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No. 105682

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CLERK

THE SUPREME COURT OF THE STATE OF OKLAHOMA

OKLAHOMA DEPARTMENT OF SECURITIES
ex rel., **IRVING L. FAUGHT, ADMINISTRATOR,**

Plaintiff/Respondent

v.

BARRY AND ROXANNE POLLARD

Defendants/Petitioners

RESPONSE OF THE OKLAHOMA DEPARTMENT OF SECURITIES
TO PETITIONERS' BRIEF IN CHIEF

APPEAL FROM THE DISTRICT COURT OF OKLAHOMA COUNTY
CASE NO. CJ-2005-3799
THE HONORABLE VICKI ROBERTSON
DISGORGEMENT

June 19, 2008

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SUMMARY OF THE RECORD

Marsha Schubert *dba* Schubert and Associates (Schubert) operated a fraudulent “Ponzi” scheme in violation of federal and state laws including the Oklahoma Uniform Securities Act of 2004 (Act), Okla. Stat. tit. 71, §§ 1-101 through 1-701 (Supp. 2003), and the Oklahoma Securities Act (Predecessor Act), Okla. Stat. tit. 71, §§ 1-413, 501, 701-703 (1991 & Supp. 2003). Order of Permanent Injunction, Exhibit A to *Plaintiff’s Motion for Summary Judgment* at R. 73; Schubert’s Federal Plea Agreement, Exhibit B to *Plaintiff’s Motion for Summary Judgment* at R. 84; Schubert’s State Guilty Plea (wherein she stated as the factual basis for her plea that she obtained money in a “Ponzi” scheme in which she promised that the funds would be invested but instead, used the funds to pay prior investors). Exhibit C to *Plaintiff’s Motion for Summary Judgment* at R. 111.

Schubert’s “Ponzi” scheme began as early as December 1999, and continued until October 2004. ¶ 4 of Dan Clarke’s affidavit, Exhibit D to *Plaintiff’s Motion for Summary Judgment* at R. 125. The deposit items to and disbursements from the Schubert F&M Account, the Kattails Account, the Farm Account, and the Schubert BancFirst Account, for the period beginning in December of 1999 and ending in October of 2004, were reviewed and analyzed. ¶ 4 of Dan Clarke’s affidavit, Exhibit D to *Plaintiff’s Motion for Summary Judgment* at R. 125. Schubert, promising large financial returns, accepted funds in excess of Two Hundred Million Dollars (\$200,000,000) for purported investment (Schubert Investment Program). ¶ 5 of Dan Clarke’s affidavit, Exhibit D to *Plaintiff’s Motion for Summary Judgment* at R. 125. Marsha Schubert did not make the investments that she represented she would make, but instead, used most of the money to make distributions to other persons (“Ponzi” scheme). ¶ 7 of Dan Clarke’s affidavit,

Exhibit D to *Plaintiff's Motion for Summary Judgment* at R. 125. In connection with the Schubert scheme, investors, including Defendants Pollard, did not receive profits on their investment dollars because no investments were ever made. ¶ 7 of Dan Clarke's affidavit, Exhibit D to *Plaintiff's Motion for Summary Judgment* at R. 125. Rather, Defendants received the return of their own principal and/or that of other investors. ¶¶ 2 and 3 of Supplemental Affidavit of Dan Clarke, Exhibit A to *Plaintiff's to Defendants Pollards' Response to Motion for Summary Judgment* at R. 571-572.

Approximately 87 persons lost in excess of Nine Million Dollars (\$9,000,000) in the "Ponzi" scheme (Short Investors). ¶ 8 of Dan Clarke's affidavit, Exhibit D to *Plaintiff's Motion for Summary Judgment* at R. 125. Over 150 persons made approximately Six Million Dollars (\$6,000,000) in the "Ponzi" scheme (Relief Defendants). ¶ 9 of Dan Clarke's affidavit, Exhibit D to *Plaintiff's Motion for Summary Judgment* at R. 125.

On May 11, 2005, the Department brought an unjust enrichment action against Defendants Barry and Roxanne Pollard ("Defendants Pollard") in case number CJ-2005-3799. *Petition* at R. 1-4. Defendants Pollard received monies from Schubert to their enrichment, and that the monies received by the Pollards were to the detriment and expense of others deemed "short" investors. *Petition* at R. 4. Defendants Pollard did not give reasonably equivalent value for these monies and that such monies do not belong to the Defendants Pollard. *Petition* at 3.

From April 2000 through October 2004, Defendants Pollard paid a total of Fifty-Nine Thousand One Hundred Ten Dollars and Thirty-Five Cents (\$59,110.35) directly to Schubert which was deposited into her bank accounts. Accountant's Compilation Report

prepared by BKD, LLP (BKD) for Defendants Pollard, Exhibit G to *Plaintiff's Motion for Summary Judgment* at R. 133-136. From April 2000 through October 2004, Defendants Pollard received a total of Four Hundred Forty-Five Thousand Two Hundred Sixty-Eight Dollars and Six Cents (\$445,268.06) from Schubert's bank accounts. Accountant's Compilation Report prepared by BKD, LLP (BKD) for Defendants Pollard, Exhibit G to *Plaintiff's Motion for Summary Judgment* at R. 133-136. Defendants Pollard received a net gain of \$386,158.06. Accountant's Compilation Report prepared by BKD, LLP (BKD) for Defendants Pollard, Exhibit G to *Plaintiff's Motion for Summary Judgment* at R. 133-136. Defendant Barry Pollard admitted that the accounting compiled by BKD is correct. Transcr. Depo. Barry Pollard 25:3-12 (February 15, 2007), Exhibit H to *Plaintiff's Motion for Summary Judgment* at R. 166-167.

Defendants Pollard filed a motion to dismiss in this case on July 27, 2005 arguing, *inter alia*, that the Department did not have authority to bring its claims and that the Department did not have capacity to sue. *Defendant Pollards' Motion to Dismiss Plaintiff's Petition* at R. 47 -49. Like the court in Case No. CJ-2005-3796, the trial court overruled Defendants Pollards' motion to dismiss finding that the Department is entitled to seek disgorgement from Defendants Pollards for the money received from Schubert in excess of the value exchanged. Order of Judgment, Exhibit M to *Plaintiff's Motion for Summary Judgment* at R. 69.

In March of 2005, Defendant Barry Pollard filed a lawsuit in Logan County against Schubert, AXA Advisors LLC, and AXA Equitable Life Insurance Company. *Petition*, Exhibit 10 to *Defendant Pollards' Motion for Summary Judgment* at R. 760. Defendant Barry Pollard claimed that although he directly made payments to AXA and

AXA Equitable for his investments, Schubert also made money for him through options and day trading in her company, Schubert and Associates. *Petition*, Exhibit 10 to *Defendant Pollards' Motion for Summary Judgment* at R. 760. Defendant Barry Pollard received a judgment against Schubert in an amount not supported by evidence. Barry Pollard's Interrogatories, Exhibit K to *Plaintiff's Reply to Defendants Pollards' Response to Motion for Summary Judgment* at R. 626-629.

Defendant Barry Pollard's action violated the Logan County Court's *Temporary Restraining Order, Order Appointing Receiver, Order Freezing Assets and Order for Accounting* that stayed "all creditors and other persons seeking money, damages or other relief from the Defendants" from "doing any act or thing whatsoever to interfere with the orderly transfer of the Receivership assets to the Receiver or with the possession of or management by the Receiver of the Receivership assets" except upon leave of court. *Temporary Restraining Order*, Exhibit 9 to *Defendant Pollards' Motion for Summary Judgment* at R. 758. Upon the Receiver's inability to sell a Schubert asset, the Department filed an application to hold Defendant Barry Pollard in indirect contempt for attaching a lien on certain Receivership property (Lien). OSCN Court Minute, Exhibit B to *Plaintiff's Response to Defendant Pollards' Motion to Certify Questions for Interlocutory Appeal* at R. 1003-1004. The Department argued that such filing impeded the Receiver's ability to sell the property in contradiction of the Logan County order establishing the Receivership. OSCN Court Minute, Exhibit B to *Plaintiff's Response to Defendant Pollards' Motion to Certify Questions for Interlocutory Appeal* at R. 1003-1004. Judge Worthington ordered that the contempt citation be dismissed upon the release of the lien by Defendant Barry Pollard. OSCN Court Minute, Exhibit B to

Plaintiff's Response to Defendant Pollards' Motion to Certify Questions for Interlocutory Appeal at R. 1003-1004.

On March 29, 2007, the Department moved for summary judgment on the issues of the existence of a Ponzi Scheme and that the Defendants Pollard were unjustly enriched by approximately \$386,000 to the detriment of 87 "short" investors. *Plaintiff's Motion for Summary Judgment* at R. 62. In response, the Defendants Pollard argued that they had not been unjustly enriched and that they were entitled to setoff both the Logan County judgment against Schubert and a receivership claim they held by assignment. *Defendants Pollards' Response to the Plaintiff's Motion for Summary Judgment* at R. 202.

On May 9, 2007, Defendants Pollard filed the Notice of Assignment of Claim of a "short" Schubert investor, L&S Pollard Farms LLC. Assignment of Claim, Exhibit 12 to *Defendant Pollards' Motion for Summary Judgment* at R. 407. Defendants Pollard have asked the trial court to setoff 100% of the claim to any judgment granted to the Department. Assignment of Claim, Exhibit 12 to *Defendant Pollards' Motion for Summary Judgment* at R. 219-220. The Receiver did not recognize the assignment and made a 17% distribution to L&S Pollard Farms LLC in October of 2007. *Plaintiff's Response to Defendant Pollards' Motion to Certify Questions for Immediate Interlocutory Appeal* at R. 992. A 100% setoff would allow Defendant Pollards to receive a greater benefit than they already have.

Although Defendants Pollard do not deny they received thousands of dollars directly from Schubert, they deny they were unjustly enriched and for their proof attached an affidavit from their accountant, David Morley. Affidavit of Morley, Exhibit 6 to

Defendant Pollards' Response to the Plaintiff's Motion for Summary Judgment, at R. 359-363. The Department filed a motion to strike Morley's affidavit on the grounds that he provided a summary with no checks, deposits, tax documentation, bills of sale, calculations or other evidentiary material to support the annualized lump sum figures listed in the summary. *Plaintiff's Motion to Strike Affidavit of David Morley* at R. 418-419. The conclusory nature of Morley's summaries and the undocumented statements contained in his affidavit were not sufficient to defeat a summary judgment motion. *Plaintiff's Motion to Strike Affidavit of David Morley* at R. 418-419.

The Department conducted an exhaustive financial analysis as part of its investigation of Schubert's fraudulent scheme thereby identifying those who received less than the amount contributed to the scheme money ("short" investors) and those who benefited by receiving in excess of the amount contributed ("long" investors). A summary of certain of the transactions between Schubert and the Defendants was attached as Exhibit B to *Plaintiff's Reply to Defendants' Response to Motion for Summary Judgment* at R. 573-579. The summary specifically shows whose money Defendants Pollard received through the distributions made to them by Schubert. Summary of transactions, Exhibit B to *Plaintiff's Reply to Defendants' Response to Motion for Summary Judgment* at R. 573-579.

On October 26, 2007, the trial court granted a Partial Summary Judgment in favor of the Department regarding the existence of a "Ponzi" scheme and unjust enrichment of Defendants Pollard. Further the trial court denied the Defendants Pollards' right to any setoffs or offsets against any funds ordered to be disgorged by the Defendants Pollards. On January 10, 2008, this Court denied the Defendants Pollards' *Motion to Reconsider*

and/or Vacate Order Granting Partial Summary Judgment dated November 18, 2007; Motion for New Trial and/or Motion to Clarify and Brief in Support (“Motion to Reconsider”). On January 30, 2008, the trial court granted *Defendants’ Motion to Certify Questions of Immediate Interlocutory Appeal and Motion to Stay* under 12 Okla. Stat. 952(B)(3).

In granting a partial summary judgment in favor of the Department, the trial court held that the Ponzi scheme existed, that the Defendants Pollards were unjustly enriched under the Ponzi scheme and that the Defendants Pollards are not entitled to any setoffs. The only remaining issue to be decided by the district court is the amount by which the Defendants Pollards were unjustly enriched.

SUMMARY OF THE ARGUMENT

This case arises out of a multi-million dollar “Ponzi” scheme orchestrated by Marsha Schubert individually, and doing business as Schubert and Associates (“Receivership Subjects”). The gravamen of the matter is a request by the Defendants for preferential treatment over all other investors in the Schubert “Ponzi” Scheme. As a matter of law, such preferential treatment must be avoided. As a matter of law, the Department may seek the relief necessary to avoid such preferential treatment.

First, the lower court has the statutory and constitutional authority to fashion effective and complete equitable relief. In addition, the Department has the authority to seek equitable relief, to include disgorgement against non-violators of the securities laws. In proving its case, the Department is not required to “trace” the source of the funds paid to Defendants Pollard by Marsha Schubert. Finally, there is no mutuality of obligations

or parties to allow Defendants' request for setoff, in any amount, against the Department's disgorgement claim.

ARGUMENT

In orchestrating her investment scheme, Marsha Schubert collected in excess of Two Hundred Million Dollars (\$200,000,000) from numerous individuals, including Defendants Pollard, over a period of at least 58 months. ¶¶ 4, 8 and 9 of Dan Clarke's affidavit, Exhibit D to *Plaintiff's Motion for Summary Judgment* at R. 124-126. However, in connection with the Schubert scheme, investors, including Defendants Pollard, did not receive profits on their investment dollars because no investments were ever made. ¶ 7 of Dan Clarke's affidavit, Exhibit D to *Plaintiff's Motion for Summary Judgment* at R. 124-126. Rather, Defendants received the return of their own principal and/or that of other investors. ¶¶ 2 and 3 of the Supplemental Affidavit of Dan Clarke, Exhibit A to *Plaintiff's Reply to Defendants' Response to Motion for Summary Judgment* at R. 571-572.

It is uncontroverted that Marsha Schubert was operating a "Ponzi" scheme for an extended period of time prior to mid-October of 2004. The securities fraud known as a "Ponzi" scheme has long been described as:

a pyramid-type investment scheme where investors are paid profits from newly attracted investors promised large returns on their principal investments. Typically it is not supported by any underlying business venture. *An investor that does receive money is not receiving income on his or her investment, but merely a return of his or her own principal, or that of another investor.*

In re Fin. Federated Title & Trust, Inc., 309 F.3d 1325, 1327 n.2 (11th Cir. 2002) (emphasis added); see *In re Ponzi*, 15 F.2d 113 (D. Mass. 1926).

Through its investigation, the Department determined that most of the investment monies collected by the Receivership Subjects, including monies from Defendants Pollard, were deposited and commingled in bank accounts controlled by Schubert. In addition, the Department identified Schubert investors who received less than the total amount of their contributions to the scheme ("Short Investors") as well as investors who received in excess of the total amount of their contributions to the scheme ("Long Investors"). ¶¶ 8 and 9 of Dan Clarke's affidavit, Exhibit D to *Plaintiff's Motion for Summary Judgment* at R. 124-126.

In addition to its underlying action against Marsha Schubert, the Department filed civil actions against more than 150 of "long" Investors (Relief Defendants), including the action below against Defendants Pollard.¹ *Oklahoma County District Court Case Nos. CJ-2005-3796 consolidated with CJ-2005-3299, and CJ-2005-3799*. None of the Relief Defendants were alleged by the Department to have violated Oklahoma's securities laws, and with only rare exceptions, the Department does not believe they were willing participants in the fraud. As a matter of law, the Long Investors who financially benefited through the scheme should not be allowed to retain the funds that are the product of Marsha Schubert's fraudulent conduct at the expense of the Short Investors. *Cunningham v. Brown*, 265 U.S. 1 (1924).

DEPARTMENT MAY SEEK DISGORGEMENT FROM NON-VIOLATORS

The Act and the Predecessor Act confer upon the Department the ability to seek a wide range of legal and equitable relief in its efforts to enforce the securities laws.

¹ Except for Defendants Pollard, the relief defendants have been ordered to disgorge the amounts received in excess of their contributions to the Schubert scheme. Most have paid their judgments, made arrangements to settle their judgments through a payment plan, or filed for bankruptcy. Some of the relief defendants have appealed the judgments. Those appeals are currently before this Court in case Numbers 104004, 104161, 104262 and 104304.

Sections 1-603 of the Act and 406 of the Predecessor Act. This Court has recognized that the Oklahoma Legislature intended equitable remedies be available to the Administrator of the Department for enforcement under the Oklahoma securities laws and determined that the Administrator has the power to seek such remedial relief. *State ex rel. Day v. Southwest Mineral Energy, Inc.*, 1980 OK 118, ¶¶ 18-21, 617 P.2d 1334.

In *Southwest Mineral*, this Court interpreted a version of the Predecessor Act that did not specifically authorize the Administrator of the Department to seek general equitable remedies in district court actions. Under that version of the Predecessor Act, the Administrator was specifically authorized to seek an injunction or writ of mandamus, but was not specifically authorized to seek other equitable remedies such as disgorgement. This Court ruled that a specific provision authorizing the Administrator to seek disgorgement is not necessary as equity jurisdiction is conferred upon Oklahoma's district courts by the Oklahoma Constitution². *Southwest Mineral* at ¶¶ 17-21. This Court specifically held that disgorgement is a remedy available to the Administrator and to private investors. *Southwest Mineral* at ¶ 21.

The Court also stated that in interpreting the Predecessor Act, which was modeled after the Uniform Securities Act, it is proper to consider the interpretive history of the federal securities laws to construe similar state securities law provisions. *Id.* at ¶¶ 17-21.

The Court specifically said:

The Official Comments in the Draftsmen's commentary to the Uniform Securities Act make it clear that the interpretative history of the Federal Act was intended to be carried over into the State Act when the draftsmen elected to pattern the Uniform Securities Act language after the language of the Federal statutes.

² The Legislature subsequently amended both the Act and the to include very broad language authorizing the Administrator of the Department to seek equitable remedies in the district courts. See Sections 1-603 and 406 respectively.

Id. The Act likewise is modeled after the Uniform Securities Act of 2004.

The Oklahoma Supreme Court has not considered the issue of ordering disgorgement of monies fraudulently given to persons who did not themselves violate the Act. However, federal courts interpreting the federal securities laws have determined that the United States Securities and Exchange Commission may seek disgorgement from non-violator third parties who received funds from the person who violated the federal securities laws. *SEC v. Egan*, 856 F. Supp. 401 (N. D. Ill. 1993); *SEC v. Cherif*, 933 F.2d 403, n. 11 (7th Cir. 1991). The court in *SEC v. Colello*, 139 F.3d 674, 676 (9th Cir. 1998) stated:

[A]mple authority supports the proposition that the broad equitable powers of the federal courts can be employed to recover ill gotten gains for the benefit of the victims of wrongdoing, whether held by the original wrongdoer or by one who has received the proceeds after the wrong. For example, the Supreme Court has held that a plaintiff who has a cause of action under the securities laws can enforce those rights "by such legal or equitable actions or procedures as would normally be available to him." *Deckert v. Independence Shares Corp.*, 311 U.S. 282, 287-288. This court has declared that "federal courts have inherent equitable authority to issue a variety of 'ancillary relief' measures in actions brought by the SEC to enforce the federal securities laws." *SEC v. Wencke*, 622 F.2d 1363, 1369 (9th Cir. 1980).

In *Egan*, the court found no meaningful difference between wrongdoers and a third party for purposes of disgorgement:

... the deterrence purpose is not dependent on that status—for it is just as important to discourage illegal conduct by taking the proceeds of that illegality from those who have given no current value for the ill-gotten gains that have been turned over to them (even though they themselves have not directly engaged in the illegal activity).

Egan at 402 n.2.. The reason was to prevent unjust enrichment.

The Department's authority to seek disgorgement from non-violators flows from its authority to seek disgorgement from the violator. In addition, the district court has its own authority under the Constitution, the Act and the Predecessor Act to fashion effective and complete relief in resolution of this securities fraud. Even were that not the case, the Department prevails against the relief defendants under the theory of unjust enrichment.

Unjust enrichment is recognized by Oklahoma courts as an equitable remedy. This Court defines "unjust enrichment" as "a condition which results from the failure of a party to make restitution in circumstances where it is inequitable; i.e. the party has money in its hands that, in equity and good conscience, it should not be allowed to retain." *Harvell v. Goodyear Tire & Rubber Co.*, 2006 OK 24, ¶ 18, 164 P.3d 1028, 1035. To recover on a theory of unjust enrichment, the Department must establish that there was enrichment to the defendant(s) at the expense of other investors. *N.C. Corff P'ship. Ltd. v. OXY USA, Inc.*, 1996 OK CIV APP 92, 929 P.2d 288, 295.

Defendants cite *Johnson v. Studholme*, 619 F. Supp. 1347, 1350 (D. Colo. 1985) *aff'd*, 833 F.2d 908 (10th Cir. 1987) for their proposition that the Department cannot recover under a theory of unjust enrichment, but they fail to address the more recent and relevant caselaw. Over the twenty (20) years since *Johnson* was decided, courts have concluded that non-violators may be unjustly enriched by the receipt of fictitious profits from a "Ponzi" scheme and should not be allowed to keep the profits. *See Scholes v. Ames*, 850 F. Supp. 707 (N.D. Ill. 1994); *Chosnek v. Rolley*, 688 N.E.2d 202 (Ind. App. 1997); and *Egan* at 401-402.

Defendants also cite to *Stenger v. World Harvest Church, Inc.*, 2006 WL 870310 (N.D. Ga.) for their proposition that unjust enrichment is not the proper vehicle by which the Department may seek recovery. Because it is not a published decision, *Stenger* lacks any precedential value pursuant to Sup.Ct.R. 1.200(b)(5).

Nevertheless, the *Stenger* case relied on Georgia unjust enrichment law that differs from Oklahoma's in that it focused narrowly on the harm between the two parties to the original contract. *Stenger* at 3. In this case, Defendants had an investment relationship that presupposed a continual give and take of monies between the two parties. The more money Marsha Schubert purportedly made for Defendants, the more money they were likely to invest with her. Here, the resulting injustice is the harm caused to the Short Investors. It would be inequitable to allow Defendants to keep the funds they received in excess of the monies they invested when the Short Investors were not similarly treated and may never recover the full amount of their monies invested.

Braniff v. Coffield, 1947 OK 369, 190 P.2d 815, cited by Defendants for their proposition that the Department may not seek equity against persons who have not violated the securities laws, does not apply to the facts of this case. The *Braniff* plaintiffs asked the court to hold a corporation liable for fraud as an agent of the issuer of stock. *Id.* at 819-820. The securities laws defined an agent as a natural person, which, of course, a corporation is not. *Id.* at 819-820. The *Braniff* court refused to extend the penal provisions of the securities laws to the corporation because it believed the Oklahoma Legislature had expressed a clear intent that only natural persons are agents. *Id.* at 819-820.

The Department, in bringing this lawsuit, has not sought to extend the penal provisions of the Act to the Defendants. The Department sued Marsha Schubert for violations of the Act and the Predecessor Act, but has never suggested that Defendants violated the securities laws. Nevertheless, to allow the Defendants to keep the fictitious profits would only further Marsha Schubert's fraudulent scheme. Where as here the Defendants are family members of the violator, the natural beneficiaries of her generosity, it seems even more important to discourage illegal conduct by taking the proceeds of the illegality.

DEPARTMENT IS NOT REQUIRED TO TRACE TO SOURCE OF FUNDS

Appellants contend that the Department must demonstrate a legal or equitable right to the property sought, that is, that either the Department or the Short Investors are the rightful owners of the money. The United States Supreme Court in *Cunningham*, the original "Ponzi" scheme case, considered the attempt by the trustee of Charles Ponzi's estate to recover as unlawful preferences certain payments made to investors within the four months prior to Ponzi's bankruptcy filing. The *Cunningham* Court recognized that when a perpetrator has commingled the funds of multiple investors in a single account, "those assets lose their character as the peculiar assets of their investor" and are not specifically traceable. *Adams v. Moriarty*, 2005 OK CIV APP 105, ¶ 12, 127 P.3d 621, 624 (case relating to the deposit and commingling of investors' funds in the general operating account used in a "Ponzi" scheme). The decision by the Supreme Court in *Cunningham* was grounded on the principle that "equality is equity." *Cunningham*, 265 U.S. at 13. When dealing with the fruits of a fraud perpetrated against a multitude of

people, equity requires that all victims receive equal treatment. *Id.* To do otherwise, will result in unlawful preferences. *Id.*

The Oklahoma Court of Civil Appeals, citing to the analysis in *Cunningham* and the case of *In re M & L Bus. Mach. Co.*, 59 F.3d 1078 (10th Cir. 1995), has also opined: “In a Ponzi scheme, or other scenario where creditors are almost exclusively defrauded parties, there is no distinguishing characteristic [of the fraudulently obtained assets] which promotes the interests of one [defrauded party] over the other.” *Adams*, 127 P.3d at 625. Without a showing that funds can be specifically traced, inequitable treatment of investors will clearly result. *Id.*

The *Cunningham* defendants challenged the trustee’s attempt to recover certain payments made to them by Ponzi – payments the trustee believed to be unlawful preferences under bankruptcy laws. The Supreme Court ruled that a successful challenge by the defendants carried an impossible burden of proof – to specifically identify the source of the payments they received as the money they had previously paid to Ponzi. Similarly, the *Adams* defendants were attempting to recover 100% of their funds contributed to a “Ponzi” scheme rather than the pro-rata distribution recommended by the receiver. The *Adams* court concluded that allowing later depositors of investment money to have priority over earlier investors, by receiving a 100% recovery, would be inequitable unless the monies are specifically traceable. *Adams* at ¶ 13.

The Department has shown that Defendants Pollard received more money from Schubert than they contributed, while others were not similarly treated. The burden shifts to Defendants Pollard to prove that all of the funds they received through the Schubert

scheme belonged to them in order to successfully retain the excess funds.³ *Id.* at 624, (citing *Cunningham*, 265 U.S. 1). Following the decisions in *Cunningham* and *Adams*, the funds of Defendants Pollard cannot be specifically identified within the funds commingled in the Schubert bank accounts. Therefore, Defendants Pollard have not, and cannot, meet their burden of proof. Defendants Pollard have not, and cannot, show that the funds they received as distributions from Schubert are specifically traceable to their contributions. Consequently, as decided by the trial judge below, it is not in equity and good conscience for Defendants Pollard to retain all of the funds they received from Schubert.

The Department acknowledges that courts in other jurisdictions have held that “an innocent investor in a Ponzi scheme is not unjustly enriched when he receives returns on his investment in good faith and while ignorant of the scheme, **so long as the returns do not exceed the amount of the original investment.**” *Chosnek*, 688 N.E.2d at 210.. The Department calculates the financial benefit or unjust enrichment to Defendants as the difference between the total monies they received through the “Ponzi” scheme less the total monies contributed to the scheme. It is this difference that the Department is asking Defendants Pollard to disgorge. It is this difference that, in equity or good conscience, Defendants Pollard should not be allowed to keep.

DEFENDANTS PROPOSED SETOFFS SHOULD NOT BE ALLOWED

In this matter, Defendants ask the Court to apply the amount of a Logan County judgment obtained by default against Schubert and a receivership claim assigned to them

³ Although not required for purposes of proving unjust enrichment, the Department can identify whose money Defendants received through the payments made to them by Marsha Schubert. ¶¶ 3 and Exhibit 1 of the Supplemental Affidavit of Dan Clarke, Exhibit A to *Plaintiff's Reply to Defendants' Response to Motion for Summary Judgment* at 571 to 577.

by a “short” investor as setoffs to the Department’s disgorgement claim against them. However, based on the facts of this case and established Oklahoma law, the trial court rightly decided the issue of setoff.

No mutuality of obligations exists.

Both parties agree that a setoff is defined as the equitable right which one party has against another to use his claim in full or partial satisfaction of what he owes to the other. *Studley v. Boylston Nat. Bank*, 229 U.S. 523, 528 (1913); *Caldwell v. Stevens*, 1917 OK 250, 167 P.610, 612; *S. Sur. Co. of New York v. Maney*, 1941 OK 388, 121 P.2d 295, 298. However, Defendants’ argument omits the necessary prerequisite for allowing a setoff, that is, mutual obligations between the parties to the same suit. *See Studley*, 229 U.S. at 528; *Caldwell*, 167 P. at 612; *S. Sur. Co. of New York*, 121 P. 2d at 298.

Oklahoma courts likewise impose a mutual obligations requirement in connection with a request for setoff. In *Sarkeys v. Marlow*, 1951 OK 195, 235 P.2d 676, 677, the Court stated: “[t]o warrant a set-off debts must be mutual and the principle of mutuality requires that the debts should be due to and from the same persons and in the same capacity.” (Syllabus by the Court, ¶ 3.) The requirement is also preserved in the current language of the Oklahoma Pleading Code, which provides that a setoff or counterclaim relates only to claims between opposing parties. 12 O.S. § 2013. The Department’s disgorgement claim and the Defendants’ judgment and claim assignment are not mutual obligations. Therefore, the lower court correctly decided that setoff is not appropriate.

Defendant Barry Pollard seeks to apply 100% of the Receivership claim of a “short” Schubert investor, L&S Pollard Farms LLC, which was assigned to the

Defendants two years after the appointment of the receiver.⁴ The Department owed no debt to L & S Pollard Farms, LLC. Again, there is no mutuality of obligations or parties to enable this Court to allow a setoff of the assigned claim of L&S Pollard Farms LLC, against the amount to be disgorged by Defendants Pollard.

The Logan County judgment is invalid as a setoff.

On March 4, 2005, Defendant Barry Pollard⁵ brought an action in Logan County against Marsha Schubert *dba* Schubert & Associates, AXA Advisors LLC, and AXA Equitable Life Insurance Company. Petition, Exhibit D to *Motion to Certify Questions for Immediate Interlocutory Appeal* at R. 955. Defendant Barry Pollard claimed that although he directly made payments to AXA and AXA Equitable for his investments, Schubert also made money for him through options and day trading through her company, Schubert and Associates. Petition, Exhibit D to *Motion to Certify Questions for Immediate Interlocutory Appeal* at R. 955-961. Defendant Barry Pollard's action violated the Logan County Court's *Temporary Restraining Order, Order Appointing Receiver, Order Freezing Assets and Order for Accounting* that stayed "all creditors and other persons seeking money, damages or other relief from the Defendants" from "doing any act or thing whatsoever to interfere with the orderly transfer of the Receivership assets to the Receiver or with the possession of or management by the Receiver of the Receivership assets" except upon leave of court. *Temporary Restraining Order, Exhibit 9 to Defendant Pollards' Motion for Summary Judgment* at R. 758. Despite Defendants' assertions, the Department did not receive notice of the petition, the default judgment

⁴ While Defendants have asked for a setoff of 100% of the assigned claim, "short" investors received only seventeen cents on the dollar in the first distribution made by the Receiver. The Receiver did not recognize the assignment for purposes of the initial distribution and made payment directly to L&S Pollard Farms, LLC.

⁵ Defendant Roxanne Pollard was not a party to the Logan County suit against Schubert.

hearing or the hearing on damages. Notice Mailings, Exhibit G and J to *Defendant Pollards' Motion to Certify Questions for Immediate Interlocutory Appeal* at R. 965 and R. 969.

Upon the Receiver's inability to sell a Schubert asset, the Department filed an indirect contempt application against Defendant Barry Pollard for filing a lien on that Receivership property (Lien). OSCN Court Minute attached as Exhibit B to *Plaintiff's Response to Defendant Pollards' Motion to Certify Questions for Immediate Interlocutory Appeal* at R. 1003-1004. The Department argued that such filing impeded the Receiver's ability to transfer the asset in contradiction of the Logan County order establishing the Receivership. As evidenced by his Court Minute, Judge Worthington ordered that the contempt citation be dismissed only upon the release of the Lien by Defendant Barry Pollard. OSCN Court Minute attached as Exhibit B to *Plaintiff's Response to Defendant Pollards' Motion to Certify Questions for Immediate Interlocutory Appeal* at R. 1003-1004.

The Receivership claims process was the proper channel for Defendants to assert any rights they may have as creditors in connection with the Schubert matter. Defendants chose not to file a proof of claim during the claims process in 2005. However, to facilitate resolution of this matter, the Department suggested to Judge Worthington during the indirect contempt hearing, that Defendants be permitted to file an out-of-time claim with the Receivership to consider amounts due them, if any. OSCN Court Minute attached as Exhibit B to *Plaintiff's Response to Defendant Pollards' Motion to Certify Questions for Immediate Interlocutory Appeal* at R. 1003-1004.

Allowance of any setoff would be inequitable.

The only remaining issue at the trial court level is the amount by which Defendants Pollard were unjustly enriched. In *SEC v. Haligiannis*, 470 F. Supp. 2d 373, (S.D.N.Y. 2007), the court held that a proper estimation of defendant's ill-gotten gains is the total difference between contributions and distributions after the fraud began. Therefore, only a reasonable approximation of profits causally connected to the violation is necessary to establish the amount of disgorgement. *Id.*; *SEC v. Levine*, 517 F. Supp. 2d 121, 128 (D.D.C. 2007). The burden then falls on the defendants to dispel uncertainty as to the proper calculation of disgorgement. *Id.*

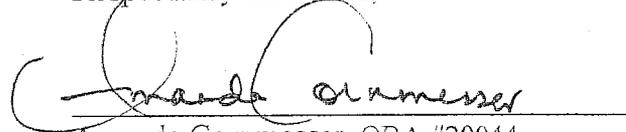
Defendants Pollard have been given credit by the Department for all monies paid directly to Schubert during the time of the "Ponzi" scheme. Any other monies purportedly paid by Defendants to Schubert prior to the "Ponzi" scheme have not been supported by evidence. If given credit for undocumented payments to Schubert, monies paid directly to AXA/Equitable, and any purported "profits," Defendants Pollard would receive preferential treatment over the "short" Schubert investors. *See SEC v. George*, 426 F.3d 786, 799 (6th Cir. 2006) (recovery of both "profits" and the original investment is deemed inequitable as a claimant's original investment would be repaid at the expense of equally innocent later investors). The Department has shown that the money Defendants Pollard received from the scheme came not from profits on their investments but from investments of others. ¶¶ 2 and 3 and Exhibit 1 of the Supplemental Affidavit of Dan Clarke, Exhibit A to *Plaintiff's Reply to Defendants' Response to Motion for Summary Judgment* at R. 571 to 572. The eighty-seven Short Investors victimized by Schubert's scheme will only recover a portion of their investment, not the 100% to which

the Defendants Pollard claim to be entitled. The mere coincidence that Schubert chose her family members, Defendants Pollard, as recipients of funds from other investors in order to perpetuate and delay discovery of her scheme, does not entitle them to preferential treatment. *Id.* at 798. Allowing any of the setoffs requested by Defendants Pollard would (a) negatively decrease recovery to the Short Investors of Schubert's fraudulent scheme, and (b) provide preferential treatment to Defendants Pollard over the other Long Investors, thereby causing an inequitable result.

CONCLUSION

The Department requests this Court to affirm the lower court's rulings and remand the case back for the determination of the disgorgement amount owed by Defendants Pollard.

Respectfully submitted,

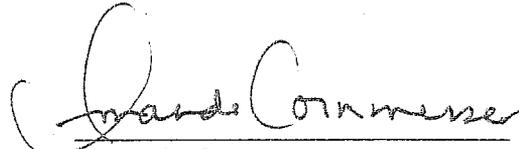
A handwritten signature in cursive script, reading "Amanda Cornmesser", is written over a horizontal line.

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CERTIFICATE OF MAILING TO PETITIONERS

I hereby certify that a true and correct copy of the above *Response of the Oklahoma Department of Securities to Petitioners' Brief in Chief* was mailed this 19th day of June, 2008, by depositing it in the U.S. Mail, postage prepaid, to:

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Amanda Commesser