

**UNITED STATES DISTRICT COURT  
MIDDLE DISTRICT OF FLORIDA  
TAMPA DIVISION**

SECURITIES AND EXCHANGE  
COMMISSION,

Plaintiff,

v.

Case No. 8:09-cv-0087-T-26TBM

ARTHUR NADEL;  
SCOOP CAPITAL, LLC;  
SCOOP MANAGEMENT, INC.

Defendants,

SCOOP REAL ESTATE, L.P.;  
VALHALLA INVESTMENT PARTNERS, L.P.;  
VALHALLA MANAGEMENT, INC.;  
VICTORY IRA FUND, LTD.;  
VICTORY FUND, LTD.;  
VIKING IRA FUND, LLC;  
VIKING FUND, LLC; AND  
VIKING MANAGEMENT, LLC,

Relief Defendants.

---

**THE RECEIVER'S INTERIM REPORT ON  
QUEST ENERGY MANAGEMENT GROUP, INC.**

Burton W. Wiand, the Court-appointed Receiver for Quest Energy Management Group, Inc. (“**Quest**” or the “**Company**”), hereby files this Interim Report On Quest (the “**Report**”) to inform the Court, investors, and others interested in this Receivership of activities from May 24, 2013, the date the Receiver was appointed as Receiver of Quest, through the date of the filing of this Report as well as the proposed course of action.

## **BACKGROUND**

On January 21, 2009, the Securities and Exchange Commission (“**SEC**”) instituted this enforcement action following the collapse of a massive Ponzi scheme (the “**scheme**”) perpetrated by Arthur Nadel (“**Nadel**”) through hedge funds (the “**Hedge Funds**”) from 1999 until January 2009. As part of this scheme, Nadel paid himself and his purported business partners, Neil and Christopher Moody (“the **Moodys**”), more than \$90 million in bogus management and performance fees which were based on fabricated asset values and performance data. Due to that conduct, Nadel was charged and pled guilty to securities, mail, and wire fraud. Nadel was convicted of all charges and died in prison while serving a 14-year sentence.

During the course of the 10-year scheme, Nadel and the Moodys used scheme proceeds – money stolen from the Hedge Funds’ investors – to found or otherwise fund numerous businesses. Since the inception of this Receivership and in accordance with his mandate to marshal assets for the benefit of defrauded investors, the Receiver has successfully sought expansion of the Receivership to include those businesses.<sup>1</sup> Quest is one such entity that was funded in large part with scheme proceeds.

---

<sup>1</sup> Those business include: Venice Jet Center, LLC; Tradewind, LLC; Laurel Mountain Preserve, LLC; Laurel Preserve, LLC; Laurel Mountain Preserve Homeowners Association, Inc.; Marguerite J. Nadel Revocable Trust UAD 8/2/07; Guy-Nadel Foundation, Inc.; Lime Avenue Enterprises, LLC; A Victorian Garden Florist, LLC; Viking Oil & Gas, LLC; Home Front Homes, LLC; Traders Investment Club; Summer Place Development Corporation; Respiro, Inc.; and Quest Energy Management Group, Inc. For more information on the Receivership as a whole, please refer to the Receiver’s regularly filed Interim Reports.

Quest is an oil and gas exploration and production company based in Texas. Paul Downey was its Chief Executive Office, and his son Jeff Downey was its Chief Operating Officer (collectively the “**Downeys**”). The Moodys, through Receivership Entities Viking Oil & Gas, LLC, and Valhalla Investment Partners, L.P., used approximately \$5.1 million of scheme proceeds to fund Quest.<sup>2</sup> Before moving to include Quest in this Receivership, the Receiver attempted to reach a resolution with Quest relating to the large amount of scheme proceeds used to fund the Company. In February 2009, the Receiver began communications with the Downeys for recovery relating to the scheme proceeds provided to Quest. After considerable time and effort, the Receiver reached a conditional agreement to resolve his claims against Quest dependant upon receipt of \$2.3 million from Quest.<sup>3</sup> Quest failed to make this payment and ignored the Receiver’s repeated demands for payment. In February 2013, Quest informed the Receiver it was having cash flow problems. Because of Quest’s failings and to try to preserve the value of Quest for the benefit of the Receivership estate and, ultimately, for defrauded investors in Nadel’s scheme, on March 21, 2013, the Receiver moved to expand the Receivership to include Quest (Doc. 993). The Court granted this motion on May 24, 2013 (Doc. 1024).<sup>4</sup>

---

<sup>2</sup> In part, Quest’s obligation to the receivership entities was secured by a pledge of 100% of Quest’s stock.

<sup>3</sup> Because of the Receiver’s lack of faith in the Downeys, he structured the proposed resolution so that it would not become an agreement until Quest delivered \$2.3 million to him. That never occurred.

<sup>4</sup> The Downeys, purporting to act on behalf of Quest, have appealed the Court’s May 24, 2013, order to the United States Court of Appeals for the Eleventh Circuit (Doc. 1027). On July 19, 2013, the Circuit Court informed the parties to the appeal that the court may lack  
(footnote cont’d)

## **I. Overview of Findings To Date**

The Receiver has formed some preliminary conclusions based on his review of a portion of the records obtained from Quest. While these conclusions are not final, and may change as the review becomes more complete, the Receiver believes they should be shared with the Court, the investors, and other potentially interested parties. As a result of his actions and investigations, the Receiver has discovered that Quest (1) was severely mismanaged, in default of millions of dollars of outstanding debt, and insolvent; (2) had serious regulatory issues; (3) was sustained exclusively by money from new investors who were misled about the company's financial state or potential; and (4) was a defendant in several lawsuits and was facing other potential litigation. These findings are discussed in more detail below.

### **A. Brief Overview of Receiver's Efforts to Date**

Since his appointment on May 24, 2013, the Receiver has taken a number of steps to fulfill his mandates under the Order appointing him as Receiver for Quest. The Receiver and his attorneys promptly secured bank accounts and began to review Quest's business records. The Receiver traveled to Texas to secure Quest's office, interview personnel, and examine records and assets. The Receiver also retained the services of Wheeler, Fairman & Kelley, CPAs ("**Wheeler**"), experienced forensic accountants in Texas familiar with the oil and gas industry, to examine Quest's financial records. The Receiver also has been assisted by his

---

jurisdiction over the appeal and requested briefing from them on this issue by August 2, 2013. On August 2, 2013, the Receiver responded to the Circuit Court's request and also moved to dismiss the appeal on other jurisdictional grounds. No decision has been rendered on these matters.

lawyers in efforts to gather information and compile a complete understanding of Quest's affairs.

**B. Paul Downey's Refusal to Testify**

On June 5, 2013, the Receiver's attorney deposed Paul Downey in an effort to gather important information about Quest's affairs under oath. However, Mr. Downey asserted his Fifth Amendment privilege against self-incrimination and refused to answer any questions without first receiving immunity from prosecution.

**C. Quest Was Insolvent**

Upon review, the Receiver discovered that Quest's financial records were in disarray. Despite this challenge, Wheeler has been able to determine that Quest was insolvent almost since its inception in 2006 and expenses were outpacing revenue by more than two to one. A copy of Wheeler's Preliminary Report is attached hereto as **Exhibit A**. At the time of the Receiver's appointment, the Company owed investors and others millions of dollars but had virtually no revenue with which to repay this debt. One way the Downeys had raised money on behalf of Quest from investors was through promises to repay the principal amount plus periodic interest. The Company had ceased making interest payments to those investors more than one year before the Receiver's appointment. Quest's records reflect that approximately \$19,124,326 was raised from investors between 2006 and May 2013. Due to the convoluted and disorganized nature in which the Company maintained its financial records, total liabilities have not yet been quantified although it is clear they are very significant. Further, Quest's minimal income was insufficient even to satisfy its operating expenses, let alone its debt obligations. As a result, there was no potential for the Downeys

to satisfy Quest's obligations other than by using money received from new investors to pay existing investors. The Company's operational failure and dire financial condition was not disclosed to the solicited investors.

#### **D. Quest's Operations and Affairs Were in Shambles**

Not only did the Downeys place Quest in dire financial conditions, but they also failed to properly manage Quest's oil and gas operations. The Receiver's investigation has uncovered the following:

- Due to the Downeys' failure to comply with regulatory requirements prior to the Receiver's appointment, the renewal of Quest's Operator's License had been denied by the Texas Railroad Commission ("RRC");<sup>5</sup>
- Additional prior regulatory violations by the Downeys had resulted in a significant fine of \$75,625;
- Quest's oil and gas wells were in disrepair and the Downeys failed to make even nominal efforts to maintain them as viable producing assets;
- As discussed in more detail below, the Downeys failed to disclose to existing and prospective investors that Quest was insolvent, not compliant with its regulatory obligations, and had few producing assets;
- Although the Downeys raised more than \$19 million from investors, it appears no more than \$1.5 million was ever used in connection with the purchase of oil and gas equipment;
- While the Receiver's motion to expand the Receivership to include Quest was pending, the Downeys solicited and received a \$350,000 investment from an investor without disclosing to the investor the pending motion, that the Company was insolvent, or that the renewal of the Company's operational license had been denied. The Downeys then used a portion of those funds to

---

<sup>5</sup> The RRC is the primary regulator of the oil and gas industry in Texas. The RRC has extensive recording and compliance requirements and also has an enforcement division to enforce those requirements.

hire an attorney for themselves and failed to apply those funds to resolve Quest's critical outstanding regulatory issues;

- The Downeys had failed for some time to pay gas royalties owed by Quest on its gas sales. At the time of the Receiver's appointment over Quest, Quest owed approximately \$42,000 in gas royalties, and those payments had not been made since May 2012 on one property and October 2012 on another property;
- The Downeys never made a material investment of their own funds into the Company. Yet, they used Company funds to pay personal expenses of approximately **\$918,506** for the Downey family which included car payments for a BMW, Chevy Tahoe, Chevy Yukon, and Lexus. The Company also paid Jeff Downey's rent and expenses associated with another residential property in a subdivision near Houston as well as substantial rents and personal expenses for a condominium Paul Downey was renting in Naples, Florida;
- In addition to the personal expenses noted above, at the time of the Receiver's appointment, the Downeys were receiving annual salaries in the combined amount of \$352,000. Assuming they received this amount since the beginning of Quest's operation, they would have received approximately \$2,464,000 in addition to the personal expenses of \$918,506 noted above for a total of approximately **\$3,382,506**; and
- In 2010, the Downey family caused Quest to issue a series of notes payable to themselves in the amount of \$10,000,000 in exchange for shares of family member stock. Quest was insolvent at that time. The transaction was later reversed but before reversal Jamie Downey and Sandy Downey were paid a total of \$117,000 for no justifiable reason.

As is evident from the above, without the appointment of the Receiver, the collapse of Quest was inevitable.

#### **E. Quest Faced Significant Regulatory Issues**

In 2012 (well before the Receiver's appointment), Quest was notified that various wells were not in compliance with certain regulatory requirements and that because of these compliance issues the RRC would not renew Quest's Operator's License. Without its Operator's License, Quest would have to cease operations. Quest was given ninety days,

until April 2, 2013, to cure its deficiencies. The Downeys failed to resolve significant issues and further failed to request a hearing on these issues as permitted by law. As a result, on June 13, 2013, the RRC issued an order denying Quest's renewal application. A copy of the order denying the application is attached as **Exhibit B**. Upon learning of the situation, the Receiver took immediate steps to resolve these issues. The Receiver had extensive dialogue with the RRC's enforcement counsel and secured the RRC's consent to a Motion for Rehearing of the renewal application. The Receiver retained local counsel in Austin, Texas, to assist in accomplishing the tasks necessary to bring the various wells into compliance. The Receiver's professionals and remaining Quest employees expended extensive efforts to ensure this compliance; two of the four violations have been resolved and the remaining two are close to being resolved.<sup>6</sup>

This was not the first time the Downeys had failed to satisfy their regulatory obligations. In September 2011, the RRC informed the Downeys it was pursuing a penalty against Quest for violation of rules pertaining to safety or the prevention and control of pollution. A copy of this letter is attached as **Exhibit C**. To resolve this matter, in October 2011, the Downeys agreed to a Consent Order which required them to pay a \$75,625 fine which they agreed to pay in monthly installments over an 18-month period. Payments were

---

<sup>6</sup> To satisfy the RRC's demands, the Receiver was required to make considerable corrections to records which had been improperly filed with the RRC. The Receiver also had to complete substantial work on a number of wells which included plugging certain wells and resolving some environmental issues.

not timely made and when the Receiver was appointed, the final payment on this settlement was overdue.<sup>7</sup>

**F. Misrepresentations Made to Investors**

The Receiver's preliminary investigation indicates that from 2006 through May 2013, approximately \$19 million was raised by the Downeys on behalf of Quest from approximately 115 investors. Included in this sum is approximately \$5.1 million owed to the Receivership as a result of the scheme proceeds transferred to Quest by the Moodys. Based on the documents the Receiver has reviewed to date, it appears that numerous misrepresentations, or material omissions, were made to investors. The Downeys failed to disclose to investors that Quest was insolvent and did not have the financial means needed to maintain the wells, produce the amount of oil and gas represented to investors, and resolve its regulatory issues. In Status Update Memoranda, Paul Downey represented to investors that a Fortune 100 Company was interested in purchasing Quest's assets which purportedly would have allowed Quest to repurchase all notes at full face value and pay interest. A copy of the Status Update Memoranda dated September 24, 2012 and October 16, 2012 are attached as composite **Exhibit D**. This never came to pass and the Receiver has been unable to find any evidence of any Fortune 100 company interested in purchasing Quest's assets, and, frankly, has found no evidence supporting any reason why such a company would have any genuine

---

<sup>7</sup> Soon after the filing of the motion to expand the Receivership to include Quest, the Texas State Securities Board ("TSSB") contacted the Receiver because it had initiated an investigation of Quest following complaints by several Quest investors. The TSSB has requested information and assistance in its investigation of Quest and the Downeys' efforts to raise money on behalf of the Company. The Receiver is working cooperatively with the TSSB.

interest in Quest. Similar representations regarding other saviors continued to be made to investors until the Receiver's appointment. It is further believed that the Downeys, while knowing that Quest did not have the ability to pay its operating expenses, let alone outstanding debt, made repeated misrepresentations to investors that Quest would resume paying interest on the notes or, as noted above, would secure a purchaser who would allow Quest to pay the notes in full.

Most recently, the Downeys secured an investment from an individual investor after the Receiver had filed his motion to expand the Receivership to include Quest. The Downeys entered into an assignment of a lease agreement with this investor. The assignment purported to assign 91% of Quest's interest in an oil property lease agreement in exchange for the payment of \$350,000 to Quest. The Downeys were fully aware of the Receiver's pending motion to expand the Receivership to include Quest yet the Receiver's investigation has revealed they failed to disclose this information to the investor. Further, the Downeys did not disclose the insolvency of Quest and misrepresented to the investor how the funds obtained would be used by the Company. Without informing the investor, the Downeys then used a portion of the funds received from the investor to retain an attorney for themselves and to pay themselves wages while only 10% of these funds were used for well production. The assignment was not recorded until after the Receiver was appointed as Receiver of Quest. Further, the lessors have asserted that Quest's assignment to the investor invalidated the lease because the lease agreement contains a provision prohibiting any such assignment. The Receiver will vigorously contest the assignment and the alleged invalidation of the lease.

### **G. Pending and Prospective Litigation**

At the time of the Receiver's appointment, Quest had three lawsuits seeking large amounts in damages pending against it in Texas State Courts. *Integrity Directional Services, LLC v. Quest*, Case No. 2013-028 (Tx. D. Ct. 259<sup>th</sup> Jud'1 Dist., Shackelford County, TX) (seeking damages of \$899,583.50 for goods and services which were provided to Quest for which payment was not received); *Ploegsma Sulpher Co. LLC v. Quest*, Case No. 2013-17235 (Tx. D. Ct. 189<sup>th</sup> Jud'1 Dist., Harris County, TX) (brought by an investor seeking damages of more than \$1.25 million for payment of a note); *Wallace d/b/a Graham Mud Co. and Rocking R Drilling Co., Inc. v. Quest*, Case No. 2013-050 (Tx. D. Ct. 259<sup>th</sup> Jud'1 Dist., Shackelford County, TX) (seeking to foreclose on liens for unpaid goods or services in the combined amount of \$398,722.93).<sup>8</sup> The Receiver has filed Notices of Receivership and Injunction Barring Proceedings Against Quest in each action. Accordingly, these actions have been stayed as to Quest.

Further, the Receiver has reviewed documents indicating that several investors were threatening suit against Quest for the recovery of their investments. Absent the appointment of the Receiver, numerous additional claims were inevitable.

### **II. Current Operations and Assets**

As noted above, upon the Receiver's appointment, he promptly secured Quest's bank accounts and its office located at 64 South Jacobs, Albany, Texas (the "Office"). At that

---

<sup>8</sup> These litigation matters are in addition to the Receiver's claim for approximately \$5.1 million against Quest.

time, Quest had approximately \$58,570.67 in its bank accounts.<sup>9</sup> The Receiver retained experienced forensic information technology experts with the firm E-Hounds, Inc. to assist in securing and analyzing the electronic data on computers located in the Office. E-Hounds personnel have secured the data and have begun their forensic analysis.

After interviewing personnel, the Receiver determined to reduce Quest's staff. The Downeys were terminated as well as an individual involved in "investor relations" who was instrumental in disseminating information for the Downeys. Two other employees resigned. The Company retained a supervisor and two field employees. The Receiver has obtained a significant volume of documents from the Office and is in the process of reviewing these documents. The Receiver is evaluating the Company's assets and determining the appropriate course of action to take with respect to these assets. Quest's assets include (1) leases held on fields containing oil and gas wells and related equipment; (2) various vehicles; (3) residential property which is currently being used as the Office; and (4) other miscellaneous assets including office furniture, computers and the like.

#### **A. Oil and Gas Wells**

The Receiver has determined that Quest maintains leases on three fields which in turn contain 88 gas and oil wells. Of these 88 wells, only five wells are currently producing. The Receiver has begun evaluating the potential well output relative to the cost of making the wells productive. Since taking control of Quest, the Receiver has implemented some repair and maintenance activities designed to increase production and revenues. These efforts are

---

<sup>9</sup> Quest's payables at that time substantially exceeded this amount.

showing signs of success. From the Receiver's review of the wells, it was evident that simple maintenance and basic well management had been ignored for some time. The Receiver has already more than tripled production by reinvesting a nominal amount of money in these wells. By taking relatively simple measures, the Receiver increased production from approximately 7 barrels per day to over 30 barrels per day.<sup>10</sup> Indeed, in the last day Quest produced 45 barrels of oil.

### **B. Vehicles**

The Receiver acquired possession and control of 16 vehicles titled in Quest's name or otherwise paid for by Quest, which primarily include trucks and trailers used in connection with business operations. One of the vehicles, however, was a 2009 BMW 535i ("BMW") which was being used by Paul Downey. On August 12, 2013 the Receiver filed a motion to approve the sale of the BMW for \$17,000 (Doc. 1049). The Court approved this motion on August 13, 2013 (Doc. 1050). After payment of the outstanding loan on the vehicle, the Receivership received the net amount of \$3,566.12 from this sale.

### **C. The Office Property**

The Receiver has possession and control of an Office, which is a small free-standing office building. The Office has one known encumbrance: a loan with First National Bank with an outstanding balance as of July 2013 in the amount of \$46,522.48. Parties interested in purchasing the Office should contact:

---

<sup>10</sup> The Receiver also sold approximately 160 barrels of stored oil for the gross amount of \$16,197.14 which prior management had made no attempt to sell for over a year.

David Cleveland  
Clear Fork Realty  
332 South Second  
Albany, Texas 76430  
(325) 762-3614 (office)  
[clrfork@camalott.com](mailto:clrfork@camalott.com)

**D. Miscellaneous Items**

The Receiver has also recovered a myriad of other items that he may be able to sell, including office furniture, computers, and miscellaneous supplies. The Receiver will make reasonable efforts to maximize the amount he is able to recover from the possible sale of these items.

**III. Proposed Course of Action**

As a result of the Receiver's preliminary investigation, it appears that the oil well leases held by the Company have potential value and may be able to be sold for the benefit of investors and other creditors. The Receiver will continue to evaluate the wells and their potential for production relative to the expense required to maintain the wells and make them productive. This activity is intended to generate cash flow while evaluation and liquidation activities are attempted. The Receiver will continue to work with the RRC to resolve all regulatory issues and will rework certain wells as required by the RRC and as appropriate. The Receiver will evaluate and market leases in an effort to generate as much value as reasonably possible. While marketing these assets, the Receiver will continue to operate the business in an effort to enhance its value. The Receiver will continue to review financial documents and other documents from the Company to further his investigation. The Receiver has and will continue to maintain a separate accounting of revenues and expenses

for Quest. He will also continue to consider all of the information he has gathered to date, additional information he gathers, and the Company's or its assets' prospects and value to determine how to address claims held by Quest investors and other creditors. At this time, the Receiver contemplates that he will conduct a separate claims process to deal with the claims of investors and other creditors of Quest if the sale of Quest's assets warrants such a process. The Receiver, however, currently believes that the assets and potential value of Quest is significantly less than the outstanding balance of investors' investment amount in Quest.

### **CONCLUSION**

Creditors and investors in the Receivership Entities are encouraged to periodically check the informational website ([www.nadelreceivership.com](http://www.nadelreceivership.com)) for current information concerning this Receivership. The Receiver and his counsel have received an enormous amount of emails and telephone inquiries and have had to expend significant resources to address them. To minimize those expenses, creditors and investors are strongly encouraged to consult the Receiver's website before contacting the Receiver or his counsel. However, if you are an investor or creditor of Quest and have not yet provided your email or other contact information to the Receiver, please contact Jeffrey Rizzo by email to [jrizzo@wiandlaw.com](mailto:jrizzo@wiandlaw.com) or telephone (813) 347-5100. The Receiver also encourages anyone who may have information that may be helpful in securing further assets for the Receivership estate or identifying other potential parties who may have liability to either the Receivership estate or investors to also contact Mr. Rizzo with that information.

Dated this 26th day of August, 2013.

Respectfully submitted,

**s/Burton W. Wiand**

Burton W. Wiand, Receiver

**CERTIFICATE OF SERVICE**

**I HEREBY CERTIFY** that on August 26, 2013, I electronically filed the foregoing with the Clerk of the Court by using the CM/ECF system.

**s/Gianluca Morello**

Gianluca Morello, FBN 034997

[gmorello@wiandlaw.com](mailto:gmorello@wiandlaw.com)

Maya M. Lockwood, FBN 0175481

[mlockwood@wiandlaw.com](mailto:mlockwood@wiandlaw.com)

WIAND GUERRA KING P.L.

5505 West Gray Street

Tampa, FL 33609

T: (813) 347-5100

F: (813) 347-5198

*Attorneys for the Receiver, Burton W. Wiand*