

IN THE UNITED STATES COURT OF APPEALS  
FOR THE TENTH CIRCUIT

In Re:	)	
	)	
ROBERT WILLIAM MATHEWS,	)	
	)	Case No.: 10-6057
Debtor,	)	
	)	APPEAL FROM UNITED STATES
	)	DISTRICT COURT FOR THE
	)	WESTERN DISTRICT OF
	)	OKLAHOMA;
	)	CASE NO.: CIV-09-185D
	)	HONORABLE TIMOTHY DeGIUSTI
OKLAHOMA DEPARTMENT OF	)	
SECURITIES <i>ex rel.</i> IRVING L.	)	BANKRUPTCY CASE NO.
FAUGHT, Administrator, et al.,	)	BK-07-10108-BH
	)	ADVERSARY NO. 07-1140-BH
Plaintiff/Appellee,	)	
	)	
v.	)	
	)	
ROBERT WILLIAM MATHEWS,	)	
	)	
Defendant/Appellant.	)	

**BRIEF IN CHIEF OF THE APPELLANT ROBERT WILLIAM MATHEWS**

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE  
WESTERN DISTRICT OF OKLAHOMA CASE NO.: CIV-09-185D;  
THE HONORABLE TIMOTHY DeGIUSTI

ORAL ARGUMENTS REQUESTED

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**CORPORATE DISCLOSURE STATEMENT**

The Appellant is not required by Federal Rules of Appellate Procedure 26.1 to file a disclosure.

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**I. STATEMENT OF RELATED CASES**

There is a related case involving the same issues before this court styled In Re: Marvin Lee Wilcox, Pamela Jean Wilcox, debtors, Oklahoma Department of Securities vs. Marvin Lee Wilcox, Case No. 10-6056.

**II. JURISDICTIONAL STATEMENT**

This is an appeal from a final judgment of the United States District Court for the Western District of Oklahoma and is taken pursuant to Rules 3 and 4 of the Rules of Appellate Procedure and 28 U.S.C. § 158(d). The final judgment was entered on February 10, 2010 and the Notice of Appeal was filed on March 5, 2010. The Appeal to the United States District Court was taken from a final judgment of the Bankruptcy Court pursuant to 28 U.S.C. § 158(a)(1) and Bankruptcy Rule 8001. The final judgment of the Bankruptcy Court was filed on December 12, 2008 and the Notice of Appeal by Robert William Mathews ("Mathews") was filed on December 22, 2008 pursuant to Bankruptcy Rules 8001 and 8002. Mathews elected to appeal to the United States District Court for the Western District of Oklahoma by filing the Notice of Appeal to the District Court on December 22, 2008 pursuant to 28 U.S.C. § 158(c)(1)(A).

**III. STATEMENT OF ISSUES PRESENTED FOR REVIEW**

1. The District Court erred in affirming the Bankruptcy Court's findings that there were sufficient undisputed facts to entitle the

Oklahoma Department of Securities to summary judgment and finding that the Plaintiff had met its burden of proof under 11 U.S.C. § 523 (a)(19), as there were numerous disputed facts, which precluded summary judgment in the bankruptcy case. (*See* Appendix pages 15 and 27 – 28).

2. The District Court erred in affirming the Bankruptcy Court's decision that the Oklahoma Department of Securities had met its burden of proof that the discharge should be denied the Appellant, Robert William Mathews based on 11 U.S.C. § 523(a)(19). (*See* Appendix pages 15 and 16 – 25).

3. The District Court erred in affirming the Bankruptcy Court's opinion finding that the decision of the District Court of Oklahoma County found that the Appellant, Robert William Mathews had violated federal securities laws, which is an essential requirement for a denial of discharge under 11 U.S.C. § 523 (a)(19). (*See* Appendix pages 15 and 16 – 25 and 25 – 27).

4. The District Court erred in affirming the Bankruptcy Court's decision finding that Oklahoma law does not require wrongful intent in order to prove a violation of Oklahoma securities laws. (*See* Appendix pages 15 and 16 – 25 and 25 – 27).

5. The District Court erred in affirming the Bankruptcy Court's findings that the Appellant, Robert William Mathews under the undisputed facts presented should have been denied a discharge under 11 U.S.C. § 523(a)(19). (*See* Appendix pages 15 and 16 – 25).

6. The District Court erred in affirming the Bankruptcy Court's findings that were based on an Oklahoma Court of Civil Appeals decision, which has been subsequently vacated and the case reversed and remanded for further proceedings. (*See* Appendix pages 15 and 28).

7. The District Court erred in affirming the Bankruptcy Court's decision in finding that Robert William Mathews had met the requirements under 11 U.S.C. § 523(a)(19) for denial of his discharge. (*See* Appendix pages 15 and 16 – 25 and 25 – 27).

8. The District Court erred, in that its decision is based in part on the affirmance of the Oklahoma County District Court decision by the Oklahoma Court of Civil Appeals, which required disgorgement of the profits received by Appellant Mathews, which the Court of Civil Appeals decision had subsequently been vacated and the case reversed and remanded for further proceedings in the District Court of Oklahoma County. (*See* Appendix pages 15 and 28).

9. The District Court erred as part of its decision was based upon the Oklahoma Court of Appeals decision holding that "the defense of being innocent victims" has no merit under the facts of this case. That Court of Civil Appeals decision was vacated and the case reversed and remanded for further proceedings. (See Appendix pages 15 and 28).

#### **IV. STATEMENT OF THE CASE**

Mathews was one of the numerous victims of a Ponzi scheme run by Marsha Schubert d/b/a Schubert and Associates ("Schubert"). Beginning on or about 2001, Schubert, an individual residing in Oklahoma engaged in the issuance, offer, and sales securities to "Investors." Schubert represented that the Investors would pool their funds and would gain large profits from the investment through Schubert's day trading. Schubert stated that the Investors' money would be used to make trades on option contracts and promised that the investment program was full proof and would bring profits of 30% annually. Mathews, like other investors, placed his trust and confidence in Schubert to act for his benefit in this investment program.

It was subsequently discovered that Schubert was in fact running a Ponzi scheme and Mathews was an investor/victim, just like all of the other numerous investors caught up in Schubert's Ponzi scheme. The Appellee, Oklahoma Department of Securities ("Department of Securities") sued Mathews, and 158

other Investors of Schubert in Oklahoma County District Court, alleging these investors had received more funds than they had invested with Schubert and sought to have those funds disgorged to a Trustee appointed by The District Court of Logan County to gather funds in order to repay investors.

In The District Court of Oklahoma County, in a case styled *Oklahoma Department of Securities, Ex Rel, Irving L. Faught, Plaintiff v. Marvin Lee Wilcox and Pamela Jean Wilcox, et al.*, Case No. CJ-2005-3796, the Court found that Mathews in this case, had been *unjustly enriched* and ordered Mathews, along with 158 other investors of Schubert, in this case to disgorge the funds the investors received from Schubert. That case has subsequently been reversed by the Oklahoma Supreme Court and remanded for future proceedings.<sup>1</sup>

Subsequently, Mathews sought bankruptcy protection in The United States Bankruptcy Court for the Western District of Oklahoma, Case No. BK 07-10108 BH. The Department of Securities, sought to have Mathew's discharge denied in an adversary proceeding in the bankruptcy court alleging that 11 U.S.C. § 523(a)(19) disallowed discharge of the state court judgment to Mathews. The bankruptcy court in its order, found in favor the Department of Securities and against Mathews, and from that order, Mathews appealed to the U. S. District

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<sup>1</sup>The Judgment was reversed; however, the case has been remanded for further proceedings, Mathews was not a party to the appeal in the Oklahoma Supreme Court.

Court, which affirmed the bankruptcy court, which necessitated this appeal, to the Tenth Circuit.

#### **V. RELEVANT FACTS**

1. On October 14, 2004, the Department of Securities sought an application for temporary restraining order and freezing assets of Schubert, with respect to the Ponzi scheme that she was operating. (*See* Appendix pages 225 - 240)

2. On November 15, 2004, an Order for permanent injunction was entered enjoining Schubert from offering or selling any securities, transacting business as a broker/dealer, and ordered that Schubert should pay restitution to investors in a sum to be determined by the Court. (*See* Appendix pages 241 - 256)

3. On April 13, 2005, in Case No. CR-05-078-HE, Schubert petitioned the United States District Court to enter a plea of guilty in her criminal case. (*See* Appendix pages 257 - 267)

4. On September 7, 2005, a judgment in said criminal case was entered on a plea of guilty to one (1) count of money laundering against Schubert, and she was ordered imprisoned for 120 months and ordered to pay restitution in an amount and in excess of \$9,000,000.00. (*See* Appendix pages 268 - 278)

5. On May 11, 2005, the Department of Securities filed in the District Court of Oklahoma County, Case No. CJ-2005-3796, a suit against numerous

former investors of Schubert, which included Mathews. In that petition, it was alleged, that the defendants, including Mathews, had received money from Schubert and that he had been unjustly enriched to the detriment of other investors. (See Appendix pages 294 - 306)

6. On October 24, 2006, the Department of Securities in Case No. CJ-2005-3796, filed a motion for summary judgment against Mathews, alleging only that he had been unjustly enriched as an investor with Schubert. In the motion for summary judgment, The Department of Securities argued that they were entitled to summary judgment because Mathews was unjustly enriched by payments he received from Schubert and alleged that he had received fictitious profits in the amount of \$524,826.19 from Schubert. In the motion for summary judgment filed by the Department of Securities, they did not make any allegations of any wrongdoing or securities violations on the part of Mathews. (See Appendix pages 391 - 448)

7. On February 5, 2007, the District Court of Oklahoma County, entered summary judgment against Mathews in The Oklahoma District Court case and found that Mathews had been unjustly enriched in the amount requested by the Department of Securities. The Court made no findings of any wrongdoing on the part of Mathews. (See Appendix pages 453 - 456)

8. As a result of a state court judgment against Mathews, he filed for bankruptcy protection in The United States Bankruptcy Court for the Western District of Oklahoma in a Chapter 7 case, Case No. BK 07-10610 BH.

9. On October 25, 2007, the Department of Securities filed an adversary proceeding, Case No. 07-1226 BH, seeking to deny Mathews' discharge of the state district court judgment on the basis of 11 U.S.C. § 523(a)(2) and (a)(19). (*See Appendix pages 69 - 81*)

10. On May 30, 2008, the Department of Securities filed its motion for summary judgment in the adversary proceeding, seeking to deny discharge to Mathews for the state court judgment. In its motion for summary judgment, the Department of Securities alleged that the state court judgment should be nondischargeable under 11 U.S.C. § 523(a)(19) as it was related to a securities violation and there was an order of disgorgement. Mathews filed a response on June 25, 2008, alleging that he was not a participant in the scheme of Schubert and that Schubert had committed all of the wrongful acts and the securities violations. Mathews argued he was merely an investor with Schubert, just like all the other investors who were victims of Schubert's scheme. The lack of involvement in Schubert's scheme by Mathews is uncontroverted. (*See Appendix pages 93 – 133 and 134 - 177*)

11. On December 12, 2008, the Bankruptcy Court entered judgment in favor of the Department of Securities and against Mathews, finding that under 11 U.S.C. § 523(a)(19) of the Bankruptcy Code that the debt of the state court judgment ordering disgorgement for unjust enrichment was non-dischargeable in bankruptcy. (See Appendix 560 – 566 and 567 - 568)

12. The state court judgment was appealed by some of the defendants and the judgment was affirmed by the Oklahoma court of civil appeals in Case No. 104,262 on April 13, 2007. The Oklahoma Supreme Court reversed the court of civil appeals and remanded the case for further proceedings. Mathews was not a party to that appeal. (See Appendix 457 – 480 *Oklahoma Department of Securities v. Blair*, 2010 OK 16, – P. 3<sup>rd</sup> –.

It is from the decision of the Bankruptcy Court affirmed by the U. S. District Court denying Mathews discharge that Mathews takes this Appeal.

## **VI. SUMMARY OF ARGUMENT**

Mathews was a target of Schubert's Ponzi scheme. The facts are uncontroverted that Schubert was the wrongdoer. Schubert was the person who violated the securities laws. Mathews merely invested his money with Schubert, who Mathews believed was a legitimate day trader. There were no allegations that Mathews was a wrongdoer and the order from the district court of Oklahoma county found that Mathews, along with other investors with Schubert, were

unjustly enriched. The Oklahoma county district court did *not* find that Mathews or the other investors were wrongdoers.

Title 11 U.S.C. § 523(a)(19) is targeted to deny discharge in bankruptcy based on the debtor's violation of securities laws. It was intended to prevent wrongdoers from using the bankruptcy laws to receiving a discharge. In this case the wrongdoer (Schubert) is not the debtor. The person who violated the securities laws was Schubert and not Mathews (who is the debtor). Since Mathews was not a wrongdoer 11 U.S.C. § 523(a)(19) cannot be used to deny Mathews of a discharge. For this reason the Bankruptcy Court and U. S. District Court have improperly applied § 523(a)(19) to Mathews and those decisions should be reversed.

## **VII. ARGUMENTS AND AUTHORITIES**

### **PROPOSITION I**

**THE U. S. DISTRICT COURT ERRED IN AFFIRMING THE BANKRUPTCY COURT'S FINDING THAT THE DEPARTMENT OF SECURITIES HAD MET ITS BURDEN IN PROVING THAT THE DISCHARGE OF THE STATE COURT JUDGMENT SHOULD HAVE BEEN DENIED MATHEWS BASED ON 11 U.S.C. § 523(A)(19).**

#### **A. STANDARD OF REVIEW**

This is an Appeal from Final Order of the U. S. District Court affirming the granting of summary judgment by the bankruptcy court.

The bankruptcy court made a legal conclusion that Mathews' discharge should be denied as to the state court judgment pursuant to 11 U.S.C. § 523(a)(19) of the Bankruptcy Code. Those findings were affirmed by the U. S. District Court. Legal conclusions or determination of a bankruptcy court are subject to a *de novo* review on appeal to the United States District Court. *In re Herd*, 840 F.2d 757 (10<sup>th</sup> Cir. 1988). *See also, In re Hollytex Carpet Mills, Inc.*, 73 F.3d 1516 (10th Cir. 1996). Additionally, issues of whether debts are dischargeable under 11 U.S.C. § 523 are questions of law and are subject that are reviewed *de novo*. *In re Woodcock*, 45 F.3d 363 (10th Cir. 1995).

## **B. ARGUMENT**

This argument covers issues 2, 3, 4, 5 of 7 of the Issues on Appeal set forth above.

In early 2002, Congress introduced the Sarbanes-Oxley Act (“SOA”) in response to wrongdoing by corporate executives at Enron and the perceived negative effect said had on the capital markets. Title VIII of the SOA entitled, “The Corporate and Criminal Accountability Act (“CCAA”),” was designed to punish corporate criminals and hold them accountable for defrauding investors. [S. REP. NO. 107-146, at 2 (“[An Act] to provide for criminal prosecution and enhanced penalties of persons who defraud investors in publicly traded securities...

to disallow debts **incurred in violation of securities fraud laws** from being discharged ....”) (Emphasis added).]

Included in § 803 of the CCAA was an amendment to § 523(a) of the Bankruptcy Code, adding subsection (19) to the exceptions to discharge. U.S.C. § 523(a)(19) states that it applies to a debt that

(A) *is for*—

(i) *the violation* of any of the Federal securities laws . . . , any of the State securities laws, or any regulation or order issued under such Federal or State securities laws; or

(ii) common law fraud, deceit, or manipulation in connection with the purchase or sale of any security; and

(B) results, before, on, or after the date on which the petition was filed, from—

(i) any judgment, order, consent order, or decree entered in any Federal or State judicial or administrative proceeding;

(ii) any settlement agreement entered into by the debtor; or

(iii) any court or administrative order for any damages, fine, penalty, citation, restitutionary payment, disgorgement payment, attorney fee, cost, or other payment owed by the debtor. (Emphasis added)

Paragraph (A)(i) will only except from discharge a debt that “is for - the violation” of the securities laws. A court cannot ignore a term or phrase selected by Congress. *See Circuit City Stores, Inc. v. Adams*, 532 U.S. 105, 115 (2001) (noting each provision within an act must have an intended meaning); *United*

*States v. Coward*, 296 F.3d 176, 183 (3rd Cir. 2002) (meaning should be given to each statutory phrase). The Department of Securities' argument can be summed up as a novel interpretation of the preposition "for" and the term "violation." The dictionary defines "for" in the very context used in the statute as "for - in punishment of ... as in *payment for the crime*." The bankruptcy court's decision has the effect to hold that the Congress in using the preposition "for," meant non-dischargeability of a debtor's debt "in punishment of" a crime committed by someone other than the debtor.

Black's Law Dictionary defines a "violation" as "[a]n infraction or breach of the law." *See Black's Law Dictionary* 1564 (7th Edition 1999). However, the term "violation" is not defined in the Bankruptcy Code or the securities' laws. 15 U.S.C. §§ 77b, 78b; 11 U.S.C. § 101. The Department of Securities appears to argue that "violation" means any debt arising under the securities laws. The bankruptcy court in its decision found that Mathew's "innocent victims" defense is of no legal consequence. (*See Appendix pages 560 – 566*). Interpreting "violation" to mean all claims arising under the securities laws or arising out of any litigation, which touches on securities' laws contravenes several canons of statutory interpretation.

Section 523(a)(19) was added to the bankruptcy code to prevent wrongdoers from benefiting from a bankruptcy discharge. "Congress' inclusion of § 523(a)(19) was 'meant to prevent *wrongdoers* from using the bankruptcy laws as a shield and

to allow defrauded investors to recover as much as possible." *In re Lewendowski*, 325 B.R. 700, 704 (U.S.B.C. M.D. Penn. 2005), *quoting* Legislative History of Title VIII of HR 2673 (emphasis added).

If Congress intended to except from discharge all debts arising under the securities laws then it could have left out the word "violations." By selecting violation Congress is clearly targeting the wrongdoer for denial of discharge.

Therefore, the bankruptcy court's adoption of Department of Securities' interpretation requires the court to invade the domain of the legislative branch by affirmatively disregarding a word selected by Congress. *Mobil Oil Corp. v. Higginbotham*, 436 U.S. 618, 625 (1978). ("There is a basic difference between filling a gap left by Congress' silence and rewriting rules that Congress has affirmatively and specifically enacted."); *Senator Linie GMBH & Co. KG v. Sunway Line, Inc.*, 291 F.3d 145, 167 (2nd Cir. 2002) (noting even when judicial power is at its apex, courts should not rewrite statutes); *In re Weilein*, 319 B.R. 175 (Bankr. N.D. Iowa 2004) ("Analysis of §523(a)(19) must begin 'with the language of the statute itself.'" *United States v. Ron Pair Enterprises, Inc.*, 489 U.S. 235, 241 (1989) ("When a 'statute's language is plain, the sole function of the courts is to enforce it according to its terms....").

Additionally, the inclusion of the exception in paragraph (A)(ii) of § 523(a)(19) suggests that "violation" cannot mean "all debts arising under the

securities laws." Paragraph (A)(ii) renders nondischargeable any debt that is for fraud, deceit or manipulation in connection with a securities transaction. If all debts arising from claims under federal and state securities laws are nondischargeable pursuant to paragraph (A)(i), it is difficult to discern what independent purpose paragraph (A)(ii) serves. It is not proper to interpret a paragraph in a way that will render another paragraph within the same subsection superfluous. *Kawaauhau v. Geiger*, 523 U.S. 57, 62 (1998) ("[W]e are hesitant to adopt an interpretation of" section 523(a)(6) that would render section 523(a)(9) "superfluous."); *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 546, 556-57 (1994) (construing term in a way that would not render another provision superfluous).

Neither does the legislative history support The Department of Securities' interpretation.

First, The Department of Securities ignores the fact that Congress made a decision to narrow the applicability of paragraph (A)(i) of subsection 19 to violations *per se*. In the Senate Bill the original language, which stated

(A) arises under a claim relating to –

(i) the violation of any of the Federal securities laws... [S. REP. NO. 107-146 at 33 (2002)]

was changed in the final Act that became law to:

(A) is for-

(i) the violation of any of the Federal securities laws...[Sarbanes-Oxley Act, Pub. L. No. 107-204, § 803, 116 Stat. 801 (2002).]

This change clearly argues against The Department of Securities' interpretation that all debts relating to securities laws are exempt from discharge regardless of whether the debtor himself violated securities law.

Second, the Committee Report stated that subsection 19 was added because "Current bankruptcy law may permit such **wrongdoers** to discharge their obligations under court judgments or settlements based on securities fraud and other securities violations." (Emphasis added) and because "[u]nder current laws, state regulators are often forced to 'reprove' their fraud cases in bankruptcy court to prevent discharge...." [S. REP. NO. 107-146 at 16 (2002)] Under The Department of Securities' twisted interpretation, Congress would have to have meant the term "wrongdoers" to include those who committed no "wrongdoing."

Third, § 803 of the CCAA reads "Debts Nondischargeable if Incurred in Violation of Securities Fraud Laws." The Sarbanes-Oxley Act, Pub. L. No. 107-204, 116 Stat. 745, 801, 802 (2002). A review of the surrounding text of the CCAA reveals that no other provision appears on its face to target non-culpable conduct. *Id.* at §§ 801-07.

Lastly, perhaps the most important policy of the Bankruptcy Code is the "fresh start." *Grogan v. Garner*, 498 U.S. 279, 286 (1991) (endorsing fresh start policy of Code); *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934)

(acknowledging central purpose of Bankruptcy Act was to provide debtor with new beginnings). The fresh start ensures that an innocent debtor receives a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt. Due to the importance of the fresh start, the creditor must demonstrate that one of the enumerated exceptions applies even though the creditor was the deserving party outside of bankruptcy. *Grogan, supra*, at 291 (requiring creditor to prove exception applies by a preponderance of evidence); *Century 21 Balfour Real Estate v. Menna (In re Menna)*, 16 F.3d 7, 9 (1st Cir. 1994) ("[T]he claimant must show that its claim comes squarely within an exception enumerated in Bankruptcy Code section 523(a)."). Exceptions to discharge are construed strictly against the Creditor. It is clear that § 523 (a)(19) was designed to close loopholes allowing a debtor who violated the securities laws from receiving a discharge and not to deny a discharge to everyone including the targets of the violation to be denied a discharge. *See, Prime Equity Fund LP v. Lichtman (In re Lichtman)*, 388 B.R. 396 (M.D. Fla. 2008).

Generally, most debts are dischargeable, but if the debt stems from a culpable act personally committed by the debtor, a conduct exception may prevent the debtor from discharging the debt. *Stackhouse v. Hudson (In re Hudson)*, 859 F.2d 1418, 1420 (9th Cir. 1988). These conduct exceptions focus solely on the debtor's conduct. *Rutanen v. Baylis (In re Baylis)*, 313 F.3d 9, 19 (1st Cir. 2002).

The ability to discharge debts unless the debt stems from a culpable act personally committed by the debtor is a fundamental and rarely disturbed policy of the Bankruptcy Code.

Congress could have easily created an exception that would clearly and unambiguously cover all securities debts. There is little evidence that such an exception was what Congress intended. As it would fundamentally change the concept of the fresh start for non-culpable debtors, this Court should not adopt this interpretation.

In this case, Mathews was an investor of the wrongdoer (Schubert). All of the evidence presented in the state court, and the bankruptcy court affirmed by the U. S. District Court, by the Department of Securities proved that Schubert was a wrongdoer. (*See* Appendix pages 225 – 278). Schubert plead guilty, she committed the securities violations. The only allegation against Mathews was that he was an investor. He happened to be an investor who had received money from Schubert, but there is no evidence that Mathews was a wrongdoer. (*See* Appendix pages 93 – 177). Even the state court judgment merely found that Mathews had been unjustly enriched. (*See* Appendix pages 449 – 452). There was no finding that Mathews had violated any securities laws or assisting in wrongdoing. *See Oklahoma Department of Securities v. Blair*, 2010 OI 16, ¶ 10; – P. 3<sup>rd</sup> –.

Without wrongdoing by Mathews, § 523(a)(19) does not come into play and the discharge should not be denied.

The bankruptcy court in Colorado has stated:

Essentially, this statute precludes dischargeability if two conditions are met. First, the Plaintiffs must establish that the debt is for violation of securities laws or for fraud in connection with the purchase or sale of a security (the 'Subsection A requirement'). In addition, the debt must be memorialized in a judicial or administrative order or settlement agreement (the 'Subsection B requirement'). If Plaintiffs cannot establish both requirements, their claim will fail.

*In re Bahram Amir JAFARI*, 2009 WL 416849 (Bkrtcy D. Colo. 2009); *see also*, *MCI Worldcox Network Services, Inc. v. Graphnet, Inc.*, 2005 WL 1116163 at 13 (D. N.J. 2005) (excepts from discharge 'debts arising from judgment ... based upon debtor's violation of certain federal securities laws, state securities laws ...').

Therefore, both the statutory language, the legislative history and case law strongly indicate that § 523(a)(19) is for the violation of securities laws by the debtor. Since Mathews has *not* been found to have committed a violation of securities laws, the Department of Securities should not be able to utilize the exception in § 523(a)(19), to deny his discharge. For these reasons, Mathews assert the bankruptcy court erred in invoking § 523(a)(19) to deny Mathews' discharge.

## PROPOSITION II

**THE U. S. DISTRICT COURT ERRED IN AFFIRMING THE BANKRUPTCY COURT'S FINDING THAT THERE WAS NO NEED TO PROVE A VIOLATION OF EITHER OKLAHOMA OR FEDERAL SECURITIES LAWS IN ORDER TO DENY MATHEWS DISCHARGE UNDER § 523(A)(19) AS THE CONSENSUS OF THE COURTS IS THAT ONLY A DEBT WHICH RESULTS FROM A VIOLATION BY THE DEBTOR OF SECURITIES LAWS IS NONDISCHARGEABLE.**

### A. STANDARD OF REVIEW

*See* Proposition I(A).

### B. ARGUMENT

This argument is intended to address Issues 3, 4, 5, 6, 8 and 9 on Appeal set forth above.

It is clear from a review of cases in the various circuits that § 523(a)(19) does not apply to the case at bar because the debt in question was not the result of a securities violation by Mathews. *See* Appendix pp. 93-177 and 449-452. The Department of Securities has not and cannot show that said debt arose from a securities violation or fraud in connection with the purchase or sale of a security, by Mathews.

In *Peterman and Reactence, Inc v. Whitcomb (In re Whitcom)*, 305 B.R. 806 (Bankr. N.D. Ill. 2004), the court found that Whitcomb's debt was nondischargeable under 523(a)(19) because Whitcomb's "debt **results from** fraud,

fraudulent inducement and fraudulent misrepresentations **made by the Debtor...**" in the sale of securities to the plaintiffs (emphasis added). *Id.* at 810.

In *Barnes v. Jeffrey Michael Dupree (In re Dupree)*, 336 B.R. 520 (Bankr. M.D. Fla. 2005), the court noted "Obviously, Congress intended to design a broad provision to except from bankruptcy discharge all securities fraud and other securities violations by '**wrongdoers.**'" (emphasis added). *Id.* at 527.

In *Frost, et al. v. Civiello (In re Civiello)*, 348 B.R. 459 (Bankr. N.D. Ohio 2006), the court found that "The judgment '**results from' Defendant's violation** of the securities law identified in the cease and desist order, thereby satisfying the requirement of 11 U.S.C. § 523(a)(19)(B)" (emphasis added). *Id.* at 467.

Analogously, in *MCI Worldcom Network Services, Inc. v. Graphnet, Inc.*, 2005 WL 1116163 (D.N.J. 2005) the court stated "[r]ather, a closer look at the statute reveals that the exception under 11 U.S.C. § 523(a)(19) is not just for any debt that results from a settlement, but only for debts that arise out of a settlement agreement **based upon the debtors violation of federal or state securities laws** (emphasis added)... Because defendant does not argue, nor could it, that the Settlement Agreement here arose from plaintiffs violations of securities laws, this argument too must fail." *Id.* at 12-13. In this case, before this court, while there is no settlement or agreement at issue, the application is clear § 523(a)(19) only applies upon the violation by the debtor of Federal or State Securities Laws.

The consensus of the cases over the last six years in which a court found a debt nondischargeable under Section 523(a)(19), it arose as a result of the individual debtor(s) committing securities law violations or fraud in connection with the purchase and sale of securities. *See also State of Idaho, Department of Finance, Securities Bureau v. Robert O. McClung (In re McClung)*, 304 B.R. 419 (Bankr. D. Idaho 2004); *Nortman, et al. v. Gordon Sloan Smith (In re Smith)*, 362 B.R. 438 (Bankr. D. Ariz. 2007); *Trucks v. Williams (In re Williams)*, 370 B.R. 397 (Bankr. M.D. Fla. 2007); *Fishbach, et al v. Simon (In re Simon)*, 311 B.R. 641 (Bankr. S.D. Fla. 2004).

In *Shaefer v. Demar (In re Demar)*, 373 BR 232 (E.D.N.Y. 2007) the bankruptcy court dismissed the adversary proceeding in part because the "...plaintiff has not alleged facts that show that the debt was for a violation of federal or state securities laws or regulations." 373 B.R. at 239 (emphasis added).

The clear consensus of these cases is that § 523(a)(19) denies discharge to a debtor who violated the securities laws. Mathews in this case did not violate the securities laws. The violation was by Schubert and not Mathews. (*See Appendix pages 241 – 278*). The only finding by any court (the Oklahoma County district court) was that Mathews has been unjustly enriched. (*See Appendix pages 449 – 452*). If Schubert was before the bankruptcy court, then a denial of her discharge would be clear, but Schubert is not the debtor, she, was the architect of the Ponzi

scheme that gave rise to this case, Mathews who put his trust in Schubert like the other investors, is the debtor. Mathews is not the wrongdoer; and therefore, § 523(a)(19) is not applicable because the first element is missing. *See, In re Bahram Amir JAFARI*, 2009 WL 416849 (Bkrcty D. Colo. 2009).

In the Oklahoma Supreme Court case recently decided on the Oklahoma county district court case, the Oklahoma Supreme Court recognize the defendant investors as innocent victims of a Ponzi scheme. The Court also recognized the Department of Securities was only seeking restitution from 158 defendants (which included Mathews) on grounds of unjust enrichment, and fraudulent transfer and that the claim of fraudulent transfer was withdrawn and the Department of Securities was only proceeding against the investors (Mathews) based on unjust enrichment. *Oklahoma Department of Securities v. Blair*, 2010 OK 16, ¶ 1 and ¶ 10; – P. 3<sup>rd</sup> –.<sup>2</sup>

The Oklahoma Supreme Court goes on to say, "In the trial court the Department explained that it made no allegation that the defendants (Mathews) violated the securities statutes or materially aided in the violation of those statutes." *Oklahoma Department of Securities v. Blair*, 2010 OI 16, ¶ 10; – P. 3<sup>rd</sup> –.

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<sup>2</sup> Even though Mathews was not a party to this appeal to the Oklahoma Supreme Court, the Court is discussing the same case that included Mathews as one of the 158 investors.

The Oklahoma Supreme Court did hold that the Department of Securities could proceed against the 158 defendants on equitable grounds for unjust enrichment if the investors received artificially high dividends. The case was reversed and remanded for further proceedings. *Oklahoma Department of Securities v. Blair*, 2010 OK 16, ¶ 30; – P. 3<sup>rd</sup>–.

For these reasons Mathews assert that the U. S. District Court erred in affirming the bankruptcy court's denying Mathews' discharge.

### **PROPOSITION III**

**THE U. S. DISTRICT COURT ERRED IN AFFIRMING THE BANKRUPTCY COURT'S FINDING THERE WAS SUFFICIENT UNDISPUTED FACTS TO ENTITLED THE OKLAHOMA DEPARTMENT OF SECURITIES TO SUMMARY JUDGMENT AS THERE WERE NUMEROUS DISPUTED FACTS CONCERNING THE CULPABILITY OF MATHEWS.**

#### **A. STANDARD OF REVIEW**

*See* Proposition I(A).

#### **B. ARGUMENT**

This Proposition addresses Issue 1 of the Issues on Appeal above.

In the response to the Department of Securities' motion for summary judgment, Mathews argued that he had not violated any securities laws and that he had merely an investor with Schubert. As part of Mathews' response to the motion for summary judgment, Mathews attached his affidavit that they were unaware that

Schubert was involved in any illegal activities. His only involvement with Schubert was as an investor in her "day trading" operation. (See Appendix pages 134 – 177) and *Oklahoma Department of Securities v. Blair*, 2010 OK 16, ¶ 10; – P. 3<sup>rd</sup>–. Mathews' response at the very least created a question of fact as to whether Mathews had violated any securities laws which is a key eliminate for the denial of discharge under § 523(a)(19). Since there was a clear question of fact concerning the culpability of Mathews' summary judgment by the bankruptcy court was inappropriate and should not have been affirmed by the U. S. District Court. *Celotex Corp. v. Catrett*, U. S. 317 (1986).

### **VIII. CONCLUSION**

Based upon the foregoing Mathews would pray that this court would reverse the judgment of the U. S. District court affirming the bankruptcy court denying dischargeability of the state court judgment against Mathews. Mathews would ask that the judgment of the U. S. District Court affirming the bankruptcy court be reversed and the bankruptcy court be instructed to enter judgment on behalf of Mathews allowing the dischargeability of the state court judgment, or in the alternative, remanding the case for further consideration.

### **ORAL ARGUMENTS**

Oral Arguments are necessary because § 523 (a)(19) is a relatively new statute and is being contested in various circuits.

Respectfully submitted,

/s/ Robert N. Sheets

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APPELLANT, ROBERT WILLIAM  
MATHEWS**

**CERTIFICATE OF SERVICE**

I hereby certify that on the 16<sup>th</sup> day of June, 2010, I electronically transmitted the attached document to the Clerk of the Court using the ECF System for filing and I served the attached document by Regular U.S. Mail on the following, who are registered participants of the ECF System:

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I also hereby certify that:

(1) All required privacy redactions have been made and, with the exception of those redactions, every document submitted in Digital Form or scanned PDF format is an exact copy of the written document filed with the Clerk, and;

(2) The digital submissions have been scanned for viruses with the most recent version of a commercial virus scanning program (Symantec AntiVirus, Version 10.1.5.5000, updated 10/04/2007, Revision 20) and, according to the program, are free of viruses.

/s/ Robert N. Sheets

**CERTIFICATE OF COMPLIANCE**

1. This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because:

  x   this brief contains 5513 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

/s/ Robert N. Sheets

IN THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF OKLAHOMA

OKLAHOMA DEPARTMENT OF SECURITIES )
ex rel. IRVING L. FAUGHT, Administrator, )
Plaintiff/Appellee, ) No. CIV-09-185-D
vs. )
ROBERT WILLIAM MATHEWS, ) APPEAL FROM UNITED STATES
Defendant/Appellant. ) BANKRUPTCY COURT FOR THE
WESTERN DISTRICT OF
OKLAHOMA:
CASE NO. BK-07-10108-BH;
ADVERSARY NO. 07-1140-BH

ORDER

Defendant/Appellant Robert William Mathews ("Appellant") brings this action to appeal an order of the United States Bankruptcy Court for the Western District of Oklahoma (the "Bankruptcy Court") granting judgment against the Appellant in an adversary proceeding brought in Appellant's Chapter 7 bankruptcy action. In the adversary proceeding, the Bankruptcy Court granted the summary judgment motion of Plaintiff/Appellee the Oklahoma Department of Securities, ex rel. Irving L. Faught, Administrator ("Appellee") on Appellee's claim that a debt resulting from an Oklahoma state court judgment against Appellant was not dischargeable in his Chapter 7 bankruptcy action.

Background:

According to the Bankruptcy Order, the undisputed facts reflect that Appellant and others were investors in a securities fraud scheme, described as a Ponzi scheme and a check exchange scheme, operated by Marsha Schubert of Crescent, Oklahoma. Schubert defrauded investors of

more than \$9 million.<sup>1</sup> Pursuant to the Ponzi scheme, instead of investing participants' funds in legitimate investments, Schubert would utilize those funds to pay purported profits to other individuals. Absent the improper use of investor funds, the latter individuals would not have received a profit. In the check exchange scheme, Schubert utilized other individuals' checking accounts to "float" payments to investors as the investors' purported profits. Appellant was among the investors who received payment in the form of purported profits, but consisting of funds belonging to other individuals. He received funds estimated to be in excess of \$500,000.

Appellee brought a state court action pursuant to the Oklahoma Uniform Securities Act, Okla. Stat. tit. 71 § 1-101 *et. seq.*, alleging Appellant and others were liable for unjust enrichment as a result of the funds they received from Schubert. It sought a judgment requiring Appellant to disgorge the profits he allegedly received from the securities scheme. Appellee moved for summary judgment on its unjust enrichment theory, arguing that Appellant should be directed to disgorge any profit he received as a result of the scheme.

The District Court of Oklahoma County ruled in favor of Appellee and against the Appellant and other investors, holding that they were liable on the unjust enrichment theory. Its judgment required Appellant and other investors to disgorge and repay the funds. That decision was appealed, and the Oklahoma Court of Civil Appeals ("Court of Appeals") affirmed the judgment of the state court. A copy of the appellate opinion is included in the instant record on appeal. After the state court entered judgment, Appellant filed a Chapter 7 bankruptcy action; among the debts he sought to discharge in bankruptcy is the state court judgment requiring him to disgorge the profits he received from Schubert.

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<sup>1</sup>Schubert was convicted of both state and federal crimes based on her fraudulent scheme.

Appellee brought the underlying adversary proceeding, seeking a determination that the state court judgment against Appellant is not dischargeable in bankruptcy because the debt is governed by the exception to discharge set forth at 11 U. S. C. § 523(a)(19). It filed a motion for summary judgment on that issue, and the Bankruptcy Court granted the motion. In doing so, it held that the state court judgment requiring disgorgement of profits gained from a violation of the Oklahoma securities laws, as interpreted by the state court and Court of Appeals, satisfied the requirements of the § 523(a)(19) exception.

Appellant argues the Bankruptcy Court erred because § 523(a)(19) is limited to judgments resulting from the debtor's direct violation of the state securities law, and the Appellant did not directly violate the Oklahoma securities law. Furthermore, Appellant argues, the Bankruptcy Court ignored numerous factual disputes which preclude summary judgment. Appellee contends the Bankruptcy Court correctly interpreted the law; it also notes that the only facts relevant to its determination were found to be undisputed. Thus, any factual disputes that may have been asserted do not preclude a finding on the ultimate issue that the debt was not dischargeable in bankruptcy.

Standard of review:

The legal conclusions or determinations of a bankruptcy court are subject to *de novo* review on appeal to a federal district court. *In re Albrecht*, 233 F. 3d 1258, 1260 (10<sup>th</sup> Cir. 2000); *In re Herd*, 840 F.2d 757 (10<sup>th</sup> Cir. 1988). Factual findings are reviewed for clear error, and will be adopted unless clear error is found. *In re Garrett*, 64 F. App'x 739, 740 (10<sup>th</sup> Cir. 2003)(unpublished opinion) (citing *Turner v. FDIC*, 18 F. 3d 865, 868 (10<sup>th</sup> Cir. 1994)). Whether a debt is dischargeable under 11 U. S. C. § 523 is a question of law subject to *de novo* review. *In re Troff*, 488 F. 3d 1237, 1239 (10<sup>th</sup> Cir. 2007).

Analysis:

Although the Bankruptcy Code provides for the discharge of the debtor's debts, certain debts are determined by statute to be excepted from discharge. 11 U. S. C. § 523. In this case, the parties agree that the only exception applicable to the facts is set forth at 11 U. S. C. § 523(a)(19), which provides an exception to discharge of a debt:

(19) that—

(A) is for—

- (i) the violation of any of the Federal securities laws (as that term is defined in section 3(a)(47) of the Securities Exchange Act of 1934), any of the State securities laws, or any regulation or order issued under such Federal or State securities laws; or
- (ii) common law fraud, deceit, or manipulation in connection with the purchase or sale of any security; and

(B) results, before, on, or after the date on which the petition was filed, from —

(i) any judgment, order, consent order, or decree entered in any Federal or State judicial or administrative proceeding;

(ii) any settlement agreement entered into by the debtor; or

(iii) any court or administrative order for any damages, fine, penalty, citation, restitutionary payment, disgorgement payment, attorney fee, cost, or other payment owed by the debtor.

11 U. S. C. § 523(a)(19). In its Order, the Bankruptcy Court noted the § 523(a)(19) provisions applicable to this case involve two elements which must be established: 1) a debt that is for a violation of state securities laws; and (2) the debt results from a judgment or order in a federal or state judicial proceeding. Bankruptcy Order at p. 5; *In re Civiello*, 348 B. R. 459, 464 (Bankr. E. D. Ohio 2006).

In this case, Appellant does not argue the state court judgment fails to qualify as a judgment for purposes of § 523(a)(19). Because the decision is a judgment within the meaning of the statute,

that element of § 523(a)(19) is clearly satisfied. Appellant's arguments focus instead on the initial element of the exception, as he contends the debt did not result from his violation of state securities laws. He contends that, as an investor in the Ponzi scheme, he did not violate state law; instead, he asserts that he and the other investors are victims of a violation of state securities law by Schubert.

Appellant's arguments regarding the application of Oklahoma securities law to his status as an investor were, however, considered and rejected by the state court. The state court rejected Appellant's arguments that he was an innocent victim of the Ponzi scheme; its decision applying Oklahoma securities law was affirmed by the Court of Appeals, which held the "defense of being 'innocent victims' has no merit under the facts here. Appellants are in possession of funds which, in equity and good conscience, belong to other investors." Court of Appeals Opinion, ¶ 13.<sup>2</sup>

In its Order, the Bankruptcy Court noted that the Court of Appeals opinion concluded the Oklahoma Securities Act authorizes the disgorgement of funds received by investors who "directly and pecuniarily benefitted" from the violation of the Act by a third party. Thus, the Bankruptcy Court concluded that the judgment against Appellant and others was made pursuant to Oklahoma securities law, and further noted the Court of Appeals' conclusion that such law does not require wrongful intent, rejecting Appellant's contention that he could not have violated the law because he was an innocent victim of the Ponzi scheme. Order, at p. 6.

Because the underlying judgment which created the debt at issue involves only Oklahoma law, the Bankruptcy Court correctly found that this case is controlled by the application of Oklahoma securities law, as "[s]ection 523(a)(19) discharge exceptions are often defined by law

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<sup>2</sup>To the extent Appellant also argues that the Bankruptcy Court erroneously failed to consider factual disputes regarding his status, the Court disagrees. The Bankruptcy Court correctly focused on the only facts relevant to its decision regarding the applicability of §523(a)(19).

external to the Bankruptcy Code.” *In re Lichtman*, 388 B. R. 396, 409 (Bankr. M. D. Fla. 2006). The Bankruptcy Court clearly did not err in relying on the Court of Appeals’ interpretation of Oklahoma securities law as extending to Appellant and authorizing his disgorgement of profits obtained through a violation of the securities law by Schubert. The Bankruptcy Court concluded that the Court of Appeals interpretation of Oklahoma law as extending to Appellant was sufficient to satisfy the § 523 (a)(19) element of a debt resulting from a violation of state securities law, and this Court agrees.

Appellant further argues, however, that § 523(a)(19) cannot apply to the resulting judgment and debt because it did not result from his “violation” of state securities law.

Although Appellant discusses at some length the definition of a “violation” and presents authority addressing exceptions to the discharge of a debt in bankruptcy, he offers no authority holding that § 523(a)(19) applies only to a debtor who has been determined to have personally violated state or federal securities law. He correctly notes, however, that ““exceptions to discharge are to be narrowly construed, and because of the fresh start objective of bankruptcy, doubt is to be resolved in the debtor’s favor.”” *In re Millikan*, 188 F.App’x 699, 701 (10<sup>th</sup> Cir. 2006) (unpublished opinion) (quoting *Bellco First Fed. Credit Union v. Kaspar*, 125 F. 3d 1358, 1361 (10<sup>th</sup> Cir. 1997)).

Notwithstanding the general narrow application of the statutory exceptions to discharge, however, the § 523(a)(19) exception has an express purpose and is broadly construed to achieve that purpose. The exception is designed to be broadly applied because the purpose of that exception is to protect investors and hold accountable those who violate securities laws. *In re Civiello*, 348 B. R. at 463. As Appellee points out, § 523(a)(19) does not expressly state that the exception is limited to the debtor’s personal violation of such laws. Moreover, other subsections of § 523 include

language indicating that discharge is limited where certain actions have been taken “by the debtor.” Certainly, Congress could have included similar language in § 523(a)(19), but chose not to do so. Further, as Appellee also points out, § 523(a)(19) specifically includes a “disgorgement” order as among the judgment debts which are excepted from discharge under its terms. The statute provides that it extends to “any court or administrative order for any damages, fine, penalty, citation, restitutionary payment, disgorgement payment, attorney fee, cost, or other payment owed by the debtor. § 523(a)(19)(B)(iii) (emphasis added). The statute does not expressly state that the payment owed must result from the direct violation of the state law by the debtor, so long as it is owed by the debtor.

In this case, the Court of Appeals held that, under Oklahoma law, a judgment requiring disgorgement of profits gained from a violation of Oklahoma securities laws is not limited only to the individual who actually violated those laws. Instead, disgorgement extends to those who profited or benefitted from the violation by another person. Applying that interpretation of the Oklahoma law underlying the state judgment entered against Appellant, the Bankruptcy Court implicitly found that § 523(a)(19) is not limited to a debtor who has directly violated a state securities law. In extending the statute to Appellant, the Bankruptcy Court applied the Oklahoma Court of Appeals decision; that decision held that Appellant and others who pecuniarily benefitted from a violation of Oklahoma securities law may be directed to disgorge the profits representing that benefit.

Appellant’s arguments do not convince the Court that the Bankruptcy Court erred in its application of Oklahoma law underlying the judgment and debt which Appellant seeks to have discharged in his bankruptcy. The Bankruptcy Court did not err in holding that the Appellee

satisfied its burden of proving that, under the exception set forth in § 523(a)(19), the debt involved here is not dischargeable in bankruptcy. Accordingly, the decision should be, and is, AFFIRMED.

Conclusion:

For the foregoing reasons, the decision of the Bankruptcy Court granting summary judgment in favor of Appellee and against the Appellant is AFFIRMED.

IT IS SO ORDERED this 10<sup>th</sup> day of February, 2010.



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TIMOTHY D. DEGIUSTI  
UNITED STATES DISTRICT JUDGE

IN THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF OKLAHOMA

OKLAHOMA DEPARTMENT OF SECURITIES )  
ex rel. IRVING L. FAUGHT, Administrator, )

Plaintiff/Appellee, )

vs. )

ROBERT WILLIAM MATHEWS, )

Defendant/Appellant. )

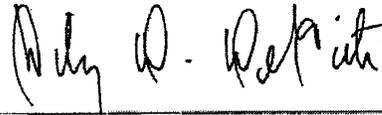
No. CIV-09-185-D

APPEAL FROM UNITED STATES  
BANKRUPTCY COURT FOR THE  
WESTERN DISTRICT OF  
OKLAHOMA:  
CASE NO. BK-07-10108-BH;  
ADVERSARY NO. 07-1140-BH

**JUDGMENT**

Pursuant to the Order filed separately herein in which this Court affirmed the decision and judgment of the United States Bankruptcy Court for the Western District of Oklahoma, judgment is hereby entered in favor of Plaintiff/Appellee Oklahoma Department of Securities *ex rel.* Irving L. Faught, Administrator, and against the Defendant/Appellant Robert William Mathews, judgment is hereby entered in favor of Plaintiff/Appellee and against Defendant/Appellant on the appeal filed herein by Appellant.

IT IS SO ORDERED this 10<sup>th</sup> day of February, 2010.



TIMOTHY D. DEGIUSTI  
UNITED STATES DISTRICT JUDGE