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UNITED STATES DISTRICT COURT
DISTRICT OF NEVADA

SECURITIES & EXCHANGE COMMISSION v. MATTHEW WADE BEASLEY; *et al.*; Defendants, THE JUDD IRREVOCABLE TRUST; *et al.*; Relief Defendants.	Case No. 2:22-cv-0612-JCM-EJY **DEFENDANT RICHARD R. MADSEN'S REPLY TO RECEIVER'S RESPONSE TO MOTION TO CLARIFY ASSET FREEZE AND TO ALLOW ATTORNEYS TO RETAIN EARNED FEES** ORAL ARGUMENT REQUESTED [LR 78-1]

Richard Madsen is accused of **only** two things in the Amended Complaint: selling unregistered securities and failing to register as a broker or dealer, both "strict liability" offenses. (*See* ECF No. 118 at 23-24, First Claim for Relief, ECF No. 118 at 27, Fifth Claim for Relief.) If the SEC thought Richard Madsen committed fraud, it would have made that allegation in the Complaint. It did not. If there was precedent for imposing an asset freeze limiting the ability to pay attorney's fees for strict liability violations, the Receiver would cite authority. He did not. Instead,

the Receiver intentionally misrepresents the claims against Richard Madsen. There may be fraud claims against others in this case but that does not support a freeze of Mr. Madsen's assets that effectively divests him of the benefit of legal representation that has been fully paid for and **fully earned**.

In his response to Richard Madsen's motion to clarify the asset freeze to allow Mr. Madsen's attorneys to retain their property, Receiver Geoff Winkler misrepresents the claims against Mr. Madsen and ignores that the attorney's fees are fully earned. The Receiver states the "Amended Complaint is replete with express factual allegations" that Mr. Madsen "knew the purchase agreements were fraudulent." But that is patently untrue: no such allegation appears anywhere in the Amended Complaint. At the same time, the Receiver cites no precedent for freezing assets to restrict a defendant not alleged to have engaged in fraud to pay his attorneys. Further, the Receiver simply ignores the fact that Mr. Madsen's attorneys are not holding funds for Mr. Madsen in trust to secure payment for past or future legal work like other defendants' counsel in this case, but were paid fixed fee retainers. The attorney's fees were fully earned before the asset freeze order. Finally, the Receiver continues to offer no legal support for his overbroad and unbounded interpretation of what constitutes the "commingling" of assets. Mr. Madsen respectfully requests this Court enter an order declaring that his counsel are entitled to retain the retainers he paid them.[1]

1. The Amended Complaint Makes No Allegation That Mr. Madsen Engaged In, Or Was Aware Of, Any Fraud.

[1] As more thoroughly explained in his motion, (ECF No. 17-18), Mr. Madsen is not seeking a release of all of his assets that did not originate from the illegal activities carried out by Defendant Beasley and the other defendants allegedly engaged in fraudulent activity. To calculate that amount with precision would undoubtedly require an unnecessary expenditure of judicial resources, not to mention the parties' resources, particularly when Mr. Madsen may lose his legal representation depending on the result of this motion.

The Receiver intentionally misstates the allegations in the Amended Complaint – or to use his words – makes an "abhorrent misrepresentation of the record in this matter" (*see* ECF No. 338 at 10) when he says that the "Amended Complaint is replete with express factual allegations" that Mr. Madsen "knew the purchase agreements were fraudulent." (*Id.*) Richard Madsen is accused of only two things in the Amended Complaint: selling unregistered securities and failing to register as a broker or dealer, both "strict liability" offenses. (*See* ECF No. 118 at 23-24, First Claim for Relief, ECF No. 118 at 27, Fifth Claim for Relief.)

The Amended Complaint makes the following non-fraud allegations regarding Mr. Madsen:

- (¶4) Mr. Madsen (and others) represented to actual and potential investors that investor money would be used to purchase interests in personal injury settlements. The Amended Complaint alleges that Defendants Beasley, Judd, and Humphries knew or were reckless in not knowing the purchase agreements were fictitious. [There is no allegation that Mr. Madsen knew or was reckless in not knowing this.]
- (¶5) Mr. Madsen (and others) recruited investors and received compensation for doing so. Mr. Madsen (and others) were not registered brokers or dealers, nor associated with registered brokers or dealers. [This is a strict liability violation.]
- (¶28) Mr. Madsen is a resident of Utah, promoted the purchase agreement investments to multiple investors, received compensation for the investments he procured and handled investor funds to and from accounts of four companies he owned and controlled.[2]
- (¶43) The J&J Entities (which do not include Mr. Madsen) offered investments in purported personal injury settlement through Mr. Madsen (and others). The paragraph makes a number of other allegations relating to Defendants Beasley and Judd. [There is no allegation that Mr. Madsen knew or was reckless in not knowing this.]
- (¶76) Mr. Madsen (and others) solicited investors and received compensation for doing so. The investors' interests allegedly constituted securities under federal law. [There is no

[2] As the Receiver ominously highlights (*see* ECF No. 338 at 10), the Amended Complaint alleges that Mr. Madsen owned and controlled at least four "shell corporations." (*See* ECF No. 118 at ¶¶ 28 & 89.) Even if those allegations were true, (*see* ECF No. 195, Defendant Richard R. Madsen's Answer to Amended Complaint, at 10-11 (¶ 28)), however, the Amended Complaint does not allege that formation of a shell company is somehow fraudulent and the Receiver does not allege why it would be relevant. *See, e.g., Cellular Communications Equipment LLC v. Apple*, No. 6:14-cv-251-KNM, 2016 U.S. Dist. LEXIS 185341, at * 5 (E.D. Tex. Sept. , 2, 2016) (granting motion in limine to exclude any "argument, evidence, testimony, or reference regarding irrelevant terms like … 'shell company'").

allegation that Mr. Madsen knew or was reckless in not knowing that these interests were securities.]

- (¶77) Mr. Madsen (and others) used the means and instrumentalities of interstate commerce, including the internet, wire transfers, email and the telephone, to solicit and sell securities. [There is no allegation that Mr. Madsen knew or was reckless in not knowing that these interests were securities.]
- (¶78) Mr. Madsen (and others) handled investor funds, which sometimes, after intermediate steps, were paid into or out of the Beasley Law Group's IOLTA account, or into accounts of entities Mr. Madsen (or others) controlled. [There is no allegation that this was fraudulent conduct.]
- (¶89) Mr. Madsen handled investor funds through accounts in two Nevada corporations over which he had sole control. [There is no allegation that this was fraudulent conduct.]
- (¶92) Mr. Madsen (and others) received compensation payments for investor solicitations in accounts of entities Mr. Madsen (or others) controlled. [There is no allegation that this was fraudulent conduct.]
- (¶99) Mr. Madsen told investors that he received commissions on their investments. [There is no allegation that this was fraudulent conduct.]
- (¶100) Mr. Madsen (and others) were not registered with SEC as a broker or dealer, nor associated with a registered broker or dealer. [This is a strict liability violation.]

Clearly, there is no allegation that Mr. Madsen committed fraud, knowingly made any false statements, exercised any control over the alleged illegal conduct, or had any knowledge of the alleged Ponzi scheme. Whether Mr. Madsen's actions somehow furthered the alleged Ponzi scheme, which the Receiver argues instead (*see* ECF No. 338 at 10-11), is irrelevant because there is no allegation that Mr. Madsen knew or should have known that he was working for an alleged Ponzi scheme. The Receiver simply wants to improperly impute the knowledge of other defendants in this action to Mr. Madsen.

The Receiver's misrepresentation of the allegations in the Amended Complaint's allegations is not merely sloppiness. No court has ever previously ordered the relief sought by the SEC and Receiver against a defendant who was not accused of fraud. (*See* ECF No. 332, R. Madsen's Motion to Clarify, at 13) (collecting all prior cases cited by SEC and the Receiver). The presence of fraud allegations in those cases was integral to the holding in each and every case. The

Receiver, knowing this, now attempts to portray the fraud allegations in those cases as coincidental. (*See* ECF No. 338 at 11.)

The Receiver clearly thought allegations of fraud were important when opposing other defendants' requests for asset releases in this case. For example, in the Receiver's response to Defendant Humphries's argument that the SEC had not sufficiently proven that he possessed the requisite scienter to be liable for fraud, the Receiver did not even hint that a finding of fraud was not necessary to deny Humphries' request. The Receiver never argued that the mere fact that Mr. Humphries was a defendant in a case involving an alleged fraudulent Ponzi scheme, or that other defendants engaged in fraud or had knowledge of the fraud was sufficient to deny him a release from the asset freeze for attorney's fees. Instead, the Receiver argued only about the *quality of evidence* establishing Humphries's fraud. (*See* ECF No. 254 at 5-8, Receiver's Response to Humphries' Motion for Release of Funds for Attorney's Fees). The Receiver's sudden about-face, now arguing that fraud allegations are irrelevant, should not be credited by the Court.

2. There Is No Precedent For Limiting The Ability Of A Defendant Such As Mr. Madsen From Paying Attorney's Fees.

As discussed above, the SEC alleges that Mr. Madsen violated the federal securities laws by being involved in an unregistered offering of securities and acting as an unregistered broker-dealer. Neither of these alleged violations constitutes fraud. Neither the SEC nor the Receiver have identified a single case in which any court limited a conduct defendant's use of their own funds for attorney's fees when not charged with fraud.[3] Instead, the Receiver cites *SEC v. Hickey*, 322 F.3d 1123 (9th Cir. 2003) for the general proposition that a court can order an asset freeze to prevent

[3] The possibility that Mr. Madsen may be ordered to disgorge some portion of his assets in the future, however, does not support limiting his ability to pay his attorneys prior to the judgment. There is no precedent for such a pre-judgment freeze in the absence of fraud allegations, and were it otherwise, the SEC could seek to freeze the assets of every defendant in virtually every case it brings – a power that it never claims.

dissipation to preserve assets for disgorgement. (ECF No. 338, Receiver's Response to Defendant Richard Madsen's Motion to Clarify Asset Freeze and to Allow Attorneys to Retained Earned Fees, at 11.) But the Receiver relies on *Hickey* without reference to its context. The "nominal defendant" in *Hickey* was a brokerage firm which was under the "unfettered control" of the defendant who had already been found liable for fraud and contempt. 322 F.3d at 1132-33. The freeze of Mr. Madsen's assets is not analogous to the freeze in *Hickey*, which the court held was necessary "to *effectuate relief already given*." *Id.* at 1133 (emphasis in original.) There is no allegation that Mr. Madsen has any type of control over any defendant accused of fraud.

Similarly, as explained in Mr. Madsen's Memorandum of Points and Authorities in Support of his Motion to Clarify Asset Freeze and to Allow Attorneys to Retained Earned Fees (ECF No. 332 at 10, fn. 1), the only other cases cited by the Receiver (ECF No. 338 at 11) involved relief defendants or the equivalent who had reason to know or at least suspect fraud. Specifically, in *SEC v. Byers*, No. 08 Civ. 7104, 2009 U.S. Dist. LEXIS 59689, at *8, 11 (S.D.N.Y. Jan. 7, 2009), the party holding the asset at issue had suspiciously purchased it for only $1 shortly before the case was filed. In *SEC v. Cavanaugh*, 155 F.3d 129, 136-37 (2d Cir. 1998), the relief defendant had paid no consideration for the proceeds transferred to it, and in *SEC v. Cherif*, 933 F2d 403, 414 n. 11 (7th Cir. 1991), the court explained that the freeze would only be appropriate if the "nominal" defendant had no claim to the relevant assets. In contrast, the Receiver cannot rely on such an assumption here – the Amended Complaint explicitly alleges that Mr. Madsen provided consideration for the commissions he received. (*See* ECF No. 118, Amended Complaint, at ¶¶ 5, 28, 43, 75-78, 89, 92, 99-100.)

It is not merely academic for a court exercising its equitable jurisdiction to distinguish between individuals like Mr. Madsen, who are only alleged to have engaged in registration offenses subject to strict liability, from defendants who allegedly committed fraud or relief defendants who

took money without providing any consideration. Those defendants, i.e., who personally engaged in fraud or took money without providing any consideration, had notice that they had no claim on the funds in the first place. The same cannot be said for an individual like Mr. Madsen (or his attorneys), particularly since the SEC has never previously argued that someone like Mr. Madsen should not be entitled to pay for his legal defense.

3. The Funds Held By Mr. Madsen's Attorneys Are Already Earned.

Unlike the other defendants in this case, Mr. Madsen's attorneys are not holding funds for Mr. Madsen in trust to secure payment for past or future legal work. Mr. Madsen paid fixed fee retainers to Bragança Law and Howard & Howard, which were fully earned when paid. Thus, the Receivership has no property interest in the funds. But the Receiver says nothing about the retainer agreements themselves. (*See* ECF No. 338 at 12-13.)

Mr. Madsen's agreements with his counsel explicitly provide that the agreements are for fixed fees *which are earned upon receipt*. *See* ECF No. 332-1, Ex. 1, Confidential Engagement Agreement (May 14, 2022), at 2 (§ II); ECF No. 332-2, Ex. 2, Confidential Engagement Agreement (July 5, 2022), at 2 (§ II); ECF No. 332-3, Engagement for Performance of Legal Services (July 11, 2022), at 3 (¶ 5). As described in Mr. Madsen's motion (ECF No. 332 at 18), a "fixed fee agreement" exists where "a sum of money [is] paid by a client to secure an attorney's availability over a given period of time," so that "the attorney is entitled to the money regardless of whether he actually performs any services for the client." *In re McDonald Bros. Constr., Inc.*, No. 90 B 884, 114 B.R. 989, 998,1990 Bankr. LEXIS 1242, at *19 (N.D. Ill. Bankr. June 11, 1990) (citing Black's Law Dictionary 1479 (4th ed. 1968) and 7A C.J.S. *Attorney & Client* § 282 (1980)).

Mr. Madsen's engagements with Bragança Law and Howard & Howard are unlike other defendants' retainers that the Court has considered in this case. Those retainers were not designed

to serve as security for his future payments for past or future services rendered and were not fully earned upon payment. *See SEC v. Interlink Data Network of L.A. Inc.*, 77 F.3d 1201, 1205 (9th Cir. 1996). Thus, there is no basis for the Receiver's contention that these retainer funds were simply "transferred" to the attorneys prior to Mr. Madsen being subject to the relevant court orders (*see* ECF No. 338 at 12). In fact, those funds had become the property of the attorneys. That is the express purpose of this type of retainer.

Thus, Mr. Madsen did not attempt to "avoid court orders requiring the freezing or turnover of assets by simply moving them into a trust or other account held by [his] attorney," as this Court described with respect to Defendant Humphries (ECF No. 318, Order Denying Defendant's [Humphries] Motion for Release of Funds, at 8), but Mr. Madsen had fully divested himself of any interest in the funds, just as if he were paying a utility or tax bill. *See, e.g., Ulrich v. Schian Walker, P.L.C. (In re Boates)*, 551 B.R. 428, 438 (B.A.P. 9th Cir. 2016) (under terms of retainer agreement, funds paid to attorney before filing for bankruptcy "never became property of his bankruptcy estate"); *Stephens v. Bigelow (In re Bigelow)*, 271 B.R. 178, 188 (B.A.P. 9th Cir. 2001) (affirming bankruptcy court's determination that payment to attorney was a nonrefundable prepaid retainer, even in absence of written agreement); *In re Heritage Mall Assocs*., No. 694-64711, 184 B.R. 128, 134 1995 Bankr. LEXIS 972, at *20 (D. Ore. Bankr. July 11, 1995) ("classic retainer" earned upon receipt); *In re Production Assocs., Ltd.*, No. 00 B 3644, 264 B.R. 180, 190, 2001 Bankr. LEXIS 814, at *23 (N.D. Ill. Bankr. July 11, 2001) (attorney does not need to even apply to court to use funds paid in "classic retainer"); *In re Gray's Run Techs., Inc.*, No. 5-96-02395, 217 B.R. 48, 52-53, 1997 Bankr. LEXIS 2182, at *7-10 (M.D. Pa. Bankr. Nov. 19, 1997) ("availability fee" or "classic retainer" earned when paid).[4] Accordingly, the funds paid are

[4] Notably, the Receiver does not dispute that the amounts Mr. Madsen paid to his attorneys "were reasonable in light of the circumstances." *See* ECF No. 332 at 19.)

the property of Mr. Madsen's counsel, not subject to any applicable order, and not required to be turned over.

4. The Receiver's Interpretation Of What Constitutes The "Commingling" Has No Support In The Law.

The Receiver continues to offer no precedent for its overbroad position that all of Mr. Madsen's assets have been "commingled" with "tainted funds," and are thus Receivership Property. In making its demand to Mr. Madsen's lawyers, the Receiver asserted that any funds earned by Mr. Madsen that were deposited in the same financial account as what it considers "tainted funds," or funds which were used to pay expenses that could otherwise have been paid by "tainted funds," were "commingled" and thus subject to the Receivership Order. (ECF No. 332 at 16.) But Mr. Madsen shared his financial records with the Receiver nearly two months ago, and the Receiver has never disputed – nor does he even mention in his Response to this motion – that since the beginning of the events described in the Amended Complaint, Mr. Madsen's income and assets with no connection whatsoever to the conduct alleged in Amended Complaint are substantially greater (by a factor of at least ten) than the amount he paid his attorneys. *See* ECF No. 332 at 17-18. Yet because Mr. Madsen did not know to segregate and refrain from spending any money he received from the other defendants in this action – even though neither the SEC nor the Receiver has alleged he had any reason to believe such money was obtained fraudulently – the Receiver takes the position that all of Mr. Madsen's assets have been commingled and thus subject to the asset freeze. That is not the law and does not follow from the text of the orders entered in this matter.

Courts have been clear that to constitute commingling, a defendant must do something more than simply deposit money into an account that also contains tainted funds. The broad approach taken by the Receiver has been uniformly rejected by the courts in other contexts. *See, e.g., US v. $448,342.85, et al.*, 969 F.2d 474, 476 (7th Cir. 1992) ("Bank accounts do not commit crimes; people do. It makes no sense to confiscate whatever balance happens to be in an account bearing a

particular number, just because proceeds of crime once passed through that account."). "Commingled" funds are funds either derived from the fraud, or that have been used to facilitate the fraud – neither of which can be said of Mr. Madsen's separate income and assets. *See, e.g., US v. Ritchie, et al.*, No.: 2:15-CR-0285-APG-GWF, 2019 U.S. Dist. LEXIS 112121, at *3-4 (D. Nev. July 5, 2019) (citing *US v. $448,342.85*) (funds must be "proceeds of the criminal activity" or "used to facilitate the crimes"); *US v. Salvagno, et al.*, No. 5:02-CR-51, 2006 U.S. Dist. LEXIS 61471 at **47-48, 77 (N.D.N.Y. July 21, 2006) (rejecting forfeiture of $200,000 paid to attorneys where money came from account including untainted funds, including gains and earnings). Completely ignoring this requirement, the Receiver (ECF No. 338 at 14) only even mentions one of the cases cited by Mr. Madsen (*US v. 448,342.85*), which ultimately concluded that it was unnecessary to distinguish between tainted and untainted funds because a final judgment had already been entered exceeding the amounts in the accounts at issue. 969 F.2d at 477. But there is no judgment against Mr. Madsen and there is no precedent for treating all of his assets as tainted as if a final judgment had been entered.

5. Conclusion

For the foregoing reasons, Defendant Richard R. Madsen respectfully requests a declaration from the Court that Bragança Law and Howard & Howard may retain the amounts he has paid to them pursuant to Mr. Madsen's engagement agreements with both firms, as they were not and are not subject to the asset freeze and receivership orders previously entered by this Court.

Date: November 4, 2022

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CERTIFICATE OF SERVICE

I, David A. O'Toole, hereby certify that on November 4, 2022, I electronically filed **DEFENDANT RICHARD R. MADSEN'S REPLY IN SUPPORT OF HIS MOTION TO CLARIFY ASSET FREEZE AND TO ALLOW ATTORNEYS TO RETAIN EARNED FEES,** along with supporting papers, with the Court using the CM/ECF system, which will automatically send copies to any attorney of record in the case.

Respectfully Submitted,

/s/ David A. O'Toole
DAVID A. O'TOOLE