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UNITED STATES DISTRICT COURT  
MIDDLE DISTRICT OF LOUISIANA

SIGN  
RICHARD T. MARTIN  
CLERK

WILLIAM G. HAYS, JR., RECEIVER  
AND DISBURSING AGENT ON BEHALF  
OF THE DEBTORS

CIVIL ACTION  
NO. 95-2030-B-M2

VERSUS

JIMMY SWAGGART MINISTRIES, ET AL

RULING

William G. Hays, Jr. ("Hays"), the trustee of the bankruptcy estate, appeals the ruling of the bankruptcy court which denied the receiver's claims under 11 U.S.C. §§ 548(a)(1), (a)(2), (c), and 544(b). For reasons which follow, the decision of the Bankruptcy Judge is hereby reversed.

I. FACTS

Hays brought this action against Jimmy Swaggart Ministries ("JSM") to recover funds paid to JSM by the debtors.<sup>1</sup> The bankruptcy court's memorandum opinion of September 7, 1995 sets forth the facts of this proceeding in great detail. Briefly restated and summarized, the relevant facts are as follows. The debtors in this matter were improperly raising capital to fund a shopping mall development project in violation of state and federal

<sup>1</sup>Sam J. Racile, the principal behind the development plan, formed and used various corporations in this scheme, and the corporations will be collectively referred to by this Court as the debtors.

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securities laws. In order to develop the mall, the debtors needed to purchase certain land owned by "JSM". In order to secure the property for purchase, the debtors, through various corporations, negotiated a series of options and agreements to purchase land owned by JSM. The debtors made numerous, substantial payments to JSM in order to "tie up" the property while the debtors tried to arrange financing. On several occasions, the parties were to execute acts of sale, but these meetings were either cancelled or did not take place. At times, the debtors made large daily payments, many in cash, which ranged from \$7,500 to \$25,000 to maintain an option to purchase. No sale was ever completed between the debtors and JSM. During these negotiations between JSM and the debtors and while some of the options were pending and daily cash payments were being paid to JSM, JSM actively sought other purchasers.

The debtors then filed for bankruptcy. The receiver sought to avoid the payments made to JSM by the debtors and bring the payments back into the bankruptcy estate.

The bankruptcy court ultimately found in favor of JSM and against the receiver on all claims.<sup>2</sup>

## **II. STANDARD OF REVIEW**

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<sup>2</sup>Bankruptcy Court Memorandum Opinion of September 7, 1995, (hereinafter "Memorandum Opinion") p. 30, ¶ 109; Bankruptcy Court Judgment of September 7, 1995.

Generally, findings of fact made by the bankruptcy judge are reviewed under the clearly erroneous standard.<sup>3</sup> Factual determinations should only be overturned if, after a full review of the record, the Court is "left with a 'firm and definite conviction' that the bankruptcy court committed a mistake."<sup>4</sup> The legal conclusions of the bankruptcy court are reviewed under the less deferential de novo standard.<sup>5</sup> If, however, the bankruptcy court "premises a finding of fact upon an improper legal standard, the finding of fact 'loses the insulation of the clearly erroneous rule.'"<sup>6</sup> As the Fifth Circuit has stated, the clearly erroneous standard "is subject to modification if the bankruptcy court invokes improper methodology in reaching its conclusion."<sup>7</sup> The Court will discuss each of the claims at issue on this appeal.

### **III. ANALYSIS**

#### **A. The 11 U.S.C. § 548(a)(1) Claim**

The receiver alleges that the estate has the right to recover the payments made to JSM under § 548(a)(1). Section 548(a)(1)

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<sup>3</sup>*In re Dunham*, 110 F.3d 286, 289 (5th Cir. 1997); *In re Bradley*, 960 F.2d 502, 507 (5th Cir. 1992).

<sup>4</sup>*Bradley*, 960 F.2d at 507.

<sup>5</sup>*Bradley*, 960 F.2d at 507. (citations omitted).

<sup>6</sup>*Bradley*, 960 F.2d at 507 (citations omitted).

<sup>7</sup>*Dunham*, 110 F.3d at 289.

provides that:

The trustee may avoid any transfer of an interest of the debtor in property, that was made or incurred on or within one year before the date of the filing of the petition, if the debtor voluntarily or involuntarily --

(1) made such transfer or incurred such obligation with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date of that such transfer was made or such obligation was incurred, indebted; ...

To void a transfer and recover funds under § 548(a)(1), the receiver must show that the transfer: (1) is a transfer of the debtor's interest in property; (2) occurred within one year of the filing; and, (3) was made with the actual intent to hinder, delay, or defraud.<sup>8</sup> The bankruptcy court found that the receiver proved the first two elements, but failed to prove the third element even though the bankruptcy court found as a matter of *fact* that Racile did act with the intent to hinder, delay, and defraud. The Court finds that as a matter of *law*, the receiver did prove that the payments were made with the intent to hinder, delay and defraud under the facts of this case.

Whether or not the transfers were made with the "actual intent to hinder, delay or defraud any entity to which the debtor was or became ... indebted" is a legal issue.

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<sup>8</sup>The bankruptcy court correctly set forth this standard; Memorandum Opinion, p. 44. See *Max Sugarman Funeral Home, Inc. v. A.D.B. Investors*, 926 F.2d 1248, 1254 (1st Cir. 1991).

Hays argues that the bankruptcy court erred as a matter of law in its finding that Racile lacked the requisite intent to defraud when it made the payments to JSM. The receiver also contends that the bankruptcy court misapplied the law set forth in § 548(a)(1) to the facts found by the bankruptcy court and erroneously required that the transferee have the intent to defraud in accepting the payments. A review of the record reveals that the bankruptcy judge found as a matter of *fact* that "Recile acted with the intent to hinder, delay, and defraud investor/creditors of Hannover/Place Vendome in effecting transfers to JSM".<sup>9</sup> However, the bankruptcy court then erroneously concluded that as a matter of *law* the receiver "failed to prove that the transfers to JSM were made with the intent to hinder, delay, or defraud."<sup>10</sup> In other words, the receiver contends that once the bankruptcy court found the requisite intent to defraud as a matter of fact, it was required, as a matter of law, to find the transfers voidable under § 548(a)(1). The Court agrees.

After reviewing the entire record and the applicable jurisprudence, this Court finds that the bankruptcy court did err as a matter of law in its analysis under § 548(a)(1). In its

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<sup>9</sup>Receiver's Original Brief, rec. doc. no. 4, p. 15, citing Memorandum Opinion, p.30, ¶ 109.

<sup>10</sup>Receiver's Original Brief, Rec. Doc. No. 4, p. 15, citing Memorandum Opinion, p. 49.

Findings of Fact, the bankruptcy court found that "Recile acted with the intent to hinder, delay, and defraud investor/creditors of Hannover/Place Vendome in effecting transfers to JSM."<sup>11</sup> However, when the bankruptcy court analyzed the receiver's claim under § 548(a)(1), it apparently required the receiver to prove its claim under a stringent badges of fraud test. The bankruptcy court held that there could be no § 548(a)(1) liability absent proof of a sufficient number of badges of fraud. The bankruptcy court further held that there can be no badges of fraud without proof of fraud by the transferee.<sup>12</sup> This Court disagrees with the bankruptcy court's application of the badges of fraud test.

Courts use the badges of fraud test because it is unlikely that a receiver will be able to present adequate direct evidence to establish the debtor's intent to defraud creditors.<sup>13 14</sup> "Therefore, courts look for common indicia . . . which have frequently bespoken

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<sup>11</sup>Memorandum Opinion, p. 30, ¶ 109.

<sup>12</sup>Memorandum Opinion, p. 49 and p. 48.

<sup>13</sup>*Kelly v. Armstrong*, 141 F.3d 799, 802 (8th Cir. 1998); *In re Armstrong*, 217 B.R. 569, 573 (Bkrtcy. E.D. Ark. 1998), citing *Brown v. Third National Bank (In re Sherman)*, 67 F.3d 1348, 1353 (8th Cir. 1995).

<sup>14</sup>Fraud or bad faith on the part of the recipient of the transferred interest is not an element of proof. *In re Armstrong*, 217 B.R. 569, 573 (Bkrtcy. E.D. Ark. 1998).

fraudulent intent in the past."<sup>15</sup> If a confluence of several badges of fraud is established, then the receiver is entitled to a presumption of fraudulent intent.<sup>16</sup> This presumption shifts the burden of proof to the transferee to prove some "legitimate supervening purpose" for the transfers.<sup>17</sup>

In this case, however, the bankruptcy court found as a matter of fact that Racile had the requisite intent to hinder, delay and defraud when he made the transfers. Therefore, the application of the badges of fraud test was unnecessary under the factual findings made by the bankruptcy court. This Court concludes that once the receiver has, as a matter of fact, proven to the bankruptcy court's satisfaction that Racile had the requisite intent, the receiver has proved the third element of § 548(a)(1). This is particularly so under the facts of the case considering the amount and frequency of the daily payments and the manner in which the payments were made by the debtors and received by JSM.

This Court does not reject the badges of fraud tests used by other courts and relied upon by the bankruptcy court. This Court

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<sup>15</sup>*Id.*

<sup>16</sup>*Id.*

<sup>17</sup>*Kelly v. Armstrong*, 141 F.3d at 802, citing *In re Acequia, Inc.*, 34 F.3d 800, 806 (9th Cir. 1994).

simply does not believe that the five badges of fraud test the bankruptcy court employed is the only means of proving the intent requirement under § 548(a)(1). This is particularly so under the facts of this case because the bankruptcy court found as a matter of fact that the debtors had the requisite fraudulent intent when they made the transfers. Thus, the Court finds that as a matter of fact and law, that the receiver has proven the third element of § 548(a)(1) and is entitled to recover the funds paid to JSM under this provision.

Because the bankruptcy court failed to apply the correct legal standard to the facts, the Court may also review the factual findings in conjunction with this claim under a de novo standard of review. A full consideration of the record reveals that the facts in evidence fully support a factual finding made by the bankruptcy court that the debtor made the transfers to JSM with the intent to defraud investor/creditors. The primary evidence of this fraudulent conduct is the fact that the transfers were made in the context of a Ponzi scheme. While it is true that Recile needed the money to complete the project, it is also clear that Recile was intentionally defrauding investors to reach that end. Such conduct cannot be condoned by the Court. The receiver has proven its claim under § 548(a)(1).

**B. The § 548(a)(2) Claim**

The Court now turns to a consideration of the receiver's claims against JSM under § 548(a)(2). Under § 548(a)(2), a transaction is avoidable if it is (1) a transfer of the debtor's interest in property; (2) made within one year of the filing of the bankruptcy petition; (3) an exchange for which the debtor received less than a reasonably equivalent value; and, (4) made while the debtor was insolvent.<sup>18</sup> The bankruptcy court concluded that the receiver proved all the elements except for the third. In effect, the bankruptcy court found that the receiver failed to show that the payments made were not reasonably equivalent to the rights received in return. Thus, the bankruptcy court concluded that money paid JSM was reasonably equivalent to the value the debtor received in keeping the property tied up for over two years.<sup>19</sup> The receiver appeals this finding.

The test for reasonably equivalent value "is whether the investment conferred an economic benefit on the debtor," and the benefit must be valued as of the time the investment was made.<sup>20</sup> The reasonably equivalent value determination is a question of fact to be reviewed under the clearly erroneous standard.<sup>21</sup> The clearly

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<sup>18</sup>*In re McConnell*, 934 F.2d 662, 664 (5th Cir. 1991).

<sup>19</sup>Memorandum Opinion, p. 51.

<sup>20</sup>*In re Fairchild*, 6 F.3d 1119, 1127 (5th Cir. 1993).

<sup>21</sup>*In re Dunham*, 110 F.3d 286, 289 (5th Cir. 1997).

erroneous standard is, however, subject to modification if the bankruptcy court fails to invoke the proper method of analysis.<sup>22</sup>

The appropriate method of review for reasonably equivalent value is set forth in *In re Fairchild Aircraft Corp.*<sup>23</sup> and *In re R.M.L., Inc.*<sup>24</sup> Under the standards set forth in these cases, the bankruptcy court must first find that the debtor received value as defined in the statute. The court must then consider whether or not the value realized sufficiently constituted reasonably equivalent value.<sup>25</sup>

The receiver contends that the bankruptcy court failed to follow this method of analysis when it reviewed the issue of reasonably equivalent value because: (1) it did not first determine value; and, (2) failed to determine value separately from its determination of reasonably equivalent value. The receiver argues that the investor/creditors received no value at all for the money the debtors paid to JSM. The receiver contends that at the time these payments were made, there was no chance that the debtors would receive any benefit for the daily payments because there was no chance the project would eventually succeed. JSM disputes this,

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<sup>22</sup>*Dunham*, 110 F.3d at 289.

<sup>23</sup>*Fairchild*, 6 F.3d at 1127.

<sup>24</sup>*In re R.M.L., Inc.*, 92 F.3d 139, 149-50.

<sup>25</sup>*Fairchild*, 6 F.3d at 1127; *R.M.L., Inc.* 92 F.3d at 150.

and contends that the bankruptcy court properly found that as a matter of fact and law, the debtors received real rights reasonably equivalent in value to the payments made.

To properly resolve this issue, this Court must first determine the appropriate standard of review. To make this determination, the Court must decide if the bankruptcy court employed the proper method of analysis; a review of methodology is de novo.<sup>26</sup> Under the facts of this case, the Court finds that the bankruptcy court failed to use the appropriate methodology in analyzing reasonably equivalent value because the bankruptcy court failed to properly consider value before determining reasonable equivalent value. To determine value correctly, the bankruptcy court must look to see if the benefit received had any economic benefit to the investor/creditors. A review of the voluminous record reveals that the bankruptcy court did not consider whether the rights received had any value to these particular creditors and investors in light of the circumstances at the time the payments were made. Instead, the bankruptcy court found that the rights were, in and of themselves, valuable. However, the bankruptcy court failed to consider the fact that the rights were useless if there was no chance that the project would ever be financed. Since the bankruptcy court did not invoke the proper methodology, the

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<sup>26</sup>*Dunham*, 110 F.3d at 289, n. 11.

bankruptcy court's factual findings are not insulated by the clearly erroneous rule.<sup>27</sup>

To determine reasonably equivalent value, the Court must first look to see if the debtor received value, in the form of an economic benefit, for the payments made. To do so, the Court must consider the circumstances that existed at the time and determine if "there was any chance that the investment would generate a positive return."<sup>28</sup> If there was no such chance at the time of the transfers that the payments would generate a positive return, then no value was conferred within the meaning of § 548(a)(2).

A thorough review of the record reveals that at the time the payments were made by the debtors to JSM, there was no chance that a sale would actually occur. The payments in cash or otherwise were made to JSM, but there was simply no way under the facts of this case that the debtors could put the financing together to make the sale happen. This is not to say that Racile did not believe that he could make the deal come together. Nor does this Court conclude that another group of investors could not have successfully developed the property. It is, however, clear from the facts of this case that **this project** had no chance of success and the rights received by the debtors conferred no benefits on the

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<sup>27</sup>*In re Bradley*, 960 F.2d 502, 507 (5th Cir. 1992).

<sup>28</sup>*R.M.L., Inc.*, 92 F.3d at 152.

investor/creditors. Since no value was received in exchange for these payments, all four elements of § 548(a)(2) were met. Thus, this Court must conclude as a matter of fact and law that the transaction is avoidable.

Even if the Court were to find that the rights had any value, the facts clearly indicate that the rights were not reasonably equivalent in value to the payments received. The bankruptcy court concluded that the agreements successfully tied up the property for over two years. A de novo review of the facts<sup>29</sup> reveals that the property was not truly tied up because JSM could easily get out of the agreement with little notice or other complications.

**C. JSM'S Defense Under § 548(c)**

Even though the bankruptcy court found the transactions were not voidable under § 548(a), it considered the "good faith" defense JSM would have made under 11 U.S.C. § 548(c) if the receiver had proven his claims. Since this Court has found the transactions voidable under § 548(a), it must review the bankruptcy court's conclusions on this defense.

Section 548(c) provides that an initial transferee who takes for value and in good faith may retain an interest transferred to the extent that the transferee gave value to the debtor in exchange

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<sup>29</sup>De novo review is appropriate here as the bankruptcy court misapplied the legal standard to the facts.

for such transfer or obligation. The key determination here is whether JSM (1) was in good faith when it took the payments; and, (2) gave value in exchange for the payments. JSM has the burden of proving good faith and value under § 548(c).

The bankruptcy court found that JSM proved it was in good faith when it received the transfers from the debtors and also proved that it gave value. The trial court concluded that Racile was a very effective salesman who convinced JSM to tie up its property for two years.

Good faith is determined on a case-by-case basis using an objective standard of what the transferee knew or should have known.<sup>30</sup> Specifically, the inquiry is whether the transferee had knowledge of the debtor's insolvency.<sup>31</sup> The Court will review these findings of fact under the clearly erroneous standard.

A review of the facts in this case reveals that JSM did indeed have notice of the debtor's insolvency. The facts of this case reveal that JSM had knowledge of the debtors fraud and JSM'S knowledge of the fraud can only lead this Court to conclude that JSM also knew that the debtor was insolvent. To reach any other conclusion would cause this Court to ignore the facts of this case.

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<sup>30</sup>*Meeks v. Greenville Casino Partners, L.P. (In re Armstrong)*, 217 B.R. 569, 575 (Bkrtcy. E.D. Ark. 1998). (citations ommited).

<sup>31</sup>*Id.*

Thus, this Court concludes JSM was on notice of the debtors insolvency and was not in good faith at the time it received the payments.

Furthermore, the circumstances surrounding the transactions were highly suspicious, and were sufficient to put JSM on notice that the debtors were possibly involved in fraudulent activity or were possibly insolvent. JSM cannot be allowed to extend its hand while closing its eyes and mind to what was really happening at the time the payments were made and received. The record shows that Clyde Fuller, who was negotiating with Recile on behalf of JSM, knew of the SEC investigation and knew that it involved allegations of fraud. JSM never looked into the debtors' ability to actually pay for the property and the evidence reveals that JSM knew that it was unlikely the project would ever be funded. Fuller admitted that he suspected wrongdoing when he stated that Recile "looked like he was guilty."<sup>32</sup> The daily payments made to JSM were in and of themselves suspicious because they were often in cash or were checks signed over from a third party. It is clear the debtors were not able to produce checks on their own accounts. Additionally, the numerous changes of corporations by the debtors should have indicated and put JSM on notice that there was a

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<sup>32</sup>Original Brief on Behalf of Appellant, rec. doc. no. 4, p. 33 (citing transcripts).

problem. The evidence further shows that as Fuller began to demand that JSM step away from the deal, he was shut out of the negotiations. The circumstances surrounding the Power Malls option were also highly suspicious. The evidence clearly shows that JSM did not accept the payments with a good faith belief that the project was legitimate. JSM may have honestly hoped that the deal would come to pass, but it must or should have known from the suspicious circumstances that it was dealing with a potentially fraudulent development scheme. Therefore, the Court finds the receiver has met its burden of proving the bankruptcy court clearly erred in its finding that JSM was in good faith.

This Court also finds that the bankruptcy court also erred in finding that JSM gave value. JSM's expert looked at the transaction as if it was a loan or other investment rather than a payment for rights to buy property. Also, the facts indicate that the bankruptcy court clearly erred in finding that the property was tied up. Because the option was day-to-day, JSM could legally cancel this option at its will.

**D. The § 544(b) Claim under Louisiana Law**

Under § 544(b) the trustee is authorized to avoid "any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowed under ... this

title." The receiver argued that transfers to JSM were voidable under the Louisiana revocatory action found in Louisiana Civil Code article 2036.

Article 2036 provides:

An obligee has a right to annul an act of the obligor, or the result of a failure to act of the obligor, made or effected after the right of the obligee arose, that causes or increases the obligor's insolvency.

The bankruptcy court found that a plaintiff in a revocatory action "must prove: (1) pre-existing and accrued indebtedness, (2) that causes or increases the insolvency of the debtor."<sup>33</sup> The bankruptcy court based its legal conclusion on *Central Bank v. Simmons*.<sup>34</sup> The bankruptcy court found that the transfers caused or increased the insolvency of the debtor and held that the receiver proved the second element of the test set forth above. The bankruptcy court failed to make a finding as to the first element of the above test. Thus, the bankruptcy court did not decide whether plaintiff established the revocatory claim.

A review of the bankruptcy court's opinion shows that the bankruptcy court failed to invoke the proper methodology in analyzing the revocatory issue; therefore, the Court will review this issue de novo.

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<sup>33</sup>Memorandum Opinion, p. 60.

<sup>34</sup>595 So.2d 363, 356.

To succeed in a revocatory action, a plaintiff must prove anteriority of the debt and insolvency of the debtor.<sup>35</sup> Thus, the receiver must prove that: (1) the debtors owed the investor/creditors before they made the transfers to JSM; and, (2) the transfers caused or increased the insolvency. The receiver met the burden of proving the anteriority of the debt, since it is clear that the debtors owed the debts to the investor/creditors before the transfers were made to JSM. The facts also support the bankruptcy court's finding that the transfers increased the insolvency of the debtors. Thus, the receiver has proven the necessary elements to revoke the transactions under Article 2036 and 11 U.S.C. § 544(b).

The Court now turns to JSM's defense which relies on Louisiana Civil Code article 2040. Article 2040 provides that "[a]n obligee may not annul a contract made by the obligor in the regular course of his business." The bankruptcy court held that the transfers were made in the ordinary course of business and could not be annulled.

It is difficult for this Court to find that Recile was acting in the course and scope of his business when at the same time the bankruptcy court held that "Recile acted with the intent to hinder,

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<sup>35</sup>La. C.C. art. 2036, cmt. (f); *See Central Bank v. Simmons*, 595 So.2d 363 (La. App. 2 Cir. 1992).

delay, and defraud investor/creditors of Hannover/Place Vendome in effecting transfers to JSM."<sup>36</sup> The Court has previously summarized the facts on the fraudulent conduct of Racile and the debtors. The Court has also set forth findings that JSM did not act in good faith, was aware or should have been aware that the debtors were acting in a fraudulent manner and knew the debtors were insolvent at the time of the payments. Such findings prevent this Court from also finding that Racile and the debtors were acting in the ordinary course of business and thus allow JSM to assert a defense to the Louisiana revocatory action.

**E. Conclusion:**

For reasons set forth above, the Court hereby reverses the decision of the bankruptcy court. This matter is remanded to the bankruptcy court for further proceedings in accordance with this opinion.

Judgment shall be entered accordingly.

Baton Rouge, Louisiana, this 4 day of February, 1999.



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FRANK J. POLOZOLA, CHIEF JUDGE  
MIDDLE DISTRICT OF LOUISIANA

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<sup>36</sup>Memorandum Opinion, p. 30, ¶ 109.

UNITED STATES DISTRICT COURT  
MIDDLE DISTRICT OF LOUISIANA

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MIDDLE DISTRICT OF LA  
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CIVIL ACTION NUMBER ~~95-2030-B~~  
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CLERK

IN RE:  
HANNOVER CORPORATION OF AMERICA  
REDWOOD RAEVINE CORPORATION  
RUBICON XXI CORPORATION  
PLACE VENDOME, INC.  
PLACE VENDOME CORPORATION  
OF AMERICA  
PENZANCE, LTD.  
ATG, INC.

CASE NUMBER 92-11010  
CASE NUMBER 92-11011  
CASE NUMBER 92-11012  
CASE NUMBER 92-11013  
CASE NUMBER 92-11014  
  
CASE NUMBER 92-11015  
CASE NUMBER 92-11016

WILLIAM G. HAYS JR., RECEIVER  
AND DISBURSING AGENT, ON BEHALF  
OF THE DEBTORS

ADVERSARY PROCEEDING

VERSUS

NO. 94-1009

JIMMY SWAGGART MINISTRIES, ET AL

J U D G M E N T

For the written reasons assigned:

IT IS ORDERED AND ADJUDGED that the decision of the bankruptcy court be reversed.

IT IS FURTHER ORDERED AND ADJUDGED that this case is hereby REMANDED to the bankruptcy court for further proceedings in accordance with the Court's opinion.

Baton Rouge, Louisiana, February 5, 1999.

Frank J. Polozola  
FRANK J. POLOZOLA, CHIEF JUDGE  
MIDDLE DISTRICT OF LOUISIANA

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UNITED STATES DISTRICT COURT  
MIDDLE DISTRICT OF LOUISIANA

CIVIL ACTION NUMBER 95-2030-B

IN RE:  
HANNOVER CORPORATION OF AMERICA  
REDWOOD RAEVINE CORPORATION  
RUBICON XXI CORPORATION  
PLACE VENDOME, INC.  
PLACE VENDOME CORPORATION  
OF AMERICA  
PENZANCE, LTD.  
ATG, INC.

CASE NUMBER 92-11010  
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CASE NUMBER 92-11014  
  
CASE NUMBER 92-11015  
CASE NUMBER 92-11016

WILLIAM G. HAYS JR., RECEIVER  
AND DISBURSING AGENT, ON BEHALF  
OF THE DEBTORS

ADVERSARY PROCEEDING

VERSUS

NO. 94-1009

JIMMY SWAGGART MINISTRIES, ET AL

AMENDED JUDGMENT

For the written reasons assigned:

IT IS ORDERED AND ADJUDGED that the decision of the bankruptcy court be reversed.

IT IS FURTHER ORDERED AND ADJUDGED that the Receiver is entitled to the return of \$84, 875.00 form Power Malls and Jimmy C. Thompson, and of \$43,000.00 from George B. Russell and Russkan Corporation.

IT IS FURTHER ORDERED AND ADJUDGED that this case is hereby REMANDED to the bankruptcy court for further proceedings in

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Anderson

accordance with the Court's opinion.

Baton Rouge, Louisiana, February 9, 1999.

*Frank J. Polozola*  
FRANK J. POLOZOLA, CHIEF JUDGE  
MIDDLE DISTRICT OF LOUISIANA

UNITED STATES DISTRICT COURT  
MIDDLE DISTRICT OF LOUISIANA

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NUMBER 95-2030

IN RE:

HANNOVER CORPORATION OF AMERICA	CASE NO. 92-11010
REDWOOD RAEVINE CORPORATION	CASE NO. 92-11011
RUBICON XXI CORPORATION	CASE NO. 92-11012
PLACE VENDOME, INC.	CASE NO. 92-11013
PLACE VENDOME CORPORATION OF AMERICA	CASE NO. 92-11014
PENZANCE, LTD.	CASE NO. 92-11015
ATG, INC.	CASE NO. 92-11016

WILLIAM G. HAYS JR., RECEIVER AND  
DISBURSING AGENT, ON BEHALF OF THE DEBTORS,  
APPELLANT

VERSUS

JIMMY SWAGGART MINISTRIES, POWER MALLS OF  
AMERICA, LTD., GEORGE B. RUSSELL,  
AND JIMMY C. THOMPSON,  
APPELLEES

Adversary No. 94-1009

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ON APPEAL FROM THE UNITED STATES BANKRUPTCY COURT  
FOR THE MIDDLE DISTRICT OF LOUISIANA

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SUMMARY OF ARGUMENT ON BEHALF OF  
WILLIAM G. HAYS, JR., RECEIVER AND  
DISBURSING AGENT, ON BEHALF OF THE DEBTORS

TAYLOR, PORTER, BROOKS & PHILLIPS, L.L.P.  
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Attorneys for William G. Hays, Receiver and  
Disbursing Agent

1. Section 548(a)(1) -- Actual Fraud.

The Bankruptcy Court erred as a matter of law in rejecting the Receiver's §548(a)(1) claim to recover \$1,502,500 paid to JSM and \$145,000 paid to Power Malls within one year of bankruptcy. The court adopted an erroneous legal standard in concluding that the Receiver failed to prove actual intent to hinder, delay or defraud creditors, despite the court's factual finding that Recile had intended to defraud creditors in effecting the transfers to JSM. The only way the court's contradictory findings can be reconciled is that the court interpreted §548(a)(1) to require proof of the transferee's fraudulent intent -- which JSM now concedes is not an element of a §548(a)(1) claim.

In analyzing the "actual intent" issue, the Bankruptcy Court used a "badges of fraud" analysis to determine whether actual fraudulent intent could be inferred from the objective facts. [See Memo. Op., p. 45.] The court eliminated two of the undisputed badges of fraud present here -- pending or threatened litigation and insolvency -- reasoning that the transferee, JSM, lacked knowledge of each. [Id., pp. 46, 48.] The court then concluded that in the absence of a sufficient number of badges of fraud, there could be no §458(a)(1) liability. [Id., p. 49.] However, in rejecting those "badges" tending to prove Recile's fraud -- because there was no "proof of fraud on JSM's part" [Id., p. 48] -- the court required proof of the transferee's fraudulent intent. In so holding, the court erred as a matter of law.

The court should have held that its factual finding of Recile's actual fraudulent intent to defraud creditors in effecting

the transfers to JSM (Findings, ¶109) compelled the legal conclusion that the Receiver met his burden under §548(a)(1), without the further need to prove additional "badges of fraud." The badges of fraud approach is merely a judicial technique used by some courts to determine whether the Debtors' actual fraudulent intent should be inferred from the objective facts, since rarely does one admit to having intended to defraud his creditors. Here, however, Recile pleaded guilty to having engaged in a criminal scheme to defraud the investor/creditors. See, In re Randy, 189 B.R. 425, 439 (Bankr. N.D. Ill. 1995) (criminal conviction for fraud established intent to defraud creditors of a Ponzi scheme). Recile made the transfers to acquire "pieces of paper" (phony loan commitments and escrowed property sales) which he used to fraudulently induce more people to invest by convincing them the project was real. [Findings, ¶109.] This technique was strikingly similar to that used by Ponzi scheme artists who make payments to early investors in order to induce other victims to invest, by creating the appearance of a genuine, profitable venture. [Mem. Op. p. 52.] Courts have unanimously held that the very existence of such a scheme is clear, almost irrebuttable evidence of a debtor's intent to hinder, delay or defraud existing or future creditors within the meaning of §548(a)(1). See Mark Benskin & Company, Inc. v. Maples, 59 F.3d 170 (6th Cir. 1995); Hayes v. Palm Seedlings Partners-A (In re Agricultural Research and Technology Group, Inc.), 916 F.2d 528 (9th Cir. 1990); In re Independent Clearing House Company, 77 B.R. 843 (D. Utah 1987); and In re Randy, supra. The court's §548(c)(1) ruling should be reversed.

2. Section 548(a)(2) -- Constructive Fraud.

The court also erred as a matter of law in holding that the Debtors received reasonably equivalent value for the transfers. In exchange for the payments, the Debtors obtained no assets that could be used in the Debtors' business or that could be used to reduce the Debtors' indebtedness. Instead, all the Debtors received were extremely short extensions of the right and the obligation to purchase real property for prices that the Debtors were incapable of paying. These short-term, intangible rights (with offsetting obligations) were not reasonably equivalent in value to the daily payments, because the Debtors were never capable of exercising those rights. The Debtors had incurred unmanageable indebtedness, and all proposals to finance the project were illusory. Thus, under Butler Aviation International, Inc. v. Whyte (In re Fairchild Aircraft Corp., 6 F.3d 1119 (5th Cir. 1993), the Debtors' payments to extend the land contracts (i.e., "investments" in the hope that the Debtors might one day buy the land), were of no value once the "hope" had objectively become a lost cause. By any objective standard the cause was lost well before September 27, 1991, the date of the first payment within a year of bankruptcy, for by then the Debtors were approximately \$25 million in debt but had almost no assets. [See Exh. B-5.]

Moreover, the daily extensions made in 1992 were worthless even if the land could have been bought. JSM's property was not taken "out of commerce." The parties never recorded the extension agreements paid for with the \$1,252,500 in daily payments; rather, JSM engaged Jimmy Thompson and Barbara Dixon to market the property

at the same time that JSM was accepting the Debtors' payments. [Findings ¶121.] Indeed, JSM sold the \$4 million parcel covered by the Bluebonnet Transfer agreement to a real buyer, General Health Corporation, which posted a \$25,000 deposit on the same day that JSM accepted a daily payment from the Debtors for the same property. [Exhs. C-86, C-80.] Hence, in reality the daily payments purchased nothing of value from the standpoint of the creditors because the payments did not effectively prevent others from buying the property. JSM would have sold its property (as it in fact did) to whomever first tendered JSM's asking price.

The \$250,000 payment to JSM on September 27, 1991, should also be avoided for the additional, independent reason that the contract under which it was paid was "null, void and unenforceable" under Louisiana law, and therefore the payment is voidable as a matter of law under §548(a)(2). In re Fairchild Aircraft Corp., supra. The closing lawyer had torn up the July 31, 1991, escrowed credit sale, and by September 27th JSM had formally terminated the Place Vendome purchase agreement in writing at least three times. Under Louisiana law Fuller's subsequent verbal rescissions of the terminations and verbal extensions of the purchase agreement had no legal effect. Hoth v. Schmidt, et al., 220 La. 249, 56 So.2d 412 (1952). The recorded Power Malls back-up option became primary automatically upon termination of the Hannover/Place Vendome agreement. Hence, the Place Vendome/JSM "September \_\_\_, 1991," agreement purporting to "fund" the (previously destroyed) July 31, 1991, sale of the property, was null, because the Power Malls' recorded option could not then be defeated "by a subsequent sale of the property to

a third person; such a sale is illegal, null and void." Versal Management, Inc. v. Monticello Forest Products Corp., 479 So.2d 477, 481 (La. App. 1st Cir. 1985). The court's dismissal of the Receiver's §548(a)(2) claim should therefore be reversed.

3. Section 548(c) -- Value.

The Bankruptcy Court clearly erred in finding that the defendants proved they gave value and were in good faith. The defendants have the burden of proving both under §548(c). The value issue is partly addressed above in the Receiver's §548(a)(2) argument. Further, the court erred as a matter of law in accepting Dr. Aguilar's testimony on value. Dr. Aguilar admitted that all he valued was the "return" received by JSM; he did not determine the market value of the property or of the options. In analyzing JSM's "return," Dr. Aguilar valued the wrong side of the transaction -- he never placed a value on any property given by JSM to the Debtors. His testimony was therefore irrelevant under §548(c).

Dr. Aguilar's testimony was legally and factually flawed for other reasons. He improperly assumed the property was continuously "tied up," without differentiating between the long term option obtained by the Debtors in mid-1990 and the 1992 day-to-day extensions of purchase agreements. He also erroneously assumed that JSM's "risk" in signing a purchase agreement was equivalent to investing over \$12 million of JSM's cash in junk bonds, despite the fact that JSM gave up neither the ownership nor possession of the property. By accepting this testimony as proof of value given to the Debtors under §548(c), the Bankruptcy Court erred as a matter of law.

4. Section 548(c) -- Good Faith.

The Bankruptcy Court also clearly erred in finding good faith. Under the law a transferee's good faith is determined by an objective standard (what the transferee objectively knew or should have known). In re Agricultural Research and Technology Group, Inc., 916 F.2d at 535-36. Notice of the transferor's possible insolvency or fraudulent purpose negates good faith. Id.; Brown v. Third National Bank (In re Sherman), 67 F.3d 1348, 1353 (8th Cir. 1995); 4 Collier on Bankruptcy, ¶548.07 (L. King 15th ed. 1987).

To reverse the Bankruptcy Court's finding of good faith on the part of the defendants, this court must apply the "clearly erroneous" standard. This does not mean that the appellate court must find there was no evidence to support the lower court's finding; rather, "[a] finding of fact is clearly erroneous when, although there is evidence to support it, the reviewing court on the entire evidence is left with a firm and definite conviction that a mistake has been committed." Hays v. State Farm Mut. Automobile Ins. Co. (In re Hannover Corp. of America), 67 F.3d 70 (5th Cir. 1995), citing Haber Oil Co. v. Swinehart (In re Haber Oil Co.), 12 F.3d 426, 434 (5th Cir. 1994).

In finding good faith the Bankruptcy Court held that (1) JSM was not on notice of the fraud because JSM had no knowledge of the SEC suit, and that (2) JSM should not have been cognizant of the overwhelming insolvency of the Debtors because JSM had no reason to ask for proof of the Debtors' financial ability to buy the property -- all of the sales were for cash. [Mem. Op. pp. 46, 56.] On these two points, alone, the court clearly erred. JSM's own

witnesses admitted they knew of the SEC suit, obtained copies of it, and asked their lawyers to determine whether it had been settled. Further, all of the proposed sales within a year of bankruptcy were to be credit sales, with JSM agreeing to finance over \$11 million of the purchase price. JSM therefore had every reason to ask for proof of ability to pay.

For the finding of good faith to stand, JSM must have believed, in good faith, that the project was real, the financing was imminent or just around the corner, and the daily payments were not part of Recile's fraud. Most importantly, JSM must not have been on notice of circumstances calling such beliefs into serious question. But the "entire evidence," particularly the testimony of JSM's own witnesses, establishes that JSM was on notice of circumstances sufficient to negate its good faith.

(a) Notice of the fraud --

"The newspapers was full of something about Sam Recile every day."

Clyde Fuller, Tr. 2/1/95, p. 198.

"He looked like he was guilty."

Clyde Fuller, Depo. Vol 2, p. 45.

On the issue of whether JSM was on notice of Recile's fraud, the evidence is overwhelming. Clyde Fuller's testimony quoted above establishes not only notice, but that JSM officials appropriately concluded that the SEC's allegations were probably true. JSM held this belief about Recile from almost the beginning of JSM's dealings with him in 1990. Fuller testified:

Q. When did you become concerned about Sam Recile?

A. I don't know that I could put a date on it, but it wasn't too long after I met him.

\* \* \*

Q. Days, weeks, months?

A. Weeks.

Fuller Depo., Vol. 1, p. 59.

One of the causes of Fuller's concern was, "He came up with too many groups that was furnishing the money to suit me." [Id., 60.] Recile's continuing lies were another cause for concern. Recile told Fuller the SEC suit had been settled, but Fuller found out through Stone Pigman that this was a lie. [Tr. 2/22/95, pp. 34-35.] Fuller eventually got so aggravated with Recile that after November, 1991, Fuller no longer wanted to speak to him, let alone do business with Recile. [Fuller Depo., Vol. 2, pp. 113-116.] Even after Fuller inexplicably resumed direct dealings with Recile in April, 1992, the lies continued: "I didn't like the way Sam Recile was lying again after we went back with him." [Id., p. 173.] Fuller further admitted:

Q. What was he lying about?

A. What hadn't he lied about.

[Id., p. 174.]

Yet JSM accepted between \$7,500 and \$10,000 per day for the extensions -- sometimes delivered by Beasley in the form of cash carried in his suit pockets, sometimes in the form of investors' checks endorsed to JSM, and sometimes in the form of wire transfers directly from Place Vendome investors. JSM's blind acceptance of these payments -- in the face of Recile's lies, and without checking the court record or asking the SEC if these payments were permissible -- was not good faith.

(b) Notice of Misuse of Corporate Form --

"Q. [E]ven though Sam changed names, you were just dealing with Sam?

A. It's the same color duck."  
Fuller Depo., p. 201.

JSM, the entity, was also on notice of the fraud through its own complicity in Recile's use of yet-to-be-formed and newly-formed corporations to evade the injunctions. On April 4, 1991, JSM learned of the corporate switch from Hannover Corporation of America (named in the Louisiana Securities Commissioner's cease and desist order) to Place Vendome, Inc. (a newly-formed Delaware corporation). [Exh. C-34.] Within a week the SEC filed suit, and Judge Livaudais pencilled in "Place Vendome, Inc." as an additional entity subject to the temporary restraining order. [Exh. A-3, p. 5.] Later, JSM received further notice of Recile's attempts to evade the injunctions. JSM gave a receipt to "Sam Recile" for the \$50,000 price of an option in favor of Royal Marque Company, Ltd. (not named in the injunction but, according to the option, having the same address as the named defendants). [Findings ¶51; Exh. C-48.] Yet the preliminary injunction froze the assets of all defendants, including Recile's.<sup>1</sup> [Exh. A-4, ¶V.] JSM had only to check the court record to discover that this payment violated the injunction and was concealed from the Special Master.

Late in 1991 -- after Fuller wanted nothing further to do with him -- Recile, Russell and Beasley concocted a scheme to use Blue-bonnet Transfer Corporation, which was yet to be formed, to front

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<sup>1</sup> Recile was permitted to spend \$4,000 per month for living expenses. [Exh. A-4, ¶VI.]

for another new Recile entity, Place Vendome Corporation of America, which had not yet been discovered by the SEC and therefore was not named in the lawsuit. Beasley told Fuller that Beasley represented an undisclosed principal and that Recile was not involved. But JSM officials -- including Jimmy Swaggart (president), Donnie Swaggart (vice president), Emile Weber (pro bono in-house attorney) and Linda Westbrook (sister-in-law/executive secretary to Jimmy Swaggart) -- knew of Recile's connection to Bluebonnet. One or more of them credited Place Vendome with the daily payments, addressed Bluebonnet correspondence to Recile's home/office, and regularly ate lunch there -- while officially advising Recile, by letter sent at Fuller's request, that JSM's deal with Recile's company was over. [Findings, ¶¶101-2, 115; Exh. C-85; Appendix Tab 19.] According to Fuller, they never told him about Recile's behind-the-scenes involvement in Bluebonnet Transfer. [Findings, ¶94.]

Only Fuller was authorized to sell the properties on behalf of JSM. But even if local JSM executives and their lawyer acted beyond their authority, JSM is nevertheless accountable for its agents' conduct. Here, JSM accepted more than \$1.5 million fraudulently obtained by Recile -- aided, in part, by JSM's agents in helping to conceal the source of the payments. "Where an agent acts beyond the scope of his authority but the principal accepts and insists on retaining the benefits and advantages of the fraudulent transaction, this constitutes a ratification." American Guaranty Co. v. Sunset Realty & Planting Co., Inc. et al., 23 So.2d 409, 451, 208 La. 772 (1944).

At oral argument, JSM's counsel tried to justify this concealment, arguing that JSM needed an intermediary, Beasley, to insulate Fuller from Sam Recile because Fuller, exasperated with Recile, no longer wanted to do business with him. But this admitted purpose in and of itself establishes JSM's bad faith. If Recile were so untrustworthy that he needed a shill to secretly front for him, then no businessman would consider genuinely "tying up" property in reliance upon nothing more than Recile's word that he could lawfully obtain the millions of dollars necessary to buy the property. Indeed, if the Bluebonnet Transfer charade could successfully be used to conceal from Clyde Fuller the fact of Recile's involvement and the true source of the daily payments, then what made the local JSM officials believe that the court, the SEC, and the Special Master were not similarly being deceived? JSM's blind acceptance of the daily payments without making any inquiry of the court or the SEC negates good faith.

(c) Notice of Insolvency.

"Q. Were you concerned about Mr. Recile's ability to perform about this time period?

A. I had doubts the first day I signed the contract."  
Fuller Depo., Vol. 2, p. 18.

"I think the only thing we were taking [for the daily payments] was cashier's checks. We had too many bounced checks."

Fuller Depo., Vol. 1, p. 169.

"[A]nytime anybody's got the right bunch of money and can't write a check, I get concerned about them."

Fuller, Tr. 2/1/95, p. 147.

JSM was plainly on notice of the Debtors' overwhelming insolvency. A June, 1991, Advocate article found in JSM's files reported the interim results of the Special Master's investigation -- the Debtors had raised more than \$7 million by issuing double-

your-money-back notes, but had acquired almost no assets. [Exh. H-2.] Yet Fuller admitted that the Recile group never presented evidence of their financial ability to buy the property. [Fuller Depo., Vol. 2, p. 19.] Recile claimed in a November, 1991, letter to JSM to have already spent \$27 million on the project. [Id., pp. 14-16.] But Fuller never questioned Recile about that figure; Fuller never asked Recile for a financial statement; and Fuller never talked with anyone about the Recile group's ability to perform. [Id., p. 17.] It is not good faith for a landowner contemplating more than \$12 million in owner-financing, to ask no questions about the buyer's ability to perform -- particularly where the prospective buyer is a known liar who cannot write a check without it bouncing, who claims to have spent tens of millions of dollars of borrowed money with no assets to show for it, and who cannot produce a financial statement.

(d) Notice of Illusory Nature of Financing "Commitments" --

"[Emile Weber] was a good information man -- he would go over and talk with Sam and tell us what's going to happen next week, who's furnishing the money and everything."

Fuller Depo., Vol. 2, p. 193.

"Q. And he would describe when the anticipated closing would be, when the money was coming in, correct?"

A. It was always right around the corner, yes, sir.

\* \* \*

I humored him....I didn't believe the Colonel. No, sir, I didn't put a lot of stock in what the Colonel told us."

Westbrook, Tr. 12/12/94, p. 273.

Critical to the court's finding of good faith was its conclusion that like Judge Livaudais, JSM was duped into believing that Recile had obtained or was about to get permanent financing. The testimony of JSM's witnesses contradict this finding. While the

SEC was kept in the dark about the identity of the would-be lenders after Don Beckner presented Weber's false affidavit to the court, JSM learned of the identity of the so-called Kiowa Indian "bank." Both Linda Westbrook and JSM's lawyer laughed about it. [Tr. 12/6/94, p. 168; Tr. 12/12/94, p. 283.]

When the daily payments began in 1992 under the Bluebonnet Transfer agreement, Fuller was never given proof of Recile's proposed financing, because Fuller believed Recile was not involved -- "No way, no fashion or form." [Fuller Depo., Vol. 2, p. 167.] The Bankruptcy Court found that the Kennedy Funding "commitment" "confirmed" the imminence of financing. Yet, Fuller never received this written "commitment." Rather, Fuller was verbally led to believe, "That's who Bluebonnet was supposed to get their money from, one of the Kennedys." [Id., p. 173.] Clearly, had someone from JSM's Baton Rouge office sent Fuller the written Kennedy "commitment" addressed to Place Vendome, Fuller would have quickly discerned that (1) the "commitment" was worthless and (2) he had been deceived about Recile's lack of involvement in the Bluebonnet deal. But Fuller never saw it or any other documentation evidencing financing. [Id., Tr. 2/2/95, p. 29.] JSM's "reliance" upon this "commitment" was not good faith.

Fuller admitted that his hope that someone would buy the property stemmed not from Recile's continual lies about financing, but from the economics of the daily payments themselves:

I said if their investors are paying \$10,000 a day surely they'll buy the property.

Fuller Depo., Vol. 2, p. 177.

JSM was on notice that these payments from investors (and the cash in Beasleys' suit pockets) may have been procured by Recile's fraudulent, criminal conduct. Yet Fuller admitted that the origin of the payments was of no concern to him and that he had no conversations with anyone (not even JSM's lawyers) about investors wiring \$10,000 per day directly to JSM. [Id., p. 205.] "If we could keep it [the daily payments] coming in, it didn't matter how I got it just so I got it." [Id., p. 163.] This cavalier attitude was not good faith in the face of the SEC's allegations of Recile's fraud, the court's injunctions attempting to halt it, and JSM's own knowledge of Recile's lies and deceit.

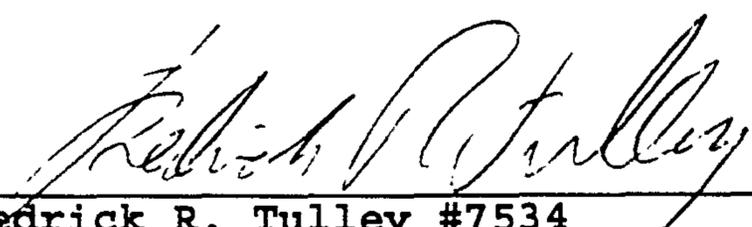
**5. Section 544(b) and the Louisiana Revocatory Action.**

The Bankruptcy Court also erred as a matter of law in rejecting Hays' §544(b) claim to recover all payments -- even those beyond one year. As the court found, the payments were part of Recile's Ponzi-like scheme. Transfers made pursuant to such a scheme are not made in the ordinary course of business as a matter of federal law; Louisiana law should be no different. See, Wider v. Wooton, 907 F.2d 570, 571 (5th Cir. 1990). Further, without notice to Hays the Bankruptcy Court took judicial notice of Recile's past real estate dealings, thereby erroneously relieving the transferees of their burden of proving the ordinary course of business defense.

On the prescription issue, Hays' knowledge of pre-September, 1991 transfers -- acquired while Hays was Special Master -- is irrelevant. He did not have capacity prior to bankruptcy to bring a Louisiana revocatory action on behalf of creditors. Now, after

bankruptcy, Hays stands in the shoes of the unsecured creditors for purposes of §544(b). Such a claim is not prescribed if under state law there existed any creditor who could have brought such a claim on the day before bankruptcy (September 23, 1992). In re Topcor, 132 B.R. 119, 126 (Bankr. N.D. Tex. 1991); In re Mahoney, Trocki & Associates, Inc., 111 B.R. 914 (Bankr. S.D. Cal. 1990). Knowledge by some creditors of the transfers, but not all, will not preclude the Trustee's §544(b) claim. In re Hunt, 136 B.R. 437, 450-1 (Bankr. N.D. Tex. 1991). Here, the evidence established that Recile defrauded all of the creditors, concealing from them the huge sums being paid to acquire extensions of "pieces of paper" that Recile then used to mislead the investor/ creditors into believing Place Vendome owned the property. Lacking knowledge of the fraudulent transfers, the defrauded creditors had three years under Louisiana law to bring a revocatory claim; and bankruptcy intervened within that three year period. See La.Civ.Code Art. 2041. The action therefore has not prescribed; and since the Debtors' insolvency was worsened by the transfers, all \$2,472,500 paid to JSM should be avoided.

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CERTIFICATE OF SERVICE

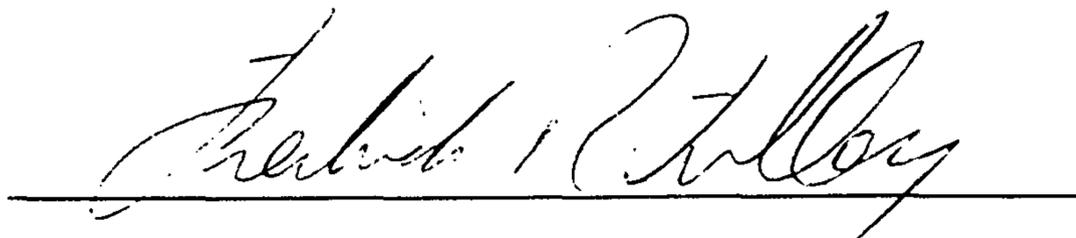
The undersigned hereby certifies that a copy of the foregoing has been sent by depositing same in the United States Mail, postage prepaid, on the 25th day of April, 1996 to the following:

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A handwritten signature in cursive script, appearing to read "Robert J. Kelly", is written over a horizontal line.