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,	§	CIVIL ACTION NO. 3:06-CV-1435-N
v.	§	**ECF**
GLENN M. STARK,	§	
Defendants.	§	

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

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

COMES NOW Michael J. Quilling, the appointed Receiver for Sardaukar Holdings IBC and Bradley C. Stark, ("Plaintiff" or "Receiver") and files this Reply Brief in support of his Motion for Summary Judgment [Dkt. No. 13] and would respectfully show the Court as follows:

I. INTRODUCTION

Defendant's Response Brief [Dkt. No. 17] fails to raise a disputed issue of material fact precluding summary judgment in this case. 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). With respect to the Receiver's fraudulent transfer claim, the only material facts are those that relate to (1) whether Sardaukar was operated as a Ponzi scheme and (2) whether Sardaukar funds totaling $87,280.00 were transferred to Defendant. *See* Tex. Bus. & Com. C. § 24.005(a)(1). The Receiver has presented bank records, his declaration, and the Defendant's own admissions as undisputed

material facts supporting those elements. Defendant has not challenged the substance of those exhibits and failed to raise a timely affirmative defense under the Uniform Fraudulent Transfer Act. Furthermore, Defendant's Response Brief completely ignores all case law and evidence supporting the Receiver's claim for constructive trust and disgorgement. Therefore, as explained more fully below, this case is ripe for summary judgment on the undisputed material facts.

II.
ARGUMENTS AND ANALYSIS

A. Summary Judgment is Appropriate in this Case Because Defendant Does Not Dispute the Material Facts Establishing a Fraudulent Transfer Under the UFTA.

1. Defendants Do Not Dispute the Bank Records Establishing the Existence of a Ponzi Scheme.

The Ponzi scheme at issue in this case is self-evident from Sardaukar's account records. *Summary of Sardaukar's Account at JPMorgan Chase*, Exhibit "B" [Dkt. No. 14] (App. at 9-21). 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 legitimate investments; and (3) what funds remained were commingled and used to pay "returns" to earlier investors. *Id; Receiver's Declaration,* Exhibit "A" [Dkt. No. 14] at ¶ 5 (App. at 6-7). Without question, this constitutes a classic Ponzi scheme and the Court should enter that finding through summary judgment. *See Quilling v. Stark,* Cause No. 3:05-CV-1976 (N.D. Tex. Feb. 7, 2007); *Quilling v. Tschebaum,* Cause No. 3:05-CV-1465 (N.D. Tex. Jul. 21, 2006).

In his Response Brief, Defendant never once challenges these facts, he never challenges Sardaukar's account records supporting them, and he never submits any contradictory evidence of his own. It is, therefore, undisputed that Sardaukar showed all the characteristics of a classic Ponzi

scheme. Defendant cannot survive summary judgment based solely on his general denial of a Ponzi scheme and his opinion that the Receiver's evidence is not "definitive." *Defendant's Response Brief* [Dkt. 17] at ¶ 14. To the contrary, the Receiver's evidence is the only evidence before the Court regarding Sardaukar's operation and it leads to the unmistakable conclusion that Sardaukar was a Ponzi scheme. *See Quilling v. Stark*, Cause No. 3:05-CV-1976 (N.D. Tex. Feb. 7, 2007); *Quilling v. Tschebaum*, Cause No. 3:05-CV-1465 (N.D. Tex. Jul. 21, 2006).[1]

The only challenge mounted by Defendant is to the Receiver's declaration, which he dismisses as "opinion" evidence. *Response Brief* [Dkt. No. 17] at ¶¶ 10-14. The Receiver's declaration, however, expressly incorporates and relies upon Sardaukar's account records in explaining why the Ponzi scheme is self-evident. *Receiver's Declaration,* Exhibit "A" [Dkt. No.15] at ¶ 3 (App. at 6). By not offering evidence to the contrary, the Defendant has failed to raise a genuine issue of material fact precluding summary judgment.

2. Defendant Raises No Genuine Issue of Material Fact Regarding his Receipt of Investor Funds from Sardaukar.

Sardaukar's bank records also show that Defendant received investor funds totaling $87,280.00 from Sardaukar. *See Summary of Sardaukar's Account at JPMorgan Chase Bank,* Exhibit "B" [Dkt. No. 15] (App. at 11); *Sardaukar's Check to Defendant,* Exhibit "C" [Dkt. No. 15] (App. at 23). Defendant admits that the transfer occurred and the amount is not in dispute. *See Answer* [Dkt. No. 5] at ¶ 6. Therefore, the Receiver has established all facts necessary to prove his

[1] Defendant asks this Court to disregard its finding in the *Stark* and *Tschebaum* cases because "those cases did not involve this Defendant and I have not had an opportunity to respond thereto." *Defendant's Response Brief* [Dkt. 17] at ¶ 10 n.1. In this case, however, Defendant did have an opportunity to challenge and respond to the same Sardaukar account records and failed to do so. They are, therefore, undisputed material facts showing that Sardaukar was a Ponzi scheme, and this Court should enter that finding just as it did in the *Stark* and *Tschebaum* cases.

claim under the UFTA. Tex. Bus. & Com. C. § 24.005(a)(1). As explained below, summary judgment is appropriate in this case because the Defendant has failed to raise any colorable defenses.

B. Summary Judgment is Appropriate in this Case Because Defendant Fails to Properly Raise or Prove his Affirmative Defenses Under the UFTA.

1. Defendant Cannot Raise New Affirmative Defenses for the First Time in His Response Brief.

When a defendant fails to raise his affirmative defenses in the first responsive pleading, the Fifth Circuit generally considers those defenses waived. *Bayou Fleet Inc. v. Alexander*, 234 F.3d 852, 860 (5th Cir. 2000) ("Generally, a party's failure to raise an affirmative defense in its first responsive pleading results in waiver"); *see also* Fed. R. Civ. P . 8(c). Defendant's Answer fails to raise a single affirmative defense to any of the Receiver's claims. Instead, he waited to raise new defenses under Tex. Bus. & Com. C. § 24.009 for the first time in his Response Brief [Dkt. No. 17] and after the close of discovery. This unexplained delay denied the Receiver an opportunity to conduct discovery on those matters, thereby prejudicing his chance to respond. *See Chambers v. Johnson*, 197 F.3d 732, 735 (5th Cir. 1999) (District Court may allow late affirmative defenses if raised at a "pragmatically sufficient time" and "the plaintiff was not prejudiced in its ability to respond."). Defendant has not shown good cause for failing to raise those defenses earlier and the Court should, therefore, dismiss them as waived. *See, e.g., Davignon v. Clemmey*, 322 F.3d 1, 15 (1st Cir. 2003) (late affirmative defense may be allowed upon showing that, among other things, the defense was not available at the time the answer was filed).

Nevertheless, even if this Court considers Defendant's new affirmative defenses, summary judgment is still appropriate. As explained below, the Defendant has failed to show that he is (1) a "subsequent transferee" or (2) a "person who took in good faith and for a reasonably equivalent

value" for purposes of UFTA.

2. Even if Allowed to Raise his New Affirmative Defenses, Defendant Fails to Prove that He is a Subsequent Transferee.

Without any basis in law or fact, Defendant intimates that transfers from a Ponzi scheme are not fraudulent so long as they are made by cashier's check. Defendant notes that he received $87,280.00 of Sardaukar investor funds "by a cashier's check, not directly from any accounts of Sardaukar or Bradley Stark." *Defendant's Response Brief* [Dkt. No. 17] at ¶ 17. Without further explanation, the Defendant concludes that this fact relieves him from liability as a "subsequent transferee" under Tex. Bus. & Com. C. § 24.009. *Id.*

That section of the UFTA sets out the affirmative defenses available for transfers that are otherwise fraudulent:

> (a) A transfer or obligation is not voidable under Section 24.005(a)(1) of this code against a person who took in good faith and for a reasonably equivalent value or against any subsequent transferee or obligee.

Tex. Bus. & Com. C. § 24.009; *see also SEC v. Cook*, 2001 WL 256172, * 3 (N.D. Tex. Mar. 8, 2001) (defendants have the burden to raise and prove this defense). Defendant claims that, by accepting investor funds in the form of a cashier's check, he was a "subsequent transferee" and not the "immediate transferee." *Defendant's Response Brief* [Dkt. No. 17] at ¶ 17. Courts addressing the issue, however, have found that cashier's checks are voidable under the UFTA as fraudulent transfers directly from the debtor to the recipient. *In re Mussa*, 215 B.R. 158 (Bankr. N.D. Ill., 1997) (avoiding transfer of cashier's checks that debtor gave to family members); *see also In re M. Blackburn Mitchell Inc.*, 164 B.R. 117, 122-24 (Bankr. N.D. Cal., 1994) (bank that issued cashier's checks was a "financial intermediary" and not an initial transferee for purposes of the Bankruptcy

Code section that is "similar in its provisions to . . . the Uniform Fraudulent Transfer Act"); *see also In re Lee*, 179 B.R. 149, 159 (B.A.P. 9th Cir. 1995) ("the cashier's check, like an ordinary check, is utilized as a means of transferring the purchaser's cash to the check's payee. The issuing bank is not a transferee, it is simply a conduit").

Defendant's own statements underscore the fact that he was the immediate recipient of the investor funds. In his Answer, Defendant admits "receiving $87,280.00 from his brother." *Defendant's Answer* [Dkt. No. 5] at ¶ 6 (emphasis added). Defendant's Response Brief further explains that those funds were a "repayment" of a personal obligation by Brad Stark. *Defendant's Response Brief* [Dkt. No. 17] at ¶ 20. Clearly Defendant understood that he received the $87,280.00 directly from Brad Stark and not as a separate, independent transfer from a third party.

3. Even if Allowed to Raise his New Affirmative Defenses, Defendant Fails to Prove that He Took Investor Funds for Reasonably Equivalent Value and in Good Faith.

In order for Defendant to prevail on his second affirmative defense, he must show that he took the investor funds in good faith *and* that Sardaukar received an equivalent value in exchange. *See Cook*, 2001 WL 256172 at *4. The elements are conjunctive, meaning that Defendant must prove both good faith *and* an exchange of equivalent value. *Id.* at *3. Failing to prove both elements negates Defendant's affirmative defense. *Id.* Defendant has not carried his burden of proof on both elements because (1) Sardaukar received no actual benefit in exchange for the $87,280.00 transferred to Defendant and (2) Defendant offers no objective evidence showing that he took those funds in good faith. From Sardaukar's point of view, that transfer of funds was manifestly unreasonable and no rational jury could find for the Defendant.

The undisputed material facts show that Sardaukar received no actual benefit in exchange

for the investor funds that Brad Stark transferred to his brother. The primary consideration for determining whether a reasonably equivalent value was exchanged is "the degree to which the transferor's net worth is preserved." *Warfield v. Byron,* 436 F.3d 551, 560 (5th Cir. 2006). Defendant explains that he received the investor funds in exchange for "repayment of loans defendant personally gave to Bradley Stark." *Defendant's Response Brief* [Dkt. No. 17] at ¶ 20 (emphasis added). Therefore, by Defendant's own admission, Sardaukar and its investors received no actual benefit for the $87,280.00 and a reasonable jury could not conclude that this transfer would be justified at arm's length. *See Tex. Bus. & Com. C.* §24.004(d)(4) (defining "reasonably equivalent value" as the range of values that Sardaukar would have been willing to pay Defendant had the transaction been at arm's length.)

Defendant also fails to show any objective evidence that he accepted investor funds from his brother in good faith. Under the UFTA, Defendant must prove that he accepted the funds in good faith under an objective standard. *Warfield v. Byron,* 436 F.3d 551, 559-60 (5th Cir. 2006); *Quilling v. Stark,* Cause No. 3:05-CV-1976 (N.D. Tex. Feb. 7, 2007). Instead, Defendant rests solely on his own self-serving and subjective testimony that the transfer occurred in good faith. *Defendant's Response Brief* [Dkt. No. 17] at ¶ 23. Those legal conclusions, however, will not prevent entry of summary judgment in this case. *Marshall v. E. Carroll Parish Hosp.,* 134 F.3d 319, 324 (5th Cir. 1998) (summary judgment is appropriate when the nonmoving party relies solely upon his own "conclusory allegations").

Defendant has not offered any objective evidence supporting his affirmative defenses. *Cook,* 2001 WL 256172 *4 ("If [respondent] wishes to raise section 24.009 as a defense he may do so, but the burden falls on him to present facts that support it"). The only objective evidence in this case

favors summary judgment for the Receiver. Like other transfers to friends and relatives, Brad Stark's transfer of investor funds to his brother is highly suspect under the UFTA. *See* Tex. Bus. & Com. Code §§ 24.002(7), 24.005(b)(1) (disfavoring transactions to insiders, which specifically includes "a relative of the debtor or of a general partner"); UNIF. FRAUDULENT TRANSFER ACT § 5, comment 5 ("a transfer to a closely related person warrants close scrutiny of the other circumstances, including the nature and extent of the consideration exchanged"); *Jackson Sound Studios, Inc. v. Travis*, 473 F.2d 503 (5th Cir. 1973) (holding that the transfer to a corporate officer's mother was fraudulent); *J. Michael Putman, M.D.P.A. Money Purchase Pension Plan v. Stephenson*, 805 S.W. 16 (Tex. App.—Dallas 1991) (holding that transfers between an insider under the UFTA and his close friends were not in good faith and not for reasonably equivalent value). Without question, this transfer only benefitted Brad Stark and his brother and was not made in good faith or for reasonably equivalent value to Sardaukar.

C. Summary Judgment is Appropriate in this Case Because Defendant Does Not Dispute the Material Facts Imposing a Constructive Trust Upon the $87,280.00 that he Received.

Despite the requirements of Local Civil Rule 56.4, Defendant fails to set out any elements or legal authorities relating to the Receiver's constructive trust and disgorgement claim. The Receiver submits that a constructive trust arises at the moment investor funds are paid into a fraudulent investment scheme. *See 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). As explained above, account records show that Defendant received $87,280.00 from investor funds commingled in Sardaukar's JPMorgan Chase account. *See Summary*

of Sardaukar's Account at JPMorgan Chase, Exhibit "B" [Dkt. No. 14] (App. at 11). Those funds were impressed with a constructive trust at the moment they arrived in Sardaukar's account and the trust remained in place from that point forward. The fact that Brad Stark may have owed the Defendant money for a personal loan does not dissolve the investors' constructive trust or give Defendant a superior claim to those funds. Equity demands that the full $87,280.00 be disgorged and returned to the constructive trust's beneficiaries.

III.
CONCLUSION

In short, the Receiver has offered uncontroverted evidence to support every element of his claims for fraudulent transfer and constructive trust and disgorgement. Defendant has not challenged those exhibits with competent evidence or proven an affirmative defense under the Uniform Fraudulent Transfer Act. Furthermore, Defendant's Response Brief completely ignores all case law and evidence supporting the Receiver's claim for constructive trust and disgorgement. Therefore, this Court should grant the Receiver summary judgment based on the undisputed material facts.

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 April 12, 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 Candelero
Chula Vista, California 91910-6811

/s/ Brent J. Rodine
Brent J. Rodine