

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

MICHAEL J. QUILLING, Receiver for
SARDAUKAR HOLDINGS, IBC and
BRADLEY C. STARK,

Plaintiff,

v.

3D MARKETING LLC,

Defendant.

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CIVIL ACTION NO. 3:06-CV-0293-L (BD)

ECF

Referred to U.S. Magistrate Judge

**BRIEF IN SUPPORT OF PLAINTIFF'S
MOTION FOR SUMMARY JUDGMENT**

Michael J. Quilling
State Bar No. 16432300
Brent J. Rodine
State Bar No. 24048770
QUILLING SELANDER CUMMISKEY & LOWNDS, P.C.
2001 Bryan Street, Suite 1800
Dallas, Texas 75201-4240
(214) 871-2100 (Telephone)
(214) 871-2111 (Facsimile)

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TO THE HONORABLE JEFF A. KAPLAN, UNITED STATES MAGISTRATE JUDGE:

COMES NOW, Michael J. Quilling as Receiver for Sardaukar Holdings IBC and Bradley C. Stark ("Plaintiff" or "Receiver") and, in accordance with Local Rule 56.5, files this his Brief in Support of Plaintiff's Motion for Summary Judgment against Defendant 3D Marketing LLC ("Defendant") and would respectfully show the Court as follows:

**I.
 INTRODUCTION**

It is well settled that, under the Uniform Fraudulent Transfer Act, all transfers out of a *Ponzi* scheme are fraudulent as a matter of law. The undisputed material facts in this case conclusively show that Brad Stark operated Sardaukar as a *Ponzi* scheme. This conclusion is supported by Sardaukar's own bank records, which clearly establish that: (1) investor funds constituted virtually all of Sardaukar's revenue; (2) those funds were commingled and used for undisclosed expenses not related to any legitimate investments; and (3) any investment "returns" to earlier contributors were

actually *Ponzi* payments from the commingled funds of later contributors. These facts establish as a matter of law that transfers from Sardaukar were made with the intent to hinder, delay, or defraud creditors under the Uniform Fraudulent Transfer Act.

In this case, the undisputed material facts show that Sardaukar made two transfers to Defendant totaling \$150,000.00. The Receiver is entitled to summary judgment on his claims to recover all or part of those funds because they constitute fraudulent transfers out of a *Ponzi* scheme or were otherwise held in constructive trust for the benefit of Sardaukar's defrauded investors.

II.
STATEMENT OF UNDISPUTED MATERIAL FACTS

The Receiver's Appointment in this Case

1. On July 1, 2005, the Securities and Exchange Commission ("SEC") initiated *SEC v. Megafund Corporation, et al.*, Civil Action No. 3:05-CV-1328-L (N.D. Tex.) (the "Receivership Proceeding"). *Receiver's Declaration*, Exhibit "A" at ¶ 3 (App. at 5-6). The SEC alleges that Bradley C. Stark ("Stark"), the director of Sardaukar Holdings IBC ("Sardaukar"), raised funds through an investment scheme and then used the money on luxury cars and other lavish expenses. *Complaint* [Dkt. No. 1] at ¶ 3 (3:05-CV-1328).

2. In connection with that lawsuit, the SEC sought to have a receiver appointed for the defendants and relief defendant in that case. *Receiver's Declaration*, Exhibit "A" at ¶ 4 (App. at 6). The Court appointed Michael J. Quilling as Receiver for Stark, Sardaukar, and others and he has since continued to function in that capacity. *Order Appointing Temporary Receiver* [Dkt. No. 9], as amended July 19, 2005 [Dkt. No. 36] (3:05-CV-1328).

3. Since his appointment, the Receiver has investigated the businesses, transactions,

assets, liabilities, books, and records of both Stark and Sardaukar. *Receiver's Declaration*, Exhibit "A" at ¶ 5 (App. at 6). He has also interviewed witnesses, taken depositions, and reviewed all available documents concerning the underlying investment scheme and transfers of investor funds. *Id.*

The Sardaukar Investment Scheme

4. The Receiver's investigation has revealed that Stark operated a *Ponzi* scheme and fraudulent investment program through Sardaukar, an entity under his sole direction and control. *Id.* at ¶ 6 (App. at 6). In fact, Sardaukar's own bank records clearly establish that: (1) investor funds constituted virtually all of Sardaukar's revenue; (2) those funds were commingled and used for expenses not related to any legitimate investment; and (3) any investment "returns" to earlier contributors were actually *Ponzi* payments from the commingled funds of later contributors. *Id.* These account records are voluminous so the Receiver's accountant has prepared a spreadsheet summary attached as Exhibit "A-1" (App. at 9-21), which is fully incorporated for all purposes. *Id.*

5. These records show that, as Sardaukar received investor funds, Stark systematically diverted large sums to support an extravagant lifestyle and to personally benefit himself, his friends, and his family. *Receiver's Declaration*, Exhibit "A" at ¶ 7 (App. at 6-7).

Sardaukar Investor Funds Transferred to Defendant

6. Among those who benefitted from Stark's scheme was an entity called 3D Marketing, LLC ("Defendant"). *Id.* In all, Defendant sent \$100,000.00 to Stark and received a certificate for 100,000 shares of Sardaukar stock, along with two payments totaling \$150,000.00. *Id.*

7. On August 27, 2004, Defendant sent a \$50,000.00 cashier's check to Stark's personal account at Bank of America. *See 3D Marketing Cashier's Check*, Exhibit "B" (App. at 23); *Brad*

Stark's Bank of America Account Statement, Exhibit "C" (App. at 25-34). Defendant then sent a second \$50,000.00 check on February 22, 2005 to another Bank of America account held by Sardaukar. *See 3D Marketing Check*, Exhibit "D" (App. at 36); *Sardaukar's Bank of America Account Statement*, Exhibit "E" (App. at 38-39).

8. Three weeks later, on March 10, 2005, Stark issued Defendant a certificate for 100,000 shares of Sardaukar stock purportedly valued at \$100,000.00. *See Stock Certificate*, Exhibit "F" (App. at 41-42).

9. In the next month, Stark made two transfers of investor funds totaling \$150,000.00 to Defendant's bank account at Wells Fargo Bank. *See Sardaukar Wire Transfers*, Exhibits "G" and "H" (App. at 44-45, 47-48); *3D Marketing Wells Fargo Account Statements*, Exhibits "I" and "J" (App. at 50, 52).

10. Receivership Estate records show that neither Sardaukar nor its investors received any benefit in exchange for the \$150,000.00 paid to Defendant. *Receiver's Declaration*, Exhibit "A" at ¶ 7 (App. at 6-7).

III. ARGUMENTS AND ANALYSIS

As explained more fully below, the Receiver submits that Sardaukar sent Defendant \$150,000.00 that was fraudulently transferred out of a *Ponzi* scheme or otherwise imposed with a constructive trust. To the extent that Defendant received the \$150,000.00 as compensation for participating in the *Ponzi* scheme as an equity owner, this Court should order Defendant to disgorge those ill-gotten gains. Alternatively, equity at least entitles the Receiver to summary judgment for the \$50,000.00 difference between Defendant's contribution and the investor funds sent to its

account at Wells Fargo Bank.

A. Standards for Granting Summary Judgment.

A party may obtain summary judgment when there is no genuine issue as to any material fact. Fed. R. Civ. P. 56(c); *Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986). A fact is “material” only if it might affect the outcome of the case. *MacDonald v. Delta Air Lines, Inc.*, 94 F.3d 1437, 1440 (10th Cir. 1996); *see also Poulis-Minot v. Smith*, 388 F.3d 354, 363 (1st Cir. 2004). An issue is “genuine” only if a reasonable jury could return a verdict for the non-movant on the evidence. *MacDonald*, 94 F.3d at 1440; *Poulis-Minot*, 388 F.3d at 363. Stated another way, the Court should award summary judgment where the record, taken as a whole, could not lead a rational jury to find for the non-moving party. *See Logan v. Commercial Un. Ins. Co.*, 96 F.3d 971 978 (7th Cir. 1996).

B. Summary Judgment is Appropriate in this Case Because the Undisputed Material Facts Show that Funds Fraudulently Transferred from a Ponzi Scheme were Paid to Defendant.

There is no genuine issue as to the material facts establishing the Receiver’s claim under the Texas Uniform Fraudulent Transfer Act (“UFTA”).¹ In relevant part, the UFTA provides that:

(a) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor’s claim arose within a reasonable time before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation:

- (1) with actual intent to hinder, delay, or defraud any creditor of the debtor . .

Tex. Bus. & Com. C. § 24.005. While creditors must ordinarily prove fraudulent intent in order to recover under this provision of the UFTA, that element is automatically established for transfers out

¹ The California Uniform Fraudulent Transfer Act contains the same provisions. *See* Cal. Civ. C. §3439 *et seq.*

of a *Ponzi* scheme. *Quilling v. Gilliland*, Civil Cause No. 3:01-CV-1617 (N.D. Tex. Mar. 6, 2002); *S.E.C. v. Cook*, 2001 WL 256172, *3 (N.D. Tex. Mar. 8, 2001); *see also, In re Ramirez Rodriguez*, 209 B .R. 424, 434 (Bankr. S.D. Tex.1997); *In re Independent Clearing House Co.*, 77 B.R. 843 (Bankr. D. Utah 1987). This presumption is necessarily true because a *Ponzi* scheme is insolvent from conception. *Warfield v. Byron*, 2006 WL 118250, *5 (5th Cir. Jan. 17, 2006), *citing Cunningham v. Brown*, 265 U.S. 1, 7-8 (1924).

Accordingly, all payments from a *Ponzi* scheme—including those purporting to be compensation—are fraudulent transfers hindering, delaying and defrauding creditors. *SEC v. Cook*, 2001 WL 256172, *3-4 (N.D. Tex. Mar. 8, 2001) (granting Receiver's motion for summary judgment to recover compensation paid from a *Ponzi* scheme); *see also Warfield*, 2006 WL 118250 at *6-7 (disgorging compensation skimmed from investor payments into a *Ponzi* scheme); *In re Alpha Telecom, Inc.*, 2004 WL 3142555, *4 (D. Or. Aug. 18, 2004) (disgorging compensation for selling securities for a *Ponzi* scheme).

In this case, the undisputed material facts show that (1) Sardaukar was operated as a *Ponzi* scheme and (2) Stark transferred \$150,000.00 of investor funds to Defendant's account at Wells Fargo Bank. Those transfers were, therefore, fraudulent under the UFTA and the Receiver is entitled to summary judgment against Defendant to recover all or part of those funds.

1. The Undisputed Material Facts Show that Sardaukar was a *Ponzi* Scheme.

For purposes of summary judgment, a *Ponzi* scheme may be proved by uncontroverted testimony offered by the Receiver. *See Cook*, 2001 WL 256172 at *3. In his declaration, the Receiver clearly explains how the undisputed material facts show that Sardaukar was operated as a *Ponzi* scheme. *Receiver's Declaration*, Exhibit "A" at ¶¶ 6-7 (App. at 6-7) . Defendant has not

challenged this conclusion and no legitimate evidence to the contrary has yet been offered this action, the Receivership Proceedings, or in any other ancillary cases.²

Furthermore, the evidence before this Court conclusively shows that Sardaukar was a *Ponzi* scheme. A *Ponzi* scheme exists where money from new investors is used to pay “profits” to earlier investors, without the operation of an actual revenue-producing business. Black’s Law Dictionary 1180 (7th ed. 1999). The Receiver has taken possession of Sardaukar’s account records at JPMorgan Chase Bank. *Receiver’s Declaration*, Exhibit “A” at ¶ 6 (App. at 6). Those records conclusively show that: (1) investor funds constituted virtually all of Sardaukar’s revenue; (2) those funds were commingled and used for expenses not related to any legitimate investments; and (3) what funds remained were commingled and used to pay “returns” to earlier investors. *Id.*; *see also Summary of Sardaukar’s JPMorgan Account*, Exhibit “A-1” (App. at 9-21). This kind of arrangement illustrates a classic *Ponzi* scheme. *Receiver’s Declaration*, Exhibit “A” at ¶ 6 (App. at 6).

2. There is No Genuine Issue of Material Fact Regarding Sardaukar’s Transfer of Funds to Defendant’s Account at Wells Fargo Bank.

Receivership Estate records clearly show that Defendant sent \$100,000.00 to Stark and received an ownership interest in the *Ponzi* scheme, along with two payments totaling \$150,000.00.

In late 2004 and early 2005, Defendant sent a total of \$100,000.00 to two accounts that Stark maintained at Bank of America. *See 3D Marketing Cashier’s Check*, Exhibit “B” (App. at 23); *Brad Stark’s Bank of America Account Statement*, Exhibit “C” (App. at 25-34); *3D Marketing Check*,

² In *Quilling v. Tschebaum, et al.*, Civil Action No. 3:05-CV-1465 (N.D. Tex.), Brad Stark attempted to challenge the *Ponzi* scheme’s existence by offering his own affidavit and some account records purporting to be from Man Financial, Inc. [Dkt. No. 15] (3:05-CV-1465). Testimony from a Man Financial representative, however, exposed Stark’s affidavit as perjury and the records as forgeries. [Dkt. No. 17] (3:05-CV-1465). The Court later accepted the Receiver’s conclusion that Stark operated Sardaukar as a *Ponzi* scheme. *Findings and Recommendation of the U.S. Magistrate Judge* [Dkt. No. 72] (3:05-CV-1465).

Exhibit “D” (App. at 36); *Sardaukar’s Bank of America Account Statement*, Exhibit “E” (App. at 38-39). Two weeks after its final payment, Stark issued Defendant a certificate for 100,000 shares of Sardaukar stock with a face value of \$100,000.00. *Stock Certificate*, Exhibit “F” (App. at 41-42).

Defendant previously attempted to mislead the Receiver about its participation as an equity holder in the *Ponzi* scheme. In correspondence with the Receiver’s counsel, Defendant stated that:

There were no stock purchases in anything that 3-D Marketing did. 3-D Marketing received no Sardaukar positions/stock. Our investment was based on contributing to a trading account that would expand and we would be paid as a result of that, nothing more, nothing less.

E-mail from Dean Steeves, January 12, 2006, Exhibit “K” (App. at 54-55) (emphasis added) (original appears in all capital letters). During discovery, however, Defendant produced the stock certificate attached as Exhibit “F” showing that it purportedly held 100,000 shares of Sardaukar stock.

Within a month after issuing Defendant’s stock certificate, Sardaukar sent two transfers of investor funds totaling \$150,000.00 to Defendant’s account at Wells Fargo Bank. *See Sardaukar Wire Transfers*, Exhibits “G” and “H” (App. at 44-45, 47-48); *3D Marketing Wells Fargo Account Statements*, Exhibits “I” and “J” (App. at 50, 52).

Since Sardaukar was a *Ponzi* scheme, it was insolvent at the time it made those transfers. *Warfield v. Byron*, 2006 WL 118250, *5 (5th Cir. Jan. 17, 2006), *citing Cunningham v. Brown*, 265 U.S. 1, 7-8 (1924). The law of this district, therefore, presumes that Sardaukar transferred those funds with the intent to “hinder, delay or defraud” other parties. *Quilling v. Gilliland*, Civil Cause No. 3:01-CV-1617 (N.D. Tex. Mar. 6, 2002); *S.E.C. v. Cook*, 2001 WL 256172, *3 (N.D. Tex. Mar. 8, 2001); *see also, In re Ramirez Rodriguez*, 209 B.R. 424, 434 (Bankr. S.D. Tex. 1997); *In re Independent Clearing House Co.*, 77 B.R. 843 (Bankr. D. Utah 1987). Accordingly, there is no

genuine issue of material fact precluding summary judgment in this case and the Court should avoid both of Sardaukar's transfers to Defendant. *See* Tex. Bus. & Com. C. § 24.008(1). Alternatively, the Receiver is at least entitled to summary judgment for the difference between Defendant's \$100,000.00 contribution and the \$150,000.00 that Sardaukar wired to Defendant's account at Wells Fargo Bank. *See* Tex. Bus. & Com. C. § 24.008(3) (permitting "any other relief the circumstances may require" within the principles of equity).

C. Summary Judgment is Also Appropriate in this Case Because the Undisputed Material Facts Show that Defendant Received Funds Impressed with a Constructive Trust.

It is a long-standing principle of equity that assets acquired by fraud are held subject to a constructive trust for the benefit of the defrauded parties. Restatement (First) of Restitution § 166 (1937). Under Texas law, a constructive trust is an equitable remedy for situations where a person holding title to property would be unjustly enriched if he were allowed to retain it. *See, e.g., Dyll v. Adams*, 167 F.3d 945, 948 (5th Cir.1999), *citing Omohundro v. Matthews*, 161 Tex. 367, 341 S.W.2d 401, 405 (1960); *United States v. Durham*, 86 F.3d 70, 72 (5th Cir.1996) (District Court has discretion to impose a constructive trust pursuant to its inherent equitable powers). While there is no strict formula dictating when a District Court sitting in equity is bound to impose a constructive trust, this remedy is appropriate to protect investor funds paid into a fraudulent investment scheme. *See Meadows v. Bierschwale*, 516 S.W.2d 125, 131 (Tex.1974) (no strict formula for creating constructive trust under Texas law); *see also SEC v. Paige*, 1985 WL 2335 (D.D.C. July 30, 1985), *aff'd* 810 F.2d 307 ("federal legal precedent [is] clear that a thief obtains no title to the stolen property and holds such property and the proceeds thereof in trust for the victim"); *United States v. Fontana*, 528 F.Supp. 137, 146 (S.D.N.Y. 1981) ("Where the title to property is acquired by one

person under such circumstances that he is under a duty to surrender it, a constructive trust immediately arises”), quoting 5 A. Scott, LAW OF TRUSTS § 462.4 (3d ed. 1967).

The Court overseeing these Receivership Proceedings clearly anticipated that the funds of Sardaukar investors were imposed with such a constructive trust. In the Order Appointing Receiver, the Court expressly directed that: “[t]he Receiver is hereby authorized to institute such actions or proceedings to impose a constructive trust ... with respect to persons or entities who received assets or funds traceable to investor monies.” *Order Appointing Receiver*, [Dkt. No. 36] (3:05-CV-1328). The Receiver, therefore, submits that all transfers or proceeds Defendant received are held in constructive trust and ought to be disgorged for the benefit of Sardaukar’s investors. *Receiver’s Declaration*, Exhibit “A” at ¶ 8 (App. at 7).

Respectfully submitted,

QUILLING SELANDER CUMMISKEY & LOWNDS, P.C.
2001 Bryan Street, Suite 1800
Dallas, Texas 75201-4240
(214) 871-2100 (Telephone)
(214) 871-2111 (Facsimile)

By: /s/ Brent J. Rodine
Michael J. Quilling
State Bar No. 16432300
E-mail: mquilling@qsclpc.com
Brent J. Rodine
State Bar No. 24048770
E-mail: brodine@qsclpc.com

ATTORNEYS FOR PLAINTIFF

CERTIFICATE OF SERVICE

On the 17th day of November, 2006 a true and correct copy of the above and foregoing was sent to opposing counsel by the Court's electronic filing system.

/s/ Brent J. Rodine
Brent J. Rodine