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UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

COMMODITY FUTURES TRADING COMMISSION, **Plaintiff,** **vs.** **EQUITY FINANCIAL GROUP, LLC, TECH TRADERS, INC., TECH TRADERS, LTD., MAGNUM INVESTMENTS, LTD., MAGNUM CAPITAL INVESTMENTS, LTD., VINCENT J. FIRTH, ROBERT W. SHIMER, COYT E. MURRAY, and J. VERNON ABERNETHY** **Defendants.**	)	**Civil Action No.: 04CV 1512** **Honorable Robert B. Kugler** **Hearing Date: February 18, 2005**

MEMORANDUM IN SUPPORT OF MOTION OF EQUITY RECEIVER FOR AUTHORITY TO MAKE INTERIM DISTRIBUTION ON ACCOUNT OF INVESTOR CLAIMS

Stephen T. Bobo (the "Receiver"), the Equity Receiver of Defendants, Equity Financial Group, LLC, Tech Traders, Inc., Tech Traders, Ltd., Magnum Investments, Ltd., Magnum Capital Investments, Ltd., Vincent J. Firth, and Robert W. Shimer, submits this memorandum in support of his motion for authority from this Court to make an interim distribution of estate funds on account of investor claims. In support of his motion, the Receiver states as follows:

A. The Claim Process

1. This Court appointed the Receiver as part of the initial restraining order entered on April 1, 2004. The responsibilities of the Receiver include taking control of the Defendants' assets frozen by the Court and determining how they should be distributed.

2. Pursuant to authority from this Court, the Receiver has carried out an investor claim process, which requires all persons who invested funds with the Defendants to submit proofs of claim to the Receiver in order to receive a distribution from the receivership estate. Proofs of claim were required to be accompanied by documentary proof of all funds invested with and received from the Defendants. A copy of that order is attached hereto as Exhibit A.

3. The Receiver has reviewed the 103 proofs of claim and the supporting documentation submitted by investors. In many cases, the claim form or the documentation was incomplete, which caused the Receiver to contact the claimant and seek additional information.

4. Only 89 of the claims submitted can be considered as part of the proposed distribution.[1] Of that number, the Receiver presently agrees with 49 claims, based upon the information the investors submitted and the information otherwise available concerning the Defendants' investment activities. The current list of agreed claims is attached hereto as Exhibit B.

5. The Receiver does not currently agree with the remaining 40 claims. A list of those claims is attached hereto as Exhibit C. In certain cases, the Receiver is awaiting additional information from the investor before the claim can be agreed to. In other cases, the Receiver has received sufficient information but does not agree with the proof of claim either in full or in part.

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[1] Of the total of 103 proofs of claim received, 3 persons acknowledge they did not actually invest with the Defendants, 2 investors made their entire investments after the initial freeze order, and 9 investors were already included as part of the claim forms submitted by an investment group that had invested directly with Tech Traders or Shasta. Therefore, the proposed plan of interim distribution and the attached Exhibits B and C only include a total of 89 claims.

In those latter cases, the Receiver intends to file a formal claim objection for resolution by this Court.

B. The Receiver's Preliminary Conclusions Regarding The Defendants' Investment Activities

6. The Receiver and his attorneys and accountants have spent considerable time investigating the investment activities of the Defendants. These efforts have included obtaining and reviewing the paper and electronic records of Equity Financial Group, LLC, Shasta Capital Associates, LLC ("Shasta"), the Tech Traders and Magnum entities and Robert W. Shimer ("Shimer") and Vincent J. Firth ("Firth"). The Receiver's accountants have reviewed and summarized the records of nearly 50 bank and trading accounts used by the Defendants in their investment activities. The Receiver has interviewed numerous investors, as well as Defendants Shimer and Jack Vernon Abernethy. The Receiver also participated in the depositions taken in the case.

7. Based on the investigatory work done, the Receiver has gained a general understanding of the investment activities of the Defendants.[2]

i. The Magnum Entities

8. Defendant Coyt E. Murray ("Murray") operated a commodity trading investment company known as Magnum Investments, Ltd. ("Magnum") beginning some time before 1998. Magnum offered outside investors an opportunity to participate in commodity futures trading. Investors would place funds with Magnum by what were typically structured as unsecured loans. Magnum promised that they would receive a significant amount of interest on those funds plus one-half of the profits realized by Magnum from trading those funds. Magnum had several

[2] These conclusions are necessarily preliminary and certain details may be subject to revision because discovery is ongoing and other investigatory work continues as well. However, the Receiver is satisfied that the conclusions expressed are substantially accurate.

commodity futures trading accounts with Refco, LLC, a futures commission merchant or brokerage firm located in Chicago, Illinois. Magnum transferred much of the funds it received from investors to the Refco accounts.

9. Magnum's bank records show that it took in a total of approximately $5.4 million from sources other than Tech Traders since January 1998. Magnum had a sister company known as Magnum Capital Investments, Ltd., apparently organized as a Bahamian-based entity for international funds. It is unclear whether Magnum Capital Investments, Ltd. had a bank account. The only account identified in which it may have had an interest does not appear to have been a large one and was with a Bahamian bank that was itself shut down in March 2001.

10. Although investors were apparently informed that Magnum's trading activities had been significantly profitable, the Magnum accounts at Refco lost a total of $2.9 million in commodity trading between February 1998 and May 2002. One of those accounts was in the name of Magnum Capital Investments, Ltd., and it had losses of approximately $190,000 over that period.

ii. The Tech Traders Entities

11. For reasons not yet fully known by the Receiver, the Magnum investment and trading activities appear to have been phased out during the period of early 2001 through the middle of 2002. After that point, Magnum continued to receive regular transfers of funds from Tech Traders, which it disbursed to a variety of payees. Many of those disbursements are still under review by the Receiver and his accountants.

12. During that same period, Coyt E. Murray began similar operations through the two Tech Traders entities. The principal place of business of Tech Traders, Inc. was the Gastonia, North Carolina premises used by Magnum, and it conducted commodity trading

activities similar to what Magnum had done. Many of the Tech Traders investors placed funds with Tech Traders in transactions styled as loans in return for a fixed amount of interest plus a substantial share of the trading profits, similar to the Magnum investment activities.

13. Another Tech Traders entity, Tech Traders, Ltd., was established ostensibly to handle foreign transactions in Nassau, Bahamas. However, little or no actual business appears to have been done through that entity. No financial records or trading accounts have been identified for Tech Traders, Ltd., and the only bank account found in its name is with a Bahamian bank that was shut down and placed under the control of a provisional liquidator in March 2001. Although certain investors signed investment agreements bearing the name of Tech Traders, Ltd., their funds were deposited in a commingled Tech Traders, Inc. bank account and some or all of those funds were transferred to trading accounts maintained in the name of Tech Traders, Inc. Therefore, it appears that Tech Traders, Ltd. had no separate economic existence and no distinction should be made between the two Tech Traders entities for purposes of distributing receivership funds to the investors.

14. A total of approximately $43.2 million was invested with Tech Traders from April 2001 through April 1, 2004. Approximately $13.9 million of that amount came from Shasta. Another total of approximately $15.9 million was put into Tech Traders by the various Sterling entities. The largest portion of this Sterling amount appears to represent funds invested with or through the Sterling entities by non-insiders of Sterling. New Century Trading LLC, a much smaller commodity pool for international investors controlled by Defendant Shimer, invested another approximately $273,000 with Tech Traders. The balance of the funds invested with Tech Traders was from approximately 13 other investors who have no apparent ties to

Shimer, Firth or the Sterling entities. Many of those other investors consist of groups of individuals who pooled their funds for investment with Tech Traders.

15. Tech Traders used the $43.2 million it received in approximately the following ways:

Approximate Uses Of Funds By Tech Traders[3]	
Net Trading Losses	$ 7.4 million
Repayments to Investors (including Shasta and the Sterling entities)	$12.0 million
Transferred to affiliate Magnum	$ 2.4 million
Operating Expenses (including payments to or on behalf of members of the Murray family and commissions)	$ 1.8 million
Transferred to Kaivalya Holding Group, Edgar Holdings and Equity Financial Group	$ 2.2 million
Unknown or not yet categorized	$ .1 million
Remaining as of April 1, 2004 in Tech Traders' accounts	$17.5 million

16. There is no evidence of profitable economic activity undertaken by Tech Traders. Accordingly, the only funds that Tech Traders used to repay its investors or for any of the other purposes were the funds received from its various investors.

17. Tech Traders regularly reported substantial trading profits to its investors. Shasta and at least some of the other groups that invested with Tech Traders in turn reported the supposed profit amounts to their own respective investors.

[3] These are updated estimated figures which are not yet final but will continue to be refined as the accounting work is finalized. Totals do not add up to $43.2 million due to rounding.

iii. Shasta and Equity Financial Group, LLC

18. Shasta was a commodity pool operated by Shimer and Firth. It was organized in mid-2001 and began accepting investor funds at the beginning of 2002. The managing member of Shasta was Equity Financial Group, LLC, which was also controlled by Defendants Shimer and Firth. Shasta took in approximately $14 million from investors, deducted a 1 percent charge for expenses and sent the balance to Tech Traders to fund trading in the commodity futures markets. Shasta did not place any of the funds received from its investors in any other investments. Shasta had approximately 70 investors. Shasta received back approximately $1.6 million from Tech Traders, and it disbursed this amount to certain of its investors.

C. The Timing and Amount of the Initial Distribution

19. The Receiver has considered the following issues in the context of this case in formulating and recommending a plan of distribution to the Court:

- The timing of the distribution;
- The total dollar amount of an initial distribution;
- Whether to disregard profits or earnings reported by the Defendants in determining claim amounts;
- Whether to distribute the funds pro rata or according to tracing principles;
- How to treat amounts already repaid to investors;
- Whether multiple accounts in which an investor holds a beneficial interest should be aggregated for purposes of distribution;
- Whether funds invested after the initial freeze order should be returned to the investors; and

- In the cases of investors that are themselves investment groups, how to ensure that those groups in turn fairly allocate the distributions among their members.

20. The Receiver is holding approximately $17,750,000, which was transferred from accounts in the name of Tech Traders and from the Shimer escrow account used for Shasta. Those funds are held in receivership interest-bearing accounts. The Receiver also holds another nearly $2 million in a frozen account at Man Financial in the name of Sterling Trust (Anguilla), Ltd. The Receiver seeks authority to make an initial distribution of approximately $10.4 million to investors of Tech Traders and Shasta at this time.

21. The Receiver believes that only a partial distribution should be made at this time for a number of reasons. The investigatory efforts of the Plaintiff CFTC and the Receiver are ongoing. Additional investors could be identified in the future who have not been notified of the claim process and therefore have had no opportunity to submit proofs of claim. Certain of the investors' claims are disputed and there is no good reason to wait until all objections are resolved before making a distribution. There has not yet been a comparable claim process for creditors of the Defendants, and funds need to be held back to be able to treat any such claims fairly.[4] Funds must also be reserved to satisfy the continuing costs of administering this receivership estate.

22. Finally, funds also need to be reserved for the possibility that the Court may later determine that the Magnum entities should be consolidated with Tech Traders for purposes of distribution, thereby requiring any outstanding Magnum investors and creditors to share in the receivership funds. The Receiver does not yet have all of the records of Magnum and cannot identify all of the Magnum investors and creditors or determine whether they are still owed

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[4] Based on the records reviewed by the Receiver, trade creditor claims are estimated to total only a small fraction of the total amount of the investors' claims.

anything by Magnum. No claim process has yet been instituted for Magnum investors or creditors. However, the Receiver has determined from an initial review of the Magnum bank records that approximately $5.4 million was deposited into its bank account from outside sources after January 1, 1998, not including the $2.4 million that Tech Traders transferred to Magnum. Additional information is expected from further analysis of Magnum's accounts and records handled. Therefore, at this time the Receiver recommends, out of an abundance of caution, that sufficient funds be reserved for the possibility that the Court might later direct a comparable distribution be made from the receivership estate on account of investor and creditor claims against Magnum.

23. As the Magnum situation becomes clearer, the Court will be in a position to determine whether Magnum should be consolidated with Tech Traders for purposes of distribution or be treated separately.

D. Issues to Resolve Regarding the Proposed Distribution

24. A number of issues require resolution in determining how to distribute the receivership funds. A threshold issue is whether to recognize claims for profits, interest or other earnings shown on investors' account statements or instead to allow claims only for the actual dollar amount invested. The circumstances of this case strongly support ignoring "paper" profits and allowing claims based only on funds actually invested. Tech Traders ran a classic Ponzi scheme operation where relatively large gains were reported to investors even through the economic activities of the company actually resulted in large losses. Since there were no actual gains, it would be inequitable to give some investors credit for them in determining how to divide up the limited receivership funds. To recognize such gains would cause recent investors (whose accounts had supposedly accrued little or no profits) to give up a share of the money they

actually invested in order to fund a return of fictitious profits to earlier investors (whose accounts would have supposedly accrued relatively large profits). Courts have rejected this approach in similar circumstances. See, e.g., In re Tedlock Cattle Co., 552 F.2d 1351, 1353-54 (9th Cir. 1977); In re Young, 294 F. 1, 4 (4th Cir. 1923).

i. Tracing or Pro Rata Distribution

25. The Receiver also has considered whether all allowed claims should share in the distributions pro rata or whether the investors who put their funds in last and can trace their investments to the frozen funds ought to be allowed to recover them in full, even though this result might leave little or nothing for the remaining investors.

26. The Receiver proposes a pro rata distribution to the claimants who hold allowed claims, all of whom are similarly situated. Each claimant invested money with the Defendants before April 1, 2004 when the CFTC initiated this action,[5] each expected a return on that investment from the same underlying trading activities, and each awaits relief from the Receiver, who controls assets insufficient to repay the claimants in full. Under the facts of this case, law and equity favor a pro rata distribution.

27. In the seminal "Ponzi" scheme case, the United States Supreme Court held that equity dictates that all victims of the fraud be treated equally. Cunningham v. Brown, 265 U.S. 1, 12-13 (1924). In that case, defrauded creditors sought to establish a presumption that Charles Ponzi wrongfully converted funds in the order in which investors invested the funds.[6] Id. at 12. They argued that they should be permitted to trace their funds and should be paid distributions

[5] The Receiver's recommended treatment of the claimants who invested funds after April 1, 2004 is discussed *infra*, ¶¶ 45-47.

[6] This "first in, first out" method emerged from Clayton's Case, 1 Merivale 572 (1816 Ch.), wherein the English court established the rebuttable presumption that the trustee wrongfully converted the victims' funds in order in which they were paid in.

under the "first in, first out" method – i.e., the funds first invested with Ponzi should be considered to be the funds he had first lost or paid out to subsequent investors. Id. Therefore, the funds remaining when the fraudulent scheme collapsed would belong to those who put their money in last. Id. The Supreme Court rejected this argument and concluded, instead, that all creditors occupied the same legal position for purposes of receiving a distribution. Id.

28. This fundamental principle – that, in any distribution, similarly situated investors must be treated alike so as to preserve equity and fairness – has withstood the test of time. E.g., SEC v. Credit Bancorp, Ltd., 290 F.3d 80, 88-89 (2d Cir. 2002); Commodity Futures Trading Comm'n v. Topworth Int'l, Inc., 205 F.3d 1107, 1115-16 (9th Cir. 1999); United States v. Vanguard Inv. Co., 6 F.3d 222, 226-28 (4th Cir. 1993) SEC v. Elliott, 953 F.2d 1560, 1569 (11th Cir. 1992), rev'd in part on other grounds, 998 F.2d 922 (11th Cir. 1993) Cf. In re Harvey Goldberg v. New Jersey Lawyers' Fund for Client Protection, 932 F.2d 273, 280 (3d Cir. 1991) (concluding, in a bankruptcy proceeding, that a pro rata distribution of funds is generally favored among similarly-situated creditors). Courts have recognized that a pro rata distribution is especially appropriate for victims of a "Ponzi" scheme in which "earlier investors' returns are generated by the influx of fresh capital from unwitting newcomers rather than through legitimate investment activity." See SEC v. Credit Bancorp, Ltd., No. 99 CIV 11395 RWS, 2000 WL 1752979, at *13 (S.D.N.Y. Nov. 29, 2000) (citing Cunningham, 265 U.S. at 12-13), aff'd. 290 F.3d 80 (2d Cir. 2002).

29. The Receiver considered the feasibility and effectiveness of allowing investors to trace their investments but rejected such an approach as both arbitrary and inequitable. Consistent with Cunningham and its progeny, tracing fictions would be inappropriate in this case, which involves multiple victims of fraud whose funds Defendants have commingled.

Allowing one defrauded claimant to recover at the expense of another merely because the former has the good fortune of being able to trace his or her funds would be unjust. See SEC v. Credit Bancorp, Ltd., 194 F.R.D. 457, 463-64 (S.D.N.Y. 2000). Most Courts of Appeals also have expressly rejected tracing as a method of distribution in similar cases. See Credit Bancorp, Ltd., 290 F.3d at 88-89; United States v. 13328 and 13324 State Highway 75 North, 89 F.3d 551, 553-54 (9th Cir. 1996); United States v. Durham, 86 F.3d 70, 73 (5th Cir. 1996); Vanguard, 6 F.3d at 226-28; Elliott, 953 F.2d at 1569; Ruddle v. Moore, 411 F.2d 718, 719 (D.C. Cir. 1969). In the words of Judge Learned Hand: "When the law adopts a fiction [such as the 'first in, first out' method of tracing], it is, or at least it should be, for some purpose of justice. To adopt it here is to apportion a common misfortune through a test which has no relation whatever to the justice of the case." In re Walter J. Schmidt & Co., 298 F. 314, 316 (S.D.N.Y. 1923).

30. For several reasons, the Receiver also proposes the same pro rata distribution for those claimants holding allowed claims who invested funds with Shasta shortly before the freeze order where those funds remained in Shasta's account *at the time of the freeze order* and therefore had never been actually transferred to Tech Traders. First, the Defendants who operated Shasta have a history of close dealings with Tech Traders and, at this time, it is unclear how much (or how little) these Defendants knew about the Ponzi scheme.[7]

31. Second, Shasta engaged in no investment activity except through Tech Traders and exercised no discretion over the investor funds it received merely as a conduit to Tech Traders (with the exception of deducting 1 percent for legal and accounting fees from the amounts invested with it).[8]

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[7] In fact, at times Shimer served as counsel for Murray and Tech Traders.

[8] According to the Shasta Capital Associates Confidential Private Placement Memorandum: "Ninety nine percent (99%) of the proceeds from the offering shall be invested by the Manager for the benefit of

32. Third, all who invested with Shasta did so for the sole purpose of participating in its commodity futures trading account with Tech Traders. Consequently, all Shasta investor funds were effectively "at risk" as soon as the funds were deposited with Shasta. Only the fortuitous entry of the freeze order on April 1, 2004 prevented these funds from being commingled with Tech Traders' funds. Shasta investors whose investments were the source of the funds remaining in the Shasta account at the time of the freeze order therefore should be entitled to the same pro rata share of the remaining receivership funds as other investors.

ii. How to Treat Withdrawal Amounts Already Received by Investors

33. Another important issue is how each investor's distribution should be affected by any withdrawals the investor received from the Defendants before April 1, 2004. Some investors received back the entire amount they invested,[9] some received a portion of the amount they invested, and some received no withdrawals. Alternative means of treating the withdrawals already received from the Defendants include the following:

a. Withdrawals already received should be ignored and each investor should receive a distribution based on the full amount invested;

b. Withdrawals already received by each investor should be subtracted from the total amount invested and investors' claims should be allowed for those net amounts;

c. Each investor's claim should be allowed for the full amount invested but the amount of the distribution to be made by the receivership estate on that

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the Company's members. The remaining 1% shall be applied to legal and accounting fees associated with preparation of this Offering."

[9] Some investors appear to have received back more funds than they invested. This is a separate issue that gives rise to claims on behalf of the receivership estate to recover those returns of "profits" for the benefit of all other investors.

claim should be reduced by the total amount of withdrawals already received; and

d. All withdrawals are repaid to the receivership estate and then redistributed equally. Investors must repay all withdrawals received back to the receivership estate before their respective claims can be allowed for the full amounts invested.

34. The Receiver believes that the first and last of these alternatives are clearly inequitable and will lead to undesirable results. The first alternative is rejected because it would totally disregard payments already received. Although this has the virtue of simplicity, the failure to consider withdrawals already received in a Ponzi scheme case would lead to clearly inequitable results. Certain investors who have already received back most or all of their funds would share the same percentage distribution on all amounts invested with other investors who have received back little or nothing. This approach could cause the Receiver to make distributions to some investors of more than they invested, while others would receive back only a fraction of what they invested.

35. At the other extreme, the last alternative listed above attempts to achieve perfect equality through recovery of all withdrawals received and redistribution of those amounts back to the investors pro rata. Although perhaps laudable in theory, it would be far from perfect in practice here. Since the investors are primarily individuals or investment partnerships, not large corporate entities, in many instances recovery will be at least difficult and not cost-effective as a practical matter. The legal basis for recovering such withdrawals which did not exceed the amount invested also seems questionable to the extent that investors received them in good faith, without knowledge of any fraud and in exchange for value provided to the Defendants. Finally,

the cost of such recovery and redistribution efforts would likely dwarf any actual benefits realized without coming close to achieving perfect equality of distribution among the investors. For all of these reasons, the Receiver does not recommend this alternative.

36. The Receiver believes that both the second and third approaches deserve further consideration. After weighing the merits of the second, or "net investment," and the third, or "rising tide," alternatives[10] for treating withdrawals in calculating the pro rata distribution in the context of this case, the Receiver believes that the third, or "rising tide," method is more equitable. This method would allow investors to retain the withdrawals they received, but require that those withdrawals be credited against the investors' respective pro rata shares calculated based on the full amounts invested. Thus, distributions would be calculated according to the following formula: (actual dollars invested x pro rata multiplier) - withdrawals previously received = distribution amount. Under this approach, the Receiver would make distributions at this time only to investors with a positive result applying the above formula, i.e., investors who already received withdrawals less than their respective calculated distribution amounts. Investors who already received withdrawals in excess of their respective calculated distribution amounts would receive no distribution at this time.

37. This method is the most equitable in that it advances the goal of equal pro rata returns to similarly situated investors without causing the Receiver to attempt the difficult and likely expensive task of recovering all the withdrawals paid out and redistributing them equally. It will enable investors who did not receive withdrawals to receive a relatively greater return on

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[10] Courts frequently refer to these methods by other names. The "net investment" method has been referred to as the "net principal investment" approach, "Option 4," or the "Franklin method of distribution" because the district court adopted this method in Commodity Futures Trading Commission v. Franklin, 652 F. Supp. 163 (W.D. Vir. 1986), rev'd on other grounds sub nom., 875 F.2d 76 (4th Cir. 1989). The "rising tide" theory is most often referred to as "Option 3," again, based on the terminology employed by the Franklin court. Id. at 169.

their investment. In addition, as more receivership funds are later disbursed in a second distribution, resulting in a higher total percentage amount returned to investors, a larger number of investors will be entitled to share in the "rising tide" of those additional distributions. Two cases, in particular, recognize the many advantages of the "rising tide" method and authorize its use in determining distributions to investors. Commodity Futures Trading Comm'n v. Hoffberg, No. 93 C 3106, 1993 WL 441984, at *2-3 (N.D. Ill. Oct. 28, 1993); Commodity Futures Trading Comm'n v. Skorupskas, No. 83-CV-1885DT (E.D. Mich. Aug. 22, 1988). These unpublished decisions are attached as Exhibit D.

38. By contrast, the net investment method listed above as the second alternative would allow investors to retain all withdrawals already received, but they would be subtracted them from each investor's total cash investment before calculating each investor's pro rata share. Thus, distributions would be calculated according to the following formula: (actual dollars invested - withdrawals previously received) x pro rata multiplier = distribution. Most significantly, this method would cause the Receiver to distribute additional funds to investors who had already received back more than a proportionate share of their investments. This violates the basic principle of equality of distribution. E.g., Hoffberg, 1993 WL 441984, at *3. This method of distribution also fails to take into account the fact that the Defendants' fraud covered all funds, not just those remaining in the accounts on the day of the freeze order. Under the net investment method, an investor who had already received a withdrawal thus would benefit at the expense of other investors by retaining the benefit of the full amount of his withdrawal plus a distribution calculated on the basis of net funds invested, rather than the recommended distribution amount adjusted to take into account all amounts already received.

39. For the Court's convenience in evaluating the alternatives, the following example shows how each distribution alternative would work under the following assumptions: (i) three investors each contributed $100,000; (ii) Investor A received withdrawals totaling $50,000 from the Defendants prior to any distribution, Investor B already received $20,000 in withdrawals, whereas Investor C received no withdrawals; and (iii) a proposed interim distribution of 30 percent. The following chart shows the amount of interim distributions that Investors A, B, and C would receive under each method:

"Rising tide" method	**Net investment method**
Investor A has an allowed claim in the amount of $100,000. However, he will receive no additional distribution since he already received $50,000, which is greater than the $30,000 distribution that he otherwise would have been entitled to receive. Investor A's total percentage return of his investment is 50%.	Investor A has an allowed claim of $50,000 ($100,000 invested less the withdrawals already received totaling $50,000). Investor A would receive a distribution in the amount of $15,000, plus retain the $50,000; therefore, the total amount he would receive is $65,000, and Investor A's total percentage return of his investment would be 65%.
Investor B has an allowed claim in the amount of $100,000. The prior withdrawals he received of $20,000 are credited against his calculated distribution amount of $30,000. Consequently, Investor B receives $10,000 distribution for a total amount back of $30,000. Investor B's total percentage return of his investment is 30%.	Investor B has an allowed claim of $80,000 ($100,000 invested less $20,000 in withdrawals). Investor B would receive a distribution in the amount of $24,000 plus retain the $20,000. His total recovery would be $44,000, and his total percentage return of the investment would be 44%.
Investor C also has an allowed claim in the amount of $100,000. He will receive a distribution in the amount of $30,000, and Investor C's total percentage return of his investment is 30%.	Investor C will receive $30,000, and Investor C's total percentage return of the investment would be 30%.

40. Another important advantage of the recommended "rising tide" method not made explicit by the above example is that it provides a more effective remedy for those who need it

the most. By fully crediting for prior withdrawals, more funds will be available to distribute to those investors who received back little or nothing on their investments. Therefore, those investors will be able to receive a higher percentage return on their claims.

41. The Receiver proposes an initial distribution of 38 percent of each investor's total investment amount. Applying the "rising tide" method to account for previous withdrawals, the individual distribution amounts would be calculated according to the following formula:

a. For each claim, multiply the total amount actually invested by 38 percent to derive a gross pro rata amount for each investor (the "Gross Distribution Amount").

b. Any amount that the Defendants already paid as withdrawals to each investor is subtracted from its Gross Distribution Amount, leaving a Net Distribution Amount.

c. The Net Distribution Amount will be disbursed to investors whose claims have been allowed. The Net Distribution Amounts for claims that are not yet allowed will be reserved until such time as the claims are either allowed or disallowed. To the extent such claims are ultimately disallowed in full or in part by agreement or by order of this Court, the respective Net Distribution Amounts will be transferred from reserved funds back to general receivership funds.

42. The Receiver has determined from the financial analysis by his accountants and the claim forms submitted by investors pursuant to the Court's August 23, 2004 Order that investors sent a total of approximately $43.2 million to Tech Traders between April 12, 2001 and April 1, 2004. However, the total amount shown on claim forms for actual funds invested (and disregarding any claimed "profits" or "interest" shown on Defendants' account statements) is

$42,875,576.11.[11] The investors claim to have received a total of $8,182,094.12 in withdrawals before the freeze order. The Receiver holds a total of $17,747,511.74 as of December 30, 2004; however, this amount does not include interest accrued during the month of December 2004. In addition, funds remain frozen in account number 37923 at Man Financial which have a value of nearly $2 million. The initial distribution of 38 percent proposed by the Receiver would result in the withdrawal or reserve of approximately $10.4 million.[12] This $10.4 million represents nearly 60 percent of the funds now held in the name of the Defendants.

iii. Multiple Accounts of a Single Investor

43. For investors with ownership interests in multiple accounts in different capacities, the Receiver recommends that the transactions in those accounts be consolidated for purposes of calculating the distribution amount. By way of example, certain investors have invested with the Defendants both directly and through their IRA accounts. Any withdrawals they received in one such account ought to be taken into account in calculating the distribution amount in their other account. Otherwise, an investor who already received a return of all funds in one account would be entitled to a full pro rata distribution on his other account, resulting in receipt of a disproportionately large distribution compared to other investors who maintained only single

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[11] This amount does not include the $497,000 Shasta received after the freeze order. The Receiver proposes in Section D.iv. of this Memorandum to return nearly all of those funds to the respective investors.

[12] Exhibits B and C contain the distribution calculations illustrating the amounts each investor would receive by applying the "rising tide" method, assuming that their respective claims are allowed and that a 38 percent distribution is authorized. Exhibit B lists the following information for allowed claims: (1) claim identification, (2) the amount the investor deposited, (3) any withdrawals the investor received from the scheme before April 1, 2004, (4) the net cash balance for the claim, (5) The Net Distribution Amount, which is the actual amount the investor would receive from the Proposed Plan of Distribution, and (6) the cumulative percentage return from the Proposed Plan of Distribution as well as prior withdrawals. Exhibit C lists similar information for those investors whose claims are disputed at this time. Versions of these schedules that reveal the names of investors are filed separately under seal.

accounts with the Defendants. Therefore, all accounts in which an investor has a beneficial interest need to be aggregated to the extent of that beneficial interest in calculating the distribution amounts.

44. For investors who are members of a group of beneficial owners of a particular investor account, the account should be deemed to be owned in equal shares by its owners unless another ownership method is proven. For example, if such an account had three beneficial owners, each owner would be treated as owning a one-third share and receiving one-third of all withdrawals made by the Defendants.

iv. Return of Funds Deposited After the Freeze Order

45. Another distribution-related issue is the treatment of investor funds received by the Defendants after this Court froze their assets and suspended their operations on the afternoon of April 1, 2004. Several investors' funds were received in Shasta's account on April 2, 2004 and thereafter. Specifically, Dr. Marsha Green transferred $47,000 on April 2, 2004; Michael Duff's check in the amount of $200,000.00 was negotiated by Defendant Shimer on April 2, 2004;[13] Jolin Investments, LLC transferred $100,000.00 on April 5, 2004; and Broadtree Reinsurance Company, Ltd. transferred $150,000.00 on April 5, 2004. The total amount in question, $497,000.00, was transferred to the receivership account along with the other funds held in Shasta's Citibank account. These four investors have made demands upon the Receiver for the return of their funds.

46. In light of the express language of the Court's April 1, 2004 order, the Receiver

[13] Charles Schwab, as custodian for Michael Duff's IRA, issued this $200,000.00 check to Shasta Capital Associates, LLC just days before the April 1, 2004 Order. But Defendant Shimer did not endorse Mr. Duff's check and send it to Citibank for deposit into Shasta's account until April 2, 2004.

recommends that the post-freeze deposits of Jolin Investments, LLC, Broadtree Reinsurance Company, Ltd., and Michael Duff be returned in full. By directing the Receiver to "take all steps necessary to secure the business premises of the Defendants Firth and Equity Financial Group, LLC" and prohibiting all Defendants from "withdrawing, transferring, removing, dissipating or disposing of funds" held in their accounts,[14] the Court's order effectively serves as a legal impediment to any further business conduct by Equity Financial Group, LLC and Shasta, including attempts to deposit investor funds into Shasta's bank account. Accordingly, with the one exception discussed below, all funds deposited after entry of the order should be returned to the appropriate investors. Allowing these post-freeze deposits to become a part of the receivership assets and distributed pro rata among all investors would conflict with the specific directive of this Court's order and the general purpose of a freeze order, which is to "maintain the status quo and prevent additional losses to customers." E.g., Anderson v. Stephens, 875 F.2d 76, 78 (4th Cir. 1989).

47. The one exception to this recommendation is Dr. Marsha Green because of the source of her funds and because of the receivership estate's claims and setoff rights against her.

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[14] The April 1, 2004 freeze order states in pertinent part:

> Defendants Equity Financial Group LLC, Tech Traders, Inc., Vincent J. Firth, and Robert W. Shimer, and all persons insofar as they are acting in the capacity of their agents, successors, assigns, and attorneys, and all persons insofar as they are acting in active concert or participation with them who receive actual notice of such order by personal service or otherwise, shall be prohibited from directly or indirectly: *Withdrawing, transferring, removing, dissipating or disposing of funds, assets or other property, wherever situated, including but not limited to, all funds, personal property, money or securities held in safes, safety deposit boxes and all funds on deposit in any financial institution, bank or savings and loan account held by, under the control, or in the name of the Defendants including, but not limited to, any accounts in the name of or under the control of Shasta Capital Associates LLC.*

(April 1, 2004 Ct. Order at I.A) (emphasis added).

Although Dr. Green deposited an additional $47,000 with Shasta on April 2, 2004, the Receiver recommends that those funds continue to be held subject to a determination of the validity of her claim and the Receiver's objection to that claim. The Receiver's objections arise from her receipt of these, as well as a much larger amount of Tech Traders' funds, on account of an unrelated investment she made through Kaivalya Holding Group ("Kaivalya"), discussed more fully below.

v. Payments to Investors in Kaivalya and Edgar Holdings

48. In 1999, Robert Shimer introduced Dr. Green to an investment opportunity known as Kaivalya, which apparently intended to pool investor funds and use them, at least in part, for commodity trading through Magnum. Defendant Shimer was one of the persons who directed Kaivalya's activities. The Kaivalya funds apparently never actually reached Magnum and instead were improperly diverted to other uses. As detailed below, Dr. Green received the $47,000 withdrawal in question from Tech Traders' funds, in partial repayment of her Kaivalya loss, a short time before she deposited the amount with Shasta.

49. In 2002, Shimer arranged with Murray that Tech Traders would pay Shadetree Investment Trust ("Shadetree"), another Shimer-controlled entity, one-half of Tech Traders' 50% share of the net profits purportedly earned on Shasta funds each month. Beginning in July 2002 and each month thereafter, Shimer told Murray how much of Shadetree's portion of Tech Traders' share of the earnings for Shasta to send directly to various Shimer-controlled entities, including Kaivalya and Defendant Equity Financial Group, LLC. Since Tech Traders had no actual trading profits or other earnings, the funds it sent monthly to Kaivalya and the other Shimer-controlled entities necessarily came from the money that other people had invested with

Tech Traders. Kaivalya received a total of $1.3 million from Tech Traders between July 2002 and March 2004, and Kaivalya had no other significant source of funds during that period. Kaivalya used almost all of the funds received from Tech Traders to repay some (but not all) of its investors, including Dr. Green. Those repayments were not made on account of any funds actually invested with Tech Traders, or even invested with its predecessor, Magnum. Persons who did not invest with Tech Traders have no right to receive or retain funds that came from Tech Traders' investors.

50. Because Dr. Green's $47,000 came from Tech Traders through Kaivalya by check dated on or about March 18, 2004, her claim to that amount is subject to the Receiver's right of offset for his claim against her for the return of all funds she received from Tech Traders through Kaivalya. The total amount of the Tech Traders' funds she received from Kaivalya is $126,000. The Receiver recommends that the $47,000 not be returned to Dr. Green at this time and, instead, that it be held until the Court rules on the Receiver's objections to her claim.

51. Certain other claimants also received funds originating from Tech Traders as repayment of their earlier investments with Kaivalya and Edgar Holdings, Inc., another Shimer-controlled entity. The Receiver intends to object to the claims submitted by those investors as well.

vi. Ensuring Equitable Allocation of Distributions By Investment Groups Among Their Members

52. Another area of concern for the Receiver is ensuring that the various investment groups that invested with Tech Traders and Shasta allocate the distribution fairly and consistently among members of their respective groups. Although not parties in this case, they have voluntarily submitted themselves to this Court's jurisdiction by filing proofs of claim.

Those groups should be required to take into account withdrawals previously received by their respective members on account of their investments with the Defendants and to make their own pro rata distributions of any distributions received from the receivership estate.

53. The Receiver recommends that an authorized representative of each investment group be required to submit to the Receiver a proposed means of allocating the distribution funds among those having a beneficial interest in the funds. Upon review and approval of the proposed allocation of the investment group's distribution, the Receiver will release the group's share of the interim distribution. Any disputes concerning whether a proposed allocation is fair and equitable could be resolved by the Court. After the distribution is made, the investment group's authorized representative should be required to submit to the Receiver a declaration under oath attesting to the manner in which the investment group actually allocated the funds received from the estate, along with copies of the checks or other documents showing the disbursements made to the members.

WHEREFORE, the Receiver recommends, following written notice to all investors and an opportunity for objections to be filed and considered, that the Court: (i) approve the Proposed Plan of Distribution; (ii) authorize the Receiver to make 38 percent interim distribution totaling approximately $10,400,000 of receivership estate funds on account of allowed investor claims and reserve the distribution amounts corresponding to disputed investor claims until they are allowed, all in the manner detailed above and as set forth on Exhibits B and C hereto; (iii) authorize the Receiver to return the investor funds received after the freeze order, except the funds of Dr. Marsha Green; (iv) require representatives of claimants that are investment groups to submit for the Receiver's approval their proposed allocations of the distribution between their respective members and thereafter certify completion of the allocation approved by the Receiver;

and (v) grant such further relief to the Receiver as is equitable and appropriate under the circumstances.

DATED: January 7, 2005

Respectfully submitted,

STEPHEN T. BOBO
Equity Receiver

By: s/ Jeffrey A. Carr
One of his attorneys

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EXHIBIT A

UNITED STATES DISTRICT COURT
FOR THE
DISTRICT OF NEW JERSEY

COMMODITY FUTURES TRADING COMMISSION,	)	
Plaintiff,	)	
vs.	)	**Civil Action No.: 04CV 1512**
EQUITY FINANCIAL GROUP, LLC, TECH TRADERS, INC., VINCENT J. FIRTH, and ROBERT W. SHIMER,	)	**Honorable Robert B. Kugler**
Defendants.	)	

ORDER

This matter coming to be heard on the Motion of Stephen T. Bobo, Temporary Equity Receiver (the "Receiver"), to Approve Investor Claim Process and the Court having considered the contents of the motion and the evidence previously presented in this matter, and being fully advised in the premises,

IT IS HEREBY ORDERED THAT:

1. The Receiver is authorized and directed to distribute the claim forms and accompanying letter in the form attached hereto to all investors who may have invested funds with one or more of the Defendants through Shasta Capital Associates, LLC, through New Century Trading, LLC, and directly with Tech Traders.

2. In order to submit a valid claim to the funds held by the Receiver, investors must identify to the Receiver the nature and extent of their interest in the receivership assets, as well the identity of all persons having a beneficial interest of any kind in their account with the Defendants.

3. To participate in the claim process, investors must complete and return the claim form to the Receiver within thirty (30) days from the date of mailing out of the claim forms. Investors must also submit to the Receiver copies of the documents showing all funds invested with and received back from Defendants. Investors who fail to return these forms and the supporting documentation within this time

period will be barred from participating in the distribution of the receivership assets unless they can demonstrate to this Court good cause for the delay, all reasonable diligence in submitting the information at the earliest possible date thereafter, and absence of any prejudice to the receivership estate.

4. The Receiver will propose a plan of distribution to the Court upon notice to all investors. Any objections to the proposed distribution plan must be placed in writing, filed with this Court, and served upon the Receiver and the parties in the case no later than seven (7) days before the scheduled hearing on the proposed plan of distribution.

DATED: ~~July~~ August 23, 2004

BY THE COURT

United States District Judge

209393/0001/663269/Version #:.3

EXHIBIT B

Claim Number	Name of Claimant *	Funds Invested (per claim form)	Previous Disbursements (per claim form)	Net Cash Balance	Gross Distribution Amount	Net Distribution Amount	% Total Cumulative Distribution Received
1		$450,000.00	$0.00	$450,000.00	$171,000.00	$171,000.00	38.00%
2		$100,000.00	$0.00	$100,000.00	$38,000.00	$38,000.00	38.00%
3		$115,000.00	$0.00	$115,000.00	$43,700.00	$43,700.00	38.00%
6		$150,000.00	$0.00	$150,000.00	$57,000.00	$57,000.00	38.00%
7		$519,914.60	$0.00	$519,914.60	$197,567.54	$197,567.54	38.00%
8		$200,000.00	$0.00	$200,000.00	$76,000.00	$76,000.00	38.00%
9		$150,000.00	$0.00	$150,000.00	$57,000.00	$57,000.00	38.00%
11		$499,968.00	$0.00	$499,968.00	$189,987.84	$189,987.84	38.00%
12		$100,000.00	$100,000.00	$0.00	$38,000.00		
13		$675,000.00	$0.00	$675,000.00	$256,500.00		
	TOTAL:	**$775,000.00**	**$100,000.00**	**$675,000.00**	**$294,500.00**	**$194,500.00**	**38.00%**
14		$100,000.00	$0.00	$100,000.00	$38,000.00	$38,000.00	38.00%
15		$150,000.00	$0.00	$150,000.00	$57,000.00	$57,000.00	38.00%
16		$250,000.00	$0.00	$250,000.00	$95,000.00	$95,000.00	38.00%
17		$200,000.00	$0.00	$200,000.00	$76,000.00	$76,000.00	38.00%

* The Receiver intends to file Names of Claimants under seal with the Court.

as of January 7, 2005

Claim Number	Name of Claimant *	Funds Invested (per claim form)	Previous Disbursements (per claim form)	Net Cash Balance	Gross Distribution Amount	Net Distribution Amount	% Total Cumulative Distribution Received
18		$225,000.00	$0.00	$225,000.00	$85,500.00		
19		$150,000.00	$0.00	$150,000.00	$57,000.00		
	TOTAL:	**$375,000.00**	**$0.00**	**$375,000.00**	**$142,500.00**	**$142,500.00**	**38.00%**
27		$125,000.00	$156,487.00	($31,487.00)	$47,500.00	$0.00	125.19%
28		$100,000.00	$0.00	$100,000.00	$38,000.00	$38,000.00	38.00%
33		$100,000.00	$0.00	$100,000.00	$38,000.00	$38,000.00	38.00%
34		$200,482.00	$0.00	$200,482.00	$76,183.16	$76,183.16	38.00%
35		$136,000.00	$0.00	$136,000.00	$51,680.00	$51,680.00	38.00%
36		$100,000.00	$0.00	$100,000.00	$38,000.00	$38,000.00	38.00%
39		$95,000.00	$60,000.00	$35,000.00	$36,100.00	$0.00	63.16%
41		$100,000.00	$0.00	$100,000.00	$38,000.00		
42		$366,000.00	$366,000.00	$0.00	$139,080.00		
	TOTAL:	**$466,000.00**	**$366,000.00**	**$100,000.00**	**$177,080.00**	**$0.00**	**78.54%**
44		$200,000.00	$0.00	$200,000.00	$76,000.00	$76,000.00	38.00%
45		$350,000.00	$0.00	$350,000.00	$133,000.00	$133,000.00	38.00%
53		$400,000.00	$0.00	$400,000.00	$152,000.00	$152,000.00	38.00%

* The Receiver intends to file Names of Claimants under seal with the Court.

Claim Number	Name of Claimant *	Funds Invested (per claim form)	Previous Disbursements (per claim form)	Net Cash Balance	Gross Distribution Amount	Net Distribution Amount	% Total Cumulative Distribution Received
54		$300,000.00	$0.00	$300,000.00	$114,000.00	$114,000.00	38.00%
55		$2,850,000.00	$870,000.00	$1,980,000.00	$1,083,000.00	$213,000.00	38.00%
58		$500,000.00	$0.00	$500,000.00	$190,000.00	$190,000.00	38.00%
59		$110,000.00	$0.00	$110,000.00	$41,800.00	$41,800.00	38.00%
61		$22,794.15	$0.00	$22,794.15	$8,661.77		
62		$244,000.00	$105,000.00	$139,000.00	$92,720.00		
63		$42,066.20	$0.00	$42,066.20	$15,985.16		
	TOTAL:	**$308,860.35**	**$105,000.00**	**$203,860.35**	**$117,366.93**	**$12,366.93**	**38.00%**
64		$60,000.00	$0.00	$60,000.00	$22,800.00	$22,800.00	38.00%
68		$175,000.00	$0.00	$175,000.00	$66,500.00		
69		$50,000.00	$0.00	$50,000.00	$19,000.00		
	TOTAL:	**$225,000.00**	**$0.00**	**$225,000.00**	**$85,500.00**	**$85,500.00**	**38.00%**
77		$285,939.16	$0.00	$285,939.16	$108,656.88		
78		$250,000.00	$0.00	$250,000.00	$95,000.00		
	TOTAL:	**$535,939.16**	**$0.00**	**$535,939.16**	**$203,656.88**	**$203,656.88**	**38.00%**
79		$100,000.00	$0.00	$100,000.00	$38,000.00	$38,000.00	38.00%

* The Receiver intends to file Names of Claimants under seal with the Court.

Claim Number	Name of Claimant *	Funds Invested (per claim form)	Previous Disbursements (per claim form)	Net Cash Balance	Gross Distribution Amount	Net Distribution Amount	% Total Cumulative Distribution Received
80		$430,000.00	$0.00	$430,000.00	$163,400.00	$163,400.00	38.00%
81		$300,000.00	$0.00	$300,000.00	$114,000.00	$114,000.00	38.00%
82		$200,000.00	$0.00	$200,000.00	$76,000.00	$76,000.00	38.00%
83		$238,000.00	$66,660.00	$171,340.00	$90,440.00	$23,780.00	38.00%
84		$125,000.00	$0.00	$125,000.00	$47,500.00	$47,500.00	38.00%
86		$220,000.00	$50,000.00	$170,000.00	$83,600.00	$33,600.00	38.00%
88		$250,000.00	$0.00	$250,000.00	$95,000.00	$95,000.00	38.00%
89		$100,000.00	$0.00	$100,000.00	$38,000.00	$38,000.00	38.00%
				TOTAL:		**$3,548,522.35**	

* The Receiver intends to file Names of Claimants under seal with the Court.

EXHIBIT C

Disputed Claims Interim Distribution Schedule

CFTC v. Equity Financial Group, LLC et al., Case No. 04CV 1512

Claim Number	Name of Claimant *	Funds Invested (per claim form)	Previous Disbursements (per claim form)	Net Cash Balance	Gross Distribution Amount	Net Distribution Amount	% Total Cumulative Distribution Received
4		$100,000.00	$52,000.00	$48,000.00	$38,000.00	$0.00	52.00%
5		$1,508,000.00	$410,000.00	$1,098,000.00	$573,040.00	$163,040.00	38.00%
10		$222,789.00	$0.00	$222,789.00	$84,659.82	$84,659.82	38.00%
20		$300,000.00	$0.00	$300,000.00	$114,000.00	$114,000.00	38.00%
21		$100,000.00	$0.00	$100,000.00	$38,000.00	$38,000.00	38.00%
22		$1,083,000.00	$280,146.00	$802,854.00	$411,540.00	$131,394.00	38.00%
23		$75,000.00	$0.00	$75,000.00	$28,500.00	$28,500.00	38.00%
24		$410,000.00	$90,000.00	$320,000.00	$155,800.00	$65,800.00	38.00%
25		$60,000.00	$0.00	$60,000.00	$22,800.00	$22,800.00	38.00%
26		$105,000.00	$0.00	$105,000.00	$39,900.00	$39,900.00	38.00%
29		$205,000.00	$0.00	$205,000.00	$77,900.00	$77,900.00	38.00%
30		$400,000.00	$411,115.00	($11,115.00)	$152,000.00	$0.00	102.78%
31		$175,000.00	$115,000.00	$60,000.00	$66,500.00	$0.00	65.71%
32		$284,000.00	$0.00	$284,000.00	$107,920.00	$107,920.00	38.00%
37		$95,000.00	$0.00	$95,000.00	$36,100.00	$36,100.00	38.00%
38		$25,000.00	$0.00	$25,000.00	$9,500.00	$9,500.00	38.00%

* The Receiver intends to file Names of Claimants under seal with the Court.

as of January 7, 2005

Claim Number	Name of Claimant *	Funds Invested (per claim form)	Previous Disbursements (per claim form)	Net Cash Balance	Gross Distribution Amount	Net Distribution Amount	% Total Cumulative Distribution Received
40		$100,000.00	$0.00	$100,000.00	$38,000.00	$38,000.00	38.00%
43		$100,000.00	$130,576.00	($30,576.00)	$38,000.00	$0.00	130.58%
46		$195,000.00	$0.00	$195,000.00	$74,100.00	$74,100.00	38.00%
47		$1,510,000.00	$0.00	$1,510,000.00	$573,800.00		
48		$250,000.00	$0.00	$250,000.00	$95,000.00		
49		$350,000.00	$0.00	$350,000.00	$133,000.00		
50		$1,000,000.00	$1,143,333.00	($143,333.00)	$380,000.00		
51		$900,000.00	$0.00	$900,000.00	$342,000.00		
52		$200,000.00	$2,000,000.00	($1,800,000.00)	$76,000.00		
	TOTAL:	**$4,210,000.00**	**$3,143,333.00**	**$1,066,667.00**	**$1,599,800.00**	**$0.00**	**74.66%**
56		$48,000.00	$0.00	$48,000.00	$18,240.00	$18,240.00	38.00%
57		$28,000.00	$0.00	$28,000.00	$10,640.00	$10,640.00	38.00%
60		$360,000.00	$0.00	$360,000.00	$136,800.00	$136,800.00	38.00%
65		$200,100.00	$100,000.00	$110,000.00	$76,038.00		
66		$100,000.00	$0.00	$100,000.00	$38,000.00		
	TOTAL:	**$300,100.00**	**$100,000.00**	**$200,100.00**	**$114,038.00**	**$14,038.00**	**38.00%**

* The Receiver intends to file Names of Claimants under seal with the Court.

Claim Number	Name of Claimant *	Funds Invested (per claim form)	Previous Disbursements (per claim form)	Net Cash Balance	Gross Distribution Amount	Net Distribution Amount	% Total Cumulative Distribution Received
67		$150,000.00	$0.00	$150,000.00	$57,000.00	$57,000.00	38.00%
70		$1,480,000.00	$ 724,370.40	$755,629.60	$562,400.00		
71		$250,000.00	$ 175,000.00	$75,000.00	$95,000.00		
72		$ 9,177,500.00	$0.00	$ 9,177,500.00	$3,487,450.00		
73		$190,000.00	$0.00	$190,000.00	$72,200.00		
74		$4,567,845.00	$240,000.00	$ 4,327,845.00	$1,735,781.10		
75		$0	$100,000.00	($100,000.00)	$0.00		
76		$278,678.00	$0.00	$278,678.00	$105,897.64		
	TOTAL:	**$15,944,023.00**	**$1,239,370.40**	**$14,704,652.60**	**$6,058,728.74**	**$4,819,358.74**	**38.00%**
85		$3,079,500.00	$432,335.00	$2,647,165.00	$1,170,210.00	$737,875.00	38.00%
87		$53,000.00	$4,071.72	$48,928.80	$20,140.00	$16,068.80	38.00%
				TOTAL:		**$6,841,634.36**	

* The Receiver intends to file Names of Claimants under seal with the Court.

as of January 7, 2005

EXHIBIT D

C
Motions, Pleadings and Filings

Only the Westlaw citation is currently available.

United States District Court, N.D. Illinois, Eastern Division.

COMMODITY FUTURES TRADING COMMISSION, Plaintiff,
v.
BUFF AARON HOFFBERG, individually and doing business as Echo Trading, Inc., Defendant.

No. 93 C 3106.

Oct. 28, 1993.

MEMORANDUM OPINION

KOCORAS, District Judge:

*1 This case is before the Court on the Motion of the Temporary Equity Receiver for Authority to Make Initial Distribution of Estate Funds. For the reasons that follow, the proposed initial distribution is approved.

BACKGROUND

This case involves an investment scheme gone sour. The plaintiff, Commodity Futures Trading Commission ("CFTC"), is an independent federal regulatory agency charged with enforcing the Commodity Exchange Act. *See* 7 U.S.C. § 1 et seq. It brought this action against Buff Aaron Hoffberg ("Hoffberg") individually and doing business as Echo Trading, Inc. ("ETI"), alleging violations of the Commodities Exchange Act and the Commission Regulations thereunder.

The complaint alleges that Hoffberg, individually and doing business as ETI, has been acting as a Commodity Pool Operator since December 1989, without being registered with the CFTC. Further, the complaint alleges that Hoffberg falsely reported the performance of the pool and the value of the investors' units of participation in the pool. The complaint states that Hoffberg reported trading profits to the investors when in fact he incurred trading losses.

On May 28, 1993, this Court entered an agreed temporary restraining order against Hoffberg, enjoining him from violating provisions of the Commodity Exchange Act, from dissipating any assets held in his individual capacity or by ETI, and from accepting any new deposits of funds. This order also appointed a temporary equity receiver ("Receiver") of the assets and affairs of Hoffberg individually and doing business as ETI. The order authorized the Receiver to take into custody the assets of Hoffberg, individually and doing business as ETI, and to liquidate all commodity futures positions held by Hoffberg or ETI.

Accountants hired by the Receiver reported that over two million dollars was deposited to accounts held by ETI. Amended Preliminary Report of Receiver, at 5. Of these funds, over one million dollars was returned to investors. *Id.* Net trading losses accounted for $259,468.60 of the funds and operating expenses consumed $177,920.43. *Id.* Of the remaining funds, $380,508.92 was paid to Hoffberg directly or for his benefit or paid to "cash" and $6,934.81 was paid to third parties in unexplained transfers. *Id.* The accountants and the Receiver have identified thirty-nine participant accounts. [FN1]

The Receiver has taken control of funds totalling $265,325.42. Amended Preliminary Report of Receiver, at 2. Additionally, the Receiver has possession of a promissory note to Hoffberg for $125,000 payable in January, 1994. Whether this note will prove to be collectible is not known at this time.

The Receiver now seeks authority from this Court to make an initial distribution of a significant portion of those funds. The Receiver plans to reserve the undistributed funds pending resolution of discrepancies between amounts claimed by investors and amounts shown on ETI records, and identification of other claimants. The Receiver's Proposed Plan for Initial Distribution was mailed to all identified investors and they were given the opportunity to comment upon the Plan. Nine responses were received by this Court.

DISCUSSION

The Investors' Claims

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***2** We are faced here with the problem of a small pie and many disappointed investors. Every investor who responded to the Plan urges that we authorize a "fair" distribution, but there was a sharp split of opinion as to what that means in this case. Two approaches were proposed. One is contained in the Plan advanced by the Receiver and the other was suggested by several of the investors. Each is described below.

The Plan promulgated by the Receiver would distribute the collected funds according to the following formula:

(Total Investment x 0.15)--Amounts Previously Received

The "Amounts Previously Received" reflects all monies received by the investors, whether withdrawn from the account by the investor or distributed to the investor by Hoffberg. [FN2] The result of this formula is that investors who had withdrawn or otherwise received back more than 15% of their initial investment will recover no additional amounts at this time. Understandably, investors in that category objected to this formula. However, it is important to note that this formula does not require investors who have already received money in excess of 15% of their total investment to return any of that money.

The alternative formula proposed by the objecting investors is as follows:

(Total Investment--Amounts Previously Received) x 0.15

The objecting investors call the (Total Investment--Amounts Previously Received) figure the "net investment." Under this formula, everyone would receive money now. At first blush, that result is preferable. However, the formula as proposed by the objecting investors overlooks the fact that we have a fixed amount of money available for distribution. If we adopt this second formula, we will have to reduce the 0.15 multiplier to about 0.10. Thus, everyone would receive approximately 10% of the amount they had invested on the date of the restraining order.

Is it more equitable to return 15% of the initial investment to 30 investors and return no additional money to 9 investors or to return 10% of the "net investment" to each of the 39 investors? The Receiver and others who favor the first option believe that the Amounts Previously Received should be considered in deciding the amounts to be distributed now. We will examine the Damatos' investment as an example. The Damatos invested $263,132 and previously withdrew or otherwise received $135,500. Under the first option, the Damatos will receive no additional money. The Receiver's view of this result is that it leaves the Damatos with 51.5% of their total investment, whereas the persons who never withdrew or otherwise received money will be left with 15% of their original investment. On the other hand, the Damatos characterize the first option as penalizing them for having withdrawn or otherwise having received money from their accounts. They do not view themselves as having received 51.5% of their total investment. Instead, they focus on their "net investment" and state that the first option gives them 0% of their net investment while it gives persons such as the Kendalls, who have never received money from their accounts, 15% of their "net investment." The Kendalls invested $10,000 and never withdrew or otherwise received money from their account. Under the first option, they will receive $1,500.

***3** Now let us examine the outcome for the Damatos and the Kendalls if we apply the second formula. The percentage returned must be reduced because we wish to share the same amount of money among more people. Under the second formula, the Damatos would receive approximately 10% of their net investment of $127,632, or about $12,763.20. The Kendalls would receive approximately 10% of $10,000, or about $1,000. The Damatos would gain under this formula but the Kendalls would receive less than under the Receiver's formula. The Damatos urge that this result is nonetheless fair, because it gives everyone a percentage of their "net investment." The Receiver urges that this result is unfair, because the Damatos have already received 51.5% of their total investment and this formula gives them an additional 10%, for a total of 61.5% versus the Kendalls' 10%.

Both of the above formulas have support in the case law. In *CFTC v. Skorupskas,* No. 83-CV-1885DT (E.D.Mich. Aug. 22, 1988), the court adopted the first formula and expressly rejected the second. The court observed that the "profits" paid out to certain investors were actually part of the res. *Skorupskas,* slip op. at 5. The court considered it unfair to give those investors additional portions of the res. *Id.* The court observed that allowing those investors an additional recovery would come at the expense of other investors. *Id.* at 6.

On the other hand, the court in *CFTC v. Franklin,*

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652 F.Supp. 163 (W.D.Va.1986), *rev'd on other grounds sub nom. Anderson v. Stephens,* 875 F.2d 76 (4th Cir.1989), applied the second formula above and rejected the first. However, we note that the court in *Franklin* was operating under an incorrect assumption: that investors who had not previously received money would receive the same return under either of the formulas. *See Franklin,* 652 F.2d at 170. As discussed above, that assumption is incorrect because the pot of money to be divided is a fixed amount. If more people are to receive money from it, as provided by the second formula, investors who had not previously received money will receive less than they would under the first formula.

We believe that *Skorupskas* was the better-reasoned opinion and that its holding is more appropriate for application to the facts of this case. Thus, we will approve the Receiver's proposed initial distribution to the investors.

Claims of ETI's Creditors

The Receiver proposes to handle the claims of three creditors as follows. First, the Receiver proposes to pay $328 to Midwest Moving & Storage as full payment for the service of moving Hoffberg's office furnishings from his Glenview office to an auction site. We approve that expenditure.

The next creditor identified by the Receiver is Devon Bank, which acquired the property where Hoffberg leased office space. Devon Bank has filed a claim for unpaid rent in the amount of $1525 [FN3] and a charge of $41.66 for changing the lock on the office. These claims total $1566.66. Devon Bank was able to recover $152.62 by seizing money from two of Hoffberg's accounts with the bank. Thus, Devon Bank seeks $1414.04. The Receiver proposes to pay in full the amounts incurred after the restraining order was entered and to pay a pro rata share of the rent owing prior to May 28, 1993 (the date of the order). We approve this proposal.

***4** Finally, the Receiver identified Centel (Central Telephone Company) as a creditor. Centel has filed a claim for $107.84 for service to the ETI office from May, 1993 to June 17, 1993, when service was disconnected. The Receiver proposes to pay Centel $23.50 as the estimated amount incurred after the restraining order was entered and to pay a pro rata amount of the charges incurred prior to entry of the order. We approve this proposal.

The Claim of Alex Livshin

The Receiver received $14,450 from Hoffberg's attorney, who represented that it was the remaining proceeds from a $25,000 loan made by Alex Livshin to Hoffberg in early May, 1993. Although Livshin was also an investor, the Receiver considers Livshin's documentation adequate to establish that the $25,000 was a loan and not an investment disguised as a loan. Livshin requests that the entire $14,450 be returned to him. The Receiver proposes to treat Livshin the same as the other unsecured creditors having claims arising before May 28, 1993 and pay him a pro rata amount of his claim. We approve a pro rata return based on the $25,000 loan amount.

CONCLUSION

For the reasons discussed above, we grant the Temporary Equity Receiver authority to make initial distribution of funds as outlined in his motion.

FN1. Although some of these 39 accounts are held by more than one person, we will refer to 39 investors.

FN2. Neither the Receiver nor the investors have made clear the nature of the Amounts Previously Received, that is, whether the investors withdrew the funds as capital withdrawals or whether Hoffberg distributed these amounts as "profits."

FN3. This represents rents for May, June, July, and August, 1993 at a rate of $375 per month, plus a previous balance of $25.

Motions, Pleadings and Filings (Back to top)

- 1:93CV03106 (Docket) (May. 24, 1993)

END OF DOCUMENT

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

COMMODITY FUTURES TRADING COMMISSION
and THE STATE OF MICHIGAN, ex rel.
FRANK J. KELLEY, Attorney General,

Plaintiffs,

CIVIL NO. 83-CV-1885-DT
HON. PHILIP PRATT, CHIEF JUDGE

v.

BARBARA A. SKORUPSKAS, BARAL CORP.,
d/b/a BARAL INVESTMENTS, INC., and
SIDEREAL CORPORATION, d/b/a
SIDEREAL INVESTMENT CORP.,

Defendants.
_______________________________________/

MEMORANDUM OPINION AND ORDER

This case is presently before the Court on the equity receiver's motion to approve a plan of distribution of the assets held in the defendants' estate. As is fully described in this Court's findings of fact and conclusion of law of March 20, 1985, reported at 605 F.Supp. 923 (E.D. Mich. 1985), defendants operated a Ponzi-type scheme which defrauded numerous investors. The proposed plan involves $400,000 of the funds held in the receivership estate, representing 80% of that estate. The Court set a schedule permitting investors to comment upon the plan. Relatively few comments on the plan of distribution were received by the Court. After considering the comments and submissions of the parties which opposed particular portions of the plan, the Court hereby adopts the plan with the noted amendments.

The equity receiver determined, from the proofs of claim submitted by investors pursuant to the Court's July 29, 1986 order, that approximately $2.65 million had been invested in total in the Skorupskas related entities. Just over $500,000 were marshaled by Mr. Woods into the estate. Basically the equity receiver proposes to distribute $400,000 according to the following formula:

1. A proportionate share of the total investment amount is calculated for each investor by dividing the amount invested by $2,648,708.
2. This fraction is then multiplied by the amount to be distributed to derive a pro rata share for each investor.
3. Any amounts paid as "profits" to the investor are subtracted from the pro rata share, leaving a net recovery amount.

As a preliminary matter, the equity receiver had to determine which investors to include in the plan of distribution. All parties are agreed that those filing proofs of claim should participate in the distribution. The entire balance of monies in the estate are derived from investments made <u>before</u> the June 7, 1983 injunction. While approximately $700,000 were received by Skorupskas after the Court's injunction of June 7, 1983, none of it has been traced or recovered by the estate. At the outset, then, the equity receiver could have limited the distribution to

those investors who made contributions before the June 7, 1983 injunction date to funds invested prior to the court's order. The proposed plan lumps the "old" money (invested before June 7, 1983) together with the "new" money (post June 7, 1983) and all investors recover proportionally regardless of when the investment was made.

The equity receiver argues that this treatment is proper because Skorupskas continued to operate the fraudulent scheme in the same fashion despite the Court's June 7, 1983 injunction. Thus, "old" investors received "profits" which were actually investments by "new" investors. Similarly, some "old" investors continued to invest after the order. Plaintiffs objected to this portion of the plan.

Both the Commodity Futures Trading Commission and the State of Michigan argued that persons who invested funds or garnered "profits" with knowledge of this Court's June 3, 1983 injunctive order should be precluded from recovery under the plan. In addition, plaintiffs urged that those investors who participated in the Caribbean cruise organized by Skorupskas after this Court's order should have the value of the trip subtracted from their proportionate share. The Court finds that giving effect to the June 7, 1983 order in this fashion would be inequitable in light of the circumstances. The continued participation of persons in this scheme as well as the vituperative campaign waged in opposition to this Court's order reveals not so much the wilful miscon-

duct of those victimized by Skorupskas as their frailty and guillibility. The court declines plaintiffs' invitation to bar those deceived by the defendants from participation in the plan of distribution.[1]

The only substantive aspect of the plan which generated any criticism from investors was the equity receiver's treatment of the "profits" some investors received from the scheme. As discussed in CFTC v. Franklin, 652 F.Supp. 163, Comm. Fut. L. R. (CCH), ¶ 23, 363 (W.D. Va. 1986), there are four possible treatments of the problem: (1) investors would be required to return all "profits" to the estate with a distribution based on a proportion calculated with reference to the total invested; (2) investors could retain the "profits" and still claim a proportionate share based on the amount invested; (3) investors could retain "profits" but have this amount subtracted from their proportionate share calculated with regard to their total investment, or (4) investors could retain their profit but have this amount subtracted from their total investment in calculating their proportionate share. See, Franklin, supra, 652 F.Supp. at 169. Franklin would appear to be the only discussion of this point in the case law.

Options one and two were not discussed by the equity receiver or suggested by any investors or other parties. The

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[1]The Court recognizes that had the investors responded promptly and forthrightly to the Court's orders and requests, larger sums could have been recovered and more equitable distributions made. However, at the time the "investors" were still victims in the fullest sense, and sympathy is not misplaced.

equity receiver rejected the fourth option. Essentially this position would provide a pro rata recovery of the loss sustained by each investor as any "profits" recovered would be subtracted from the total invested before a pro rata share is determined. The third option adopted by the equity receiver provides for recovery limited to the pro rata share of the amount invested. The fourth option was adopted in Franklin. The mainspring behind the Franklin decision seems to be that courts view that adoption of the approach where "profits" are subtracted from a pro rata share based on the total invested does not accurately account for what occurred because it treats the bogus profits as actual profits as opposed to recycled capital. See Franklin, supra, 652 F.Supp. at 169. The court did not develop this point at length and the reasoning is somewhat opaque. If anything, the option permitting an investor who received "profits" to state a claim from principal not withdrawn most accurately treats the bogus "profits" as actual profits and thus ignores the reality of the Ponzi scheme.[2] Any "profits" received were actually part of the res. Given the basic proposition that all investors should share proportionately in the estate, a position not contested by any investor or party and generally supported in the law, see 1 G. Palmer The Law of

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[2]This treatment was rejected in In Re: Young, 294 F.1 (4th Cir. 1923) as contrary to equitable principals. The court held in no uncertain terms "all sums paid as profits to one adventurer from the common fund, when there was no profit, was an unjust enrichment of that adventurer from the fund belonging to all in common [. . .] [e]quity therefore requires that he should account for all sums paid to him as profit before he can share with others in the application of the funds on hand for the debts due for sums actually paid in." 294 F. at 4. The implicit rejection of this position here is clearly warranted.

Restitution, § 2.18 at 216 (1978),[3] the Franklin rule would permit those few investors who insisted on cashing out their "profits" to receive more from the res held in constructive trust than a proportionate share based on their total investment.[4] Given that all monies were impressed with the constructive trust at the time they were put in Skorupskas' hands, the Franklin result permits the fortunate few to retain more in "profits" than they would have obtained as a proportionate share. Thus, if anything, the Franklin rule is insensitive to the legal character of the "profits" as funds impressed with a constructive trust. By permitting an investor to reap more than the proportionate share of his investment Franklin permits the investor to in effect reap a "profit" on the scheme that defeats the pro rata scheme of distribution. For these reasons, the Court rejects use of the approach favored in Franklin and adopts the equity receiver's solution to the problem.

At a hearing conducted on the plan, the receiver agreed to certain amendments in light of comments received by investors. In particular, the receiver agreed to correct an arithmetic error

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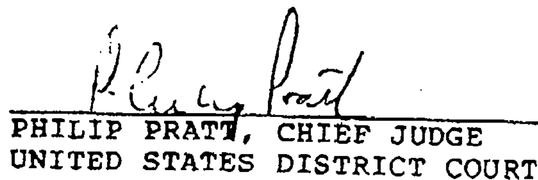
[3]Earlier cases had adopted the rule in Clayton's Case, 1 Mer. 572, 35 Eng. Rep. 781 (1816), presuming that the order of withdrawals from the trust was on a "first in, first out" basis. This would not only complicate recovery but would be inequitable. Use of the rule in analogous situations has been wisely criticized and a pro rata scheme of distribution adopted. See, e.g., Ruddle v. Moore, 411 F.2d 718 (D.C. Cir. 1969); Palmer, supra, at 214-216.

[4]To its credit this inequity is recognized by the Franklin court. 652 F.Supp. at 170.

with regard to the claim of Mark Boker, to permit Mark Kosaki's claim despite the receiver's contention that he had not received a proof of claim form, and to adjust the claim of Allen LaMotte to conform to his actual investment as specified in his letter to the Court. The plan of distribution is hereby approved with these amendments.

IT IS SO ORDERED.



PHILIP PRATT, CHIEF JUDGE
UNITED STATES DISTRICT COURT

Dated: AUG 2? 1988