CAUSE NO. D-1-GV-10-000454

STATE OF TEXAS, Plaintiff v. RETIREMENT VALUE, LLC, RICHARD H. "DICK" GRAY, HILL COUNTRY FUNDING, LLC, a Texas Limited Liability Company, HILL COUNTRY FUNDING, a Nevada Limited Liability Company, and WENDY ROGERS Defendants, AND KIESLING, PORTER, KIESLING, & FREE, P.C. Relief Defendants	§ § § § § § § § § § § § § § § §	IN THE DISTRICT COURT OF 126TH JUDICIAL DISTRICT TRAVIS COUNTY, TEXS

TSSB'S PLEA TO THE JURISDICTION AND/OR MOTION FOR SUMMARY JUDGMENT AND SUPPORTING BRIEF

TO THE HONORABLE JUDGE OF THE COURT:

The Texas State Securities Board ("TSSB") files this plea to the jurisdiction, and/or motion for summary judgment, and supporting brief, in response to the motions and briefing filed by Wendy Rogers ("Rogers") and Michael McDermott ("McDermott").

I.

BACKGROUND

This controversy arises out of Rogers and McDermott's settlement agreements with the State of Texas, the Receiver for Retirement Value, LLC, and persons who invested in

securities sold by Retirement Value. *See* Exhibits A and J. The background, which is shown by the Travis County district clerk's file in this case, is as follows.

The State of Texas, acting by and through Greg Abbott, then the Attorney General of Texas, and at the request of John Morgan, Securities Commissioner of the State of Texas, brought suit upon verified information complaining of Retirement Value, Wendy Rogers and others.

The suit alleged that Retirement Value, Rogers and others organized Retirement Value to fraudulently sell unregistered securities to the investing public. Specifically, the petition alleged, defendants offered for sale and sold investments in the death benefits of life insurance policies. From April 2009, through February 28, 2010, they raised $77 million from over 800 investors through the sale of these fraudulent securities.

The State sought receivership, injunctive relief, restitution, disgorgement and other equitable relief under the Texas Securities Act, Tex. Rev. Civ. Stat. art. 581-1 et seq. (hereinafter referred to as the "Texas Securities Act" or the "Securities Act"). The State also sought remedies pursuant to the Attorney General's authority under the Texas Deceptive Trade Practices Act, Tex. Bus. & Com. Code § 17.41, et seq.

The Court issued Temporary Restraining Orders, and later issued an Agreed Temporary Injunction against Retirement Value, LLC and other defendants. It also appointed Eduardo S. Espinosa as Receiver for Retirement Value ("RV Receiver").

The RV Receiver filed his Third Amended Cross-Claim and Third-Party Claim joining McDermott as an additional Third-Party Defendant in this lawsuit. The RV Receiver asserted claims against McDermott for, among other things, illegally selling unregistered securities, aiding and abetting the illegal sale of unregistered securities by others, and conspiring with and aiding and abetting the officers of RV in breaching their fiduciary duties to Retirement Value.

On December 7, 2011, this court concluded that Retirement Value's product was a security. *See* Exhibit B**.**

On March 13, 2012, after being served with the Receiver's Third Amended Petition, McDermott filed his Special Appearance, Plea to the Jurisdiction, Plea in Abatement, Special Exceptions, and after and subject thereto, Original Answer.

McDermott later filed a Motion for Clarification of the Court's December 7, 2011 order seeking clarification as to whether it was binding on him, and in response, this court entered an order confirming that it was.

Substantial discovery was developed in the course of the suit, including the deposition of Rogers and other persons associated with Retirement Value.

In August 2012, Rogers entered into a settlement agreement with the State, the Receivers[1] and the intervening investors, which agreement is attached as Exhibit A. McDermott also entered into a settlement agreement with the State, the RV Receiver and

[1] This court also appointed a separate Receiver, Donald R. Taylor, for Hill Country Funding, LLC.

the intervening investors, which agreement is attached as Exhibit J. Both settlements were approved by this Court.

On February 21, 2013, this court further concluded that Retirement Value had engaged in fraudulent practices in the course of selling unregistered securities, violating section 32(A) of the Texas Securities Act. Pursuant to section 32(B) of the Act, it ordered Retirement Value to make restitution in the amount of $ 77.6 million. *See* Exhibit C.

In February 2015, Rogers was indicted by a Collin County grand jury for theft of property, money laundering and fraud in connection with Retirement Value's sale of securities. *See* Exhibit D. In February, 2015, McDermott was also indicted for fraud in connection with Retirement Value's sale of securities and theft of property. *See* Exhibit K.

Both Rogers and McDermott allege that these indictments are a breach of their settlement agreements and have filed motions to enforce the settlement agreements and requests for evidentiary hearing. Rogers has also served two notices of depositions for the testimony of Joe Rotunda and Letha Sparks, both TSSB employees (*see* Exhibits F and G) and the TSSB has moved to quash those notices and for a protection order.

II.

SUMMARY OF ARGUMENT

First, with respect to Rogers and McDermott's claims for breach of the settlement agreements, the State is entitled to immunity from suit. The narrow waiver of immunity established in *Texas A & M University-Kingsville v. Lawson,* 87 S.W.3d 518 (Tex.2002) does not apply here. The holding in *Lawson* was expressly limited to suits for alleged

breach of settlement agreements disposing of Whistleblower Act claims. The court reasoned that, "having waived immunity from suit in the Whistleblower Act, the State may not now claim immunity from a suit brought to enforce a settlement agreement reached to dispose of a claim brought under that Act." Thus, the waiver in *Lawson* was expressly based on the underlying statutory waiver in the Act itself.

Further, this court does not have jurisdiction over criminal proceedings pending before the Collin County district court, and therefore cannot grant the relief requested by Rogers and McDermott in their motions—relief plainly intended to derail the criminal proceedings or effectively undercut the Collin County court's jurisdiction.

Second, the settlement agreements are unambiguous and dispositive as a matter of law; they are expressly limited to civil claims that were or could have been brought in this lawsuit. The agreements are also by their express terms fully integrated. Thus, this court cannot entertain any evidence of extrinsic agreements or understandings.

Third, any information relevant to Rogers and McDermott's motions is protected by section 28 of the Texas Securities Act—and their claims for breach and "enforcement" of the settlement agreements do not come close to establishing "good cause" that would overcome the confidentiality of TSSB investigations. This court should not allow these defendants, under the guise of "enforcing" settlement agreements, to conduct liberal discovery they would not otherwise be entitled to in the Collin County criminal proceeding.

Fourth, instances in which TSSB attorneys have served as special prosecutors do not amount to a "rule" as that term is defined in the APA.

III.

ARGUMENTS & AUTHORITIES

A. The State has immunity from claims for breach of the settlement agreement.

Sovereign immunity refers to the State's immunity from suit and liability. *Wichita Falls State Hosp. v. Taylor*, 106 S.W.3d 692, 694 n. 3 (Tex.2003); *Lowe v. Tex. Tech Univ.*, 540 S.W.2d 297, 298 (Tex.1976). In addition to protecting the State from suit and liability, it also protects the various divisions of state government, including agencies, boards, hospitals, and universities. *Taylor*, 106 S.W.3d at 694 n. 3; *Lowe*, 540 S.W.2d at 298. Sovereign immunity not only bars suits for money damages but also protects the State against suits to "control state action." *Texas Logos, L.P. v. Texas Dept. of Transp.*, 241 S.W.3d 105, 118 (Tex. App.–Austin 2007, no pet.).

1. Immunity bars the suit in the absence of express consent.

Immunity from suit bars an action against the State unless the State expressly consents to the suit. *Tex. Dep't of Transp. v. Jones*, 8 S.W.3d 636, 638 (Tex.1999) (per curiam); *Federal Sign v. Texas Southern Univ.*, 951 S.W.2d 401, 405 (Tex.1997). The party suing the governmental entity must establish the State's consent, which may be alleged either by reference to a statute or to express legislative permission. *Jones*, 8 S.W.3d at 638. Absent the State's consent to suit, a trial court lacks subject-matter jurisdiction. *Id.*

The claimants—here, Rogers and McDermott—have the burden to plead facts affirmatively showing that the trial court has jurisdiction. *Tex. Ass'n of Bus. v. Tex. Air*

Control Bd., 852 S.W.2d 440, 446 (Tex.1993*); Univ. of N. Tex. v. Harvey*, 124 S.W.3d 216, 220 (Tex. App.—Fort Worth 2003, pet. denied). The absence of subject-matter jurisdiction may be raised by a plea to the jurisdiction, as well as by other procedural vehicles, such as a motion for summary judgment. *Bland Indep. Sch. Dist. v. Blue*, 34 S.W.3d 547, 554 (Tex.2000).

2. The narrow exception identified in *Lawson* and *Kalyanaram* does not apply here.

Rogers relies on a single case, *Kalyanaram v. University of Texas System*, 2009 WL 1423920 (No. 03-05-00642, March 20, 2009). But that case and a related case *Kalyanaram v. University of Texas System*, 230 S.W.3d 921, 926-28 (Tex. App.-Dallas 2007, pet. denied) ("*Kalyanaram I*") show that this court does *not* have jurisdiction.

In *Kalyanaram I* the plaintiff relied on *Texas A & M University-Kingsville v. Lawson*, 87 S.W.3d 518 (Tex.2002), to argue that the University was precluded from claiming sovereign immunity in a suit for alleged breach of an earlier settlement agreement. *See Kalyanaram I* at 926. *Lawson*, in turn, involved the alleged breach of a settlement disposing of Whistleblower Act claims. A faculty member had sued Texas A & M University at Kingsville, a State employer, for violations of the Whistleblower Act, Texas Government Code sections 554.001 et seq. *See Lawson*, 87 S.W.3d at 518-19. The parties settled, and as part of that settlement the faculty member released his claims. Later, he sued for breach of the settlement agreement, and in response the university filed a plea to the jurisdiction based on sovereign immunity. *Id* at 519.

The Supreme Court affirmed the court of appeals' decision that the university could not claim immunity in a suit for breach of a settlement of Whistleblower Act claims. The court reasoned that, "having waived immunity from suit in the Whistleblower Act, the State may not now claim immunity from a suit brought to enforce a settlement agreement reached to dispose of a claim brought under that Act." *Id*. at 522–23 (emphasis added); *see also* Tex. Gov't Code Ann. § 554.0035 (Vernon 2004) (waiving sovereign immunity for suits by a public employee alleging violation of Whistleblower Act).

Accordingly, *Lawson* established a narrow exception to the rule that in a breach of contract suit the government must consent to the suit and waive its immunity fully through statute or legislative resolution. *See IT–Davy*, 74 S.W.3d at 858. But this exception was expressly grounded on the statutory waiver of immunity in the Whistleblower Act, and that statutory waiver clearly does not apply here.

3. McDermott's argument that the class-action settlement confers subject-matter jurisdiction on this court is similarly unconvincing.

For his part, McDermott suggests that this court's Final Order and Judgment Approving Class Settlement and Class Counsel Fees and Expenses—in which the court "retains exclusive jurisdiction over the consummation, performance, administration, effectuation and enforcement of the Settlement Agreement, and this Order"—confers subject-matter jurisdiction on this court to hear his claim for enforcement of the settlement agreement. *See* Exhibit L at 13.

But that order refers to the court's approval of the class-action settlement. Nowhere in the court's order is there a suggestion that the court viewed itself as having continuing jurisdiction over *the State's* settlement with McDermott. In any case, district courts cannot enlarge their subject-matter jurisdiction via their own orders. It is also axiomatic that the parties themselves cannot confer subject-matter jurisdiction on the court by agreement. The State's consent to suit can only be established by reference to a statute or to express legislative permission. *See Jones*, 8 S.W.3d at 638; *see also IT–Davy*, 74 S.W.3d at 858.

B. Section 3 of the Texas Securities Act vested the Collin County district court with jurisdiction over the criminal proceedings, and, accordingly, this court lacks jurisdiction to grant relief that would interfere with the those proceedings.

In her motion and brief, Rogers claims that she is "not asking this court to take any action, or make any ruling regarding the indictments themselves, as that action can only be taken by the Collin County District Court." Rogers Brief at 1. But the relief sought in her motion belies this representation. In fact, Rogers is requesting an order that the State "withdraw[] any and all complaints upon which the indictments are based" and that this court decide "whether Rogers' due process rights have been violated by the State, when she was asked to give up legal rights, without being informed or warned that a criminal complaint(s) were being contemplated against her." *See* Rogers Amended Motion at 4. McDermott is more direct: he requests in his motion that this Court "enjoin the TSSB from further prosecuting" him. McDermott Motion at 45. These requests for relief can only be calculated to collaterally attack, interfere with or undermine the criminal proceedings in Collin County.

But neither defendant persuasively addresses two threshold issues: (1) how exactly the State has "breached" its agreement so as to give rise to a claim to "enforce" the settlement; and (2) how, in any case, such a claim could divest the Collin County court of its jurisdiction over the criminal proceedings, or alternatively, support concurrent jurisdiction in this Travis County court *and* the Collin County court.

As to the first threshold issue, neither Rogers nor McDermott can overcome the legally dispositive language in the settlement agreements. Both agreements establish as a matter of law that criminal proceedings are not barred by the agreements. McDermott in particular has spilled considerable ink arguing that attorneys employed by the TSSB may not serve as special prosecutors in criminal proceedings. But even setting aside the question of whether his analysis is convincing, *it has nothing to do with his settlement agreement*—which plainly does not relate to or preclude criminal proceedings.

The second threshold issue is just as important—and both Rogers and McDermott fail to explain how or why this court rather than the Collin County court has jurisdiction to hear claims relating directly to the criminal proceedings.

1. The settlement agreements show as a matter of law that criminal proceedings are not barred.

Although the defendants have asserted claims in this court under the guise of enforcing their settlement agreements, those agreements show as a matter of law that they have nothing to do with criminal proceedings in Collin County—that such proceedings were not, and could not have been, released by the agreements.

Rogers' settlement includes the following:

> The State does hereby forever agree to RELEASE, ACQUIT, FOREVER DISCHARGE AND HOLD HARMLESS Wendy Rogers and her attorneys, insurers, representatives, successors and assigns, and all persons or entities in privity therewith, from any and all civil claims, demands, damages, actions, causes of actions, and suits at law or in equity, of any kind or nature, whether arising under statute or common law, whether known or unknown, that have been brought, should have been brought, *in the Pending Case*. *The State does not release or waive its right to demand additional enforcement of the laws and regulations of the State of Texas or the United States, except* with regard to those claims and causes of action, whether statutory, legal or equitable, which were, or should have been, or could have been asserted *in the Pending Case*, regarding Retirement Value or Hill Country Finding, and which occurred prior to this settlement.

See Exhibit A at 10-11 (emphasis added).

The agreement states at least twice that the only claims being released are those that could have been asserted in "the Pending Case"—that is, *this* civil lawsuit. "Pending Case" is specifically defined in the settlement agreement as Cause No. D-1-GV-10-000454, *State of Texas v. Retirement Value LLC, et al.*, in the 126th District Court of Travis County. *See* Exhibit A at 2.

McDermott's agreement contains nearly identical language. The release extends to all claims whether in law or equity "arising out [of] Retirement Value, which were or could have been asserted by [the Releasing Parties] *in the Lawsuit*." *See* Exhibit J. "Lawsuit" is expressly understood to mean this civil action. *See* Exhibit J at 2 (emphasis added).

It is fundamental that neither the Attorney General nor the Securities Commissioner had authority to bring criminal proceedings in this lawsuit. Section 32 of the Texas

Securities Act specifically describes the type of relief that can be obtained in this suit. Tex. Rev. Civ. Stat. Ann. art. 581-32 (West 2015).

Further, the duty of criminal prosecution in the trial courts resides in the county attorney and the district attorney (or criminal district attorney). *E.g.*, *Saldano v. State*, 70 S.W.3d 873, 876 (Tex. 2002). Section 3 of the Securities Act provides in pertinent part that:

> In the event of neglect or refusal of [the district or county] attorney to prosecute such violation, the Commissioner shall submit evidence to the Attorney General, who is hereby authorized to proceed therein with all rights, privileges and powers conferred by law upon district or county attorneys, including the power to appear before grand juries and interrogate witnesses before such grand juries.

It is undisputed that the Collin County DA did not refuse or neglect to prosecute the securities fraud but instead sought and obtained grand jury indictments. Thus, the conditions for the Attorney General's instituting criminal proceedings under section 3 were not present. Tex. Rev. Civ. Stat. art. 581-3. In short, it goes without saying—or should go without saying—that the State of Texas, the Attorney General, and the Securities Commissioner could not have commenced criminal proceedings in this lawsuit.

Next, the settlement agreements, and releases contained therein, say nothing about "crimes, criminal actions, prosecution, or similar concepts." *See U.S. v. Brekke*, 97 F.3d 1043, 1049 (8th Cir. 1996). In order for the settlement agreements to have precluded the Collin County indictments, they needed to specifically mention crimes, criminal actions, prosecutions, or an offer of immunity. *Id.*

In *Brekke*, the Eighth Circuit denied issue preclusion where the only fact contained in the judgment of dismissal was that the parties stipulated to the dismissal of the action. *Id.* The criminal defendants in *Brekke* had earlier settled False Claims Act civil litigation brought against them by the Small Business Administration. *Id.* The court held that the settlement's stipulation for dismissal did not establish issue preclusion in the subsequent prosecution for bank fraud arising out of the same transaction.

The court explained that any "general language is qualified by the specific language which precedes it" and because each of the claims specifically released by the parties was civil, the parties did not understand the settlement to be a non-prosecution agreement. *Id.* Thus, because the agreement did not mention "crimes, criminal actions, prosecution, or similar concepts", it did not preclude the government from prosecuting the defendants criminally. *Id.*

The defendants' breach of settlement claims are also contradicted by express language in their agreements confirming that the terms represent the *entire* agreement between the parties, and supersede any prior or contemporaneous agreements or understandings, oral or written. *See* Exhibit A at 14; Exhibit J at 16. McDermott and Rogers also expressly affirmed that they had not relied on any statement or representation other than those expressly contained in the agreements, that they each had separate counsel, and that their settlement agreements had been explained to them by their attorneys. *See* Exhibit A at 14; Exhibit J at 17.

Notwithstanding this explicit language, Rogers and McDermott now claim they entered into settlements with an understanding that they would not be prosecuted—and relied on it in executing their agreements. But it is beyond credulity to suppose—as defendants are asking this court to suppose—that in a $77.6 million securities fraud, it never occurred to these defendants or their attorneys that there existed a risk of criminal prosecution, or alternatively, that any such risk had been effectively eliminated by the settlement agreements.

Further, this very line of argument has already been rejected by the courts. In *Kalyanaram II*, the court concluded:

> Kalyanaram alleges that the University orally represented it would "abandon" its criminal charges if the parties settled. This allegation does not constitute evidence of fraud for two reasons. First, the settlement agreement expressly states that it "constitutes the entire agreement between the parties [and] shall not be varied by . . . oral representation." It also states that the parties "have each read this Agreement, and have consulted with their counsel concerning it, or have had the opportunity during a period of at least 21 days to consult with their counsel and consider the Agreement, and understand that this is a full and final release of all possible claims." Thus, Kalyanaram cannot argue that he relied on oral representations made before the agreement.

2009 WL 1423920 at *4: *Id.* (citing *Sun Oil Co. v. Madeley,* 626 S.W.2d 726, 731-32 (Tex.1981).

2. The Collin County district court cannot be divested of jurisdiction by an alleged defect in the criminal proceedings.

In addition to the dispositive language in the settlement agreements, this court does not have jurisdiction over the criminal proceedings in Collin County, and therefore it does

not have jurisdiction to grant the requested relief. Because the Texas Constitution vests the district courts with their power to hear cases, this court must first look to the Constitution's text when determining whether it has jurisdiction. Article V, section 8 of the Texas Constitution authorizes the creation of the district courts and it states:

> District Court jurisdiction consists of exclusive, appellate, and original jurisdiction of all actions, proceedings, and remedies, *except in cases where exclusive, appellate, or original jurisdiction may be conferred by this Constitution or other law on some other court, tribunal, or administrative body*.

Tex. Const. Art. V §8 (emphasis added). "It is well settled that '[a] judgment may properly be rendered against a party only if the court has authority to adjudicate the type of controversy involved in the action.'" *Dubai Petroleum Co. v. Kazi*, 12 S.W.3d 71, 74-75 (Tex. 2000) (quoting Restatement (Second) of Judgments § 11).

Although the Texas district court is a court of general jurisdiction, "where the cause of action and remedy for its enforcement are derived not from the common law but from the statute, the statutory provisions are mandatory and exclusive, and must be complied with in all respects or the action is not maintainable. *Id.* at 75.

Here, statutory law has vested the Collin County court with the jurisdictional authority to hear the contested criminal proceedings. Tex. Rev. Civ. Stat. Ann. art. 581-3 (West 2015). Section 3 of the Securities Act grants to the Securities Commissioner and the Attorney General the power to make such investigations as will detect or prevent violations of the Securities Act. Further, under section 3, the Commissioner "shall at once" lay evidence of criminality "before the District or County Attorney of the proper county."

Because the criminal activity with which Rogers and McDermott are charged occurred in Collin County, and because the Collin County DA has initiated criminal proceedings, exclusive jurisdiction has been conferred on the district court in that county. Any attempt by this court to order the TSSB to withdraw its complaint, to enjoin the criminal prosecution or to find that defendants' due process rights have been violated by the criminal proceedings, would amount to impermissible interference with the Collin County court's jurisdiction. *See Counsel Fin. Servs. L.L.C. v. Leibowitz*, 2011 WL 2652158, at *7 (Tex. App. July 1, 2011); *Scott v. Graham*, 292 S.W.2d 324, 327 (1956).

Even if the parties had had the power to enter into a non-prosecution agreement and had in fact entered into such an agreement, the agreement could not have waived a subsequent court's subject-matter jurisdiction or granted to this court subject-matter jurisdiction that it did not otherwise have. *See* U.S. Const. art. III; *United States v. Cotton*, 535 U.S. 625, 630 (2002) (finding that "subject matter jurisdiction … can never be forfeited or waived."); Id. at 598-99. As discussed above, the settling parties cannot purport to grant this court jurisdiction over the Collin County criminal proceedings unless this court already had jurisdiction over those proceedings. It did not and does not.

Finally, McDermott's argument that an attorney employed by the TSSB may not serve as a special prosecutor does not give rise to jurisdiction in this Court or divest the Collin County court of its jurisdiction. Even assuming arguendo that the TSSB attorney's prosecutorial role constituted a defect in the criminal proceedings, that defect would not be jurisdictional. Assuming *arguendo* that Collin County indictment was incorrect or

defective—due to the TSSB's role as the complaining party or Dale Barron's role as the special prosecutor—such defects would not be jurisdictional. Thus even if defendants allege that the Collin County indictment was improper, or that the TSSB employees' deputation as special prosecutors was improper, such defects would not deprive the Collin County court of its authority to hear the case under section 3 of the Texas Securities Act.[2]

C. Any information relevant to Rogers' amended motion is protected by the attorney-client privilege or by the confidentiality provisions in the Texas Securities Act.

Finally, both Rogers and McDermott request an evidentiary hearing. And Rogers has served notices of deposition on two TSSB employees in connection with her request. *See* Exhibits F and G. But the Securities Act—along with the affidavits submitted by the TSSB employees (Exhibits H and I) in support of TSSB's motion to quash—shows that the information sought is protected under Tex. Rev. Civ. Stat. Ann. art. 581–28 (Vernon 2010). It provides:

> A. Investigations by Commissioner. The Commissioner shall conduct investigations as the Commissioner considers necessary to prevent or detect the violation of this Act or a Board rule or order. For this purpose, the Commissioner may require, by subpoena or summons issued by the Commissioner, the attendance and testimony of witnesses and the production of all records, whether maintained by electronic or other means, relating to any matter which the Commissioner has authority by this Act to consider or investigate, and may sign subpoenas, administer oaths and affirmations, examine witnesses and receive evidence; provided however, that all information of every kind and nature received in connection with an investigation and all internal notes, memoranda, reports, or communications made in connection with an investigation shall be

[2] *U.S. v. Cotton*, 535 U.S. 625, 630 (2002); *and see U.S. v. Williams*, 341 U.S. 58, 66 (1951) (holding that a ruling "that the indictment is defective does not affect the jurisdiction of the trial court to determine the case presented by the indictment.").

> treated as confidential by the Commissioner and shall not be disclosed to the public except under the order of court for good cause shown ....

Section 28 protects the Commissioner's law enforcement file which includes the TSSB's internal attorney's notes, communications with investors, and witness statement notes. The broad language of this confidentiality statute clearly encompasses testimony about the Board's investigations, as well as requests for documents. Section 28 protects "all internal notes, memorandums, reports or *communications made in connection with an investigation*. . ." Absent a showing of good cause, then, the defendants may not conduct discovery regarding the Commissioner's investigation. *See Texhoma Stores, Inc. v. American Central Ins. Co.,* 424 S.W.2d 466, 472 (Tex.Civ.App.—Dallas 1968, writ ref'd n.r.e.).

There is nothing before this court showing a need for an evidentiary hearing. Quite the opposite: the settlement agreements themselves and this court's lack of subject-matter jurisdiction show that good cause is manifestly lacking.

The Texas Supreme Court has also explicitly recognized a common-law law enforcement privilege by noting: "[w]e recognized this privilege in civil litigation for law enforcement investigation." *Hobson v. Moore,* 734 S.W.2d 340, 341 (Tex.1987). In upholding the agency's position that "section 28 protects all the Commissioner's law enforcement file," the court in *Texas Attorney General's Office v. Adams,* 793 S.W.2d 771, 775-76 (Tex. App.—Fort Worth 1990), emphasized that "it is beyond dispute that the law

enforcement agencies could not function if criminal defendants could use liberal civil discovery processes to their advantage in their criminal defense."

> The legislature recognized the extent of this privilege and the abuse to which criminal defendants may put such discovery when there is a related civil suit, when it enacted in 1989 section 28 to article 581. Section 28 provides that defendants must demonstrate good cause to obtain any internal reports or law enforcement documents of the state Securities Board . . .

Id. This court should not allow McDermott and Rogers, under the guise of "enforcing" their settlement agreements, to delve into facts relating to the criminal investigation, facts they would not otherwise be entitled to in the Collin County criminal proceeding.

The good cause requirement under this section 28 operates as it does in other discovery statutes. The party seeking discovery must file a motion seeking to establish "good cause"—meaning the party has substantial need for the material and that it is unable to obtain it from any other source. *See Texhoma*, 424 S.W.2d at 472–73. The defendants have not met this burden of showing good cause—nor can they, in view of the settlement agreements themselves and the state's immunity from suit.

D. That attorneys employed at TSSB have served as special prosecutors does not amount an agency "rule."

McDermott's attorneys also argue that instances in which TSSB attorneys have served as a special prosecutor amounts to an agency "rule." But APA section 2001.038 cannot confer jurisdiction here, because the challenged agency practice is not a "rule" under the APA.

While agency rules must be adopted pursuant to proper APA procedures, the APA definition of a "rule" explicitly excludes "a statement regarding only the internal management or organization of a state agency and not affecting private rights or procedures." APA at § 2001.003(6); *Brinkley v. Texas Lottery Comm'n*, 986 S.W.2d 764, 769 (Tex. App.–Austin 1999, no pet.) (explaining that "agencies routinely issue letters, guidelines, and reports" that are not "rules" for purposes of the APA).

The agency practices here are, at most, intended to manage and direct the work of agency attorneys. As such, they do not constitute an "agency statement of general applicability." *See Tex. Mut. Ins. Co.*, 275 S.W.3d at 555. In view of the exception for statements regarding the internal management or organization of a state agency, the phrase "statement of general applicability" can refer only to persons or categories of persons *outside* the agency.

Perhaps most important, these practices do not have *in themselves* the force of law—that is, the "power to bind others"—outside the agency. They affect only those employees working within the agency.

In deciding whether an agency statement constitutes a "rule" or concerns only the agency's internal management or organization, "the core concept is that the agency statement must *in itself* have a binding effect on private parties." *Slay v. Texas Comm'n. on Envtl. Quality*, 351 S.W.2d 532, 546 (Tex. App.—Austin 2011, pet. denied) (emphasis added); *see also Texas Dep't of Public Safety v. Salazar*, 304 S.W.3d 896, 905 (Tex.

App.—Austin 2009, no pet.) ("Agency statements that 'have no legal effect on private persons are not considered rules.'") (quoting *Brinkley v. Texas Lottery Comm'n,* 986 S.W.2d 764, 770 (Tex.App.—Austin 1999, no pet.).

In *Slay* the TCEQ brought an administrative enforcement action against landowners, based on alleged inaction regarding hazardous wastes found on their property. The enforcement action proceeded to a contested-case hearing before SOAH. Following the hearing, the ALJ issued proposed findings and conclusions that the landowners had committed several regulatory violations, and recommended penalties in a specific amount. *Slay*, 351 S.W.3d at 536-37.

When the ALJ's proposal for decision came before the commission, the TCEQ executive director recommended penalties pursuant to the agency's "penalty policy," a document prepared by the enforcement division that set forth an elaborate methodology for applying the statutory criteria for imposing penalties (below, the "Penalty Policy"). *Id.* at 538. The Penalty Policy provided guidance on how the TCEQ staff was to evaluate violations for the purpose of recommending administrative penalties to the commission.

Based on the Penalty Policy, the executive director recommended penalties in the amount of $596,625—an amount in stark contrast with the $1500 penalty recommended by the ALJ, who had concluded that worksheets underlying the executive director's recommendations "contain[ed] errors, unproven assumptions, and unproven bases." *Id.* at 541. Ultimately, in its final decision, the commission modified the ALJ's recommended

penalty to reflect that, consistent with the executive director's recommendation, three of the violations had been continuing monthly violation events. But the Commission differed with the executive director on the number of months that should be used to calculate the monthly penalties for each such violation. As a result, the final agency decision imposed $177,500 in penalties on the landowners. *Id.* at 542.

The landowners brought an APA section 2001.038 claim, arguing that the TCEQ Penalty Policy was a "rule" that had not been adopted in accordance with the APA's formal rulemaking requirements. Relying on the "core concept" that "the agency statement must in itself have a binding effect on private parties," this court rejected the landowners' "rule" claim, explaining:

> There was also evidence before the district court—including the text of the Policy itself—that TCEQ staff was required to follow the Penalty Policy's methodology in determining penalty recommendations. And the executive director purported to do just that, as we have previously detailed. Moreover, the penalties ultimately imposed by the TCEQ commissioners were in amounts consistent with the violation base penalties the executive director had recommended, adjusted for differences in the multipliers used (i.e., "counting" five rather than ten months of continuing monthly violations and one rather than four violations of TCEQ rule 335.6(c)). But what ultimately matters is that the district court also had evidence to the effect that the TCEQ commissioners were not *bound* to follow the Penalty Policy's methodology when exercising their legislatively conferred discretion to impose penalties.

Id. at 546 (emphasis in original). "The introductory section of the Penalty Policy states that the Policy's purpose is to explain 'how TCEQ staff are to evaluate violations for the *purpose of recommending administrative penalties to the commission*.'" *Id.* at 546-47 (emphasis in original).

If anything, TSSB's practice is even further removed from a legally binding agency statement than the TCEQ Penalty Policy in *Slay*. *E.g.*, *Saldano v. State*, 70 S.W.3d 873, 876 (Tex. 2002); *see also* Tex. Rev. Civ. Stat. art. 581-3. TSSB offers additional assistance to the district attorney upon the referral of a case for criminal prosecution. Of course, that offer of assistance does not have the force of law or the power to bind anyone, including the district attorney. If the offer of assistance is accepted, TSSB attorneys are often deputized as special assistant district attorneys. But the powers and duties of criminal prosecution in the trial court resides in and derives from the district attorney (or criminal district attorney)—not from the TSSB's practice of offering assistance. Here, attorneys employed at TSSB who are acting as special prosecutors are exercising those powers and duties that the Collin County DA's office has conferred on them via deputization.

At the same time, the Collin County court exercises jurisdiction in this matter, because under section 3 of the Act the Securities Commissioner has "[laid] before the District or County Attorney of the proper county" evidence of criminality. The indictments of Rogers and McDermott have been handed down by a Collin County grand jury in the exercise of *its* powers and duties.

In an effort to establish agency policy having "a binding effect on private parties" as required by *Slay*, McDermott is blending the TSSB's internal policies regarding its attorneys with the powers of the grand jury, the district attorney and the criminal court in Collin County. But in order to decide whether an agency statement or practice constitutes

a "rule," it is critical to focus on what, if any, legal effect *that* practice in itself has on private parties—separate and apart from the powers and duties of the Collin County district attorney, grand jury and courts.

Finally, although McDermott is seeking to enjoin TSSB's employees from pursuing their prosecutorial roles in the Collin County court, APA section 2001.038 does not authorize injunctive relief.

WHEREFORE, PREMISES CONSIDERED, the State of Texas and TSSB request that the plea to the jurisdiction be granted and that these claims be dismissed for lack of subject-matter jurisdiction. In the alternative, and without waiving the foregoing, the State of Texas and TSSB move for summary judgment and for such other relief, legal or equitable, to which they may show themselves entitled.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on this 1st day of June, 2015, the above and foregoing plea and motion was served on the following attorneys of record via File & Serve Express and as shown below:

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