Before the
COPYRIGHT ROYALTY JUDGES
Washington, DC

In the Matters of	)	
	)	
Phase II Distribution of the 2000 2001, 2002, and 2003 Cable Royalty Funds	)	Docket No. 2008-2 CRB CD 2000-2003 (Phase II)
	)	
Phase II Distribution of the 1998 and 1999 Cable Royalty Funds	)	Docket No. 2008-1 CRB CD 2000-2003 (Phase II)
	)	
Phase II Distribution of the 2004, 2005, 2006, 2007, 2008, and 2009 Cable Royalty Funds	)	Docket No. 2012-6 CRB CD 2004-2009 (Phase II)
	)	
Phase II Distribution of the 1999, 2000, 2001, 2002, 2003, 2004, 2005, 2006, 2007, 2008, and 2009 Satellite Royalty Funds	)	Docket Nos. 2012-7 CRB SD 2000-2009; 2008-8 CRB SD 1999-2000 (Phase II)

SETTLING DEVOTIONAL CLAIMANTS' OPPOSITION TO INDEPENDENT PRODUCERS GROUP'S MOTION FOR PARTIAL DISTRIBUTION

The Settling Devotional Claimants ("SDC") submit this Opposition to Independent Producers Group's Motion for Partial Distribution of 2000, 2001, 2002 and 2003 Cable Royalties Allocated to the Program Suppliers Category and Devotional Programming Category, or Alternatively, Partial Distribution of 1999-2009 Cable Royalties and 1999-2009 Satellite Royalties.

This is the second motion that Independent Producers Group ("IPG") has filed seeking partial distribution of cable royalty funds for 2000-2003. The Judges should deny the motion for the same reasons that they denied the last one. Given the lack of agreement by all claimants to the partial distribution requested, the partial distribution may only be ordered if the Judges determine that "no claimant entitled to receive such fees has stated a reasonable objection to the

partial distribution." 17 U.S.C. § 801(b)(3)(C). Importantly, the SDC's objection need only be "reasonable" to prevail; the Judges need not necessarily agree with it. If reasonable minds can differ, then there can be no partial distribution over the SDC's objection.

The SDC's objection to a partial distribution at this time is reasonable. As the Judges have previously ruled:

> IPG, despite its assertion to the contrary, is not an established claimant to cable royalties. ... The royalties that the Judges have withheld from distribution to resolve Phase II controversies for the 2000-2003 cable royalty years remain in controversy regarding their distribution. Barring a settlement, proceedings under section 803 of the Copyright Act ... are the proper means for resolving the distribution of these royalties.

Order Denying Independent Producers Group's Motion for Partial Distribution, *In the Matter of Distribution of 2000, 2001, 2002 and 2003 Cable Royalty Funds*, Docket No. 2008-2 CRB CD 2000-2003 (Phase II) (Jan. 17, 2012) ("Order of Jan. 17, 2012"). IPG is still not an "established claimant," and the royalties withheld by the Judges for the 2000-2003 cable royalty years remain in controversy. Moreover, the SDC have reasonable concerns that IPG will not be willing or able to fulfill its obligation to return excess funds if necessary to comply with a final determination, as required by 17 U.S.C. § 801(b)(3)(C)(ii).

IPG argues that the SDC's objection to a partial distribution is no longer reasonable because IPG is now an "established claimant" by virtue of the Judges' Final Determination of Distributions: Phase II, *In re Distribution of Cable Royalty Funds 2000-2003*, Docket No. 2008-2 CRB CD 2000-2003 (Phase II) (Aug. 13, 2013) ("Final Determination"). But both the SDC and IPG have appealed the decision to the United States Court of Appeals for the District of Columbia Circuit, so the Judges' determination is not yet final and the royalties withheld from distribution remain in controversy. The Judges have previously rejected IPG's argument that it can be regarded as an "established claimant" without ever having received a final award, even

after a favorable determination by the Copyright Arbitration Royalty Panel ("CARP") that was later vacated. *See* Order of Jan. 17, 2012 ("IPG implies that it has previously established an entitlement to cable royalties by virtue of the CARP's award of [royalties] in the 1997 cable distribution. ... The Librarian subsequently vacated that decision ..., meaning that there is no final determination with respect to IPG for any cable royalties."). In the same way, it would be premature for the Judges to assume that the Final Determination will not be vacated, reversed, remanded, or otherwise modified on appeal, as both the SDC and IPG are requesting.

Although IPG asserts that the partial distribution it requests is less than the amount to which the SDC argued it was entitled, this is false. The SDC have never agreed that IPG is entitled to any award. At the preliminary hearing in this case, held before the Judges on November 13-14 and December 5, 2012, the SDC argued that the participation in proceedings before the Copyright Royalty Board and its predecessor by IPG and its sole fact witness, Raul Galaz, has been so tainted with fraud and perjury that IPG should be disqualified as a claimant in these proceedings. *See* SDC's Proposed Findings of Fact and Conclusions of Law, *In re Distribution of Cable Royalty Funds 2000-2003*, Docket No. 2008-2 CRB CD 2000-2003 (Phase II), at ¶¶ 208-217 (Jan. 15, 2013) ("SDC Proposed Findings"). The SDC also argued with respect to all of IPG's claimants in the Devotional Category except for Eagle Mountain International Church ("EMIC") that IPG failed to demonstrate that it had authority to represent its claimants when it filed claims and a petition to participate on their behalf. *Id.* at ¶¶ 2-7, 179-200. Indeed, Mr. Galaz's history of false claims and false testimony, a history that is now well-known to the Judges (*see* Final Determination at 50-51), casts his assertions of authority, often unsupported by signed authorization agreements, into considerable doubt. In the SDC's written

direct case, the SDC argued that they were entitled to 100% of the royalty funds in the Devotional Category, and that IPG was entitled to none.

The Judges disagreed with the SDC on most of its challenges to IPG's authority to represent its claimants. *See* Memorandum Opinion and Order Following Preliminary Hearing on Validity of Claims, *In re Distribution of Cable Royalty Funds 2000-2003*, Docket No. 2008-2 CRB CD 2000-2003 (Phase II) (Mar. 21, 2013) ("Preliminary Order"). The SDC therefore presented rebuttal testimony as to how the funds in the Devotional Category should be divided if the claimants allowed by the Judges in their Preliminary Order were allowed to proceed. The submission of a rebuttal case was not an abandonment of the SDC's position in the preliminary hearing. While the SDC respect the Judges' Preliminary Order, they retain the right to challenge that decision on appeal, and they have exercised that right.

The issues on appeal include, among other issues, whether IPG was qualified to participate as a party, whether any of IPG's claimants were valid joint claimants, and whether IPG had authority to represent any of them other than EMIC. *See* SDC's Statement of Issues to be Raised, *Settling Devotional Claimants v. Copyright Royalty Board*, Case No. 13-1276 (Dec. 6, 2013), attached hereto as Exhibit A. That appeal could lead to a decision vacating, remanding, or otherwise modifying the Judges' Final Determination. The SDC's objection to a partial distribution to IPG while that appeal is pending is therefore not "unreasonable."

For the same reason, IPG's suggestion that a partial distribution could be issued subject to recoupment of the amounts from its potential asserted shares in other cable and satellite royalty proceedings does nothing to satisfy the SDC's very real concern that the Copyright Royalty Board might not succeed in recouping the partial distribution if the SDC prevails on appeal. If the SDC prevails, then IPG may be largely or entirely disqualified from representing

its claimants in other proceedings, in addition to the 2000-2003 cable royalty proceedings. IPG might not be around to make good on its repayment obligations, and there is no telling what Mr. Galaz will have done with the money distributed. David Joe, an attorney for three of IPG's claimants, has previously accused Mr. Galaz of absconding with royalty funds. *See* E-mail from David Joe (July 15, 2002), attached hereto as Exhibit B; E-mail from David Joe (Oct. 4, 2004), attached hereto as Exhibit C. Neither IPG nor Mr. Joe has responded in full to requests for information about how those accusations were resolved, if at all.

Even since completing his prison term, Mr. Galaz and his various entities have continued to be embroiled in litigation regarding money laundering and fraudulent transfers of assets. In *Galaz v. Jackson*, B184916, 2006 Cal. App. Unpub. LEXIS 2175 (Mar. 16, 2006), attached hereto as Exhibit D, the California Court of Appeals affirmed a superior court judgment refusing to grant equitable relief requiring a fellow conspirator of Mr. Galaz to return money that Mr. Galaz stolen royalty funds that Mr. Galaz had given him to launder. The court found based on Mr. Galaz's own admissions that the agreement to launder the money was void as illegal, and that equitable relief was therefore unavailable. "In effect, Galaz asks us to restore stolen property to the thief because he was double-crossed by the person who agreed to fence the goods." *Galaz*, 2006 Cal. App. Unpub. LEXIS 2175, at *15.

In an adversary petition brought by his ex-wife and former co-owner of IPG, Lisa Galaz, the Bankruptcy Court for the Western District of Texas found that Mr. Galaz fraudulently transferred assets of another company they owned together, Artist Rights Foundation, LLC. *Galaz v. Galaz (In re Galaz)*, Case No., 07-53287-RBK2012 Bankr. LEXIS 5750 (Dec. 13, 2012), attached hereto as Exhibit E. The assets of the company at issue included copyright royalty funds that Mr. Galaz attempted to appropriate for himself. *Id.*

In short, Mr. Joe's allegations and Mr. Galaz's admitted history of money laundering and fraudulent conveyances of copyright royalty funds further support the reasonableness of the SDC's objection to any partial distribution.

IPG argues that the Judges have awarded the Joint Sports Claimants a distribution of cable royalty funds for 2000-2003 even though IPG has appealed the Judges' determination in that matter. There is at least one major distinction between that case and this one – the Joint Sports Claimants are long-established and firmly recognized claimants. Moreover, the amount of royalties in the Sports Category claimed by IPG is a minuscule percentage of the total amount of the distribution in that category. There is no reasonable argument that the Joint Sports Claimants would not be both willing and able to fulfill their agreement to repay amounts distributed if IPG were later successful on appeal. As to IPG, on the other hand, the SDC have ample reason to doubt that any funds distributed will never be seen again. In sum, the SDC object to and oppose any partial distribution to IPG at this time.[1]

Finally, a word should be said about IPG's request that the Judges grant the partial distribution without publishing a notice in the Federal Register. IPG argues, "because all parties with standing in any of the relevant proceedings have been served by IPG, no need exists for publication of IPG's motion in the Federal Register prior to consideration by the Judges." IPG Motion at 3-4 n. 2. Ordinarily, the SDC would agree with this proposition. As the Judges know, however, IPG has challenged the distribution of cable royalties for 1998 in the Devotional

[1] If the Judges are inclined to grant IPG any partial distribution, then only a partial distribution from the Program Suppliers Category should be made. Unlike the SDC, the MPAA-represented Program Suppliers have not appealed the Final Decision. Nevertheless, if the SDC is successful in its appeal challenging IPG's status as a valid party, then no partial distribution in any category would be appropriate.

Category – a distribution to which IPG agreed in a settlement agreement and that was subsequently disbursed to IPG-represented claimants and others in accordance with IPG's instructions. *See* Order Denying IPG's Motion for Reconsideration, *In the Matter of Distribution of the 1998 and 1999 Cable Royalty Funds*, Docket No. 2008-1 CRB CD 98-99 (Phase II) (Mar. 11, 2013); SDC's Opposition to IPG's Motion for Reconsideration of Order Granting Final Distribution of the 1998 Cable Royalty Funds (Devotional), *In the Matter of Distribution of the 1998 and 1999 Cable Royalty Funds*, Docket No. 2008-1 CRB CD 98-99 (Phase II), at 2-5 and Exs. 3 and 9-11 (Feb. 25, 2013). IPG's challenge to the 1998 cable distribution is based in part on its risible contention that that it had no notice of the distribution order to which it agreed because the order was not published in the Federal Register. IPG's Motion for Reconsideration of Order Granting Final Distribution of the 1998 Cable Royalty Funds (Devotional), *In the Matter of Distribution of the 1998 and 1999 Cable Royalty Funds*, Docket No. 2008-1 CRB CD 98-99 (Phase II) (Feb. 2013), at 2 (arguing that IPG had no "constructive notice" of the CRB order distributing funds pursuant to settlement agreement signed by IPG's president because "such orders were not published in the Federal Register ..."). IPG's willingness to play games[2] like this should cast further doubt on its responsibility as a participant in these proceedings, and therefore whether it can be trusted to return excess funds if necessary to comply with a final determination, as required by 17 U.S.C. § 801(b)(3)(C)(ii). At any rate, in light of the possibility that IPG itself might later challenge the propriety of any distribution ordered at IPG's own

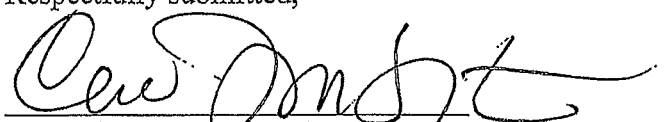
[2] IPG made its challenge without any evidence that it consulted the copyright claimant who actually received a share of the 1998 Devotional Category Settlement, EMIC. Turning a blind eye to actual facts and filing a pleading based on false claims is subject to sanctions under federal law, *see* Federal Rules of Civil Procedure, Rule 11(b), and should be not countenanced by the Judges or rewarded by the grant of IPG's Motion.

request, the Judges should not order any partial distribution to IPG without first publishing IPG's motion in the Federal Register as required by the statute.

Conclusion

For the foregoing reasons, IPG's renewed motion for partial distribution should be denied.

Respectfully submitted,



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December 16, 2013

CERTIFICATE OF SERVICE

I, Victoria N. Lynch, hereby certify that a copy of the foregoing "SETTLING DEVOTIONAL CLAIMANTS' OPPOSITION TO INDEPENDENT PRODUCERS GROUP'S MOTION FOR PARTIAL DISTRIBUTION" was sent overnight delivery via Federal Express, or when not possible, via United States Postal Service, overnight delivery, this 16th day of December, 2013 to the following:

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Victoria N. Lynch

EXHIBIT A

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

Settling Devotional Claimants	)	
	)	
Petitioner,	)	
	)	
v.	)	**Case Nos. 13-1276**
	)	**(Consolidated with**
Copyright Royalty Board,	)	**Case Nos. 13-1274,**
Library of Congress	)	**13-1275, 13-1296)**
	)	
Respondent.	)	
	)	

APPELLANT SETTLING DEVOTIONAL CLAIMANTS' STATEMENT OF ISSUES TO BE RAISED

Pursuant to the Court's Order dated November 6, 2013, Petitioner Settling Devotional Claimants ("SDC")[1] hereby submits its Statement of Issues to Be Raised.

BACKGROUND AND PROCEDURAL HISTORY

On June 3-6, 2013, the Copyright Royalty Board ("CRB") conducted a Combined Direct and Rebuttal Hearing to determine the appropriate Phase II

[1] The Settling Devotional Claimants include the following entities: Amazing Facts, Inc., American Religious Town Hall, Inc., Catholic Communications Corporation, The Christian Broadcasting Network, Inc., Coral Ridge Ministries Media, Inc., Cottonwood Christian Center, Crenshaw Christian Center, Crystal Cathedral Ministries, Inc., Evangelical Lutheran Church in America, Faith For Today, Inc., Family Worship Center Church, Inc. d/b/a Jimmy Swaggart Ministries, In Touch Ministries, Inc., It Is Written, Liberty Broadcasting Network, Inc., Rhema Bible Church aka Kenneth Hagin Ministries, Joyce Meyer Ministries, Inc. f/k/a Life In The Word, Inc., Oral Roberts Evangelistic Association, Inc., RBC Ministries, Reginald B. Cherry Ministries, Ron Phillips Ministries, Speak The Word Church International, The Potter's House of Dallas, Inc. d/b/a T.D. Jakes Ministries, and Zola Levitt Ministries.

distribution of the 2000, 2001, 2002, and 2003 royalty funds attributable to the devotional and program suppliers programming categories in Docket No. 2008-2 CRB CD 2000-2003 (Phase II). These funds were to be distributed among the parties representing the valid claimants in each category. The CRB identified the valid claimants in each category in its March 21, 2013, "Memorandum Opinion and Order Following Preliminary Hearing on Validity of Claims" (Judge Roberts, dissenting) ("MO&O"). In that MO&O, the CRB refused to disqualify Independent Producers Group ("IPG") as a party and denied parties the opportunity to amend their direct written statements based on the MO&O.[2] The hearing on June 3-6, 2013, addressed the claims of the MPAA Program Suppliers ("MPAA") and IPG in the program suppliers category, and the claims of the SDC and IPG in the devotional category.

At the hearing, each party introduced direct and rebuttal testimonial and documentary evidence in support of a proposed methodology for how the CRB should allocate the funds. However, the CRB refused to allow the SDC to submit evidence regarding its methodology at the hearing, holding that such evidence had to have been presented as part of the SDC's direct case testimony, not rebuttal testimony. After the hearing and after each party submitted proposed findings of

[2] The CRB also ordered that the appropriate allocation of funds in the sports category would be determined on the papers.

fact and conclusions of law, the CRB issued its July 10, 2013, determination of distributions among MPAA and IPG in the syndicated programming category and the SDC and IPG in the devotional category. The SDC immediately moved for rehearing. The CRB denied the SDC's motion on August 7, 2013, and issued its final determination on August 13, 2013. Following the conclusion of a 60-day review period of the CRB's decision for legal error by the Register of Copyrights, the Librarian of Congress approved the decision and caused the final distribution order to be published in the Federal Register on October 30, 2013.

ISSUED PRESENTED

The SDC seek review of the share of cable royalty funds awarded to it by the CRB in the 2000-2003 distribution proceeding. Specifically, the SDC present the following issues for this Court's review:

(1) Whether the CRB violated 17 U.S.C. § 803(a)(1) and 5 U.S.C. § 706 by acting arbitrarily and capriciously and in a manner that is unsupported by substantial evidence in the record in ruling in its Preliminary Hearing Order dated March 21, 2013, that IPG was qualified to participate as a party and that any of IPG's purported devotional clients were valid joint claimants, despite overwhelming evidence presented at the Preliminary Hearing that IPG:

(a) had engaged in fraud by including scores of entities in joint claims without legal basis and by intentionally withholding evidence establishing that it lacked authority to make many of the joint claims;

(b) did not have written authority to submit joint claims on behalf of its clients prior to filing their claims, and instead filed "place holder" claims and then subsequently requested that its clients execute back dated agreements;

(c) relied on representation agreements that were unauthenticated, not signed or dated, contained indecipherable signatures, and/or authorized IPG to collect funds only from copyright collective societies and not the Copyright Office;

(d) purported to represent clients who had terminated IPG's authorization to represent them; and

(e) relied primarily on the testimony of IPG founder Raul Galaz, who has admittedly submitted false claims and given false testimony in prior copyright royalty proceedings, and has been accused of absconding with clients' funds;

(2) Whether the CRB violated 17 U.S.C. § 803(a)(1) and 5 U.S.C. § 706 by acting arbitrarily and capriciously, abusing its discretion, and

failing to act in accordance with law and procedure required by law by prohibiting the SDC from amending its direct written statement after ruling on the validity of IPG claims;

(3) Whether the CRB violated 17 U.S.C. § 803(a)(1) and 5 U.S.C. § 706 by acting arbitrarily and capriciously, abusing its discretion, and failing to act in accordance with law and procedure required by law in excluding the rebuttal testimony of SDC witness Alan Whitt at the Direct and Rebuttal Hearing on June 3-6, 2013, on the grounds that the testimony was set forth in the SDC's rebuttal case rather than its written direct statement;

(4) Whether the CRB violated 17 U.S.C. § 803(a)(1) and 5 U.S.C. § 706 by acting arbitrarily and capriciously, abusing its discretion, and failing to act in accordance with law and procedure required by law in failing to consider the rebuttal testimony of SDC expert witness Dr. William Brown in its distribution determination issued June 10, 2013 and August 13, 2013, despite the fact that Dr. Brown's testimony was admitted into evidence at the Direct and Rebuttal Hearing without objection;

(5) Whether the CRB violated 17 U.S.C. § 803(a)(1) and 5 U.S.C. § 706 by acting arbitrarily and capriciously, abusing its discretion, and

acting in a manner that is unsupported by substantial evidence in the record in determining the appropriate allocations of the devotional funds without addressing uncontroverted record evidence that IPG's data and proposed allocation exaggerated its proposed share by:

(a) including the claims of IPG-represented claimants Jack Van Impe, Salem Baptist Church, and Bishop W.R. Portee that were expressly stricken by the CRB in its Preliminary Hearing Order dated March 21, 2013, and

(b) excluding the SDC claims of One Cubed, Jimmy Swaggart, American Religious Town Hall, and Frederick Price that the CRB deemed valid in its Preliminary Hearing Order dated March 21, 2013;

(6) Whether the CRB violated 17 U.S.C. § 803(a)(1) and 5 U.S.C. § 706 by acting arbitrarily and capriciously, abusing its discretion, and acting in a manner that is unsupported by substantial evidence in the record in permitting use of the results of IPG's methodology to determine the appropriate allocations of the devotional funds and an alleged "zone of reasonableness," despite the fact that the evidence presented at the Direct and Rebuttal Hearing on June 3-6, 2013, discredited IPG's methodology as severely flawed and deficient;

(7) Whether the Librarian of Congress violated 17 U.S.C. § 803(a)(1) and 5 U.S.C. § 706 by failing to act in accordance with law and procedure required by law, and by acting in a manner that is unsupported by substantial evidence in the record, in approving the CRB's determination concerning the allocation of the devotional funds and publishing it in the Federal Register on October 30, 2013.

Respectfully submitted,

/s/

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December 6, 2013

CERTIFICATE OF SERVICE

I, Victoria N. Lynch, hereby certify that on this 6th day of December, 2013, a copy of the foregoing "Appellant Settling Devotional Claimants' Statement of Issues to Be Raised" was served electronically through the Court's CM/ECF system on all parties who were registered users, and also served through First Class Mail, on the following:

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/s/
Victoria N. Lynch

EXHIBIT B

Lynch, Victoria N.

From: Barry.Gottfried@pillsburylaw.com
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To: Jack.McKay@pillsburylaw.com; Clifford.Harrington@pillsburylaw.com
Cc: randy.morell@cbn.org
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cc: <Barry.Gottfried@shawpittman.com>, <arnie@lutzker.com>, <dmiddlebrook@bbamlaw.com>, <psudbay@bbamlaw.com>
Subject:Letter to Barry Gottfried of July 11, 2002

Dear Ms. Oshita,

I have been provided a copy of your letter to Mr. Gottfried, a portion of which appears to allege that Mr. Gottfried was ill-motivated in contacting me, that I would now like to address. First, let me say that I don't have the benefit of the history of all of the parties' dealings with each other, which is apparently extensive, but I can comment directly on inferences and allegations drawn since the time of Mr. Gottfried's "June 26th letter to me.

I received Mr. Gottfried's letter of June 26th in the spirit I believe it was written, namely to inform me, as legal counsel for Kenneth Copeland Ministries, that a major distribution was soon to be forthcoming, and to apprise me of the three prior distributions within the United States that had been made, if for whatever reason, I was not already aware of them

I cannot fully express my gratitude for Mr. Gottfried's preparation of that letter. Marian, as you well know from conversations with me, those prior distributions were not known to me, and as it turns out, were not known to you either, at the time I confronted you with them. In previous requests to Mr. Galaz about activity in the United States, those distributions, some of which were two years old, were actually concealed from my knowledge. After my insistence that royalty statements be provided, as they should have been even without our urging, according to the contract, those distributions again went completely unmentioned. Neither Mr. Galaz, nor any of the entities he controlled, has ever apprised me of, or accounted for those distributions, which WWSG had 30 days to do under the agreement. This, of course, was beyond a breach of the agreement. This was civil fraud of the highest order and probably criminally actionable under a number of statutes and common law, to my thinking.

More alarmingly, when Raul Galaz and I last spoke about the fact that I may need to actually confirm your company's representation of KCM by speaking with the attorneys involved, Mr. Galaz ominously intimated that I should keep the conversation as short as possible, that I should "not get chatty with them," and that they would be attempting to "undo the agreement." This conversation preceded Mr. Gottfried's letter, and it became abundantly clear to me after Mr. Gottfried's letter that Mr. Galaz had been intentionally deceptive - he wanted the conversations kept short and guarded because the prior distributions that he had concealed from me might otherwise come up, not because the agreement was in jeopardy. In fact, Mr. Galaz apparently had hoped that conversations between myself and other counsel would not transpire, and that the simple letter of representation you had forwarded would suffice. Mr. Galaz attempted this last ploy after trying to first reestablish credibility by confessing his wrong-doing, distancing himself from the old person capable of deceit, affirming his loyal representation of KCM, casting the other attorneys in an overly antagonistic light, and finally implying that he had nothing at stake to gain.

But as Mr. Galaz is now aware, the past can indeed catch up. Even so, in conversations that have included weighty matters such as his sentencing and loss of licensure, Mr. Galaz has been inordinately concerned about competitors, of all things. You, for that matter, after reading your letter, also appear unduly worried about whether another person or entity will have the business of our clients. And since you have attempted to rely on my conversations with you, let me clarify that it has been you, on several occasions, probing me about whether Mr. Gottfried or Mr. Hammerman has so much as made the possibility of his services evident to me. This expenditure of your efforts frustrates me because one, in my opinion and experience as a lawyer, neither of them has done anything wrong, two, I have not been affected by the conversations, and three, there are far more productive uses of WWSG time as it relates to my Clients - we have many unresolved issues.

In the wake of these revelations, I have intended and will continue to give WWSG, under new direction, the benefit of the doubt but that will not withstand misdirection such as scurrilous charges or lack of progress with handling our issues, such as those prior distributions.

Mr. Gottfried's actions brought to light a serious violation of our rights.
I would ask, as much as I would prefer that it be unnecessary, that transactions, and the precursors of transactions, continue to be round-tabled insofar as they involve Kenneth Copeland Ministries, Benny Hinn Ministries, and Creflo Dollar Ministries, and I would hope there is no further opposition to this from WWSG.

Sincerely,
David R. Joe

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EXHIBIT C

Marian Oshita

From: "David Joe" <DJoe@brewerlawgroup.com>
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Sent: Monday, October 04, 2004 12:51 PM
Subject: Galaz vs. Oshita et al.

To Lisa Katona Galaz and Brian D. Boydston.

For those of you whom I have not met, I am an attorney in Texas known to WSG as the primary contact person for several of its devotional category claimants. Let me say at the outset that no one receiving this letter has asked that I write it, nor has any idea whatsoever that I have undertaken to review the pleadings and attachments filed in this case. Marian Oshita had mentioned the existence of this case to me fairly recently, observing a long-standing request of mine that I be informed of anything controversial involving this company, as this company has demonstrated ample reason for me to remain vigilant in recent years; and speaking for my clients, we are ever interested in the integrity and honorable name of those acting on our behalf.

That said, allow me to further state that Marian Oshita has an arm's length relationship with this firm, and that this firm's clients are not beholden to WSG for any reason, nor are they presently committed to any long-term relationship with it. There are no agendas and no underlying loyalties or axes to grind that have prompted me to write this letter. I have a limited opinion of each of you based on what you have written and plead, but I have no particular affinity for, stake, trust in, or willingness to vouch for or support any of you, motivating me.

I find it incredible that the felon Raul Galaz and his "assignee" Lisa Galaz have the gall to plead that Raul Galaz sold his interest only because he thought Marian Oshita was due some certain specific amount of money that had to be paid. Raul Galaz sold his interest because he had been humiliated, (rightfully) lost all credibility and wanted to proclaim to me and probably others that he was out of the company, so that it could potentially survive. And this he did, imploring me over the phone to see that he would be paying the price for what he did, and that he was out of the company, but that he had not besmirched or compromised his devotional category clients.

But even aside from being sentenced after duping the copyright offices and bilking copyright owners, Raul had another (even stronger) reason to release his interest. Raul had recovered literally hundreds of thousands of dollars for one of my clients, over a long period of time, but had not told me or my client about any of it. Needless to say, somewhere in the back of Raul's corrupt and greedy mind he knew there would be a day of reckoning when I discovered this fact, and indeed there was - at the worst possible time for Galaz, when a Washington DC attorney wrote me directly, relaying specific distributions that had been concealed from me, totaling an amount greater, I believe, than even that large amount he went to prison for. I am sure Raul had been petrified for quite some time that I would learn of and level this fact against him with the U.S. Attorneys, at the same time that he was vying for leniency and pleading guilty, which would have just finished him off. I could sense the desperation in his voice, and let me just tell you that both Raul and Marian in one call in particular did not simply join in harmony that Raul was divested, they proclaimed it emphatically, utterly and without the slightest hint of reservation, hoping upon hope that his divestiture and sentence would be seen by me as punishment enough, without a strong recommendation from me to my clients to abandon WSG. When I pressed for whether Raul was permanently out as an employee and also as any form of silent owner, they were ever so quick to

affirm that he was out in both respects, again, hoping their own response would be seen by me as having inflicted enough recompense.

Raul was so adamant that he was out of the company, that it even made me wonder why he would care to go to such effort with me to remain with Marian, which I now suppose had to do with the fact that his children would benefit from the company's survival after the divorce. There had been some mention that Marian was not the only owner but that she would be running the company, which casts doubt on the assertions now that there was no authorization. So it is absolutely incredible to me that Raul would dare plead otherwise, because Raul squeezed every drop of sympathy he could with me out of the fact that he was permanently out of the company.

To Lisa and Raul, let me say further that I do not know much at all of what Marian does day to day, and I don't know her well enough to fully trust her, either, but I can tell you that Raul's story about the sale in a bid to get rosiglitazone rings as false as the garbage Raul manufactured before he went to prison. If Raul is telling the truth now, then he was lying back then, because in 2002 Raul could not have been more certain and steadfast that he was totally and completely out.

To my thinking, without Marian, who eventually did repay the hundreds of thousands of dollars absconded with, there would be nothing to fight over at all in this ridiculous lawsuit you two have brewed. If this enormous, unmitigated "taking" (and spending) of my Client's moneys had not been remedied along the reasonable lines I had been insisting on, then you all would have been pointing fingers in bankruptcy court, instead of this one. And from what I know at the moment, only Marian has contributed to a modicum of integrity at WSG.

David R. Joe
Brewer Anthony Middlebrook & Dunn, PC
1702 E. Tyler St., Suite 1
Harlingen, TX 78550
phone: 956.428.5300
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EXHIBIT D

1 of 1 DOCUMENT

RAUL GALAZ, Plaintiff and Appellant, v. JULIAN JACKSON, Defendant and Respondent.

B184916

COURT OF APPEAL OF CALIFORNIA, SECOND APPELLATE DISTRICT, DIVISION FIVE

2006 Cal. App. Unpub. LEXIS 2175

March 16, 2006, Filed

NOTICE: [*1] NOT TO BE PUBLISHED IN OFFICIAL REPORTS. CALIFORNIA RULES OF COURT, RULE 977(a), PROHIBIT COURTS AND PARTIES FROM CITING OR RELYING ON OPINIONS NOT CERTIFIED FOR PUBLICATION OR ORDERED PUBLISHED, EXCEPT AS SPECIFIED BY RULE 977(B). THIS OPINION HAS NOT BEEN CERTIFIED FOR PUBLICATION OR ORDERED PUBLISHED FOR THE PURPOSES OF RULE 977.

PRIOR HISTORY: APPEAL from a judgment of the Superior Court of Los Angeles County, No. BC302194. Kenneth R. Freeman, Judge.

DISPOSITION: Affirmed.

COUNSEL: Pick & Boydston and Brian D. Boydston for Plaintiff and Appellant.

Law Offices of Eugene Paolino and Eugene Paolino for Defendant and Respondent.

JUDGES: KRIEGLER, J.; TURNER, P.J., MOSK, J. concurred.

OPINION BY: KRIEGLER

OPINION

Plaintiff and appellant Raul Galaz, having successfully defrauded owners of a television program of a large amount of royalty payments, entered into an illegal money-laundering contract with defendant and respondent Julian Jackson. Under their oral agreement, Galaz would give Jackson $ 59,000 in illicit royalty proceeds, which Jackson would place in an offshore bank account and return the funds in untraceable cash to Galaz, less a five percent commission for himself. Jackson, however, eschewed the commission and [*2] kept the cash. Galaz, aggrieved to find so little honor among thieves, sued Jackson for rescission and fraud. Following a bench trial, the court denied relief and ruled in favor of Jackson. The court refused to grant any relief under the illegal contract, and found Galaz's unclean hands precluded the equitable remedy of rescinding the illegal contract. Alternatively, the court found that Galaz's actions on the oral contract and for fraud were barred by the applicable two-and three-year statutes of limitation. [1]

1 At the close of testimony, the trial court granted Galaz's motion for a nonsuit on Jackson's cross-complaint. That ruling was not appealed.

In his timely appeal, Galaz contends (1) the trial court erred in refusing to rescind the illegal contract, and (2) his claims were not barred by the statutes of limitations. We disagree with the first contention and, therefore, have no reason to reach the second. As our courts have long recognized, an illegal contract may not serve as the foundation of *any* [*3] action, either in law or in equity. This state's courts are not in the business of helping criminals recover the proceeds of their fraudulent schemes.

STATEMENT OF FACTS

Plaintiff's Case

Galaz graduated law school in 1988 and began his practice as a California attorney, specializing in entertainment law at various law firms. Jackson was a music

producer. They met sometime between 1996 and 1997, and Galaz became Jackson's attorney and business partner. In 1998, the two formed Artist Rights Foundation, LLC, to collect unpaid royalties on behalf of a recording group called the Ohio Players.

In 1998, Galaz also started a company named Worldwide Subsidy Group to collect film and television royalties from governmental agencies on behalf of producers. Around that time, Galaz offered to collect such royalties for the owners of the television program, "Garfield and His Friends." When he was rebuffed, Galaz submitted a false claim to the United States Copyright Office to obtain the royalties for himself under an alias-Francisco Diaz, doing business as Tracee Productions. At the time Galaz made the false royalty application, he knew his conduct was illegal. Within a few [*4] years, he started receiving royalty payments under the false claim. Galaz directed that the illicit proceeds, amounting to several hundred thousand dollars, be deposited into a brokerage account under his alias.

Seeking a way to draw the money out of the account without it being traced to him under his real name, Galaz entered into an oral agreement with Jackson, whereby Galaz would transfer the funds to Jackson's offshore banking account under the Diaz/Tracee Productions alias. In consideration for a five percent commission, Jackson would transfer the funds back to Galaz in cash "almost immediately." At the time they entered into the agreement, Galaz had explained to Jackson the illicit nature of the funds and the contemplated transaction.

According to Galaz, "the agreement was that I would transfer to Mr. Jackson monies that I was holding in this account under an alias. He would transfer it to an offshore [banking account], it would return, get back to me in some fashion or another[,] cash had been described, less a five per cent fee." At Jackson's direction, Galaz wrote three checks from the brokerage account (one in the amount of $ 33,000 and two for $ 26,000) to an entity [*5] called Interceptor, Inc. and gave them to Jackson who endorsed and attempted to deposit them. Two of the checks were negotiated, but one of the $ 26,000 checks was returned. Galaz understood that his transfers to Jackson were inherently illegal. He considered Jackson to be a coconspirator.

Jackson, however, refused to return any of the money. Instead, at a meeting in July of 2000, Jackson told Galaz, "'Look, you're lucky if you get anything back.'" At the same meeting, Jackson told Galaz that he needed to keep the money for a year before he could return it. Galaz felt he had no choice but to agree and wait: "I really didn't have a choice because I couldn't exactly go in and sue him for illicitly received monies . . . ." Galaz made several more unsuccessful attempts to contact Jackson, but never received any portion of the $ 59,000 he had transferred to Jackson.

In late 2001 or early 2002, Galaz learned that the Federal Bureau of Investigation was investigating him concerning the false claim for "Garfield and His Friends" royalties. In his meeting with the federal investigators, Galaz admitted his illegal conduct. He entered into a pre-indictment plea agreement to one count of mail [*6] fraud and was sentenced to an 18-month term under the Federal Sentencing Guidelines. At the time of the underlying trial, he had been released and was serving a three-year term of supervised release. According to Galaz, if he prevailed in his lawsuit, he would keep none of the damages award. Rather, he would apply it to legal fees and his federal restitution obligation, which amounted to approximately $ 300,000.

Defense Case

Jackson testified that he had hired Galaz as legal counsel to help draft and negotiate his music production agreements. Jackson denied having anything to do with the three checks from Galaz to Interceptor, Inc., an entity Jackson had never heard of. The endorsements on the checks were not his signature. Jackson believed Galaz's contrary testimony was motivated by a desire to prevent Jackson from sharing in the $ 28 million in profits that their Ohio Players venture would realize. Jackson never had an "offshore" or foreign bank account. According to Jackson, he and Galaz never had any communications after early 1999.

Trial Court Findings

Having listened to the testimony of the two witnesses, Galaz and Jackson, the trial court found [*7] Galaz had testified truthfully, while Jackson had given false testimony. Nevertheless, the trial court found two independent legal impediments to Galaz's claims. First, the underlying oral agreement upon which all the claims were based was illegal and could not be enforced, whether under contract or tort theories. Moreover, the equitable remedy of rescission was not available because of Galaz's "unclean hands." Second, the claims were barred by the applicable statutes of limitation-two years for recovery on an oral contract and three years for fraud. The trial court gave the parties the opportunity to brief those issues, explaining that if Galaz could not overcome the two specified legal impediments, it would rule in favor of Jackson.

On March 23, 2005, having considered the parties' evidence and the post-trial briefs, the trial court entered judgment in favor of Jackson and against Galaz.

DISCUSSION

Plaintiff's Action For Rescission is Barred by The Doctrines of In Pari Delicto and Unclean Hands; He May Not Use His Illegal Contract as the Basis for a Tort Action

Galaz premises his rescission and fraud claims on the same illegal money-laundering contract with [*8] Jackson. We have recently set out the general principles regarding illegal contracts: "California statutes require that a contract have 'a lawful object.' (*Civ. Code, § 1550, subd. (3)*; see *Civ. Code, § 1596.*) Otherwise the contract is void. (*Civ. Code, § 1598.*) *Civil Code section 1668* provides that a contract that has as its object a violation of law is 'against the policy of the law.' *Civil Code section 1667* states that 'unlawful' is '1. Contrary to an express provision of law; [P] 2. Contrary to the policy of express law, though not expressly prohibited; or, [P] 3. Otherwise contrary to good morals.' (See also *Civ. Code, §§ 1441* ['A condition in a contract, the fulfillment of which is . . . unlawful . . . is void'], 1608 ['If any part of a single consideration for one or more objects, or of several considerations for a single object, is unlawful, the entire contract is void'].) California courts have stated that an illegal contract 'may not serve as the foundation of any action, either in law or in equity' (*Tiedje v. Aluminum Taper Milling Co. (1956) 46 Cal.2d 450, 453-454),* [*9] and that when the illegality of the contract renders the bargain unenforceable, '"the court will leave them [the parties] where they were when the action was begun"' (*Wells v. Comstock (1956) 46 Cal.2d 528, 532*; see also *Kolani v. Gluska (1998) 64 Cal.App.4th 402, 408* ['illegal contracts are void'], disapproved on other grounds in *Bonifield v. County of Nevada (2001) 94 Cal.App.4th 298*)." (*Kashani v. Tsann Kuen China Enterprise Co. (2004) 118 Cal.App.4th 531, 541*; see also *Wong v. Tenneco, Inc. (1985) 39 Cal.3d 126, 135, 216 Cal. Rptr. 412* ["'"No principle of law is better settled than that a party to an illegal contract cannot come into a court of law and ask to have his illegal objects carried out . . . ."'"]; *Lewis & Queen v. N. M. Ball Sons (1957) 48 Cal.2d 141, 150* ["the courts generally will not enforce an illegal bargain or lend their assistance to a party who seeks compensation for an illegal act"]; *Tri-Q, Inc. v. Sta-Hi Corp. (1965) 63 Cal.2d 199, 218, 45 Cal. Rptr. 878* [courts will "withhold relief under the terms of an illegal contract" that "is [*10] violative of public policy"].)

As the Restatement Second of Contracts puts it, the general rule is that "a party has no claim in restitution for performance that he has rendered under or in return for a promise that is unenforceable on grounds of public policy unless denial of restitution would cause disproportionate forfeiture." (*Rest.2d Contracts, § 197,* p. 71.) This is based on the rationale that "if a court will not, on grounds of public policy, aid a promisee by enforcing the promise, it will not aid him by granting him restitution for performance that he has rendered in return for the unenforceable promise. Neither will it aid the promisor by allowing a claim in restitution for performance that he has rendered under the unenforceable promise. It will simply leave both parties as it finds them, even though this may result in one of them retaining a benefit that he has received as a result of the transaction." (*Rest.2d Contracts, § 197, com. a,* p. 71.)

Here, as the trial court found, the money-laundering contract fell firmly within the general rule, precluding relief. Galaz's own testimony established [*11] that the underlying agreement between him and Jackson had a single, illegal object-the concealment of the fruits of a fraudulent transaction by illegal means. Indeed, Galaz originated the scheme and Jackson was fully aware of its illicit nature at all times.

Seeking to avoid application of the general rule, Galaz-as he did below-urges application of a recognized exception: "'By the weight of authority where money has been paid in consideration of an executory contract which is illegal, the party who has paid it may repudiate the agreement at any time before it is executed and reclaim the money. . . .' [Citations.]" (*Murphy v. San Gabriel Mfg. Co. (1950) 99 Cal. App. 2d 365, 368-369.*) Galaz argues that the illegal aspect of his agreement with Jackson remains executory because Jackson never repaid him in laundered funds. Even if we were to agree with that characterization, we would find the exception wholly inapplicable to Galaz.

First, as the *Murphy* court explained, the exception applies only when "'it is the duty of the court in furtherance of justice to aid one not in *pari delicto,* though to some extent involved in the illegality . . . .' [Citations. [*12]]" [2] (*Murphy v. San Gabriel Mfg. Co., supra, 99 Cal. App. 2d at p. 369*; *Randall v. Beber (1951) 107 Cal. App. 2d 692, 705* ["A right to recover the consideration paid is not a right which the law accords a purchaser who is *in pari delicto,* if the consideration was illegally collected"].) The fact that Jackson was guilty of an additional layer of duplicity in no way absolves Galaz from being a party to the wrong. To the contrary, Galaz and Jackson were co-authors of the illegal agreement; both shared the same degree of guilty knowledge; both would have shared in its illegal proceeds if the scheme had not miscarried-and it was Galaz whose prior fraudulent scheme provided the source of the funds that fueled the money-laundering agreement. In short, this was nothing like the situation in *Murphy*, where the plaintiff was not a knowing participant in the illegality infecting the underlying agreement-in fact, the plaintiff was more accurately described as a victim thereof. (See *Murphy v. San Gabriel Mfg. Co., supra, 99 Cal. App. 2d at pp. 366-368.*)

2 Similarly, as the Restatement Second of Contracts explains, a party may have a claim for restitution under an unenforceable contract "if he did not engage in serious misconduct" and "he withdraws from the transaction before the improper purpose has been achieved." (*Rest.2d Contracts, § 199*, p. 76.) This exception would not apply to Galaz because he did engage in serious misconduct and he failed to withdraw from the illegal transaction in a timely fashion. "To come within the rule, a party must actually withdraw by refusing any further participation in or benefits from the transaction. It is not enough that the achievement of the purpose has been prevented by circumstances beyond his control." (*Rest.2d Contracts, § 199, com. a*, p. 77.)a

[*13] Second, and more fundamentally, the fact that Galaz never had any legal right to the $ 59,000 he seeks to recover serves to distinguish his case from every California case finding an exception to the general rule that precludes a party who is in pari delicto from rescinding or recovering on an illegal contract. (See *Kashani v. Tsann Kuen China Enterprise Co., supra, 118 Cal.App.4th at pp. 541-542*, listing exceptions.) Nor is this a situation in which the underlying illegality could be fairly described as a mere "*malum probihitum*" regulatory technicality, and where enforcement of the contract would not be contrary to the purpose of the regulatory scheme. (*Asdourian v. Araj (1985) 38 Cal.3d 276, 292-294, 211 Cal. Rptr. 703*; see *Rest.2d Contracts, § 197, com. b*, p. 72 ["The exception is especially appropriate in the case of technical rules or regulations that are drawn so that their strict application would result in such forfeiture if restitution were not allowed"].)

The decision in *Morrison v. Willhoit (1944) 62 Cal. App. 2d 830* provides the proper analogy to Galaz's case. In *Morrison* [*14] , the plaintiff unsuccessfully sought to recover on two promissory notes she had executed for the purpose of defrauding creditors. As with Galaz and Jackson, the parties in *Morrison* were aware of the illegal nature of the transaction at the time of its conception: "[Plaintiff] was not only *in pari delicto;* she herself conceived the purpose of moral obliquity and invited [defendants] Willhoit and Gibson to her home where she confided her fraudulent design to them and prevailed upon them to enter into a contract violative of good morals. The authorities cited by defendants [citations] are in point. One who transfers his property for the purpose of cheating his creditors will plead in vain for relief from his own chosen distress. [Citation.] Even though it were unfair for a transferee under a fraudulent conveyance to keep the property as against the fraudulent grantor, still equity is so jealous of its principles that it turns away at its very threshold those who have been parties to wrongs. [Citation.] The burden is upon the complainant in equity to prove that, so far as the transaction involved in his demands is concerned, he is free from vice. Equity interposes a barrier [*15] against such an inequitable demand for the sake of the law itself, and upon ascertaining the fraudulent nature of the original transaction it will deny relief to a demand stemming from the original, tainted arrangement. [Citation.] . . . The notes in suit had their genesis in no place and arose out of no event other than the transfer of plaintiff's properties in 1929 for the purpose of defrauding a creditor." (*Morrison v. Willhoit, supra, 62 Cal. App. 2d at pp. 837-838.*)

In effect, Galaz asks us to restore stolen property to the thief because he was double-crossed by the person who agreed to fence the goods. To do so would be contrary to our courts' time honored precedent. "The courts generally will not enforce an illegal bargain or lend their assistance to a party who seeks compensation for an illegal act. The reason for this refusal is not that the courts are unaware of possible injustice between the parties, and that the defendant may be left in possession of some benefit he should in good conscience turn over to the plaintiff, but that this consideration is outweighed by the importance of deterring illegal conduct. Knowing that they will receive no help from [*16] the courts and must trust completely to each other's good faith, the parties are less likely to enter an illegal arrangement in the first place." (*Lewis & Queen v. N. M. Ball Sons, supra, 48 Cal.2d at p. 150.*)

DISPOSITION

The judgment is affirmed. The parties are to recover their own costs on appeal.

KRIEGLER, J.

We concur:

TURNER, P.J.

MOSK, J.

EXHIBIT E

IN RE: LISA ANN GALAZ, DEBTOR; LISA ANN GALAZ VS. RAUL GALAZ, ALFREDO GALAZ, SEGUNDO SUENOS, LLC VS. JULIAN JACKSON

CASE NO. 07-53287-RBK, CHAPTER 13, ADVERSARY NO. 08-5043-RBK

UNITED STATES BANKRUPTCY COURT FOR THE WESTERN DISTRICT OF TEXAS, SAN ANTONIO DIVISION

2012 Bankr. LEXIS 5750

December 13, 2012, Decided
December 13, 2012, Filed, Entered

PRIOR HISTORY: *Galaz v. Galaz (In re Galaz), 480 Fed. Appx. 790, 2012 U.S. App. LEXIS 14261 (5th Cir. Tex., 2012)*

COUNSEL: [*1] For Lisa Ann Galaz (07-53287-rbk), Debtor: Benjamin R. Bingham, Bingham & Lea, PC, San Antonio, TX; H. Anthony Hervol, Law Office of H. Anthony Hervol, San Antonio, TX.

For Denise Vernon (08-05043-rbk), Plaintiff: Richard P. Corrigan, San Antonio, TX; Todd A. Prins, Prins Law Firm, San Antonio, TX.

For Lisa Ann Galaz (08-05043-rbk), Plaintiff: Benjamin R. Bingham, Royal B. Lea, III, Bingham & Lea, P.C., San Antonio, TX; H. Anthony Hervol, Law Office of H. Anthony Hervol, San Antonio, TX.

For Lisa Ann Galaz (08-05043-rbk), Defendant: Benjamin R. Bingham, Royal B. Lea, III, Bingham & Lea, P.C., San Antonio, TX; H. Anthony Hervol, Law Office of H. Anthony Hervol, San Antonio, TX.

For Raul Galaz, Alfredo Galaz, Segundo Suenos, LLC (08-05043-rbk), Defendants: J. Scott Rose, Karen A. Monsen, Toni Price, Jackson Walker, L.L.P., San Antonio, TX.

Julian Jackson (08-05043-rbk), 3rd Pty Defendant, Pro se, Marina Del Rey, CA.

JUDGES: Ronald B. King, United States Chief Bankruptcy Judge.

OPINION BY: Ronald B. King

OPINION

OPINION ON DAMAGES

In 2007, Lisa Ann Galaz ("Debtor") filed a petition under Chapter 13 of the Bankruptcy Code. On April 22, 2008, Debtor brought this adversary proceeding against her ex-husband, Raul Galaz ("Galaz"); [*2] his father, Alfredo Galaz ("Alfredo"); and Segundo Suenos, LLC ("Suenos") [1] (collectively, "Defendants"). Julian Jackson ("Jackson") was joined as a third-party defendant, asserting his claims in concert with Debtor. Debtor's claims arose from Galaz's fraudulent transfer of the assets of Artist Rights Foundation, LLC ("ARF") to Suenos in June 2005. ARF was a California limited liability company formed by Galaz and Jackson in which Debtor and Jackson held ownership interests. The primary contention of Debtor and Jackson (the "Claimants") was that the Defendants defrauded them of the value of royalties to the music of the recording group, The Ohio Players (the "Royalties"), which ARF acquired and held as its primary asset until the fraudulent transfer occurred.

1 Although not apparent from the record, "Segundo Suenos" was most likely formed with the intention of reading "Segundo Sueños," which is Spanish for "Second Dreams." This Opinion will use the spelling used by the entity itself.

On November 12, 2010, the Court found that the transfer of assets from ARF to Suenos was invalid, that it constituted a fraudulent transfer under the Texas Uni-

form Fraudulent Transfer Act, and that Galaz [*3] breached the fiduciary duties he owed to Jackson and ARF. (Case No. 08-5043, ECF No. 344) The Court set aside the transfer from ARF to Suenos and affirmed ownership of ARF to be as follows: 50% to Jackson, 25% to Debtor, and 25% to Galaz as an economic interest only. The Court awarded actual and exemplary damages to the Claimants, and the Defendants subsequently appealed to the United States District Court for the Western District of Texas. (Case No. 08-5043, ECF No. 347)

On April 19, 2012, the Honorable Harry Lee Hudspeth, United States District Court, Western District of Texas, issued a Memorandum Opinion upholding the decision of the Court on the merits of the case, but vacating the damage awards and remanding the case for reconsideration of the awards of actual and exemplary damages. The District Court stated:

> The Bankruptcy Court provided no explanation as to how it calculated actual damages, and it is unclear whether the Court considered Segundo Suenos's expenses and found them unreliable or if the expenses were not taken into consideration at all. Thus it is impossible for this Court to conduct a meaningful review of the calculation of actual damages . . . .

(Case No. 08-5043, [*4] ECF No. 484)

Because the award of exemplary damages "appear[ed] to be based upon the finding of actual damages," that award was vacated as well. Accordingly, in addition to the Opinion entered on November 12, 2010, the Court hereby makes the following findings and conclusions under *Rule 7052* with regard to actual and exemplary damages.

FACTS

Galaz graduated from law school in 1988 and began practicing law in California, specializing in entertainment law at various law firms. Jackson was a music producer. After the two met, Galaz became Jackson's attorney and business partner. In 1998, the two formed ARF to collect unpaid royalties of the Ohio Players. Raul was to contribute his expertise as an entertainment and copyright lawyer, and Jackson had a relationship with one of the members of the band. Together, Galaz and Jackson successfully secured all rights to the Ohio Players' music catalogue. Initially, the Royalties did not generate any revenue.

In May 2002, Debtor and Galaz divorced and executed an agreement (the "Divorce Decree"), which stipulated that Galaz was to assign one-half of his 50% interest in ARF to Debtor, leaving both Debtor and Galaz with a 25% ownership interest in ARF. [*5] Because Galaz transferred half of his interest without Jackson's consent in violation of the company's written operating agreement (the "Operating Agreement"), Debtor received an economic interest only with no management or voting rights. In October 2004, Galaz sent a letter to Jackson (the "Demand Letter"), insisting that Jackson send money to cover expenses incurred by ARF in accordance with provisions in the Operating Agreement for a capital call upon ARF's members. [2] (Def.'s Exs. 2, 4) Galaz claimed that he had incurred out-of-pocket expenses of over $8,500, that a tax debt of more than $5,000 existed, and that he had not been paid anything for his "services." (Def.'s Ex. 4) He demanded that Jackson remit $6,750 to him personally for his share of the expenses, plus an amount equal to the fair value of his services, which he described as several hundred hours at a rate of $250 per hour. Galaz made no such demand upon Debtor and did not contribute any personal funds for his proportionate share of the expenses and taxes.

> 2 Section 2.1 of the Operating Agreement provided that, in addition to an initial cash contribution to ARF, additional contributions to the capital of ARF would be [*6] required of its members in amounts sufficient to maintain the business of ARF and in proportion to each member's ownership interest in the company. (Def.'s Ex. 2)

At trial Galaz argued that providing notice to Jackson of the transfer to Suenos was not necessary because Jackson's membership interest in ARF had been terminated as a result of his failure to respond to the Demand Letter or contribute his share of the expenses and taxes. It is clear, however, that Galaz knew that the address to which he sent notice was no longer valid. In December 2003, Jackson received a complaint in the mail, styled "Raul Galaz vs. Julian Jackson," at his correct address in Marina Del Rey, California, and a second complaint at his Nevada address. (Def.'s Ex. 72) Despite providing notice to Jackson at the correct address in those matters, in October 2004 Galaz sent the Demand Letter to Jackson's previous address listed in the Operating Agreement in Los Angeles, California. (Def.'s Exs. 2, 4) As was fully intended by Galaz, Jackson never received the letter or remitted any money to Galaz. (Def.'s Ex. 72) Furthermore, Galaz knew the letter would not result in the notice actually reaching Jackson because Galaz [*7] was aware that Jackson no longer resided at that address. The two were pitted against one another in litigation immediately prior to the transfer, and this was expressly referenced in the letter. (Def.'s Ex. 4)

On June 3, 2005, Galaz fraudulently transferred all of ARF's rights to Suenos by way of a three-page document titled "Agreement of Assignment and Transfer of Assets of Artist Rights Foundation, LLC, (California)." (Def.'s Ex. 23) At the time of the transfer, Suenos was not organized as a business entity under the laws of any state. On September 28, 2005, three months after the transfer, Galaz assisted his father in filing the documents required to establish Suenos as a limited liability company ("LLC") with the state of Texas. (Pl.'s Ex. 9) Galaz did not inform the Claimants of the transfer or otherwise obtain their consent. The terms of the transfer purportedly obligated Alfredo and Suenos to pay the liabilities Galaz recited in the Demand Letter: Galaz's out-of-pocket expenses, expenses for Galaz's "services," and the past-due California franchise taxes. The Royalties soon began to generate a substantial amount of revenue. From the time of transfer to the time of trial, Suenos's [*8] gross revenue from the Royalties totaled nearly one million dollars, but all of the money was paid to the Defendants, with the Claimants receiving no share of the profits despite their ownership interests in ARF.

After making the fraudulent transfer, Galaz wrongfully dissolved ARF by filing a Certificate of Cancellation with the California Secretary of State on December 27, 2006. (Def.'s Ex. 5) Galaz's dissolution was wrongful because the Articles of Organization and the Operating Agreement specifically listed events which, upon their occurrence, required the dissolution of the company. [3] (Def.'s Exs. 1, 2) None of those conditions were met when Galaz dissolved ARF. [4] Because ARF was wrongfully dissolved without any notice to Jackson, there was no winding up of its affairs as contemplated by the Operating Agreement. (Def.'s Ex. 2) As a result of Galaz's wrongful dissolution, ARF ceased its active existence as an LLC, and the assets of ARF have devolved to the individual owners of the company. (Case No. 08-5043, ECF No. 344)

> 3 The Operating Agreement provided that dissolution was to occur upon the death, withdrawal, resignation, retirement, insanity, bankruptcy, or dissolution of any member. [*9] (Def.'s Ex. 2) It continued to define certain conditions of dissolution, which included: (1) the aforementioned events; (2) the entry of a decree of judicial dissolution pursuant to the California Corporate Code; (3) a vote of members holding at least 51% of the membership interests; or (4) the sale of all or substantially all of ARF's assets. (*Id.*)
>
> 4 The purported transfer from ARF to Suenos did not constitute the sale of all or substantially all of the company's assets because the Operating Agreement did not authorize the transfer without approval of the majority of membership interests and Galaz did not provide notice to Jackson, whose vote of approval for the transfer was necessary. Because Debtor's membership interest in ARF at that time was economic only, she did not have the voting rights necessary to approve or disapprove a sale of ARF's assets. (Def.'s Ex. 2)

This Court set aside the transfer to Suenos and awarded damages to the Claimants on three different theories: (1) the transfer from ARF to Suenos was invalid; (2) the transfer violated the Texas Uniform Fraudulent Transfer Act ("TUFTA"); and (3) Galaz breached the fiduciary duties he owed to Jackson and ARF. The District [*10] Court affirmed the holding of the Court on all three theories. At issue is the amount of damages awarded to the Claimants for the Defendants' fraudulent transfer and breach of fiduciary duty with respect to Jackson.

ANALYSIS

1. *Actual Damages Based on the Value of the Ohio Players Royalties.*

TUFTA creates a statutory cause of action through which a creditor may seek recourse for a fraudulent transfer. *See TEX. BUS. & COM. CODE ANN. § 24.005* (Vernon 2009). TUFTA authorizes both equitable relief, through the avoidance of a fraudulent transfer, and money damages up to the value of the property transferred. ***Wohlstein v. Aliezer**, 321 S.W.3d 765, 776 (Tex. App.--Houston [14th Dist.] 2010, no pet.)* (citing ***Chu v. Hong**, 249 S.W.3d 441, 446 (Tex. 2008)*). Specifically, the remedies for a fraudulent transfer under TUFTA include: (1) avoidance of the transfer to the extent necessary to satisfy the creditor's claim; (2) an attachment or other provisional remedy; (3) other equitable remedies such as injunctions or the appointment of receivers; or (4) any other relief that the circumstances may require. *TEX. BUS. & COM. CODE ANN. § 24.008(a)*; ***Airflow Houston, Inc. v. Theriot**, 849 S.W.2d 928, 933--34 (Tex. App.--Houston [1st Dist.] 1993, no writ)*. [*11] "The last option is quite broad." ***Airflow**, 849 S.W.2d at 934.*

The Claimants are entitled to relief in the amount of the value taken by the Defendants in order to restore the Claimants to the position they would have occupied had the fraudulent transfer never occurred. [5] *See **Asarco LLC v. Ams. Mining Corp.**, 404 B.R. 150, 170--73 (S.D. Tex. 2009)* (stating that the court can award an amount of damages necessary to put a claimant in the financial condition in which it would have been before the fraudulent transfer took place). A court has wide discretion to approximate the value that a claimant has lost as a result of a defendant's fraudulent transfer of assets. *See **West v. Hsu (In re Advanced Modular Power Sys.)**, 413 B.R. 643, 678 (Bankr. S.D. Tex. 2009)* (citing ***Asarco**, 404 B.R.*

at 162) (stating that it is within the discretion of the court to award relief in the amount of value taken by a defendant). In awarding damages based upon the value of the asset transferred, a court may adjust the award "as the equities may require." *TEX. BUS. & COM. CODE ANN. § 24.009(c)(1)*. With these principles in mind, the Court will determine the amount of value lost by the Claimants, adjusted equitably according [*12] to the circumstances of the case.

> 5 Because the assets of ARF have devolved to the individual owners of the LLC, any relief granted will be to the owners of ARF in their individual capacities.

The Royalties did not begin to generate *revenue* until after the transfer occurred, but this does not mean they did not have value. Rather, a determination of the value of the Royalties must take into account their potential to generate revenue in the future. Because the Royalties generated a significant amount of income after the transfer, equity requires an adjustment of value to reflect the revenue they generated between the time they were fraudulently transferred to Suenos and the date the Court nullified the transfer. *See id.* Galaz testified that the total income generated by the Royalties was $988,000, which included revenue from royalties owned by ARF, a one-time sale of royalties to Bridgeport Music, Inc., dividend and interest income, and contributions by Alfredo Galaz, the ostensible owner of Suenos. (Trial Tr., 49, Feb. 23, 2010) Alfredo testified that Suenos received $998,000 from the rights during that time period. (Trial Tr., 237, Feb. 23, 2010) A twelve-page document titled "Segundo [*13] Suenos Income/Expenses (from inception thru 12-1-09)" (the "Expense Report") was admitted into evidence which listed the total revenue received by Suenos from the Royalties at $968,529.17, dividend income of $401.91, and interest income of $386.85 (Pl.'s Ex. 14A; Def.'s Ex. 49) In light of the conflicting evidence, the Expense Report is the most reliable indicator of the revenue received by Suenos. Using the figures in the Expense Report, the total value of the Royalties as evidenced by the income they generated for Suenos including interest and dividend income totals $969,317.93. *Id.*

In the prior Opinion, this Court restored the Royalties to ARF and affirmed the ownership of ARF as follows: a 50% interest held by Jackson, a 25% interest held by Debtor, and a 25% interest held by Galaz as an economic interest only. [6] Because the Claimants lost the benefit of their ownership interests from June 2005 until November 2010, they are entitled to their proportionate share of the $969,317.93 in gross income generated by the Royalties during that period of time. Accordingly, Jackson's share of the revenue totals $484,658.97 and Debtor's share totals $242,329.48, less allowable expenses. These [*14] amounts will be used as a starting point to determine the amount of value that the Claimants were deprived of as a result of the fraudulent transfer.

> 6 Jackson has consented to Debtor's ownership of ARF as a full member. (Pl.'s Ex. 68, 69)

a. ***Valuation of the Royalties Considering Reasonable and Necessary Expenses.***

Galaz argued that the Court improperly disregarded evidence of $694,642.57 in expenses that should have been factored into the valuation of the Royalties. [7] A review of the Expense Report is therefore necessary to determine whether the equities of the case compel a reduction in the valuation based on the expenses incurred by ARF or Suenos. At the outset it is important to note that ARF, as a wholly distinct entity from Suenos, is not liable for the debts, liabilities, or obligations that were incurred by *Suenos*. ARF was an LLC that was formed under the laws of California and owned by Jackson, Debtor, and Galaz. On the other hand, Suenos is an LLC that was formed under the laws of Texas and owned by Alfredo Galaz. Because the Expense Report reveals expenses which were incurred *after* the date of the transfer by a wholly distinct entity formed for the purpose of defrauding the [*15] Claimants of their share of revenue, the expenses of Suenos will not be factored into a determination of the value of the Royalties. *See Advanced Modular Power Sys., 413 B.R. 643, 679 (Bankr. S.D. Tex. 2009)* (declining to reduce damage award in breach of fiduciary duty and fraudulent transfer case where doing so would reward wrongdoers for their actions). As owners of ARF, the Claimants would be responsible for their proportionate share of reasonable and necessary expenses that were incurred by *ARF* prior to the date of the transfer. Accordingly, the equities of the case require that a calculation of the Royalties should take into account any such expenses. Because the assets of ARF have devolved to the individual owners of the LLC, any expenses properly attributable to ARF prior to the transfer will be reflected by a reduction in the damage awards to the Claimants.

> 7 As the document used to determine revenue, the Expense Report should also be used to determine expenses. The Expense Report lists the total expenses of Suenos at $694,642.57. (Def.'s Ex. 49)

i. ***Franchise Taxes Incurred by ARF Prior to the Fraudulent Transfer.***

Two letters from Galaz to the California Franchise Tax Board on [*16] behalf of ARF purport to include payment of past-due franchise taxes from the year it was registered as an LLC in 1998 through the year of the fraudulent transfer in 2005, although the letters did not evidence actual payment. (Def.'s Exs. 61, 63) Two bank account statements for Suenos, however, were admitted into evidence that reflect payments of $9,376 and $1,508.05 to the California Franchise Tax Board in amounts matching those recited in the letters. [8] (Def.'s Exs. 62, 64) If the fraudulent transfer had never occurred, ARF would have still owed its unpaid California franchise taxes between 1998 and 2005. Suenos paid a total of $10,884.05 for ARF's tax liabilities between 1998 and 2005. The members of ARF are therefore liable for their share of ARF's unpaid franchise taxes during that period of time.

8 The letters and bank account statements also reflect a payment for ARF's franchise taxes for the year 2006. No reduction in value should be applied from this payment because it was incurred after the date of the fraudulent transfer in an effort to defraud ARF and its members of revenue. Therefore, the 2006 tax payment is outside of the scope of expenses that may equitably be attributed [*17] to ARF.

ii. *Expenses in the Expense Report of Suenos.*

The Expense Report does not reflect any expenses that were incurred prior to the date of the transfer. (Def.'s Ex. 49) Additionally, there were no regularly-kept profit and loss statements or balance sheets for Suenos. (Trial Tr., 250-52, Feb. 25, 2010)) Further, Defendants neither offered nor presented any evidence of invoices, receipts, work orders, or other documentation to support or explain the transactions in the Expense Report. Accordingly, there was insufficient evidence to prove the existence, reasonableness, or necessity of the expenses in the Expense Report. Without sufficient proof of the existence, necessity, or reasonableness of any of the expenses in the Expense Report, equity does not compel them to be considered in determining the value of the Royalties. Regardless, the Court will review the Expense Report to support this conclusion.

Defendants claimed that a substantial portion of the revenue was used to pay legal fees incurred in obtaining the Royalties. The Expense Report lists the total amount of legal and professional fees incurred at $331,968.38; however, no evidence was presented to establish that the legal [*18] fees were incurred to obtain the Royalties. (Def.'s Ex. 49) Payments totaling $125,000 went to the law firm of Pick & Boydston. *Id.* Pick & Boydston represented Galaz in a number of lawsuits, only one of which appears to be directly related to the acquisition of the Royalties. *See* ***Segundo Suenos, LLC v. Satchell,*** *Nos. B213178, B213251, 2009 Cal. App. Unpub. LEXIS 9750, 2009 WL 4646145 (Cal. App. 2d Dist. 2009), cert. denied, 131 S. Ct. 164, 178 L. Ed. 2d 40 (2010).* Two other lawsuits in which Pick & Boydston represented Galaz and one of his former entities had nothing to do with the acquisition of the Royalties. In ***Galaz v. Jackson,*** *No. B184916, 2006 Cal. App. Unpub. LEXIS 2175, 2006 WL 648852 (Cal. App. 2d Dist. 2006),* Galaz engaged Pick & Boydston to bring suit against Jackson to enforce an illicit money laundering agreement in connection with royalties that Galaz illegally acquired to the television show "Garfield and His Friends." [9] Further, in ***Worldwide Subsidy Group v. Bogert,*** *No. B213979, 2009 Cal. App. Unpub. LEXIS 9696, 2009 WL 4609258 (Cal. App. 2d Dist. 2009),* one of Galaz's former entities retained Pick & Boydston to assert a legal malpractice action that was held to be barred by the statute of limitations. In addition to the lack of evidence showing that these expenses were reasonable or [*19] necessary, the Expense Report failed to specifically identify the matters for which the payments to Pick & Boydston were made. Moreover, by examining the time frame in which the fees were paid after the transfer between 2006 and 2009, in conjunction with entries showing payments to "James S. Wilk...," "Jackson Walk...," "Clerk, U.S. Ba...," "Federal Court...," and "Pacer," it appears that a substantial portion of the revenues were used to pay for Galaz's legal fees incurred in defending this lawsuit. *See* Case No. 08-5043, ECF Nos. 67, 106. In light of the inability to determine whether any legal and professional fees were reasonable or necessary in order to generate revenue from the Royalties, the Defendants did not establish that a reduction in valuation for these expenses is equitable.

9

> Raul Galaz, having successfully defrauded owners of a television program of a large amount of royalty payments, entered into an illegal money-laundering contract with . . . Julian Jackson. Under their oral agreement, Galaz would give Jackson $59,000 in illicit royalty proceeds, which Jackson would place in an offshore bank account and return the funds in untraceable cash to Galaz, less a five percent [*20] commission for himself. Jackson, however, eschewed the commission and kept the cash. Galaz, aggrieved to find so little honor among thieves,

> sued Jackson for rescission and fraud.
>
> . . . .
>
> As our courts have long recognized, an illegal contract may not serve as the foundation of any action, either in law or in equity. This state's courts are not in the business of helping criminals recover the proceeds of their fraudulent schemes.

***Galaz v. Jackson**, 2006 Cal. App. Unpub. LEXIS 2175, 2006 WL 648852, at *1 (Cal. App. 2d Dist. 2006).*

Furthermore, the Expense Report contains multiple other categories of expenditures that were not proven or otherwise shown to have been reasonable or necessary for the generation of revenue. For example, $48,785.08 was spent on "Auto" expenses, including $42,000 for a Hummer sport utility vehicle for Galaz's personal use, $79.40 to register the Hummer, $2,568.42 for service on the vehicle, $820 for car washes at the "Wash Tub," and $1,843.26 in fuel. (Def.'s Ex. 49) The Expense Report also reveals that Galaz paid himself $48,619.22 in "Consulting Fees," and that $174.70 was spent on "Dining," for meals at Outback Steakhouse, Carrabba's, and Fatty's. *Id.* A total of $77,155.16 was paid in "Rent" [*21] to Ruth Galaz and Shantell Sloan. It is unclear whether this rent was paid for personal or commercial use; however, because Shantell Sloan is Raul Galaz's wife and Ruth Galaz is his mother, the legitimacy of these expenses was not established. The Expense Report further reveals that $12,124.73 was spent on "Travel," $10,000 on a loan to "Amado Ramos Phone Cente...," and a number of transfers that were made between multiple accounts at multiple banks.

The Defendants also claimed that consideration should be given to $420,000 that Galaz allegedly incurred for his legal services on behalf of ARF. These purported expenses will not be considered because the Defendants failed to present any contemporaneous evidence specifically showing what services Galaz provided, whether those services were provided before or after the fraudulent transfer, or whether they were reasonable or necessary. At no point in time did Galaz ever present any bills to ARF for his legal services. (Trial Tr., 217, Feb. 25, 2010) In any case, Galaz would not be entitled to any fees for legal services after 2002 because he forfeited his law license that year. (Pl.'s Ex. 12) *See **Cruse v. O'Quinn**, 273 S.W.3d 766, 772 (Tex. App.--Houston [14th Dist.] 2008, pet. denied).*

Because [*22] the evidence failed to show that any of the expenditures in the Expense Report or those for Galaz's legal services were reasonable or necessary, equity does not compel a reduction in valuation of the Royalties to reflect these transactions. Moreover, the existence of a number of clearly illegitimate expenses in the Expense Report renders reliability of the expenses tenuous, at best. Accordingly, this Court declines to consider these expenses because to do otherwise would be to indirectly countenance the Defendants' improper conduct. *See TEX. BUS. & COM. CODE ANN. § 24.009(c)(1)* (Vernon 2009) (damage award for value of property transferred "subject to adjustment as the equities may require").

b. ***Assessment of Actual Damages Based on Value of the Royalties.***

The value of the Royalties at the time of the transfer, as adjusted to reflect the revenue they generated between the date of the fraudulent transfer and the date the Court nullified the same, yields an initial valuation of $969,317.93. An equitable reduction in value will be applied to reflect Jackson's and Debtor's proportionate shares of ARF's past-due California franchise tax liability between the date of its inception and the date [*23] that the fraudulent transfer occurred. The total amount of tax liability of ARF during the relevant period of time equals $10,884.05.

From 1998 until 2002, Galaz and Jackson were the sole members of ARF, each with a one-half ownership interest in the company. After the Divorce Decree in 2002, ownership of ARF was split between Jackson, Galaz, and Debtor in 50%, 25%, and 25% economic-only interests, respectively. Therefore, in order to accurately determine the proportion of tax liability owed, it is necessary to calculate the tax liability incurred from 1998 to 2002 separately from the liability incurred from 2003 to 2005.

There was insufficient evidence to determine the amount of yearly tax liability incurred by ARF between 1998 and 2005. In light of the Court's equitable power to determine the true value of the Royalties, the yearly amount will be calculated pro rata by dividing the total amount of unpaid taxes over the entire eight-year period from 1998 to 2005. Therefore, the yearly pro rata tax liability of ARF equals $1,360.51. After totaling this amount for the two relevant periods of ownership of ARF, the company incurred a total of $6,802.53 in liability from 1998 to 2002, and [*24] a total of $4,081.52 in liability from 2003 to 2005. Galaz and Jackson, as the two sole members of ARF from 1998 to 2002, are liable for the tax liability incurred during that time in proportion to their respective 50% interests. Thus, Galaz and Jackson are each responsible for $3,401.26 of ARF's tax

liability from 1998 to 2002. For the period of time from 2003 to 2005, Jackson is responsible for $2,040.76 of the taxes and Debtor and Galaz are each responsible for $1,020.38, in accordance with the parties' respective ownership interests in ARF.

In total, the members of ARF are responsible for tax liabilities incurred from 1998 until 2005 in the amounts as follows: Jackson for $5,442.02, Debtor for $1,020.38, and Galaz for $4,421.64. Because the Claimants must account for their proportionate share of the taxes, the actual damage awards to Debtor and Jackson will be reduced by their respective obligations. Accordingly, Jackson is entitled to actual damages of $479,216.95, and Debtor is entitled to actual damages of $241,309.10. Because the Defendants failed to show that any further reduction of the value of the Royalties was reasonable or necessary, equity does not compel an adjustment [*25] of the amount of actual damages for the expenses incurred by the Defendants after attempting to defraud Jackson and Debtor of their share of the revenues.

2. *Exemplary Damages Based on Fraud, Malice, and Gross Negligence.*

A bankruptcy court may rely on state law to award exemplary damages where the Bankruptcy Code does not specifically allow such measures. ***Franklin Bank, S.S.B. v. Barnes (In re Barnes), 369 B.R. 298, 310 (Bankr. W.D. Tex. 2007)***; ***Smith v. Lounsbury (In re Amberjack Interests, Inc.), 326 B.R. 379, 391 (Bankr. S.D. Tex. 2005)***. Under Texas law, courts of equity have the power to assess exemplary damages. ***Id.*** As a court of equity, a bankruptcy court may assess exemplary damages where state law supports such an award. ***Id.*** Furthermore, exemplary damages are proper in order "to punish the defendant for outrageous, malicious, or otherwise morally culpable conduct." ***Transp. Ins. Co. v. Moriel, 879 S.W.2d 10, 16 (Tex. 1994)***. In addition to punishing a wrongdoer, exemplary damages serve to deter others from engaging in similar conduct. ***Owens-Corning Fiberglas Corp. v. Malone, 972 S.W.2d 35, 40 (Tex. 1998)***.

Exemplary damages may be awarded only where the plaintiff proves by clear [*26] and convincing evidence that the loss or injury results from: (1) fraud; (2) malice; or (3) gross negligence. *See* ***In re Barnes, 369 B.R. at 310*** (citing *TEX. CIV. PRAC. & REM. CODE ANN. § 41.003* (Vernon Supp. 2012)). The Texas Civil Practice and Remedies Code defines fraud as "fraud other than constructive fraud." *TEX. CIV. PRAC. & REM. CODE ANN. § 41.001(6)* (Vernon 2008). Malice is defined as "a specific intent by the defendant to cause substantial injury or harm to the claimant." *TEX. CIV. PRAC. & REM. CODE ANN. § 41.001(7)*. Specific intent means that "the actor desires to cause the consequences of his act, or that he believes the consequences are substantially certain to result from it." ***Mission Res., Inc. v. Garza Energy Trust, 166 S.W.3d 301, 314 (Tex. App.--Corpus Christi 2005), rev'd on other grounds, 268 S.W.3d 1 (Tex. 2008)***. Further, gross negligence is defined as an act or omission:

> (A) which when viewed objectively from the standpoint of the actor at the time of its occurrence involves an extreme degree of risk, considering the probability and magnitude of the potential harm to others; and
>
> (B) of which the actor has actual, subjective awareness of the risk involved, but nevertheless [*27] proceeds with conscious indifference to the rights, safety, or welfare of others.

TEX. CIV. PRAC. & REM. CODE ANN. § 41.001(11) (Vernon 2008).

Based upon the evidence presented at trial, the Claimants have proven that they were harmed by the Defendants' acts of gross negligence, malice, and fraud based in connection with the Defendants' breach of fiduciary duty and fraudulent transfer of assets from ARF to Suenos. Accordingly, the circumstances of this case compel an award of exemplary damages.

a. ***Malice in Connection with the Defendants' Breach of Fiduciary Duty.***

Under the California LLC statute, a managing member owes fiduciary duties of loyalty and care to the other members of an LLC and to the LLC itself. *See, e.g., CAL. CORP. CODE §§ 16404(a), 17153* (West 2006); ***Berg & Berg Enters., LLC v. Boyle, 178 Cal. App. 4th 1020, 100 Cal. Rptr.3d 875, 890--91 (Cal. App. 6th Dist. 2009)***. The duties of loyalty and care include the responsibility to account for and hold as trustee any property, profit, or benefit derived from the conduct of the business. *CAL. CORP. CODE § 16404(b)(1)*. Further, the duties forbid a managing member from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing [*28] violation of the law. ***Id.*** at *§ 16404(c)*. Because Jackson was a co-owner of ARF with management and voting rights, a fiduciary relationship existed between Galaz, Jackson, and ARF. Galaz breached his fiduciary duties of loyalty and care through his failure to account for the property and profits derived from the business of ARF, the perpetration of an intentional fraud in an effort to secure the Royalties for his own benefit, and the wrongful dissolution of ARF after making the transfer. In breaching his fiduciary duties of loyalty and care, Galaz acted with malice. As a law school graduate, convicted felon, and disbarred attorney

with extensive experience in entertainment law, Galaz was well aware of the impropriety of his actions. (Pl.'s Ex. 11, 12) By acting at all times with full knowledge of the illegitimacy of his actions, Galaz acted with a specific intent to cause harm to Jackson and ARF. *See TEX. CIV. PRAC. & REM. CODE ANN. § 41.001(7)*. Accordingly, an award of exemplary damages in favor of Jackson is proper against the Defendants for malice in connection with Galaz's breach of fiduciary duty. *See In re Barnes, 369 B.R. at 310* (citing *TEX. CIV. PRAC. & REM. CODE ANN. § 41.003* [*29] (Vernon Supp. 2012)).

b. ***Fraud and Malice in Connection with the Fraudulent Transfer.***

In accordance with *Section 41.003 of the Texas Civil Practice and Remedies Code* and *Section 24.005(a)* of TUFTA, Galaz's conduct constituted acts of fraud and malice because he made the transfer to Suenos with the actual intent to hinder, delay, and defraud the Claimants. *See TEX. BUS. & COM. CODE ANN. § 24.005(a)* (Vernon 2009) ("A transfer made or obligation incurred by a debtor is fraudulent as to a creditor . . . if the debtor made the transfer or incurred the obligation: (1) with actual intent to hinder, delay, or defraud any creditor of the debtor."). On appeal the District Court affirmed the finding that Galaz acted with the actual intent to defraud. (Case No. 08-5043, ECF No. 484) Because Galaz acted with the intent to defraud, the completed transfer of assets from ARF to Suenos constituted fraud under TUFTA. Furthermore, Galaz acted with malice because he acted with a specific intent to defraud the Claimants of their share of revenue from the Royalties and of their ownership interests in the Royalties themselves. Therefore, an award of exemplary damages in favor of Jackson and Debtor is proper [*30] in light of Galaz's violation of TUFTA.

c. ***Assessment of Exemplary Damages.***

Under Texas law, exemplary damages are capped at the greater of: "(1)(A) two times the amount of economic damages; plus (B) an amount equal to any noneconomic damages found by the [fact finder], not to exceed $750,000.00; or (2) $200,000.00." *TEX. CIV. PRAC. & REM. CODE ANN. § 41.008* (Vernon 2011). "The amount awarded must be reasonably proportional to actual damages, though no set ratio exists for measuring reasonableness." ***Smith v. Lounsbury (In re Amberjack Interests, Inc.), 326 B.R. 379, 393 (Bankr. S.D. Tex. 2005)*** (citing ***Alamo Nat'l Bank v. Kraus, 616 S.W.2d 908, 910 (Tex. 1981))***. The Court weighs the following six factors in determining the reasonableness of an award: (1) the nature of the wrong; (2) the character of the conduct involved; (3) the degree of culpability of the wrongdoer; (4) the situation and sensibilities of the parties concerned; (5) the extent to which such conduct offends a public sense of justice and propriety; and (6) the net worth of the defendant. *TEX. CIV. PRAC. & REM. CODE ANN. § 41.011(a)*; ***In re Amberjack Interests, 326 B.R. at 393*** (citing ***Kraus, 616 S.W.2d at 910***). Exemplary [*31] damages awarded by the Court are "presumptively reasonable" if the award is within the statutory limits. ***In re Amberjack Interests, 326 B.R. at 393*** (citing ***Peco Constr. Co. v. Guajardo, 919 S.W.2d 736, 742 (Tex. App.--San Antonio 1996, writ denied))***.

Under *Section 41.008 of the Texas Civil Practice and Remedies Code*, the Court will assess an exemplary damage award of $500,000 in favor of Jackson and $250,000 in favor of Debtor. *TEX. CIV. PRAC. & REM. CODE ANN. § 41.008*. These modest figures represent significantly less than a doubling of the awards of actual damages. Because the awards of exemplary damages are within the statutory limits, the awards of exemplary damages are reasonable under Texas law. Further, after a careful review of the circumstances surrounding the nature of the wrong, the character of the Defendants' conduct, the degree of the Defendants' culpability, the situation and sensibilities of the parties, and the extent to which the Defendants' conduct offends a public sense of justice and propriety, the awards of exemplary damages are reasonable under the factors set forth in *Section 41.011(a) of the Texas Civil Practice and Remedies Code*. *See* ***In re Amberjack Interests, 326 B.R. at 393*** [*32] (citing ***Kraus, 616 S.W.2d at 910***). The actions perpetrated by the Defendants were sufficiently malicious to justify an award of exemplary damages and such an award is necessary to deter Galaz and others from engaging in similar conduct in the future.

3. ***Conclusion.***

For the reasons set forth herein, the Court concludes that Jackson and Debtor are entitled to an award of actual damages in the amount of $479,216.95 to Jackson and $241,309.10 to Debtor. Further, the circumstances surrounding the Defendants' conduct were sufficiently egregious to compel an award of exemplary damages in the amount of $500,000 to Jackson and $250,000 to Debtor. Therefore, Jackson is entitled to an award of actual and exemplary damages in the amount of $979,216.95, and Debtor is entitled to actual and exemplary damages in the amount of $491,309.10. All proceeds attributable to Galaz's interest shall be paid to the Claimants until their damage awards are satisfied. Debtor's attorney may submit a post judgment affidavit concerning post remand attorney's fees within fourteen days. Judgment will be rendered simultaneously with the entry of this Opinion.

Signed December 13, 2012.

/s/ Ronald B. King

Ronald B. King United [*33] States Chief Bankruptcy Judge