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BEFORE THE ARIZONA CORPORATION COMMISSION RECEIVED

1
2 **MARC SPITZER**
Chairman
3 **JIM IRVIN**
Commissioner
4 **WILLIAM A. MUNDELL**
Commissioner
5 **JEFF MATCH-MILLER**
Commissioner
6 **MIKE GLEASON**
Commissioner
7

Arizona Corporation Commission

DOCKETED

MAY 28 2003

2003 MAY 28 P 4: 17

AZ CORP COMMISSION
DOCUMENT CONTROL

DOCKETED BY

8 In the matter of:
9 MUTUAL BENEFITS CORPORATION,
10
11 Respondent.

DOCKET NO. S-03464A-03-0000

12 **MOTION TO DISMISS, OR IN THE ALTERNATIVE,**
13 **MOTION FOR MORE DEFINITE STATEMENT**

14 Respondent Mutual Benefits Corporation ("MBC") hereby files its Motion to Dismiss, or
15 in the alternative, Motion for More Definite Statement (the "Motion") pursuant to Rules 9(b) and
16 12(e), Ariz. R. Civ. P., and Arizona Administrative Code R14-3-101. This Motion is supported
17 by: (i) the attached Memorandum of Points and Authorities and (ii) the Commission's entire file
18 in this matter.

19 RESPECTFULLY SUBMITTED this 28th day of May, 2003.

20 ROSHKA HEYMAN & DeWULF, PLC

21
22 By _____

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MEMORANDUM OF POINTS AND AUTHORITIES

I. INTRODUCTION AND SUMMARY OF ARGUMENT

The Securities Division (the "Division") has filed a Notice of Opportunity for Hearing (the "Notice") that does little more than make vague, ambiguous, unclear, and incomplete assertions of fraudulent conduct. Despite filing a 64 paragraph complaint, the Notice does not include one act of alleged fraud that would satisfy the pleading requirements of Rule 9(b). As a result, the Notice should be dismissed, or in the alternative, the Division must be required to file an amended pleading containing a more definite statement of the allegedly fraudulent conduct.¹

MBC was founded in 1994 to enhance the financial security of terminally ill individuals by helping them sell their life insurance policies to generate income while they are still alive. Such policy sales were initially known as "viatical settlements," but have also come to be known in some contexts as "life settlements." From the beginning, MBC's service answered an acute need of AIDS patients, cancer patients and others for funds to pay for living expenses, medical costs and hospice care not covered by medical insurance.

MBC's services found a ready market because life insurance companies themselves offered minimal buyout opportunities to their policyholders. Thus, many life policies simply lapsed because their owners could no longer afford the premiums, while the owners' families used up their life savings to pay for their care. In order that policy owners could realize some of the value of the assets they had purchased, MBC adopted a system for facilitating the sale of qualified life insurance policies to individual purchasers² and groups of purchasers.³

¹ In accordance with the Commission's Rules, MBC will file its Answer on or before May 30, 2003. This Answer should not be treated as a waiver of this challenge to the Division's flawed Notice. It is being filed to be certain MBC complies with the Commission's Answer requirements.

² MBC intends to challenge the Division's concept of "investor" within the Notice. Accordingly, MBC uses the more appropriate word "purchaser" throughout this pleading.

³ Recognizing the critical importance of this industry to terminally ill patients, the federal government enacted statutes granting tax-free status to the proceeds from the sale of viatical policies.

1 Under MBC's business model, the price a purchaser pays is a fixed percentage of the
2 stated death benefit, based on the predicted life expectancy of the insured. In exchange for this
3 payment, the purchaser acquires from the seller a well-defined property interest: a direct,
4 undivided interest in the seller's incontestable life insurance policy. On completion of the sale,
5 each purchaser receives documentation that confirms the following facts:

- 6 (1) The purchaser is a named beneficiary on the seller's life insurance policy, and
7 expressly acknowledged as such by the insurer.
- 8 (2) The policy is typically owned by a trustee, *unrelated to MBC*, who holds it in
9 trust pursuant to an express written contract with the purchaser.
- 10 (3) The policy documents, of which the purchaser has received a copy, reflect a
11 commitment by the insurer to pay a defined sum *directly* to the purchaser
12 upon the death of the insured.
- 13 (4) The insurer is a company rated B+ or better by a nationally recognized rating
14 service.
- 15 (5) An independent licensed physician, *not employed by or affiliated with MBC*,
16 has reviewed the medical records of the insured to predict his or her life
17 expectancy.
- 18 (6) *The life expectancy prediction is uncertain by nature*, and the purchaser will
19 not receive payment until the insured actually dies. Therefore, a multi-layer
20 escrow fund is in place to provide for future premium payments if the insured
21 should outlive his or her stated life expectancy.
- 22 (7) The trustee, *acting on behalf of the purchasers*, has engaged a servicing
23 company to track the health of the insured and process the death claim when
24 the time comes to do so.

25 Under this business mode, MBC facilitated the sale of insurance policies. By means of
26 this service, many Arizona citizens were able to sell their life insurance policies and, thus, gain a
27 measure of financial freedom at the end of their lives. Some of the purchasers of policy interests
received death benefits earlier than predicted, others waited longer than anticipated, especially
after revolutionary medications were introduced which extended the lives of many AIDS patients
in the late 1990s. Throughout its history, however, *no purchaser who acquired interests in*

1 *policies through MBC has ever been called upon to pay a premium. Nor has any purchaser failed*
2 *to collect the bargained-for death benefit after the death of the insured.*

3 In 2000, the Arizona Legislature enacted a law adding viatical settlements to the list of
4 property interests that may be regulated as “securities” in Arizona, thereby amending A.R.S. §
5 44-1801. The Legislature also enacted A.R.S. § 44-1850 providing an exemption from the
6 requirements of A.R.S. § 44-1841. MBC believes it has complied with the filing requirements of
7 A.R.S. § 44-1850, but the Division has failed to confirm the exemption.

8
9 MBC withdrew altogether the opportunity for Arizona residents to purchase insurance
10 policy interests after the new law became effective on July 18, 2000. Despite this change in
11 MBC’s official practice, sales were inadvertently made to Arizona purchasers after July 18, 2000.
12 MBC is in the process of offering rescission to each of these purchasers. With that exception,
13 MBC has effectively ceased doing business in Arizona since the new statute took effect. Despite
14 MBC’s withdrawal from the Arizona viatical market, on April 25, 2003 the Division issued the
15 Notice against it even though it knew MBC had ceased doing business in Arizona and MBC had
16 complied with the filing requirements of A.R.S. § 44-1850.

17
18 With respect to transactions completed before July 18, 2000 (“pre-statutory sales”), no
19 violation of law has occurred. Because the sale of interests in life insurance policies did not
20 constitute the sale of securities before July 18, 2000, no registration or exemption from
21 registration was required. Indeed, such sales are beyond the jurisdiction of the Commission and
22 may not lawfully be the subject of this enforcement action. The Division would not have needed
23 to go to the Legislature in 2000 if these interests were already securities.

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1 **II. THE NOTICE OF OPPORTUNITY FOR HEARING**

2 The Notice attempts to allege violations of: (i) A.R.S. § 44-1841; (ii) A.R.S. § 44-1842;
 3 and (iii) A.R.S. § 44-1991. This Motion addresses only the allegation that MBC violated A.R.S. §
 4 44-1991 which is captioned, "Fraud in Connection with the Offer or Sale of Securities."

5 The Notice alleges that MBC committed fraud in a variety of ways. [Notice ¶¶ 13, 20, 27,
 6 37-38, 40-42, 45-46, 48, 50, 53] The Notice, however, is replete with vague references,
 7 incomplete information, and allegations that generally are insufficient when measured against the
 8 standard of Rule 9(b). By way of example, the following vague, ambiguous, and incomplete
 9 allegations in the Notice are inadequately plead in an attempt to support a violation of A.R.S. §
 10 44-1991:
 11

12 In mid-May 2001, a **MBC marketing employee** deliberately
 13 mislead an **Arizona agent** by telling the agent that he could sell
 14 viaticals in Arizona . . .

15 MBC engaged in deceptive and manipulative acts to effect sales to
 16 **Arizona residents** by encouraging the use of out-of-state addresses
 17 to create the false appearance that these were not Arizona sales.

18 Furthermore, **numerous investors** believed that returns were annual
 19 returns while **still others** believed that whether or not the investment
 20 matured, they had purchased a one, two or three-year investment that
 21 would pay the stated percentage at the end of the defined term.

22 **Investors** also did **not generally** understand that they had the right
 23 to perform post-purchase efforts. **If they understood** they had that
 24 option, **many** did not feel qualified as they lacked the requisite
 25 knowledge or access to information to perform these functions. . . .

26 At least with respect to MBC's viatical sales effected between 1995
 27 and 1999, **agents generally followed** MBC's marketing literature. **Agents** represented that investments in a viatical settlement present little to no risk and provide returns that were higher than most other investments. **Agents** claimed MBC viaticals were a "solid" "no gamble" "guaranteed" "fully insured" investment always emphasizing that investors could not lose any money. **Agents** misrepresented or omitted to tell **investors** about the potential risks.

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Investors were not advised of the detrimental effect on the **investors'** profits should the viator live beyond the projected life expectancy . . .

MBC through its sales **agents** mislead **investors** by minimizing the risk that viators would live beyond their projected life expectancies.

At least **two viator attending physicians** maintain they never spoke with Dr. Mitchell regarding the condition, treatment or anticipated life expectancy of the viator . . .

Furthermore, MBC made a material misrepresentation of fact when it advised **investors** that the viator's physician would have verified and validated that the viator was of sound mind prior to the **investor** purchasing the viatical. **At least with respect to one attending physician**, no verification or validation was given to MBC.

Some of MBC's investors did not understand that they would never receive more than the stated fixed return or that the longer the viator lived the less they would earn on an annualized basis.

Other misrepresentations and omissions include but are not limited to:

- a. **Some investors** were not told . . .
- b. **Agents** did not disclose, . . .
- c. **Agents** did not disclose . . .
- f. **Agents** did not disclose, . . .⁴
- g. **Agents** failed to provide, . . .
- h. **Agents** did not discuss, . . .
- i. **Agents** failed to advise, . . .

[Notice ¶¶ 13,20,27, 37-38, 40-42, 45-46, 48, 50, 53 (emphasis added).]

There is not one instance in the Notice where the Division points to a particular independent agent or MBC itself making a specific fraudulent statement or omission to an identifiable purchaser. These broad generalizations are precisely the type of allegations that Rule 9(b) is intended to avoid when the complaint sounds in fraud, as this Notice does. Vess v. Ciba-Geigy Corp.USA, 317 F.3d 1097, 1107 (9th Cir. 2003).

⁴ There are no Paragraph Nos. 53(d) or 53(e) in the Notice.

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III. LAW AND ARGUMENT

The Notice must be dismissed for failure to plead fraud with particularity pursuant to Rule 9(b) Ariz. R. Civ. P. In the alternative, due to the vague nature of the allegations found in the Notice, the Administrative Law Judge should, at a minimum, require the Division to file an Amended Notice pursuant to MBC's request for a more definite statement in accordance with Rule 12(e) Ariz. R. Civ. P.

The Division must comply with Rules 9(b) and 12(e) since the Commission follows the Rules of Civil Procedure for the Superior Court of Arizona absent a law, administrative rule, regulation or order of the Commission addressing the topic. A.A.C. R14-3-101(A).

A. The Division Must Plead Any Alleged Misrepresentations with Particularity as Required by Rule 9(b).

Since the Notice is grounded in fraud, the Division must plead the alleged misrepresentations, and the facts showing their falsity, with particularity under Rule 9(b). Hall v. Romero, 141 Ariz. 120, 124, 685 P.2d 757, 761 (Ct. App. 1984); Vess, 317 F.3d at 1103-07; In re Stac Elec. Sec. Litig., 89 F.3d 1399, 1404-05 & n.2 (9th Cir. 1996). Applying Rule 9(b) in this manner serves its underlying purpose, namely to protect defendants against unsubstantiated charges of fraud. Vess, 317 F.3d at 1104.

1. **The Notice fails to identify the who, what, when, where, and how of fraud.⁵**

To satisfy Rule 9(b), "a plaintiff must set forth more than the neutral facts necessary to identify the transaction. The plaintiff must set forth what is false or misleading about a statement, and why it is false. In other words, the plaintiff must set forth an explanation as to why the

⁵ Paragraph No. 5 of the Notice alleges that from 1995 to 2002, MBC sold \$11,400,000 viatical and life settlements through approximately 55 individuals and corporate agents to approximately 349 Arizonians. Which agent or agents, which transactions and which Arizonians are referred to in the Notice is, at present, anyone's guess. The \$11,400,000 figure contradicts the \$9,200,000 figure contained in Paragraph No. 7 of the Notice, adding to the confusion.

1 statement or omission complained of was false or misleading.” Yourish v. California Amplifier,
2 191 F.3d 983, 993 (9th Cir. 1999). Rule 9(b) also requires that a plaintiff plead the “who, what,
3 when, where, and how” of fraud. Credit Insurance Consultants, Inc. v. Gerling Global
4 Reinsurance Corp. of America, 210 F. Supp. 2d 980, 983 (N.D. Ill. 2002).

5 The Division fails to plead the “time, place, and nature of the alleged fraudulent
6 activities,” but relies instead on impermissible conclusory allegations, vague references to
7 “Agents” and “Investors” and impermissible generalizations to attempt to establish a fraud. A.G.
8 Edwards & Sons, Inc., 736 F. Supp. 1030, 1033 (D. Ariz. 1989). The Division fails to identify a
9 single transaction that MBC entered into that would support a claim of fraud. And, the Division
10 does not allege any particularized facts showing that a statement was false when made. Hall, 141
11 Ariz. at 124.

12 The Division does not adequately allege that MBC made any misrepresentations or
13 omissions to specific purchasers. [Notice ¶¶ 13, 20, 27, 37-38, 40-42, 45-46, 48, 50, 53] The
14 “who, what, when, where and how” of the alleged misrepresentations, and particularized facts
15 showing their falsity, are absent from the Notice. [Id.] Accordingly, the Notice fails to state a
16 claim for fraud. Vess, 317 F.3d at 1103-04, 1106-07.

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19 **B. The Division Must File a More Definite Statement.**

20 Rule 12(e) Ariz. R. Civ. P. states, in pertinent part:

21 If a pleading to which a responsive pleading is permitted is so vague
22 or ambiguous that a party cannot reasonably be required to frame a
23 responsive pleading, the party may move for a more definite
24 statement before interposing a responsive pleading. The motion
shall point out the defects complained of and the details desired.

25 Rule 12(e) Ariz. R. Civ. P. (West 2003). The Notice is vague and ambiguous as outlined more
26 fully in Section II, *supra* (pp. 4-6). As discussed more fully therein, the Division does not identify

1 to whom its allegedly fraudulent statements are attributed, nor does it allege to whom they were
2 made, when they were made, where, or any other fact surrounding them.

3 Rule 12(e) requires the moving party to point out the defects in the pleading and set forth
4 the details desired. The deficiencies in the Notice have been outlined, in part, in Section II, *supra*
5 (pp. 4-6). The Division should be ordered to file a pleading that complies with Rules 9(b) and
6 12(e), Ariz. R. Civ. P. With respect to the specific allegations below, the Amended Notice should,
7 at a minimum, contain the following information:
8

9 In mid-May 2001, a **MBC marketing employee** deliberately
10 mislead an **Arizona agent** by telling the agent that he could sell
viaticals in Arizona . . .

11 The Division should identify: (i) which MBC "employee" it attributes this statement to, (ii)
12 to which Arizona independent agent it was made, (iii) where the communication occurred, and (iv)
13 how it took place.

14 MBC engaged in deceptive and manipulative acts to effect sales to
15 Arizona residents by encouraging the use of out-of-state addresses to
create the false appearance that these were not Arizona sales.

16
17 The Division should identify: (i) who at MBC encouraged the use of out-of-state
18 addresses, (ii) who, if anyone, used such an address, (iii) all communications on which this
19 allegation is based, (iv) when the alleged conduct took place, (v) where the conduct occurred, and
20 (vi) how the conduct occurred.

21 Furthermore, numerous **investors** believed that returns were annual
22 returns while **still others** believed that whether or not the investment
23 matured, they had purchased a one, two or three-year investment that
would pay the stated percentage at the end of the defined term.

24 The Division should identify: (i) the numerous purchasers who believed the returns were
25 "annual returns," (ii) which "still other" purchasers believed they had purchased a one, two or
26 three-year investment, (iii) who at MBC is alleged to have informed these purchasers of this
27

1 information, (iv) when the communications occurred, (v) in where the communications occurred,
2 and (vi) how the communications occurred.

3 **Investors** also did **not generally** understand that they had the right
4 to perform post-purchase efforts. If they understood they had that
5 option, many did not feel qualified as they lacked the requisite
6 knowledge or access to information to perform these functions

7 The Division should identify: (i) the specific purchasers who did not “generally”
8 understand they had the right to perform post-purchase efforts, (ii) the specific purchasers who
9 apparently did understand they had this right but did not feel qualified to exercise it, (iii) the
10 specific post-purchase efforts they could perform, (iv) the independent agent to whom the
11 fraudulent statement or omission in connection with this allegation is attributed, (v) when the
12 communication occurred, (vi) where the communication occurred, and (vii) how the
13 communication occurred.

14 At least with respect to MBC’s viatical sales effected between 1995
15 and 1999, **agents generally followed** MBC’s marketing literature.
16 **Agents** represented that investments in a viatical settlement present
17 little to no risk and provide returns that were higher than most other
18 investments. **Agents** claimed MBC viaticals were a “solid” “no
19 gamble” “guaranteed” “fully insured” investment always
20 emphasizing that investors could not lose any money. **Agents**
21 misrepresented or omitted to tell **investors** about the potential risks.

22 The Division should identify: (i) which “agents” “generally” followed MBC’s “marketing
23 literature,” (ii) the marketing literature referred to, (iii) specific transactions in which this allegedly
24 fraudulent “marketing literature” was used, (iv) the identity of specific purchasers involved in the
25 allegedly fraudulent transactions, (v) when the transactions and/or communications occurred, (vi)
26 which independent agents allegedly misrepresented or omitted to tell purchasers about the
27 potential risks, and (vii) the specific purchasers who were unaware of the potential risks.

Investors were not advised of the detrimental effect on the
investors’ profits should the viator live beyond the projected life
expectancy . . .

1 The Division should identify: (i) the specific purchasers who were not advised of the
2 detrimental effect on their profits should the viator live beyond the projected life expectancy, (ii)
3 the independent agents to whom the fraudulent statements or omissions are attributed, (iii) when
4 the communications occurred, (iv) where the communications occurred, and (v) how the
5 communications occurred.
6

7 For **investors**, the projected life expectancy assigned by MBC was a
8 material factor in making **their** investment decision.

9 The Division should identify: (i) the specific purchasers referred to in this allegation, and
10 (ii) the specific transactions at issue.

11 MBC through its sales agents mislead **investors** by minimizing the
12 risk that viators would live beyond their projected life expectancies.

13 The Division should identify: (i) the specific purchasers who were allegedly misled, (ii)
14 the independent agents who allegedly misled them, (iii) when the communications occurred, (iv)
15 where the communications occurred, and (v) how the communications occurred.

16 At least **two viator attending physicians** maintain they never spoke
17 with Dr. Mitchell regarding the condition, treatment or anticipated
18 life expectancy of the viator . . .

19 The Division should identify the “two viator attending physicians” referred to in this
20 allegation.

21 Furthermore, MBC made a material misrepresentation of fact when
22 it advised investors that the viator’s physician would have verified
23 and validated that the viator was of sound mind prior to the investor
24 purchasing the viatical. **At least with respect to one attending
25 physician**, no verification or validation was given to MBC.

26 The Division should identify the “attending physician” referred to in this allegation.

27 **Some of MBC’s investors** did not understand that they would never
receive more than the stated fixed return or that the longer the viator
lived the less they would earn on an annualized basis.

1 The Division should identify: (i) the specific purchasers referred to in this allegation, (ii)
2 the independent agents the fraudulent statements or omissions are attributed to, (iii) when the
3 communications occurred, (iv) where the communications occurred, and (v) how the
4 communications occurred.

5 Other misrepresentations and omissions include, but are not limited to:

- 6 a. **Some investors** were not told . . .
7 b. **Agents** did not disclose, . . .
8 c. **Agents** did not disclose . . .
9 f. **Agents** did not disclose,⁶ . . .
g. **Agents** failed to provide, . . .
10 h. **Agents** did not discuss, . . .
i. **Agents** failed to advise, . . .

11 The Division should identify: (i) the specific purchasers referred to in this allegation, (ii)
12 the specific independent agents referred to in this allegation, (iii) when the alleged
13 communications occurred, (iv) where the communications occurred, and (v) how the
14 communications occurred. [Notice ¶¶ 13, 20, 27, 37-38, 40-42, 45-46, 48, 50, 53 (emphasis
15 added)].

16
17 MBC cannot completely respond to the Notice unless the Division is ordered to provide
18 the information requested above. Therefore, if the Commission does not dismiss the Notice for
19 failure to comply with Rule 9(b), MBC respectfully requests that the Division be required to
20 provide a more definite statement in accordance with Rule 12(e) Ariz. R. Civ. P.

21 **IV. CONCLUSION**

22 The Notice sounds in fraud. As such, it is subject to the strict pleading requirements of
23 Rule 9(b). The Notice does not allege fraud with particularity as required by Rule 9(b) and must,
24 therefore, be dismissed. In the alternative, the Division should, at a minimum, be required to file
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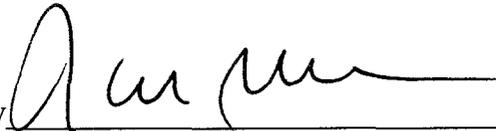
⁶ As note earlier, there are no Paragraphs Nos. 53(d) or 53(e) in the Notice.

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1 a pleading that MBC is able to respond to in accordance with Rule 12(e). Therefore, MBC
2 respectfully requests that the Commission dismiss the Notice for failure to plead fraud with
3 particularity in accordance with Rule 9(b), or in the alternative, enter an order requiring the
4 Division to file an Amended Notice setting forth, at a minimum, the information requested above.

5 RESPECTFULLY SUBMITTED this 28th day of May, 2003.

6 ROSKA HEYMAN & DeWULF, PLC

7
8
9 By 

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18 Attorneys for Respondent
19 Mutual Benefits Corporation

20 ORIGINAL and thirteen copies of the foregoing
21 hand-delivered this 28th day of May, 2003 to:

22 Docket Control
23 Arizona Corporation Commission
24 1200 West Washington Street
25 Phoenix, Arizona 85007

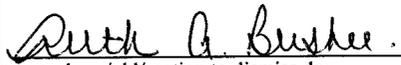
26 COPY of the foregoing hand-delivered
27 this 28th day of May, 2003 to:

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