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Via ECF

April 25, 2017

Chief Judge Dora L. Irizarry  
United States District Court  
Eastern District of New York  
225 Cadman Plaza East  
Brooklyn, NY 11201

**Re: *SEC v. Platinum Management (NY) LLC et al.*, Civil Case No. 16-cv-6848 (DLI)(VMS)**

Dear Chief Judge Irizarry:

We are counsel to Bart M. Schwartz (the "Receiver"), the court-appointed receiver for Platinum Partners Credit Opportunities Master Fund, LP ("PPCO") and certain related entities (collectively, the "Receivership Entities"). We write on behalf of the Receiver to request your approval of a settlement agreement the Receiver entered into after a court-supervised mediation in Texas (the "Arabella Settlement Agreement"). If approved by this Court, and the Texas bankruptcy courts that must also approve the Agreement for it to become effective, the Arabella Settlement Agreement will resolve expensive, protracted litigation over PPCO's interest in property that secures a loan (the "Arabella Loan") made by PPCO to Arabella Exploration, Inc. ("AEI").<sup>1</sup>

PPCO or property that secures the Arabella Loan are currently involved in the following proceedings:

- *In re Arabella Petroleum Company, LLC*, No. 15-70098-RBK (Bankr. W.D. Tex.) (the "APC Bankruptcy Case") and related adversary proceeding, Adv. Proc. No. 16-07002-RBK (the "APC Adversary Proceeding");
- *In the Matter of Arabella Exploration, Inc.*, Case No. FSD 72 of 2016, RMJ (Grand Court of the Cayman Islands) (the "AEI Liquidation");
- *In re Arabella Exploration Inc.*, No. 17-40119 (Bankr. N.D. Tex.) (the "AEI Bankruptcy Case");
- *In re Arabella Exploration, LLC*, No. 4:17-bk-40120 (Bankr. N.D. Tex.) (the "AEX Bankruptcy Case");
- *In re Arabella Operating, LLC*, No. 17-41479-RFN (Bankr. N.D. Tex.) (the "AO Bankruptcy Case");
- Multiple actions commenced in the 143rd Judicial District Court of Reeves County, Texas by, among others, Founders Oil and Gas Operating LLC ("Founders") (the "Founders Litigation").

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<sup>1</sup> PPCO acted through its subsidiary Platinum Long Term Growth VIII, LLC ("PLTG8"). As used in this application, "PPCO" refers collectively to PPCO and PLTG8.



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As discussed below, the Receiver concluded that the Arabella Settlement Agreement is a very favorable resolution for the Receivership Estate as it resolves, or provides a means for resolving, expensive, ongoing litigation challenging, directly or indirectly, the Receiver's interest in the property that secures the Arabella Loan. As a result of the Arabella Settlement Agreement, that property will be able to be sold, and the Receivership Estate will be entitled to obtain a portion of the sale proceeds. Prior to the Arabella Settlement Agreement, it was not clear that the Receivership Estate would realize *anything* from its collateral.

In support of this Application, the Receiver attaches the following Exhibits:

- Exhibit 1 Declaration of Bart M. Schwartz, executed April 25, 2017 (the "Schwartz Declaration"); and
- Exhibit 2 Declaration of Michael E. Baum, executed April 24, 2017 (the "Baum Declaration"); and
- Exhibit 3 Declaration of Stephen B. O'Connell, executed April 24, 2017 (the "O'Connell Declaration"); and
- Exhibit 4 a proposed Order.

The SEC Staff consents to this Application.

## Background

On December 19, 2016, the U.S. Attorney for the Eastern District of New York unsealed an eight-count indictment against Mark Nordlicht and six other individuals who were formerly affiliated with Platinum Partners ("Platinum"), a purported \$1.7 billion hedge fund family based in New York that includes the corporate defendants named in this action (the "Indictment"). The Indictment alleges, among other things, that the defendants defrauded Platinum investors through, among other things, the overvaluation of assets, the concealment of severe cash flow problems, and the preferential payment of redemptions. That same day, the SEC filed a complaint against the same seven individuals, Platinum Management (NY) LLC, and Platinum Credit based on conduct similar to that alleged in the Indictment. The SEC simultaneously moved by order to show cause for a temporary restraining order and the appointment of a receiver. Judge Matsumoto entered an order pursuant to which Bart M. Schwartz was appointed Receiver of the Receivership Entities on December 19, 2016, which Your Honor amended on January 30, 2017 (the "Receiver Order") [Docket Nos. 6, 59-2]. On March 8, 2017, Your Honor entered a preliminary injunction, enjoining violation of the federal securities laws, and ordering that Bart M. Schwartz continue to act as Receiver pursuant to the Receiver Order [Docket Nos. 105, 106].

Under the Receiver Order, the Receiver was appointed to preserve the *status quo*, ascertain the extent of commingling of funds, ascertain the true financial condition of the Receivership Entities, prevent further dissipation of property and assets of those entities, prevent the encumbrance or disposal of property or assets of the Receivership Entities, preserve the books, records, and documents of the Receivership Entities, be available to respond to investors inquiries, protect investors' assets, conduct an orderly wind down, including a responsible liquidation of assets and orderly and fair distribution of those assets to investors, and determine whether one or more of the Receivership Entities should undertake bankruptcy filings, among other things (Receiver Order at 2).

The Receiver is empowered to "take custody, control and possession of all Receivership Property," (Receiver Order ¶ 6.B), "manage, control, operate and maintain the Receivership Entities," (Receiver Order ¶ 6.C), transfer, compromise, or otherwise dispose of any Receivership Property, other than real estate, in



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the ordinary course of business” in the manner the Receiver deems “most beneficial” to the Receivership Entities (Receiver Order ¶ 28), “manage [and] maintain” the business operations of the Receivership Entities (Receiver Order ¶ 31).

### **The Arabella Loan**

Prior to the Receiver’s appointment, PPCO made a \$16 million loan to AEI pursuant to a \$45 million credit facility. Baum Decl. ¶ 6. AEI was involved in oil and gas operation in Texas through its subsidiaries. *Id.* The Arabella Loan was secured by all of AEI’s assets, and was guaranteed and secured by the assets of AEI’s subsidiaries Arabella Exploration, LLC (“AEX”) and Arabella Operating LLC (“AO” and together with AEX and AEI, the “Arabella Entities”) through a series of documents including a Securities Purchase Agreement, a Senior Secured Note Agreement, a Security and Pledge Agreement, and Deeds of Trust. AEX and AO also pledged their assets to secure the Arabella Loan. Jason Hoisager controlled the Arabella Entities as of the time of the Arabella Loan. *Id.* The interests in the Arabella Entities that PPCO acquired as a result of the Arabella Loan are referred to collectively the “Arabella Interests.”

AEI only made two payments toward interest to PPCO under the Arabella Loan, resulting in an event of default in mid-2016. *Id.* ¶ 7. After PPCO formally notified AEI of its default, PPCO pursued its rights under the Arabella Loan documents, including appointing Charles “Chip” L. Hoebeke II to manage AEX and AO. Mr. Hoebeke placed AEI into liquidation, initiating the AEI Liquidation. *Id.* ¶¶ 32-37

Although the Arabella Loan was secured, PPCO was unable to foreclose on its collateral because of the legal challenges described below. Baum Decl. ¶ 8. If those challenges were successful, the Arabella Interests would have been wiped out entirely. *Id.* ¶¶ 63-64. Indeed, as of the Receiver’s appointment, it appeared that PPCO’s Arabella investment could be a complete loss. Schwartz Decl. ¶¶ 7-8.

### **The Challenges to PPCO’s Arabella Interests**

**The APC Bankruptcy and Adversary Proceeding** – The Arabella Interests include certain rights and working interests in oil wells that Arabella Petroleum Company, LLC (“APC”), transferred to AEX and AO prior to the Arabella Loan. Through these transfers, AO was to hold the rights to operate the various oil wells owned by the Arabella Entities, which were previously owned by APC; AEX was to hold a portion of the working interests previously owned by APC (together with all other working interests previously held by APC, the “Arabella Working Interests”). Baum Decl. ¶¶ 9-11.

After APC declared bankruptcy, the Chapter 11 Trustee<sup>2</sup> filed the APC Adversary Proceeding, alleging (a) that transfers from APC to AEX and AO were avoidable fraudulent conveyances, (b) that the security interests held by PPCO should be avoided because PPCO knew or should have known of the fraudulent conveyances, (c) that the APC bankruptcy estate is owed money for interests in receivables that were not paid by AEX, and (d) and that those unpaid expenses constitute a priority lien impressed on PPCO’s collateral. *Id.* ¶ 15.

The Chapter 11 Trustee alleged that the only consideration paid by AEX in exchange for the transfer of some of the Arabella Working Interests to it was an increase in the amounts booked as due to APC under an agreement between the entities, which was later recharacterized as \$3 million of equity in AEX issued to Mr. Hoisager, and an assumption of a \$3 million note issued from APC to Mr. Hoisager. *Id.* ¶ 17. Thus,

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<sup>2</sup> Capitalized terms not defined herein are defined in the Schwartz or Baum Declarations.



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according to the Chapter 11 Trustee, APC received no consideration for the transfer of Arabella Working Interests to AEX, as the consideration flowed directly to Mr. Hoisager. *Id.*

As a subsequent transferee, PPCO could have prevailed on the Fraudulent Conveyance Claim even if there was a fraudulent conveyance. *Id.* ¶ 18. To do so, it would have needed to prevail on its affirmative defenses. Specifically, PPCO would have had to carrying its burden of proving (1) that it entered into the Arabella Loan in good faith, for value, and without knowledge of the alleged underlying fraud, or (2) that its interest in the Arabella Loan should be maintained as a result of the significant expenditures PPCO made to lift liens and improve the value of AEX's property. *Id.* To establish the first of these defenses, PPCO would have had to prove the good faith and lack of knowledge of the Platinum personnel involved in the Arabella Loan transaction, including Mark Nordlicht, who is under indictment and unlikely to testify in connection with the APC Adversary Proceeding. *Id.* To establish the second, PPCO would have had to prove the extent to which the money advanced by PPCO improved the value of AEX's property through the payment of debt secured by liens. *Id.* These were significant hurdles; indeed, PPCO's motion to dismiss was denied by the court in the APC Bankruptcy Case on June 8, 2016. *Id.* ¶ 38.

The Chapter 11 Trustee also alleged that AEX owed APC millions of dollars for expenses it incurred operating the Arabella Working Interests. These unpaid expenses were the basis of a lien APC placed against the Arabella Working Interests (the "JIB Lien"). Unless the JIB Lien was cleared (*i.e.*, paid or declared invalid), the collateral securing the Arabella Loan could not be sold. Baum Decl. ¶¶ 20-26.

If the Chapter 11 Trustee prevailed in the Adversary Proceeding, substantially all of the Arabella Interests would have been lost. *Id.* ¶¶ 19, 26.

**The Founders Litigation** – During the APC Bankruptcy Case, Founders took over operation of the various wells located on the Arabella properties, including the properties that secured the Arabella Loan. Founders eventually claimed that AEX owed Founders expenses relating to improvements made those wells, and commenced the Founders Litigation, seeking to foreclose against AEX's Arabella Working Interests. Had that foreclosure occurred, the most valuable of the Arabella Interests would have been destroyed. *Id.* ¶¶ 27-30. In order to protect its assets in the face of the Founders Litigation, AEX initiated the AEX Bankruptcy Case. *Id.* ¶ 49.

**Mechanics' and Materialman's Liens** – Mechanic's and Materialman's Liens ("M&M Liens") are liens placed by those who worked on the property in question. Approximately \$2.5 million in M&M Liens had been placed against AEX's Arabella Working Interests. These M&M Liens must be cleared for any sale of the Arabella Interests to take place. *Id.* ¶ 31. As discussed below, the Arabella Settlement Agreement acknowledges that AEX has title to its Arabella Working Interests, thus enhancing AEX's ability to clear the M&M Liens. *Id.* ¶ 62; O'Connell Decl. ¶ 9.

**The Tag-Along Rights** – Tag-along rights are contractual provisions that allow the owners of certain working interests (arising from a reversionary right) the opportunity to "tag-along" with any sale of the underlying asset to a third party and receive a *pro rata* portion of the sale price. The Tag-Along Rights potentially pertaining to the Arabella Interests were unknown to the Receiver or his counsel until January 2017, when both APC and AEX claimed ownership of the Arabella Entities' Tag-Along Rights. The Tag-Along Rights are believed to be worth between \$6.8 million and \$9 million. *Id.* ¶ 51.

The Chapter 11 Trustee argued that APC was entitled to the Tag-Along Rights as it held record title of the assets in question, and filed motions in the APC Bankruptcy Case to obtain authority to execute the necessary documents to effectuate the Tag-Along Rights. *Id.* ¶ 52. AEX received its putative interests in the Tag-Along Rights as the result of a transfer from APC which had not been recorded. APC claimed that



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this transfer was not effective as to the Chapter 11 Trustee and, if it was effective, was a fraudulent conveyance. *Id.* ¶ 52-53. To establish a right to the Tag-Along Rights, AEX needed to demonstrate that the owners of the underlying properties were on notice of reservation of AEX's position by virtue of references to AEX's rights in documents recorded by others. *Id.* Even if this were established, AEX still needed to defend against APC's allegation that it received the Tag-Along Rights as a result of a fraudulent transfer. *Id.* Prior to the Mediation, these were highly disputed issues. *Id.*

### **The Mediation and the Arabella Settlement Agreement**

With the approval and encouragement of the APC Bankruptcy Case court, APC, AEX, AEI, AO, the Official Committee of Unsecured Creditors of APC, Mr. Hoebeke, Mr. Hoisager, and the Receiver agreed to enter into mediation before the Honorable Christopher Mott, U.S. Bankruptcy Judge for the Western District of Texas, Austin/EI Paso Division. The Mediation took place on March 27 and 28, 2017. Judge Mott does not preside over any of the Arabella Cases but agreed to serve as mediator for the parties. The Receiver attended in person, represented by Schafer & Weiner, PLLC ("S&W"), O'Connell PLLC ("O'Connell"), and Kessler Collins PLLC. Schwartz Decl. ¶ 3; Baum Decl. ¶ 55, O'Connell Decl. ¶ 5.

As a result of the Mediation, the parties other than Mr. Hoisager reached an amicable resolution, memorialized in the Arabella Settlement Agreement. Baum Decl. ¶ 59-62; O'Connell Decl. ¶¶ 5-6. A copy of the Arabella Settlement Agreement is attached to the Baum Declaration as Exhibit A. The Arabella Settlement Agreement is subject to the approval of this Court, and the bankruptcy courts supervising the APC, AEX, and the AO Bankruptcy Cases. Baum Decl. Ex. A ¶ 10.

Under the Arabella Settlement Agreement:

- The parties to the Arabella Settlement Agreement will work together to sell the assets in the respective bankruptcy cases. The proceeds of the sale of the disputed oil and gas assets (the Arabella Working Interests transferred to AEX) will be distributed 65% to AEX and 35% to APC. AEX and APC will divide the proceeds from the exercise of the Tag-Along Rights 22.5% to 77.5%. Because AEX's assets secure the Arabella Loan, recovery provided to AEX will flow to the Receivership Estate.
- APC will offer a debtor-in-possession loan to AEX so AEX can resolve the claims brought by Founders.
- Ongoing expenses owed to Founders will be divided 65% by AEX and 35% by APC.
- There will be a mutual release of the parties, including a release of the former owners, members, agents, and principals of PPCO, and the Receivership Entities will be released, while any potential causes of action against former owners, board members, and officers of APC, AEX, APO, and AEI are maintained.

Baum Decl. ¶ 62.

The Arabella Settlement Agreement is a compromise: it shares the proceeds that will be realized from the sale of assets that were claimed by both AEX and APC, while recognizing that the greater share should go to the entity with record title to the claimed asset. Baum Decl. ¶¶ 62, 66; Schwartz Decl. ¶¶ 11-14. The Arabella Settlement Agreement avoids costly, prolonged litigation over the ownership of the Arabella Working Interests and Tag-Along Rights, and eliminates the very real litigation risk that the Receiver would



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obtain nothing for the Arabella Interests. Baum Decl. ¶¶ 63-66; O'Connell Decl. ¶ 8. It also gives the Receiver the ability to release APC's multi-million dollar liens against AEX, allows the Receivership Entities to retain their interest in AEX and AEI, and requires the parties to the Arabella Settlement Agreement to work together to monetize the assets of the various entities. Baum Decl. ¶¶ 62, 65; Schwartz Decl. ¶¶ 15-16; O'Connell Decl. ¶ 9.

For the reasons set forth above and described in greater depth in the Baum, O'Connell and Schwartz Declarations, the Receiver concluded that the Arabella Settlement Agreement is a very favorable resolution of these matters for the confers the Receivership Entities, and asks this Court to approve the Arabella Settlement Agreement.

### **The Retention of the Arabella Professionals, the Guaranty of Fees and the Participation Agreement**

On December 30, 2016, on the recommendation of S&W, the Receiver entered into an agreement with a funder called 30294 LLC under which the funder agreed to purchase 45% of Platinum's interest in and under its secured investment in AEI in exchange for providing \$500,000 to pay lawyers representing PPCO and lawyers and professionals working for AEI, AEX and AO (the "Participation Agreement"). The Participation Agreement and pre-Receivership agreements related to the payment of and security for fees for the same group of lawyers and professionals are described in the Baum and Schwartz Declarations. Schwartz Decl. ¶¶ 18-20; Baum Decl. ¶¶ 32-50. When the Participation Agreement was entered into, the Receiver understood that the costs of litigating the various Arabella matters could well exceed any recovery received, but that without immediate action the Arabella Interests would have been lost entirely. Schwartz Decl. ¶ 18; Baum Decl. ¶ 48.

The Receiver is not seeking approval of the Participation Agreement or related Arabella matters in this application. The Receiver has described the Participation Agreement in this application in order to give the Court a full picture of the events leading up to the Arabella Settlement Agreement. The Receiver anticipates submitting separate applications regarding other Arabella-related matters in the future. Schwartz Decl. ¶ 20. This application seeks only the approval of the Arabella Settlement Agreement. As noted above, the parties to the Arabella Settlement Agreement cannot carry out the plan they agreed to in the Mediation to monetize the Arabella Interests (and thus obtain a recovery for the Receivership Estate) without this Court's approval of Arabella Settlement Agreement.

### **Consent**

The SEC Staff consents to the relief requested in the instant application. However, the SEC has expressed concerns regarding the Participation Agreement and the apparent conflict of interest by counsel who was involved in that agreement, and has therefore requested that all matters concerning the participation agreement, retention of attorneys, and payment of fees be separately presented to the Court. The Receiver has agreed to do so. Given the complicated nature of this Arabella Settlement Agreement, Cooley has not sought the consent of the non-Receivership Entity defendants in the above-captioned action in advance of filing this application. Under the Court's order of March 23, 2017, those defendants have seven calendar days to advise the Court of their position on this application.



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Respectfully submitted,

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Enclosures