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IN THE THIRD DISTRICT COURT, SALT LAKE COUNTY

STATE OF UTAH

A. DAVID BARNES, M.D., P.C., Plaintiff, vs. FFCF INVESTORS, LLC, et al. Defendants.	**RECEIVER'S REPLY ON HIS NOTICE AND REPORT ON POTENTIAL CONFLICTS OF INTEREST** Case No. 080922273 Judge: Denise P. Lindberg
FFCF INVESTORS, LLC, Plaintiff, vs. RICHARD SMITH, et al. Defendants.	

The Receiver, Wayne Klein, at the request of the Court, submits this memorandum in reply to the response filed by James J. Warner in which Warner avers that no conflict exists in his continuing to represent Roger Taylor after also having represented FFCF and Ascendus.

COMMENTS ON BACKGROUND DISCUSSION

The response of Roger Taylor contains a lengthy recital of background information. Rather than engage in a detailed rebuttal, the Receiver notes generally that this story contains substantial differences from what the Receiver believes has been represented to the Court in the past and is not supported by documents provided to the Receiver by Taylor. For example:

1. **Consulting Agreement** Taylor's Response discloses that he had entered into a consulting agreement with Smith and FFCF. Taylor Response at 3. The Receiver believes this is the first time this has been disclosed. It is surprising that this relationship is being disclosed at this time, and was not mentioned during prior Court hearings and in prior filings with the Court. Instead, prior filings by Taylor suggested – if not outright stated – that Taylor had no role with FFCF until after Smith's reported suicide attempt in July 2008.

   The Receiver notes for the Court that Taylor did not provide a copy of this consulting agreement with his Response and the Receiver has not found a copy of the consulting agreement in any of the documents Warner provided to the Receiver. Moreover, the Receiver has not found indications that Taylor was paid "1-2% of the invested funds for his services." *Id.* While $7.3 million was invested by FFCF into LBS Advisors between February 21, 2006 and March 1, 2006, there is no indication that $70,000 to $140,000 in consulting fees were paid to Taylor under this supposed consulting agreement. No payments were made from FFCF to Taylor or Taylor Holdings before 2008. Taylor Holdings did receive one payment of $3,500 from Ascendus on February 6, 2006 and three payments totaling $3,550 from Consilium Trading Company in 2006. This

lack of payments from FFCF to Taylor before 2008 and the lack of any other payments consistent with a 1-2% consulting fee suggest that Taylor was not actually being paid consulting fees he now claims was the basis for his involvement in FFCF.

2. **Cessation of Ascendus** Taylor implies that it was only after the collapse of FFCF that he became aware that Ascendus did not terminate activity at the end of 2005. However, Taylor received two payments from Ascendus bank accounts a year and a half after he says he thought Ascendus had ceased operations. The first payment was a September 4, 2007 transfer of $75,000 into his bank account from Ascendus bank account #2153 (for which Taylor was a signatory). The second was a transfer of $650,000 to Taylor Holdings on September 7, 2007 from a newly-opened bank account, also in the name of Ascendus Capital Management. Taylor was not a signatory on this second account.[1] Copies of the bank documents showing these transfers are attached as Exhibit A.

3. **Linda Taylor** The Receiver apologizes for incorrectly stating in his Third Report that Linda Taylor was the wife of Roger Taylor. Taylor Response at 2, 11. In fact, knowing that Jennifer Taylor is the wife of Roger Taylor provides additional evidence of conflicts of interest. The bank records of Ascendus Capital Management indicate that between March

[1]Taylor seeks to pin responsibility on Smith for the failure to cease operations of Ascendus at the end of 2005. Taylor says "Smith may not have provided these [ending account statements] to all Members [of Ascendus]." Taylor Response at 3. "Mr. Smith advised Mr. Taylor that all Members had signed a closing statement acknowledging their closing balances . . . ." *Id.* "Mr. Smith . . . did not inform all Ascendus members that Ascendus had stopped operating." *Id.* This ignores the responsibility that vested in Taylor. As Taylor acknowledges in the first paragraph of his "Background" section, "Mr. Taylor was the Manager and Investment Advisor Representative. Mr. Taylor became a licensed Investment Advisor." *Id.* at 2. As the manager of the LLC and as the licensed investment adviser representative, Taylor had responsibility to ensure actions were taken to close down Ascendus and that clients were accurately informed. Taylor had responsibility to ensure the bank account on which he was a signatory did not continue to be used for another year and a half. Instead, documents identified by the Receiver in his July 10 Notice and Report and the $725,000 Taylor received from "Ascendus" in September 2007 indicate Taylor was aware the company was still operating.

2004 and March 2007, over $22,000 was paid by Ascendus to Tooele Federal Credit Union (now Heritage West Credit Union). As noted in Exhibit B, these were payments on an automobile loan by the credit union to Jennifer Taylor. It is notable that these payments continued until March 2007, over a year after Taylor says he believed Ascendus had ceased operating and after Taylor says he ceased to be involved with Ascendus. These payments indicate: a) Taylor's knowledge that Ascendus was still in operation as late at March 2007, b) Taylor was benefitting from the continuing operations of Ascendus, and c) a conflict will exist if FFCF, through the Receiver, seeks to recover these payments from Roger Taylor and his wife, while Taylor is represented by the former counsel for FFCF and Ascendus.

4. **Ability to Transfer Funds from Penson** Using disparaging language, Taylor says information provided to the Court by the Receiver regarding Ascendus being able to transfer funds from Penson to Ascendus or FFCF was wrong. Taylor Response at 12, 22, 25, and Taylor Exhibit J. Taylor insists that individual investors had to order the transfers. While Taylor's description may be accurate in theory, it appears that at least in some cases Ascendus found ways to get around this theoretical requirement.

Attached as Exhibits C and D are copies of Penson "Wire Request Forms," similar to those attached to Taylor's Response as Exhibit J. Exhibit C contains two wire request forms for the account of Daniel Schayes. The first form (#002733) is dated September 1, 2005. The signature appears to be in different handwriting and pen than other instructions written on the form. When this is compared to the second form (#002734), it appears that

the signature location is identical to that on #002733 and that Ascendus had blank wire request forms they could use to complete as they saw fit and fax to Penson to request transfers in or out of accounts. If so, this would explain how transfers were made from Penson to Ascendus without the prior knowledge of investors.

Exhibit D contains wire request forms for Gene Yamagata. While the Receiver has not found a form "signed in blank" for Mr. Yamagata, these ten forms all have an identical signature (noting their identical location on the line, stray marks, and apparent erasures on the signature). Moreover, many of these forms misspell Mr. Yamagata's name as "Yamgata" or "Yamogata." The Receiver believes Mr. Yamagata would not have signed these forms with these errors. Instead, the Receiver suspects that there was a wire transfer form signed in blank by Mr. Yamagata and that Ascendus representatives ordered wire transfers from Yamagata's account at Penson – without Mr. Yamagata making those transfers himself. It is notable that the first nine of these forms were used to instruct Penson to send money from Yamagata's account at Penson to Ascendus as payment for commissions to Ascendus.

ARGUMENT

The Receiver recognizes that the factual issues discussed above still need to be resolved. The question presently before the Court is not whose version of the facts is correct, but whether James Warner and Sara Pfrommer should be allowed to continue representing Taylor while these and other factual disputes are resolved.[2]

[2] It should be noted that most of the documents attached to and facts described in the Receiver's Notice of Potential Conflicts of Interest are not disputed by Taylor. Taylor also argues that the examples cited by the Receiver in his

The key issue before the Court is whether Rule 1.9 of the Utah Rules of Professional Conduct precludes Warner from continuing to represent Taylor.[3] Rule 1.9 (a) provides:

> A lawyer who has formerly represented a client in a matter shall not thereafter represent another person in the same or a substantially related matter in which that person's interests are materially adverse to the interests of the former client unless the former client gives informed consent, confirmed in writing.

Warner formerly represented FFCF, Ascendus, and Roger Taylor. He continues to represent Taylor. The receivership action is the same action in which Warner represented FFCF and Ascendus. In addition Warner represented FFCF in *FFCF Investors v. Richard Smith, et al.*, Civ. No. 080925879, which has now been consolidated into the present action. Thus, the only remaining question is whether Taylor's interests "are materially adverse to the interests of" FFCF and Ascendus. The Receiver believes they are.

Taylor as a "Consultant" to FFCF

Accepting as true Taylor's new claim that he was a consultant for FFCF (Taylor Response at 3), the interests of the Receiver and Taylor are adverse.

1. Taylor appears to admit that he received $1,500,000 of funds withdrawn from LBS Advisors in December 2007. Response at 15. The Receiver expects to demand of Taylor an accounting of these funds that were paid to Taylor, but which belonged to FFCF.

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report and notice only indicate limited activity by Taylor. Taylor Response at 13, 18. The Receiver did not intend to imply that these examples constituted the universe of documents showing Taylor's continued role in Ascendus; they are a representative sample.

[3] Taylor complains that because the Receiver's suggestion of a conflict was not raised in a formal motion to the court, he has been substantially prejudiced and "left to surmise what legal basis could possibly exist." Taylor Response at 23. Because the conflict of interest issue was briefed and argued to the Court extensively between December 2008 and March 2009, the Receiver believes Taylor was not left ignorant of the legal basis of a claim of conflicts of interest and disagrees that this "violates the principles of fundamental fairness and Due Process." *Id.*

2. Taylor acknowledges that he received $84,000 from FFCF in August 2008,[4] representing the balance of funds in FFCF's account with LBS Advisors. *Id.* The Receiver believes those funds belong to investors, not to Taylor. As such, the Receiver expects to demand that Taylor return these funds.

3. Between September 4, 2007 and February 15, 2008, Taylor and Taylor Holdings received $1,009,000 in payments from FFCF and Ascendus.[5] The Receiver expects to seek to recover these payments as fraudulent transfers.

4. Taylor's wife was the beneficiary of more than $22,000 in payments from Ascendus to Tooele Federal Credit Union to pay for a car for Mrs. Taylor. If Taylor had a role in approving this payment, while the manager of Ascendus, the Receiver expects to seek a return of these funds from Taylor. Even if Taylor did not have a culpable role, a suit by the Receiver against Taylor's wife for fraudulent transfer can be expected to put the Receiver in a materially adverse position against Taylor.

5. If the Receiver determines that Taylor did not act in good faith, that his consulting work (whereby he expected to receive 1-2% of amounts given to FFCF by investors) would require that he be licensed as an investment adviser, or that he failed to discharge his duties to Ascendus and FFCF properly, the Receiver could

[4] This payment went to Taylor Holdings.

[5] These payments were: a) $75,000 on September 4, 2007 from Ascendus to Roger Taylor, b) $650,000 on September 19, 2007 from Ascendus to Taylor Holdings, c) $240,000 on January 30, 2008 from FFCF to Roger Taylor, and d) $44,000 on February 15, 2008 from FFCF to Roger Taylor.

seek repayment of all funds Taylor received from the Receivership entities or from LBS. This amount exceeds $3.1 million.

In sum, the Receiver expects to bring actions against Taylor, who was the former manager of Ascendus (which the Receiver now controls) and who was a former consultant to FFCF (which the Receiver now controls). In doing so, the Receiver should not have to face an opposing counsel who previously was counsel to the companies now controlled by the Receiver. Put another way, should Taylor be permitted to hire as his attorney the former counsel for the companies who will be suing him?

Warner as Recipient of FFCF Funds

Taylor now acknowledges not only that he was the recipient of the last $84,000 that FFCF received from LBS Advisors, but that he paid these funds to Warner.[6] Taylor Response at 15-16. These funds belong to FFCF, not to Taylor or Warner.

Even if Taylor had a right to direct the expenditure of funds belonging to FFCF (which he denies having), none of those FFCF funds could be used for the representation of Taylor. The Receiver expects to seek a return of these funds from Warner. This means not only that FFCF will be suing its former attorney, but that FFCF will be suing current counsel for Taylor. Having Taylor's legal counsel as a defendant in an action brought by the Receiver creates an entirely separate set of conflicts of interest.

RECEIVER'S RECOMMENDATIONS TO THE COURT

The Receiver respectfully recommends to the Court the following:

[6] The Receiver's recollection is that Taylor represented to the Court that he was paying Warner out of his own pocket. If the Receiver's recollection is correct, the acknowledgement that Taylor gave $84,000 of FFCF funds to Warner casts doubt on Taylor's claim of charitable motives and his forthrightness to the Court.

1. That Warner and Pfrommer be disqualified from continuing to act as counsel for Taylor based on a) their prior representation of FFCF and Ascendus and b) the potential for them to be defendants in an action by the Receiver to recover funds paid to them from Receivership entities.

2. That if the Court determines to disqualify Warner and Pfrommer, they be ordered not to provide to Taylor, or any successor counsel, information that they obtained as a result of their representation of FFCF and Ascendus. This includes information gathered during the time that Warner says he was acting as a quasi-receiver. As Taylor acknowledged in Exhibit C of his Response (attached hereto as Exhibit E), Warner obtained information from investors in FFCF under the guise of representing FFCF and giving the impression he was acting in the interests of the investors. Similarly, attached Exhibit F indicates that investors sent information to Warner under the impression that he was gathering information to benefit them, rather than to benefit Taylor. As such, the fruit of this conflicted representation should not redound to the benefit of Taylor and successor counsel.[7]

DATED this 20th day of August, 2009.

R. WAYNE KLEIN #3819
Receiver for FFCF, Ascendus, and Smith Holdings

[7] The Receiver does not agree that the information Warner gained from investors while acting as counsel for FFCF and Ascendus has become "generally known." Taylor Response at 26-27. Further, the California case cited by Taylor, *Gong v. RFG Oil, Inc.*, 166 Cal.App.4th 209 (2008) is not analogous. FFCF was not a closely held corporation where two owners were fighting between themselves. The FFCF and Ascendus dispute centers on duties owed by company managers to its members and investors. The interests of those members and investors are now the responsibility of the Receiver. Warner asks the Court to legitimize his decision to have worked on both sides of this dispute – for the investors and also for Taylor.

CERTIFICATE OF SERVICE

I hereby certify that on the 20th day of August, 2009, true copies of the foregoing Receiver's Reply on Potential Conflicts of Interest and Notice to Submit were mailed to:

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