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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re: **DEWEY & LEBOEUF LLP,** **Debtor.**	**Case No. 12-12321 (MG)** **Chapter 11**
ALAN M. JACOBS, as Liquidating Trustee of the Dewey & LeBoeuf Liquidation Trust, **Plaintiff,** **v.** **STEPHEN H. DiCARMINE and JOEL I. SANDERS,** **Defendants.**	**Adversary No. 13-01765 (MG)**

FIRST AMENDED COMPLAINT

Alan M. Jacobs, solely in his capacity as Liquidating Trustee ("Trustee") for and on behalf of the Dewey & LeBoeuf Liquidation Trust ("Trust"), by and through his undersigned counsel, files this First Amended Complaint against Stephen H. DiCarmine ("DiCarmine") and Joel I. Sanders ("Sanders"), and alleges as follows:

INTRODUCTION

1. Defendants DiCarmine and Sanders (together, the "Insiders") enriched themselves at the expense of Dewey & LeBoeuf LLP ("Dewey" or the "Debtor") and its creditors. Prior to Dewey's formation, the Insiders arranged sweetheart compensation agreements with the Debtor's future chairman, Steven Davis ("Davis"), who himself benefitted from the deals. The purported contracts awarded the Insiders exorbitant compensation and required, literally, nothing in return.

2. Acting as the Executive Director and the Chief Financial Officer, respectively, of Dewey, DiCarmine and Sanders saw to it that Dewey paid their inflated salaries, contractual bonuses, and even discretionary bonuses, on a regular schedule, like clock-work, even while Dewey failed to pay creditors as obligations matured, breached loan covenants, and fell deeper and deeper into insolvency.

3. Acutely aware of Dewey's deteriorating financial condition, the Insiders went to considerable lengths to ensure that their own financial well-being was not disrupted. They arranged for their compensation to be paid into trusts. They arranged for the Debtor to extend them special letters of credit. They even attempted, on the eve of bankruptcy, to have the Debtor grant them indemnities for their wrongful conduct.

4. The Insiders' malfeasance knew no boundaries. Acting in a manner inconsistent with the trust bestowed upon them and their agency as high ranking employees of Dewey, DiCarmine and Sanders orchestrated a long-running scheme to inflate Dewey's financial

statements. Their scheme is detailed in the criminal indictment of the Insiders ("Indictment") (copy attached at **Exhibit A**), the civil complaint filed against the Insiders by the United States Securities and Exchange Commission (copy attached at **Exhibit B**), and the plea agreements of seven other co-conspirators (copies attached at **Exhibits C-I**).[1] The indictment, SEC complaint and plea deals are all incorporated here by reference. The Insiders' misconduct and unfaithfulness to the Debtor substantially violated their purported contracts for services, and, as faithless servants, the Insiders should forfeit all compensation paid to them during the time of their disloyalty.

5. The Trustee files this lawsuit to accomplish two goals on behalf of Dewey's hundreds of creditors. First, the Trustee seeks to recover the millions of dollars the Insiders paid themselves. Second, the Trustee seeks to disallow the Insider's claims for even more millions of dollars from Dewey's estate. The factual and legal support for both modes of relief is overwhelming.

JURISDICTION AND VENUE

6. This adversary proceeding arises out of the bankruptcy of the Debtor and is commenced pursuant to sections 541 through 550 of the Bankruptcy Code and Federal Rules of Bankruptcy Procedure 3007 and 7001.

7. This Court has jurisdiction under 28 U.S.C. §§ 157 and 1334.

8. This is a core proceeding under 28 U.S.C. § 157(b)(2). To the extent necessary, the Trustee consents to entry of a final order or judgment by this Court.

9. The Defendants filed proofs of claim, claim numbers 1068 (DiCarmine) and 1069 (Sanders), against the Debtor's estate in the above-captioned main bankruptcy case and the

[1] All documents attached hereto as exhibits are true and correct copies.

Defendants have been active participants in this case on a number of matters considered by this Court.

10. The Defendants consent to entry of a final order or judgment by this Court.

11. Venue is proper in this Court under 28 U.S.C. § 1409 because the Debtor's chapter 11 case is pending in this judicial district.

PARTIES

12. The Trust was created by the Second Amended Chapter 11 Plan of Liquidation of Dewey & LeBoeuf LLP, Dated January 7, 2013 ("Plan"), which the Court confirmed on February 27, 2013. On March 22, 2013, the effective date of the Plan, the Trust was vested with all causes of action available to the Debtor, excluding those that are Secured Lender Trust assets and those released in the Plan.

13. Defendant DiCarmine is an individual who may be served with process by any manner of service authorized by Rule 7004 of the Federal Rules of Bankruptcy Procedure. Defendant DiCarmine was at all relevant times the Debtor's Executive Director.

14. Defendant Sanders is an individual who may be served with process by any manner of service authorized by Rule 7004 of the Federal Rules of Bankruptcy Procedure. Defendant Sanders was at all relevant times the Debtor's Chief Financial Officer.

THE DEBTOR

15. The Debtor was the product of the combination, on October 1, 2007, of two prominent law firms, Dewey Ballantine LLP ("Dewey Ballantine") and LeBoeuf, Lamb, Greene & MacRae LLP ("LeBoeuf Lamb").

16. The Debtor was at all relevant times a registered limited liability partnership under the Partnership Law of the State of New York ("NYPL").

17. The Debtor was governed by the Dewey & LeBoeuf LLP Partnership Agreement ("DLPA"), which was effective October 1, 2007, and was amended on April 12, 2010, and again on April 3, 2012. Unless otherwise indicated, references to the DLPA are to the version of the document in effect at the time of the alleged events.

18. The Debtor filed a voluntary petition for relief under chapter 11 of the United States Bankruptcy Code on May 28, 2012 ("Petition Date").

THE DEBTOR'S INSOLVENCY

19. From at least 2009, the Debtor was insolvent, unable to pay its debts as they came due, and undercapitalized. The trouble started when Dewey was formed.

A. The Creation of Dewey LeBoeuf

20. Dewey Ballantine was an elite law firm plagued with financial difficulties. Despite wide recognition as one of the most prestigious New York-based firms, it consistently failed to meet financial projections in the years prior to 2007. Extravagant unfunded pension liabilities posed an increasing financial burden that was exacerbated by a decline in the performance of key practice groups. As a result, Dewey Ballantine sought to merge with a larger and more financially sound firm.

21. LeBoeuf Lamb was a New York-based firm with over 700 attorneys at the time of the combination with Dewey Ballantine. Prior to 2007, LeBoeuf Lamb had grown aggressively by acquiring lateral partners, practice groups, and other law firms. Traditionally a law firm specializing in insurance and public utilities, LeBoeuf Lamb sought to become a leader in mergers and acquisitions and other areas that were traditionally Dewey Ballantine's strengths. Merger talks between Dewey Ballantine and LeBoeuf Lamb began in the summer of 2007, resulting in a deal that closed in October 2007.

B. Partner Compensation and "Participation Targets" Under the DLPA

22. The DLPA provided that equity partner compensation was based on the profitability of the partnership. Shares of net profit were allocated among the partners by the Compensation Committee. Early each year, the Compensation Committee would meet and assign partners "Participation Targets" expressed as a dollar amount.

23. A partner's Participation Target was not a fixed salary, and in no way guaranteed a particular distribution. Rather, the Participation Targets were just that—a projection of a partner's share of profits if the Debtor achieved its projected net income.

24. The Participation Targets also served as an allocation tool used in a formula to determine each partner's percentage share of the firm's profits in the event the firm failed to meet projections. Under DLPA § 2.1, each partner's "Percentage Share" of the firm and its profits was calculated by dividing a given partner's Participation Target by the sum total of all Participation Targets. In the event that the firm's net income did not reach the aggregate amount of all Participation Targets (*i.e.*, if the firm failed to meet profitability projections), DLPA § 6.4(a) provided that partner distributions were determined by multiplying individual partner's Percentage Shares by the Debtor's actual net income. DLPA § 6.4(b) required that a partner return any amount received in excess of what was due under DLPA § 6.4(a).

25. In early 2008, the firm's Compensation Committee met to determine Participation Targets for the year. A problem quickly arose from the reconciliation of pay scales for partners from LeBoeuf Lamb and those from Dewey Ballantine. At some pay levels, Participation Targets were higher for legacy LeBoeuf Lamb partners. At other pay levels, the legacy Dewey Ballantine Participation Targets were higher. Rather than split the difference and adjust all

Participation Targets toward a median amount at each pay level, the Debtor instead assigned Participation Targets based on whichever legacy target was higher.

26. Naturally, this decision caused the aggregate Participation Target and projected net income to increase dramatically. Although the DLPA's distribution mechanism could prevent inflated Participation Targets from resulting in over-distributions, it had the negative effect of creating over-optimistic expectations amongst partners. In order for all of the partners' distributions to fall in line with their respective Participation Targets, the Debtor would need to immediately perform at a higher level from a fiscal standpoint.

27. The problem was further compounded by the allocation of inflated Participation Targets to other partners. New lateral hires were brought on with high Participation Targets that did not reflect the firm's economic reality, exacerbating the problem by creating internal competition among partners for equal treatment and compensation. Some legacy partners learned of these arrangements and leveraged their own influence with management to secure similarly inflated Participation Targets.

28. Coupled with the constricting market for legal service providers, the inflated Participation Targets set the stage for frustration and angst among the partners. Some incorrectly viewed their Participation Target as a salary. But the partners were equity holders, only entitled to their proportionate share of firm profits under the DLPA. Although a given partner's distributions could reach his or her Participation Target when the firm's net income met expectations, the Debtor failed to meet the aggregate of Participation Targets from 2008 through the bankruptcy filing. Management never reduced partners' Participation Targets in an amount necessary to bring the aggregate of all Participation Targets in line with realistic expectations for

net income. As a result, individual partners' pro rata share of the firm's income was far less than their Participation Targets.

C. Dewey Was Unable to Pay Debts As They Came Due.

29. The Debtor's economic woes began almost immediately. Having just combined in late 2007, the Debtor faced hurdles in working through the costs of the combination. The Debtor was forced to deal with massive expenses related to the combination, including redundant overhead (such as multiple office leases in the same city, duplicative staffing, and equipment leases), all which necessarily affected the firm's bottom line while it worked toward integration. Of course, these costs were to be expected and may have potentially been overcome. However, the Debtor failed to accurately predict the looming economic downturn and the resulting negative impact on the firm.

30. The Debtor was hit hard by the global economic downturn in 2008 as demand for legal services plummeted. Some clients stopped paying altogether, and receivables were frequently stretched long past due. From 2008 to 2009, the Debtor's audited financial statements reflected that its fee revenue decreased by a staggering $146 million. And during that same period, receivables over 365 days past due increased by almost $14 million. Aged work-in-progress accounts ("WIP") (*i.e.*, work performed but not yet billed) saw similar results, with WIP over 365 days old jumping approximately $10 million from 2008 to 2009 and steadily increasing by almost $24 million from 2008 to 2011.

31. The firm's revenues continued to decrease in 2010, falling by another $49 million from the prior year. And although the Debtor's fee revenue increased by just under $22 million from 2010 to 2011, these improved results were still over $170 million less than the revenue collected in 2008. Moreover, collection issues continued through 2011, as reflected by an

increase of approximately $16 million in receivables over 365 days past due over the prior year. Although future business prospects showed some promise, it was simply too late for the Debtor.

32. As early as February 2008, the Debtor began "holding checks." This meant that Dewey would issue checks to vendors in the ordinary course of business but that, due to cash constraints, management would prevent the checks from being sent out. By April 2008, the Debtor's finance director implemented a standing policy that vendors were not to be paid until at least "net 60 days." In many cases, payments were held up much longer than that.

33. By the middle of February 2008, the Debtor's finance staff divided its accounts payable into "must pay" vendors with "the power to turn the lights out" and other vendors where payments would be delayed for longer periods of time.

34. Dewey's finance staff repeatedly warned partners of the Debtor's inability to pay debts in the ordinary course of business. In February 2008, a finance manager gave this dire warning to a partner by email: "We have a severe cash shortage and can only pay what is absolutely necessary. . . I am not sure if the associate bonuses will be paid this month."

35. In March 2008, Defendant Sanders sent a frantic email to the finance department: "Any reason I'm not getting the cash report anymore . . . please hurry – I'm sweating bullets with the cash position."

36. Critical vendors threatened to cut off service. In March 2008, Lexis Nexis, a legal research service, warned the Debtor that "future service is in jeopardy."

37. The cash crunch went global. In April 2008, the London office was scrambling to pay rent. The Frankfurt office ran out of cash.

38. In August 2008, Dewey's Chief Information Officer complained that Dell, a computer manufacturer, put Dewey on a "credit hold." The CIO demanded to know from the

Debtor's finance staff in an email "Why are we not paying our bills again? This is ridiculous." A staffer replied: "We have been paying invoices as quickly as our cash flow allows. I work continually with [another staffer] and others on the priority vendors to get them paid."

39. During 2009, the Debtor stopped making contractually obligated benefits payments to some former partners. At the time of the merger in 2007, the present value of Dewey Ballantine's and LeBoeuf Lamb's future obligations to retirees was over $60 million. But by early 2009, the firm's cash crunch caused the Debtor to stop making monthly payments to retirees. Following a series of meetings during 2009, the Debtor entered into contracts with certain retirees in an effort to restructure the obligations and improve the Debtor's cash flows. The Debtor ultimately proved unable to meet even the revised payment schedules.

40. Dewey also stopped paying certain "must pay" vendors in 2009. On December 14, 2009, Pitney Bowes, a postage machine vendor, cut Dewey off, leaving the Debtor without the capacity to send metered mail. Service was restored only after Dewey's management intervened and found the money to pay Pitney Bowes's bills, which were then over 120 days past due.

41. Even a bond offering in April 2010 did not resolve Dewey's cash crunch. In May 2010, finance staffers continued to ask for permission to pay the bills, asking "[I]s it ok for [a staffer] to stamp these checks? Fyi, after paying retirement wire we have $4.7 million in cash." "These checks" included $275,000 to pay an invoice from Westlaw, a legal research service, dated September 2009 – approximately seven months earlier.

42. In October 2010, a partner complained that co-counsel in a case had not been paid, even though the client had advanced funds for that purpose. The partner stated "[a]gain,

we face a very embarrassing and inconvenient situation: the client has paid us and we should have paid our co-counsel immediately, and failed to do so."

43. The pattern of holding checks and failing to pay debts as they came due continued until the Debtor filed for bankruptcy in May 2012.

D. Dewey Was Undercapitalized.

44. The financial crisis of 2008 left Dewey severely undercapitalized, a condition from which it never recovered.

45. The Debtor's cash reserves steadily decreased year-over-year in 2009, 2010, and 2011 by $3.5 million, $74.2 million, and $10.4 million, respectively. In fact, cash reserves plummeted from $122.4 million in 2008 to $34.3 million in 2011—a reduction of 72% of the Debtor's capital. This reality exacerbated the cash management problems of the Debtor and was yet another indication that Dewey lacked adequate capital to remain financially viable.

46. The Debtor's lack of adequate capital also prevented the firm from making distributions to partners in line with management forecasts and partner expectations. No law firm can exist without its partners, and the ability to make timely and adequate distributions to partners was absolutely critical to Dewey. Unfortunately, Dewey lacked the capital to do it.

47. When the financial reporting data for the Debtor was completed for fiscal year 2008 – the first full fiscal year of the combined firm – net income fell short of projections by approximately $140 million. This represented a shortfall of nearly 40% based on firm projections. This economic reality caused the firm to make distributions to most partners for 2008 that were well below expectations.

48. In early 2009, Davis proposed that the Executive Committee authorize a "bonus" to partners that would attempt to make up for the shortfall in their projected distributions from

2008. The Executive Committee agreed, and the Compensation Committee approved a slate of Participation Targets for 2009 that included intended bonuses based on the 2008 shortfall.

49. But the Debtor's net profit again fell well short of projections in 2009. Management again proposed make-up bonuses payable in 2010 and 2011. But the Debtor's net profit never improved enough to allow the Debtor to make distributions in line with the inflated Participation Targets and related "bonus" payments. Put simply, the firm could not distribute income it did not earn or receive.

50. By early 2010, the formal distribution system had completely collapsed. The Compensation Committee did not propose Participation Targets in the first half of the year. When the Compensation Committee met toward the end of 2010, it was already clear the Debtor would, yet again, fail to meet its profit target. Rather than adjust projected distributions downward, management again planned to make up for missed Participation Targets in future years. The Compensation Committee allocated to partners both a Participation Target for 2010 and a "bonus" on account of 2008 and 2009 that it planned to pay out over 2010, 2011 and 2012.

51. The Debtor was never able to catch up to expectations for partner distributions, and it was never able to rebuild enough capital to continue as a viable enterprise.

E. Dewey Was Balance-Sheet Insolvent

52. Dewey's liabilities exceeded the fair salable value of Dewey's assets from at least 2009, and continuously until the Petition Date.

53. Dewey's audited financial statements were prepared on a tax-basis or modified cash-basis accounting. This means that the financial statements did not reflect the net realizable value of assets. Nor did the financial statements reflect probable liabilities.

54. For example, the book values presented in the financials overstate the present fair salable value of assets because they include assets with no marketable value (such as leasehold improvements, technology, furniture, and other fixtures).

55. The financial statements also understate probable liabilities on existing debts because they do not include obligations to retirees (such as unfunded pension obligations), future property lease obligations, equipment lease obligations, and other contractual payment obligations.

56. In fact, the Debtor's financial statements do not even include an accrual for accounts payable because the statements were prepared on an income tax cash basis.

57. Properly adjusted to account for the marketable value of the Debtor's assets and the existence of future cash obligations, the financial statements confirm that the Debtor's liabilities exceeded its assets as of December 31, 2008, and during all time periods from that date until the Petition Date.

THE INSIDER DEALS

58. The Insiders' compensation arrangements were not negotiated at arm's length and were well outside the ordinary course of the Debtor's business and industry practice. As the Debtor's financial condition deteriorated, the Insiders paid themselves significant "discretionary bonuses," granted themselves "letters of credit" and arranged for payments to be made to "trusts" for their benefit – putting their self-interest above the interests of the Debtor and its creditors.

59. On or about August 29, 2007, on the eve of the looming merger combination between Dewey Ballantine and LeBoeuf Lamb, Defendant DiCarmine signed an Employment and Long Term Incentive Plan Agreement with the Debtor ("DiCarmine Deal," attached at **Exhibit J**). Though not yet appointed as the Debtor's Chairman, Steven Davis nevertheless signed the DiCarmine Deal on behalf of the Debtor.

60. Similarly, Defendant Sanders signed an Employment and Long Term Incentive Plan Agreement with the Debtor on or about August 29, 2007 ("Sanders Deal," attached at **Exhibit K**). As with the DiCarmine Deal, Steven Davis signed the Sanders Deal on behalf of the Debtor, even though he had not yet been appointed as the Debtor's Chairman.

61. The DiCarmine Deal and the Sanders Deal (together, the "Insider Deals") provided DiCarmine and Sanders with four types of cash compensation from the Debtor, each for a period of six years beginning on January 1, 2008: (i) Contractual Salary; (ii) Contractual Bonuses; (iii) Discretionary Bonuses; and (iv) Trust Payments.

62. **Contractual Salary**. Under the Insider Deals, DiCarmine and Sanders were each to be paid a fixed base salary from 2008 to 2013. DiCarmine's Contractual Salary was $950,000 per annum, or $5,700,000 for the six-year contract term. Sanders's Contractual Salary was $900,000 per annum, or $5,400,000 for the six-year contract term.

63. **Contractual Bonuses**. Under the Insider Deals, DiCarmine and Sanders were each to be paid a fixed bonus from 2008 to 2013. Both DiCarmine and Sanders's Contractual Bonuses were $200,000 per annum, or $1,200,000 each for the six-year term.

64. **Discretionary Bonuses.** DiCarmine and Sanders were each entitled to receive bonuses "based on the economic performance of DL and the performance of the Employee," as determined "at the discretion of the chairman." DiCarmine Deal at § 2; Sanders Deal at § 2. There is no limit under the Insider Deals to the amount of Discretionary Bonuses.

65. **Trust Payments.** Under the Insider Deals, the Debtor was also required to make annual deposits of $200,000 into two irrevocable grantor trusts – one for DiCarmine's benefit ("DiCarmine Trust"), and another for Sanders's benefit ("Sanders Trust"). These annual deposits were to be made on December 31 of each year beginning in 2008 through 2013. Every

three years – once in 2010, and again in 2013 – DiCarmine and Sanders were to receive "the amount of funds in the Trust" from the Debtor. This adds up to an additional $1,200,000 each for the six-year term.

66. All in, non-discretionary payments under the Insider Deals to DiCarmine and Sanders totaled $15,900,000 over six years – with an opportunity for unlimited discretionary bonuses – an astronomically generous arrangement for law firm administrators, and far in excess of the reasonably equivalent value of the services contracted for or provided.

67. The Insider Deals were plainly outside the ordinary course of the Debtor's business.

68. The Insider Deals were entered before the Debtor even existed. Although Davis purported to sign the Insider Deals on behalf of the Debtor, the instruments giving him the authority to act for the Debtor had not been created. Regardless of whether Davis and the Insiders were able to use their positions to cause the Debtor to make the lavish payments called for in the Insider Deals, the creation of those deals was outside the ordinary course.

69. The Insider Deals created an extraordinary conflict of interest. Davis stood to benefit personally from the "poison pill" in the Insider Deals that would force the Debtor to pay millions to DiCarmine and Sanders if Davis were ever replaced. This also proves the Insider Deals were not negotiated at arm's length and that the Insider Deals were totally unlike ordinary employment contracts of the Debtor.

70. Further, the Insider Deals provide that DiCarmine and Sanders could only be terminated for cause, which was narrowly defined as "the commission of fraud or any criminal act by Employee against DL." Ex. J at § 1; Ex. K at § 1. If DiCarmine and Sanders were terminated for any reason other than cause – including, for example, a complete and total

abdication of their job responsibilities – the Insider Deals purport to require the Debtor to pay immediately all remaining payments due under the full term of the Insider Deals plus a penalty of two times the highest annual compensation (including Discretionary Bonuses) for any prior year – a potentially limitless number that would, at the very least, amount to several million dollars. Such one-sided terms do not appear in ordinary employment contracts.

71. The Insider Deals were struck with no serious consideration of any other individuals for the jobs.

72. The Insider Deals did not require any work to be performed by the Insiders at all. The Insider Deals do not so much as mention the titles the Insiders would use or their roles. The Debtor's ordinary course employment contracts, by contrast, had such provisions.

73. These characteristics show the Insider Deals were well outside the Debtor's ordinary course of business. These and other characteristics also demonstrate the Insider Deals fell far outside ordinary industry practice, meaning the business practices of other large law firms based in New York.

74. In the industry, it is common for multiple individuals to be considered for high paying positions. That does not appear to have occurred with the Insider Deals.

75. In the industry, it is common to review prevailing market compensation prior to determining compensation packages for employees. That does not appear to have occurred with the Insider Deals.

76. In the industry, employment contracts generally include a description of the responsibility of the employee. The Insider Deals have no such description or, indeed, any requirement that the Insiders do anything at all.

77. In the industry, it is common for law firms to retain the right to dismiss employees for poor performance. The Insider Deals would force the Debtor to pay millions in severance upon dismissal of the Insiders for anything other than committing a crime.

78. In the industry, it is common for discretionary bonuses to be tied to performance. The Insiders' discretionary bonus payments *increased* as the Debtor's finances crumbled.

79. At best, the Insider Deals were unusual and extraordinary compensation arrangements far outside the ordinary course of the Debtor's business or usual industry practice. At worst, the Insider Deals were outright shams arranged by a group of greedy and unscrupulous business associates to enrich themselves at the expense of the Debtor and its creditors.

THE INSIDERS' WRONGFUL CONDUCT

80. The Insiders engaged in extensive wrongdoing. Some of it was self-dealing of a faithless servant lacking in loyalty and good faith. Some of it may well have been criminal, as the People of the State of New York have alleged.

81. There is no question the Insiders were "insiders" of the Debtor under any definition of the term. Approximately one month after the Debtor entered into the Insider Deals, the Debtor adopted the DLPA, which confirms Defendants' status as insiders of the Debtor.

82. Under the DLPA, the Debtor was to be managed by an Executive Committee, but the Executive Committee could (and did) delegate its powers to the firm's Chairman (Davis). See DLPA § 4.1. As Chairman, Davis was "responsible for the day-to-day management of the business of the Firm." DLPA § 4.6. To fulfill those responsibilities, Davis was empowered to "designate all of the initial non-legal executive and administrative positions of the Firm…" (DLPA § 4.9(a)), which he did, in part, by appointing DiCarmine as the Debtor's Executive Director and Sanders as the Debtor's CFO.

83. Upon information and belief, the Debtor's Executive Committee permitted Davis, DiCarmine, and Sanders to manage the Debtor with little or no oversight. Under Davis, DiCarmine and Sanders exerted substantial control over the Debtor's management decisions.

84. As insiders, the Insiders had a duty of loyalty and good faith to the Debtor. This duty required that the Insiders not engage in self-dealing and not commit fraud.

85. The Insiders abused their position as insiders to arrange special and unusual arrangements for their own personal benefit.

86. In 2007, when arranging the Insider Deals, the Insiders arranged for payments to themselves to be made through trusts. The reason for this was plainly to ensure that the Insiders got paid before other creditors in the event of financial difficulty.

87. In 2008, DiCarmine and Sanders had approximately $1.2 million each of personal loans owed to a certain third-party and related to a personal joint business venture that had nothing to do with the Debtor. DiCarmine and Sanders each transferred their loans to the Debtor, which assumed the debts. The Debtor then entered into promissory notes with DiCarmine and Sanders, on repayment terms with interest rates more favorable than their personal loans. Upon information and belief, no other employee or partner of the Debtor obtained such multi-million dollar, preferential financing from the Debtor. This was an extraordinary, and blatant, example of self-dealing at the expense of the Debtor.

88. In January 2010, the Insiders each obtained an irrevocable standby letter of credit from the Debtor worth $1.9 million. The Insiders even admit – under oath – that the purpose was to ensure that they would be paid before other creditors. See DiCarmine Decl. ¶ 14; Sanders Decl. ¶ 14.[2] The testimony confirms that the Insiders were well aware of the Debtor's financial

[2] On October 22, 2013, Sanders filed in the main bankruptcy case a declaration in support of his response to the Trust's Twenty-Fourth Omnibus Claims Objection. See Docket No. 1775. On the same day – in the same case

condition and, despite such knowledge, chose to favor their own self-interest over the interests of the Debtor and its creditors.

89. Further, in February 2012, Sanders granted himself a purported indemnity from the Debtor for representations made to lenders. The reason could be none other than that Sanders realized the Debtor was going to collapse and someone would eventually discover his accounting fraud. Causing the Debtor to take on responsibility for the Insider's own wrongdoing is a clear example of self-dealing and bad faith. The indemnity was reduced to writing ("Sanders Indemnity Agreement") and would indemnify "oral and written representations and/or certifications to the Firm's lenders under the terms of the Firm's credit arrangements." Sanders Decl. ¶ 15 & Ex. C (copy attached at **Exhibit L**).

90. These are just a few specific and discrete examples of the Insiders acting for their own benefit at the expense of the Debtor. Each one constitutes self-dealing and a lack of loyalty and good faith.

91. The Insiders also deceived others by committing fraud.

92. As early as 2008, the Insiders arranged to "cook the books" to make it appear the Debtor was more financially healthy than it was.

93. The specific fraudulent acts are detailed in the Indictment and the SEC Complaint. The factual allegations in those documents are incorporated by reference and not repeated in full here.

94. There is little question that fraud actually occurred. Seven Dewey employees have already entered plea agreements admitting to their roles in the scheme to inflate the

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and in response to the same objection – DiCarmine filed a similar declaration. See Docket No. 1777. These are the declarations to which this paragraph of the First Amended Complaint refers.

financials and lie to lenders and auditors. (See Exhibits C-I.) The sworn factual statements of the Dewey Seven are incorporated by reference and are not repeated in full here.

95. The accounting fraud of the Insiders continued from 2008 until the Debtor's collapse in 2012. The fraud shows that the audited financial statements of the Debtor cannot be relied upon, except to show that they overstate the financial performance of the Debtor.

96. The State of New York believes the Insiders' conduct was criminal. The criminal allegations are incorporated by reference and are not repeated in full here. The Trustee reserves the right to rely upon the eventual criminal conviction to the extent he does not obtain complete relief on his causes of action on grounds unrelated to the criminal conduct.

THE INSIDERS PAID THEMSELVES

97. While the Debtor was insolvent, the Insiders managed to find the cash to pay themselves their salary and contractual bonuses under the Insider Deals like clock-work.

98. As if the millions in salary and contractual bonuses were not enough, they paid themselves millions more in *discretionary* bonuses – while they were, in their own words, "cooking the books" and the Debtor was on the verge of complete collapse.

99. In 2008, DiCarmine received from the Debtor (either paid to him or for his benefit), Contractual Salary of $950,000; Contractual Bonus of $200,000; and a Discretionary Bonus of $1,011,992, or approximately 88% of his base salary and fixed bonus. In addition, the Debtor funded the DiCarmine Trust with $200,000.

100. In 2008, Sanders received from the Debtor (either paid to him or for his benefit), Contractual Salary of $900,000; Contractual Bonus of $200,000; and a Discretionary Bonus of $1,017,617, or approximately 93% of his base salary and fixed bonus. In addition, the Debtor funded the Sanders Trust with $200,000.

101. In 2009, DiCarmine received from the Debtor (either paid to him or for his benefit), Contractual Salary of $950,000; Contractual Bonus of $200,000; and a Discretionary Bonus of $1,300,000, or approximately 113% of his base salary and fixed bonus. In addition, the Debtor funded the DiCarmine Trust with an additional $200,000.

102. In 2009, Sanders received from the Debtor (either paid to him or for his benefit), Contractual Salary of $900,000; Contractual Bonus of $200,000; and a Discretionary Bonus of $1,300,000, or approximately 118% of his base salary and fixed bonus. In addition, the Debtor funded the Sanders Trust with an additional $200,000.

103. In 2010, the same year the Debtor's cash reserves collapsed by $75 million and the Debtor had to issue bonds to raise cash to stay afloat, DiCarmine received from the Debtor (either paid to him or for his benefit), Contractual Salary of $950,000; Contractual Bonus of $200,000; and a Discretionary Bonus of $900,000, or approximately 78% of his base salary and fixed bonus. In addition, the Debtor funded the DiCarmine Trust with an additional $200,000. At the end of 2010, the DiCarmine Trust disbursed to DiCarmine the $600,000 that the Debtor had deposited in 2008, 2009 and 2010.

104. In 2010, Sanders received from the Debtor (either paid to him or for his benefit), Contractual Salary of $900,000; Contractual Bonus of $200,000; and a Discretionary Bonus of $900,000, or approximately 82% of his base salary and fixed bonus. In addition, the Debtor funded the Sanders Trust with an additional $200,000. At the end of 2010, the Sanders Trust disbursed to Sanders the $600,000 that the Debtor had deposited in 2008, 2009 and 2010.

105. In 2011, DiCarmine received from the Debtor (either paid to him or for his benefit), Contractual Salary of $950,000; Contractual Bonus of $200,000; and a Discretionary Bonus of $900,000, or approximately 78% of his base salary and fixed bonus.

106. In 2011, Sanders received from the Debtor (either paid to him or for his benefit), Contractual Salary of $900,000; Contractual Bonus of $200,000; and a Discretionary Bonus of $900,000, or approximately 82% of his base salary and fixed bonus.

107. Between January 1, 2012, and the Petition Date, DiCarmine received $1,705,848 from the Debtor (either paid to him or for his benefit), consisting of Contractual Salary of $356,250; Contractual Bonus of $200,000; and a Discretionary Bonus of $1,148,077, which is approximately 206% of his base salary and fixed bonus that year.

108. Between January 1, 2012, and the Petition Date, Sanders received $1,683,126 from the Debtor (either paid to him or for his benefit), consisting of Contractual Salary of $338,895; Contractual Bonus of $200,000; and a Discretionary Bonus of $1,144,231, or approximately 212% of his base salary and fixed bonus that year.

109. During the year preceding the Petition Date ("Preference Period"), DiCarmine received from the Debtor total payments (to him or for his benefit) of $2,799,598. Specifically, the Debtor made payment of cash to or for the benefit of DiCarmine in the amount of $951,521 in Contractual Salary, $200,000 in Contractual Bonuses, and $1,648,077 in Discretionary Bonuses pursuant to the DiCarmine Deal during the Preference Period.

110. During the Preference Period, Sanders received from the Debtor total payments (to him or for his benefit) of $2,845,626. Specifically, the Debtor made payment of cash to or for the benefit of Sanders in the amount of $901,395 in Contractual Salary, $200,000 in Contractual Bonuses, and $1,744,231 in Discretionary Bonuses pursuant to the DiCarmine Deal during the Preference Period.

111. All payments made to or for the benefit of DiCarmine and Sanders are summarized on a chart appearing at **Exhibit M**.

112. A detailed listing of all transfers to or for the benefit of DiCarmine and Sanders on account of Contractual Salary, Contractual Bonus and Discretionary Bonus are attached hereto as **Exhibit N**.

113. On or about May 11, 2012, the Insiders were terminated by the Debtor.

LACK OF VALUE TO THE DEBTOR

114. The Insiders oversaw the decline and fall of one of the most prestigious and venerable law firms in the world. The Insiders can blame the recession, but the fact is that the vast majority of other similar-scale law firms weathered the recession without collapsing. Whatever the Insiders thought they were doing, they failed to save the Debtor and instead succeeded only in lining their own pockets.

115. First, the payments under the Insider Deals were not for value because the Insider Deals did not require any value or work to be performed. If the Insider Deals are binding, as the Insiders have claimed, any work the Insiders did would have been gratuitous and therefore not in exchange for the payments they received under the Insider Deals.

116. Second, under New York's faithless servant doctrine, insiders who engage in misconduct in breach of their duties of loyalty and good faith or otherwise act adversely to their employer are not entitled to *any* compensation. This is true even if the services provided value to the employer. Here, the Insiders' conduct fell well below the standards required by New York law, meaning they were not entitled to any compensation. Therefore, the millions in payments they received should be forfeited.

117. Third, even if the Insiders somehow escape the implications of the law as it applies to their faithless conduct, it is far from clear how much value can reasonably be ascribed to their services, if any, in cooking the books and destroying the partnership. Certainly that work did not merit millions in *discretionary* bonuses. The lack of an arm's length negotiation of the

terms of the Insider Deals means that those arrangements are no indication of the true value of the services, if any, to be performed.

118. Fourth, fair consideration under New York law requires good faith. The Insiders did not act in good faith for at least two reasons. For one reason, under New York law, the insider transactions set forth in this First Amended Complaint are designated as *per se* bad faith. Second, for all the reasons described above, the Insiders *actually* acted in bad faith. They lined their pockets at the Debtor's expense. As a matter of law in New York they cannot claim to have provided fair consideration in such one-sided, self-interested transactions.

THE INSIDERS' CLAIMS

119. On September 7, 2012, DiCarmine filed proof of claim number 1068 (the "DiCarmine Proof of Claim") and Sanders filed proof of claim number 1069 (the "Sanders Proof of Claim"; collectively, the "Proofs of Claim"). In the Proofs of Claim, Defendants allege entitlements to: (a) Unpaid Contractual Salary and Bonuses; (b) Change of Control Penalties; (c) Termination Penalties; and (d) Indemnification Damages.

120. Additionally, DiCarmine alleges a claim in an unliquidated amount for hostile work environment against the Debtor.

121. Both Defendants assert a right to "setoff," and that any claims against Defendants should be reduced by the amounts asserted in the Proofs of Claim.

122. **Unpaid Contractual Salary and Contractual Bonuses**. Both Defendants claim entitlement to the *pro rata* share of their Contractual Salary and Contractual Bonus for 2012 (although neither worked for the Debtor after their termination on or about May 11, 2012) and the entire amount of their Contractual Salary and Contractual Bonus for 2013 (although neither worked for the Debtor during 2013 because the law firm was winding down).

123. DiCarmine alleges the Debtor owes him $793,750 in unpaid Contractual Salary and Contractual Bonus for 2012 and $1,150,000 for 2013. See DiCarmine Decl. at ¶ 6.

124. Similarly, Sanders alleges the Debtor owes him $762,500 in unpaid Contractual Salary and Contractual Bonus for 2012 and $1,100,000 for 2013. See Sanders Decl. at ¶ 6.

125. **Change of Control Penalties**. The Insider Deals contained a poison pill in favor of DiCarmine and Sanders if Davis were replaced as the Chairman of the Debtor. Specifically, the Insider Deals define "Change of Control," in part to "mean change in the chairman of DL." See Ex. J at § 1; Ex. K at § 1. If there is a "Change in Control," the Insider Deals purportedly require the Debtor to incur two obligations to DiCarmine and Sanders: (1) "immediately deposit into the Trust all remaining funds due to Employee from December 31 of the year of the Change of Control through December 31, 2013" and "immediately direct the trustee of the Trust to release to Employee all funds allocated to Employee under the Trust"; and (2) "continue to pay Employee each year, not less than the Employee's Highest Employee Compensation Package" – which is defined as the highest amount of money the Debtor paid DiCarmine or Sanders in any year, including all bonuses "through the period ending December 31, 2013." Ex. J at § 6; Ex. K at § 6.

126. Davis was removed as Chairman of the Debtor on or about April 3, 2012.

127. DiCarmine and Sanders have both asserted a claim to Change of Control Penalties allegedly worth millions of dollars. DiCarmine claims to be owed $2,442,115 in Change of Control Penalties and Sanders claims to be owed $2,400,000. DiCarmine Decl. at ¶ 11; Sanders Decl. at ¶ 11. Stated another way, DiCarmine and Sanders claim to be owed over $4.8 million simply because the Debtor's management replaced Davis in an effort to save the firm.

128. **Termination Penalties**. The Insider Deals contain an extremely narrow definition of "Cause" under which the Debtor may terminate DiCarmine and Sanders. Specifically, the Insider Deals define "Cause" as "the commission of fraud or any criminal act by Employee against DL." See Ex. J at § 1; Ex. K at § 1. If there is termination without cause, the Insider Deals purportedly require the Debtor to incur three obligations to DiCarmine and Sanders: (1) "immediately deposit into the Trust all remaining funds due to Employee from December 31 of the year of the Termination…through December 31, 2013"; (2) "deposit into the Trust for the Employee two (2) times the Employee's Highest Employee Compensation Package" – which is defined as the highest amount of money the Debtor paid DiCarmine or Sanders in any year, including all bonuses through the period ending December 31, 2013; and (3) "immediately direct the trustee of the Trust to release to Employee all funds allocated to Employee under the Trust." Ex. J at § 5; Ex. K at § 5 (the "Termination Penalties").

129. The Debtor terminated DiCarmine and Sanders on or about May 11, 2012.

130. DiCarmine and Sanders assert that the Debtor owes them millions of dollars in Termination Penalties. DiCarmine claims to be owed $4,884,230 in Termination Penalties and Sanders claims to be owed $4,800,000. DiCarmine Decl. at ¶¶ 8-10; Sanders Decl. at ¶¶ 8-10. Stated another way, DiCarmine and Sanders claim to be owed another $9.6 million because the Debtor's management replaced them as part of their effort to save the firm.

131. **Indemnification Damages**. Finally, DiCarmine and Sanders have both demanded to be indemnified by the Debtor from all lawsuits filed against them in connection with their pre-petition work for the Debtor, including without limitation, the following pending lawsuits: *Bunsow v. Davis, et al.*, Adv. No. 12-02067 (Bankr. S.D.N.Y.) (hereinafter the "Bunsow Litigation"); *Aviva Life and Annuity Company v. Davis, et al.*, Case No. 4:12-cv-603

(S.D. Iowa) (hereinafter the "Aviva Litigation"); *ePlus Group, Inc. v. DiCarmine, et al.*, Case No. 13 Civ. 2845 (S.D.N.Y.) (hereinafter the "ePlus Litigation"); *McMillan v. Barclays Bank PLC, et al.*, Case No. 13 Civ. 1095 (S.D.N.Y.) (hereinafter the "McMillan Litigation"). To date, DiCarmine and Sanders are asserting Indemnification Damages totaling less than $100,000, but allege that the amount could escalate quickly if any of these matters became active or additional matters were filed.

132. The Insiders' claims for even more payments from the Debtor have no basis in law or fact.

COUNT I

Actual Intent Fraudulent Transfers
Pursuant to 11 U.S.C. § 548(a)(1)(A)

133. The Trustee repeats and re-alleges all allegations set forth in each preceding paragraph of the Complaint as though set forth fully again in support of this claim for relief.

134. Within two years of the Petition Date, the Debtor made transfers to or on behalf of DiCarmine under the DiCarmine Deal totaling $4,949,598. Specifically, the Debtor made payment of cash to or for the benefit of DiCarmine in the amount of $1,901,521 in Contractual Salary, $400,000 in Contractual Bonuses, and $2,648,077 in Discretionary Bonuses pursuant to the DiCarmine Deal during the two years prior to the Petition Date.

135. Within two years of the Petition Date, the Debtor made transfers to or on behalf of Sanders under the Sanders Deal totaling $4,845,626. Specifically, the Debtor made payment of cash to or for the benefit of Sanders in the amount of $1,801,395 in Contractual Salary, $400,000 in Contractual Bonuses, and $2,644,231 in Discretionary Bonuses pursuant to the Sanders Deal during the two years prior to the Petition Date.

136. The payments to DiCarmine and Sanders under the Insider Deals constituted one or more transfers of property of the Debtor to the Defendants.

137. The Debtor made the payments with actual intent to hinder, delay, or defraud one or more entities to which the Debtor was indebted or became indebted on or after the date of such transfers.

138. The circumstances surrounding the Debtor's transfer of the payments reveal several badges of fraud, including, among other things:

139. **Inadequate Consideration.** Defendants were each paid nearly $16 million over six years, including a fixed bonus paid to each of $1.2 million per year, compensation that vastly exceeds what is reasonable or customary for law firm administrators. In addition, under the Insider Deals, DiCarmine and Sanders could only be terminated if they committed fraud or criminal conduct. If they were terminated for any other reason—including for cause other than criminal conduct—they were entitled to additional millions more in penalty payments. For example, the Debtor could not have terminated Defendants without paying a huge penalty even if they altogether stopped performing work for the Debtor. Such an agreement is devoid of true consideration because Defendants were not obligated to do anything. The Insider Deals were not negotiated at arm's length, were a sham, and are therefore a badge of actual fraud.

140. **Close Relationship of Parties.** The Insider Defendants' close association with Davis, and the incentive structure of their Insider Deals are badges of fraud. Davis, DiCarmine and Sanders exerted substantial control of the Debtor's management decisions, including decisions concerning Defendants' own compensation. Their Insider Deals were structured such that Davis's fate and their fate were linked—if Davis was removed as chairman, they were purportedly entitled to (and have asserted here) claims for nearly $5 million. Defendants had

complete control over the Debtor and the Debtor had a management structure that could not be changed without massive penalty payments to DiCarmine and Sanders.

141. **Financial Condition of the Debtor.** The Debtor was insolvent, unable to pay its debts as they came due, and undercapitalized at the time of the transfers. The Insiders knew this, yet effected the transfers for their own benefit and to the detriment of the Debtor and its creditors.

142. **Pattern of Events.** As detailed in the preceding paragraphs, the Insiders not only regularly paid themselves under the Insider Deals, they also provided themselves lavish discretionary bonuses and engaged in a series of self-dealing transactions that demonstrate a clear intention to enrich the Insiders at the expense of the Debtor and its creditors.

143. **Chronology of Events.** The transfers increased in value as the Debtor's financial condition deteriorated, culminating in millions in payments to the Insiders in the months prior to the Debtor's bankruptcy.

144. **Questionable Nature of Transactions.** As detailed in preceding paragraphs, the transfers were far outside the ordinary course of business.

145. These badges of fraud and other badges of fraud support the inference that the transfers to the Insiders were made with actual intent to defraud creditors.

146. Defendants were initial transferees of such transfers and/or the entities for whose benefit the transfers were made.

147. The Debtor made such Distributions within two years of the Petition Date.

148. Pursuant to 11 U.S.C. § 548(a)(1)(A) and 11 U.S.C. § 550, the Trustee is entitled to judgment against the Defendants: (a) avoiding the Insider Deals; (b) directing the Insider Deals to be set aside; and (c) requiring the Defendants, as the recipients of the Insider Deals

and/or persons or entities for whose benefit the Insider Deals were given, to return the proceeds of the Insider Deals, or the value thereof, to the Trustee for the benefit of the Trust.

COUNT II

Actual Intent Fraudulent Transfers
Pursuant to 11 U.S.C. §§ 544 and 550 and
New York Debtor and Creditor Law §§ 276 and 278

149. The Trustee repeats and re-alleges all allegations set forth in each preceding paragraph of the Complaint as though set forth fully again in support of this claim for relief.

150. Within six years of the Petition Date, the Debtor made payments of cash to or for the benefit of DiCarmine in the amount of $4,157,771 in Contractual Salary, $1,000,000 in Contractual Bonuses, $5,260,068 in Discretionary Bonuses, and $600,000 in Trust Payments pursuant to the DiCarmine Deal.

151. Within six years of the Petition Date, the Debtor made payment of cash to or for the benefit of Sanders in the amount of $3,937,500 in Contractual Salary, $1,000,000 in Contractual Bonuses, $5,261,848 in Discretionary Bonuses, and $600,000 in Trust Payments pursuant to the Sanders Deal.

152. The payments to DiCarmine and Sanders under the Insider Deals constituted one or more transfers of property of the Debtor to the Defendants.

153. The Debtor made the payments with actual intent to hinder, delay, or defraud one or more entities to which the Debtor was indebted or became indebted on or after the date of such transfers.

154. The circumstances surrounding the Debtor's transfer of the payments reveal several badges of fraud, including, among other things:

155. **Inadequate Consideration.** Defendants were each paid nearly $16 million over six years, including a fixed bonus paid to each of $1.2 million per year, compensation that vastly

exceeds what is reasonable or customary for law firm administrators. In addition, under the Insider Deals, DiCarmine and Sanders could only be terminated if they committed fraud or criminal conduct. If they were terminated for any other reason—including for cause other than criminal conduct—they were entitled to additional millions more in penalty payments. For example, the Debtor could not have terminated Defendants without paying a huge penalty even if they altogether stopped performing work for the Debtor. Such an agreement is devoid of true consideration because Defendants were not obligated to do anything. The Insider Deals were not negotiated at arm's length, were a sham, and are therefore a badge of actual fraud.

156. **Close Relationship of Parties.** The Insider Defendants' close association with Davis and the incentive structure of their Insider Deals are badges of fraud. Davis, DiCarmine and Sanders exerted substantial control of the Debtor's management decisions, including decisions concerning Defendants' own compensation. Their Insider Deals were structured such that Davis's fate and their fate were linked—if Davis was removed as chairman, they were purportedly entitled to (and have asserted here) claims for nearly $5 million. Defendants had complete control over the Debtor and the Debtor had a management structure that could not be changed without massive penalty payments to DiCarmine and Sanders.

157. **Financial Condition of the Debtor.** The Debtor was insolvent, unable to pay its debts as they came due, and undercapitalized at the time of the transfers. The Insiders knew this, yet effected the transfers for their own benefit and to the detriment of the Debtor and its creditors.

158. **Pattern of Events.** As detailed in the preceding paragraphs, the Insiders not only regularly paid themselves under the Insider Deals, they also provided themselves lavish

discretionary bonuses and engaged in a series of self-dealing transactions that demonstrate a clear intention to enrich the Insiders at the expense of the Debtor and its creditors.

159. **Chronology of Events.** The transfers increased in value as the Debtor's financial condition deteriorated, culminating in millions in payments in the months prior to bankruptcy.

160. **Questionable Nature of Transactions.** As detailed in preceding paragraphs, the transfers were far outside the ordinary course of business.

161. These badges of fraud and other badges of fraud support the inference that the transfers to the Insiders were made with actual intent to defraud creditors.

162. Defendants were initial transferees of such transfers and/or the entities for whose benefit the transfers were made.

163. The Debtor made such Distributions within two years of the Petition Date.

164. Pursuant to 11 U.S.C. §§ 544 and 550 and New York Debtor and Creditor Law Sections 276 and 278, the Trustee is entitled to judgment against the Defendants: (a) avoiding the Insider Deals; (b) directing the Insider Deals to be set aside; and (c) requiring the Defendants, as the recipients of the Insider Deals and/or persons or entities for whose benefit the Insider Deals were given, to return the proceeds of the Insider Deals, or the value thereof, to the Trustee for the benefit of the Trust.

COUNT III

Avoidance and Recovery of Constructively Fraudulent Transfers Pursuant to 11 U.S.C. §§ 548(a)(1)(B)(ii)(I)-(III) and 550

165. The Trustee repeats and re-alleges all allegations set forth in each preceding paragraph of the Complaint as though set forth fully again in support of this claim for relief.

166. Within two years of the Petition Date, the Debtor made transfers to or on behalf of DiCarmine under the DiCarmine Deal totaling $4,949,598. Specifically, the Debtor made

payment of cash to or for the benefit of DiCarmine in the amount of $1,901,521 in Contractual Salary, $400,000 in Contractual Bonuses, and $2,648,077 in Discretionary Bonuses pursuant to the DiCarmine Deal during the two years prior to the Petition Date.

167. Within two years of the Petition Date, the Debtor made transfers to or on behalf of Sanders under the Sanders Deal totaling $4,845,626. Specifically, the Debtor made payment of cash to or for the benefit of Sanders in the amount of $1,801,395 in Contractual Salary, $400,000 in Contractual Bonuses, and $2,644,231 in Discretionary Bonuses pursuant to the Sanders Deal during the two years prior to the Petition Date.

168. The Debtor did not receive reasonably equivalent value for all or part of the transfers made under the Insider Deals; and

169. The transfers made under the Insider Deals were made while the Debtor alternatively (i) was balance sheet insolvent, (ii) held remaining property constituting an unreasonably small capital, or (iii) was unable to pay its debts as they matured.

170. As a result of the foregoing, pursuant to 11 U.S.C. § 548(a)(1)(B)(ii)(I)-(III), the Trustee is entitled to a judgment against the Defendants: (a) avoiding the transfers under the Insider Deals made within two years of the Petition Date; (b) directing the transfers under the Insider Deals be set aside; and (c) requiring the Defendants, as recipients of the transfers under the Insider Deals and/or the parties for whose benefit the Distributions were given, to return the transfers or the value thereof, to the Trustee for the benefit of the Dewey estate.

COUNT IV

Avoidance and Recovery of Constructively Fraudulent Transfers Pursuant to 11 U.S.C. §§ 548(a)(1)(B)(ii)(IV) and 550

171. The Trustee repeats and re-alleges all allegations set forth in each preceding paragraph of the Complaint as though set forth fully again in support of this claim for relief.

172. Within two years of the Petition Date, the Debtor made transfers to or on behalf of DiCarmine under the DiCarmine Deal totaling $4,949,598. Specifically, the Debtor made payment of cash to or for the benefit of DiCarmine in the amount of $1,901,521 in Contractual Salary, $400,000 in Contractual Bonuses, and $2,648,077 in Discretionary Bonuses pursuant to the DiCarmine Deal during the two years prior to the Petition Date.

173. Within two years of the Petition Date, the Debtor made transfers to or on behalf of Sanders under the Sanders Deal totaling $4,845,626. Specifically, the Debtor made payment of cash to or for the benefit of Sanders in the amount of $1,801,395 in Contractual Salary, $400,000 in Contractual Bonuses, and $2,644,231 in Discretionary Bonuses pursuant to the Sanders Deal during the two years prior to the Petition Date.

174. The payments to DiCarmine and Sanders under the Insider Deals constituted one or more transfers of property of the Debtor to the Defendants.

175. Neither the Insider Deals nor the transfers made under the Insider Deals were within the ordinary course of the Debtor's business.

176. The Debtor did not receive reasonably equivalent value for all or part of the transfers made under the Insider Deals.

177. DiCarmine and Sanders are insiders of the Debtor.

178. Defendants received these payments under the Insider Deals and were therefore the initial transferees of such transfers and/or the parties for whose benefit the transfers were made.

179. As a result of the foregoing, pursuant to 11 U.S.C. § 548(a)(1)(B)(ii)(IV), the Trustee is entitled to a judgment against the Defendants: (a) avoiding the transfers under the Insider Deals made within two years of the Petition Date; (b) directing the transfers under the

Insider Deals be set aside; and (c) requiring the Defendants, as recipients of the transfers under the Insider Deals and/or the parties for whose benefit the Distributions were given, to return the transfers or the value thereof, to the Trustee for the benefit of the Dewey estate.

COUNT V

Avoidance of Incurred Obligations as Constructively Fraudulent Transfers Pursuant to 11 U.S.C. §§ 548(a)(1)(B)(ii)(IV) and 550

180. The Trustee repeats and re-alleges all allegations set forth in each preceding paragraph of the Complaint as though set forth fully again in support of this claim for relief.

181. Within two years of the Petition Date, the Debtor incurred obligations to DiCarmine and Sanders under the Insider Deals related to the Unpaid Contractual Salary and Contractual Bonuses, the Change of Control Penalties, the Termination Penalties, and the Indemnification Damages. Specifically, the Debtor incurred these obligations within two years of the Petition Date because the events triggering such obligations – for example (and without limitation), the removal of Davis as Chairman – occurred in 2012.

182. Neither the Insider Deals nor the obligations incurred under the Insider Deals were within the ordinary course of the Debtor's business.

183. The Debtor did not receive reasonably equivalent value for all or part of the obligations incurred under the Insider Deals.

184. DiCarmine and Sanders are insiders of the Debtor.

185. Defendants were the parties for whose benefit the Debtor incurred the obligations under the Insider Deals.

186. As a result of the foregoing, pursuant to 11 U.S.C. §§ 548(a)(1)(B)(ii)(IV), the Trustee is entitled to a judgment against the Defendants: (a) avoiding the obligations incurred under the Insider Deals made within two years of the Petition Date; (b) directing the obligations

incurred under the Insider Deals be set aside and/or avoided; and (c) declaring that the Debtor shall have no further obligations to the Defendants under the Insider Deals.

COUNT VI

Avoidance and Recovery of Constructively Fraudulent Transfers Pursuant to 11 U.S.C. §§ 544 and 550 and NYDCL §§ 273, 274-275, 277-278

187. The Trustee repeats and re-alleges all allegations set forth in each preceding paragraph of the Complaint as though set forth fully again in support of this claim for relief.

188. The Debtor had numerous lessor, trade, pension/retirement, and other creditors with unsecured claims that are allowable under Bankruptcy Code § 502 and that arose prior to the date of each of the payments to the Defendants described in this claim for relief.

189. The Debtor was a partnership and the payments described in this claim for relief were transfers of partnership property from the Debtor partnership to a person not a partner and without fair consideration to the partnership.

190. Within six years of the Petition Date, the Debtor made payments of cash to or for the benefit of the Defendants pursuant to the Insider Deals in the form of Contractual Salary, Contractual Bonuses, Discretionary Bonuses, and Trust Payments.

191. Specifically, the Debtor made payment of cash to or for the benefit of DiCarmine in the amount of $4,157,771 in Contractual Salary, $1,000,000 in Contractual Bonuses, $5,260,068 in Discretionary Bonuses, and $600,000 in Trust Payments pursuant to the DiCarmine Deal within six years before the Petition Date.

192. Specifically, the Debtor made payment of cash to or for the benefit of Sanders in the amount of $3,937,500 in Contractual Salary, $1,000,000 in Contractual Bonuses, $5,261,848 in Discretionary Bonuses, and $600,000 in Trust Payments pursuant to the Sanders Deal within six years before the Petition Date.

193. The amounts identified in the preceding two paragraphs are referred to as the "Contract Cash Transfers."

194. Defendants received the Contract Cash Transfers and were therefore the initial transferee of such transfers and/or the parties for whose benefit the Contract Cash Transfers were made.

195. At the time the Debtor made the Contract Cash Transfers to Defendants, Debtor: (i) was insolvent on the date that such transfers were made or such obligations were incurred, or became insolvent as a result of such transfers or obligations; (ii) was engaged in business or a transaction, or was about to engage in business or a transaction, for which any property remaining with the Debtor was unreasonably small capital; and/or (iii) intended to incur, or believed that the Debtor would incur, debts that would be beyond the Debtor's ability to pay as such debts matured.

196. At all relevant times: (i) the present salable value of the Debtor's assets was lower than the probable value of its liabilities; (ii) the Debtor was unable to pay its debts, contractual and otherwise, as they came due; and (iii) the firm had unreasonably small capital in light of its reasonably anticipated obligations.

197. The Contract Cash Transfers were made without fair consideration, because, although the Contract Cash Transfers arguably were in discharge of an antecedent debt, neither DiCarmine nor Sanders exchanged fair equivalent value for the Contract Cash Transfers. The Contract Cash Transfers were not made in good faith, because they were made by an insolvent partnership to an officer and/or director.

198. As a result of the foregoing, pursuant to 11 U.S.C. §§ 544 and 550 and New York Debtor and Creditor Law §§ 273, 274-275, 277-278, the Trustee is entitled to a judgment against

the Defendants: (a) avoiding the Contract Cash Transfers; (b) directing the Contract Cash Transfers be set aside; and (c) requiring the Defendants, as recipients of the Contract Cash Transfers and/or the parties for whose benefit the Contract Cash Transfers were made, to return the Contract Cash Transfers, or the value thereof, to the Trustee for the benefit of the Dewey estate.

COUNT VII

Avoidance and Recovery of Preferential Transfers Pursuant to 11 U.S.C. §§ 547 and 550

199. The Trustee repeats and re-alleges all allegations set forth in each preceding paragraph of the Complaint as though set forth fully again in support of this claim for relief.

200. The Debtor made payments of cash to or for the benefit of the Defendants in the form of Contractual Salary, Contractual Bonuses, and Discretionary Bonuses during the Preference Period.

201. The Debtor made payments to or for the benefit of DiCarmine in the total amount of $2,799,598 during the Preference Period. Specifically, the Debtor made payment of cash to or for the benefit of DiCarmine in the amount of $951,521 in Contractual Salary, $200,000 in Contractual Bonuses, and $1,648,077 in Discretionary Bonuses pursuant to the DiCarmine Deal during the Preference Period**.**

202. The Debtor made payments to or for the benefit of Sanders in the amount of $2,845,626 during the Preference Period. Specifically, the Debtor made payment of cash to or for the benefit of Sanders in the amount of $901,395 in Contractual Salary, $200,000 in Contractual Bonuses, and $1,744,231 in Discretionary Bonuses pursuant to the DiCarmine Deal during the Preference Period**.**

203. The amounts identified in the preceding two paragraphs are referred to as the "Preferential Transfers."

204. The Preferential Transfers to DiCarmine and Sanders were on account of an antecedent debt – namely, the Insider Deals.

205. DiCarmine and Sanders were either statutory or non-statutory insiders of the Debtor.

206. At the time the Debtor made the Preferential Transfers to the Defendants, the Debtor: (i) was insolvent or became insolvent as a result of such Transfers; (ii) was engaged in business or a transaction, or was about to engage in business or a transaction, for which any property remaining with the Debtor was an unreasonably small capital; and/or (iii) intended to incur, or believed that the Debtor would incur, debts that would be beyond the Debtor's ability to pay as such debts matured.

207. At all times during the Preferential Transfers: (i) the present salable value of the Debtor's assets was lower than the probable value of its liabilities; (ii) the Debtor was unable to pay its debts, contractual and otherwise, as they came due; and (iii) the Debtor had unreasonably small capital in light of its reasonably anticipated obligations.

208. DiCarmine and Sanders received more from the Preferential Transfers than each would have received if the Debtor's bankruptcy case were under chapter 7 of title 11 of the Bankruptcy Code, the Preferential Transfers had not been made, and DiCarmine and Sanders were paid in accordance with the Bankruptcy Code.

209. As a result of the foregoing, pursuant to 11 U.S.C. §§ 547 and 550, the Trustee is entitled to a judgment against the Defendants: (a) avoiding the Preferential Transfers; (b) directing the Preferential Transfers be set aside; and (c) requiring the Defendants, as recipients of

the Preferential Transfers and/or the party for whose benefit the Preferential Transfers were made, to return the Preferential Transfers, or the value thereof, to the Trustee for the benefit of the Dewey estate.

COUNT VIII

Declaratory Judgment Regarding Indemnification Damages

210. The Trustee repeats and re-alleges all allegations set forth in each preceding paragraph of the Complaint as though set forth fully again in support of this claim for relief.

211. There is an actual case and controversy between the Debtor and Defendants regarding whether the Debtor is obligated by contract or operation of law to indemnify DiCarmine and Sanders for liability arising from acts undertaken during the course and scope of their employment with the Debtor.

212. Specifically, DiCarmine and Sanders have demanded indemnity for the Bunsow Litigation, the Aviva Litigation, the ePlus Litigation, and the McMillan Litigation.

213. Moreover, Sanders has alleged he is entitled to indemnification from the Debtor, in part, because of the Sanders Indemnification Agreement. See Ex. L.

214. Based on all the facts alleged herein, the Sanders Indemnification Agreement is not enforceable because it was procured through actual or constructive fraud, among other reasons.

215. To the extent the Sanders Indemnification Agreement was effective, it establishes a transfer subject to avoidance under counts I, II, III, VI, and VII.

216. The Trustee therefore seeks a declaratory judgment that: (a) it has no obligation – by virtue of contract, operation of law, or otherwise – to indemnify DiCarmine or Sanders for acts taken in the course and scope of their employment by the Debtor; (b) it has no obligation – by virtue of contract, operation of law, or otherwise – to indemnify DiCarmine or Sanders in the

Bunsow Litigation, the Aviva Litigation, the ePlus Litigation, or the McMillan Litigation; or (c) additionally and in the alternative, if the Debtor is found to have any obligation to indemnify DiCarmine or Sanders, their indemnity is limited and/or satisfied by the Debtor's procurement of management liability insurance policies under which DiCarmine and Sanders are insureds.

COUNT IX

Declaratory Judgment Regarding Interpretation of the Insider Deals

217. The Trustee repeats and re-alleges all allegations set forth in each preceding paragraph of the Complaint as though set forth fully again in support of this claim for relief.

218. There is an actual case and controversy between the Debtor and Defendants regarding what amounts, if any, the Debtor owes DiCarmine and Sanders under the Insider Deals, with DiCarmine and Sanders alleging that the Debtor owes the Unpaid Salary and Contractual Bonuses, the Termination Penalties and the Change of Control Penalties.

219. For the reasons already stated herein, these obligations are unenforceable. Only in the event that the Debtor's claims (Counts I-VII) are unsuccessful, however, the Debtor pleads additionally and in the alternative that this Court should enter a declaratory judgment construing the Insider Deals as follows: (a) the Insider Deals provide that if there is a Change of Control, DiCarmine and Sanders will continue to be employed by the Debtor "at the sole discretion of the chairman"; (b) there was a Change of Control on or about April 3, 2012; (c) after the Change of Control, DiCarmine and Sanders were employed by the Debtor "at the sole discretion of the chairman"; (d) the Debtor's ability to terminate the employment of DiCarmine and Sanders at the Debtor's discretion superseded the narrow definition of "cause" provided in the Insider Deals; and therefore (e) the Debtor's May 2012 termination of DiCarmine and Sanders did not run afoul of the Termination Penalties contained in the Insider Deals.

220. The Trustee is entitled to judgment against Defendants that properly interprets the Insider Deals, as well as attorneys' fees, costs, prejudgment interest thereon at the legal rate and with such other relief the Court deems just and proper.

OBJECTIONS TO PROOFS OF CLAIM

221. The Trustee repeats and re-alleges all allegations set forth in each preceding paragraph of the Complaint as though set forth fully again in support of this claim for relief.

222. On September 7, 2012, Defendants filed their Proofs of Claim against the Debtor's estate in the above-captioned main bankruptcy case. The Proofs of Claim assert claims on account of Defendants' Insider Deals with the Debtor (for the amounts identified above). Additionally, Defendant DiCarmine has asserted a hostile work environment claim against the Debtor. DiCarmine's Proof of Claim number 1068 is attached hereto as **Exhibit O**. Sanders' Proof of Claim number 1069 is attached hereto as **Exhibit P**.

223. The Trustee hereby objects to Defendants' Proofs of Claim under Bankruptcy Rule 3007(b), providing that objections may be included in an adversary proceeding.

224. The Trustee further fully incorporates by reference and adopts all objections to the Proofs of Claim asserted in any of the Debtor's omnibus objections to claims filed in the main case, including but not limited to the Corrected Twenty-Fourth Omnibus Objection to Claims. See Docket No. 1742.

225. **Debtor is Not Liable on Defendant's Claims.** For the reasons stated above, the Insider Deals are avoidable and/or cannot be enforced according to the terms urged by the Defendants, so the Debtor has no liability to Defendants on their Proofs of Claim. Further, Defendant DiCarmine's hostile work environment claim is not supported by fact or law and should be dismissed.

226. **Defendants' Indemnification Damages Claims Must Be Subordinated as a Matter of Law**. Under 11 U.S.C. § 510(b), even if this Court were to allow Defendants' claims for Indemnification Damages, these claims "shall be subordinated to all claims or interests that are senior to or equal the claim or interest represented by such security." 11 U.S.C. § 510(b).

227. **Defendants' Claims Must Be Subordinated Under Principles of Equitable Subordination**. Even if this Court finds that Defendants' claims have a lawful basis, under 11 U.S.C. § 510(c)(1), those claims should nonetheless be subordinated for purposes of distribution under principles of equitable subordination. Defendants' claims result from their own inequitable behavior, including, among other things, potentially criminal conduct; as insiders, causing the Debtor to commit actual and constructive fraud on its creditors; knowing accounting violations; and breach of their duties of good faith and loyalty to the Debtor.

228. **Defendants' Claims Exceed the Reasonable Value of their Services to the Debtor**. For the reasons stated above, DiCarmine and Sanders were insiders of the Debtor. Thus, their claims must be disallowed to the extent the amount sought exceeds the reasonable value of their services. See 11 U.S.C. § 502(b)(4).

229. **Defendants' Claims Are Subject to Disallowance under 11 U.S.C. § 502(d).** The Trustee objects to the Proofs of Claim under Bankruptcy Code § 502(d) on the ground that the Defendants are liable for the return of property that is recoverable pursuant to 11 U.S.C. Sections 544, 547, 548, and 550, as alleged above. See 11 U.S.C. § 502(d).

RESERVATION OF RIGHTS

230. The Trustee hereby specifically reserves the right to bring any and all other causes of action that it may maintain against the Defendants including, without limitation, causes of action arising out of the same transaction(s) set forth herein, to the extent discovery in this action or further investigation by the Trustee reveals such further causes of action.

231. The Trustee further reserves the right to bring any and all objections to the Proofs of Claim that it may have now or discover in the future upon further investigation and discovery.

PRAYER FOR RELIEF

The Trustee respectfully requests that this Court enter judgment in favor of the Trustee and against Defendants as follows:

a. On the First Claim for Relief, a judgment in the amount of $9,795,224;

b. On the Second Claim for Relief, a judgment in the amount of $21,817,187;

c. On the Third Claim for Relief, a judgment in the amount of $9,795,224;

d. On the Fourth Claim for Relief, a judgment in the amount of $9,795,224;

e. On the Fifth Claim for Relief, a judgment avoiding any and all future obligations that the Debtor may owe the Defendants under the Insider Deals;

f. On the Sixth Claim for Relief, a judgment in the amount of $21,817,187;

g. On the Seventh Claim for Relief, a judgment in the amount of $5,645,224;

h. On the Eighth Claim for Relief, a declaration that the Debtor does not owe any Indemnification Damages to the Defendants;

i. On the Ninth Claim for Relief, a declaration that the Debtor does not owe any Termination Penalties to the Defendants;

j. On the Objection to the Proofs of Claim, disallowance of the Proofs of Claim or, alternatively, subordination of the Proofs of Claim;

k. Any and all pre- and post-judgment interest due; and

l. Such other relief that the Court deems appropriate under the circumstances, including, but not limited to, reasonable attorneys' fees, expenses, and costs.

Dated: New York, New York
June 9, 2014

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