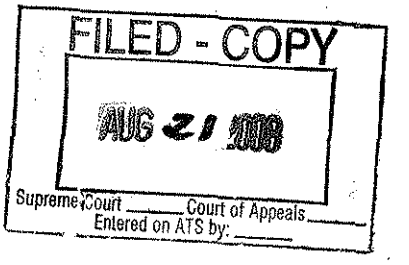
8-21-2008

Christian v. Mason Appellant's Brief Dckt. 35331

IN THE SUPREME COURT OF THE
STATE OF IDAHO

JERRY CHRISTIAN and JOY CHRISTIAN, husband and wife, Plaintiffs/Appellants, vs. DAVID MASON, Defendant/Respondent.	)	**Supreme Court Case No. 35331**



BRIEF OF APPELLANTS

On Appeal from the District Court of the Seventh Judicial
District of the State of Idaho, in and for the County of Bonneville

The Honorable Jon J. Shindurling, District Judge, Presiding

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I. STATEMENT OF THE CASE

A. Nature of the case: This case involves a claim by appellants, the Christians, to avoid a fraudulent transfer by Robert McClung to the appellee, Mason, following the revelation of McClung's operation of a Ponzi scheme in which both the Christians and Mason were victims. Mason received payments from McClung in excess of the amounts he originally was induced to give to McClung, while the Christians suffered a substantial loss and are judgment creditors of McClung.

B. Course of proceedings below: The parties cross-moved for summary judgment. The district court dismissed the Christians' claim, concluding the claim was the property of the estate of McClung's bankruptcy, and that the Christians lacked standing to pursue the claim. This appeal followed.

C. Statement of facts:

This case involves a Ponzi scheme in which both parties to this case were victims. Defendant Mason received over $32,000 more back from the perpetrator of the scheme, Robert McClung (who now resides in federal prison as a result of the scheme), than he gave to McClung. Plaintiffs the Christians, who suffered a loss of almost $155,000, sued to recover from Mason the amount of the excess, as a fraudulent transfer by McClung.

Christians filed their Complaint against Mason on July 20, 2006. CR 4. The first eight paragraphs of Christians' Complaint alleged as follows:

> 1. Plaintiffs JERRY CHRISTIAN and JOY CHRISTIAN, husband and wife, are residents of Idaho Falls, Idaho.

2. Defendant DAVID MASON is a resident of Idaho Falls, Idaho.

3. Plaintiffs are judgment creditors of Robert O. McClung ("McClung") in the amount of $154,690.80. A true and correct copy of the judgment in favor of Plaintiffs and against McClung is attached hereto as Exhibit A.

4. Plaintiffs and Defendant were victims of a fraudulent scheme by McClung in which he purported to act as an investment advisor and "day-trader," soliciting funds from victims and representing to them that he was investing the funds on their behalf via day-trading.

5. McClung provided Plaintiffs, Defendant and other victims with fraudulent "account statements" purporting to evidence investment gains. In fact, McClung engaged in virtually no trading of victim funds, and appropriated the funds for his own use, or to pay fictitious "gains" to some "investors" in a Ponzi scheme while the scheme remained active.

6. In approximately July 2002, the Idaho Department of Finance began investigating McClung's activities. McClung's fictitious "account statements" provided to victims showed that he "quit trading" on or about July 29, 2002. He sent a letter to victims at the end of August, 2002, providing excuses for not currently trading. His last statements (that showed no "trading") were for August and September, 2002.

7. On or about November 25, 2002, the Idaho Department of Finance initiated a civil lawsuit against McClung and entities he controlled as part of his fraudulent scheme seeking a judgment against McClung for unreturned victim funds, and to prohibit him from further violating the Idaho Securities Act.

8. On or about January 25, 2005, McClung pleaded guilty in United States District Court to a charge of mail fraud relating to his fraudulent investment scheme. A true and correct copy of McClung's plea agreement, in which he admits the operative facts of his fraudulent scheme, is attached hereto as Exhibit B.

> McClung was sentenced to approximately thirty-six months in prison, and presently is incarcerated in a United States correctional facility.

Complaint, ¶¶ 1-8; CR 5-6. In his Answer, Mason responded in pertinent part: "Defendant David Mason . . . hereby answers Plaintiffs Jerry and Joy Christian's (Christian) Complaint to Avoid Fraudulent transfer as follows: . . . 2. Admits paragraphs 1, 2, 3, 4, 5, 6, 7 and 8." Answer, ¶ 2; CR 22. Thus, Mason admitted that Christians are judgment creditors of McClung; that McClung perpetrated a fraudulent Ponzi scheme of which the parties were victims; that the account statements provided by McClung purporting to show investment gains were fraudulent; that McClung engaged in virtually no trading of "investor" funds, and appropriated the funds for his own use, or to pay fictitious "gains" to some victims; that McClung ultimately pleaded guilty to mail fraud as a result of his scheme; and that copy of McClung's plea agreement, in which he admitted the operative facts of his fraudulent scheme, was true and correct.

In his plea agreement,[1] McClung admitted as follows:

> The defendant assured Mr. Christian and other investors that their investment would be at minimal risk because all transactions would be closed out before the end of the close of business. The defendant further represented to Mr. Christian and other investors that they could earn three percent (3%) return per month on their investment. The defendant showed investors, including Mr.

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[1] McClung's plea agreement is also publicly available via the ECF and PACER systems for accessing the files of the United States District Court for the District of Idaho, as Document 13 filed in case number CR 04-0241-E-BLW. Idaho Rule of Evidence 201(b) provides that a court may take judicial notice of a fact when the fact is capable of accurate determination by resort to sources whose accuracy cannot reasonably be questioned. A court must take judicial notice if requested by a party and supplied with the necessary information. I.R.E. 201(d). Judicial notice may be taken at any stage of a proceeding. I.R.E. 201(f). Even absent Mason's admission regarding the accuracy of the plea agreement, the district court could and should have taken judicial notice of it and its contents.

> Christian, monthly statements with consistent earnings and no losses. . . . Mr. Christian and other investors would not have provided the defendant with investment funds had they known the defendant would misapply investment funds to his own personal use. Nor would Mr. Christian have invested monies when **the defendant was not, in fact, realizing profits from his purported day trading.** The evidence would show that defendant conducted day trading on only thirty-two (32) days during 2000, 2001, and 2002, not on a daily or regular basis as he represented to investors. Further more, the **defendant received approximately $1.7 million from approximately one hundred investors and caused investors to lose $1.1 million**. . . . The defendant misapplied a substantial sum of said investment proceeds to his own personal use.

Complaint, Ex. B, pp. 1-2 (emphasis added); CR 14-15. Thus, McClung admitted that his scheme did not produce "earnings," but that he was diverting funds to his personal use, and that over $1 million of his victims' money was unaccounted for.

Following the revelation of his Ponzi scheme, McClung filed for bankruptcy. On October 14, 2004, the Christians obtained a judgment against him in the bankruptcy proceeding in the amount of $154,690.80. CR 8-9. The judgment reflected that the Christians' claims against McClung were nondischargeable. CR 9.

McClung was sentenced to 37 months in federal prison for his crimes. Affidavit of Michael Christian ("Christian Affidavit"), Ex. A; CR 118. He served his sentence as an inmate in federal prison in Elkton, Ohio. Christian Affidavit, Ex. B; CR 126-127.

Unlike the Christians, Mason received $32,873.12 more from McClung than he provided to him. *Affidavit in Support of Motion for Summary Judgment (David Mason)*, ¶ 7; CR 66. Mason admitted that he "invested" various amounts with McClung. Mason Affidavit,

¶¶ 4, 5; CR 66. His affidavit, and the "account statements" attached to his affidavit, the accuracy of which he acknowledged, showed total additions of $166,042.06 and total withdrawals of $198,915.18, resulting in excess payments to Mason of $32,873.12. Mason Affidavit, ¶ 4 and Ex. B; CR 66, 68-88.[2] The excess was included in the last payments to Mason of $14,000 on July 22, 2002, $709.13 on July 29, 2002, and $30,905.06 on October 2, 2002. CR 27, 49, 66, 68, 86. Mason acknowledged the dates and amounts of these withdrawals in his brief in support of his own summary judgment motion. CR 27.

The parties cross-moved for summary judgment. Mason initially asserted, without substantiation, that any excess "in Mason's account" actually belonged to his father, and that he only "invested for" his father. CR 66; CR 27. No corroborating evidence of any kind supported these conclusory assertions. Whether he ultimately owed the money to his father is irrelevant, however, if Mason was the transferee of money from McClung. In briefing on the parties' cross-motions for summary judgment, Mason acknowledged that he was the transferee. CR 27 ("After November 2001, reported earnings continued to be withdrawn each month and eventually the principal was paid back to Mason by McClung."). Mason also admitted that the money "was invested with Mr. McClung under my name." Mason Affidavit, ¶ 6; CR 66. The documents attached to Mason's affidavit showed that from May of 2001 on, only David Mason dealt with McClung, and money was paid by McClung to David Mason himself. Mason Affidavit, Ex. B; CR 68-88. Documents produced by Mason in discovery showed that, on the

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[2] Mason's own accounting, attached as Exhibit A to his affidavit, erroneously omitted the $1,476.18 he received from McClung in September 2001, as reflected in the "account statement" for that period. CR 76.

dates corresponding to the excess payments of $14,000 on July 22, 2002 and $30,905.06 October 2, 2002, David Mason wrote checks from the checking account for his business to an investment account owned by him, for $14,000 and $30,000, respectively. Christian Affidavit, Ex. C; CR 128-132. Finally, checks for the disputed transfers (and other transfers from McClung which Mason asserted were "withdrawals" made by his father) were made payable to David Mason, not to his father. CR 105-111. In its Opinion, Decision and Order dismissing the Christians' claim, the district court found that "Mason gave McClung $166,042.06 and received $198,915.08, a net gain of $32,873.12." CR 146. David Mason was the transferee of the excess payments.

Mason also asserted without substantiation that the last payments McClung made to him were "returns of principal," and that earlier payments to him were "earnings" on his "investment." Mason Affidavit, ¶ 7; CR 66. As further discussed below, in a Ponzi scheme, there are no "earnings" -- the scheme is based on a fraudulent report of "earnings" to induce victims to provide more money. McClung's guilty plea established this fact, as did Mason's admissions in response to the key allegations of the Christians' Complaint. CR 15, 22. They and the judgment of the bankruptcy court established that any payments to Mason were not "earnings" but were, to the extent in excess of money provided by Mason to McClung, fraudulent transfers of money owed to others, including the Christians.

Following the hearing on the parties' motions, the district court ruled, essentially *sua sponte*, that Christians lacked standing to pursue their fraudulent transfer claim against Mason. The Court concluded that the claim belonged exclusively to the bankruptcy estate, and that the state law fraudulent transfer claim was therefore preempted by federal law. CR 146-151.

In part, the district court ruled that because the bankruptcy trustee had not pursued a fraudulent transfer claim against Mason within two years pursuant to 11 U.S.C. § 548, "[a]llowing Plaintiffs an alternate route around the limitations found in the bankruptcy code would only serve to circumvent the process and frustrate the orderly administration of the bankruptcy estate." CR 150.

McClung's Chapter 11 bankruptcy case, District of Idaho Bankruptcy Court, Case No. 03-40682, was filed on April 16, 2003. The trustee was appointed in the Chapter 11 case on April 17, 2003, and again on October 17, 2003 after the case was converted to a Chapter 7 proceeding.[3] As noted, the Christians received their judgment against McClung from the bankruptcy court on October 14, 2004. The bankruptcy trustee apparently took essentially no action to pursue recovery of McClung's excess payment to Mason.

II. ISSUES PRESENTED ON APPEAL

1. Do Christians have standing to pursue their fraudulent transfer claim against Mason, where the trustee in the fraudulent transferor's bankruptcy failed to timely pursue the claim and the bankruptcy is closed?

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[3] McClung's bankruptcy case records are publicly available via the ECF and PACER systems for accessing the files of the United States Bankruptcy Court for the District of Idaho, in case number 03-40682. The court may take judicial notice of a fact when the fact is capable of accurate determination by resort to sources whose accuracy cannot reasonably be questioned. I.R.E. 201(b). Judicial notice may be taken at any stage of a proceeding. I.R.E. 201(f); Trautman v. Hill, 116 Idaho 337, 340 (Ct. App. 1989). Given its reliance upon the existence of McClung's bankruptcy case, the district court could and should have taken judicial notice of its records. This Court also should take judicial notice of those records.

2. Should the district court have granted summary judgment to the Christians on their fraudulent transfer claim, since Mason admitted the essential elements of the claim and no genuine issue of material fact remained?

III. ARGUMENT

A. Standard of review.

This court reviews the district court's rulings on issues of law *de novo*. Basic American, Inc. v. Shatila, 133 Idaho 726, 734 (1999). A ruling on a motion for motion for summary judgment is an issue of law reviewed *de novo*. Cascade Auto Glass, Inc. v. Idaho Farm Bureau Ins. Co., 141 Idaho 660, 662 (2005).

B. The district court erred by ruling that the fraudulent transfer claim against Mason was the property of McClung's bankruptcy estate and could not be pursued by McClung's creditors.

A trustee in bankruptcy may avoid fraudulent transfers made by the debtor. 11 U.S.C. §548. The pre-BAPCPA version of 11 U.S.C. § 546(a) in effect at the time of McClung's bankruptcy limited the time for the trustee to pursue a fraudulent transfer claim against Mason to:

> the earlier of—
> (1) the later of --
> (A) 2 years after the entry of the order for relief; or
> (B) 1 year after the appointment or election of the first trustee under section 702, 1104, 1163, 1202, or 1302 of this title [11 USCS § 702, 1104, 1163, 1202, or 1302] if such appointment or such election occurs before the expiration of the period specified in subparagraph (A); or
> (2) the time the case is closed or dismissed.

The "order for relief" is the petition for bankruptcy in a voluntary bankruptcy case. 11 U.S.C. § 301; In re Smith, 235 F.3d 472, 475 (9th Cir. 2000).

As noted, McClung's bankruptcy petition was filed on April 16, 2003. A trustee was appointed on April 17, 2003, and again on October 17, 2003 following conversion of the case from a Chapter 11 proceeding to a Chapter 7 liquidation. Thus, even giving 11 U.S.C. § 546(a)(1) a liberal interpretation, the trustee's ability to pursue recovery of the excess transfer to Mason expired no later than one year after the appointment of the trustee following conversion of the case, or October 17, 2004.

Contrary to the district court's conclusion, the trustee's abandonment of the claim did not extinguish or preempt individual creditors' claims to avoid the same fraudulent transfer. Nothing in either the Bankruptcy Code or the Uniform Fraudulent Transfer Act provides for this result. To the contrary, numerous courts have recognized that once the trustee fails to timely pursue a fraudulent transfer claim, creditors of the bankruptcy debtor are free to pursue their own claims against the excess transferee, exactly as the Christians did.

For example, in Klingman v. Levinson, 158 B.R. 109 (N.D. Ill. 1993), Levinson, an attorney, embezzled money from his clients. Klingman sued to have Levinson's assignment of an interest in a trust to his wife set aside as a fraudulent transfer. Levinson filed for bankruptcy, and Levinson's debt to Klingman for the embezzlement was held to be nondischargeable.[4] Klingman's action was removed to the federal court, and then removed to

[4] The same is true of McClung's debt to the Christians; its nondischargeability is expressly stated in the Christians' judgment against McClung.

the bankruptcy court following Levinson's bankruptcy filing. Levinson and his wife them moved for summary judgment, making exactly the same argument as relied upon by the Court in this case, contending that Klingman "lack[ed] standing to pursue [the] fraudulent conveyance action because once Melvin filed his bankruptcy petition, the allegedly fraudulently conveyed property became part of the debtor's estate, and only the trustee has standing to assert this cause of action." 158 B.R. at 112. The district court rejected the argument. While noting that the bankruptcy trustee initially has the exclusive right to pursue fraudulently conveyed assets of the debtor, the court stated:

> However, the trustee does not retain this exclusive right in perpetuity. The trustee's exclusive right to maintain a fraudulent conveyance action expires and creditors may step in (or resume actions) when the trustee no longer has a viable cause of action. Kathy B. Enterprises, Inc. v. United States, 779 F.2d 1413, 1415 (9th Cir. 1986) (IRS entitled to pursue collection action after bankruptcy closed); Federal Deposit Insurance Corp., 733 F.2d 1083, 1085 (4th Cir. 1984) ("once a bankruptcy case has been closed, creditors having unavoided liens on fraudulently conveyed property can pursue their state law remedies independently of the trustee in bankruptcy"); Dixon v. Bennett, 72 Md. App. 620, 531 A.2d 1318, 1323-25 (1987) ("once a trustee's statutory time period has expired, an unsecured creditor can bring an action against a fraudulent transferee under state law provided the state statute of limitations has not yet expired"), cert denied, 311 Md. 557, 536 A.2d 664 (1988).
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> Here, there is no dispute that the trustee never sought to recover the conveyance challenged by Klingman and the United States.[5] The statute of limitations has long since run on the trustee's right to bring that action. The court finds that Klingman and the United States have standing to pursue their claims in this action.

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[5] The United States had intervened in Klingman's action to satisfy a tax debt of Levinson.

158 B.R. at 113.

See also Barber v. Westbay, 313 B.R. 419, 427 (C.D. Ill. 2004) ("The landscape changes, however, once it is determined that the trustee's claim is no longer viable. A creditor regains standing to pursue a state fraudulent conveyance action, in its own name and for its own benefit, once the statute of limitations expires on the bankruptcy trustee's right to bring the claim."); Casey Nat'l Bank v. Roan, 668 N.E.2d 608, 612-13 (Ill. App. 1996) ("While the trustee has the exclusive right to pursue fraudulently conveyed assets pursuant to section 546(a) of the Code once bankruptcy has been initiated (11 U.S.C. § 546(a) (1988)), the trustee loses that right and creditors may step in once the trustee longer has a viable cause of action (in this case because the statute of limitations for initiating a cause for fraudulent conveyance had expired as to the trustee").

Other courts have reached the same conclusion by rejecting similar arguments, among them that a creditor is barred by *res judicata* from pursuing a state law fraudulent transfer claim following a debtor's discharge in bankruptcy.

In Roberson v. Johnson, 950 So.2d 317 (Ala. App. 2006), Roberson loaned Johnsons $60,000. Johnsons transferred $10,000 to Fred, and shortly thereafter filed for bankruptcy. Johnsons listed the debt owed to Roberson in their schedule of debts. Johnson's debt to Roberson was eventually discharged. Roberson then sued Fred in state court to avoid the $10,000 transfer from Johnson to Fred as a fraudulent transfer. Fred moved for summary judgment, asserting that the bankruptcy court had exclusive jurisdiction over the matter and had discharged Johnson's debt to Roberson, fully disposing of the matter. The trial court granted

Fred's motion, but the appellate court reversed. In doing so, the court reasoned that the discharge provision of the Code, 11 U.S.C. § 524(e) "had no effect on Roberson's rights with regard to the alleged fraudulent transfer to Fred. 950 So.2d 321 (citing National Union Fire Ins. Co. v. Grusky, 763 So.2d 1206, 1208-9 (Fla. App. 2000) (holding similarly). Roberson was allowed to continue pursuing his fraudulent transfer claim against Fred.

In Grusky, Elliot defaulted on a loan from Lawrence, and was indebted to National Union. By the time he defaulted on Lawrence's loan, National Union was already a judgment creditor of Elliot. Elliot transferred stock to Lawrence, then filed for Chapter 7 bankruptcy. National Union urged the trustee to avoid the transfer to Lawrence, but the trustee chose not to. National Union then filed suit against Lawrence in state court to avoid the transfer. The trial court granted summary judgment to Lawrence, ruling in part that National Union was barred by res judicata because of the bankruptcy court proceedings, and had no standing because it was no longer a creditor, Elliot's debt to it having been discharged in bankruptcy. The appellate court reversed, reasoning: (a) that National Union was not barred by res judicata, since the fraudulent transfer action was never litigated in the bankruptcy court; and (b) National Union had standing because discharge granted to the debtor under § 524(e) of the Bankruptcy Code expressly "does not affect the liability of any other entity on, or the property of any other entity for, such debt." 763 So.2d at 1208. The court stated that § 524(e) "reveals a congressional intent to broaden the rights of creditors, by preserving their actions against third parties and their property, and to restrict the effect of a discharge solely to a release of the personal property of the debtor." Id. At 1209. The court also emphasized that "the present action is brought against

Lawrence and not against Elliot, the debtor in the bankruptcy proceeding," and since National Union constituted a "creditor" under the UFTA, "[e]ven though National Union's claim against Elliot was discharged in bankruptcy, the claim against Lawrence, a third party, was still viable." Id.

See also Kathy B. Enterprises, Inc. v. United States, 779 F.2d 1413, 1414 (9th Cir. 1986) (holding that the debtor's discharge did not affect a fraudulent transferee's liability for the same debt, and stating: "We see no reason to infer an exception to clear statutory language for the benefit of recipients of fraudulent conveyances. . . . The bankruptcy proceedings are over. Even if the government's actions did violate the stay, it will be permitted to pursue collection actions now."); Dwyer v. Meramec Venture Assoc., 75 S.W.3d 291, 294 (Mo. App. 2002) ("[A] debtor's discharge in bankruptcy does not protect fraudulent transferees from collection efforts by a judgment creditor. To permit a bankrupt debtor to shield his assets by engaging in a fraudulent transfer would result in a windfall to the fraudulent transferees at the expense of the unprotected creditor. We cannot permit the debtor to do indirectly what the law forbids him to do directly.").

In Clark v. Bank of Bentonville, 824 S.W.2d 358, 361 (Ark. 1992), the Arkansas Supreme Court ruled that a bank could pursue a fraudulent transfer claim after the trustee in the transferor debtor's bankruptcy failed to do so. The Court stated in pertinent part:

> Appellants further argue that *res judicata* should bar the bank's fraudulent conveyance action because the claim was not pursued in the bankruptcy proceeding. However, the bankruptcy code does not give a creditor the power to pursue a cause of action to set aside a fraudulent conveyance. [Citation omitted]. In fact, 11

> U.S.C. § 362(a) imposes an automatic stay that prohibits creditors form acting against a debtor's property during the pendency of the bankruptcy proceeding. [Citation omitted]. While a trustee may elect to pursue a creditor's unsecured state law claim under 11 U.S.C. § 544(b) . . . such an action is an exercise of the avoidance power for the benefit of all creditors. Since the bank did not have standing as a single creditor to pursue the fraudulent conveyance action during the bankruptcy proceeding, *Id.*, *res judicata* did not prohibit the bank's subsequent state court action.

824 S.W.2d at 361 (emphasis added).

The Christians were entitled to pursue their fraudulent transfer claim against Mason once the trustee in McClung's bankruptcy lost the right to do so, and the trustee's abandonment of his claim had no effect on the continued viability of the Christians' separate state law claim against Mason. The district court erred in dismissing the Christians' claim on this basis.

C. No genuine issue of material fact remained regarding the existence of a fraudulent transfer, and the district court should have granted summary judgment to the Christians.

Because the essential facts were not in dispute, and no genuine issue of material fact remained, the district court should have denied Mason's motion for summary judgment, and instead granted the Christians summary judgment.

1. Summary judgment standards.

Summary judgment may be granted when "the pleadings, depositions, admissions on file, together with the affidavits, if any, show that there is no genuine issue of material fact and that the moving party is entitled to a judgment as a matter of law." I.R.C.P. 56(c); see also

Reis v. Cox, 104 Idaho 434, 438, 660 P.2d 46 (1982); Collard v. Cooley, 92 Idaho 789, 791, 451 P.2d 535 (1969). The purpose of summary judgment proceedings is to eliminate the necessity of trial of a claim or defense where existent and undisputed facts lead to a conclusion of law which is certain. Berg v. Fairman, 107 Idaho 441, 444, 690 P.2d 896 (1984). Summary judgment is an appropriate tool to eliminate groundless defenses in cases which would end in directed verdicts or other rulings of law. Lipe v. Javelin Tire Co., Inc., 97 Idaho 805, 806, 554 P.2d 1302 (1976). If uncontroverted facts exist which lead to definite disposition as a matter of law, summary judgment may be granted. G&M Farms v. Funk Irrigation Co., 119 Idaho 514, 524, 808 P.2d 851 (1991).

A mere scintilla of evidence or only slight doubt as to the facts is not sufficient to prevent summary judgment. Stafford v. Weaver, 136 Idaho 223, 225 (2001). The non-moving party must respond to a summary judgment motion with "specific facts showing that there is a genuine issue for trial." Id.

Under Rule 56(e), conclusory assertions, made without substantiation by underlying facts in the record, do not create a genuine issue of material fact.

> Where an affidavit merely states conclusions and does not set out facts, such supporting affidavit is inadmissible to show the absence of a genuine issue of material fact. *Matthews v. New York Life Insurance Co.*, 92 Idaho 372, 443 P.2d 456 (1968). *Accord, Openshaw v. Allstate Insurance Co.*, 94 Idaho 192, 484 P.2d 1032 (1971).
>
> A supporting affidavit is inadmissible to show the presence of a genuine issue of material fact if it merely states conclusions and does not set out the underlying facts. *See also Corbridge v. Clark Equip. Co.*, 112 Idaho 85, 87, 730 P.2d 1005, 1007 (1986)

> (affidavit not establishing specific facts "is precisely the type of flawed affidavit contemplated by I.R.C.P. 56(e)"); Wright, Miller & Kane, Federal Practice & Procedure: Civil (Second) § 2738 (1983) (ultimate or conclusory facts cannot be utilized on a summary judgment motion).

Casey v. Highlands Ins. Co., 100 Idaho 505, 508, 600 P.2d 1387, 1390 (1979); See also Jerome Thriftway Drug v. Winslow, 110 Idaho 615, 618 (1986) ("Unsupported general or conclusory allegations are not sufficient in the face of a motion for summary judgment[.]"); Hecla Mining Co. v. Star-Morning Mining Co., 122 Idaho 778, 786 (affidavits which are "conclusory" and not supported by "specific facts" do not satisfy the requirements of competency and admissibility under Rule 56(e) and cannot prevent summary judgment); State v. Shama Resources L.P., 127 Idaho 267, 271 (1995) ("The requirements of Rule 56(e) are not satisfied by an affidavit that is conclusory, based on hearsay, and not supported by personal knowledge.").

Similarly, internally inconsistent testimony or affidavit testimony which contradicts a prior admission cannot create a genuine issue of material fact. See, e.g., U.S. v. 1980 Red Ferrari, 827 F.2d 477, 480 n. 3 (9th Cir. 1987) (self-contradictory deposition testimony could not raise genuine issue of material fact to prevent summary judgment); Buie v. Quad/Graphics, Inc., 366 F.3d 496, 506 (7th Cir. 2004 (stating that, on motion for summary judgment, "internally contradictory affidavits are generally disfavored.").

2. The excess payments by McClung to Mason were fraudulent transfers.

Idaho's version of the Uniform Fraudulent Transfer Act provides in pertinent part: "Every transfer of property . . . with intent to delay or defraud *any* creditor or other person of

his demands, is void against *all* creditors of the debtor and their successors in interest[.]" I.C. § 55-906 (emphasis added). A transfer[6] is fraudulent, whether the creditor's claim arose before or after the transfer was made, if:

> (a) With actual intent to hinder, delay, or defraud any creditor[7] of the debtor; or
> (b) Without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor:
> 1. was engaged or about to engage in a business or transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or
> 2. intended to incur, or believed or reasonably should have believed that he or she would incur, debts beyond his or her ability to pay as they became due.

I.C. § 55-913(1)(a), (b).

Additionally, a transfer is fraudulent as to a creditor whose claim arose before the transfer was made if the debtor made the transfer without receiving a "reasonably equivalent value" in exchange for the transfer and the debtor was insolvent at that time or the debtor became insolvent as a result of the transfer or obligation. § 55-914(1).

Once found to exist, a fraudulent transfer may be avoided. I.C. § 55-916(1)(a). Judgment may be awarded against the transferee in favor of the creditor seeking avoidance of the transfer, in the amount of the transfer. I.C. § 55-917(2)(a).

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[6] A "transfer" includes the payment of money. I.C. § 55-910(12).

[7] A "creditor" is a person who has a "claim." I.C. § 55-910(4). A "claim" is a right to payment, whether or not reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured or unsecured. I.C. § 55-910(3). As noted, Christians are judgment creditors of McClung, but under the definitions of the Act, had a "claim" and were "creditors" of McClung once they had provided money to him as a result of his fraud.

Several courts have held that actual intent to defraud may be inferred by the "mere existence of a Ponzi scheme," such that excess payments to victims of a Ponzi scheme constitute fraudulent transfers by the perpetrator of the scheme. In re Agricultural Research And Technology Group, Inc., 916 F.2d 528, 535 (9th Cir. 1990). There is a general rule -- known as the "Ponzi scheme presumption" -- that such a scheme demonstrates "actual intent" as matter of law because "transfers made in the course of a Ponzi scheme could have been made for no purpose other than to hinder, delay or defraud creditors." In re Manhattan Fund Ltd., 359 B.R. at 517-18; see also Drenis v. Haligiannis, 452 F. Supp. 2d 418, 429 (S.D.N.Y. 2006); In re Old Naples Securities, Inc., 343 B.R. 310, 320 (M.D. Fla. 2006) (collecting other decisions); Warfield v. Carnie, 2007 U.S. Dist. LEXIS 27610, *28 (N.D. Tex., April 13, 2007) ("Under the UFTA, a debtor's actual intent to hinder, delay, or defraud is conclusively established by proving that the debtor operated as a Ponzi scheme."). This is obvious from the character of a Ponzi scheme: each payment to a victim of fictitious "earnings" is actually a transfer of some other victim's money, and is necessarily done to "hinder, delay, or defraud" all other victims to the extent of the payment. McClung's guilty plea to a charge of mail fraud is direct evidence of his actual intent to defraud. See Schreiber Distrib. Co. v. Serv-Well Furniture Co., 806 F.2d 1393, 1399-1400 (9th Cir. 1986) (noting that the elements of mail fraud include the specific intent to deceive or defraud).

Similarly, courts have held that a Ponzi scheme victim receiving an excess payment received *no* value, let alone "reasonably equivalent value," for excess payments from the perpetrator of the scheme. See, e.g., United States v. Frykholm, 362 F.3d 413, 417 (7th Cir.

2004); In re United Energy Corp., 944 F.2d 589, 595 n. 6 (9th Cir. 1991) (where an "investor" receives more than his total "investment" from the debtor, "[s]uch excess amounts would be avoidable because the debtor would not have received reasonably equivalent value for them.").

Finally, by running a Ponzi scheme and promising "investor" victims high rates of "return," the perpetrator of the scheme obviously knows or should know that he is incurring debts far greater than his ability to pay. Indeed, courts have uniformly held that a Ponzi scheme *is insolvent from its inception.* E.g., Warfield v. Byron, 436 F.3d 551, 558 (5th Cir. 2006) (Ponzi scheme "is, as a matter of law, insolvent from its inception."); Quilling v. 3D Mktg., LLC, 2007 U.S. Dist. LEXIS 24914, *6 (N.D. Tex., Feb. 8, 2007) (same); Terry v. June, 432 F. Supp. 2d 635, 640 (W.D. Va. 2006) (same). This fact established the insolvency element of the Christians' claims under I.C. §§ 55-913(1)(b) and 55-914(1). It did not affect Christians' claim under I.C. § 55-913(1)(a), which requires only a transfer with the actual intend to hinder, delay or defraud any creditor.

The material facts are undisputed, largely as a result of Mason's admissions in response to the Christians' Complaint, and satisfy the required elements under I.C. 55-913(1) and 55-914(1). As a result, the district court should have ruled as a matter of law that the excess transfers to Mason were fraudulent transfers, that the transfers could be avoided, and that judgment in the amount of the excess be entered against Mason:

1. Mason admitted that McClung operated and pleaded guilty to operating an illegal Ponzi scheme, of which he and the Christians were victims.

2. The existence of the scheme conclusively established McClung's actual intent to defraud his creditors, and his insolvency at the time the excess transfers were made.

3. Mason admitted that Christians were creditors of McClung.

4. Mason admitted that monies were provided to McClung in his name.

5. Mason admitted, through his own accounting and the "account statements" attached to his affidavit, that McClung paid back $32,873.12 more than was provided to him.

6. Because the excess payments were beyond the amounts Mason provided to McClung, McClung received no value for them, let alone "reasonably equivalent" value.

While Mason asserted (without substantiation) that the transfers in question involved money belonging to his father, these conclusory assertions did not satisfy Rule 56(e). Mason's own documents established that the fraudulent transfers were made to him, not to his father.

While it is relevant only to a claim under I.C. §55-914(1), the fact of McClung's insolvency and the fraudulent nature of his Ponzi scheme means that the Christians have been "creditors" of McClung with a "claim" against him since their first investment with him. See I.C. § 55-910(3), (4). It is undisputed that their payments to McClung were complete before McClung made the excess transfers to Mason. The timing of their creditor status is irrelevant to their claims under I.C. § 55-913(1)(a) and §55-913(1)(b).

3. Mason could not avail himself of the good faith defense under I.C. § 55-917, because the defense: (1) does not apply to voiding of a transfer under I.C. § 55-913(1)(b); (2) does not apply to voiding of a transfer under I.C. § 55-914(1); and (3) does not apply to the voiding of a transfer under I.C. §55-913(1)(b) where the transferee did not also give reasonably equivalent value.

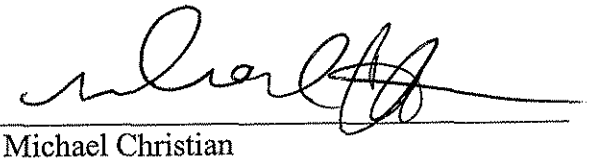
Mason argued below that good faith is a defense under I.C. § 55-917 to a claim for fraudulent transfer under I.C. §55-913(1)(a). This is true, however, only if the transferee *also* gave "reasonably equivalent value." I.C. § 55-917(1) provides in pertinent part that a "transfer or obligation is not voidable under section 55-913(1)(a), Idaho Code, against a person who took in good faith *and for a reasonably equivalent value*[.]" Because as a matter of law Mason did not give reasonably equivalent value for the excess transfers, his good faith is irrelevant. The defense does not apply to claims under I.C. § 55-913(1)(b) or §55-914(1).

IV. CONCLUSION

The district court erred in ruling that the Christians lacked standing to pursue their fraudulent transfer claim against Mason. Mason admitted all of the facts essential to the Christians' claim, and no genuine issue of material fact remained. The district court should have granted summary judgment in favor of the Christians. Its ruling should be reversed and judgment should be entered in favor of the Christians in the amount of the excess transfers to Mason, $32,873.12.

Dated this 21st day of August, 2008.

MARCUS, CHRISTIAN & HARDEE, LLC

By 

Michael Christian
Attorneys for Plaintiff/Respondent

CERTIFICATE OF SERVICE

I hereby certify that on this 21st day of August, 2008, I caused to be served a true and correct copy of the foregoing **BRIEF OF APPELLANTS** in the above-referenced matter by the method indicated below, and addressed to the following:

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