UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION, Plaintiff, - against - 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.	:	Docket No.:16-CV-6848 (BMC)

RECEIVER'S OMNIBUS MEMORANDUM OF LAW IN OPPOSITION TO: (I) DEFENDANT JOSEPH SANFILIPPO'S MOTION FOR THE SEC RECEIVER TO INDEMNIFY HIM PROMPTLY FOR HIS REASONABLE ATTORNEYS' FEES AND DEFENSE COSTS; AND (II) DEFENDANT DAVID LEVY'S MOTION TO COMPEL INDEMNIFICATION

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Melanie L. Cyganowski, the duly appointed Receiver (the "Receiver") of various Platinum entities (the "Receivership Entities" or "Platinum"), respectfully submits this Omnibus Memorandum of Law in Opposition to: (i) Defendant Joseph SanFilippo's ("SanFilippo") Motion to Compel the SEC Receiver to Indemnify Him Promptly for His Reasonable Attorneys' Fees and Defense Costs, Dkt. No. 490, (the "SanFilippo Motion") and (ii) David Levy's ("Levy" and collectively with SanFilippo, the "Defendants") Motion to Compel Indemnification, Dkt. No. 494, (the "Levy Motion" and together with the SanFilippo Motion, the "Motions").

PRELIMINARY STATEMENT

This Court has already ruled that the Defendants are not entitled to "jump the line" ahead of the claims of other unsecured creditors, let alone the entities currently claiming to have senior secured claims against the receivership assets, and against whom, and with respect to which, the Receiver is currently actively litigating.[1] Yet, that is exactly the relief sought by the Defendants, whose Motions do not provide any legal or factual basis for this Court to revisit its November 25, 2018 Memorandum Decision and Order, Dkt. No. 417 (the "Indemnification Decision"). For this reason alone, the Motions should be denied. In addition, the Motions should be denied because:

- As Judge Rakoff recently ruled on a motion brought by Levy in the Senior Lien Litigation, it is still premature, even following his acquittal, for Levy to be deemed entitled to the indemnification he seeks. The same reasoning applies to SanFilippo, as, both Defendants are still subject to civil liability, as well as potential subordination of their claims.

- The Defendants' claims arise out of pre-receivership obligations, and should be treated in the same manner as all the other pre-receivership claims. That is, they should be subjected to the claims adjudication process that will be instituted by the Receiver once the Senior Lien Litigation is resolved.

[1] *Cyganowski, et al v. Beechwood Re LTD. et al*, U.S. District Court for the Southern District of New York, Case No. 18-cv-12018 (JSR) (the "**Senior Lien Litigation**").

- Neither the Defendants, nor their counsel, have added value to the receivership estate merely by virtue of their criminal acquittals. As a result, they are not entitled to a priority payment either as an estate professional (they have not been retained), or upon what appears to be Defendants' analogy to a Bankruptcy Code 503(b)(1)(A) administrative expense priority claim.

- To the extent the Motions are motions to reconsider the Indemnification Decision, or to appeal the same, they are untimely and should be overruled.

For these reasons, as more fully set forth herein, the Defendants' Motions should be denied.

FACTUAL BACKGROUND

A. The Operating Agreements

The Defendants' claims for indemnification are premised on provisions contained within various operating agreements. Both Defendants rely on Section 5.4 of the Platinum Partners Credit Opportunities Fund LLC Fourth Amended and Restated Limited Liability Company Agreement (the "PPCO LLC Agreement"). SanFilippo Motion at 5; Levy Motion at 5. Additionally, Levy relies on:

i. Section 11.2 of the Amended and Restated Operating Agreement of Credit Funding LLC (the "Credit Funding Agreement");

ii. Section 5.4 of the Third Amended and Restated Operating Agreement of Limited Partnership of Platinum Partners Credit Opportunities Master Fund LP (the "PPCO LP Agreement"),

iii. Section 5.4 of the Platinum Partners Credit Opportunities Fund (TE) LLC Fourth Amended and Restated Limited Liability Company Agreement (the "PPCO (TE) LLC Agreement"), and

iv. Section 5.4 of the Platinum Partners Credit Opportunities Fund (BL) LLC Amended and Restated Limited Liability Company Agreement (the "PPCO (BL) LLC Agreement" and collectively with the Credit Funding Agreement, the PPCO LP Agreement and the PPCO (TE) LLC Agreement, the "Agreements"). Levy Motion 2-5.

The cited provisions within each of the Agreements contain similar language and have carve-out provisions that nullify the Defendants' rights to indemnification if the defendants are found to have acted with, among other things, gross negligence, willful misconduct or violation of the law, and/or fraud (the "Bad Actor Exclusions").

B. The D & O Policy and Indemnification Decision

Prior to the onset of the receivership, Platinum increased its directors' and officers' liability insurance policy ("D & O Policy") from $5 million to $25 million, from which the Defendants sought and obtained reimbursement of their attorneys' fees and costs incurred as a result of the Criminal Case[2] and other matters. *See Freedom Specialty Ins. Co., et al. v. Platinum Management (NY) LLC, et al.*, Supreme Court of the State of New York, County of New York, Index. No. 652505/2017, Dkt. No. 15. In addition to increasing the D & O Policy, Platinum management or its affiliates purportedly entered into agreements to pay legal fees incurred by certain Platinum management-related officers and directors, including Levy's counsel Wilson Sonsini Goodrich & Rosati P.C. ("WSGR") (Dkt. No. 404-406 at 165-166), and SanFilippo's counsel, Ford O'Brien, LLP (Dkt. No. 392 at 6-7).

In October 2018, nearing the exhaustion of the D & O Policy, and with the criminal trial still months away, the Defendants sought to compel the Receiver to advance their attorneys' fees and costs. Dkt. Nos. 392 and 402. Following briefing, this Court issued its Indemnification Decision, holding, *inter alia*, that the Defendants were not entitled to priority payment ahead of other unsecured creditors and that the Defendants' claims were neither administrative nor secured. Indemnification Decision at 1, 9.

[2] References to the "Criminal Case" are to *United States v. Nordlicht, et al.*, No. 1:16-cr-00640-BMC (E.D.N.Y. 2016).

C. The Criminal Case

Following the Criminal Case, the jury returned a verdict acquitting SanFilippo on all counts with which he was charged, and convicting Levy of defrauding bondholders in portfolio company Black Elk Offshore Operations LLC, but acquitting him on the remaining charges. Criminal Case, Dkt. No. 774. Subsequently, Levy filed a Rule 29 motion for a judgment acquittal, which the Court granted. Criminal Case, Dkt. No. 785, 800. The Department of Justice is appealing that decision. Criminal Case, Dkt. Nos. 803-805.

D. The Senior Lien Litigation

On December 19, 2018, the Receiver commenced the Senior Lien Litigation, seeking, among other relief, the avoidance of certain liens which may otherwise adversely impact potential distributions to investors and creditors, as well as damages for claims arising from a fraudulent scheme perpetrated to the detriment of Platinum. Senior Lien Litigation Amended Complaint, Dkt. No. 207 at 1. The defendants in the Senior Lien Litigation have presented documentation purporting to grant them security interests in all or certain of Platinum's assets, which exceeds the total value of the Receivership Entities. *Id.* As of September 30, 2019, the Receivership Entities have approximately $37.7 million in cash. Receiver's Ninth Status Report at 12, Dkt. No. 495 (the "Status Report"). Such amount is less than the secured debt at issue in the Senior Lien Litigation, meaning that if the Receiver loses that litigation, there may not be any cash available for distribution to unsecured creditors, such as the Defendants. Declaration of Melanie L. Cyganowski, as Receiver, in Support of Omnibus Opposition to Defendants' Indemnification Motions (the "Cyganowski Decl.") at ¶ 2.

ARGUMENT

POINT I:

THE DEFENDANTS' CLAIMS ARE NOT ENTITLED TO PRIORITY

This Court has already ruled that the Defendants are not entitled to upend the priority of creditors' entitlement to payment from this receivership estate by claiming entitlement to payment ahead of not only unsecured creditors, but secured and administrative creditors as well. The Defendants' claim to the contrary has no support in law or fact because the indemnification sought by the Defendants is a pre-receivership obligation, and the claims are not administrative or secured. The Receiver should therefore be allowed to continue to "apply [ ] the fundamental rule of equal distribution among creditors of like kind." Indemnification Decision at 9.

As this Court explicitly held, the Defendants' claims were neither secured nor administrative. "The former officers want [100% payment], as if their claims were secured or administrative, which they are not." Indemnification Decision at 9. Therefore, this Court's consideration of these Motions should end there, and any consideration of Defendants' indemnification claims should be deferred until the claims of the other unsecured creditors are adjudicated following the resolution of the Senior Lien Litigation.

A. The Defendants' Indemnification Agreements are Pre-Receivership Obligations

The Defendants' indemnification claims are nothing more than unsecured pre-receivership obligations that are not entitled to priority. *See SEC v. Lauer*, 2012 WL 12892878, at *1 (S.D. Fla. July 24, 2012). In *Lauer*, John W. Bendall, Jr. ("Bendall") was a member of the Board of Directors of his former employer, Lancer Offshore, Inc. and Omnifund Ltd. ("Lancer"). The Securities and Exchange Commission ("SEC") brought an enforcement action against Lancer, and Bendall was subpoenaed in connection with the SEC's enforcement action. *Id.*

Bendall asserted that he was entitled to indemnification based on a pre-receivership agreement issued by Lancer, and he sought to have his post-receivership attorneys' fees and costs paid from the receivership estate. *Id.* The district court rejected his request, holding that, "Bendall's purported indemnification claim of the Legal Fees is no different than any other claim against the Lancer Entities arising from pre-receivership occurrences and pre-receivership contract[s]." *Id.* at *2. Similarly here, the Defendants seek to have Platinum reimburse their post-receivership attorneys' fees and costs based on the pre-receivership Agreements. Thus, just like Bendall's claims in *Lancer*, the Defendants are no different than the other unsecured claims against the receivership, and are not entitled to priority.

Due to the limited amount of case law available regarding receiverships, receivership courts often look to bankruptcy law for guidance. *See SEC v. Elliott*, 953 F.2d 1560, 1567, 1572-73 (11th Cir. 1992) (analyzing bankruptcy law in the receivership context); *Marion v. TDI Inc.*, 591 F.3d 137, 148 (3d. Cir. 2010) (same); *Fidelity Bank, Nat'l Ass'n v. M.M. Grp., Inc.*, 77 F.3d 880, 882 (6th Cir. 1996) (finding it "appropriate and helpful to refer to the rules governing appellate standing in bankruptcy proceedings" when no case law existing regarding the rules in a receivership action). Under a bankruptcy analysis, Defendants' claims that the Agreements are administrative also fail. *See e.g. In re Consolidated Oil & Gas, Inc.*, 110 B.R. 535, 537 (Bankr. D. Colo. 1990) (directors' and officers' indemnification claims were not administrative expenses because the "claimants provided services to the Debtor pre-petition, exclusively and entirely"); *In re Amfesco Industries, Inc.*, 81 B.R. 777, 785 (Bankr. E.D.N.Y. 1988) ("while the Applicants may be entitled to indemnification by the Debtors, whether by statute or by contract or both, as compensation for services rendered…[it] is not sufficient to grant the claims administrative priority").

In *In re Mid-American Waste Systems, Inc.*, 228 B.R. 816 (Bankr. D. Delaware 1999), directors and officers of Mid-American Waste System, Inc. ("MAWS") sought to have their indemnification claims treated as priority administrative expenses. The claimants argued that their right to indemnification did not arise until after the bankruptcy estate and therefore were post-petition. The bankruptcy court rejected the claimants' arguments and held:

> "An indemnification claim by an officer or director based on that officer's or director's prepetition services is not a claim on account of 'services rendered after the commencement of a case' that is entitled to administrative expense priority. Instead, the O & D Claimants' indemnification claims are merely claims for prepetition compensation for services rendered, not unlike salary or other benefits."

Id. at 821.

Here, the Agreements were entered into well before the receivership. Furthermore, the conduct giving rise to the Defendants' indemnification claims occurred before the receivership. The Defendants stood trial for conduct that occurred *before* the receivership was created. "It makes no difference that the duty to indemnify [the officer of the corporation] for litigation expenses, if such duty exists, did not accrue until after the petition was filed when [the officer of the debtor] incurred those expenses; the critical fact is that the claim for indemnity arose from prepetition services [the officer of the debtor] provided the corporation." *In re Christian Life Center*, 821 F.2d 1370, 1374 (9th Cir. 1987). Similarly, here, although the purported indemnification obligations did accrue until after the receivership, the Defendants' claims for indemnification arose from pre-receivership services they provided to Platinum.

In addition to Levy seeking indemnification for his legal fees and expenses, his attorneys, WSGR, themselves seek direct compensation on the basis of a "direct" agreement with Platinum. Like Levy's agreements, Platinum's alleged agreement with WSGR is a pre-receivership

obligation, and WSGR's claims against the receivership should be treated just like every other general unsecured creditor, that is, they are not entitled to priority.

For these reasons, the Defendants' Agreements are *pre-receivership* obligations, and therefore, not analogous to administrative expenses entitled to priority. Thus, even if entitled to all the indemnification they seek, but have not yet articulated, they are not entitled to be paid in full, and ahead of other unsecured creditors.

B. The Defendants' Indemnification Claims are Not Administrative

Even if this Court had not already determined that the Defendants' indemnification claims are not administrative, nothing in their Motions rehabilitates them to that status.

Section 503(b)(1)(A) of the Bankruptcy Code defines administrative expenses as "the actual, necessary costs and expenses of preserving the estate including wages, salaries or commissions for services *rendered after the commencement of the case*." 11 U.S.C. § 503(b)(1)(A) (emphasis added). As held in a case cited by the Defendants, to qualify as an administrative expense "the bankrupt estate must incur (1) a post-petition obligation (2) as a result of actions that benefited the estate." *Andrikopoulous v. Silicon Valley Innovation Company, LLC*, 120 A.3d 19, 22-3 (Del. Ch. 2015) *aff'd*, 142 A.3d 504 (Del. 2016) (Strine, C.J.). The Defendants fail this test for several reasons.

First, as previously discussed, the Agreements are *pre-receivership* agreements, and as discussed below, the Defendants' acquittals did not add value to the receivership estate.

Second, the Defendants' professionals have not been retained by the Receiver, nor approved as such by this Court, pursuant to the applicable terms of the Receivership Order, Dkt. No. 276, or otherwise.

Third, even if "value added" were the standard, which it is not, the Defendants' acquittals did not "remove [ ] the cloud hanging over the estate" as they claim. Levy Motion at 14. The Defendants' assertions are simply not true, and the Defendants present no admissible evidence to support their contentions that they "provided similar value" to the estate as the estate's actual retained professionals have.

SanFilippo has not pointed to a single receivership asset whose value was depressed as a result of his indictment, but specifically has now increased or stabilized in value following his acquittal. Simiarly, Levy mistakenly relies on the Receiver's sale of LC Energy LLP ("LC Energy") to support his claims that his acquittal provided value to the receivership estate, which is a complete mischaracterization. Levy Motion at 15. To the contrary, LC Energy has been one of the most challenging assets in the Platinum portfolio. The Receiver had to *pay* $380,000 to the purchaser of LC Energy for potential environmental liabilities, and give the purchaser an assignment of $250,000 in cash collateral. Status Report at 12, 20. That is a far cry from the successful post-acquittal sale described by Levy. Furthermore, the Defendants unsupported assertions are moot, as the Receiver has largely sold all of the receivership assets. *See generally*, Status Report. The market has spoken, and the asset values are the true asset values, irrespective of the acquittals.

C. The Defendants' Indemnification Claims are Not Secured

The Defendants' claims are not secured, and therefore not entitled to priority payment. Specifically, the Defendants have not cited to a security agreement with Platinum and they do not assert that they have a security interest in the receivership assets. A review of the Agreements confirms the lack of a contractual basis for a claim of a security interest by the Defendants. Even if the Defendants had established a secured position, they have not alleged,

much less proven, that their secured status is senior to those of the defendants in the Senior Lien Litigation, whose aggregate claims exceed the cash currently held by the receivership. Cyganowski Decl. ¶ 2. As such, they do not have priority over secured or unsecured creditors.

D. The Defendants Misconstrue *Lawson v. Young* and *SEC v. Illarrandendi*

Just as they did on their previous motions, the Defendants cite to Delaware's strong policy in favor of indemnification. However, Levy's reliance on *Lawson v. Young*, 21 Ohio App.3d 190 (Ohio Ct. App. 1984) and *SEC v. Illarrandendi*, No. 3:11CV78 JBA, 2014 WL 545720 (D. Conn. Feb. 10, 2014), in support of his contention that Delaware's policy supports his claims for immediate indemnification, is misplaced. In *Lawson* and *Illarrandendi*, indemnification and advancement were awarded to the defendants after the former directors and officers successfully prevailed in suits brought against them *by the receiver*.

However, the critical difference in this case is that the Receiver did not bring suit against the Defendants. The Department of Justice and SEC and not the Receiver initiated suit against the Defendants. This Court recognized the distinction between the Receiver and the Government in the Indemnification Decision. Indemnification Decision 8-9. The receivership was not involved in either the prosecution of the criminal case by the Department of Justice or the advancement of the civil litigation by the SEC, and thus is not responsible for payment of their legal fees.

POINT II:

THE DEFENDANTS' INDEMNIFICATION CLAIMS ARE PREMATURE

The Defendants' claims for immediate reimbursement of their legal fees and expenses are premature because even if their acquittals stand, Levy and SanFilippo may be found civilly liable and/or the claims process may determine that the Bad Actor Exclusions render them ineligible

for indemnification. As a result, to the extent this Court declines to overrule the Motions in their entirety, it should defer ruling on the Motions until all cases involving the Defendants are resolved, and the Receiver makes a determination whether to seek to subordinate their claims.

Deferment is the manner in which United States District Judge Jed S. Rakoff recently dealt with a motion by Levy in a case related to the Senior Lien Litigation. *David Levy v. Senior Health Insurance Company of Pennsylvania*, U.S. District Court for the Southern District of New York, Case No. 19-cv-3211 (JSR). In that motion, among other relief, Levy sought immediate advancement and indemnification of his legal fees and expenses from another party to that action pursuant to the terms of an advancement and indemnification obligation contained within an investment management agreement. *Id.* Judge Rakoff decided to defer Levy's motion for advancement and indemnification until the Court of Appeals decides the Department of Justice's appeal of this Court's decision granting Levy's Rule 29 motion, reasoning that "if the Government is successful on that appeal, Levy's current motion will be moot" because a finding that Levy engaged in "fraud, gross negligence, or willful misconduct" would negate his entitlement to advancement or indemnification under the agreements. *Id.* The Agreements at issue in these Motions contain similar exclusions, and thus, while the possibility of such findings against both Levy and SanFilippo stand, an enforcement of those provisions should be deferred.

As noted, the Bad Actor Exclusions may render the Defendants ineligible for Indemnification. Specifically, Section 5.4.2 of the PPCO LLC Agreement, provides, in part:

> *No indemnification may be made...as to which the indemnified party shall have been adjudged to be liable for gross negligence, willful misconduct, or fraud in the performance of its duties to the Company or would not otherwise be entitled to be held harmless.*

(PPCO LLC Agreement, § 5.4.2; emphasis added).

Section 11.2 of the Credit Funding Agreement, provides, in part:

> [T]he Company [Credit Funding] shall indemnify each Member, the Managing Member, and each Portfolio Manager, and their respective successors and assigns, and hold each of them harmless from and against any Damages suffered or incurred by such indemnified person…*except to the extent that a judgment or other final adjudication adverse to such Person establishes that his or her acts were committed in bad faith or were the result of gross negligence or willful misconduct.*

(Credit Funding Agreement, § 11.2; emphasis added).

Section 5.4(a) of the PPCO LP Agreement provides, in part:

> To the Fullest extent permitted by law, the Partnership shall indemnify, hold harmless, protect and defend each Protected Person against any losses, claims, damages or liabilities…*unless such Liability results from such Protected Person's own gross negligence as such term is constructed under the laws of Delaware, willful misconduct or a willful violation of the law.*

(PPCO LP Agreement, § 5.4(a); emphasis added).

The Criminal Case was not the only hurdle the Defendants had to overcome to prevent the application of these provisions, and even that, at least with respect to Levy is not over. The claims process remains,[3] as do actions relating to the Senior Lien Litigation, and the SEC's civil enforcement action.

On the basis that the Defendants' claims are premature, they should at a minimum, be deferred.

POINT III:

THE MOTIONS ARE UNTIMELY APPEALS

The Motions are nothing more than an attempt to revisit the Indemnification Decisions, and the Defendants have not set forth a basis for overturning it, even in the face of the Defendants' acquittals. In October 2018, the Defendants filed motions seeking advanced

[3] Pre-receivership obligations, such as the Defendants' indemnifications claims are subject to the claims process. *See Lauer*, 2012 WL 12892878 at *2. Once the Receiver submits her recommendation concerning the claims process to the Court, as this Court has previously recognized, the Receiver may seek to subordinate the Defendants' indemnification claims. Indemnification Decision at FN 5.

payment over other unsecured creditors. In the Indemnification Decision, this Court ruled that the Defendants are not entitled to "jump the line" ahead of the claims of other creditors. The Defendants' Motions are nothing more than an improper appeal of the Indemnification Decision. For almost any type of appeal, there is a limited period, within which an appeal must be filed. According to Federal Rules of Appellate Procedure 4, in civil cases, a notice of appeal must be filed in district court within 30 days after entry of judgment or order. The Defendants filed their Motions well after the 30 day time limit to file an appeal.

This Court already held, "Platinum Partners may well indeed owe reimbursement to these former officers. But it owes lot of money to people and entities that it lacks sufficient funds to pay.... The former officers have shown no compelling reason why they should get to jump the line." Indemnification Decision at 1. In the Defendants' present Motions, they again, do not present a compelling reason why their general unsecured claims should jump the line ahead of all the other unsecured creditors' of Platinum. The Indemnification Decision did not hold that if the Defendants were acquitted in their criminal trials that they would be entitled to immediate reimbursement of their attorneys' fees and costs. To the contrary, this Court's previous decision explicitly recognized that the Defendants' indemnification rights were still subject to further adjudication, such as a request by the Receiver for equitable subordination. Indemnification Decision at FN 5.

In sum, the issues of priority payment were already decided in the Indemnification Decision, and Defendants' Motions should not serve as an opportunity to revisit that decision.

CONCLUSION

For all of the foregoing reasons, the Defendants' Motions should be denied in their entirety.[4]

Dated: New York, New York
October 30, 2019

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[4] In the event the Court grants the Motions, and it should not, the Receiver reserves her right to challenge the quantum of any fees the Defendants may demand, and the receiver respectfully requests that the court convene an evidentiary hearing or equivalent process to evaluate the propriety of the Defendants' claims for reimbursement.