UNITED STATES DISTRICT COURT
DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION, Plaintiff, -v- PLATINUM MANAGEMENT (NY) LLC; PLATINUM CREDIT MANAGEMENT, L.P.; MARK NORDLICHT; DAVID LEVY; DANIEL SMALL; URI LANDESMAN; JOSEPH MANN; JOSEPH SANFILIPPO; and JEFFREY SHULSE, Defendants.	No. 16-cv-6848 (BMC)(VMS)

SUR-REPLY BRIEF OF RECEIVER IN FURTHER RESPONSE TO THE FILINGS OF SCHAFER & WEINER ON JUNE 11 AND JUNE 13, 2018 IN SUPPORT OF ITS FEE APPLICATION

Melanie L. Cyganowski, duly appointed Receiver (the "***Receiver***") of various Platinum entities, respectfully submits this joint sur-reply brief in response to the filings of Schafer and Weiner PPLC ("***S&W***") on June 11, 2018 (the Memorandum in Opposition to the Receiver's Cross-Motion for Disgorgement of Fees and in Reply to the Receiver's Objection to Schafer and Weiner's Final Application (the "***S&W Reply***")) [Dkt. No. 332] and June 13, 2018 (the letter to the Court from Norman I. Klein, Esq. (the "***S&W Sur-reply***")) [Dkt. No. 335] (collectively, the "***S&W Filings***").

Preliminary Statement

Despite significant inaccuracies (addressed below), the S&W Filings nevertheless confirm the following core facts underpinning the Receiver's and Securities and Exchange Commission's ("***SEC***") opposition to S&W's fee application:

(1) After previously agreeing to continue working on the Arabella Loan work-out in return for a purported "first-out" participation in the loan, in the face of a foreclosure action that threatened Platinum's collateral, S&W nevertheless informed Platinum's prior management that it would not do any more work unless a portion of its outstanding fees were paid down;

(2) S&W advised Platinum's prior management that a total of $500,000 was needed to pay past and future fees of S&W and certain other professionals in order to protect the collateral;

(3) at prior Platinum management's request, S&W and the Arabella chief restructuring officer set out to find a party to purchase a participation in the Arabella Loan to fund the supposedly necessary professional fees; and

(4) after the commencement of this receivership, S&W – whose retention was never approved by this Court – drafted the Participation Agreement and advised the Prior Receiver to execute it, knowing that the proceeds would be used to pay down S&W's outstanding pre-receivership fees without prior Court approval.

For the reasons set forth in the Receiver's opening submission, these basic undisputed facts necessitate denial of S&W's fee application and the granting of the Receiver's cross-motion for disgorgement. S&W's resort to unsupportable interpretations of the Receiver Order (contradicted by its own prior words and actions) and distortions of the record in order to defend its conduct and to support its fee application are powerful evidence that no such legitimate support exists.[1]

[1] This sur-reply is intended primarily to correct the record with respect to certain of S&W's misrepresentations of fact in its filings. It is not intended to respond to all of the factual and legal misstatements in the S&W Filings. The Receiver's failure to address any particular point raised in the S&W Filings should not be construed as the Receiver's acquiescence to that point.

Argument

A. S&W's Position That It Is "Retained Personnel" Entitled to "Reasonable Compensation" Without Having Been Approved by the Court Is Baseless

S&W's interpretation of the Order Appointing Receiver (the "***Receiver Order***") [Dkt. No. 6][2] that it is entitled to reimbursement of professional fees without its retention ever having been approved by the Court is insupportable. S&W maintains that, under the "clear, unambiguous language of the . . . Receiver Order," "*any* person or entity that acts as the Receiver's agent or whom the Receiver solicits to perform work for the Receiver is 'Retained Personnel'" "entitled to 'reasonable compensation,'" whether or not that person or entity was "formally engaged" by the Receiver with "Court approval." (S&W Reply at p. 11-12.) According to S&W, "Court approval is not a requirement to be 'Retained Personnel,'" and "[e]ngagement has no bearing on whether 'Retained Personnel' can receive 'reasonable compensation.'" (*Id.*, at p. 13.) Rather, S&W maintains that, under "the plain language of the Second (and First) Receiver Order," "[p]rofessionals do not need court approval of their engagement to be considered 'Retained Personnel' and receive 'reasonable compensation.'" (*Id.*, at p. 14) S&W's position is contradicted by both the plain words of the Receiver Order and S&W's own words and conduct.

The Receiver Order, plainly and unambiguously, authorizes the Receiver "[t]o engage and employ persons in the Receiver's discretion to assist the Receiver in carrying out the Receiver's duties and responsibilities hereunder, including, but not limited to, . . . attorneys. . ., *subject to Court approval*." (Receiver Order, ¶ 6(F) (emphasis added.)) Consistent with the foregoing, it further provides that: "Subject to the specific provisions of this Order, the Receiver is authorized to solicit persons and entities ("Retained Personnel") to assist the Receiver in

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[2] There is no plausible explanation as to why S&W relies on the Second Amended Order Appointing Receiver (the "***Second Receiver Order***") [Dkt. No. 276] that was not entered until well *after* the June 13, 2017 date on which S&W asserts that its representation of Platinum ended. In all events, the provisions regarding "Retained Personnel" on which S&W relies are identical or virtually identical in both the Receiver Order and Second Receiver Order.

carrying out the duties and responsibilities described in this Order. The Receiver *shall not* engage any Retained Personnel *without first obtaining an Order of the Court* authorizing such engagement." (*Id.* ¶ 49 (emphasis added).) In short, the Receiver Order – which S&W's time records reflect its managing partner, Michael Baum, thoroughly read the day after the receivership commenced [Dkt. No. 326-3, at p. 92 of 109] – clearly and unequivocally conditions the Receiver's authority to retain, engage and/or utilize professionals on obtaining prior Court approval, approval which S&W never obtained.

S&W's view of the Receiver Order ignores the clear obligation of the Receiver to obtain prior Court approval before engaging professionals, including attorneys. Indeed, according to S&W, the Receiver *is authorized* to hire any professional as he or she sees fit *without* Court approval, to instruct the professional to perform whatever services for the receivership estate the Receiver wishes and then to apply to the Court for compensation for the professional. This is so, according to S&W, because he or she did work for the Receiver, and is therefore "Retained Personnel". In other words, according to S&W, the language repeated throughout the Receiver Order requiring Court approval of Retained Personnel is a nullity. This makes no sense.

S&W's interpretation flies in the face of generally accepted rules of construction, as well as accepted SEC receivership practice. (*See* Jacobson Decl. ¶¶ 10-15[3].) It also flies in the face of S&W's own words and conduct. Exhibit L to the S&W Reply includes an exchange of e-mails in mid-May between S&W's Michael Baum and Cooley's Celia Barenholtz. In an e-mail dated May 11, 2017, Baum wrote: "I would like to know whether there is a draft of the application for the receiver to have us appointed as his counsel that we can review. *This is a very*

[3] References to "Jacobson Decl." are to the contemporaneously filed Declaration of Neal Jacobson in Further Support of Plaintiff Securities and Exchange Commission's Joinder to Receiver's: (i) Opposition to Application of Schafer & Weiner, PLLC for Allowance of Compensation and Reimbursement of Expenses Incurred from December 19, 2016 through June 13, 2017, and (ii) Cross-Motion for Disgorgement of Previously Paid Legal Fees, at the indicated paragraph(s) or exhibit(s).

important pleading for us because, as you know, we are a small boutique law firm and *we need to know where we stand in our ability to get paid in this case*." (S&W Ex. L, at p. 4 of 16) Without question, Baum understood that Court approval of his appointment as counsel to the Receiver dictated his "ability to get paid in this case." Moreover, as set out in the Jacobson Decl., Baum's understanding that his retention required Court approval accorded with his substantial experience and practice in bankruptcy court. (Jacobson Decl. ¶¶ 19-23.) His argument now to the contrary represents a complete about face and is entirely unsustainable. Because neither the Prior Receiver nor current Receiver ever sought approval of S&W's retention, its fee application – by the plain words of the Receiver Order – cannot be granted.

Finally, S&W's contention that it was appropriate for it to receive payment of pre-receivership fees ahead of similarly situated claimants without Court approval runs contrary to the law and practice. Pre-receivership legal fees are no different than any other unsecured claim, and there was no basis for S&W to obtain a preferred position over other creditors or defrauded investors. *See, e.g., SEC v. Capital Consultants, LLC*, 397 F.3d 733 (9th Cir. 2005).

B. <u>S&W's Mischaracterizations</u>

S&W seeks to justify its conduct that it appropriately advised the Prior Receiver to enter into the Participation Agreement by claiming that "[t]he Initial Receiver and Guidepost were further advised by their counsel, Cooley LLP," which "drafted a memorandum on the Participation Agreement" that "it shared with the SEC prior to execution of the Participation Agreement." (S&W Reply, at p. 6; *also* pp. 17-18.) Said another way, S&W asserts that the Prior Receiver entered into the Participation Agreement not only on its recommendation, but with "advice he received from Cooley" and the imprimatur of the SEC. (*Id.*) This is wrong and misleading.

To support its claim that Cooley "drafted a memorandum on the Participation Agreement" that "it shared with the SEC prior to execution of the Participation Agreement" S&W cites an e-mail, *dated April 12, 2017* (more than four months *after* the Participation Agreement was signed). (*See* S&W Reply Ex. K.) However, the record shows that neither Cooley nor the SEC had any involvement with, or knowledge of, the Participation Agreement until *after* its consummation. As set forth in the Jacobson Decl., which appends contemporaneous records, Cooley informed the SEC that it "was not involved in the negotiation of the Participation Agreement. Nor was it involved with any of the Arabella-related litigations." (Jacobson Decl. ¶¶ 33-36 & Ex. 5.) Rather, Cooley has stated that it had no role with respect to Arabella until April 2017.

Nor did the SEC have any knowledge of the contents of the Participation Agreement, or of S&W's post-receivership receipt of pre-receivership fees, until April 2017, when the SEC immediately raised objections to both. (Jacobson Decl. ¶¶ 24-32 & Ex. 4.) On January 3, 2017 (before S&W contends signature pages on the Participation Agreement were released from escrow), the SEC received eight pages of bullet points concerning the status of the Receivership, of which, on one-third of one page there was a brief discussion of an "Arabella Participation." (*Id.*) But the three bullet points regarding the "Arabella Participation" contained no description of (i) the purchaser of the participation, (ii) the terms under which the participation was being offered, or (iii) the exact use of the proceeds of the participation funds. (*Id.*) The bullet points implied that the funds would be used to pay professionals on a going forward basis "to continue the process of trying to obtain a recovery," but they do not state they would be used to pay legal fees for work performed prior to the receivership. (*Id.*) In all events, the bullet points led the SEC to believe that it was not even certain the Participation Agreement would be consummated,

since "Platinum ha[d] not been able to finalize the arrangement" at that point. (*Id.*) Thus, as set forth in the Jacobson Decl., the SEC had "no knowledge of the existence or terms of any signed Participation Agreement" until April 2017, *months after the fact*. (*Id.* ¶ 26.)

In addition to mischaracterizing the evidence concerning Cooley's and the SEC's knowledge of, and consent to, its activities, S&W also misstates the facts concerning one of the other central underpinnings of its defense, namely, that the Prior Receiver was authorized to enter into the Participation Agreement and to pay $180,000 of S&W's pre-receivership fees without Court approval. S&W's own words and conduct belies its contention. As set forth in the Jacobson Decl., Cooley originally submitted an application to the SEC for review in April 2017 that sought Court approval of the Arabella Settlement [Dkt. No. 128], as well as the retention of S&W *and* the entering into the Participation Agreement *nunc pro tunc*. (Jacobson Decl. Ex. 2) According to e-mails between S&W and Cooley in April 2017, and subsequently obtained by the Receiver, S&W was aware of Cooley's intention to seek *nunc pro tunc* approval of the Participation Agreement and never disputed the need for such approval.[4] To the contrary, early drafts of a Baum declaration in support of the application (which the Receiver subsequently obtained), contain sections on "The Need for the Participation Agreement" and "The Uses of the Participation Agreement Funds" that plainly were intended to support *nunc pro tunc* approval of the Participation Agreement. S&W's current position that no such Court approval ever was required and that the Prior Receiver was authorized to enter into the Participation Agreement and pay S&W's pre-receivership fees without Court approval is contradicted by its prior actions. In sum, S&W's defense of its conduct is premised on misstatements of fact and changed stances.

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[4] To preserve privileges and/or immunities applicable to prior communications between Cooley and S&W, the Receiver does not attach, or disclose the contents, of such communications to or in this sur-reply. The Receiver, however, can share with the Court for *in camera* review the communications between Cooley and S&W referenced herein.

C. S&W's Reliance on the Arabella Bankruptcy Court's Ruling Denying the Transfer of the Receiver's Claim Is Misplaced

In the S&W Filings, S&W places heavy emphasis on the Arabella Bankruptcy Court's recent denial of the relief requested by the purported purchaser of the Arabella participation, 30294 to transfer to 30294 the Receiver's proof of claim in the AEX bankruptcy case. (*See, e.g.*, S&W Reply, at p. 24; S&W Sur-reply.) S&W urges that this Court is somehow bound by the Arabella Bankruptcy Court's interpretations of the Receiver Order, by arguing that the "Receiver already litigated whether the Initial Receiver needed court approval" to enter into the Participation Agreement and "is estopped from attempting to now litigate the very same issue before this Court." (S&W Reply, at p. 24.) In fact, when reading its ruling into the record, the Arabella Bankruptcy Court repeatedly stated that the ultimate interpretation and enforcement of the Receiver Order is within *this* Court's province. (*See, e.g.,* Dkt. No. 335-1, at pp. 8 of 19 ("if Judge Cogan deems my actions today to be a violation of Judge Irizarry's Order, he's certainly free to void them") & 9 of 19 ("I'm not dealing with any allegations concerning those improprieties. I'll leave those for another day to Judge Cogan").)

In all events, S&W's suggestion that the Receiver is unable to litigate the propriety of S&W's post-receivership receipt of pre-receivership fees in this Court, either as a matter of *res judicata*, judicial estoppel or otherwise, is erroneous. First, the Arabella Bankruptcy Court did not decide, and did not have a developed record to decide, the appropriateness of S&W's conduct or entitlement to fees. Second, even if the Arabella Bankruptcy Court's interpretations of the Receiver Order were relevant to the issues at hand in this proceeding (which they are not), the Bankruptcy Court's interpretation of the Receiver Order in a decision that ruled in the Receiver's favor (and thus from which the Receiver has no appellate rights) has no preclusive effect. (*See, e.g.,* Restatement (Second) of Judgments § 28, Comment a. (1982) ("If review is

unavailable because the party who on the issue obtained a judgment in his favor, the general rule of § 27 ["Issue Preclusion – General Rule"] is unavailable by its own terms")) And, third, judicial estoppel – which prevents a party from taking a position in a subsequent proceeding that is different from a position it prevailed on in an earlier proceeding – is inapplicable here, where the Receiver's position has been entirely consistent. In short, S&W's reliance on the recent Arabella Bankruptcy Court's ruling to support its fee application in this Court is misplaced.

Conclusion

For all the foregoing reasons, and those set forth in (1) the Receiver's opposition to S&W's fee application and cross-motion for disgorgement and (2) the SEC's joinder in same, the Court should deny S&W's fee application in its entirety and grant the Receiver's cross-motion awarding the Receivership estate disgorgement of S&W's post-receivership receipt of pre-receivership fees totaling $180,000.

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Respectfully submitted,

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