MEMORANDUM OF POINTS AND AUTHORITIES

I. INTRODUCTION

Plaintiff filed this adversary proceeding against Defendants seeking recovery of in excess of $5.6 million that Defendants allegedly received from the Debtor in connection with what the Plaintiff believes was a Ponzi scheme run by the Debtor. Plaintiff bases these allegations primarily on a plea bargain agreement wherein the Debtor admitted to running a Ponzi scheme with respect to certain of the Debtor's "investors" and on certain files and records of the Debtor (which files and records have yet to be produced to Defendants). Plaintiff ignores the fact that many of Slatkin's investments were real and resulted in real profits that were paid to investors. Plaintiff ignores evidence of the Debtor's actual solvency. Plaintiff also ignores the fact that not all of the investors actually received the profits or "net-gains" that Plaintiff alleges; investors did not necessarily withdraw the profits, but yet paid income tax and other expenses associated with the alleged net gain. While the Debtor may have been engaged in fraud with some of the transfers to certain of his investors, Plaintiff has yet to prove that any of transfers to the myriad of defendants he has sued on similar grounds were fraudulent or part of the alleged Ponzi scheme, let alone these Defendants.

Plaintiff has prevented Defendants from investigating the claims set forth in Plaintiff's complaint. Plaintiff has been unwilling to successfully coordinate an opportunity to depose the Debtor (although Plaintiff has represented that the Debtor would be made available). Plaintiff stated, through his counsel, that Slatkin would be made available through the United States Attorney's office. When the United States Attorney is contacted about deposing Slatkin, Defendants were told to contact Plaintiff. This runaround smacks in the face of due process and has effectively prevented Defendants from investigating the facts as they apply to the relevant issues.

By way of the Application, however, Plaintiff attempts to avoid his evidentiary burden of proving his case that Defendants received avoidable transfers in connection with the Debtor's alleged Ponzi scheme, but nonetheless attach over $5.6 million belonging to Defendants before their liability has been determined. As will be discussed below, there is no admissible evidence before the Court that demonstrates the probable validity of Plaintiff's underlying claims.

Notwithstanding Plaintiff's inability to demonstrate substantively that he is entitled to a right to attach order and writ of attachment, Plaintiff has failed to comply with the procedural requirements of obtaining such extraordinary relief.

First, the Application does not comply with Civil Code § 3439.07(a)(2) in that the Application fails to demonstrate that the property sought to be attached is the property that Plaintiff alleges was fraudulently transferred by the Debtor to Defendants or the proceeds thereof. Second, the Application does not comply with CCP § 484.020 in that the description of the property that Plaintiff seeks to attach is so grossly insufficient that Defendants are unable to determine whether any such property is exempt from attachment. Furthermore, Plaintiff has not demonstrated the probable validity of his underlying claim; the declarations and evidence offered in support of the Application do not establish a prima facie case demonstrating the Defendants' liability for the alleged transfers. Finally, Plaintiff has not demonstrated that the attachment is sought for the sole purpose of securing recovery on the claim. For each and all of these reasons, the right to attach order must not issue.

II. RELEVANT FACTS

In the Application, Plaintiff offers limited facts to justify the extraordinary remedy of pre-judgment attachment. Some of the facts alleged, however, are not based on any actual admissible evidence included in the supporting declarations or otherwise before this Court. Plaintiff states that "Slatkin engaged in a massive Ponzi scheme." *See* Notice Of Motion And Motion Of The Trustee's Application For A Right To Attach Order And Order For Issuance Of Writ Of Attachment; Memorandum Of Points And Authorities; And Declarations Of Grant Newton And Timothy B. Jafek In Support Thereof (the "Motion"), p.3, ln. 12. Plaintiff refers to the Declaration Of Grant W. Newton In Support Of The Trustee's Application For A Right To Attach Order And Order For Issuance Of Writ Of Attachment (the "Newton Decl.") in support of this allegation. Review of the Newton Decl. reveals, however, that the only document on which this "expert opinion" is based is the Debtor's plea agreement, which plea agreement helped the Debtor avoid a lifetime in prison, millions of dollars in criminal fines and other risks of criminal prosecution.

The plea agreement makes no reference to Defendants. *See* Newton Decl., Exhibit 1. Yet, Plaintiff relies almost exclusively on the plea bargain as a basis to attach over $5.6 million of unidentified property of the Defendants.

Plaintiff also contends that "[i]n or about September 1990, the Hutchins began 'investing' with Slatkin, as part of his scam." *See* Motion, p. 3, lns. 13 – 14. In support of this fact, Plaintiff offers a spreadsheet prepared by the Trustee's accountant that allegedly summarizes all of the financial transactions between Defendants and the Debtor. There is no showing that the documents upon which Plaintiff's expert bases his opinion represent the entire universe of transactions between the Debtor and Defendants. Because Plaintiff has denied Defendants access to all of the relevant documents, Defendants are unable to investigate the accuracy of such representations. Furthermore, contrary to Plaintiff assertion, there is no evidence that Defendants invested money with the Debtor as part of "his scam." Whether the Debtor operated a Ponzi scheme with respect to the funds he received from Defendants is an ultimate legal and factual issue in this case. Yet, Plaintiff offers no evidence that the investments with respect to Defendants were part of the alleged Ponzi scheme.

Plaintiff alleges that "[b]etween the years 1990 and 2001, the Hutchins received net transfers from Slatkin of $5,698,346.10." Id., p. 3, lns. 15 - 16. Plaintiff further contends that "[t]he money Slatkin paid to the Hutchins was money Slaktin swindled from others as part of his Ponzi scheme." Id. at p. 3, lns. 16 – 17. Plaintiff cites no evidence for this conclusory statement. To the extent that the spreadsheet and the documents that the spreadsheet is allegedly based upon are accurate, such information merely demonstrates that Defendants transferred funds to the Debtor from September 1990 to May 2001. Plaintiff's reference that Defendants participated in the Debtor's "scam" or that the transfers they received were part of the Debtor's alleged Ponzi scheme is not supported by any of the evidence proffered in support of the Application. Mr. Newton does not actually declare as his opinion that Slatkin operated a Ponzi scheme.

Finally, Plaintiff states that the purpose of his Application is to return the "improperly-transferred" funds to Plaintiff for distribution to creditors. Attached property is not deliverable to

the Plaintiff for use by the Plaintiff. He does not state that he seeks to attach the $5.6 million to secure recovery in this adversary proceeding.

Thus, the only facts that Plaintiff alleges in connection with the Application that are supported by evidence before the Court are as follows: (1) Slatkin entered into a plea bargain and avoided countless years in prison, millions of dollars in fines, and other risks of criminal prosecution, which is irrelevant to the instant action; (2) Defendants gave money to Slatkin starting in September 1990; (3) Defendants received some transfers from Slaktin; and (4) the purpose of the Application is to attach Defendants' assets funds for distribution to creditors. As will be explained below, these facts are insufficient to demonstrate the probable validity of Plaintiff's claims sufficient to justify the issuance of a right to attach order and writ of attachment.

III. ARGUMENT

The Application fails to demonstrate that the property sought to be attached is the property that Plaintiff alleges was fraudulently transferred by the Debtor to Defendants. The description of the property Plaintiff seeks to attach is so grossly insufficient that Defendants are unable to determine whether any such property is exempt from attachment. Plaintiff is unable to demonstrate the probable validity of his underlying claims. Finally, the purpose for which his attachment is expressly sought is not proper. For each and all of the foregoing reasons, the Application must be denied.

A. Standards For Granting A Right To Attach Order

The remedy of attachment is wholly statutory, its scope and procedure are limited by the statutes, and these statutes are strictly construed. Nakasone v. Randall, 129 Cal.App.3d 757 (1982); Arcata Publications Group v. Beverly Hills Publishing Co., 154 Cal.App.3d 276, 279 (1984); Bank of America v. Salinas Nissan, 207 Cal.App.3d 260, 270 (1989). CCP § 483.010 provides that an attachment order may issue only if the underlying claim being sued upon meets the following four requirements: (1) it is a "claim for money...based upon a contract, express or implied;" (2) of a "fixed or readily ascertainable amount not less than $500; (3) that is either unsecured or secured by personal property, not real property; and (4) that is a commercial claim.

The claims contained in Plaintiff's complaint, however, do not serve as a proper basis for attaching the class of the Defendants' property that Plaintiff seeks to attach.

Because Plaintiff is not suing Defendants on an express contract, to satisfy the first element of CCP § 484.090(a)(1), Plaintiff must demonstrate that the action is based on quasi- or implied contract. Some cases have held that where a defendant obtains property of a plaintiff through fraud perpetrated by the defendant upon the plaintiff, a writ of attachment should issue. *See, generally,* Klein v. Benaron, 247 Cal.App.2d 607 (1967) (defendant-corporate office obtained loan for his corporation from defendant-lender by fraud); Landry v. Marshall, 243 Cal.App.2d 170 (1966) (oral franchise/sale contact rescinded where defendants fraudulently induced plaintiff to enter into the same); Arcturus Mfg. Corp. v. Rork, 198 Cal.App.2d 208 (1961) (action to recover secret profits and kickbacks defendant-employee received from plaintiff-corporation). In each of those cases, the plaintiff was able to identify specific property that the defendants had fraudulently obtained.

Plaintiff seeks to attach assets that were allegedly fraudulently transferred to Defendants. Civil Code § 3439.07(a)(2) provides that attachment is only available for the asset transferred or its proceeds. "A creditor holding a matured claim may disregard a fraudulent conveyance and levy **upon the property conveyed** as belonging to the original debtor." Kuzmicki v. Nelson, 101 Cal.App.2d 278 (1950) (emphasis added). However, Plaintiff has not identified the specific property that was allegedly fraudulently transferred to Defendants. Instead, Plaintiff merely states that the amount to be attached is $5,698,346.10 and provides a generalized description of property that Plaintiff seeks to attach. Plaintiff by his own admission acknowledges that Defendants received transfers since 1990. It is highly unlikely that, even if the documents attached to the Newton Decl. accurately reflect the extent of the transactions between the Debtor and Defendants, the funds transferred to Defendants in those several years, or their proceeds, are still in the possession of Defendants. In fact, the funds transferred to Defendants have been subsequently commingled in Defendants' accounts and transferred to numerous third parties (a position that Plaintiff acknowledges by virtue of his 11 U.S.C. § 550 allegation in his complaint). Accordingly, Plaintiff has not complied with Civil Code § 3439.07(a)(2) because he cannot demonstrate that the

property he seeks to attach is the property allegedly fraudulently transferred by the Debtor to Defendants or the proceeds thereof.

Furthermore, the facts underlying the cases that have provided for attachment in cases of fraudulent transfers are wholly different from the facts in this case. In Whitehouse, the parties were able to identify the specific parcels of land obtained through a fraudulent transfer that were the subject of the attachment order. 40 Cal.App.4th at 531-32. Here, Plaintiff has not identified and is unable to identify any specific property that was allegedly fraudulently transferred.

Unlike in Whitehouse, there is no allegation or inference here that Defendants have transferred funds fraudulently to become judgment proof. The crux of Plaintiff's complaint is that the Debtor committed fraud on his "investors" and fraudulently obtained money from them. Even if Plaintiff's allegations are true, Defendants committed no fraud in obtaining the funds they received. This is unlike the situations in Klein, Landry and Arcturus, where it was the defendant who had committed the fraud in obtaining the money. This Defendants' hands are not stained with fraud as were the defendants in Klein, Landry and Arcturus. Thus, the cases that have deemed fraud as meeting the required element of that the underlying claim is on account of an express or implied contract are inapposite here. Therefore, Plaintiff cannot satisfy the necessary element of CCP § 484.090(a)(1) and demonstrate that the underlying claim is based on an express contract or implied contract. Plaintiff has offered no evidence that the property he seeks to attach is the property that was allegedly fraudulently transferred or that any of the transfers were as a result of the fraudulent conduct of the Defendants.

It is axiomatic that the typical situation where attachment of fraudulently transferred property is allowed involves attachment of a specific asset, e.g., Debtor transfers Blackacre for a peppercorn to Third Party, Creditor sues Third Party contending that the transfer of Blackacre was fraudulent and attaches Blackacre during the pendency of the litigation. Here, there is no hypothetical Blackacre. Plaintiff simply wants the relief prayed for in his complaint without a scintilla of evidence that the property sought to be attached was fraudulently transferred property or its proceeds or proving the probable validity of his claims. Granting the Application would be an

affront to justice and essentially award Plaintiff the victory laurel without Plaintiff having to run the race.

Furthermore, there is no authority for an attachment writ in a preference claim, to the extent that Plaintiff is proceeding on such a claim herein. Plaintiff's authority is directed, at best, to attachment in the context of fraudulent transfer claims, for which express statutory authority in limited circumstances (not met by Plaintiff here) does exist in the California Uniform Fraudulent Transfers Act, Cal. Civ. Code §§3439.01, et seq. Accordingly, the right to attach order must not issue.

C. Plaintiff's Description Of The Property Is Grossly Insufficient That It Prevents Defendants From Determining Whether The Property To Be Attached Is Exempt.

In opposing an application for a right to attach order, any claim of exemption as to the property sought to be attached may be asserted in the opposition papers or may be separately stated; otherwise, the claim of exemption is waived. CCP §§ 484.020, 484.070. To ensure that the defendant can determine whether the property sought to be attached is exempt from attachment, CCP § 484.020(e) provides that the application for a right to attach order must contain:

> "[a] description of the property to be attached under the writ of attachment and a statement that the plaintiff is informed and believes that such property is the subject of attachment...Where the defendant is a natural person, the description of the property shall be reasonably adequate to permit the defendant to identify the specific property sought to be attached."

The purpose of this requirement is to enable an individual defendant to determine whether to file a claim of exemption, i.e., if the application describes only non-exempt property; a claim of exemption is unnecessary; and court hearings are avoided. Bank of America, 207 Cal.App.3d at 268. Defendants acknowledges that Bank of America allows a plaintiff to provide a general description of an individual's property sought to be attached and does not "prohibit a plaintiff targeting for attachment everything an individual owns." Id. Due process concerns are raised, however, where there is a failure to identify the specific property to be attached before the seizure thereof which deprives the defendant of the prior notice and hearing required under Sniadach v. Family Financing Corp., 395 U.S. 337, 342 (1969)

Here, Plaintiff describes the property to be attached as follows:

> "Any asset fraudulently transferred or its proceeds including: Interests in real property except leasehold estates with unexpired terms of less than one year; accounts receivable, chattel paper, and general intangibles; equipment; farm products; inventory; final money judgments; money on the premises; deposit accounts; negotiable documents of title; instruments; securities; minerals or the like (including oil and gas) to be extracted."

See Application, p.2, ¶ 9. Plaintiff's description is grossly inadequate, not because he includes a general description more likely to be seen on a UCC-1 financing statement, but rather because the description is of "Any asset fraudulently transferred." Whether any of the funds received from the Debtor to Defendants were fraudulently transferred is the main legal and factual issue in this adversary proceeding. Defendants vehemently dispute that any funds that they received from the Debtor were fraudulent transfers. Because they disputes that the transfers were fraudulent (the ultimate issue in this adversary proceeding), the description of "any asset fraudulently transferred" does not describe any property of Defendants, let alone a staggering $5.6 million of their assets. Because Defendants deny that they are in possession of any fraudulently transferred assets, the description in the Application does not describe any of their property. *See* Declaration Of William W. Hutchins In Support Of Opposition To Application For Right To Attach Order And Order For Writ Of Attachment (the "Hutchins Decl.) at ¶¶ 3 – 4. As such, the description of the property sought to be attached is so grossly insufficient such that Defendants are unable to determine to what property Plaintiff is referring and whether any such property is exempt from attachment. Accordingly, the right to attach order should not issue because the description of the property does not allow Defendants to determine whether the property is exempt.

Furthermore, the amount alleged as being transferred between the Debtor and Defendants is not correct. Review of the documents attached to both the complaint and the Newton Decl. demonstrates that Plaintiff has not accounted for the purpose of numerous transfers between the Debtor and Defendants. Additionally, there are numerous outstanding legal issues regarding the amount actually recoverable by Plaintiff even if Plaintiff is correct on his fraudulent transfer allegations. The amount sought to be attached in the Application does not account for the numerous offsets, reductions, and other accountings that will be necessary to resolve this matter. In

light of the fact that Plaintiff is unable to even correctly identify all of the relevant transfers between the Debtor and Defendants, the description contained in the Application is made more inadequate because the dollar amount sought to be attached does not accurately reflect the net result of the transactions between the Debtor and Defendants. For all of these reasons, the right to attach order must not issue.

D. Plaintiff Is Unable To Demonstrate The Probable Validity Of His Underlying Claims Based On The Evidence Before The Court.

To obtain a right to attach order, the plaintiff has the burden of proving, *inter alia*, the probable validity of its claim. CCP § 484.090(a)(2); Loeb & Loeb v. Beverly Glen Music, Inc., 166 Cal.App.3d 1110, 1120 (1985). A claim has a "probable validity" where "it is more likely than not that the plaintiff will obtain a judgment against the defendant on that claim." CCP § 481.190. A proper foundation must be established for declarations and affidavits showing the declarant had personal knowledge of each fact stated. Generale Bank Nederland N.V. v. Eyes of the Beholder Ltd., 61 Cal.App.4th 1384, 1390 (1998). Plaintiff's contends that alleging that the Debtor was engaged in a Ponzi scheme establishes the probable validity of his underlying claims. Such a contention is not supported by applicable law nor the evidence offered in support of such contention.

1. Actual Fraud

Plaintiff contends that he has valid claims against the defrauded investors under the California Uniform Fraudulent Transfers Act (the "UFTA"), Cal. Civ. Code §§3439.01, et seq. The Trustee insists that Slatkin operated a Ponzi scheme and therefore all of an investor's "profits" or "net gains" are avoidable. The Trustee's claims are subject to numerous defenses, some of which are a complete bar to recovery.

a. Plaintiff Must Prove Fraudulent Intent At The Time Of Each Transfer.

To establish an "intentional fraudulent" transfer pursuant to Civil Code § 3439.04(a), Plaintiff must prove that Slatkin made each payment with actual intent to hinder, delay, or defraud creditors. Plaintiff contends that such intent to defraud may be inferred from the existence of a

Ponzi scheme. *See* Motion at p. 4, ln. 21 – p. 5, ln. 2. Plaintiff does not establish actual fraud by merely alleging that because the Debtor was transferring money that others entrusted to him to invest on their behalf, he had to have been working with full knowledge that he was causing to creditors.

Plaintiff's argument is wrong for at least three reasons. First, fraudulent intent is a question of fact, not of law. Arnold v. Hadgis, 226 P. 2d 641, 643 (Cal. 1951) ("Whether a transfer is in fraud of creditors is a question of fact and not of law, and where there is a consideration for the transfer the burden is on the party attacking it to establish actual fraudulent intent."). Like other fact questions, it must be determined by the trier of fact on the basis of the evidence.

Second, an "inference" is not equivalent to a "presumption," and certainly not a "conclusive presumption." Under California law, "fraud is never presumed." Cooper v. Leslie Salt Co., 451 P. 2d 406, 411, cert. denied, 396 U.S. 821 (1969). The Legislative Committee Comment to Civil Code § 3439.04(a) states unequivocally that "badges of fraud" do not create a presumption of fraud, but are "merely evidence from which an inference of fraudulent intent may be drawn." The existence of a Ponzi scheme is merely a badge of fraud, and, like other badges, does not conclusively establish fraudulent intent. Moreover, conclusive presumptions are strongly disfavored and usually violate due process. *See, e.g.*, Vlandis v. Kline, 412 U.S. 441 (1973) (statute creating conclusive presumption violated due process clause of 14th amendment).

Third, the theory that payments to Ponzi scheme investors are made with actual intent to defraud creditors applies only in cases involving a "pure" Ponzi scheme, i.e., where there is *no* underlying business, only borrowing from investors. This qualification is inherent in the definition of a Ponzi scheme: "A Ponzi scheme is a fraudulent arrangement in which an entity makes payments to investors from monies obtained from later investors rather than from any "profits" of the underlying venture." In re United Energy Corp., 944 F.2d 589, 590 n.1 (9th Cir. 1991).

If Slatkin engaged in *any* legitimate business activity, then his investment program was not a "pure" Ponzi scheme and intent to defraud may not be inferred. *See* M. McDermott, Ponzi Schemes and the Law of Fraudulent and PreferentialTransfers, 72 Am. Bankr. L.J. 157, 175 (1998) ("Thus, a presumption of actual intent cannot apply in all cases of Ponzi-type investment programs.

The court-fashioned presumption that Ponzi-scheme operators act with actual intent to defraud should be limited to those situations where it is unmistakable that the debtor purposefully orchestrated a scheme which, by its very design, could only serve to defraud investors.")

The Debtor made several investments that resulted in a profit. *See* Declaration Of James Crosser In Support Of Opposition To Application For Right To Attach Order And Order For Writ Of Attachment (the "Crosser Decl.") at ¶ 22. The Debtor made a number of investments that resulted in actual profit to the investors, which profits were accurately reflected on financial statements that the Debtor provided to them. *See* Crosser Decl. at ¶ 23. The Debtor engaged in legitimate investment activities, engaged in due diligence concerning potential investments, and took actual positions in legitimate investments. *See* Crosser Decl. at ¶ 24. Such conduct rebuts Plaintiff's assertion that every investment and transfer of the Debtor was part of the alleged Ponzi scheme.

b. <u>Plaintiff Cannot Prove That The Transfers Were Concealed</u>

Another element of Plaintiff's claims is that the transfers to his investors were concealed from other creditors. Plaintiff fails to mention this element in the Motion. Perhaps such omission is related to the fact that the investors were perfectly aware that other investors were receiving distributions. *See* Hutchins Decl. at ¶ 7. Thus, Plaintiff is unable to prove the "concealment" elements of his claims. In light of the foregoing, Plaintiff has not established the probable validity of his actual intent claims.

c. <u>Plaintiff Offers No Admissible Evidence To Prove Actual Fraud.</u>

Plaintiff briefly refers to two statements made by the Debtor that he was running a Ponzi scheme to prove actual fraud – his plea bargain and a declaration in support of an ex parte application for a right to attach order filed against a defendant in a similar adversary proceeding. These statements are insufficient to demonstrate actual fraud at this stage of this adversary proceeding. Defendants object to the admissibility of the plea bargain. *See* Defendants' Objection To Admissibility Of Declaration Of Grant M. Newton, filed and served concurrently herewith. The plea bargain obviously contains some statement of Slatkin's liability. Slatkin's admissions,

however. must be scrutinized more closely considering that he made the statement to avoid certain criminal prosecution and prison time.

Even the slightest appreciation for the pressures created by the Federal Sentencing Guidelines (the "Guidelines") and by Slatkin's guilty plea mandates the conclusion that his statements are being made solely for the purpose of demonstrating to the United States Attorney and to the United States District Court the level of his "extraordinary cooperation." Slatkin faces an as yet to be scheduled sentencing at which the District Court will be required to sentence him to what can only be a very long, multi-year sentence. As is obvious from the plea agreement itself, Slatkin's only hope of reducing the length of his sentence will be to demonstrate to the U.S. Attorney and to the District Court that he has given what is known under the Guidelines as "extraordinary cooperation" justifying a favorable recommendation under paragraph 5(K)(1). In order to quality for a 5(K)(1) downward departure from the presumptive Guideline range, Slatkin is highly motivated to say whatever he needs to say, and to do whatever he needs to do, to assist in carrying out the Government's objectives – particularly its objective of recovering large amounts of money in order to pay "restitution" to the "victims" of his fraud scheme. Given the overwhelming reasons for anyone in Slatkin's position to depart from the truth in order to improve his changes of securing his liberty, anything he says must be carefully evaluated. In this case the reliability of what Slatkin has had to say has not yet been tested.

Defendants have not had the opportunity to cross-examine or otherwise depose the Debtor in connection with his statements in his plea bargain, so this issue has not even been discussed as between the parties to this litigation. *See* Declaration Of Howard Kollitz In Support Of Opposition To Application For Right To Attach Order And Order For Writ Of Attachment (the "Kollitz Decl.) at ¶¶ 2 – 7. The documents that would be necessary to demonstrate the fundamental falsity of his statements have not been made available despite repeated requests by counsel. Id.

Also, the issue of whether Slatkin was running a Ponzi scheme was never actually litigated or decided by a jury – two essential elements for collateral estoppel. Additionally, collateral estoppel cannot be used here as a "sword" where Defendants were not parties to the criminal action in which the plea bargain was entered. Furthermore, to accept the plea bargain on its face as

establishing an issue in this case would fly in the face of Defendants' rights of due process and is effectively issue preclusion without establishing the numerous elements of collateral estoppel.

In the absence of an opportunity appropriately to test Slatkin's veracity, it is exceptionally important to observe the extent to which there is any independent corroboration for his statements. None can be found in Plaintiff's papers filed in this case. The only other documentary basis offered by Plaintiff is the Newton Decl. The Newton Decl., however, provides no independent evidence of any type to support Slatkin's statement. No forensic evaluation is revealed by the Newton Decl. To the contrary, all he has done is to collect and to provide arithmetic summaries of records. Those records themselves do not in any way demonstrate the existence of fraud and Mr. Newton does not so claim. Even the arithmetic work itself is flawed, but the important point is that it affords no weight to support the Debtor's statements. Slatkin stands alone and is entitled to no credit at this stage of the litigation.

With respect to the Debtor's declaration in support of Plaintiff's ex parte application for a right to attach order in the adversary proceeding Neilson v. Hitchman, et al., adversary proceeding number AD 02-01111-RR, Plaintiff's use of the declaration here is troubling at best. As a preliminary matter, Defendants object to its inclusion as evidence in this matter on the grounds of relevance. *See* Defendants' Objection To Admissibility Of The Declaration Of Reed E. Slatkin, filed and served concurrently herewith. The information contained in the declaration expressly relates to the actions of the defendant therein, Anthony Hitchman, not these Defendants. There is not a single reference to these Defendants in the Hitchman-case declaration whatsoever. The absence of a declaration from the Debtor with respect to the present Application begs the inquiry as to why such a declaration was not included. Similar to the plea bargain, the Defendants have not been allowed to question the Debtor about the statements contained in the Hitchman-case declaration. *See* Kollitz Decl. at ¶¶ 2 – 7. Plaintiff should not be allowed to cast the same shadow on every defendant that he has sought to cast on Anthony Hitchman.

Furthermore, some of the Debtor's statements in the Hitchman-case declaration are entirely untrue. For example, the Debtor states that Mr. Hitchman and Jack Dirmann physically restrained the Debtor from leaving Mr. Hitchman's home in March 2001 unless the Debtor executed a

document acknowledging that the Debtor was holding Earthlink stock for Mr. Hitchman. The true facts, however, are that such meeting did not occur as claimed by Slatkin. *See* Declaration Of Jack Dirmann In Support Of Opposition To Application For Right To Attach Order And Order For Writ Of Attachment. As such, the inclusion of the Hitchman-case declaration in this case is wholly inappropriate and it should not be viewed by the Court as evidence demonstrating the probable validity of Plaintiff's underlying claims.

2. Constructive Fraud

Plaintiff contends that by virtue of alleging that the Debtor ran a Ponzi scheme, he can demonstrate the probable validity of his claims. This is simply not true. As explained hereinabove, whether the Debtor was involved in a Ponzi scheme with respect to the transfers allegedly made to Defendants is an issue to be determined in this case. Plaintiff contends that the Debtor received no or reasonably equivalent value for the transfers allegedly made to Defendants, merely because of the allegation of a Ponzi scheme. Plaintiff's argument ignores several of Defendants' affirmative defenses and the underlying facts, which serve as a bar to Plaintiff's recovery.

a. Payment Of An Antecedent Debt Constitutes Value.

Slatkin was liable to investors for fraud and breach of contract, as well as for the use of their money. His payments partially satisfied these obligations. Therefore, his payments were made on account of his antecedent debt to the investors. The relationship between Slatkin and his investors was that of debtor and creditor, and the incidents of that relationship are determined by state law. *See* Raleigh v. Illinois Dept. of Revenue, 530 U.S. 15, 24-25 (2000) (debtor's obligation to the Illinois Department of Revenue for use taxes was governed by state's tax code, including the burden of proof under that statute); Butner v. United States, 440 U.S. 48, 55 (1979) ("Property interests are created and defined by state law.").

Under California law, Slatkin's investors had claims against him in tort and contract in excess of the payments they received. California courts recognize that tort damages are permitted in contract cases where the contract was fraudulently induced. *See* Lazar v. Superior Court, 909 P. 2d 981, 985 (Cal. 1996). Under California law, the false reports from Slatkin to investors

c. Slatkin Made Some Legitimate Investments

While some of the Debtor's investment choices may have been unwise or imprudent, the Trustee's own First Interim Report Of The Trustee And The Creditors Committee Under 11 U.S.C. §§ 1103, 1106(a) (3)-(4) (the "Report") acknowledges that some of the Debtor's investments did return a substantial profit (e.g., the Earthlink stock). *See* Report at p. 10, lns. 8 – 14. Thus, there is at least an inference that the Defendants gave value to the Debtor (in the form of funds transferred to him) in return for the transfers allegedly returned.

Plaintiff ignores several important facts in arriving at his incorrect conclusion that he has sufficiently demonstrated the probable validity of his underlying claims. First, not all of the investments that the Debtor made were made on behalf of the pool of investors for which the Debtor invested. *See* Crosser Decl. at ¶ 23. The Debtor made a number of investments that resulted in actual profit to the investors, which profits were accurately reflected on financial statements that the Debtor provided to them. *See* Crosser Decl. at ¶ 23. Accordingly, the Debtor would have received "reasonably equivalent value" with respect to these investments.

Second, Plaintiff also ignores that the Debtor was solvent during certain periods of time during which Plaintiff contends Defendants received transfers. Plaintiff alleges that "...by virtue of running a Ponzi scheme, and thereby paying Defendants and other investors high rates of 'return,' Slatkin knew that he was incurring debts far greater than he would be able to pay." *See* Motion at p.6, lns. 6 – 8. Plaintiff is required to lay a proper foundation for any factual evidence in support of the Application. Yet, Plaintiff does not cite to a single source that contains facts supporting such a contention. As such, there is no evidence that the Debtor knew that he was incurring debts far greater than his ability to pay. However, in light of the $100 million success with the Earthlink stock and other successful investments, there is evidence that the Debtor could have been in a position to pay off his debts as they became due and payable. Based on the limited public information available to Defendants (by virtue of Plaintiff's unwillingness to exchange documents), it appears that during certain periods during which Defendants received payments from Slatkin, he would have been able to pay a substantial portion, if not all, of his investors in full if he had liquidated his holdings in Earthlink alone. Although Plaintiff has argued that the

Earthlink stock may have contained restrictions on its sale, such restrictions could have been removed to facilitate the liquidation of the stock. Furthermore, the Debtor had other profitable investments that could have been liquidated to pay creditors' claims. *See* Crosser Decl. at ¶ 25.[1] In light of the foregoing, Plaintiff is unable to demonstrate that the Debtor was incurring debts that he was unable to pay during all of the time periods referenced in Plaintiff's complaint.

d. Slatkin Had The Right To Use His Funds To Satisfy Any Legitimate Debt.

Plaintiff contends that all "profits" received by investors are "the fruits of fraud" and recoverable under the UFTA. In reality, Plaintiff is attempting to transform fraudulent conveyance law into an expanded preference statute (i.e., one with a 7-year, rather than 90-day, "reachback" period). The policy behind fraudulent conveyance law is to prevent unjust diminution of the bankruptcy estate by assuring that the debtor received adequate consideration for the transfer. United Energy Co., 944 F.2d at 597. "This policy differs from that which undergirds the law of preferences. The aim of preference law under the Bankruptcy Code is to guard all parties by promoting equal distribution of the debtor's estate." Id.

A payment to a creditor in full or partial satisfaction of the debt is not a fraudulent transfer, regardless of the debtor's motives. *See* Cal. Civ. Code § 3432 ("A debtor may pay one creditor in preference to another, or may give to one creditor security for the payment of his demand in preference to another."); 1 G. Glenn, Fraudulent Conveyances And Preferences § 289, at 488-89 (rev. ed. 1940) ("If there is in our law one point which is more ungrudgingly accepted than others, it is that the preferential transfer does not constitute a fraudulent conveyance.").

The settled principle that a payment to one creditor in preference to others is not a fraudulent transfer is eminently sensible: "To allow such a creditor, acting alone, to set aside a preferential transfer as one in fraud of creditors would amount to substituting that creditor as the

[1] Due to Plaintiff's unwillingness to exchange documents and allow Defendants to depose the Debtor, Defendants is unable to provide documentary evidence that demonstrates the profitability of the Debtor's other investments.