* * * Unpublished Opinion * * *

IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF UTAH

CENTRAL DIVISION

In re: WAYNE R. OGDEN, Debtor, ORLANDO AND ROSEMARY NICKERSON, Appellant, v. STEVE R. BAILEY, Trustee of the Estate of Wayne Ogden, Appellee.	)	OPINION AND ORDER District Court No. 2:00-CV-49K

This matter is before the court on an appeal from the United States Bankruptcy Court for the District of Utah, Central Division. This matter came on for oral argument on April 5, 2000. The appellant was represented by Noel S. Hyde and the appellee was represented by Leslie J. Randolph. Oral argument was heard and the court took the matter under advisement. The court has carefully considered all briefs and other materials submitted by the parties. The court has further considered the law and facts relevant to this appeal. Now being fully advised, the court enters the following Opinion and Order.

I. BACKGROUND

This appeal arises out of the bankruptcy court's granting of summary judgment in favor of the trustee/appellee and against the Nickersons/appellant. In an Order and Judgment

dated December 7, 1999 the bankruptcy court granted summary judgment in favor of the trustee and entered judgment against the Nickersons in the amount of $211,237.50 together with prejudgment interest in the amount of $25,811.46 to bear interest at the rate of 5.411% until satisfied.

This case originated out of an involuntary Chapter 7 petition filed against Wayne R. Ogden ("Ogden"), filed on June 16, 1997. Ogden stipulated to an order for relief under chapter 7 on July 3, 1997. On August 5, 1997, Steven R. Bailey was appointed permanent chapter 7 Trustee ("the Trustee"). On September 9, 1998, the Trustee filed the adversary proceeding leading to this appeal.

Ogden operated a Ponzi scheme from approximately September 1995 through May of 1997. In this scheme Ogden obtained in excess of a thousand loans totaling over $23,000,000 from private individuals and business entities, most of whom were not in the business of loaning money. Ogden moved the investor money he received by personal checks and cashier's checks, through title company trust accounts and by endorsing investment checks payable to himself and passing them on to prior investors. He personally raised and disbursed some of the investor money, but Ogden also used others to collect funds from investors and to deliver returns to investors. One of these individuals was S. Matthew Schultz, through Schultz's business known as Exchange Financial Group ("Schultz"). During the time period at issue, the amount of funds Ogden received from investors and the amount of funds he repaid his investors were approximately equal on a month-to-month basis. The investors' funds were merely being funneled from one investor to another.

The Nickersons were part of a core group of investors who invested with Wayne

Ogden through Schultz. Schultz received investment funds from Wayne Ogden's investors by cashiers checks or personal checks payable either to Exchange Financial or to Ogden. The instruments payable to Exchange Financial were deposited into an Exchange Financial account. Schultz then wrote one check on the Exchange Financial account payable to Ogden and delivered directly to Ogden those instruments showing Ogden as payee. Ogden, not Schultz, personally issued promissory notes to individuals who invested with him through Schultz. Schultz repaid Ogden's investors with funds he received from Ogden for that purpose. Ogden transferred the investors' returns to Schultz by personal checks drawn on a number of Ogden's checking accounts. Schultz deposited the funds into Exchange Financial bank accounts and immediately thereafter wrote checks to the investors for their returns on their Ogden investments.

As stated previously, Orlando Nickerson was a member of Schultz's core group of Ogden investors. When Ogden presented an investment opportunity to Schultz, Schultz then contacted the Nickersons and other members of his core group of investors and explained the transaction or project Ogden had presented to him. The core group then gave Schultz money for the investment. The Nickersons invested with Ogden by instruments payable to Ogden or to Exchange Financial and received returns on their investments by checks from Ogden or by checks which passed through Exchange Financial accounts to them. The Nickersons admitted in their answers to interrogatories that they understood that their investment funds were going to Ogden through Exchange Financial and that their returns were coming back from Ogden through Exchange Financial. They stated that:

> Defendants' direct dealings were with Exchange Financial, but they did understand that Exchange Financial was remitting funds to Wayne Ogden and that Mr. Ogden was investing such funds as an

> agent for Coldwell Banker in various real estate transactions from which the investment returns were ultimately repaid through Exchange Financial.

Nickersons Response to Interrogatory No. 14.

Between October of 1995 and May of 1997, the Nickersons invested $129,500.00 with Ogden through Exchange Financial, and received returns of $340,737.50 for a profit of $211,240.00. On May 28, 1997, Ogden disappeared. After that time the Nickersons entered into a written agreement with Schultz entitled "WAIVER AND RELEASE AGREEMENT". The agreement is signed by Orlando Nickerson and Schultz. The agreement reads in pertinent part that:

> At the time of the Prior Agreement Lender [the Nickersons] understood that it was loaning money to Wayne Ogden which would be repaid with interest from the sale of real property. Lender did not intend nor did it believe that it was loaning money to S. Matthew Schultz. Lender did not intend nor did it believe it was entering into an investment contract with S. Matthew Schultz or in any manner making an equity investment.

The Nickersons filed three proofs of claims in Ogden's bankruptcy case.

In granting summary judgment in favor of the Trustee and against the Nickersons, in the adversary proceeding, the bankruptcy court held that S. Matthew Schultz was a commercial conduit for the funds from the Debtor and that the Nickersons were thereby the "initial transferees" pursuant to 11 U.S.C. § 550. Therefore the bankruptcy court found that the Nickersons must return the profits they derived from the Ponzi scheme back to the Debtor's estate. The Nickersons appealed the bankruptcy court's ruling to this court, seeking review on four issues: (1) whether the bankruptcy court applied the correct standard in evaluating factual allegations relating to the Trustees Motion for summary judgment; (2) whether the bankruptcy

court properly ruled that Schultz was a commercial conduit for the funds passed from the debtor to the defendants thereby making the defendants the "initial transferees" pursuant to 11 U.S.C. § 550; (3) whether the bankruptcy court's finding that the Debtor has an interest in all funds transferred by Schultz to the defendants was correct as a matter of law; and (4) whether the bankruptcy court erred and the defendants are not the debtor's initial transferees, but are instead mediate or immediate transferees, and as such, did the defendants produce any evidence that meets the requirements for a good faith defense pursuant to 11 U.S.C. § 550(b).

II. STANDARD OF REVIEW

In the review of orders from the Bankruptcy Court, there are three standards of review that may be applied. First, where the Bankruptcy Court is the finder of fact, the court's factual determinations will not be set aside unless they are "clearly erroneous." *See* Bankruptcy Rule 8013 and *Taylor v. I.R.S.,* 69 F.3d 411 (10th Cir. 1995). A finding of fact is clearly erroneous only if the court has a definite and firm conviction that a mistake has been committed. *See In re Mama D'Angelo, Inc.,* 55 F.3d 552 (10th Cir. 1995). Secondly, a bankruptcy court's ruling involving findings of fact may be overturned if the findings are premised on improper legal standards or on proper legal standards improperly applied. In these instances, the review of this court shall be *de novo. See In re Hedged-Investment Associates, Inc.,* 84 F.3d 1267 (10th Cir. 1996). Lastly, this court will exercise *de novo* review over the Bankruptcy Court's conclusions of law. *See Hall v. Vance,* 887 F.2d 1041 (10th Cir. 1989). Further, mixed questions of law and fact which involve primarily a consideration of legal principles are reviewed *de novo. See In re Ruti-Sweetwater, Inc.,* 836 F.2d 1263 (10th Cir. 1988). Acting as an appellate court in reviewing the bankruptcy court's summary judgment ruling, the court reviews the appeal in the same manner as

the bankruptcy court ruled the initial motion for summary judgment. The court must determine if while examining the record in the light most favorable to the nonmoving party, any genuine issue of material fact is in dispute and if the bankruptcy court correctly applied the substantive law, with all reasonable factual inferences drawn in the nonmovants favor. *See Mountain Fuel Supply v. Reliance Ins. Co.*, 993 F.2d 882 (10th Cir. 1991). Summary judgment is proper if the moving party can demonstrate that there is no genuine issue of material facts and that he is entitled to judgment as a matter of law. However, the mere existence of some alleged factual dispute between the parties does not defeat an otherwise properly supported motion for summary judgment. *See Anderson v. Liberty Loby, Inc.*, 477 U.S. 242, 248 (1986).

III. DISCUSSION

A. Standard of Review Regarding Factual Disputes

The Nickersons allege that the bankruptcy court failed to construe the alleged facts of the case in a light most favorable, to them, the non-moving party. The Nickersons allege that three transfers from Exchange Financial, totaling $43,750, were not related to investments with Wayne Ogden and rather, these transfers were related to Schultz's "check store" which is unrelated to Ogden. According to the Court in *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 247-49, genuine issues of material fact are established only by admissible evidence. The admissible evidence presented to the bankruptcy court consisted of the sworn testimony of S. Matthew Schultz, Wayne R. Ogden and Mark Hashimoto. This testimony does not support the Nickersons contention that three of the transfers were related to check store obligations and not investments with Ogden. To the contrary, the Hashimoto Affidavit sets forth a schedule of transfers in detail which support the Trustee's argument that all of the transfers were related to

the Ponzi scheme. The Nickersons offer no documentary evidence in opposition of the Trustee's evidence. Rather, they simply state that to the best of their recollection, three of the transfers are related to the check store. They state that the checks themselves are the documentary evidence in that the amounts match those that were associated with a loan to the check store.

The Nickerson's statements are not admissible evidence and raise no genuine issue of material fact. "In response to a motion for summary judgment, a party cannot rest on ignorance of facts, on speculation or on suspicion and may not escape summary judgment in the mere hope that something will turn up at trial." *Conaway v. Smith*, 853 F.2d 789, 794 (10th Cir. 1988). The Nickersons have offered no evidence to support their allegations and the bankruptcy court applied the correct standard and properly determined that there are no genuine issues of material fact.

B. Commercial Conduit

The bankruptcy court held that Schultz was a "conduit" for funds passed from the Debtor, Ogden, to the investors, and that pursuant to Section 550 of the Bankruptcy Code, the Nickersons were the initial transferees and therefore strictly liable for the return of the avoided transfers.

Section 550 of the Bankruptcy Code identifies transferees from whom a trustee may recover avoided transfers. This section reads in pertinent part as follows:

> (a) to the extent a transfer is avoided under section . . .544, 547, 548. . . of this title, the trustee may recover, for the benefit of the estate the property transferred, or, if the court so orders, the value of such property, from—
> (1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or (2) the immediate or mediate transferee of such initial transferee.

> (b) The trustee may not recover under subsection (a)(2) of this section from-
> (1) a transferee that takes for value, including satisfaction or securing of a present or antecedent debt, in good faith, and without knowledge of the viability of the transfer avoided; or
> (2) any immediate or mediate good faith transferee of such transferee.

Section 550 of the Bankruptcy Code imposes strict liability for initial transferees and "the entity for whose benefit such transfer was made", for return of avoided transfers. 11 U.S.C. § 550(a)(1). Because of this strict liability, courts protect financial intermediaries through which a debtor moves funds to a creditor as "commercial" or "mere" conduits. Where an entity is determined to be a mere conduit, that entity does not constitute an initial transferee under §550(a). Instead, the transferee of the conduit is liable as an initial transferee.

The Bankruptcy Code does not define "initial transferee," and as Judge Benson of this court states in *Big Sky Motors, Ltd v. Bailey* 2:99-CV-270B, "difficulties have arisen in determining the correct identity of an initial transferee, especially when a debtor gives money to an intermediary before transferring it to a creditor and when that intermediary appeared to be the initial transferee." The *Big Sky* opinion goes on to discuss the history of the "commercial conduit" exception to the strict liability of an initial transferee stating that the theory was developed in "an effort to avoid unfairness that might result from the literal application of § 550(a). *See Billings v. Key Bank of Utah (In re Granada),* 156 B.R. 303, 306 (D. Utah 1990).

In *Bonded Financial Services v. European American Bank,* 838 F.2d 890 (7th Cir. 1988) the Seventh Circuit established what is known as the "dominion and control" test. "The minimum requirement of status as a "transferee" is dominion over the money or other asset, [and] the right to put the money to ones own purposes. When A gives a check to B as agent for

C, then C is the "initial transferee"; the agent may be disregarded." *Id.* at 893. The Tenth Circuit applied this test in *Rupp v. Markgraf,* 95 F.3d 936, 939 (10th Cir. 1996) in which the court reversed the lower court and found that the Interstate Bank of Nevada was a commercial conduit. The Tenth Circuit explained that "those who act as mere "financial intermediaries" or "couriers" are not initial transferees under § 550".

The appellants argue that this case is factually similar to *Bailey v. Hazen*, BAP No. UT-99-044. In that matter the Bankruptcy Appellate Panel reversed the bankruptcy court relating to the designation of a financial intermediary as a conduit in connection with the Wayne Ogden Ponzi scheme. The court ruled that the existence of a debtor/creditor relationship between the intermediary entity and Wayne Ogden precluded the finding that the intermediary entity is a conduit. The appellants argue that a similar type of relationship is at issue here. However, the *Hazen* case is distinguishable from the case at hand. In *Hazen*, the financial institute, Avis & Archibald Title Insurance Company, was the escrow agent through which the real estate transaction between Ogden and certain investors was to close. A series of transaction between the Debtor, Avis & Archibald and the investors resulted in the Debtor owing Avis & Archibald over $300,000.00. The Debtor obtained monies from various people in order to repay Avis & Archibald which led to the debtor/creditor relationship. This is not the case at hand. Schultz was used only as a middleman. Schultz received investor funds on behalf of Ogden's investors and passed those funds along to their intended beneficiaries. Schultz was not free to use these funds for his own purposes; he was required to use them to satisfy Ogden's outstanding investor obligations. Further, at no time did Schultz become a creditor of Ogden. He was an employee of Ogden and did receive commissions from Ogden, but a debtor/creditor relationship was never

established.

Appellee argues that this case is analogous to *Big Sky Motors v. Bailey*, District Court Case No. 2:99-CV-270B. *Big Sky*, which also was in connection with the Ogden Ponzi scheme, involved the same title company as the *Hazen* matter, however the District Court left the title company with its conduit protection stating that it had no dominion and control over the funds received by Big Sky which Ogden directed into its trust account to replace the improperly disbursed funds. Judge Benson held that Big Sky, one of Ogden's investors, became Ogden's creditor as distinguished from Avis & Archibald. However, the District Court went on to hold that "Avis & Archibald" did derive some advantage from this transfer and was more involved that the typical financial intermediary. When Avis & Archibald wrongfully released funds to Ogden, Avis & Archibald breached its fiduciary duty owed to Big Sky, and as a result, became liable to Big Sky." *Id.* at 20. In this matter, Schultz did not derive any advantage from the transfer to the Nickersons. He was nothing more than a middleman. He simply took a pre-agreed upon commission and had no control over the funds at any time. This matter presents a much stronger case for "commercial conduit" protection than that presented in *Big Sky*. For these reasons, the bankruptcy court properly held that Schultz was afforded conduit protection and that the Nickersons were the "initial transferees" of the funds derived from Wayne Ogden.

C. <u>Debtor's Interest in the Funds Passed to the Nickersons</u>

The Nickersons further argue that there are no facts before the court which support the conclusion that Ogden had or maintained any interest in the funds which Schultz transferred to the Nickersons at the time each transfer was made. They argue that Schultz's and Ogden's funds were commingled and the burden is upon the trustee to show that the Debtor had

an interest in the funds. The evidence supports the bankruptcy court's ruling that the Debtor did have an interest in the funds which Schultz passed to the Nickersons. The testimony of Mark Hashimoto and Ogden's own admissions establish that Ogden operated a Ponzi scheme from at least September 1, 1995 through May of 1997. Hashimoto's unrefuted testimony also establishes that over 97% of the funds in Ogden's bank account during this time period came from investor loans. It also confirms the funds Ogden transferred to investors through Exchange Financial were funds from his bank accounts which he had borrowed or obtained by fraud from investors in his Ponzi scheme and commingled to the extent that tracing is not possible. Schultz testified he used Ogden's funds to pay Ogden's investor returns and that Nickerson was one of the core Ogden investors who used Schultz as the go between. Further, it is not reasonable that Schultz would have used his own funds to pay investors. It is clear that the funds came from Ogden. Further, the Waiver and Release Agreement entered into by Schultz and Mr. Nickerson, supports the fact that the Nickersons were aware that the money was coming from Ogden.

In *Merrill v. Allen*, 60 B.R. 985 (D. Utah 1986), another Ponzi case, the court held that:

> When a debtor obtains money by fraud and mingles it with other money so as to preclude any tracing and the defrauded party does not timely avoid the transaction, the money is the property of the debtor within the meaning of section 548 of the Code. As such, it is subject to the trustee's avoiding powers provided the other requirements of section 548 are satisfied.

The evidence is overwhelming that Ogden had an interest in the funds that were ultimately transferred to the Nickersons and the appellant offers no admissible evidence to the contrary other than their own statements that the money was from Schultz. This scintilla of evidence is not

sufficient to overcome the significant amount of evidence that states otherwise.

D. Good Faith Defenses

The Nickersons argue that the bankruptcy court precluded them from asserting the good faith defenses set forth in 11 U.S.C. § 550(b). Because this court affirms the bankruptcy court's ruling that the Nickersons are the "initial transferees," they are strictly liable and the good faith defenses do not apply. The bankruptcy court properly found that these defenses were not applicable.

E. Motion to Supplement the Record on Appeal

The appellees move this court to supplement the record on appeal with a complete transcript of a Rule 2004 examination of S. Matthew Schultz. That motion is DENIED and the court has only considered the record that is currently before it.

For the reasons stated herein it is hereby

ORDERED that the ruling of the bankruptcy court is AFFIRMED in its entirety and the Nickersons are ORDERED to remit $211,237.50 together with prejudgment interest in the amount of $25,811.46 which judgment shall bear interest at the rate of 5.411% until satisfied. It is further ORDERED that the appellee's Motion to Supplement the Record on Appeal is DENIED.

DATED this ____ day of April, 2000.

DALE A. KIMBALL
United States District Judge