IN THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF NORTH CAROLINA CHARLOTTE DIVISION

SECURITIES AND EXCHANGE COMMISSION,	)	
Plaintiff,	)	
vs.	)	**Civil Action**
REX VENTURE GROUP, LLC d/b/a ZEEKREWARDS.COM, and PAUL BURKS,	)	**No. 3:12-CV-519**
Defendant,	)	

PLAINTIFF SECURITIES AND EXCHANGE COMMISSION'S OPPOSITION TO MOTION TO APPOINT REPRESENTATIVE FOR AFFILIATES

Plaintiff Securities and Exchange Commission ("SEC," "Commission" or "Plaintiff") hereby submits the instant memorandum in opposition to the Motion by Fun Club USA, Inc., David Sorrells, David Kettner and Mary Kettner (collectively, "Movants") to appoint a "Representative for Affiliates." *See* Motion to Appoint Representative for Affiliates (Docket No. 77, filed 11/30/12) ("Quilling Mot."); *see also* Memorandum in Support of Quilling Mot. (Docket No. 78, filed 11/30/12) ("Quilling Mem.").

INTRODUCTION

Attorney Michael Quilling, on behalf of certain significant net "winners" in the ZeekRewards Ponzi scheme alleged in the Complaint, seeks to have himself appointed "Representative for Affiliates," provided with counsel, and compensated out of the Receivership Estate. Quilling Mot. at 1. The Quilling Motion suffers from several obvious flaws:

(1) The Motion offers no compelling factual or legal basis for the Court to consider appointing a "Representative for Affiliates" – the Commission continues to work closely with and monitor the Receiver to ensure that as much money as possible is returned to injured investors in the most efficient manner possible;

(2) Appointment of a "Representative for Affiliates" would serve only to complicate this already complex matter, obstruct the Receiver's ability to efficiently marshal Receivership Assets, and significantly and unnecessarily deplete the pool of assets available to be distributed to injured investors (given that Quilling and Alexander seek to be compensated from Receivership Assets); and

(3) The interests of Quilling and Alexander's current clients – significant net "winners" in the Ponzi scheme alleged in the Complaint – are diametrically opposed to the vast majority of ZeekRewards investors that were net "losers" in the Ponzi scheme.

Therefore, the instant motion should be denied in its entirety.[1]

FACTS

Michael Quilling and his local counsel, Rodney Alexander, purport to represent several hundred former affiliates of ZeekRewards. *See* Notice of Appearance for Fun Club USA, Inc. (Docket No. 39, filed Sept. 19, 2012); *see also* Quilling Mem. at 3 (describing Quilling and Alexander's representation of "several hundred" affiliates). Their clients appear to be substantial net "winners" in the ZeekRewards scheme, including several individuals who each received more than $1 million based on their participation in ZeekRewards. *See* Memorandum in Support of Emergency Motion for Order Requiring Release of Third-Party Assets (Docket No. 81, filed Dec. 11, 2012) ("Emergency Mot.") at 6.

Quilling and Alexander recently entered a separate appearance on behalf of several such significant net winners. *See* Notice of Appearance for D. Kettner, M. Kettner, and D. Sorrells (Docket No. 68, filed Nov. 16, 2012). One of their clients, David Sorrells, alleges that he had approximately $373,000 frozen, and two other clients (David and Mary Kettner) each had more

[1] The Commission's ability to respond to the Quilling Motion is limited by the confidential nature of the Commission's ongoing investigation. If the Court is inclined to grant the motion, the Commission respectfully requests an opportunity to provide the Court with additional information under seal or in a closed hearing.

than $25,000 frozen. *See* Emergency Mot. at 6. Upon information and belief, certain of Quilling and Alexander's clients received excess returns from ZeekRewards in addition to the amounts frozen, with Sorrells having withdrawn approximately $1 million from ZeekRewards, and the Kettners having withdrawn approximately $500,000.

Quilling also purports to represent (and has accepted service of SEC subpoenas on behalf of) several other individuals who, upon information and belief, are substantial net winners. Another client, Robert Craddock, established Fun Club USA, Inc. on or about August 28, 2012, shortly after ZeekRewards was shut down.[2] Upon information and belief, Craddock has been conducting weekly conference calls and sending written communications to former ZeekRewards affiliates. In these conference calls and written communications, Craddock has repeatedly challenged the Receiver's authority and encouraged affiliates not to cooperate with the Receiver. Moreover, Craddock has asserted (incorrectly) that the SEC has acknowledged to his lawyers that the SEC has doubts or concerns about its case and is looking for ways to "back out" in order to allow ZeekRewards to re-start its operations. Another Quilling client, David Kettner has repeated assertions similar to those made by Craddock in written communications to former ZeekRewards affiliates.

ARGUMENT

I. Movants Offer No Compelling Rationale For The Relief Requested.

Movants – significant net winners currently represented by Quilling — present a fairly limited rationale for appointing their lead attorney to "represent the collective interests of the Affiliates and all creditors of the receivership estate":

[2] *See* Articles of Incorporation for Fun Club USA Inc. (filed Aug. 28, 2012), available at http://www.sunbiz.org/COR/2012/0829/10892141.tif. Movants have yet to explain why an entity formed *after* the Court froze ZeekRewards assets and appointed the Receiver should be heard on the subject matter of the instant motion.

> Many of the actions being taken and proposed by the Receiver may substantially and irreparably impact their rights. It is impractical for the Affiliates to each retain counsel and appear in this case. Many of them cannot afford to do so. The Affiliates need representation of their interests in this case and Movants request that the Court appoint Michael J Quilling as Examiner in these proceedings to represent the collective interests of the Affiliates and all creditors of the receivership estate and that the Examiner and his counsel be compensated out of the receivership estate.

Quilling Mot. at 1; *see also* Quilling Mem. at 1 (similar language). Movants provide no cogent explanation of how the rights of affiliates may be "substantially and irreparably impact[ed]," nor do they offer any meaningful factual or legal support for proposition that appointing an examiner will avoid such a result. Movants also fail to explain why individual investors cannot adequately protect themselves when and if the Receiver attempts to claw back excess returns from ZeekRewards investors.

A. There Is No Factual Basis For The Relief Requested.

Movants provide no clear factual basis for immediate appointment of an examiner. Instead, they misstate the respective roles of the Receiver and the Commission, and they understate the role of the Court:

> None of the current parties in this case is in a position to represent or otherwise present the views of the Affiliates to the Court. The SEC firmly believes in the content of its Complaint and cannot be expected to present any counter views to what they contend. The Defendants have already entered into a Consent Decree and, likewise, cannot be expected to present the views of the Affiliates to the Court. The Receiver is the one taking the actions which the Affiliates, in some instances, oppose and cannot be expected to present the views of the Affiliates to the Court. The Affiliates need their own representative.

Quilling Mem. at 4. In fact, the Commission brought this lawsuit in order to protect all investors (referred to by Movants as "affiliates"), and Commission staff and undersigned counsel continue to fulfill that role, closely monitoring the efforts of the Receiver to ensure that as much money as possible is returned to injured investors. The issue is not whether "[t]he SEC firmly believes in the content of its Complaint," since Paul Burks and Rex Ventures settled the underlying lawsuit

without contesting the accuracy of the factual allegations of the Complaint. Instead, the issue is whether the Receiver is using best efforts to marshal the estate's assets for the benefit of all the aggrieved investors. Thus far, there is every indication that he is.

Movants also ignore the role of the Court in reviewing and, where appropriate, modifying the order that appointed the Receiver and described his duties. *See* Agreed Order Appointing Temporary Receiver and Freezing Assets of Defendant Rex Venture Group, LLC (Docket No. 4, filed Aug. 17, 2012) ("Agreed Order"); Order Granting in Part and Denying in Part Receiver's Motion Seeking Amendment of Agreed Order Appointing Temporary Receiver and Freezing Assets of Defendant Rex Venture Group, LLC (Docket No. 21, filed Aug. 30, 2012). In short, Movants offer no facts that suggest the need to appoint an additional representative for investors.

B. Movants Offer No Legal Support For The Relief Requested.

Nor do Movants provide any clear legal basis for this Court to appoint another representative for injured investors. The primary purpose of this Receivership, as with any receivership, is the marshaling of the estate's assets for the benefit of aggrieved investors. *See, e.g.*, *SEC v. Hardy*, 803 F.2d 1034, 1038 (9th Cir.1986) ("[A] primary purpose of equity receiverships is to promote orderly and efficient administration of the estate by the district court for the benefit of creditors."); *see also Quilling v. Cristell*, No. 3:04 CV 252, 2006 WL 1889155 (W.D.N.C. Jul. 7, 2006) (explaining that the purpose of receivership "was to preserve and protect the assets of the Receivership Estate for the benefit of all creditors of the Receivership Estate including investors who had been defrauded by [defendant's] Ponzi scheme"). Here, the Receiver was appointed to preserve and protect the assets of the Receivership Estate for investors injured by the scheme described in the Complaint.

To be sure, this Court has "broad discretion" to take appropriate action to protect investors, but the Quilling Motion offers no compelling rationale for the Court to appoint an examiner here. *United States v. Vanguard Inv. Co.*, 6 F.3d 222, 226–27 (4th Cir.1993) (noting district court's broad discretion). Although the significant net winners represented by Quilling and Alexander claim that "in large cases of this type, despite the prohibition against intervention, it is *very common* for the Court to appoint a person to act as the spokesperson for the 'investors' or victims," they cite no Fourth Circuit case in which another representative was appointed in a case where a receiver had already been appointed. *See* Quilling Mem. at 4. Instead, Movants rely on two unpublished cases from the Northern District of Texas where Quilling himself moved to have a representative appointed. *Id*. (citing *SEC v. Stanford Int'l Bank, Ltd.*, No. 3:09-CV-298-N, --- WL --- [Docket No. 322] (N.D. Tex. Apr. 20, 2009); *SEC v. ABC Viaticals, Inc.*, No. 3:06-CV-2136-P, --- WL --- [Docket No. 12] (N.D. Tex. Nov. 30, 2006)).

These cases do not support appointment of an examiner here. In *Stanford*, for example, the court appointed an examiner only after concerns arose regarding the approach taken by the receiver in that case. Approximately 32,000 brokerage accounts were frozen in *Stanford*, including many that held no assets related to the alleged scheme. *See, e.g.*, Receiver's Opposition to Motion to Appoint Examiner, *Stanford* Docket No.173 (noting release of more than 28,000 of 32,000 frozen accounts). Here, by comparison, the Agreed Order was narrowly tailored to freeze only assets generated by the Ponzi scheme alleged in the Complaint. This approach highlights the ability of the Court to monitor and control the activities of the Receiver. Even the funds that are the subject of Quilling and Alexander's recently-filed motion to limit the scope of the Agreed Order appear to have been generated by the scheme alleged in the Complaint, as opposed to the overwhelming majority of the accounts frozen in *Stanford*. *Cf.*

Stanford Docket No.173; Emergency Mot. Simply put, Movants provide no compelling rationale for the Court to appoint another representative to protect investors, and *Stanford* does nothing to change this analysis.

Nor does the other district court case cited by Movants change this analysis. *See* Quilling Mem. at 4 (citing *ABC Viaticals*). In *ABC Viaticals*, Quilling himself was the court-appointed receiver, and he requested appointment of an examiner with consent of the parties. Here, by comparison, the Receiver and the Commission both oppose appointment of another representative for investors.

Although the Commission agrees that this Court has "'broad powers and wide discretion' to determine appropriate relief in an equity receivership," the Ninth Circuit case cited by Movants does not support the appointment of an examiner here. *See* Quilling Mem. at 5 (noting that," quoting *SEC v. Capital Consultants, LLC*, 397 F.3d 733, 738 (9th Cir. 2005)). Instead, *Capital Consultants* provides a clear example of a district court's ability to manage a complex distribution through a receiver, with appropriate input from the Commission and other interested parties, without the appointment of an examiner. *Id*. (affirming district court's approval of receiver's distribution plan).

Movants also misleadingly assert that "the concept of a court appointed representative is expressly recognized by statute in the bankruptcy courts." *See* Quilling Mem. at 5. In fact, Section 1104 of the Bankruptcy Code provides that that an examiner may not be appointed where a Chapter 11 trustee is already in place:

> (c) if the court does not order the appointment of a trustee under this section, then at any time before confirmation of a plan, on request of a party in interest or the United States trustee, and after notice and a hearing, the court shall order the appointment of an examiner to conduct an investigation of the debtor as is appropriate, including an investigation of any allegations of fraud, dishonesty,

> incompetence, misconduct, mismanagement, or irregularity in the management of the affairs of the debtor of or by current or former management of the debtor . . . .

11 U.S.C. § 1104(c); *see also In re GHR Companies, Inc.*, 43 B.R. 165, 176 (Bankr. D. Mass. 1984) (explaining that since a trustee and an examiner may not serve concurrently, "it seems fruitless to appoint an examiner"). Thus, the analogy to bankruptcy proceedings offered by Movants does nothing to support the Quilling Motion.

Finally, Movants offer nothing to distinguish the instant case from *Cristell* or any of the other cases in which Quilling acted as a court-appointed receiver, but apparently saw no need for another court-appointed representative to protect investors. *See, e.g., Cristell*, 2006 WL 1889155; *see also* Quilling Mot., Exhibit 1 (*Curriculum Vitae* of Michael J. Quilling, listing receivership appointments).

C. Appointment Of An Examiner Would Deplete The Receivership Estate.

The instant motion is a fairly transparent effort to shift the cost of Quilling and Alexander's fees from their current clients – a limited number of significant net winners – to all injured investors. *See* Quilling Mem. at 5. ("When appointed, the Examiner is compensated out of the receivership estate through the filing of periodic fee applications. In that respect, the cost of participation in the proceedings is shared by all, not just a few, and thousands of people are given a voice in the proceedings through one person."). Movants provide no compelling justification for this added burden on the Receivership Estate.

II. Quilling and Alexander Cannot Represent All Investors.

Having failed to provide meaningful factual or legal support for appointment of an additional representative for affiliates, Movants also fail to demonstrate that Quilling and Alexander would be appropriate representatives for all investors injured by the scheme alleged in the Complaint. In particular, Movants fail to explain how Quilling and Alexander can extricate

themselves from their current attorney-client relationships with Movants, a limited number of significant net winners in the ZeekRewards scheme, and fairly represent the multitude of investors who lost money.

A. Quilling And Alexander Have A Clear Conflict Of Interest.

First and foremost, Quilling and Alexander have a clear conflict of interest based on their ongoing attorney-client relationships with a handful of significant net winners in the ZeekRewards Ponzi scheme. Many of the net winners currently represented by Quilling and Alexander, including Movants, face potential litigation by the Receiver to claw back excess returns received from ZeekRewards. Thus far, Quilling and Alexander have zealously represented this small group of significant net winners in their efforts to retain money they received from ZeekRewards. *See, e.g.*, Emergency Mot. The vast majority of ZeekRewards investors, however, lost all or most of their initial investments. Presumably, these investors would support the Receiver's efforts to claw back as much money as possible from net winners for eventual distribution to investors.

The divergent interests between net winners and net losers present Quilling and Alexander with an insurmountable conflict of interest. Quilling and Alexander cannot represent the interests of a small group of net winners with a strong interest in resisting any attempt to claw back excess returns, while simultaneously representing a much larger group of net losers with a strong interest in maximizing clawbacks.

B. Quilling And Alexander Have Acted to Disrupt The Efforts Of The Receiver.

The inherent conflict of interest between Movants and the majority of ZeekRewards investors is demonstrated by Quilling and Alexander's actions thus far. To date, Quilling and Alexander have worked exclusively to disrupt the efforts of the Receiver, advising their clients to

resist the Receiver's attempts to gather information about the amount of money they received from ZeekRewards.

In addition, Quilling and Alexander have moved to release funds to their significant net winner clients. *See* Emergency Mot. This motion is contrary to the interest of most ZeekRewards investors, since it may serve to reduce the funds ultimately available for distribution by the Receiver.

Nor have Quilling and Alexander given any indication that they could function as cooperative, constructive representatives for the affiliates they purport to represent. For example, Quilling and Alexander filed the instant motion with no meaningful effort to meet and confer with undersigned counsel. (Alexander copied undersigned counsel on an email to the Receiver less than one business day before filing the instant motion, and apparently ignored undersigned counsel's email proposing a telephone conference.) Similarly, Quilling and Alexander failed to meaningfully meet and confer with undersigned counsel before filing the Emergency Motion. Alexander refused to identify the specific assets he and Quilling sought to have released, and refused to disclose the source of the funds. This approach negated any meaningful opportunity to resolve the underlying dispute without the Court's intervention. In addition, Alexander shared certain of undersigned counsel's meet and confer communications directly with a non-party, an approach guaranteed to limit future communications.

To the extent that another court-appointed representative for affiliates is needed, which the Commission does not believe to be the case here, undersigned counsel respectfully submits that the representative (1) should be willing and able to work constructively with the Receiver and the Commission on behalf of injured investors, and (2) should not have a pre-existing attorney-client relationship with a limited subset of investors. Given the history of Quilling and

Alexander's involvement thus far in this litigation, appointment of Quilling as a "Representative for Affiliates" would serve only to complicate this already complex matter, obstruct the Receiver's ability to efficiently marshal Receivership Assets, and significantly and unnecessarily deplete the pool of assets available to be distributed to injured investors.

CONCLUSION

For the reasons set forth above, the SEC respectfully asks the Court to deny the Quilling Motion in its entirety.

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CERTIFICATE OF SERVICE

Undersigned counsel certifies that on this 17th day of December, 2012, the foregoing was filed with the Court's CM/ECF system, which will send electronic copies to counsel of record registered to receive electronic service.

/s/ John J. Bowers
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