

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

SECURITIES AND EXCHANGE
COMMISSION,

Plaintiff,

v.

JOHN GARDNER BLACK, DEVON
CAPITAL MANAGEMENT, INC., and
FINANCIAL MANAGEMENT
SCIENCES, INC.,

Defendants.

Civil Action No.: 97-CV-265-J

**MEMORANDUM IN SUPPORT OF MOTION TO
INTERVENE OF TYRONE AREA SCHOOL DISTRICT**

I. INTRODUCTION

On October 8, 1997, Tyrone Area School District ("Tyrone") filed a Motion to Intervene ("Tyrone's Motion"), pursuant to F.R.Civ.P. 24. On October 7, 1997, this Court entered its Memorandum Order denying the motion to intervene filed by Richland School District ("Richland"). The Court denied Richland's motion without prejudice, and recognized that intervention might be appropriate at some later stage in the proceedings.

As a general matter, Tyrone believes that intervention is warranted now. As discussed below, there are immediate issues regarding the timing and manner in which funds may be distributed to claimants. Plaintiffs' interests are very different from those of various claimants, and it makes sense to have claimants involved in this case now, working with plaintiffs, rather than challenging plaintiffs' actions after the fact.

More specifically, there are several reasons why the Court should grant Tyrone's Motion now. Tyrone's unique claim gives it a right to intervene under Rule 24(a). The nature of this litigation also warrants permissive intervention by Tyrone under Rule 24(b). Alternatively, to the extent the Court is concerned that Tyrone's intervention could unduly complicate this litigation, the Court may grant Tyrone's Motion on a limited basis. Finally, consistent with the Court's suggestion, Tyrone may be permitted to intervene as a representative claimant.

II. ARGUMENT

A. Intervention as of Right

Intervention as of right is governed by F.R.Civ.P. 24(a). Applying this rule, the Court concluded that Richland's application was timely; that Richland had a sufficient interest in the litigation; and that, because Richland might not receive all of the proceeds to which it claims to be entitled, its interest might be affected or impaired by the disposition of this action. Memorandum Order at 3. The Court nonetheless denied Richland's motion because it "failed to demonstrate that its interest is not adequately represented either by the SEC or the appointed trustee." Id. The Court explained that the existing plaintiffs were diligently preparing an accounting of the invested funds. Id.¹

The positions of Tyrone and Richland differ in several critical respects. Tyrone also filed a timely motion to intervene, showing a sufficient interest in the litigation, which interest might be affected or impaired by the disposition of this action. See, Tyrone's Motion at 4 (citing Mountain Top Condominium Assn. v. Dave Stabbert Master Builder, Inc., 72 F.3d 361 (3d Cir. 1995)). Tyrone, however, in addition to holding the largest claim of any school district, has the most immediate need for access to its funds.

As explained in Tyrone's Motion, defendants hold virtually all of Tyrone's funds, including its general operating fund and funds needed for ongoing major construction projects. Tyrone's Motion at 3. Tyrone has an immediate

¹ The Court subsequently denied several other motions to intervene on the same basis.

concern as to its ability to continue classes. Id. On the basis of news reports regarding Tyrone's situation, the contractor responsible for construction of Tyrone's new elementary school cancelled delivery of materials and equipment. (A copy of this letter is attached as Exhibit A.) Although the Trustee acknowledged Tyrone's "precarious position," the Trustee nonetheless stated that he did not anticipate seeking any distributions to school district creditors in the near future. Tyrone's Motion at 2. Because Tyrone's need to pursue an immediate distribution will not be satisfied by any investigation or accounting, Tyrone's interest is not adequately represented by existing parties.

Intervention also is warranted because plaintiffs are charged by law only with protecting claimants' collective interests. The interests of individual claimants may be very different from the collective interest, and plaintiffs are not charged with representing Tyrone's particular interest in expediting and maximizing its recovery. Indeed, far from protecting Tyrone's interest in assuring that all districts are treated equally, the Trustee has stated that he may propose preferential treatment of some districts. Tyrone's Motion at 2. Because the different claimants have divergent interests, any presumption that Tyrone's interest will be protected by the government has been rebutted in this case. See, Mountain Top, supra, at 368-69 (creditor has right to intervene to protect its particular interest in a discrete fund). Only by intervening can Tyrone protect its interests adequately.

Tyrone's position is almost identical to that of a creditor (Greyhound) seeking to intervene in Securities and Exchange Commission v. Flight Transportation Corp., 699 F.2d 943 (8th Cir. 1983). In Flight Transportation, the court rejected the argument that there is no intervention as a matter of right in SEC actions and reversed the denial of intervention. Starting with the observation that Greyhound had no real source of repayment other than the property held by a court-appointed receiver, the court in Flight Transportation found that Greyhound's ability to protect its interest could be impaired if it were not permitted to intervene. On the issue of adequate representation, the court wrote:

Finally, Greyhound has met the "minimal" burden of showing that its interests may not be adequately represented by existing parties. The SEC's primary goal is to protect the public by preventing further securities violations. The receiver is concerned with marshaling and protecting FTC's assets for the benefit of all concerned parties. While Greyhound's interests

may not be adverse to those of the SEC or the receiver, they are sufficiently "disparate" to warrant intervention.

Id. at 948 (citations omitted).

Similarly, in Securities and Exchange Commission v. Navin, 166 F.R.D. 435 (N.D. Cal. 1995), the court permitted a creditor (Wozniak) to intervene over the objection of the SEC. The SEC argued that creditors' distinct and separate claims could be raised after the court-appointed receiver filed its proposal for distribution of assets. The court rejected this argument on the basis that Wozniak sought remedies different from those sought by plaintiffs, and that Wozniak's interests might be foreclosed absent intervention. The court concluded that Wozniak's interests were not represented adequately because it was clear the SEC would not make all of the arguments that the intervenor would, and that the intervenor would offer "a necessary element to the proceedings that the other parties would neglect." Id. at 441.

Tyrone's case for intervention is no less compelling than that of the creditors in Flight Transportation and Navin. The SEC and the trustee are charged with preventing further securities violations, and marshaling and protecting assets for the benefit of all claimants. They will not advocate Tyrone's individual interests. Plaintiffs will not make all of the arguments that Tyrone would, and Tyrone will add a "necessary element" that plaintiffs would neglect. On the facts of this case, Tyrone's interests are sufficiently "disparate" to warrant intervention. See also, Brody v. Spang, 957 F.2d 1108 (3d Cir. 1992) (divergence of interests with regard to remedies supports a right to intervention).²

Consistent with the decisions in Flight Transportation and Navin, the opinion in Hoots v. Pennsylvania, 672 F.2d 1133, 1135 (3d Cir. 1981), explained that a party could meet its burden of showing its interests were not represented adequately by (a) establishing collusion among existing parties, (b) demonstrating

² Brody involved a constitutional challenge to religious benedictions as part of high school graduation ceremonies. The court there held that divergence of interests would not warrant intervention until the case reached the "remedial phase." 957 F.2d at 1123. In the present case, in which Tyrone and other districts may seek interim distributions on an immediate basis, the "remedial phase" is proceeding concurrently with prosecution of claims against the defendants.

"that its interests, though similar to those of an existing party, are nevertheless sufficiently different that the representative cannot give the applicant's interests proper attention," or (c) giving "an indication that the representative has not been diligent in prosecuting the litigation." In the present case, there is no suggestion of collusion. On the second point, however, although plaintiffs and Tyrone have a common interest in safeguarding assets, Tyrone's particular interests are "sufficiently different" that plaintiffs cannot give them proper attention." See also, United States v. Alcan Aluminum, Inc., 25 F.3d 1174, 1185, n. 15 (3rd Cir. 1994) ("[W]here, as here, neither party represents the applicant's interests and the existing parties contest intervention it cannot be said that the applicant's interests are being diligently prosecuted."). This alone establishes Tyrone's right to intervene.³

On the basis of the facts set forth in Tyrone's Motion, as verified by the Affidavit of Cathy L. Peachey, and the arguments set forth above, Tyrone has met its minimal burden of proving its right to intervene. See Memorandum Order at 3; see also, Mountain Top, supra, at 368. ("As the Supreme Court stated, '[t]he requirement of [Rule 24(a)] is satisfied if the applicant shows that representation of his interest 'may be' inadequate; and the burden of making that showing should be treated as minimal.'").

B. Permissive Intervention

Tyrone's Motion also seeks permission to intervene pursuant to F.R.Civ.P. 24(b). The Court denied Richland's motion for permissive intervention on the basis that Richland's intervention would "unduly complicate this litigation and delay its prompt resolution." Memorandum Order at 4. The Court further

³ On the third point, Tyrone has no indication that plaintiffs are not proceeding diligently. Tyrone is concerned, nonetheless, that plaintiffs not miss any opportunity to increase the assets available for distribution. In a letter delivered to the Trustee's counsel on October 3, 1997, Tyrone's counsel asked whether the Trustee had done any preliminary analysis of preference claims under Section 547 of the Bankruptcy Code, 11 U.S.C. § 547, that could warrant the filing of bankruptcy petitions for Devon and FMS. Because the window for avoiding preferences gets smaller every day -- as the beginning of the 90 day preference period approaches the date on which the Trustee was appointed -- Tyrone's counsel noted the need to consider this issue quickly. To date, the Trustee has not responded on this issue.

explained that intervention by numerous school district claimants "would bring the processing of the matter ... to a screeching halt." Id.

Here again, there are critical differences between the positions of Richland and Tyrone. Because Tyrone is in a unique position -- holding the largest claim and having the most urgent need for an interim distribution -- permitting Tyrone to intervene would not necessitate intervention by others. To the contrary, permitting intervention by Tyrone, as the claimant having the most compelling claim, would be consistent with a decision not to permit intervention at this time by similarly-situated claimants.

Permissive intervention also is appropriate using the analogy of bankruptcy. In many ways, this case is similar to a liquidating Chapter 11 case. After collecting assets of the defendants' estates, the Trustee may propose a plan for making distributions to creditors in accordance with the priorities of their claims. Under similar circumstances, the bankruptcy court in In re County of Orange, No. SA 94-22272-JR (Bankr. C.D. Cal. 1994), developed procedures for allowing dozens of school districts and other municipal authorities to receive interim distributions needed to avoid immediate and irreparable harm to these claimants. The court initially authorized distributions to school districts up to a cap of 30% of the amounts held by the debtors, and subsequent orders increased this cap to 60%. The present case lends itself to a similar procedure.

Were this a Chapter 11 case, however, Section 1109 of the Bankruptcy Code, 11 U.S.C. § 1109, would entitle any creditor to "raise and ... appear and be heard on any issue" in the case. Denial of intervention by a district in Tyrone's position would, in effect, encourage Tyrone to consider joining other claimants in filing an involuntary bankruptcy petition in order to assure the ability to be heard. Permitting intervention by a party in Tyrone's position would discourage the filing of a petition by claimants which believed themselves to be disenfranchised in this case.⁴

⁴ In accordance with the Court's Order Appointing Trustee, an involuntary petition may be filed only upon application to the Court, after 72 hours notice to the Trustee and the SEC. Even were an involuntary petition filed and an order for relief entered, this Court might withdraw the reference of the entire bankruptcy case in accordance with 28 U.S.C. § 157(d).

In short, Tyrone has satisfied the standard of Rule 24(b) and the Court, in exercising its discretion, should permit Tyrone to intervene.

C. Tyrone's Motion May be Granted on a Limited Basis

Where an applicant satisfies Rule 24(a), the court does not have discretion to deny intervention. Harris v. Pernsley, 820 F.2d 592, 597 (3d Cir. 1987). In unusual circumstances, however, a court may limit the scope of intervention. The Supreme Court, in Stringfellow v. Concerned Neighbors in Action, 480 U.S. 370 (1987), recognized that an intervenor's rights may be tailored to fit its particular interest. See also, Harris v. Pernsley, *supra*, at 599 (a party "may have sufficient interest to intervene as to certain issues in an action without having an interest in the litigation as a whole."); Kirkland v. New York State Dept. of Correctional Services, 711 F.2d 1117, 1126 (2d Cir. 1983); and see, Advisory Committee Notes, F.R.Civ.P. 24.

Although Tyrone believes it has a right to intervene generally, for the purpose of pursuing the claims set forth in its proposed Complaint, Tyrone's Motion demonstrates a particular interest in matters relating to the distribution of funds. In the near term, Tyrone needs a significant interim distribution; in the longer term, Tyrone needs to maximize its total recovery. Because Tyrone may be able to maximize its recovery only at the expense of other claimants, Tyrone cannot rely upon the Trustee to represent its interest. As an alternative to granting Tyrone's Motion on an unlimited basis, taking into account the Court's concern that this litigation not be unduly complicated, the Court may grant Tyrone's Motion for the limited purpose of permitting Tyrone to engage in discovery and take such other actions as may be appropriate to protect these particular interests.

D. Intervention by Tyrone as a Representative Claimant

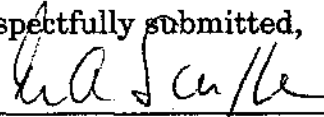
Tyrone's Motion should be considered in light of the Court's statement that it was not ruling out the possibility of intervention by a representative school district. Memorandum Order at 4. As the district with the largest claim and the most compelling need for funds, Tyrone is a particularly appropriate representative-intervenor. Tyrone is agreeable to working with other school districts to identify a small number of other "representative" districts which, collectively, could represent the interests of all claimants. Tyrone's intervention

would go a long way to protect the interests of similarly-situated claimants, while furthering the Court's interests in efficiency and judicial economy. Similarly, Tyrone could be granted leave to amend its Complaint to state a class action, in which Tyrone would serve as a representative party.⁵ On this alternative basis, Tyrone's Motion should be granted.

III. CONCLUSION

For all of the reasons discussed above, Tyrone Area School District requests that this Honorable Court permit it to intervene in this action as a party-plaintiff.

Respectfully submitted,



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⁵ In any event, if intervention is granted, Tyrone might seek to amend its Complaint based on further research or investigation that could not be completed before the expedited filing of Tyrone's Motion.