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**IN THE UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF UTAH, CENTRAL DIVISION**

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COMMODITY FUTURES TRADING  
COMMISSION, and

STATE OF UTAH DIVISION OF  
SECURITIES, through Attorney General  
Sean D. Reyes

Plaintiffs,  
v.

RUST RARE COIN INC., a Utah corporation,  
GAYLEN DEAN RUST, an individual,  
DENISE GUNDERSON RUST, an individual,  
and JOSHUA DANIEL RUST, an individual

Defendants;

and

ALEESHA RUST FRANKLIN, an individual,  
R LEGACY RACING INC, a Utah  
corporation, R LEGACY ENTERTAINMENT  
LLC, a Utah limited liability company, and R  
LEGACY INVESTMENTS LLC, a Utah  
limited liability company.

Relief Defendants.

**MOTION TO APPROVE PROPOSED  
DISTRIBUTION PLAN, OBJECTION  
PROCEDURE, AND CLAIM ANALYSIS**

Civil No. 2:18-cv-00892-TC

Judge Tena Campbell

Magistrate Judge Dustin B. Pead

Jonathan O. Hafen, the Court-Appointed Receiver over the assets of Rust Rare Coin, Inc. (“RRC”), Gaylen Dean Rust, R Legacy Racing Inc., R Legacy Entertainment LLC, and R Legacy Investments LLC (collectively, the “Receivership Defendants”), hereby submits this Motion to Approve Proposed Distribution Plan, Objection Procedure, and Claim Analysis (this “Motion”).

### **FACTUAL BACKGROUND**

This case concerns one of the biggest Ponzi schemes in Utah history, involving several hundred investors who lost in excess of \$100 million to a fraud perpetrated by Gaylen Dean Rust (“Rust”). During all relevant times, Rust owned and operated RRC, a specialty coin shop in Salt Lake City, Utah, dealing in rare coins, precious metals, and other memorabilia. From at least 2008, however, Rust also operated a massive Ponzi scheme in which he fraudulently solicited hundreds of millions of dollars from investors by claiming that their investments would be pooled together for the purpose of trading physical silver (the “Silver Pool”). Rust told investors and prospective investors that he was using the money contributed to the Silver Pool to purchase and store physical silver for investment. In other words, the Silver Pool purported to generate profits for investors by selling physical silver held in the Silver Pool when market prices began to decline and, after such a decline, Rust used the profits from the sale to purchase a larger quantity of silver at a lower price. Through this process, Rust claimed he was able to consistently increase the number of ounces of silver held in the Silver Pool and, consequently, increase the value of each investor’s share of the Silver Pool.

But these representations were false. Rust never traded silver in the manner he described to Silver Pool investors. Instead, Rust misappropriated funds invested in the Silver Pool to make payments to other investors in the manner of a Ponzi scheme. Specifically, after receiving a new deposit into the Silver Pool, Rust made payments to other investors from the same bank account

without ever transferring funds to or from a trading account or otherwise purchasing silver or other precious metals.

Additionally, Rust transferred money contributed by Silver Pool investors to other entities owned by Rust, including but not limited to R Legacy Entertainment, R Legacy Racing, and R Legacy Investments. None of these other entities owned any trading or similar accounts used to buy or sell silver or other precious metals and none had a legitimate right to funds sourced from Silver Pool investors.

As a result of this fraudulent scheme, the Commodity Futures Trading Commission (“CFTC”) and Utah Division of Securities (“DOS”) commenced the above-captioned action against Rust and the Receivership Defendants on November 13, 2018. *See* Dkt. No. 1. And on November 27, 2018, this Court entered an order (the “Receivership Order”) confirming the appointment of Jonathan O. Hafen as Receiver and authorizing him to identify, collect, and preserve the assets of the Receivership Estate for the benefit of the Estate’s creditors, including the hundreds of defrauded investors.

### **THE RECEIVER’S WORK**

Since the Receiver’s appointment, the Receiver and his team have been diligently working to complete the various tasks assigned to the Receiver by the Court, including asset identification and recovery. As part of these efforts, the Receiver has liquidated a majority of the real and personal property within the Receivership Estate, and the Receiver intends to liquidate the remainder of the Estate’s assets within the coming months. The Receiver also has filed numerous ancillary lawsuits against defendants seeking to recover fraudulent transfers made to them by Rust. He also has coordinated the execution of over 170 tolling agreements with such potential defendants. Through these processes, the Receiver is working to recover these

additional funds through either formal litigation or through settlement negotiations with investors and their counsel. To this point, the Receiver has successfully recovered approximately \$10 million for the benefit of the Receivership Estate, and he expects to recover additional funds as the receivership continues forward with its claw back efforts.

The Receiver also recently obtained approval from this Court to initiate a claims process and to set a bar date for all claim form submissions in this matter. *See* Dkt. No. 239. Pursuant to that Order, the Receiver sent out over 4,000 claim forms to potential claimants, published notice of the claims process, and set a bar date of October 4, 2019. In response, over 605 claim forms were submitted to the Receiver with a total self-reported claim amount of approximately \$168 million. To determine whether such claims will be allowed, the Receiver and his team are currently reviewing and verifying the submitted claim forms by comparing the asserted losses with data from the books and records of the Receivership Defendants. Once this process is complete, the Receiver will designate each claim as either an allowed or disallowed claim. If the Receiver objects to a claim, notice of the objection will be given to the claimant and filed with the Court, after which the Court will determine if the claim will be allowed. The Receiver anticipates that the preliminary analysis of such claims will be completed by the end of this quarter.

### **DISTRIBUTION PLAN**

Because it is clear from the facts of this case that the Receivership Defendants were operating a massive Ponzi scheme, the Receiver proposes the following distribution plan (“Distribution Plan” or “Plan”), which provides for the disbursement of net proceeds from the Receivership Estate to Claimants (defined below) using the “rising tide” method of distribution. The Receiver believes that, in his professional judgment, this Plan is in the best interest of the

Receivership Estate, provides the most equitable distribution to Claimants, and complies with applicable law. The funds available for distribution under the Plan will be generated and distributed from the Receivership Defendant's cash accounts, from the liquidation of the Receivership Estate, and from the proceeds of ancillary actions brought by the Receiver. Furthermore, the Receiver has consulted with both the Commodity Futures Trading Commission ("CFTC") and the Utah Division of Securities ("UDOS") to obtain their perspective and input on the Plan prior to filing it with the Court.

#### ARTICLE 1 – DEFINITIONS

When used in this Distribution Plan (or this corresponding Motion, which is incorporated herein by reference), the capitalized terms identified below and their plural forms have the following meanings:

**"Allowed Claim"** means a Claim presented by a Claim Form that is either (i) not objected to by the Receiver, (ii) allowed by agreement with the Receiver or (iii) allowed by a separate Order of the Court. An Allowed Claim is a necessary condition to the receipt of a Distribution.

**"Approved Claim Amount"** means the amount the Receiver agrees is owed to a Claimant based on an Allowed Claim. The Approved Claim Amount is *not the amount the Claimant will, in fact, receive in Distributions from the Receivership Estate*. Rather, it is the amount that the Claimant is entitled to receive from the Receivership Estate if a full recovery is made to all creditors.

**"Claim"** means any alleged right to a Distribution, regardless of whether or not such right to payment is reduced to judgment, liquidated, unliquidated, fixed or contingent, asserted or unasserted, matured, disputed, undisputed, legal, secured or unsecured.

**“Claims Bar Date”** means October 4, 2019, pursuant to the Order issued by the Court on August 19, 2019. *See* Dkt. No. 239.

**“Claimant”** means the holder of an Allowed Claim.

**“Class”** means a category of Claims as set forth in the Plan. As Claims are validated by the Receiver, he reserves the right to move Claims from one Class to another.

**“Court”** means the United States District Court for the District of Utah, before which this action is pending.

**“Distribution”** means any payment by the Receiver on an Allowed Claim in accordance with the procedures outlined in this Distribution Plan.

**“Person”** means an individual, corporation, partnership, limited liability company, trust, association, retirement or pension plan, or other entity.

**“Receivership Assets”** means all assets of the Receivership Defendants that have or will be collected by the Receiver.

**“Receivership Estate”** or **“Estate”** means all of the property interests of the Receivership Defendants, including, but not limited to, monies, funds, securities, credits, effects, goods, chattels, lands, premises, leases, claims, rights and other assets, together with all rents, profits, dividends, interest or other income attributable thereto, of whatever kind, which the Receivership Defendants own, possess, have a beneficial interest in, or control directly or indirectly.

## **ARTICLE 2 – DISTRIBUTION APPROACH**

Under this Plan, the Receiver proposes employing the “rising tide” distribution method. The rising tide approach seeks, where possible, to achieve an equal total percentage recovery for all Claimants, regardless of whether the recovery came before or after the commencement of the

receivership. In other words, available funds are first distributed on a pro rata basis to Claimants who were paid little or nothing from the Ponzi enterprise, and then, as those Claimants “catch up” to Claimants who received pre-receivership distributions, additional funds are distributed to Claimants who have the next lowest percentage return to date.

For example, the following illustration assumes there are only three investors:

Investor	Adjusted Investor Claim	Pre-Receivership Recovery	Percentage Return
A	\$100,000.00	\$0.00	0%
B	\$200,000.00	\$40,000.00	20%
C	\$100,000.00	\$80,000.00	80%

Under this scenario, Investor A would be the first to receive a distribution, as their percentage return is 0%. Investor B will not receive a distribution unless and until Investor A has received a 20% percentage return or, in this illustration, distributions of \$20,000.00. In the event Investor A receives \$20,000.00 in distributions and there remain additional funds to distribute, Investor B will begin receiving distributions with Investor A proportionate to their Allowed Claims. Based on the above illustration, in the event there is an additional \$6,000.00 to distribute, Investor A would receive \$2,000.00, and Investor B would receive \$4,000.00 (an additional 2% return to each Investor). Investors A and B will continue to receive distributions to the exclusion of Investor C until Investors A and B have both received an 80% percentage return. In the event Investors A and B receive distributions sufficient for both to receive an 80% percentage return and there remain additional funds to distribute, Investor C will begin receiving distributions with Investors A and B proportionate to their Allowed Claims.

The Receiver will make Distributions to each Class of Claimants using the rising tide

approach until all of the Receivership Assets have been distributed. By employing this approach, the Receiver seeks to provide the same proportional recovery to all victims who invested or got caught in the scheme, regardless of whether those funds were received prior to or after the collapse of the scheme. As set forth in more detail below,<sup>1</sup> the Receiver submits that the rising tide method is the most equitable method of calculating distribution amounts in this case.

### ARTICLE 3 – PRIORITY TREATMENT OF CLAIMS

The priority of each Claim will be determined according to its classification, as indicated below in decreasing order of priority:

- (1) Administrative claims of the Estate;
- (2) Government tax liabilities of the Estate;
- (3) Secured creditors, to be paid of out the proceeds of their collateral;
- (4) Unsecured creditors and defrauded investors;
- (5) Non-Recognized Trade Creditor Claims; and
- (6) Insider/Subordinated Claims.

Each classification and its corresponding priority status is described in greater detail below.

**Class 1: Administrative Claims.** Class 1 Claims are Claims for the actual and necessary expenses of administering the Receivership Estate, including fees and expenses paid in connection with marshaling, preserving, and distributing Receivership Assets, fees and expenses paid in accordance with the Receivership Order or other Court orders, tax obligations that are incurred from activities undertaken subsequent to the appointment of the Receiver (not tax obligations that merely become due subsequent to the appointment of the Receiver), and fees and

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<sup>1</sup> See Legal Analysis below, at 15.

expenses of the Receiver and his experts, consultants, accountants, and attorneys. All Class 1 Claims are subject to analysis by the Receiver, and a Distribution will only be made to a Class 1 Claimant after the Receiver determines, in his sole professional judgment, that the total amount claimed is equal to the actual value provided by such Claimant and received by the Estate.

The Receiver will not know the full amount of Class 1 Claims until the conclusion of this case. Accordingly, the Receiver will, in the exercise of his discretion, retain a sum as a reserve to fund the cost of securing and liquidating additional Receivership Assets and to meet all future Administrative Claims. The Receiver may reserve additional amounts from funds later obtained for the Receivership Estate, but will endeavor to reserve no more for Administrative Claims than he reasonably believes to be necessary to cover such Claims. All current and future Class 1 Claims shall be paid in full from funds held in the receivership bank accounts pursuant to the procedures set forth in the Receivership Order and shall be accorded priority over all other Claims. Any amount left in reserve at the conclusion of this case shall be distributed to Claimants pursuant to the terms of this Plan.

**Class 2: Government Tax Claims.** This claim category includes all Allowed Claims for tax or other liabilities owed to a local, state, federal, or foreign governmental body. All Class 2 Claims shall have priority over Class 3, 4, 5 and 6 Claims and must be paid in full before a Distribution will be made to a lower Class.

**Class 3: Secured Creditor Claims.** This claim category includes the Allowed Claims of all secured creditors of the Receivership Estate. Class 3 Claims, however, will be paid solely from the proceeds of the collateral held by the Estate in which the secured Claimant holds an interest. Any deficiency amount sought by a secured creditor in excess of the proceeds it receives from such collateral will be treated as a Class 6 subordinated Claim. Class 3 Claims shall be paid

upon sale of the Receivership Asset(s) securing such Class 3 Claims from the proceeds of such sale. And except as set forth above, all Class 3 Claims shall have priority over Class 4, 5 and 6 Claims and must be paid in full before a Distribution will be made to a lower Class.

**Class 4: Investors and Unsecured Creditors.** This claim category includes the Allowed Claims of (i) a Person that deposited or invested money, metals, securities or other financial instruments with one or more Receivership Defendant; or (ii) an employee, customer, vendor, independent contractor, trade creditor, retained professional, or other general unsecured creditor for fees, reimbursable expenses, goods, or services provided to one or more Receivership Defendant before the Receivership Defendant became subject to the Receivership Order. For the avoidance of doubt, Class 4 Claims include all Claims that have not been assigned to another Class under this Plan. All Class 4 Claims shall have priority over all Class 5 and 6 Claims and must be paid in full before a Distribution will be made to a lower Class. The Receiver believes that he will be able to make pro-rata Distributions to Class 4 Claimants but will be unable to pay such Claims in full.

**Class 5: Non-Recognized Trade Creditor Claims.** Notwithstanding Class 4 above, this claim category includes all Claims submitted by trade creditors whose Claim is against Gaylen Dean Rust or Denise Gunderson Rust in their personal capacity. All Class 5 Claims shall have priority over all Class 6 Claims and must be paid in full before a Distribution will be made to a lower Class. The Receiver believes that no Distributions will be made to Class 5 Claimants.

**Class 6: Insider/Subordinated Claims.** This claim category includes all Claims determined by the Receiver to be subordinate in priority of payment to Classes 1 through 5, as compelled by the equities of the case and the actions of the relevant Claimant. Class 6 Claims include, but are not limited to, Claimants who the Receiver determines were substantially

involved in furthering the illegitimate Silver Pool. All Class 6 Claims will be paid after all other Classes are paid in full. The Receiver believes that no Distributions will be made to Class 6 Claimants.

The Receiver may divide a Claim and classify it into more than one Class. The Receiver may also divide a Claim, treating part of the Claim as an Allowed Claim and treating the balance as a disallowed Claim.

#### ARTICLE 4 – MAKING DISTRIBUTIONS

As the Receiver validates Claims and receivership funds become available, the Receiver will begin distributing funds on an interim basis to Claimants in accordance with the priority classifications set forth above. The interim Distributions will be calculated using the “rising tide” distribution method described above in Article II, and the Receiver will seek Court approval prior to making any such Distributions.

1. **Payment Method.** Distributions under the Plan will be made by sending a check in the name of the Claimant to the address identified in said Claimant’s Claim Form or to the address specified by any change of address notices received by the Receiver before the funds are distributed.<sup>2</sup> Claimants are required to advise the Receiver, in writing, of any change of address or party in interest.

2. **Duty to Provide Information.** In the event the Receiver requires information or forms from a Claimant in relation to making a Distribution (such as tax forms), the Receiver may condition any payment upon receiving such information or forms from the Claimant. A Claimant’s failure to provide any such information or forms to the Receiver within 30 days after

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<sup>2</sup> See Claim Form, at 9 (“Distributions, if any, will be made to the claimant identified above at the address listed.”) (emphasis omitted).

the Receiver's written request for such information will be treated as a forfeiture of that Claimant's Allowed Claim.

3. **Interest on Claims.** Interest shall not accrue or be paid on any Claim, and no holder of an Allowed Claim shall be entitled to any interest accruing on any Claim.

4. **No De Minimis Distributions.** The Receiver is not required to make a Distribution to a Claimant if the total amount to be paid to the Claimant is less than \$50.00. The Receiver has determined that the cost involved in making a Distribution in amounts less than \$50.00 would not be cost effective. Any holder of an Allowed Claim that does not receive a Distribution, including an interim Distribution, solely because of this provision will have such payment reserved until that Claimant would receive a Distribution amount of \$50.00 or more.

5. **Rounding.** Notwithstanding any other provision to the contrary, the Receiver will round all payments under this Plan to the nearest whole dollar (up or down).

6. **Unclaimed Distributions.** Except as otherwise provided herein, any Person who fails to claim any Distribution within 90 days from any payment date shall forfeit all rights to such payment, and the funds at issue will revert back to the Receivership Estate.

7. **Undeliverable Distributions.** The Receiver is under no affirmative obligation to attempt to locate a Claimant. Accordingly, if any Distribution is returned to the Receiver as undeliverable and no appropriate forwarding address is received by the Receiver within 90 days after the attempted Distribution, the Receiver will treat the Distribution as forfeited by that Claimant, and the funds at issue will revert back to the Receivership Estate.

8. **Final Distribution.** When the Receiver determines that further efforts to liquidate the Receivership Estate are not required or would not be economical, the Receiver will, after receiving authorization from the Court, make a final Distribution. In the event that any payment

subject to this final Distribution is unclaimed, undeliverable, or forfeited by any Claimant, the Receiver will donate such funds to a non-denominational charity (to be determined at a later date) if the total amount of such funds does not exceed \$10,000. If more than \$10,000 remain after this final Distribution, the Receiver will seek Court approval to determine whether to redistribute such funds to Claimants or to donate the remaining funds to charity in accordance with this provision.

#### ARTICLE 5 – MISCELLANEOUS

1. **Court Approval.** The provisions of this Plan, upon confirmation of the Court, shall be binding upon all creditors of and parties in interest to the Receivership Estate.
2. **Right to Modify.** This Plan may be modified both before and after the Court approves this Plan, on such notice and hearing as this Court deems appropriate.
3. **Payment Effects Release.** If an Allowed Claim, or any portion thereof, is paid by the Receiver pursuant to this Plan, then any and all claims, demands, rights, and causes of action of any nature whatsoever, whether arising at law or in equity, known or unknown, asserted or unasserted, for all damages (whether actual or punitive, known or unknown, latent or patent, foreseen or unforeseen, direct or indirect or consequential, matured or unmatured, and accrued or not accrued), debts, putative interest, and liabilities of whatever nature that are or could be asserted by the Claimant or any other person against the Receiver or his agents, the Receivership Estate, the CFTC, UDOS, any Receivership Defendant, or any Receivership Assets, are hereby forever discharged, released, extinguished, and satisfied.

Neither the Receiver nor any Person acting at his direction shall have any liability in any respect for having paid or otherwise satisfied an Allowed Claim, nor for any other action taken in good faith under or relating to this Plan or arising out of the processing of any Claim, including,

but not limited to, any act or omission in connection with or arising out of the administration of Claims or this Plan or the Receivership Estate. In the event of any Claim being made against the Receiver for such matters—whether or not willful misconduct is alleged—the Receiver shall be entitled to a defense by counsel of his choice, payable as any other professional expense herein, and the provisions of the Receivership Order shall otherwise apply.

4. **Waiver.** The Receiver, his agents, attorneys, accountants, and employees, shall be held harmless for any damages or liability that may arise through the discharge of their duties under the Plan, in accordance with the Receivership Order issued by the Court on November 27, 2018. *See* Dkt. No. 54.

5. **Reserve.** The Receiver is expressly authorized to pay Claims according to the terms of this Plan without regard for the possibility that a Claim may, with good cause, be submitted to the Receiver after the Claims Bar Date. The Court will not expect the Receiver to have accrued Receivership Assets to guard against this possibility. For the purpose of making interim Distributions, the Receiver shall establish, in his discretion and without further order of this Court, reserves for all Claims that are still in dispute at the time of a Distribution.

#### **ARTICLE 6 – RETENTION OF JURISDICTION**

This Court has had jurisdiction over this matter since its commencement on November 13, 2018 and shall continue to retain exclusive jurisdiction over the Receiver, the Receivership Estate, and all Receivership Assets going forward. No action taken by or against the Receiver with regard to any pending matter in any other court shall be deemed to have terminated, limited, reduced, waived, or relinquished this Court’s exclusive jurisdiction.

Moreover, this Plan and the Order approving this Plan are not, and are not intended to be, either a final adjudication of this matter or a termination, limitation, reduction waiver or

relinquishment of this Court's exclusive jurisdiction with regard to all Receivership Assets and all matters in controversy in this case. Instead, this Court shall continue to have and retain exclusive jurisdiction over all matters existing or arising in this receivership or related in any way thereto, including, but not limited to, all matters relating to approving or denying Claims, making Distributions, locating, recovering, and settling claims, and liquidating Receivership Assets.

### LEGAL ANALYSIS

It is well established that a district court has broad discretion in determining relief in an equity receivership. *S.E.C. v. Vescor Capital Corp.*, 599 F.3d 1189, 1194 (10th Cir. 2010) (noting that a court has “broad powers and wide discretion” to determine relief in an equity receivership); *S.E.C. v. Credit Bancorp, Ltd.*, 290 F.3d 80, 91 (2d Cir. 2002) (finding that the district court's approval of a plan of distribution was “within the Court's equitable discretion”); *S.E.C. v. Infinity Group Co.*, 226 Fed. App'x 217, 218 (3d Cir. 2007) (“District Courts have wide equitable discretion in fashioning distribution plans in receivership proceedings . . . .”); *S.E.C. v. Forex Asset Mgmt. LLC*, 242 F.3d 325, 331 (5th Cir. 2001) (stating that the district court enjoys “broad discretionary power” in shaping equity decrees); *S.E.C. v. Elliott*, 953 F.2d 1560, 1566-67 (11th Cir. 1992) (“The district court has broad powers and wide discretion to determine relief in an equity receivership.”); *S.E.C. v. Wang*, 944 F.2d 80, 85 (2d Cir. 1991) (stating that the trial court is vested with “broad discretionary power . . . to craft an equitable decree”); *S.E.C. v. Hardy*, 803 F.2d 1034, 1037-39 (9th Cir. 1986) (“[I]t is a recognized principle of law that the district court has broad power and wide discretion to determine the appropriate relief in an equity receivership.”) (citations omitted).

Pursuant to these broad discretionary powers, courts tasked with overseeing the administration of a receivership for a Ponzi scheme may authorize any distribution protocol for receivership assets that is “fair and reasonable” in the overseeing court’s opinion. *S.E.C. v. Wealth Mgmt. LLC*, 628 F.3d 323, 332 (7th Cir. 2010); *S.E.C. v. Byers*, 637 F. Supp. 2d 166, 174 (S.D.N.Y. 2009) (citing *Wang*, 944 F.2d at 81) (“The Court has the authority to approve any plan provided it is ‘fair and reasonable.’”); *S.E.C. v. Enter. Trust Co.*, 2008 WL 4534154, at \*3, 2008 U.S. Dist. LEXIS 79731, at \*10 (N.D. Ill. Oct. 7, 2008) (“There are no hard rules governing a district court’s decisions in matters like these. The standard is whether a distribution is equitable and fair in the eyes of a reasonable judge.”). And unlike a case arising under title 11 of the United States Code, there is no statutory mandate that prescribes how the assets recovered in a receivership should be distributed. Thus, it is well within this Court’s discretion to approve a distribution plan that utilizes a pro rata approach—such as the one presented by the Receiver in this matter—rather than one which attempts to trace a claimant’s investment into a fraudulent scheme. *See, e.g., S.E.C. v. Quan*, 870 F.3d 754, 762 (8th Cir. 2017) (“Courts have ‘routinely endorsed’ the pro rata distribution of assets to investors as the most fair and equitable approach in fraud cases.”); *United States v. Durham*, 86 F.3d 70, 73 (5th Cir.1996) (affirming district court’s approval of pro rata distribution plan even though the majority of funds were traceable to specific claimants); *Credit Bancorp, Ltd.*, 290 F.3d at 89 (noting that the use of pro rata distributions “has been deemed especially appropriate for fraud victims of a ‘Ponzi scheme’” because whether a customer’s assets are traceable is “a result of the merely fortuitous fact that the defrauders spent the money of the other victims first.” (quoting *Durham*, 86 F.3d at 72)); *Elliott*, 953 F.2d at 1569 (holding that a district court did not abuse its discretion by disallowing tracing

where “certain investors would recoup 100% of their investment while others would receive substantially less”).<sup>3</sup>

### A. Distribution Methodology

As set forth above, the Receiver proposes using the rising tide method to distribute funds to receivership Claimants. “Rising tide appears to be the method most commonly used (and judicially approved) for apportioning receivership assets.” *S.E.C. v. Huber*, 702 F.3d 903, 906 (7th Cir. 2012). “The basic goal [of the rising tide allocation] is to equalize recovery for victims regardless of whether the recovery comes before or after the commencement of the [receivership].” See Michael L. Martinez, *The Ebb of Rising-Tide Distributions in Ponzi Scheme Bankruptcies*, 35 AM. BANKR. INST. J. 16 (June 2016). Accordingly, a “rising tide” allocation “result[s] in a pro rata distribution of available assets to victims.” *Id.*; see also *S.E.C. v. Par.*, 2010 WL 5394736, at \*3 (D.S.C. Feb. 10, 2010) (discussing “pro rata payments based on the Rising Tide calculation”).

Although the “net loss” method (sometimes referred to as “net investment” method) of distribution is also a favored method of pro rata distribution, see *Huber*, 702 F.3d at 905-06 (7th Cir. 2012), this methodology ignores how much the entity in receivership distributed to the creditor in the past and, instead, focuses solely on the amount of the creditor’s net loss on the date the receivership commences.<sup>4</sup> See, e.g., *Par.*, 2010 WL 5394736, at \*7. “A closer examination of [the net loss] proposal reveals that it suffers from serious flaws and produces

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<sup>3</sup> Not only does the Receiver believe that a pro rata approach is more equitable and appropriate in this case than employing the use of tracing, the vast majority of investor payments in this matter are not traceable to any specified investor.

<sup>4</sup> Assuming, of course, that the creditor is not a “winner” and has not received more than the creditor invested.

inequitable results because it ignores the illegal activities of the defendants, including the fact that the money paid to those investors during the course of the scheme came from other victims of the fraud.” *Id.* (internal citations and alterations omitted); *U.S. Commodity Futures Trading Comm’n v. Lake Shore Asset Mgmt. Ltd.*, 2010 WL 960362, at \*10 (N.D. Ill. Mar. 15, 2010) (noting that “a straight pro rata distribution of the available funds, irrespective of any pre-receivership payments received by investors, would be inequitable because it unfairly elevates investors who received pre-receivership payments over those who did not”).

While courts have sometimes found the “net loss” method attractive in cases where a large number of creditors would receive nothing under the rising tide method,<sup>5</sup> the Receiver’s preliminary analysis of the Claim Forms submitted in this matter shows that at least 75% of all Claimants will receive a Distribution under the rising tide approach. Moreover, the vast majority of investors who submitted a Claim Form in this matter never received *any* pre-receivership distributions from Receivership Defendants. This is due, in part, because Rust engaged in a massive fundraising effort in the final years of the Silver Pool in order to fund payment requests from earlier investors. Given this push to increase the number of investors and available Silver Pool funds during the final years of the investment scheme, the Receiver believes that it would be inequitable to allow early investors who have already recouped a significant portion of their investment to recover on the same basis as later investors who have recovered nothing from the

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<sup>5</sup> *See, e.g., S.E.C. v. Byers*, 637 F. Supp. 2d 166, 182 (S.D.N.Y. 2009) (affirming use of the net investment method where 45% of investors would receive no distribution under the rising tide method); *U.S. Commodity Futures Trading Comm’n v. Barki, LLC*, 2009 WL 3839389, at \*2 (W.D.N.C. Nov. 12, 2009) (finding the net investment method most equitable where 55% of investors would receive no distribution under the rising tide method); *but see, Lake Shore Asset Mgmt. Ltd.*, 2010 WL 960362, at \*10 (“The fact that certain investors may not receive a distribution under the ‘Rising Tide’ method is . . . not germane.”).

Receivership Defendants to date.

Therefore, the Receiver submits that the rising tide method is the most equitable method of calculating distribution amounts in this case. It strikes a reasonable balance between those Claimants who invested early and have thus received a pre-receivership withdrawal and those investors who invested near the end of the scheme and are likely to have received no withdrawals. The rising tide method gives more value to those Claimants who have received little to nothing to date while giving less to those who have already recovered a substantial percentage. It is for these reasons that the rising tide method is the “most commonly used (and judicially approved) for apportioning receivership assets.” *Huber*, 702 F.3d at 906.

### **B. Pooling Receivership Assets**

For purposes of distribution in an equity receivership, courts may ignore the separate identity of entities that are part of “a unified scheme to defraud.” *S.E.C. v. Sunwest Mgmt., Inc.*, 2009 WL 3245879 (D. Or. Oct. 2, 2009) (receivership entities considered “unitary enterprise” for distribution purposes due to extensive commingling of funds); *S.E.C. v. AmeriFirst Funding, Inc.*, 2008 WL 919546, at \*4 (“a pooled distribution is equitable when the separate legal entities were involved in a unified scheme to defraud”); *see also S.E.C. v. Forex Asset Mgmt. LLC*, 242 F.3d 325, 331 (5th Cir. 2001) (affirming plan adopted by district court pooling assets of entities for distribution); *U.S. v. Durham*, 86 F.3d 70, 71-73 (5th Cir. 1996) (same). Here, the funds used by Receivership Defendants—such as RRC, R Legacy Entertainment, R Legacy Investments, and R Legacy Racing—were sourced almost exclusively from Silver Pool investors. Indeed, the books and records of the Receivership Defendants show that Rust commingled funds between all of these entities and that he used investor funds to support the various business operations. As such, the Court is authorized to treat these various receivership entities “as one substantively

pooled estate for the purposes of distribution” under the Plan. *Sec. & Exch. Comm'n v. Detroit Mem'l Partners, LLC*, 2016 WL 6595942, at \*6 (N.D. Ga. Nov. 8, 2016) (quoting *S.E.C. v. Founding Partners Capital Mgmt.*, 2014 WL 2993780, at \*6 (M.D. Fla. July 3, 2014)).

Accordingly, the Receiver proposes distributing funds under the Plan from a single pool of Receivership Assets.

### **C. Claim Priority & Classification**

Under the Plan, the Receiver proposes classifying different Claims into different priority Classes based on the equities and factual circumstances surrounding each Claim. When deciding what claims should be recognized and in what amounts, “the fundamental principle which emerges from case law is that any distribution should be done equitably and fairly, with similarly situated investors or customers treated alike.” *Sec. & Exch. Comm’n v. Homeland Commc’ns Corp.*, 2010 WL 2035326, at \*2 (S.D. Fla. May 24, 2010) (quoting *S.E.C. v. Credit Bancorp. Ltd.*, 2000 WL 1752979, at \*13 (S.D.N.Y. Nov. 29, 2000)). Because the Receiver’s analysis of the Claim Forms submitted in this matter show that non-investor Claimants constitute a small portion (likely less than 5%) of the total unsecured Claims against the Receivership Estate, the Receiver believes that grouping investors with general unsecured creditors is in the best interest of the Receivership Estate. Indeed, if general unsecured creditors—such as customers, employees, and trade creditors—were classified below investors, they would effectively be deprived of *any* recovery in this matter given the limited amount of expected returns that will be made to Claimants. Moreover, although the total dollar amount of Claims made by general unsecured creditors is small in comparison to investors, 131 of the Claimants in this matter (or 21% of Claims) consist of non-investor Claims. And unlike the Silver Pool investors, these customers, employees, and trade creditors did not believe they were taking on any of the risks

inherent in an “investment” by simply doing business with the Receivership Defendants. In light of the above facts and the broad discretion of this Court, the general unsecured creditors of the Receivership Estate should receive more than a 0% return under the Plan. Thus, these creditors should be given the same priority of payment as Silver Pool investors.

The Receiver also proposes subordinating certain Claims under the Plan based on the factual circumstances and equities of each Claim. A court’s power to approve a Receiver’s decision on claim determinations and priority is well-settled. *See S.E.C. v. Elliott*, 953 F.2d 1560, 1566 (11th Cir. 1992). And this power includes the exercise of the court’s equitable powers to subordinate claims. *See, e.g., S.E.C. v. Ariz. Fuels Corp.*, 739 F.2d 455, 459 (9th Cir. 1984) (“Receivership courts have the general power to use summary procedures in allowing, disallowing, or subordinating the claims of creditors.”); *In re Westgate Cal. Corp.*, 642 F.2d 1174, 1177 (9th Cir. 1981) (“Subordination is an equitable power and is therefore governed by equitable principles.”). Subordination of a claim is particularly appropriate where there has been misconduct by the claimant or participation in the fraudulent scheme. *Durham*, 86 F.3d at 73 (“Sitting in equity, the district court is a ‘court of conscience.’”) (quoting *Wilson v. Wall*, 73 U.S. 83 (1867)). Accordingly, the Receiver believes it is in the best interest of the Receivership Estate to subordinate certain Claims if, in the Receiver’s professional judgment, those Claims are not supported in equity.

### **OBJECTION PROCEDURE**

Because the Receiver recognizes that there may be objections to the Receiver’s proposed Distribution Plan, the Receiver requests that the Court apply the Summary Disposition Procedure previously approved of by the Court to this Motion and all objections related thereto. *See* Dkt. No. 165. This will allow the Receiver to expeditiously resolve all disputes related to the Plan

while still preserving the due process rights of any Person claiming an interest in such Distributions.

Once the Receiver files this Motion with the Court, the Receiver will serve a copy of the Motion (which includes the Distribution Plan) via first class U.S. Mail, postage prepaid, on all creditors who submitted a Claim Form to the Receiver.<sup>6</sup> The Receiver will also email a copy of the Motion to all Persons identified on the Receiver's master mailing matrix and post the Report on the Receiver's website at <http://rustrarecoinreceiver.com>.

As set forth in the Court's *Order Granting Motion to Allow Summary Disposition Procedure*, any objection to the Receiver's proposed Distribution Plan **must be sent directly to the Receiver** within 30 days of service of this Motion. *Id.* at 2. The objecting party will not be a party to the overall proceeding, will not intervene in the case, and will not file any pleadings or other documents directly with the Court unless otherwise authorized by the Court.<sup>7</sup> *Id.* at 2-3.

If an objecting party specifically requests discovery in their objection, the parties will have an additional 30 days to complete discovery. *Id.* at 3. Discovery will be conducted pursuant to the *Federal Rules of Civil Procedure*, except that written discovery must be responded to within 14 days. *Id.* Either side may seek relief from the Court if the requested discovery is unduly burdensome or not proportional to the issues being determined. *Id.*

Following the filing of the objection or close of discovery (if specifically requested), the Receiver will then file the objections with the Court and schedule a hearing on the matter. *Id.* If

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<sup>6</sup> The Receiver will use the address provided by the creditor in their Claim Form for service of this Motion. *See* Claim Form Instruction, Dkt. No. 236, Ex. A, at 3 (“Notices and communications from the Receiver will be sent to the address provided. *You have a continuing obligation to keep the Receiver informed of your current contact information.*”).

<sup>7</sup> However, discovery documents such as certificates of service and notices of deposition may be filed with the Court without prior Court approval.

an evidentiary hearing is needed, the Receiver will schedule additional deadlines regarding disclosure of witnesses and exhibits as needed. *Id.* The Receiver may file a reply to any objection five days before the hearing. *Id.*

### **CLAIMS ANALYSIS**

Once the Receiver has reviewed and analyzed all of the Claims Forms submitted in this matter, the Receiver will prepare a Claims Analysis Report (“Report”). The Report will identify, among other things, whether each Claim submitted (or any portion thereof) is allowed or disallowed in full or in part, the Receiver’s proposed classification of each Claim, and the Approved Claim Amount. Prior to filing the Report with the Court, the Receiver will serve a copy of the Report via first class U.S. Mail, postage prepaid, on all creditors who submitted a Claim Form to the Receiver. The Receiver will also email the Report to all Persons identified on the Receiver’s master mailing matrix and post the Report on the Receiver’s website at <http://rustrarecoinreceiver.com>.

Prior to filing the Report, the Receiver will seek to resolve Claim disputes by engaging in negotiations with Claimants and filing, where appropriate, formal Claim objections. Because the Receiver recognizes he will likely need to file objections to certain Claims and there will likely be objections to the Report and the Receiver’s related Claims analysis, the Receiver also requests that the Court authorize the Receiver to employ the Summary Disposition Procedure to resolve all objections related to the Claims and the Report. *See* Dkt. No. 165.

### **CONCLUSION**

The Receiver respectfully requests that the Court approve the proposed and foregoing Distribution Plan and adopt the Summary Disposition Procedure for all objections related to the Plan and forthcoming Claim objections and Report. A proposed Order is attached hereto.

DATED this 23rd day of April 2020.

**PARR BROWN GEE & LOVELESS**

/s/ Cynthia D. Love  
Joseph M.R. Covey  
Cynthia D. Love

*Attorneys for Receiver Jonathan O. Hafen*

**CERTIFICATE OF SERVICE**

IT IS HEREBY CERTIFIED that service of the above **MOTION TO APPROVE PROPOSED DISTRIBUTION PLAN, OBJECTION PROCEDURE, AND CLAIM ANALYSIS** was (1) electronically filed with the Clerk of the Court through the CM/ECF system on April 23, 2020, which sent notice of the electronic filing to all counsel of record, (2) posted on the Receiver's website (rustrarecoinreceiver.com), and (3) emailed to all those on the Receiver's master mailing matrix.

*/s/ Cynthia D. Love* \_\_\_\_\_