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

MICHAEL J. QUILLING, as Receiver for Sardaukar Holdings, IBC and Bradley C. Stark	§	
Plaintiff,	§	
VS.	§	NO. 3-06-CV-0293-L
3D MARKETING, LLC	§	
Defendant.	§	

FINDINGS AND RECOMMENDATION OF THE UNITED STATES MAGISTRATE JUDGE

Plaintiff Michael J. Quilling, as Receiver for Sardaukar Holdings, IBC and Bradley C. Stark, and Defendant 3D Marketing, LLC ("3D Marketing") have filed cross-motions for summary judgment in this civil action brought under the Texas Uniform Fraudulent Transfer Act ("TUFTA"), Tex. Bus. & Comm. Code. Ann. § 24.001, *et seq*. For the reasons stated herein, the Receiver's motion should be granted and 3D Marketing's motion should be denied.

I.

This case arises out of a lawsuit brought by the Securities and Exchange Commission ("SEC") against various defendants and relief-defendants involving the sale of unregistered securities. *SEC v. Megafund Corp.*, No. 3-05-CV-1328-L ("the *Megafund* Litigation"). In that case, the SEC alleges that the defendants, including Sardaukar Holdings, IBC ("Sardaukar") and Bradley C. Stark ("Stark"), raised more than $13 million from unwitting investors by making false representations about the expected rate of return on their investments and by promising that a portion of the profits generated from the sale of securities would be used to benefit charitable causes.

On July 5, 2005, the court appointed Michael J. Quilling as the Receiver for all defendants in the *Megafund* Litigation. In that capacity, Quilling was authorized to:

> take[ ] exclusive jurisdiction and possession of the assets, monies, securities, claims in action, and properties, real and personal, tangible and intangible, of whatever kind and description, wherever situated, of [the named defendants and relief defendant] and any entities they control ("Receivership Assets"), and the books and records of the Defendants and Relief Defendant ("Receivership Records").

See Order, 7/5/05 at 1-2, ¶ I(1)). The order further provides:

> The Receiver is hereby authorized to institute, defend, compromise or adjust such actions or proceedings in state or federal courts now pending and hereafter instituted, as may in his discretion be advisable or proper for the protection of Receivership Assets or proceeds therefrom, and to institute, prosecute, compromise or adjust such actions or proceedings in state or federal court as may in his judgment be necessary or proper for the collection, preservation and maintenance of Receivership Assets.
>
> The Receiver is hereby authorized to institute such actions or proceedings to impose a constructive trust, obtain possession and/or recover judgment with respect to person or entities who received assets or funds traceable to investor monies. All such actions shall be filed in this Court.

Id. at 5-6, ¶ I(12) & (13)).

On February 15, 2006, the Receiver filed this action to recover $150,000.00 transferred to 3D Marketing by Sardaukar. (Plf. Compl. at 3, ¶ 9). The Receiver contends that the transfers are fraudulent as a matter of law because Sardaukar was operated as an illegal *Ponzi* scheme by Stark. 3D Marketing denies that the payments were fraudulent transfers, characterizing one payment as a return on its initial $100,000.00 investment and the second payment as a "loan" from L.B. Charitable Trust, another Sardaukar investor. The case is before the court on cross-motions for summary judgment. The issues have been fully briefed by the parties and the motions are ripe for determination.

II.

Summary judgment is proper when there is no genuine issue as to any material fact and the movant is entitled to judgment as a matter of law. FED. R CIV. P. 56(c); *Celotex Corp. v. Catrett*, 477 U.S. 317, 322, 106 S.Ct. 2548, 2552, 91 L.Ed.2d 265 (1986). Where, as here, a case is presented by way of cross-motions for summary judgment, each party has the burden of producing evidence to support its motion. A summary judgment movant who bears the burden of proof at trial must establish "beyond peradventure all of the essential elements of the claim or defense to warrant judgment in his favor." *Fontenot v. Upjohn Co.*, 780 F.2d 1190, 1194 (5th Cir. 1986). By contrast, a party seeking summary judgment who does not have the burden of proof at trial need only point to the absence of a genuine fact issue. *See Duffy v. Leading Edge Products, Inc.*, 44 F.3d 308, 312 (5th Cir. 1995). Once the movant meets its initial burden, the non-movant must show that summary judgment is not proper. *See Duckett v. City of Cedar Park*, 950 F.2d 272, 276 (5th Cir. 1992). The parties may satisfy their respective burdens by tendering depositions, affidavits, and other competent evidence. *See Topalian v. Ehrman*, 954 F.2d 1125, 1131 (5th Cir.), *cert. denied*, 113 S.Ct. 82 (1992). All evidence must be viewed in the light most favorable to the party opposing the motion. *See Rosado v. Deters*, 5 F.3d 119, 122 (5th Cir. 1993).

A.

The Receiver alleges that two $75,000.00 payments made to 3D Marketing by Sardaukar constitute voidable transfers under TUFTA. This statute provides, in pertinent part:

> (a) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or within a reasonable time 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. & COMM. CODE ANN. § 24.005(a) (Vernon 2002). Ordinarily, the creditor must prove that the challenged transfer was made with the intent to defraud. *See Quilling v. Gilliland*, 3-01-CV-1617-BD, 2002 WL 373560 at *2 (N.D. Tex. Mar. 6, 2002) (Kaplan, J.), *appeal dism'd*, No. 02-10415 (5th Cir. Jun. 3, 2002). However, in the case of a *Ponzi* scheme, courts have found that the debtor's intent to hinder, delay, or defraud is established by the mere existence of such a scheme. *Id.*; *see also Warfield v. Byron*, 436 F.3d 551, 558 (5th Cir. 2006) (burden of proving that transfers were made with actual intent to defraud is satisfied by establishing the existence of a *Ponzi* scheme "which is, as a matter of law, insolvent from its inception"); *SEC v. Cook*, No. 3-00-CV-0272-R, 2001 WL 256172 at *3 (N.D. Tex. Mar. 8, 2001), *citing In re Independent Clearing House Co.*, 77 B.R. 843, 860 (Bankr. D. Utah 1987) (finding requisite intent to defraud from fact that debtor must have known that *Ponzi* scheme would inevitably collapse and that later investors would lose their investments).

B.

In order to prove that Sardaukar was operated as an illegal *Ponzi* scheme, the Receiver offers his own declaration explaining the Sardaukar investment program. According to the Receiver, virtually all of Sarduakar's revenue came from investor funds, which were commingled with other investor monies and used to pay expenses not related to any legitimate investments. (Plf. MSJ App. at 6, ¶¶ 6-7). Any "returns" paid to investors were actually payments from the commingled funds of other contributors. (*Id.* at 6, ¶ 6; *see also id.* at 9-21). These are the features of a classic *Ponzi* scheme. *See Quilling v. Humphries*, No. 3-06-CV-0299-L, 2006 WL 2934276 at *5 n.2 (N.D. Tex. Oct. 13, 2006) (Kaplan, J.), *citing* BLACK'S LAW DICTIONARY 1180 (7th ed. 1999) (describing *Ponzi* scheme as "a fraudulent investment scheme where money from new investors is used to pay 'profits'

on the money contributed by earlier investors, without the operation of an actual revenue-producing business other than the raising of new funds by finding more investors").

3D Marketing has adduced no evidence to controvert these facts.[1] Instead, it relies on the allegations of its answer denying that Sardaukar was operated as a *Ponzi* scheme and points to the absence of expert testimony on this issue. However, a party "may not rest upon the mere allegations or denials of its pleadings[.]" *Morris v. Covan World Wide Moving, Inc.*, 144 F.3d 377, 380 (5th Cir. 1998). Nor will unsubstantiated or conclusory assertions of a fact issue suffice. *Id.* In order to avoid summary judgment, 3D Marketing must "go beyond the pleadings and by [its] own affidavits, or by the 'depositions, answer to interrogatories, and admissions on file,' designate 'specific facts showing that there is a genuine issue for trial.'" *Celotex*, 106 S.Ct. at 2553, *quoting* FED. R. CIV. P. 56(e). No such attempt has been made here. Likewise, the court is unaware of any authority requiring expert testimony to establish the existence of a *Ponzi* scheme. To the contrary, judges in this district have routinely made such a determination at the summary judgment stage based on evidence similar to that presented by the Receiver in this case. *See, e.g. Quilling v. Schonsky*, No. 3-05-CV-2122-BH, 2006 WL 3772302 at *3 (N.D. Tex. Dec. 19, 2006) (Ramirez, J.) (Receiver's uncontroverted evidence may prove existence of *Ponzi* scheme); *Gilliland*, 2002 WL 373560 at *2 (Kaplan, J.) (same); *Cook*, 2001 WL 256172 at *3 (Buchmeyer, J.) (same). The court therefore finds, as a matter of law, that Sardaukar was operated as a *Ponzi* scheme.[2]

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[1] 3D Marketing does object that the bank records relied on by the Receiver are not properly authenticated and constitute hearsay. (*See* Def. MSJ Resp. Br. at 2). However, the Receiver has not offered the records themselves into evidence. Rather, he relies on a summary of those records prepared by his accountant, which is admissible under Fed. R. Evid. 1006. *See* FED. R. EVID. 1006 ("The contents of voluminous writings, recordings, or photographs which cannot conveniently be examined in court may be presented in the form of a chart, summary, or calculation."). Significantly, 3D Marketing does not dispute the accuracy of the summary or the underlying bank records.

[2] Although not binding on 3D Marketing, the court notes two other cases where it determined that Sardaukar was operated as an illegal *Ponzi* scheme. *Quilling v. Stark*, No. 3-05-CV-1976-BD, op. at 5 (N.D. Tex. Feb. 7, 2007); *Quilling v. Tschebaum*, No. 3-05-CV-1465-L, op. at 5 (N.D. Tex. Jul. 21, 2006).

C.

The summary judgment evidence establishes that 3D Marketing made two $50,000.00 payments to Sardaukar. (Plf. MSJ App. at 23, 25, 36, 38). One payment was made on or about August 27, 2004. (*Id.* at 23, 25). Another payment was made on or about February 22, 2005. (*Id.* at 36, 38). Within weeks of the second payment, 3D Marketing received a certificate for 100,000 shares of Sardaukar stock. (*Id.* at 41-42). On March 11, 2005, Sardaukar transferred $75,000.00 from its account at JPMorgan Chase Bank to 3D Marketing's account at Wells Fargo Bank. (*Id.* at 14, 44-45). Sardaukar transferred another $75,000.00 to 3D Marketing on April 17, 2005. (*Id.* at 16, 47-48). 3D Marketing admits that it received both payments. (*See* Def. Ans. at 2, ¶ 9). However, it maintains that one payment was a return on its initial investment and the other payment was a "loan" from L.B. Charitable Trust. This may or may not be true. In either case, 3D Marketing has failed to raise a meritorious defense under TUFTA. *Warfield*, 436 F.3d at 556 (that defendant is merely an innocent investor in a *Ponzi* scheme and not a knowing participant in any fraudulent activity is irrelevant to liability under TUFTA). Because these transfers were fraudulent as a matter of law, the Receiver is entitled to summary judgment.

RECOMMENDATION

Plaintiff's motion for summary judgment [Doc. #23] should be granted and defendant's motion for summary judgment [Doc. # 27] should be denied. The court should enter judgment against 3D Marketing in the amount of $150,000.00, together with prejudgment and post-judgment interest as allowed by law. A constructive trust should be imposed on the funds transferred by Sardaukar and 3D Marketing should be ordered to disgorge the same. As the prevailing party in this case, the Receiver is entitled to recover "costs and reasonable attorney's fees as are equitable and just." *See* TEX. BUS. & COMM. CODE ANN. § 24.013. An application for attorney's fees shall be filed

within 14 days after entry of a final judgment in accordance with Fed. R. Civ. P. 54(d)(2).

A copy of this report and recommendation shall be served on all parties in the manner provided by law. Any party may file written objections to the recommendation within 10 days after being served with a copy. *See* 28 U.S.C. § 636(b)(1); FED. R. CIV. P. 72(b). The failure to file written objections will bar the aggrieved party from appealing the factual findings and legal conclusions of the magistrate judge that are accepted or adopted by the district court, except upon grounds of plain error. *See Douglass v. United Services Automobile Ass'n*, 79 F.3d 1415, 1417 (5th Cir. 1996).

DATED: February 8, 2007.

JEFF KAPLAN
UNITED STATES MAGISTRATE JUDGE