EXHIBIT C

ARBITRATION TRIBUNALS OF THE AMERICAN ARBITRATION ASSOCIATION

BURTON W. WIAND, as Receiver for VALHALLA INVESTMENT PARTNERS, L.P.; VIKING FUND, LLC; VIKING IRA FUND, LLC; VICTORY FUND, LTD.; VICTORY IRA FUND, LTD.; and SCOOP REAL ESTATE L.P., *Petitioner*, v. WORLD OPPORTUNITY FUND, L.P., *Respondent.*	CASE NO. 51-512-Y-892-12

REPLY IN FURTHER SUPPORT OF MOTION TO ENFORCE JUDGMENT CREDIT

COMES NOW World Opportunity Fund, L.P. ("WOF"), by and through its undersigned attorneys, and files this reply in further support of its motion to enforce judgment credits resulting from the Receiver's settlement of claims against H&K and GSEC, among others.

The Receiver's response (1) mistakenly argues against the strawman of contribution, which was not asserted by WOF, and (2) eschews law in a naked appeal for what it terms "Justice." The Receiver, however, does not dispute that:

- WOF is in the class of persons contemplated as having rights under the bar orders;
- WOF's claims against H&K or GSEC are precluded by the bar orders;
- WOF otherwise received no benefit for the claims it lost under the bar orders;
- The Receiver chose to settle his claims for less than the amounts he believes H&K, GSEC, and others owe for their participation in the "scheme;" and
- Had the Receiver obtained full relief from H&K and GSEC for investor losses, he would not have claims against WOF for fraudulent transfer.

It is clear from his opposition that the Receiver was content to offer bar orders to settling defendants so long as no one was eligible to claim relief under their judgment credit provisions. In his response, the Receiver does not contest that WOF is an "individual[] or entit[y] who invested money in a Receivership Entity, as well as [a person or entity] who may have liability to the Receiver, the Receivership Entities, or such investors arising or resulting from the operations of any of the Receivership Entities or from the fraudulent scheme underlying the SEC Receivership Action." H&K Bar Order at 3. Nor does the Receiver dispute that WOF's claims against H&K and GSEC are barred by the orders entered in federal court. The Receiver simply believes that WOF lost its right to sue without compensation.[1] Federal courts, however, are barred from awarding bar orders that fail to compensate affected parties. *AAL High Yield Bond Fund v. Deloitte & Touche LLP*, 361 F.3d 1305, 1312 (11th Cir. 2004) (vacating an "exceedingly broad" bar order because the trial court provided "no rationale or authority for barring claims without a settlement credit or 'set off'"). The Panel should not interpret the bar orders in a way that would render them illegal under federal law.

The Receiver suggests—in contravention of every case describing bar orders—that WOF's claims may be cancelled without compensation because entitlement to a judgment credit is limited to "such set-offs or judgment credits as permitted by law, if any." Opp. at 7. Federal

[1] The Receiver begins his opposition by re-hashing his jurisdictional objection. WOF suggests that the briefing on jurisdiction adequately addresses this issue. In brief, however, the Panel has jurisdiction over "all controversies." The arbitration clause does not purport to permit some defenses to arbitrable claims but not others—the Panel is obligated to decide the *controversies* between the parties, including the judgment credit at issue here. As noted in WOF's objection, the limitation in the arbitration clause cited in bold by the Receiver—which limits construction of the agreement to its terms—is simply a merger clause, or a prohibition on the Panel accepting parol evidence to understand what was meant by the agreement. Notably, the only party seeking to introduce parol evidence to alter or amend the terms of the withdrawal and distribution provisions of the Valhalla limited partnership agreement is the Receiver, who argues that those provisions should be disregarded because of facts and circumstances (namely the alleged fraudulent scheme) not reflected in the written agreement between WOF and Valhalla.

cases are uniform in requiring bar orders that take something to provide compensation to parties. *In re Healthsouth Corp. Sec. Litig.*, 572 F.3d 854, 861 (11th Cir. 2009) (acknowledging that "a bar order deprives a non-settling defendant of potentially valuable rights, and therefore, the non-settling defendant should be compensated. . . . [T]he instant Bar Order includes, as part of its compensation to [defendant], a judgment credit, which would credit [defendant] against any future judgment that the underling plaintiffs might obtain against him."). Because these cases arose in the context of Mr. Nadel's alleged securities fraud and is supervised by federal courts under claims based on the Securities Exchange Act of 1934, the bar orders are governed by federal common law, which provides sufficient grounds to award a judgment credit under the cases cited in its motion. *See, e.g., In re Sunrise Sec. Litig.*, 698 F. Supp. 1256, 1257 (E.D. Penn. 1988) (discussing rationale for "a uniform national settlement bar rule").[2]

In his opposition, the Receiver asks three questions, answered in reply here: (1) Does WOF have viable claims against the settling defendants, H&K and GSEC? (2) What is the relationship between an adverse decision in arbitration and WOF's lost claims against H&K and GSEC? And (3) Assuming fairness is an appropriate inquiry for the Panel, is a judgment credit fair? These questions are answered in turn.

[2] The Receiver's request for a *pro rata* allocation of judgment credit is also a red herring. Opp. at 16 n.6. Unless the Receiver is volunteering to pay each investor in Valhalla the proportionate share of the H&K and GSEC settlements, the Receiver is not arguing in good faith. Since the Receiver says that WOF is (thus far) the only investor to seek relief under the judgment credit provisions of the bar orders, the Panel need not determine how credits might be allocated should other investors determine they are entitled to credit as argued in this motion. *See In re Jiffy Lube Sec. Litig.*, 927 F.2d 155, 160 n.3 (4th Cir. 1991) (describing the three allocation methods). As noted in the original motion, the Receiver maintains approximately $32 million in claims for "false profits" cases, meaning that on any method of allocating judgment credits, the clawback cases should be deemed satisfied by the settlements and bar orders.

A. <u>WOF Lost Valuable Claims Against H&K and GSEC.</u>

The Receiver argues that WOF has no claim for indemnity against H&K and GSEC because (1) it has no damages and (2) there is something special about the *Receiver's* claims. Neither of these objections is valid.

The Receiver is correct that, so long as no judgment is entered against WOF, WOF has not been compensably damaged by H&K and GSEC. WOF's claims for indemnity (and its direct claims for damages) ripen only if this Panel enters a judgment.[3] As is true in most jurisdictions, a "cause of action for indemnification does not accrue until the litigation against the third party plaintiff has ended." *Mims Crane Serv., Inc. v. Insley Mfg. Corp.*, 226 So. 2d 836, 840 (Fla. 2d DCA 1969). That is, were the Receiver to prevail on the merits of the arbitration—a proposition that remains substantially in dispute—both WOF's direct and indemnity claims against actual misfeasors would ripen into justiciable claims.[4]

WOF has valid, though dormant, claims against H&K and GSEC. The merits of Valhalla's investors' claims against H&K and GSEC are not disputed by the Receiver, especially since he received over $35 million based on the allegation that those entities culpably participated in a fraudulent scheme. As such, once the actions by H&K and GSEC ripen into harm to WOF based losses resulting from WOF's investments in Valhalla, WOF would have a

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[3] WOF moved for recognition of the judgment credit without prejudice to its defenses on the merits. The Receiver has not argued that assuming the merits of his claims and deciding the applicability of the judgment credit is procedurally impermissible for that reason alone.

[4] In connection with its construction of the bar orders, the Receiver argues that WOF cannot meet the elements of the Florida Uniform Contribution Among Tortfeasors Act because WOF is not a joint tortfeasor with H&K and GSEC. But WOF never argued that it was a joint tortfeasor, so the Receiver's argument is a strawman. WOF's right to a judgment credit arises from its loss of direct claims and indemnity claims against H&K and GSEC, not because WOF committed the same wrong as those entities.

valid, direct claim against H&K and GSEC. The loss of its direct claims alone is sufficient to bring WOF within the ambit of the federal court's judgment credit.

Regarding the indemnity claim, the Receiver suggests that there is something about the special nature of his claims for fraudulent transfer that interferes with WOF's claims against H&K and GSEC. Opp. at 9 (WOF's "entire argument ignores the nature of the Receiver's claims").[5] Whether WOF can seek indemnity from H&K and GSEC does not depend at all on the fact that WOF's injuries result from the Receiver's claims in this arbitration. WOF's indemnity claim is based on losses it might incur based on H&K and GSEC's participation in a scheme by the hedge funds to defraud investors of money. The Receiver cannot deny that WOF has been sued for money *because of* the actions of the hedge funds, H&K, and GSEC—that is, WOF is non-negligent and being held vicariously responsible for the fraud committed by Mr. Nadel and the settling defendants.

No case cited by the Receiver supports denial of this motion. The Receiver cites a Michigan case as dispositive of the indemnity analysis. There, a federal court held that the ringleaders of a fraudulent scheme would not be entitled to common law indemnity as against an innocent recipient of funds. *Buchwald Capital Advisors, LLC v. Papas (In re Greektown Holdings, LLC)*, 475 B.R. 563, 576 (E.D. Mich. July 13, 2012). Applying that holding here, the court would have denied *Mr. Nadel* indemnity for settlements obtained by the Receiver.

[5] While WOF does not agree with the tort-vs-fraudulent-transfer distinction drawn by the Receiver, the Receiver ignores the fact that he asserted tort claims in his arbitration demand, since a claim for unjust enrichment is a classic, common law tort. *Duncan v. Kasim*, 810 So. 2d 968, 971 (Fla. 5th DCA 2002) ("We think the unjust enrichment claim is similar to the conversion claim.") The Receiver functionally concedes that the bar order operates to deny claims for torts in exchange for a judgment credit. Thus, to the extent any award is based on the tort of unjust enrichment, the Receiver has presented no non-procedural opposition to the application of a judgment credit for such claims. *See* Opp. at 13 (conceding that "tort claims for damages . . . might implicate contribution, indemnification, or vicarious liability concepts").

Greentown presents the inverse of the question in this case, and has no application to claims for indemnity *against* Mr. Nadel and the other participants in his scheme.[6]

Because WOF has good claims against H&K and GSEC that it lost under the bar orders approved by the federal court, it should receive a judgment credit in this action.

B. WOF's Injury Would Ripen if an Award Were Issued by the Panel.

The Receiver's position seems to insinuate that WOF has nothing to complain about in being required to pay the Receiver a recovery in this action. After all, the Receiver argues, WOF is simply holding proceeds of a fraudulent scheme. WOF, the Receiver argues, is not harmed by returning those proceeds for distribution to investors who lost money in Mr. Nadel's scheme. All of which ignore the fact that WOF will be distinctly harmed by having to write a check for potentially millions of dollars, if the Receiver can prevail on his claims.

The Receiver blithely argues that WOF "is not entitled to . . . compensation for the time value of money." Opp. at 15 n.5. This argument gets into the thicket of the merits of the Receiver's claims. Under fraudulent transfer laws, a person with a valid claim under the

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[6] The Receiver has never argued that WOF knew that its investments were anything other than 100% legitimate. The Receiver begins his opposition with a retelling of the "red flags" he described in his statement of claim. *See* WOF's Response to Statement of Claim at 9–10. While the Receiver focuses on the fact that Valhalla was unaudited, an audit was not required. SEC Staff Report, Implications of the Growth of Hedge Funds, at 57 ("Unlike registered investment companies, there is no statutory or regulatory requirement that a hedge fund have its financial statements audited. Whether a hedge fund undergoes an annual audit of its financial statements is a contractual matter between the hedge fund and its investors."), attached hereto as Exhibit A. Likewise, high returns are the hallmarks of successful hedge funds, not indicators of fraud. In fact, significant returns are historically legitimate: 122.92% three-year return for Paulson Credit Opportunities Fund and 65.63% three-year return for Balestra Capital Partners from 2007 through 2010. *See* Wall Street Journal Online, attached hereto as Exhibit B. A chart from June 2007 shows 50 hedge funds with three and a half year returns ranging from 30% to 93%. *See* Wall Street Journal Online, attached hereto as Exhibit C. Finally, the Receiver continues to suggest that WOF should have conducted a search of every state bar to see if Mr. Nadel was ever a licensed attorney and whether he was disbarred. Counsel for WOF searched the on-line records of the state bar of New York, and those records also do not disclose information about Mr. Nadel. *See* NY Bar Records, attached hereto as Exhibit D.

fraudulent-transfer statute is entitled to recover funds unless, among other defenses, the recipient "took [the funds] in good faith and for a reasonably equivalent value." Fla. Stat. § 726.109(1). The Receiver is attempting to argue that WOF's liability under FUFTA is an all-or-nothing proposition because the Receiver does not believe that WOF is entitled to compensation for Valhalla's use of the funds for three to five years.[7]

WOF disagrees with the Receiver's argument on the merits of the FUFTA claim.[8] More importantly, however, for this motion, the time-value of money would figure as a prominent basis for recovery as against H&K and GSEC. That is, the harm that WOF will have suffered is the loss of the use of its funds for a multi-year period.[9] If the Receiver were to recover, WOF would assert its losses in the arbitration as the damages against H&K and GSEC.

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[7] It is unclear from the Receiver's motion whether he intends to amend his statement of claim from seeking an award that can be recognized as a money judgment against WOF or whether he simply seeks an accounting of the funds transferred by Valhalla so that he can pursue others for the ultimate return of *res* which has largely been distributed to investors and placed into other investments. *See* Opp. at 12 (characterizing his claims as "*in rem* claims for the return of a specific *res* that is in investor-defendants' . . . possession").

[8] The Receiver's position that WOF should not be allowed to seek compensation for the lost time-value of money is dubious. In fact, courts in the Ponzi-scheme context have recognized the time-value of money as "equivalent value" in the fraudulent transfer context. *See, e.g.*, *Daly v. Deptula (In re Corrozzella & Richardson)*, 286 B.R. 480, 487 (D. Conn. 2002) (collecting cases and noting "[t]here is a sharp split of authority on the issue of whether payment of interest by a Ponzi scheme operator can ever constitute reasonably equivalent value"). The *Daly* court firmly concluded that proceeds of an investment are *not* always excluded from a fair-value analysis, noting that "to hold otherwise would ignore the universally accepted fundamental commercial principal that, when you loan money for a period of time in good faith, you have given value and are entitled to a reasonable return." *Id.* at 489.

[9] The Receiver acknowledges that WOF "will only suffer losses if it fails to establish its good faith affirmative defense" under FUFTA "and is required to return the amount of its principal investment." Opp. at 15. That is, the Receiver concedes that if he prevails on the full value of his claims—receiving an award for principal and the amounts in excess of principal—WOF will have a compensable injury for which it would have no recourse against H&K and GSEC. The Receiver's concession is, however, insufficient, because, as argued *supra*, WOF would also have a claim against H&K and GSEC for its losses of return due to the time-value of money.

No one seriously disputes the fact that the use of funds for a period of time has value, and WOF should either be able retain that value under the FUFTA affirmative defense (assuming the Receiver can prove his affirmative case) or as a independent claim for relief against persons responsible for WOF's losses. Either way, the Panel should not get further into the weeds of the case, except as necessary to conclude that WOF would have a valuable claim against H&K and GSEC, which has been traded on by the Receiver in his settlement of claims in federal court, and that a judgment credit is the correct way to compensate WOF for its lost legal rights.

C. The Receiver's Opposition to a Judgment Credit Is Inequitable.

Arbitrators allocate legal liabilities based on evidence and law—they are not called upon to advance societal goals or to consider unadorned pleas for justice. Nonetheless, if the Receiver wants to have a detailed conversation about equity, he does not occupy the high ground on this issue.

As an initial matter, the federal courts are not as universally supportive of clawback actions as the Receiver suggests. Courts have observed:

> By forcing the square peg facts of a "Ponzi" scheme into the rounds holes of the fraudulent conveyance statutes in order to accomplish a further reallocation and redistribution to implement a policy of equality of distribution in the name of equity, I believe that many courts have done a substantial injustice to those statutes and have made policy decisions that should be made by Congress.

Corrozzella & Richardson, 286 B.R. at 489, 491 (observing that "[t]o create what is perceived by some to be an 'equitable' exception to the plain language of the statute is to usurp the function of the legislature").

Congress's consideration of clawback actions has not viewed such actions positively. At a hearing of the subcommittee on capital markets, the representatives were incensed at the clawback suits brought by the Madoff trustee:

- "[I]nnocent investors are being held to a higher standard" and are being "hunted down and accused somehow of . . . doing some sort of wrongdoing."
- The "victims" of the fraud "are now being terrorized by the trustee."
- "[W]e are doing tremendous harm with the issue of the clawback to many, many people."
- "[T]here is a lot of collateral damage right now. . . . And I don't know if we're really addressing that—the inequity, the injustice, the horror there."
- "I've spoken to many of these people and they described to me what they're going through. They are not being treated as citizens. They are being treated as defendants. They are being treated as criminals. And it's a highhanded arrogant attitude by the trustee towards these people."
- "I mean this whole thing is bizarre, it's Kafkaesque. I mean 'first do no harm' should be the rule. . . . But instead of the Hippocratic Oath, we've taken the hypocritical. And we're saying first do no harm and then we're going after these people. The whole notion is weird."

Hearing of the Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises of the H. Fin. Serv. Comm., 111th Cong., Sept. 23, 2010. The Receiver lacks legislative support for the wealth-redistribution scheme he asks the Panel to endorse.

Furthermore, the Receiver's rhetoric, accusing WOF of seeking to "retain millions of dollars Nadel stole from other investors" (Opp. at 18), rings hollow given the fact that the Receiver has paid himself and his lawyers over $13.5 million of those same (allegedly stolen) funds. The Receiver cannot distinguish between the funds disbursed to WOF and those he uses to pay himself. WOF, at least, believes that Valhalla was not a Ponzi scheme and that it had a positive trading history from which WOF was paid its disbursements.

Finally, the Receiver paints WOF as "a sophisticated hedge fund," ignoring the fact that WOF has innocent investors of its own, whose life savings the Receiver seeks to diminish in the name of paying other innocent investors. WOF's investors have lost funds in fraudulent schemes without recompense in the past—such are the risks they took when investing in unregulated

securities. *Corrozzella & Richardson*, 286 B.R. at 490 (reasoning "that all investors took a series of risks when they invested, including that they might not get repaid their principal or their contractual interest, and that allowing those victims to keep their interesting was as fair as the trustee's partial redistribution of that interest to other investors").

The Receiver's claims are completely foreign outside of the "Ponzi" scheme context. No one has sued the class of net-winners in any of the largest, baldest securities fraud cases in our country's history. That is, no one sued the innocent net-winners of Enron (or Tyco International or WorldCom), despite the fact that people who fortuitously sold their Enron shares before the fraud was uncovered made millions of dollars to the detriment of others who bought too late. Suing "net winners" who profited in a fraudulent scheme is not the norm.

In the final analysis, the Receiver seeks to divert attention away from the deal he struck with H&K and GSEC when he received $35 million in settlement of claims for those entities participation in Mr. Nadel's investments.[10] In that deal, he sold the potential for a full recovery for the certainty of a lesser recovery. He also sold WOF's claims against H&K and GSEC for no value to WOF, except for the judgment credit he now attempts to avoid. The Receiver seeks to make up the shortfall generated by his voluntary reduction in the assets available (i.e., settlement of claims against H&K and GSEC) by continuing to press claims against innocent investors, like WOF, who happened to get out of Valhalla before it crashed. Going back on the deal he struck with the settling defendants and the federal court is the epitome of inequitable conduct.

[10] At multiple points, the Receiver criticizes WOF for failing to *object* to the entry of the H&K and GSEC bar orders. Opp. at 16. That would be a strange action for WOF to have taken since it believes the bar orders created a fair exchange of limiting WOF's claims against H&K and GSEC in exchange for a judgment credit against the Receiver's claims.

For the reasons stated in its motion and this reply, WOF respectfully asks the Panel to enforce the judgment credits provided by the bar orders. Because the Receiver seeks less than the full value of either settlement amount, he is not entitled to have any recovery in this action.

Respectfully submitted, this 14th day of January, 2013.

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CERTIFICATE OF SERVICE

The undersigned certifies that a true and correct copy of this motion has been filed electronically with the case administrator for the American Arbitration Association as well as served by email on all attorneys of record.

This 14th day of January, 2013.

/s/ Mark A. Rogers
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