

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

<b>SECURITIES AND EXCHANGE</b>	)	
<b>COMMISSION,</b>	)	
	)	
<b>Plaintiff,</b>	)	
	)	
<b>v.</b>	)	<b>Civil Action No. 3:17-cv-420-E</b>
	)	
<b>PATRICK O. HOWARD;</b>	)	
<b>HOWARD CAPITAL HOLDINGS, LLC;</b>	)	
<b>and OPTIMAL ECONOMICS CAPITAL</b>	)	
<b>PARTNERS, LLC,</b>	)	
	)	
<b>Defendants.</b>	)	

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**RECEIVER’S UNOPPOSED MOTION TO APPROVE (I) PROPOSED SETTLEMENT  
WITH FORMER COUNSEL TO RECEIVERSHIP ENTITIES; AND (II) PAYMENT OF  
HIS SPECIAL LITIGATION COUNSEL’S FEES AND EXPENSES RELATED TO  
PROPOSED SETTLEMENT AND BRIEF IN SUPPORT**

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Receiver W. Craig Stokley (the “Receiver”) files this Unopposed Motion to Approve (I) Proposed Settlement with Former Counsel to Receivership Entities; and (II) Payment of His Special Litigation Counsel’s Fees and Expenses Related to Proposed Settlement. In support thereof, the Receiver would respectfully show the Court as follows:

### **BACKGROUND**

#### **A. Appointment of Receiver and Retention of Special Counsel**

1. On February 14, 2017, the Securities and Exchange Commission (the “SEC”) initiated these proceedings and sought the appointment of a receiver. Later that same day, the Court issued its Order Appointing Receiver,<sup>1</sup> which appointed W. Craig Stokley as the Receiver for the assets of Patrick O. Howard and certain related entities (collectively, the “Receivership Entities”).

2. Pursuant to Paragraphs 42 and 43 of the Order Appointing Receiver, the Receiver was authorized and directed to investigate potential claims that might be brought for the benefit and on behalf of the receivership estate.<sup>2</sup> Thus, on April 19, 2018, the Receiver sought authority from the Court to retain Reid Collins & Tsai LLP (“RCT”) as special litigation counsel to assist him in investigating and pursuing third-party claims under a contingency-fee arrangement.<sup>3</sup> The Court entered an order granting such authority on June 14, 2018.<sup>4</sup>

#### **B. Investigation of Potential Claims Against Former Counsel**

3. After being retained by the Receiver, RCT commenced an investigation of potential claims against former counsel for the Receivership Entities: (a) an international AmLaw 100 law

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<sup>1</sup> Docket No. 10.

<sup>2</sup> *See id.* ¶¶ 42-43.

<sup>3</sup> *See* Docket No. 109. Specifically, RCT agreed to represent the Receiver in exchange for a 33% contingency fee, and RCT further agreed to advance out-of-pocket costs and expenses incurred with respect to third-party claims.

<sup>4</sup> *See* Docket No. 115.

firm ("Law Firm A"), which represented the Receivership Entities from October 2015 to September 2016; (b) an international AmLaw 200 law firm ("Law Firm B"), which represented the Receivership Entities from October 2016 to February 2017; and (c) two individual attorneys who served as the engagement partners for the representation, first at Law Firm A and then later at Law Firm B.

4. As part of its investigation for the Receiver, RCT reviewed voluminous documents, emails, and other records. First, RCT carefully reviewed the evidence submitted by the SEC in support of these proceedings, including the transcripts of testimony taken as part of the SEC's investigation. Second, RCT reviewed hundreds of emails and other documents held by the Receivership Entities. Third, RCT requested and reviewed the client files and other documents held by Law Firm A and Law Firm B related to their representation of the Receivership Entities.

5. After reviewing these documents, RCT determined that the Receivership Entities had viable legal malpractice claims against Law Firm A, Law Firm B, and the two engagement partners related to their representation of the Receivership Entities. Specifically, these firms and their attorneys knew or should have known that the Receivership Entities were violating securities laws. Yet the attorneys failed to advise the Receivership Entities regarding their securities law violations. Had the attorneys properly advised their clients, the Receivership Entities would have heeded that advice, stopped their ongoing violations, and stopped any improper disbursement of funds.

6. To confirm its conclusions regarding the legal malpractice claims, RCT retained a prominent expert witness, Professor James C. Spindler. He is a Professor and the Hart Chair of Corporate and Securities Law at the University of Texas School of Law and a Professor at the University of Texas McCombs School of Business. After conducting his own analysis of the

underlying facts and applicable law, Professor Spindler issued a preliminary expert report, which confirmed RCT's conclusions that the Receiver had viable legal malpractice claims against Law Firm A, Law Firm B, and the two engagement partners related to their representation of the Receivership Entities.

7. As it concluded the investigation, RCT prepared a detailed 32-page draft complaint setting forth the Receiver's legal malpractice claims against Law Firm A, Law Firm B, and the two engagement partners.

**C. Mediation Regarding Potential Claims Against Former Counsel**

8. In late March 2019, the Receiver provided the draft complaint, along with an offer to engage in pre-suit mediation, to Law Firm A, Law Firm B, and the two engagement partners. After further discussions, the parties eventually agreed to participate in mediation with the Honorable Glen M. Ashworth (Ret.), a well-respected former state court judge and JAMS mediator.

9. On August 14, 2019, after exchanging more than 70 pages of mediation briefs and dozens of supporting exhibits, the Receiver, Law Firm A, Law Firm B, and the two engagement partners participated in mediation with Judge Ashworth. At mediation, the Receiver was unable to reach a resolution of the Receivership Entities' claims against Law Firm A, but the Receiver was able to reach an agreement in principle for resolving the claims against Law Firm B. Over the next several weeks after mediation, the Receiver negotiated the final details of a settlement with Law Firm B.

10. Ultimately, after extensive and arms-length negotiations, the Receiver and Law Firm B agreed to enter into a proposed settlement agreement (the "Settlement Agreement"),

which—as required by its terms—is to be filed under seal<sup>5</sup> and subject to this Court’s approval. Copies of the Settlement Agreement (with the names of Law Firm B and the two engagement partners redacted), this motion, and other supporting papers may be reviewed on the Receiver’s website (www.companysreceiver.com).

**D. Proposed Settlement of Potential Claims Against Former Counsel**

11. The items below provide a general overview of the most salient terms of the proposed Settlement Agreement:

- The Settlement Agreement is by and between the following parties (collectively, the “Parties”): (a) the Receiver in his capacity as the court-appointed receiver for the Receivership Entities; and (b) Law Firm B.
- The Settlement Agreement will be effective (the “Effective Date”) upon: (a) the Court’s entry of an order giving the Receiver the authority to execute the Settlement Agreement; and (b) the subsequent execution of the Settlement Agreement by the Parties.
- Within five (5) business days after the Effective Date, Law Firm B will pay the settlement funds described in the Settlement Agreement by wire transfer to the Receiver.
- The Parties generally agreed to full releases, although these releases do not apply to the two engagement partners or their two associates for any actions undertaken by them in some capacity other than as a partner, associate, attorney, employee, or agent of Law Firm B
- The Receiver also covenants not to sue the two engagement partners and their two associates related to the released claims or name these individuals in certain court filings. However, certain limited actions by these individuals could lead to the termination of these covenants with respect to the individual triggering the termination clause.

12. As explained below, the proposed Settlement Agreement is fair, equitable, and in the best interests of the receivership estate. The Receiver, moreover, has conferred with the SEC,

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<sup>5</sup> See Docket No. 128.

which has no objection to the proposed Settlement Agreement. Similarly, Law Firm B—along with the two engagement partners—have no objection to the proposed Settlement Agreement.

### **RELIEF REQUESTED**

#### **A. Request for Approval of Proposed Settlement Agreement**

13. The Receiver requests this Court’s approval of the proposed Settlement Agreement because such approval is required under the terms of that agreement. The Receiver has generally sought the Court’s approval for any significant transactions in this case out of an abundance of caution. It should be noted, however, that nothing in the Order Appointing Receiver explicitly requires the Court’s approval of settlement agreements. Indeed, that order authorized the Receiver “to investigate” and “compromise” a “proceeding of any kind” without prior court approval, so long as the Receiver, “in his discretion, and in consultation with SEC counsel,” deems such a compromise to “be advisable or proper to recover or conserve Receivership Property.”<sup>6</sup>

14. This Court “has broad powers and wide discretion to determine the appropriate relief in an equity receivership.”<sup>7</sup> Within such broad authority lies the Court’s power to decide whether to approve a proposed settlement agreement.<sup>8</sup> Such a decision hinges on whether this Court determines that a proposed settlement agreement is “fair and equitable and in the best interests of the estate.”<sup>9</sup> Here, the proposed Settlement Agreement is fair, equitable, and in the best interests of the receivership estate for several reasons.

15. First, the proposed Settlement Agreement yields a significant payment into the receivership estate—a payment which is not only substantial, but also represents a significant

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<sup>6</sup> Docket No. 10 ¶ 42.

<sup>7</sup> *S.E.C. v. Kaleta*, 530 F. App’x 360, 362 (5th Cir. 2013) (per curiam) (quoting *S.E.C. v. Safety Fin. Serv., Inc.*, 674 F.2d 368, 372-73 (5th Cir. 1982)).

<sup>8</sup> *See, e.g., S.E.C. v. Stanford Int’l Bank Ltd.*, 927 F.3d 830, 840 (5th Cir. 2019).

<sup>9</sup> *Id.*

portion of the total damages that the Receiver could potentially recover from Law Firm B with respect to the underlying legal malpractice claims. Law Firm B was not retained by the Receivership Entities until approximately three or four months before the SEC commenced these proceedings, and the Parties dispute the date of Law Firm B's retention. Depending on that date, total damages would range from approximately \$200,000 to \$600,000 during that period.

16. Second, the proposed Settlement Agreement also eliminates Law Firm B's approximately \$26,000 claim against the receivership estate for unpaid fees and expenses related to its representation of the Receivership Entities. This claim will be released as part of the mutual releases in the proposed Settlement Agreement.

17. Third, although the Receiver believes the Receivership Entities' legal malpractice claims against Law Firm B are meritorious and would be successful, the claims involve risk and uncertainty. Indeed, Law Firm B vigorously disputes the Receiver's claims, arguing that: (a) the scope of Law Firm B's engagement did not include securities compliance; (b) Law Firm B was not aware of any improper disbursement of funds by the Receivership Entities; (c) the Receivership Entities would not have acted any differently even if Law Firm B had rendered securities compliance advice; (d) the claims against Law Firm B are barred by the statute of limitations; and (e) the claims against Law Firm B seek unrecoverable damages due to the timing and nature of the alleged losses. The Receiver believes Law Firm B's arguments have no merit, but the Receiver acknowledges that these arguments demonstrate that litigation against Law Firm B would involve substantial risk and uncertainty.

18. Fourth, litigation against Law Firm B would be complex, lengthy, and expensive. As reflected above, the litigation would involve difficult and hotly contested issues. Many of these issues would require costly expert analysis and testimony. These issues would also require costly

depositions and discovery from other witnesses. Such costs, though advanced by RCT under its contingency-fee engagement, would ultimately need to be reimbursed by the Receiver from any recovery on his claims against Law Firm B.

19. Finally, the proposed Settlement Agreement is the product of arms-length and good-faith negotiations between the Parties, with the assistance of a well-respected former judge (Judge Ashworth) serving as the mediator. The SEC, moreover, has no objection to the proposed Settlement Agreement.

20. In sum, the proposed Settlement Agreement is fair, equitable, and in the best interests of the receivership estate. The Receiver therefore requests that the Court approve the proposed Settlement Agreement.

**B. Request for Approval of Special Counsel's Fees and Expenses**

21. The Receiver also requests that the Court approve payment of his special counsel's fees and expenses related to the proposed Settlement Agreement. The Receiver retained RCT as his special litigation counsel under the following contingency-fee arrangement:

- In exchange for its services, RCT will be paid a contingency fee equal to 33% of Gross Recoveries obtained by the Receiver and the receivership estate with respect to third-party claims.<sup>10</sup>
- RCT will advance out-of-pocket costs and expenses incurred with respect to the third-party claims, but RCT will be reimbursed by the Receiver for such costs and expenses out of any Gross Recoveries obtained with respect to third-party claims.
- If no Gross Recoveries are obtained with respect to third-party claims, RCT will not be paid any contingency fee and shall not be reimbursed for any out-of-pocket expenses incurred with respect to third-party claims.<sup>11</sup>

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<sup>10</sup> "Gross Recoveries" means the fair value of all monetary and non-monetary consideration obtained by the Receiver and the receivership estate in connection with any settlement, judgment, award, or other recovery related to the third-party claims.

<sup>11</sup> See Docket No. 109 ¶ 3 & Ex. A.

The Receiver retained RCT on an contingency-fee basis because of: (a) the limited funds in the receivership estate to pursue the third-party claims on an hourly fee basis; and (b) the inherent risks of any litigation involving the third-party claims.<sup>12</sup> The Court approved the Receiver's retention of RCT under this contingency-fee agreement.<sup>13</sup>

22. Pursuant to this court-approved agreement, the Receiver seeks authority to pay RCT's contingency fee and to reimburse RCT's out-of-pocket expenses related to the proposed Settlement Agreement. Specifically, the Receiver seeks authority to pay a contingency fee of 33% of the settlement amount and to reimburse \$55,445.09 in out-of-pocket expenses.<sup>14</sup>

23. Courts use different methods to determine whether a contingency fee is reasonable. One is the percentage method, where the court awards a fee based on a percentage of the common fund.<sup>15</sup> Another method involves a multi-factor test set forth in *Johnson v. Georgia Highway Express, Inc.*, 488 F.2d 714 (5th Cir. 1974).<sup>16</sup> Both methods demonstrate that the proposed contingency fee in this case is reasonable.

24. The proposed contingency fee is reasonable under the percentage method. Courts in the Fifth Circuit often award contingency fees of 30% or more of the total recovery.<sup>17</sup> Indeed, "the typical market rate" is 33% to 40% for a complex securities-related case.<sup>18</sup> Accordingly, the proposed 33% contingency fee is reasonable under the percentage method.

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<sup>12</sup> See *id.* ¶ 5.

<sup>13</sup> See Docket No. 115.

<sup>14</sup> More than \$51,000 of these expenses were incurred in relation to the Receiver's expert witness, Professor Spindler, who provided necessary analysis and a preliminary expert report supporting the underlying claims.

<sup>15</sup> See *S.E.C. v. Stanford Int'l Bank, Ltd.*, No. 3:09-cv-00298-N, 2018 WL 1558266, at \*1 (N.D. Tex. Mar. 26, 2018).

<sup>16</sup> See *Stanford*, 2018 WL 1558266, at \*1.

<sup>17</sup> See *id.* at \*2.

<sup>18</sup> *Id.* at \*3.

25. The proposed contingency fee is also reasonable under the *Johnson* factors. These factors include: (a) time and labor required; (b) novelty and difficulty of the issues; (c) required skill; (d) whether other employment is precluded; (e) the customary fee; (f) whether the fee is fixed or contingent; (g) time limitations; (h) amount involved and results obtained; (i) attorney's experience, reputation, and ability; (j) "undesirability" of the case; (k) nature and length of the professional relationship with the client; and (l) awards in similar cases.<sup>19</sup> As explained below, these factors weigh in favor of approving RCT's contingency fee:

- Time and Labor Required: This case required substantial time and effort. Over the past 18 months, RCT has spent more than 500 hours of attorney time investigating and pursuing the underlying claims. RCT's efforts included: (i) gathering and reviewing documents; (ii) researching and drafting a detailed complaint; (iii) identifying, retaining, and consulting with a prominent expert witness; (iv) preparing extensive mediation briefing; and (v) participating in mediation and extended settlement discussions.
- Novelty and Difficulty of Issues: This case involved complex factual and legal issues. As explained above, Law Firm B asserted several challenging defenses to the Receiver's claims.
- Skill Required: Given the complexity of these factual and legal issues, this case required significant skill and effort on RCT's part.
- Preclusion of Other Employment: Although this case did not necessarily preclude RCT from accepting other employment, the sheer amount of time and effort required by this case, as reflected by the hours invested, reduced RCT's ability to devote time and effort to other matters.
- Customary Fee: The proposed fee is similar to the customary fee for comparable cases. The "typical market rate" is a 33% to 40% contingency fee for a complex securities-related case.<sup>20</sup>

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<sup>19</sup> The *Johnson* factors include: (a) time and labor required; (b) novelty and difficult of the issues; (c) required skill; (d) whether other employment is precluded; (e) the customary fee; (f) whether the fee is fixed or contingent; (g) time limitations; (h) the amount involved and the results obtained; (i) the attorney's experience, reputation, and ability; (j) the "undesirability" of the case; (k) the nature and length of the professional relationship with the client; and (l) awards in similar cases. See *Johnson*, 488 F.2d at 717-19.

<sup>20</sup> *Stanford*, 2018 WL 1558266, at \*3.

- Whether Fee Is Fixed or Contingent: The proposed fee was contingent upon obtaining a recovery from Law Firm B. As a result, RCT bore significant risk in accepting the engagement.
- Time Limitations: The engagement involved some time limitations. The receivership action had been pending for over a year when RCT was retained. RCT therefore felt compelled to act quickly on behalf of the receivership estate. Had RCT not obtained the proposed Settlement Agreement, it likely would have taken another year or more to resolve the Receiver's claims against Law Firm B.
- Amount Involved and Results Obtained: The proposed Settlement Agreement results in a significant payment to the receivership estate—a payment which is not only substantial, but also represents a significant portion of the total damages that the Receiver could potentially recover from Law Firm B with respect to the underlying legal malpractice claims.
- Attorney's Experience, Reputation, and Ability: RCT and its attorneys have significant experience in representing receivers, bankruptcy trustees, and other court-appointed fiduciaries in pursuing third-party claims.
- Undesirability of Case: This case involves legal malpractice claims. Many attorneys refuse to, or express reluctance to, handle legal malpractice claims against other attorneys. Such claims generate some level of stigma within the legal community, which can result in fewer referrals of new matters.
- Nature and Length of Professional Relationship: RCT has not represented the Receiver in other matters, but RCT has represented the Receiver since early 2018 in this matter and will continue to do so with respect to the Receiver's claims against Law Firm A.
- Awards in Similar Cases: The proposed fee is comparable to awards in similar cases. Courts often award contingency fees of 30% or more of the total recovery.<sup>21</sup> Indeed, "the typical market rate" is 33% to 40% for a complex securities-related case.<sup>22</sup>

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<sup>21</sup> See *id.* at \*2-3.

<sup>22</sup> *Id.* at \*3.

26. In sum, the proposed contingency fee is reasonable under the percentage method and the *Johnson* factors. RCT's contingency fee and out-of-pocket expenses should be approved and paid from the proceeds of the proposed Settlement Agreement.

WHEREFORE, the Receiver respectfully requests that the Court: (a) approve the proposed Settlement Agreement with Law Firm B; and (b) approve the payment of RCT's contingency fee and out-of-pocket expenses from the proceeds of the proposed Settlement Agreement.

Dated: November 19, 2019.

Respectfully submitted,

/s/ Eric D. Madden

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**CERTIFICATE OF CONFERENCE**

On November 18, 2019, I conferred with Timothy S. McCole, counsel for the U.S. Securities and Exchange Commission (the “SEC”), regarding the relief requested in this motion. Mr. McCole indicated that the SEC does not oppose this motion.

*/s/ Eric D. Madden*

Eric D. Madden

**CERTIFICATE OF SERVICE**

On November 19, 2019, I electronically filed the foregoing motion via the Court’s CM/ECF filing system, which will send a notice of electronic filing to all CM/ECF participants. I further certify that I served a true and correct copy of the foregoing motion and the notice of electronic filing via UPS and electronic mail on all non-CM/ECF parties and/or their counsel.

*/s/ Eric D. Madden*

Eric D. Madden