

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.

GLENN M. STARK,

Defendants.

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CIVIL ACTION NO. 3:06-CV-1435-N

ECF

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

TO THE HONORABLE DAVID C. GODBEY, UNITED STATES DISTRICT JUDGE:

Pursuant to Local Civil Rule 56.5, Plaintiff Michael J. Quilling, as Receiver for Sardaukar Holdings, IBC and Bradley C. Stark, ("Plaintiff" or "Receiver") files this Brief in Support of Plaintiff's Motion for Summary Judgment against Defendant Glenn M. Stark. In support of that motion, the Receiver 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 (1) Sardaukar was a *Ponzi* scheme and (2) Sardaukar transferred \$87,280.00 directly to the Defendant. Accordingly, there is no genuine issue of material fact precluding the Receiver from recovering on his fraudulent transfer claim for that amount.

II.
STATEMENT OF UNDISPUTED MATERIAL FACTS

1. This case arises out of a lawsuit brought by the Securities and Exchange Commission (the "SEC") against numerous defendants involved in a fraudulent investment program. *See Securities and Exchange Commission, v. Megafund Corporation, et al.*; Cause No. 3:05-CV-1328-L (N.D. Tex.) (the "Receivership Proceedings"). The SEC filed suit against Brad Stark, Sardaukar Holdings IBC ("Sardaukar"), and others for promising high-yield returns to investors and then squandering their money on extravagant, unrelated personal expenses. *See Complaint* [Dkt. 1] at ¶ 3 (3:05-CV-1328).

2. By order of July 5, 2005, the Court presiding over the Receivership Proceedings appointed Michael J. Quilling as Receiver for those defendants and relief defendant and he has since continued to function in that capacity. *See Order Appointing Temporary Receiver* ("Order Appointing Receiver") [Dkt. No. 9], as amended July 19, 2005 [Dkt. No. 36] (3:05-CV-1328).

3. The Receiver has seized all known bank accounts related to the Receivership Proceedings, interviewed numerous principals and investors, subpoenaed records, and investigated the underlying transfers and purchases from investor funds. *Receiver's Declaration*, Exhibit "A" at ¶ 2 (App. at 5-6). In particular, he has taken possession of all records relating to Sardaukar's account at JPMorgan Chase Bank, N.A. *Id.* at ¶ 3 (App. at 6). Those records are voluminous, so the Receiver's accountant has prepared a spreadsheet summary for easy reference. *Account Summary*, Exhibit "B" (App. at 9-21).

4. Sardaukar's account records conclusively show that (1) investor funds constituted virtually all of Sardaukar's revenue, (2) those funds were commingled and used for personal

expenses rather than legitimate investments, and (3) any investment “returns” to earlier contributors were actually *Ponzi* payments from the commingled funds of later contributors. *Id.* at ¶ 5 (App. 6).

On its face, this kind of arrangement illustrates a classic *Ponzi* scheme.¹ *Id.*

5. The Order Appointing Receiver expressly authorizes legal action to recover investor funds transferred to third parties:

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 persons or entities who received assets or funds traceable to investor monies.

Id. [Dkt. No. 36] at ¶ 13 (3:05-CV-1328).

6. The Receiver filed this action against Brad Stark’s brother, Glenn M. Stark (“Defendant”), to recover \$87,280.00 of investor funds that he admittedly received. *Answer* [Dkt. No. 5] at ¶ 7; *see also Check to Defendant*, Exhibit “C” (App. at 23).

7. Account records show that Defendant did not invest with Sardaukar or exchange an equivalent value for the investor funds he received. *Receiver’s Declaration*, Exhibit “A” at ¶ 4 (App. at 6); *Account Summary*, Exhibit “B” (App. at 9-21) (showing that Sardaukar received no contributions from Defendant).

8. As explained more fully below, the undisputed material facts show that (1) Sardaukar was a *Ponzi* scheme and (2) Defendant received \$87,280.00 of investor funds transferred from Sardaukar’s account at JPMorgan Chase Bank. Therefore, the Receiver respectfully requests that this Court enter summary judgment on his claims for fraudulent transfer and constructive trust and

¹ In three other cases, this Court relied on those account records to make its own determination that Sardaukar was operated as a *Ponzi* scheme. *See Quilling v. Tschebaum*, Cause No. 3:05-CV-1465 (N.D. Tex. Jul. 21, 2006); *Quilling v. Schonsky*, Cause No. 3:05-CV-2122 (N.D. Tex. Dec. 19, 2006); *Quilling v. 3D Marketing, LLC*, Cause No. 3:06-CV-0293 (N.D. Tex. Feb. 28, 2007).

disgorgement.

III. ARGUMENTS AND ANALYSIS

A. Standard 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 relates to the substantive law of the parties’ claims for relief. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986) (“the substantive law will identify which facts are material”); *Rogers v. Monumental Life Ins. Co.*, 289 F.3d 442, 448 (6th Cir. 2002). 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 respondent. *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 Establish that Defendant Received Fraudulent Transfers Under the UFTA.

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

(a) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor . . . 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. § 24.005.² The transferor's intent to "hinder, delay, or defraud" is established as a matter of law by the mere existence of a *Ponzi* scheme. *Quilling v. Gilliland*, 2002 WL 373560, *2 (N.D. Tex. Mar. 6, 2002); *SEC 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 its inception. *Warfield v. Byron*, 2006 WL 118250, *5 (5th Cir. Jan. 17, 2006) (*Cunningham v. Brown*, 265 U.S. 1, 7-8 (1924)). Accordingly, all transfers from a *Ponzi* scheme are intended to hinder, delay, and defraud creditors. *See Cook*, 2001 WL 256172 at *3, 4 (granting Receiver's motion for summary judgment to recover transfers from a *Ponzi* scheme); *see also Warfield*, 2006 WL 118250 at *6-7 (disgorging compensation from a *Ponzi* scheme); *In re Alpha Telecom, Inc.*, 2004 WL 3142555, *4 (D. Or. Aug. 18, 2004) (disgorging transfers made from a *Ponzi* scheme). Therefore, the only material facts at issue in this case are (1) whether Defendant received funds transferred from Sardaukar and (2) whether Sardaukar was a *Ponzi* scheme.

As explained more fully below, the Receiver is entitled to summary judgment in this case because Defendant admits receiving the \$87,280.00 transfer from Sardaukar and cannot dispute that it originated from a *Ponzi* scheme.

1. Defendant Has Raised No Genuine Issue of Material Fact Regarding his Receipt of Investor Funds from Sardaukar.

The Defendant admits that Brad Stark caused Sardaukar to transfer \$87,280.00 to him as described in the Receiver's Complaint. *Answer* [Dkt. No. 5] at ¶ 7. Sardaukar's bank records conclusively confirm this fact and, therefore, there is no genuine issue as to the dates, amounts, or

² The California Uniform Fraudulent Transfer Act contains the same provisions. *See* Cal. Civ. C. § 3439 *et seq.*

nature of these transfers. *See also Receiver's Declaration*, Exhibit "A" at ¶ 4 (App. at 6); *Account Summary*, Exhibit "B" (App. at 11). The only remaining issue for recovery under the UFTA is whether these transfers were made out of a *Ponzi* scheme.

2. There is No Genuine Issue of Material Fact Regarding the Existence of a *Ponzi* Scheme.

For purposes of summary judgment, a *Ponzi* scheme may be proved by the Reciever's uncontroverted testimony. *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 ¶¶ 5-7 (App. at 6-7). The Defendant has not challenged this conclusion and no legitimate evidence to the contrary has been offered in this case, the Receivership Proceedings, or in any ancillary cases.³

As explained in the Receiver's Declaration, the evidence before this Court conclusively shows that Sardaukar was, in fact, 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); *see also Receiver's Declaration*, Exhibit "A" at ¶ 5 (App. at 6). The Receiver has taken possession of Sardaukar's account records at JPMorgan Chase Bank, N.A., where Brad Stark received all known contributions from Sardaukar investors. *Id* at ¶ 3 (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 personal

³ In *Quilling v. Tschebaum, et al.*, Cause 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 account 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).

expenses rather than legitimate investments, and (3) what funds remained after Starks' spending sprees and handouts were commingled and used to pay "returns" to earlier investors.⁴ *See id.* at ¶ 5 (App. at 6-7); *see also Account Summary*, Exhibit "B" (App. at 9-21) (showing that money from Sardaukar investors were commingled, used for personal expenditures, and paid as returns to other investors). This kind of arrangement illustrates a classic *Ponzi* scheme. *Receiver's Declaration*, Exhibit "A" at ¶ 5 (App. at 6).

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). 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 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

⁴ When reviewing the bank records and accountant summary, it is worth noting that Sardaukar contributors included numerous corporate entities like CIG, Ltd., CDB&B Investors, Inc., Clover Investment LLC, International Consultants & Referrals, and Investment World, Inc. *See Account Summary*, Exhibit "B" (App. at 9, 11, 13). Their money was commingled with that of individual investors and should not be misconstrued as an investment or other legitimate means for generating revenue.

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 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.

IV. CONCLUSION

In short, the Defendant admits receiving funds that were undoubtedly proceeds from a *Ponzi* scheme. Therefore, under the UFTA and the settled law of this district, the Receiver has satisfied the burden for proving his fraudulent transfer and constructive trust and disgorgement claims against the Defendant. The Receiver now respectfully requests that this Court (1) enter a finding that Defendant received \$87,280.00 fraudulently transferred out of a *Ponzi* scheme, (2) enter a judgment in the amount of \$87,280.00 and an order for Defendant to disgorge that amount within 60 days, (3) award the Receiver his costs, fees, and pre- and post-judgment interest at the highest rate permitted by law, and (4) for such other and further relief, general or special, at law or in equity, to which he is otherwise justly entitled.

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 March 5, 2007 a true and correct copy of the above and foregoing was sent via first class mail, with full and proper postage prepaid thereon, to:

Glenn M. Stark
1271 Calle Candelerero
Chula Vista, California 91910-6811

/s/ Brent J. Rodine
Brent J. Rodine