

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

NAZARETH NAT'L BANK & TRUST CO. : CIVIL ACTION
:
v. :
:
E.A. INTERNATIONAL TRUST, :
E.A. INTERNATIONAL, INC., :
STEVEN STACKPOLE and :
GAVIN GREENE : NO. 98-6163

M E M O R A N D U M

WALDMAN, J.

July 26, 1999

Plaintiff has asserted a securities fraud claim against defendants pursuant to section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j, and Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5. Plaintiff has also asserted supplemental state-law claims against defendants for breach of fiduciary duty, common-law fraud, conversion and for an accounting. Presently before the court is plaintiff's motion for entry of default judgment against defendants E.A. International Trust (EAIT), E.A. International, Inc. (EAI) and Steven Stackpole.

The pertinent facts as alleged by plaintiff are as follow. Plaintiff is a trustee of pre-need funeral trusts. A pre-need funeral trust is an arrangement under which an individual contracts with a funeral director for advance purchase of funeral services. Pennsylvania law requires the funeral directors to place the funds in a Pennsylvania financial institution which acts as trustee for the management and

investment of the funds. In 1996 and 1997, plaintiff invested more than \$4 million in so-called "Private Placement Annuity Contracts" issued by EAIT and EAII. EAIT is a trust and a division of EAII. Mr. Greene is the trustee of EAIT and an officer of EAII. Mr. Stackpole is a former trustee of EAIT and an officer of EAII. He is currently incarcerated in Mid-State Prison in New Jersey. Mr. Greene and Mr. Stackpole solicited plaintiff's investment in the "Annuity Contracts" which purported to guarantee returns of 6 to 11 percent per year after a five-year period, in addition to return of the invested principal.

The annuity contracts were part of a "pyramid" or "Ponzi" scheme by which Mr. Stackpole and Mr. Greene secretly paid at least 58 percent of the invested principal to themselves and others to cover purported "fees and expenses." The funds actually invested have so depreciated in value that less than \$600,000 is actually available to pay the more than \$4 million plus interest EAII and EAIT are obligated to pay plaintiff. The New Jersey Attorney General's Office, a grand jury in the Middle District of Pennsylvania and the Pennsylvania Securities Commission are investigating defendants' actions relating to the annuity contracts.

Plaintiff originally filed its complaint in the Southern District of New York on June 30, 1998. On July 27, 1998, the summons and complaint were served on EAII and EAIT by

leaving copies with the person in charge at EAIT and EAIT's registered address for service of process. Also on July 27, 1998, plaintiff served another copy of the summons and complaint on Mr. Stackpole by leaving it, at Mr. Stackpole's direction, with the security guard in charge of Mr. Stackpole's place of residence in New Jersey.

EAIT, EAIT and Mr. Stackpole have all failed to appear, answer or otherwise defend in this action. On October 7, 1998, the Clerk for the Southern District of New York entered a default against EAIT, EAIT and Mr. Stackpole. By agreement of counsel, Mr. Greene was given additional time to respond to the claims asserted against him. Plaintiff states that on October 17, 1998 it moved for the entry of a default judgment against EAIT, EAIT and that none of the defaulting defendants responded to the motion.¹

Plaintiff and Mr. Greene subsequently agreed jointly to request that the case be transferred to this district, and on November 13, 1998 the case was transferred here pursuant to 28 U.S.C. § 1404(a). The case was assigned to a judge of this

¹ The Southern District docket report which was transmitted to this court does not reflect that such a motion was filed and the file does not contain the motion. Plaintiff, however, clearly did obtain a certificate of default from the Southern District Clerk pursuant to Southern District L. R. Civ. P. 55.1 and 55.2 against EAIT, EAIT and Mr. Stackpole, and also filed a document captioned "Supplemental Affidavit for Judgment By Default."

court, and later reassigned to this judge. On December 4, 1998, Mr. Stackpole pled guilty to various criminal charges in a New Jersey state court and was thereafter incarcerated.

On May 21, 1999, plaintiff filed a motion in this court for default judgment against EAII, EAIT and Mr. Stackpole. EAII and EAIT were served with copies of the motion at their registered address in New Jersey and at their new place of business, which is also in New Jersey. Mr. Stackpole was served with a copy of the instant motion consistent with New Jersey prison regulations.

Although a plaintiff requesting the entry of a default judgment typically has obtained the entry of a default from the clerk of the same court, the clerk's entry of default is largely a formality. Pinaud v. County of Suffolk, 52 F.3d 1139, 1152 n.11 (2d Cir. 1995). There is no apparent reason why a default judgment cannot appropriately be entered following the entry of default by the Clerk of another district court which was part of the official court record and case file at the time of a § 1404(a) transfer.²

Personal jurisdiction, including valid service of process, is a prerequisite for a valid default judgment. See,

² It appears that the Clerk of this court advised plaintiff in writing that the entry of default was as much a part of the official record and case file upon transfer as any other docket entry, and that there was no need to reapply.

e.g., In Re Tuli, 172 F.3d 707, 712 (9th Cir. 1999) ("judgment entered without personal jurisdiction over parties is void" and thus "a court should determine whether it has the power, i.e., the jurisdiction, to enter the judgment in the first place"); Rogers v. Hartford Life & Accident Ins. Co., 167 F.3d 933, 940 (5th Cir. 1999) (when court lacks personal jurisdiction because of improper service any default judgment is void); Dennis Garberg & Assocs. v. Pack-Tech International Corp., 115 F.3d 767, 771 (10th Cir. 1997) (court obligated to ensure it has personal jurisdiction over defendant before entering default judgment).

Fed. R. Civ. P. 4(e)(2) authorizes service of process on an individual by leaving a copy of the summons and complaint with a person of suitable age and discretion at the defendant's dwelling house or usual abode, or with an agent authorized to receive service of process. Plaintiff's return of service for Mr. Stackpole indicates that a copy of the summons and complaint were left with a specified security guard at defendant's residence who was "instructed by R. Steven Stackpole to accept service." Mr. Stackpole was served with process consistent with Fed. R. Civ. P. 4(e)(2).

Fed. R. Civ. P. 4(h)(1) provides that service of process on a corporate defendant is adequate if done in accordance with the laws of the state in which service is effected. New Jersey law authorizes service of process on a

corporation by leaving a copy of the summons and complaint with "a person at the registered office of the corporation in charge thereof." Copies of the summons and complaint were left with the person in charge at the address registered by EAII and EAIT for service of process in New Jersey. The return of service indicates that such person accepted service on behalf of EAII and EAIT. As to EAII, which is a corporation, this was sufficient service under New Jersey law and thus also satisfies the requirements of Fed. R. Civ. P. 4(h)(1).

Plaintiff does not aver that EAIT is a corporation and it appears from the copy of the trust agreement submitted in support of the instant motion that EAIT is not a corporation. See, e.g., Soveral v. Franklin Trust, 1991 WL 160339, *2 (D.N.J. Aug. 12, 1991) ("A trust is an unincorporated association"). Fed. R. Civ. P. 4(h)(1) authorizes service of process on an unincorporated association by leaving a copy of the summons and complaint with an agent authorized to receive service. The person in charge at EAIT's registered address for service of process accepted service, and it appears that service of process as to EAIT was also proper.

Whether a court has personal jurisdiction over a citizen of another state depends upon whether the forum state's long-arm statute authorizes an exercise of jurisdiction and whether "the defendant has purposefully directed its activities

toward the residents of the forum state, or otherwise purposefully avail[ed] itself of the privilege of conducting activities within the forum State," such that requiring it to defend in the forum would not violate due process. IMO Industries, Inc. v. Kiekert AG, 155 F.3d 254, 259 (3d Cir. 1998). Pennsylvania's long-arm statute authorizes the exercise of personal jurisdiction over out-of-state defendants to the full extent permitted by the Constitution. See 42 Pa. C.S.A. § 5322(b); Pennzoil Products Co. v. Colelli & Assocs., Inc., 149 F.3d 197, 200 (3d Cir. 1998); John Hancock Property & Cas. Co. v. Hanover Ins. Co., 859 F. Supp. 165, 168 (E.D. Pa. 1994).

Plaintiff essentially asserts that defendants defrauded it by accepting plaintiff's funds for "investment" while concealing their actual intention to divert the funds to the use of Messrs. Greene and Stackpole and others. Plaintiff avers that the claims asserted arise from defendants' transaction of business in New York and from their transaction of business in Pennsylvania where they marketed Private Placement Annuity Contracts by correspondence and telephone and in personal meetings to plaintiff and various Pennsylvania funeral directors for whom plaintiff serves as trustee. Such active solicitation in Pennsylvania of a Pennsylvania citizen successfully to establish an ongoing relationship with continuing obligations constitutes sufficient minimum contacts to support an exercise of

personal jurisdiction in an action arising from and related to those contacts. See Mellon Bank (East) PSFS Nat'l. Assoc. v. Farino, 960 F.2d 1217, 1225-26 (3d Cir. 1992). Moreover, personal jurisdiction in this case may be predicated on national contacts.

Section 27 of the Securities Exchange Act of 1934 provides for nationwide service of process. See 15 U.S.C. § 78aa. Many courts have held that this provision enables any federal district court to exercise personal jurisdiction in a case arising under Rule 10b-5 over any defendant who has the requisite minimum contacts with the United States. See United States Securities and Exchange Commission v. Carillo, 115 F.3d 1540, 1543 (11th Cir. 1997); Application to Enforce Administrative Subpoena Duces Tecum of the SEC, 87 F.3d 413, 417 (10th Cir. 1996); Busch v. Buchman, Buchman & O'Brien, 11 F.3d 1255, 1258 (5th Cir. 1994); United Liberty Life Ins. Co. v. Ryan, 985 F.2d 1320, 1329 (6th Cir. 1993); Securities Investor Protection Corp. v. Vigman, 764 F.2d 1309-1315-16 (9th Cir. 1985); SEC v. Unifund SAL, 910 F.2d 1028, 1033 (2d Cir. 1990); Fitzsimmons v. Barton, 589 F.2d 330, 332-33 (7th Cir. 1979); FS Photo, Inc. v. Picturevision, Inc., --- F. Supp. 2d ---, 1999 WL 301227, *2 (D. Del. Apr. 23, 1999) ("so long as the defendant has minimum contacts with the United States, Section 27 of the Exchange Act confers personal jurisdiction over the defendant in

any federal court"); SEC v. Euro Security Fund, 1999 WL 76801, *2 & n.1 (S.D.N.Y. Feb. 17, 1999); Ogilvie v. Beale, 1993 WL 408365, *3 (N.D. Ill. Oct. 8, 1993) ("Presence in the United States is sufficient"); Alco Standard Corp. v. Benalal, 345 F. Supp. 14, 25 (E.D. Pa. 1972). EAIT, EAIT and Mr. Stackpole clearly all have requisite minimum national contacts from which plaintiff's claims arise. If plaintiff has asserted a cognizable Rule 10b-5 claim, the court may also exercise pendent personal jurisdiction on a national-contacts theory as to plaintiff's state-law claims. See F.S. Photo, 1999 WL 301227, *3; Ogilvie, 1993 WL 408365, *3.³

The elements of a Rule 10b-5 securities fraud claim are a misrepresentation or omission of material fact made by defendant with scienter in connection with the purchase or sale of securities, upon which plaintiff justifiably relied, and from

³ It is not entirely clear that venue lies in this district under 28 U.S.C. § 1391 or 15 U.S.C. § 78aa, although a fair reading of plaintiff's averments suggests it does. See, e.g., Busch, 11 F.3d at 1256-57 (personal jurisdiction and venue proper in Texas as to New York law firm which drafted opinion in New York it knew would be included in prospectus and on which Texas investor relied in purchasing securities). In any event, the burden is on the defendants to demonstrate that venue is improper and they clearly have not done so. See Myers v. American Dental Ass'n., 695 F.2d 716, 724-25 (3d Cir. 1982), cert. denied, 462 U.S. 1106 (1983). Moreover, any defects in venue are waived by defendants who default. See, e.g., Hoffman v. Blaski, 363 U.S. 335, 343 (1960) ("A defendant, properly served with process by a court having subject matter jurisdiction, waives venue by failing seasonably to assert it, or even simply by making default"); Rogers, 167 F.3d 942 ("a defendant in default waives any objection to venue"); Williams v. Life Sav. & Loan, 802 F.2d 1200, 1202 (10th Cir. 1986) (default judgment cannot be collaterally attacked for lack of venue).

which damage resulted. See Newton v. Merrill, Lynch, Pierce Fenner & Smith, 135 F.3d 266, 269 (3d Cir.) (en banc), cert. denied sub nom Merrill, Lynch, Pierce Fenner & Smith v. Kravitz, 119 S. Ct. 44 (1998).

The "Private Placement Annuity Contracts" defendants sold to plaintiff clearly appear to be "investment contracts" within the scope of § 10(b) and Rule 10b-5. See SEC v. W.J. Howey Co., 328 U.S. 293, 298-99 (1946) ("investment contract" for purposes of 1933 Act means a "contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party"); Pollack v. Laidlaw Holdings, Inc., 27 F.3d 808, 811 (2d Cir.) (noting that while the definition of "securities" in the 1933 Act and 1934 Act "are not identical, the definitions are treated as identical in decisions dealing with the scope of the term"), cert. denied, 513 U.S. 963 (1994); Goodwin v. Elkins & Co., 730 F.2d 99, 102 n.5 (3d Cir.) (per Garth, J.) (noting that while Howey interpreted the definition of "security" under 1933 Act "it has been consistently held that this definition is essentially the same as that contained in the Securities Exchange Act of 1934"), cert. denied, 469 U.S. 831 (1984). A claim that defendants represented to plaintiff that they would invest funds and provide a specified annual return on which plaintiff relied in investing funds with defendants, with an intent to divert the

funds to defendants' own use, states a Rule 10b-5 claim. See Webster v. Omnitrition Intern., Inc., 79 F.3d 776, 785 (9th Cir.), cert. denied, 519 U.S. 865 (1996); SEC v. The Better Life Club of America, Inc., 995 F. Supp. 167, 176-77 (D.D.C. 1998) (pyramid scheme operator's misrepresentation as to destination of investor funds violates Rule 10b-5), aff'd, 1999 WL 236885 (D.C. Cir. Mar. 24, 1999).

A default judgment ordinarily is entered only when the plaintiff has stated a cognizable claim and only for relief to which he would be entitled from his pleadings. See, e.g., Wagstaff-El v. Carlton Press Co., 913 F.2d 56, 57 (2d Cir. 1990), cert. denied, 499 U.S. 929 (1991); Alan Neuman Productions, Inc. v. Albright, 862 F.2d 1388, 1392 (9th Cir. 1988), cert. denied, 493 U.S. 858 (1989); Patray v. Northwest Pub. Inc., 931 F. Supp. 865, 869 (S.D. Ga. 1996); Morales v. Farley, 1996 WL 698027, *4 (N.D. Ill. Oct. 30, 1996) (citing cases). Plaintiff has also asserted cognizable state-law claims.

The elements of a claim for breach of fiduciary duty are a negligent or intentional failure by a defendant to act in good faith and solely for the benefit of the plaintiff in all matters for which he had a duty to do so and a showing that such failure was a real factor in causing injury to plaintiff. See McDermott v. Party City Corp., 11 F. Supp. 2d 612, 626 n.18 (E.D. Pa. 1998). Plaintiff's averment that defendants intentionally

diverted funds entrusted to them states a cognizable claim for breach of fiduciary duty.

The elements of a fraud claim are a misrepresentation, an intention by the maker that the recipient will thereby be induced to act, justifiable reliance by the recipient upon the misrepresentation and damage to the recipient as the proximate result. See, e.g., Permenter v. Crown Cork & Seal Co., Inc., 38 F. Supp. 2d 372, 381-82 (E.D. Pa. 1999). Plaintiff's averments that defendants misrepresented that they would invest plaintiff's funds for its benefit with an intent to induce plaintiff to invest funds with defendants as a consequence, that plaintiff justifiably relied on the misrepresentation and suffered damages as a result states a cognizable fraud claim.

The elements of the tort of conversion are the deprivation of another's right in, or use or possession of, property, without the owner's consent and without lawful justification. Shonberger v. Oswell, 530 A.2d 112, 114 (Pa. Super. 1987); Environ Products, Inc. v. Furon Co., Inc., 1998 WL 961367, *2 (E.D. Pa. Dec. 15, 1998). Conversion occurs when property is delivered to another voluntarily for a specific purpose but is then used for an unauthorized purpose and not returned. See, e.g., Royal Ins. Co. (UK) Ltd. v. Ideal Mut. Ins. Co., 649 F. Supp. 130, 137 (E.D. Pa.) (collecting cases), aff'd, 806 F.2d 254 (3d Cir. 1986). Plaintiff's averments that it

entrusted funds to defendants for the purpose of investment and that they then diverted and dissipated the funds for an unauthorized purpose states a cognizable claim for conversion.

EAIT, EAIT and Mr. Stackpole were properly served with process in this case nearly a year ago and have failed to respond to the complaint or participate in any way in the litigation of this case. Their failure to do so can only be viewed as willful and intentional. Plaintiffs have stated a cognizable Rule 10b-5 claim and cognizable supplemental state-law claims. Plaintiff's motion will be granted. An appropriate order will be entered.

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E.A. INTERNATIONAL TRUST, :
E.A. INTERNATIONAL, INC., :
STEVEN STACKPOLE and :
GAVIN GREENE : NO. 98-6163

O R D E R

AND NOW, this day of July, 1999, upon
consideration of plaintiff's Motion for Judgment by Default
Against E.A. International Trust, E.A. International, Inc. and
Steven Stackpole (Doc. #5), consistent with the accompanying
memorandum, **IT IS HEREBY ORDERED** that said Motion is **GRANTED** in
that judgment is entered against defendants E.A. International
Trust, E.A. International, Inc. and Steven Stackpole as to
liability on plaintiff's claims in this action and damages will
be determined at the time of trial on the parallel claims against
defendant Greene.

BY THE COURT:

JAY C. WALDMAN, J.