." *Brandau v. Howmedica Osteonics Corp*., 439 F. App'x 317, 320 (5th Cir. 2011) (quoting *TIG Ins. Co. v. Aon Re, Inc*., 521 F.3d 351, 357 (5th Cir. 2008)).

Plaintiff does not affirmatively assert the discovery rule in its Complaint. Plaintiff has, however, pleaded sufficient facts to put Defendants on notice of its discovery rule theory. Plaintiff alleges that from November 2011 to November 2014, UDF III reported LOF's participation interest associated with the CTMGT Note to the SEC. (ECF No. 1 ¶¶ 40–42). Plaintiff alleges that "UDF III stopped reporting financials," (*see id.* ¶ 43), and that "LOF abruptly stopped reporting to its limited partners after the 4Q 2016 Letter to Partners . . . ." (*Id.* ¶ 9). Plaintiff asserts that the 4Q 2016 letter indicated that the CTMGT loan was still unpaid and stated that "management is evaluating this loan as part of the financial statement preparation process and experts [sic] to be able to provide a more accurate update once Eisner Amper LLP completes its audit of the Fund's financial statements." (*Id.* ¶ 43). Plaintiff further alleges that after the 4Q 2016 letter, "[n]o further information has ever been provided to LOF's limited partners about the financial condition or business of LOF or the status of the CTMGT loan." (*Id.* ¶¶ 9, 44).

These allegations are sufficient to invoke the discovery rule. *See, e.g., TIB–The Indep. BankersBank v. Canyon Cmty. Bank*, 13 F. Supp. 3d 661, 668 (N.D. Tex. 2014) (holding that plaintiff sufficiently pleaded discovery rule by alleging that plaintiff "was unaware of the issues with the Loan until on or about January 31, 2013, when Fannie Mae sent notification to [plaintiff] and demanded repurchase"). Because the discovery rule, if applicable,[3] would toll the two- and four-year statute of limitations until Plaintiff knew or should have known of the alleged injury, the Court is unable to conclude from the face of the pleadings that the statute of limitations bars Plaintiff's claims. Accordingly, the Court denies Defendants' Motions to Dismiss on limitations grounds.

C. Failure to State a Claim Under Rule 12(b)(6)

1. Breach of Fiduciary Duty

To prove a breach of fiduciary duty claim under Delaware law, a plaintiff must show (1) that a fiduciary duty exists and (2) that the fiduciary breached that duty. *York Lingings v. Roach*, Civ. No. 16622-NC, 1999 WL 608850, at *2 (Del. Ch. July 28, 1999).

Defendants argue that Section 7.8 of the LOF Partnership Agreement precludes Plaintiff's breach of fiduciary claim. (ECF No. 32 at 17–20). Section 7.8(a) provides that, "no Indemnitee shall be liable for monetary damages to the Partnership, the Limited Partners, the Assignees or any other Persons who have acquired interests in the Units, for losses sustained or liabilities incurred as a result of any act or omission if such Indemnitee acted in good faith."

[3] In holding that the discovery rule precludes the Court from granting Defendants' Motions to Dismiss based on the statute of limitations, the Court does not suggest that the discovery rule will necessarily apply in this case. Application of the discovery rule to Plaintiff's claims will depend, among other things, on whether Plaintiff can prove that its alleged injury was inherently undiscoverable. *See Woods v. William M. Mercer, Inc*., 769 S.W.2d 515, 518 (Tex. 1988) ("The party seeking to benefit from the discovery rule must . . . bear the burden of proving and securing favorable findings thereon."); *see also Bell v. Phila. Int'l Records*, 981 F.Supp.2d 621, 626 (S.D. Tex. 2013) ("Whether an injury is inherently undiscoverable is a legal question and is determined on a categorical basis.") (citing *Wagner & Brown, Ltd. v. Horwood*, 58 S.W.3d 732, 735 (Tex. 2001)).

(ECF No. 33-1 at App. 348). Defendants assert that the UDF Entity Defendants are Indemnitees. (ECF No. 32 at 17–18). Defendants also claim that Plaintiff's breach of fiduciary duty claim fails because Defendants are protected by the business judgment rule. (ECF No. 32 at 18; ECF No. 30 at 11). The business judgment rule "protects the actions of general partners, affording them a presumption that they acted on an informed basis and in the honest belief that they acted in the best interests of the partnership and the limited partners." *Zoren v. Genesis Energy, L.P.*, 836 A.2D 521, 528 (Del Ch. 2003) (internal quotation omitted). The presumption is rebutted "if the plaintiff shows that the directors breached their fiduciary duty of care or of loyalty or acted in bad faith." *In re Walt Disney Co. Derivative Litig.*, 906 A.2d 27, 52 (Del. 2006).

Plaintiff responds that Section 7.9(a), which relates to GenPar's conflicts of interest, only exculpates GenPar and not the other UDF Entity Defendants. Plaintiff draws the contrast with Section 7.8(a) and notes that "[t]he competing provisions of Section[s] 7.8(a) and 7.9(a) of the Partnership Agreement are unclear on their face as to the extent of exculpation in this case, thus raising, at the very least, an issue of fact which should not be decided on a motion to dismiss." (ECF No. 38 at 20–21). The Court need not determine at this time whether the LOF Partnership Agreement is ambiguous, because Plaintiff has adequately alleged for the purposes of Rule 12(b)(6) that Defendants acted in bad faith, which would exclude indemnification.

Delaware law defines bad faith as "an intentional dereliction of duty, a conscious disregard for one's responsibilities." *In re Walt Disney Co. Derivative Litig*., 906 A.2d at 66 (internal quotations omitted). "Such misconduct is properly treated as a non-exculpable, nonindemnifiable violation of the fiduciary duty to act in good faith." *Id.* In its Complaint, Plaintiff alleges that "[b]y 2011, UDF III, at times, did not have sufficient monthly cash flow to cover its distributions." (ECF No. 1 ¶ 36). Plaintiff asserts that,

> [I]n July 2011, Defendants, knowing that UDF III's financial condition was precarious, that it could not pay distributions to its investors and that UDF III would not be able to fully repay any loan from LOF, caused LOF to enter into a loan participation agreement with UDF III pursuant to which LOF purchased a participation interest in [the CTMGT Note] . . . . The actual purpose of the CTMGT Note – to loot LOF in order to bail out UDF III – was concealed from LOF's limited partners.

(*Id.* ¶ 39). The combination of (1) Defendants' alleged control over both UDF III and LOF; (2) UDF III's alleged problems with making distributions to investors; (3) UDF III's alleged knowledge that LOF's loan would not be fully repaid; and (4) UDF III's alleged failure to report LOF's participation interest to the SEC and to LOF's limited partners, taken together, creates an inference of faithless behavior that meets the 12(b)(6) pleading standard.

Defendants also argue that Plaintiff's breach of fiduciary duty claim fails because the UDF Entity Defendants, other than GenPar, and the Individual Defendants do not have a fiduciary relationship with LOF. (ECF No. 32 at 21; ECF No. 30 at 11–16). Plaintiff responds that GenPar's fiduciary relationship with LOF extends to the other UDF Entity Defendants and to the Individual Defendants because of the chain of ownership and control between Defendants.

Plaintiff's theory of liability relies on a line of cases, beginning with *In re USACafes, L.P. Litigation*, 600 A.2d 43 (Del. Ch. 1991), which hold that "those affiliates of a general partner who exercise control over the partnership's property may find themselves owing fiduciary duties to both the partnership and its limited partners." *Bigelow/Diversified Secondary P'ship Fund 1990 v. Damson Birtcher P'rs*, Civ. No. 16630, 2001 WL 1641239, at *8 (Del. Ch. Dec. 4, 2001); *see also Wallace ex rel. Cencom Cable Income Partners II, Inc., L.P. v. Wood*, 752 A.2d 1175, 1178 (Del. Ch. 1999) ("Officers, affiliates and parents of a general partner, *may* owe fiduciary duties to limited partners if those entities control the partnership's property.") (emphasis in original); *Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, 795 A.2d 1, 34

(Del. Ch. 2001), *aff'd in part, rev'd in part*, 817 A.2d 160 (Del. 2002) (applying *USACafes* to individuals and entities who controlled corporate general partner). The court in *USACafes* declined "to delineate the full scope of [the fiduciary] duty" owed by an entity that controls the general partner, but stated that "it surely entails the duty not to use control over the partnership's property to advantage" the controlling entity. 600 A.2d at 49; *see also Feeley v. NHAOCG, LLC*, 62 A.3d 649, 672–73 (Del. Ch. 2012) ("*USACafes* has not been extended beyond duty of loyalty claims.").

Plaintiff alleges that Defendants owe a fiduciary duty to LOF, including "the highest obligations of loyalty, good faith, due care, oversight, fair dealing and candor." (ECF No. 1 ¶ 73). The Complaint states that the Individual Defendants and the UDF Entity Defendants, other than GenPar, are upstream entities and individuals that are affiliated with and exercise control over GenPar, which, in turn, owes fiduciary duties as a general partner to LOF. (*Id.* ¶¶ 1, 14). The Court finds that Plaintiff has sufficiently pleaded under *USACafes* that Defendants owe Plaintiff a fiduciary duty.[4]

The Individual Defendants assert that Plaintiff's argument that they owe a fiduciary duty to LOF is an "attempt[ ] to pierce the corporate veil without formally making that claim." (ECF No. 30 at 14). However, under *USACafes*, a court may find that an affiliate of a general partner with control over the partnership owes a fiduciary duty to the partnership and its limited partners without allegations of piercing the corporate veil. *See Feeley*, 62 A.3d at 667 (suggesting that traditional veil-piercing doctrine should apply to claims of third-party creditors, while the theory of *USACafes* applies to "internal claims of mismanagement or self-dealing brought by investors

[4] Defendants also argue that LOF's Offering Memorandum discloses that LOF "expect[s] to make Investments with affiliates of [UMTH]." (ECF No. 32 at 20). Although the Offering Memorandum and the Partnership Agreement discuss that conflicts of interest may arise between LOF and its affiliates, neither document waives or exculpates Defendants from bad faith.

against the entity's decision-makers"); Mohsen Manesh, *The Case Against Fiduciary Entity Veil Piercing*, 72 Bus. Law. 61, 76 (2017) ("*USACafes* stands in sharp contrast to traditional veil piercing. Mere control—and not some grave injustice—is all that is required to establish liability under *USACafes*."). Thus, the Court is not persuaded by the Individual Defendant's argument that Plaintiff is required to plead a veil piercing or alter ego theory of liability to sufficiently allege a breach of fiduciary duty claim. Plaintiff's breach of fiduciary duty claim survives Defendants' Motions to Dismiss.

2. Aiding and Abetting Breach of Fiduciary Duty

To state a claim under Delaware law for aiding and abetting a breach of fiduciary duty, a plaintiff must allege (1) the existence of a fiduciary relationship; (2) a breach of that relationship; (3) knowing participation in the breach by a defendant who is not a fiduciary; and (4) damages proximately caused by the breach. *Cargill, Inc. v. JWH Special Circumstances LLC*, 959 A.2d 1096, 1125 (Del. Ch. 2008).

The UDF Entity Defendants claim that because Plaintiff has failed to show a breach of fiduciary duty, its aiding and abetting claim necessarily fails. (ECF No. 32 at 23). The UDF Entity Defendants also assert that Plaintiff has not pleaded that the UDF Entity Defendants, as non-fiduciaries, knowingly participated in the breach of a fiduciary relationship. (*Id.*). Plaintiff responds that its aiding and abetting breach of fiduciary duty claim is an alternative claim, brought in case the Court determines that any of the UDF Entity Defendants owe no fiduciary duty to LOF. (ECF No. 38 at 25).

Even though Plaintiff did not expressly plead its aiding and abetting claim in the alternative, the Court finds that the claim should not be dismissed in the event the Court later decides that Plaintiff "cannot prove the pleaded requisite control necessary to establish the

existence of a fiduciary relationship between each [UDF Entity Defendant] and [LOF]." *Wallace*, 752 A.2d at 1184 (allowing plaintiffs "to pursue the inconsistent, conflicting, aiding and abetting" breach of fiduciary duty claim). Further, Plaintiff's Complaint sufficiently pleads that the UDF Entity Defendants knowingly participated in the alleged breach. (*See* ECF No. 1 ¶¶ 39, 52) (alleging that Defendants caused LOF to enter into the loan participation agreement with UDF III while "knowing that UDF III's financial condition was precarious, that it could not pay distributions to its investors and that UDF III would not be able to fully repay any loan from LOF . . . .").

3. Unjust Enrichment

"Unjust enrichment is the unjust retention of a benefit to the loss of another, or the retention of money or property of another against the fundamental principles of justice or equity and good conscience." *Nemec v. Shrader*, 991 A.2d 1120, 1130 (Del. 2010) (citation and internal quotation marks omitted). It requires: "(1) an enrichment, (2) an impoverishment, (3) a relation between the enrichment and impoverishment, (4) the absence of justification, and (5) the absence of a remedy at law." *Id.*

Defendants argue that Plaintiff's unjust enrichment claim fails because it arises from a relationship governed by a contract. (ECF No. 32 at 21; ECF No. 30 at 16–17). Defendants point to Plaintiff's allegation that Defendants "have been enriched by receiving advisory fees and other compensation that they have not earned through performance of honest services," and contend that such fees and compensation are governed by the terms of LOF's Partnership Agreement. (ECF No. 32 at 22–23).

Defendants are correct that, under Delaware law, a claim for unjust enrichment cannot arise from a relationship governed by a contract. *Nemec v. Shrader*, No. 3878-CC, 2009 WL

1204346, at *6 (Del. Ch. Apr. 30, 2009). However, Delaware courts allow unjust enrichment claims where the contract itself constitutes the alleged wrong. *See, e.g., LVI Grp. Investments, LLC v. NCM Grp. Holdings, LLC*, 2018 WL 1559936, at *17 (Del. Ch. Mar. 28, 2018) ("[B]ecause the Complaint adequately alleges that the Contribution Agreement itself arose from the Defendants' fraud, the existence of that contract does not bar the unjust enrichment claim.").

Here, Plaintiff does not allege that Defendants were unjustly enriched by virtue of the Partnership Agreement itself. Therefore, any claims for fees or compensation that would be governed by the Partnership Agreement are denied. However, Plaintiff's Complaint adequately alleges that the CTMGT Note was itself an improper transaction designed to unjustly enrich Defendants. Plaintiff asserts that "LOF Bail[ed] out UDF III to Its Detriment," and that "[t]he actual purpose of the CTMGT Note – to loot LOF in order to bail out UDF III – was concealed from LOF's limited partners." (ECF No. 1 ¶ 39). Plaintiff alleges that the CTMGT Note was a "bad faith conflict-of-interest transaction [that] severely disadvantaged LOF to the benefit of UDF III and Defendants," and that "LOF was used by Defendants as part of their Ponzi scheme in which they looted . . . LOF, in order to pay distributions to [UDF III] investors, without disclosing the actual purpose of the fund transfers and without regard to the harm to [LOF] . . . ." (*Id.* ¶¶ 4, 53). At the motion to dismiss stage, the Court is unable to conclude that there is no conceivable set of circumstances under which Defendants were unjustly enriched. Thus, Defendants' Motions to Dismiss with respect to Plaintiff's unjust enrichment claim are denied.

IT IS ORDERED that the Motion to Dismiss (ECF No. 30) and the Motion to Dismiss (ECF No. 31) are DENIED.

IT IS FURTHER ORDERED that the Motion to Stay Discovery Pending Resolution of Defendants' Motion to Dismiss (ECF No. 41) is DENIED AS MOOT.

SO ORDERED.

June 10, 2019.

BARBARA M. G. LYNN
CHIEF JUDGE