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1 UNITED STATES DISTRICT COURT  
2 SOUTHERN DISTRICT OF NEW YORK  
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3 BEACON ASSOCIATES LLC I,  
4 et al.,  
5 Plaintiffs,

6 v.

14 Civ. 2294 (AJP)

7 BEACON ASSOCIATES MANAGEMENT  
8 CORP., et al.,  
9 Defendants.

Telephone Conference

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New York, N.Y.  
January 14, 2015  
4:30 p.m.

10

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Before:

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HON. ANDREW J. PECK

Magistrate Judge

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APPEARANCES

16

HERRICK FEINSTEIN LLP  
Attorneys for Plaintiffs  
BY: ARTHUR G. JACOBY

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HISCOCK & BARCLAY LLP  
Attorneys for Defendant Income Plus Investment Fund  
BY: BRIAN E. WHITELEY

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FOLKENFLIK & MCGERITY  
Attorneys for Trustee David Fastenberg  
BY: MAX FOLKENFLIK

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AKIN GUMP STRAUSS HAUER & FELD LLP  
Attorneys for AIJED funds  
BY: MITCHELL P. HURLEY

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1 (Case called)

2 MR. JACOBY: Your Honor, in your October 31st order,  
3 at the very end it was agreed that this Court "shall retain  
4 jurisdiction over any issues that arise with respect to the  
5 distribution of funds pursuant to this order," etc.

6 We are about to do a distribution. It is going to be  
7 made next week. An issue has arisen with respect to a few  
8 investors that we need to bring to the Court's attention. I  
9 can very quickly generally explain the issue. And the reason  
10 Mr. Hurley is on the phone is because it has a huge effect upon  
11 his client.

12 To make a very long story short, there are a few  
13 situations in Beacon where -- I will explain very quickly Mr.  
14 Hurley's situation. It was an account called AIJED Associates,  
15 and it is a fund of funds. There came a point in time when  
16 AIJED created an offshore fund. AIJED Associates was an  
17 onshore fund. They created AIJED International.

18 For example, in this case, \$6.9 million in June of  
19 2005 was transferred from AIJED Associates to the new fund that  
20 was created, which was AIJED International. The question is  
21 whether moneys that were moved over include fictitious profits  
22 and therefore how to value that new account.

23 AIJED may be a little bit of a conflicted situation.  
24 For example, we have a situation where there was a partnership  
25 and the partners, say we want individual accounts, so money was

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1 transferred from the partnership to the individual accounts.  
2 What the fund had planned on doing is looking at the accounts  
3 and saying when the moneys were transferred, fictitious profits  
4 were transferred, so for net equity purposes we are not  
5 treating the account as a brand new account, or rather a  
6 related account, and therefore subtracting out what we believe  
7 are fictitious profits.

8 AIJED is a very large number. The other accounts,  
9 there are about 12, 13 other accounts, they are much smaller  
10 numbers. What we plan to do is advise every investor that  
11 falls into that category that we are taking out the fictitious  
12 profits and calculating their net equity without that money  
13 included.

14 What we do plan to do, since we are distributing next  
15 week pursuant to your order, we are going to reserve, we are  
16 going to take a reserve. For example, AIJED, but for the fact  
17 that we are taking out what we believe, and we could be wrong,  
18 but what we believe are fictitious profits, they would have  
19 gotten \$3.5 million.

20 In case your Honor rules that they are entitled to the  
21 3.5 million, we are going to reserve all of those people, and  
22 there is going to be about a \$5 million reserve. So, we are  
23 going to be distributing a lot of money, but we are going to  
24 hold back 5 million because we realize we are not going to get  
25 a ruling before it is time to distribute.

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1           Of course, in accordance with the order, your Honor  
2           wants to stay the distribution, then we would stay it. But you  
3           should know that Mr. Hurley has agreed to the process by which  
4           we would simply reserve.

5           THE COURT: Mr. Hurley, anything you want to add at  
6           this point?

7           MR. HURLEY: Just a couple of things for  
8           clarification. My client is AIJED International, the offshore  
9           fund. It was formed in 2005. There were investors in the  
10          onshore fund that redeemed and reinvested amounts from the  
11          onshore fund into the offshore fund. That was handled on the  
12          Beacon end as a book entry, but on our end we viewed it as a  
13          redemption and reinvestment.

14          Those investors left the onshore fund and went to the  
15          offshore fund. They were not a part of the onshore fund after  
16          that. The investor group of that was invested in the onshore  
17          fund is entirely different than the investor group that  
18          investing in the offshore fund.

19          To be clear, what is going on here is those funds are  
20          being treated for equity calculation purposes as if they were a  
21          single fund. We object to that. We object to the failure to  
22          give any credit for the funds redeemed and reinvested, but also  
23          in the three years that followed the creation of the offshore  
24          fund and the investment in the offshore fund accounting against  
25          the offshore fund withdrawals that were made by the onshore

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1 fund which benefited an entirely different class of investors.

2 That is kind of where the rubber hits the road.

3 In terms of the proposal for the holdback, we have  
4 agreed that we are not going to seek to stay the distribution  
5 to everybody else based on the holdback. That doesn't mean we  
6 necessarily are prepared to concede that the math has been done  
7 right with respect to all of the other folks and distributions,  
8 and I made clear expressly to all the lawyers on this call that  
9 we are not waiving any claims we might have if we discover that  
10 it wasn't done correctly. But we are not going to try and stop  
11 the distribution.

12 MR. JACOBY: Your Honor, I would like to comment on  
13 that. Mr. Hurley knows exactly what I am going to say. There  
14 was a whole procedure process. The fund gave notice to every  
15 single investor, just like Mr. Folkenflik and Mr. Whitely  
16 availed themselves of discovery. They signed a confidentiality  
17 agreement and they went through all the records of the funds,  
18 whatever they asked for, we gave to them.

19 Mr. Hurley's client could have done that. So I have a  
20 very strong objection, and he has made it very clear to me that  
21 while he is not going to stop the distribution next week, he  
22 wants to go back and examine everything from day one. And if  
23 he finds problems, he wants to assert claims against the funds.

24 He has missed that boat. He could have done this  
25 previously. You can't come to the party late. We have no

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1 problem with him reexamining the treatment of his client. We  
2 do have a problem with him attacking the treatment of other  
3 investors when it is a little bit too late for that. He had  
4 all the time in the world. His client got notice and he was  
5 advised. Every single investor was told what's going on. If  
6 they wanted to participate, they could have.

7           Also, you should know that Mr. Hurley was aware of  
8 this issue, and there was a lawyer prior to Mr. Hurley, as  
9 early as the middle of November. We are now middle of January.  
10 They could have done something in November. Everybody was  
11 aware that there was going to be a distribution in January  
12 pursuant to your order. Every investor was given notice. He  
13 didn't file an appeal of your order. He did nothing. They sat  
14 on their hands.

15           That doesn't mean that we are going to cut off his  
16 rights to look at how we are treating him. We want him to have  
17 that right, but not the right to go back and attack how we  
18 treated other investors and try to say you paid this one too  
19 much money, I now want money to go back in the pot. Judge, we  
20 can't unscramble the eggs once we have made a distribution.  
21 It's not possible.

22           MR. HURLEY: Your Honor, just a couple of things to  
23 add color to that. First, we haven't made a determination that  
24 we are going to seek to challenge anything. We don't have the  
25 information yet, so we are just reserving rights.

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1           As recently as the first week of November, my client  
2 had actually been advised that we were going to receive a  
3 distribution. It wasn't until November 17th that we were  
4 advised that calculations had been redone I guess at the  
5 instigation of other investors who do have access to all this  
6 information.

7           The final piece of color is my understanding that  
8 Beacon itself only completed its final calculations and review  
9 like two days ago.

10           I'm not saying that we are going to attack anything.  
11 I don't know what the numbers are going to show. I don't know  
12 how much of it we are going to be entitled to see. I'm just  
13 saying that we are reserving our rights in case we find that  
14 there is something amiss. Obviously, your Honor will deal with  
15 that as you will if it turns out we raise such a challenge or  
16 objection.

17           THE COURT: Let me tell you all my gut views on that.  
18 This is not a final ruling but so you know where I'm coming  
19 from. I am not inclined, once the money has been distributed,  
20 to try to claw money back from people, because that will well  
21 outweigh any likely benefit to anybody.

22           Once this distribution goes, other than this issue of  
23 treating related funds who are members of Beacon, and for that  
24 there is the reserve so the money will be there, other than  
25 that, I'm not going to look kindly and will probably rule

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1 against any attempt to recalculate somebody else's piece of the  
2 pie and say that therefore you are entitled to your 1/1000 of  
3 that money or whatever it is it would be. That's just fair  
4 warning.

5 MR. HURLEY: Understood, your Honor. Thank you.

6 THE COURT: Let me ask one other question to  
7 everybody. That is, other than the two AIJED groups, onshore  
8 and offshore, and the smaller other partnerships and people  
9 that are in a similar position, since we, you, are distributing  
10 under the procedures that I approved and ordered, until people  
11 are made whole and then going back to the valuation method, and  
12 I will use AIJED as our example here, will AIJED onshore have  
13 maxed out or not maxed out depending on what happens to the  
14 related entity? And how does that change things, if at all?

15 MR. JACOBY: If you take out their fictitious profit,  
16 they are maxed out, so they don't get any distribution.

17 MR. HURLEY: I think I need to clarify that, your  
18 Honor.

19 MR. JACOBY: Let me pause. I should have said alleged  
20 fictitious profits because it is Mr. Hurley's position that the  
21 concept of fictitious profit, it was a brand new account and  
22 therefore it doesn't matter, and in effect there were no  
23 fictitious profits transferred in.

24 MR. HURLEY: That is actually what I just ran by your  
25 Honor. The important thing you have to remember is there are

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1 two funds. Your ruling with respect to AIJED International  
2 would have a potential impact on the precise calculation of  
3 negative net equity left at onshore. Onshore, at least our  
4 understanding, is a net winner no matter what.

5 MR. JACOBY: Correct, that's right.

6 MR. HURLEY: If you were to rule in our favor with  
7 respect to the issue at offshore, then offshore would have  
8 substantial additional net equity available.

9 MR. FOLKENFLIK: Your Honor, this is Max Folkenflik.  
10 Part of the issue is what you do with the basis, if you will,  
11 of the investment that existed in the onshore when it  
12 transferred that money to offshore. If you net both of the  
13 accounts together, which is one possibility, then collectively  
14 they have a significant negative net equity. If you treat them  
15 separately, then offshore would have positive net equity and  
16 onshore have substantial negative net equity. So the answer to  
17 your question is it depends.

18 THE COURT: Great. So glad. My question is where are  
19 you going next? It sounds like you want to brief this in front  
20 of me. I will be surprised if there is actually any case law  
21 with respect to this. Otherwise, it's just a matter of logic  
22 or fairness. What do you all want to do? I'm so glad I kept  
23 jurisdiction.

24 MR. JACOBY: You can blame me for that, Judge.

25 MR. FOLKENFLIK: We want to congratulate you.

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1           MR. JACOBY: Judge, there is some dealing with this in  
2 bankruptcy court. The Madoff trustee dealt with this. Take,  
3 for example, Beacon. Beacon is a hedge fund. We have  
4 investors coming in and out all the time. The trustee looks at  
5 it all and says, we don't care what's going on among your  
6 investors when you are coming in and out, we look at you as one  
7 investor.

8           In that context there is some case law. I would  
9 concede that it is all done under principles of bankruptcy law,  
10 but there is probably nothing right on point anywhere. That is  
11 why we come to your Honor, because there is nothing on point.

12           You should know that in terms of where we go, he wants  
13 to take some discovery. The fund has no problem producing  
14 information to him that will help him understand the issues to  
15 be briefed. My problem in terms of discovery goes back to he  
16 wants to reserve his rights to say that we paid investor Smith  
17 too much, we paid investor Jones too much. He wants to  
18 basically do a de novo review of the history of fund's  
19 treatment of investors. My answer to him is you could have  
20 gotten all this information, you could have looked at all that,  
21 but your client sat on his hands.

22           It is no different from what Mr. Whiteley gave Mr.  
23 Folkenflik. We gave them information in the context of  
24 discovery subject to a confidentiality agreement on any single  
25 investor, as your Honor knows. They spent a lot of time going

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1 through it. AIJED could have done that. They missed the boat.  
2 So, I will want discovery restricted to issues that relate to  
3 the very issue that is going to be briefed.

4 MR. HURLEY: Your Honor, could we take one step back?  
5 Mr. Jacoby, I think rightly, wanted to make sure that we have  
6 this call quickly to flag the fact that we have this dispute  
7 for you. One of the things that we talked about is that we and  
8 Mr. Folkenflik and Brian's client want to talk about proposals  
9 related to things like discovery and briefing schedules. We  
10 haven't had a chance to do that yet.

11 It may be that there is nothing for your Honor to  
12 resolve on that point, that we will be able to present a  
13 proposal to you and you will either accept it or modify it. It  
14 may make sense for all of us first to try and work on issues  
15 like the one that was just flagged out among ourselves.

16 MR. JACOBY: That's fine, your Honor.

17 THE COURT: Gentlemen, I have a 5 o'clock, so let's  
18 try to wrap this up. Work out whatever you can work out. If  
19 there is a proposal or counterproposal, how about I get a joint  
20 letter from all of you by no later than a week from Friday.  
21 Does that work for everybody?

22 MR. JACOBY: It works for me.

23 MR. HURLEY: It's good for me.

24 MR. FOLKENFLIK: Fine with us, your Honor.

25 THE COURT: The reporter will probably not know who

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1 said which there, but there was unanimity on that. I will  
2 require you all to purchase this transcript, so that is of  
3 record. We will go from there. My general druther is that any  
4 discovery, whatever it is, whether it is related to AIJED  
5 onshore and offshore or anything else, be done informally  
6 outside of court just by business judgment, whatever. That is  
7 not a ruling.

8           When you are ready, there will be a motion submitted  
9 to me and a response on how to treat the related entity  
10 problem, for lack of a better word. We will see what you all  
11 work on. The acceptance of jurisdiction was not for everything  
12 and anything and full federal rules an discovery and all of  
13 that.

14           Whatever you can work out, that's great. By the 23rd  
15 of January I will expect to hear back from you with either one  
16 joint letter with everybody's position, hopefully everyone's  
17 agreement, or one letter with something that says this is the  
18 fund management's position, this is AIJED's position, etc.

19           Generally, since I work off of sending notices out via  
20 ECF, Mr. Hurley, at the appropriate time you should either  
21 enter whatever sort of appearance on the ECF system you need or  
22 make arrangements with Mr. Jacoby or somebody to make sure that  
23 any order that I send out on the ECF system gets routed to you  
24 by somebody other than me.

25           MR. HURLEY: OK.

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1           MR. JACOBY: Your Honor, as you know, we are posting  
2 every decision by your Honor, every transcript. We are going  
3 to continue to do that. And we are going to advise all  
4 investors that this is going on as well.

5           THE COURT: Very good. I will let you, Mr. Jacoby,  
6 since I suspect everyone else will free-ride on you anyway,  
7 make arrangements by going to the reporter's website and  
8 ordering the transcript.

9           MR. JACOBY: Yes.

10          THE COURT: Then posting it accordingly.

11          MR. JACOBY: We are going to take care of that. The  
12 fun will pay the invoice as well.

13          THE COURT: Very good. We are adjourned. Thank you  
14 all.

15          (Adjourned)

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