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UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

-----x  
SECURITIES AND EXCHANGE  
COMMISSION,

Plaintiff,

v.

92 Civ. 8314 (JES)

AVELLINO & BIENES, FRANK J.  
AVELLINO and MICHAEL S. BIENES,

Defendants.  
-----x

New York, N. Y.  
January 19, 1993

Before:

HON. JOHN E. SPRIZZO,

District Judge

APPEARANCES

KATHRYN ASHBAUGH,  
Attorney for plaintiff

SQUADRON, ELLENOFF, PLESENT & LEHRER  
Attorneys for defendants

BY: IRA LEE SORKIN  
DORI HANSWIRTH

RICHARDS SPEARS KIBBE & ORBE  
Attorneys for the Trustee  
BY: LEE S. RICHARDS, III, Trustee  
LINDA IMES

1 THE CLERK: SEC versus Avellino.

2 MR. RICHARDS: Good afternoon, your Honor.

3 MR. SORKIN: Good afternoon, your Honor.

4 THE COURT: What is the purpose of the  
5 conference?

6 MR. RICHARDS: Your Honor, we requested it.  
7 There are a couple of items open. The first is the time in  
8 which Price Waterhouse will have to complete the audit,  
9 which is required by the order of the Court.

10 THE COURT: I thought we had a stipulation on  
11 that.

12 MR. RICHARDS: That is correct. It was extended  
13 until today. I am advised by Price Waterhouse that they  
14 require about a month to do an audit, if that is what the  
15 Court and the parties require us to do.

16 We have also put in --

17 THE COURT: Why should I treat this case  
18 differently from the other case?

19 MR. RICHARDS: Your Honor, not being a part of  
20 the other case, I am really not able to address that. I can  
21 tell you that all we know is we have been asked to do an  
22 audit, Price Waterhouse tells me it takes more time than  
23 they have been given to do the audit, particularly with the  
24 absence of records in this case.

25 THE COURT: Then they have to say that they can't

1 give an opinion. In the other case they put a deadline of  
2 January 31. I see no reason why we shouldn't here.

3 Do you want to be heard, Mr. Sorkin? .

4 MR. SORKIN: I do, your Honor. One thing I think  
5 should be brought to the Court's attention immediately: As  
6 your Honor was present, your Honor knows that a week ago  
7 this past Thursday Price Waterhouse, and with Mr. David  
8 Levine, the trustee in the Telfran case, made a rather  
9 impassioned plea on the telephone that they needed until the  
10 end of February.

11 THE COURT: I know that.

12 MR. SORKIN: The fact remains, Judge, that this  
13 past Friday Price Waterhouse handed the keys over to the  
14 Telfran principals and said, "The audit is over. You can  
15 have your office back." This is after a week before they  
16 said they needed until the end of February. So that was  
17 completed. In this particular case, your Honor, they  
18 began -- and I am talking about Price Waterhouse -- on or  
19 about November 18. Through December 31 they have incurred  
20 fees and disbursements in the approximate amount of  
21 \$270,000. For the first two weeks of January, they have run  
22 up another \$60,000 in fees. Yet to this day, to paraphrase  
23 the head of the New York office of the SEC, all the money  
24 was there. There has not been one scintilla of evidence  
25 that the \$330,000 has shown, or the time put in by the

1 legions of Price Waterhouse people has indicated, one, that  
2 any noteholder did not receive all the interest and all the  
3 principal that they were entitled to; and number two, that  
4 any other noteholder as yet undiscovered, exists.

5 Price Waterhouse, your Honor, is here for really  
6 two reasons: I guess the first reason is the extension of  
7 time, which we vehemently oppose.

8 THE COURT: I understand that, but I have given  
9 them until January 31 in the other case; why shouldn't I do  
10 it in this one?

11 MR. SORKIN: For the simple reason, your Honor,  
12 they began earlier than the other case.

13 THE COURT: How much earlier?

14 MR. SORKIN: I believe it is about a week, your  
15 Honor.

16 THE COURT: I should give them until January 24,  
17 to be consistent.

18 MR. SORKIN: If that is your Honor's decision, I  
19 won't argue with that.

20 The second point, your Honor, is that through  
21 that entire period, my clients, Frank Avellino and Michael  
22 Bienes -- Mr. Avellino is in court today -- have had all of  
23 their assets frozen.

24 THE COURT: I know that. That is why I was not  
25 willing to extend it. My knowledge of auditing procedures

1 and accounting procedures is that accountants do an audit on  
2 a test basis; they don't test every transaction. If they do  
3 not think they are in a position to give an opinion, they  
4 will not give one. I am not going to give them forever to  
5 find out whether they can give an opinion.

6 MR. SORKIN: The point also, your Honor, I wish  
7 to note on the record is that it is my understanding that  
8 with the Telfran case they received back approximately 77  
9 percent confirmations; in this case it is over 90 percent,  
10 from what I have been told.

11 THE COURT: If that is the case, they should be  
12 in a position to give an opinion. If they don't want to  
13 give one, they don't have to.

14 MR. SORKIN: The last point, your Honor, is that  
15 they have made their application today, as has Mr. Richards,  
16 a fee application request, to set aside over and above the  
17 quarter of a million dollars that has been put aside to pay  
18 the trustee and the accounts. We were served with these  
19 papers late Friday night.

20 THE COURT: I got those papers and I said,  
21 "Return to sender," because my practice requires a  
22 conference before you file a motion, and I do not allow my  
23 conference procedure to be circumvented by people sending me  
24 letters which are de facto motions.

25 MR. SORKIN: Your Honor, I have nothing else to

1 say.

2 THE COURT: So they have been returned to the  
3 sender without my even reading them.

4 MR. SORKIN: Then I will not address the issue of  
5 the application on behalf of --

6 THE COURT: I could treat this as a pre-motion  
7 conference, but I don't appreciate lawyers sending me what  
8 amounts to a motion in the form of a letter, evading what is  
9 clearly indicated in my rules, a pre-motion conference being  
10 a prerequisite to the filing of any motions.

11 MR. SORKIN: Your Honor, if your Honor does wish  
12 to treat this as a pre-motion conference with respect to  
13 fees, I will reserve whatever time I may have with --

14 THE COURT: For the moment the application to  
15 extend to the end of February or for one month is denied. I  
16 will extend their time to January 24 at 6 o'clock. At that  
17 point Price Waterhouse will either give an opinion or they  
18 won't.

19 MR. SORKIN: I would respectfully request, then,  
20 your Honor, on the opening of business on January 25 --

21 THE COURT: On the representation that they  
22 commenced one week earlier, is that true?

23 MR. RICHARDS: Yes.

24 MR. SORKIN: They began on January 18.

25 MR. RICHARDS: I think that is accurate, your

1 Honor.

2 THE COURT: I dealt with the first issue. Let's  
3 deal with the second.

4 MR. SORKIN: The second issue, your Honor, is  
5 that on the opening of business on January 25, as is the  
6 case with Telfran, that my clients' assets be unfrozen and  
7 they have access to them.

8 THE COURT: I haven't unfrozen them in the other  
9 case, have I?

10 MR. SORKIN: Your Honor did. Your Honor said  
11 that the audit ends on January 31.

12 THE COURT: As of that time it is unfrozen.

13 MR. SORKIN: As of that time. So, if this audit  
14 is to go to the 24th, on the 25th.

15 Lastly, your Honor, if your Honor wishes to treat  
16 this as a fee application on behalf of Price Waterhouse.

17 THE COURT: If they want to make an application  
18 for fees they can, but what I am saying is that I am not  
19 going to freeze your assets or escrow your assets pending a  
20 fee. I am not going to make them a secured creditor is what  
21 I am saying.

22 MR. SORKIN: The only point I wish to make is  
23 that if they wish to address that motion today in a  
24 pre-motion context, I will reserve some time to address  
25 that.

1 THE COURT: They can address it now.

2 MR. SORKIN: I would like the opportunity to  
3 address that.

4 THE COURT: He can file whatever motions he  
5 wants.

6 MR. RICHARDS: It was not our efforts to  
7 circumvent the rules of the Court and I apologize. It seems  
8 to us important that your Honor have the information --

9 THE COURT: Pick up the phone and arrange a  
10 conference. Don't send me a long letter in the nature of  
11 what amounts to a motion application.

12 MR. RICHARDS: The reason to put those papers  
13 before the Court was so that you would have complete  
14 information about the extension.

15 THE COURT: Then your letter should have been  
16 confined to that. You were going to be here for a  
17 conference anyway on that issue, so why send me a letter at  
18 all.

19 MR. RICHARDS: Well, because it seemed to us you  
20 ought to have the documentation with respect to the fees  
21 because Mr. Sorkin is --

22 THE COURT: Why?

23 MR. RICHARDS: Because he is objecting to the  
24 fees, and the fees are obviously important.

25 THE COURT: I will deal with the objection at the

1 appropriate time. That doesn't justify writing me a letter  
2 which amounts to a motion without a pre-motion conference.  
3 My rules are very clear on that.

4 MR. RICHARDS: They are, your Honor. I apologize  
5 for that.

6 THE COURT: Your apology is accepted.

7 MR. RICHARDS: But I did think that the fee  
8 question was relevant to the extension.

9 THE COURT: No, it wasn't. If it was, you could  
10 have brought it up in connection with the conference which  
11 we were having anyway. There was no need to send me a long  
12 letter which is designed for whatever purpose it was  
13 designed for, but it didn't serve any purpose because I  
14 didn't read it. If I read lawyers' letters when they send  
15 me letters of that sort, then that would give them an  
16 advantage, wouldn't it? I operate upon the assumption that  
17 lawyers are trial lawyers presumably because they have the  
18 ability to speak on their feet in open court and therefore  
19 don't have to send me letters when they are fully capable of  
20 telling me on the record in open court what they want to  
21 tell me.

22 MR. RICHARDS: But, your Honor, we thought it  
23 only fair, if not to the Court, at least to Mr. Sorkin for  
24 him to have the documentation with respect to our fees  
25 because, rightly or wrongly, we thought that the question of

1 fees was relevant to the question of the extension.

2 THE COURT: Obviously it is relevant to the  
3 extent that he thinks that you people are proliferating fees  
4 and that is why he opposes your extension, but I don't need  
5 to have the documentation as to the fees for that purpose.  
6 All I need is for Mr. Sorkin to tell me that he thinks your  
7 fees are too high, that is all. He is a lawyer. He used to  
8 be an Assistant U.S. Attorney, too. He can speak on his  
9 feet, presumably.

10 MR. RICHARDS: In any event, your Honor, we would  
11 request permission to file a motion for the fees.

12 THE COURT: You can file whatever motions you  
13 like, but you don't do it in the form of a letter without a  
14 pre-motion conference.

15 MR. RICHARDS: We ask for that permission.

16 THE COURT: You don't need my permission to file  
17 a motion but you just have to have a conference.

18 What is the basis for the motion?

19 MR. RICHARDS: That fees have been incurred by  
20 both institutions, and it was our understanding under the  
21 order that they would be covered.

22 THE COURT: All right. You don't object to the  
23 filing of the motion?

24 MR. SORKIN: Your Honor, I can't object to the  
25 filing of any motion either. They can file whatever motion

1 they want and we will respond in due course.

2 THE COURT: When do you want to file it?

3 MR. RICHARDS: We will be prepared to file it by  
4 the end of the week with respect to the matters that were in  
5 the letter on Friday.

6 THE COURT: All right. File your papers.

7 How much time do you need to respond to it?

8 MR. SORKIN: Your Honor -- Mr. Avellino resides  
9 in Florida -- I will need ten days, your Honor, if I may.

10 THE COURT: Fine. Friday of this week would be  
11 January 22.

12 MR. SORKIN: Your Honor, one second, with the  
13 Court's indulgence.

14 (Pause)

15 MR. SORKIN: May we have two weeks, your Honor?

16 THE COURT: Fine. The matter of fees is not a  
17 matter of urgency. Price Waterhouse, the last I heard, was  
18 not in the process of going bankrupt.

19 MR. SORKIN: Without this case, your Honor, they  
20 might.

21 THE COURT: I don't know.

22 MR. SORKIN: With the fees that they have  
23 incurred on this one. Thank you, your Honor.

24 MR. RICHARDS: Your Honor, one point of  
25 clarification. I don't think it is accurate, as I indicated

1 earlier, to say that we began our audit on November 18.  
2 What we began on November 18 was an effort to verify the  
3 noteholders who could be verified so we could --

4 THE COURT: I assume you apply ordinary auditing  
5 procedures to do that. No auditor I know requires 100  
6 percent testing to give an opinion. If you do, that is news  
7 to me.

8 MR. RICHARDS: But, your Honor, what we do  
9 require is records, and there aren't the records  
10 necessary --

11 THE COURT: That may be, but you don't test all  
12 the transactions. You need records for a sufficient number  
13 of transactions upon which, in accordance with ordinary  
14 auditing practice, you can render an opinion. If they have  
15 tested 70 percent or 60 percent, I cannot believe they are  
16 not in a position to give an opinion now.

17 MR. RICHARDS: I think there are basic records we  
18 need in order to give any opinion at all, and we try to set  
19 those out in the letter.

20 THE COURT: Then don't give an opinion. It  
21 doesn't make any difference to me.

22 MR. RICHARDS: That will probably be the position  
23 we will be in.

24 THE COURT: If Price Waterhouse doesn't want to  
25 give an opinion, they don't have to. No one can force them

1 to give an opinion. But my job is to see that assets do not  
2 stay frozen unnecessarily over time. The reason that this  
3 is happening in the first place is that they agreed to the  
4 freeze order on the assumption that these matters would be  
5 resolved within a relatively brief period of time. If the  
6 understanding or the assumption upon which the agreement was  
7 based has been met, I am not going to keep their freeze  
8 order in existence, since it was by consent. Their consent  
9 is the basis of the freeze order, so I am not going to  
10 extend their consent beyond the parameters of what they have  
11 agreed to. To the extent they oppose an extension to the  
12 24th, I have overruled their objection. I am willing to  
13 stretch it that much further, but not to the end of  
14 February, not until March, not until June, not until  
15 whatever period of time Price Waterhouse thinks is most  
16 comfortable for them. That is not what they agreed to.

17 MR. RICHARDS: I think the point here, your  
18 Honor, is that without the books and records that are  
19 missing, Price Waterhouse cannot render an opinion, and if  
20 the parties and the Court are content for it to say it  
21 can't, then it is not for us to argue, and that is our  
22 position.

23 THE COURT: If they say that they can't give an  
24 opinion, they can't give an opinion. What am I going to do  
25 about that?

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1           You don't care whether they do or whether they  
2 don't, I take it.

3           MR. SORKIN: Your Honor, I don't care what they  
4 say. They can say whatever they want. I just don't want  
5 the implication left with this Court that, based upon the  
6 affidavits which the Court has now rejected but which we  
7 expect to see again, my clients have withheld any records  
8 whatsoever. Every sheet of paper has been turned over to  
9 Price Waterhouse. Price Waterhouse wants records that don't  
10 exist. It is to that extent that Price Waterhouse continues  
11 to say we don't have the records, and it can go on ad  
12 infinitum. To that extent --

13           THE COURT: If you want to sue Price Waterhouse  
14 on the theory that their decision not to issue an opinion is  
15 in some respects a violation of the law, you can do that.

16           MR. SORKIN: Your Honor, these two fine people  
17 from the SEC are the ones who want Price Waterhouse's  
18 opinion. I don't care what Price Waterhouse has to say.

19           THE COURT: All right. Then we agree. You want  
20 two weeks to respond to the application for fees? That is  
21 fair enough.

22           MR. SORKIN: Yes, your Honor, thank you.

23           MS. ASHBAUGH: I am Kathy Ashbaugh of the  
24 Securities and Exchange Commission. As a preliminary  
25 matter, I am not a member of this Court; I do have a

1 certificate outstanding from the State of Massachusetts.

2 THE COURT: Does somebody want to move your  
3 admission?

4 MR. RICHARDS: I will make that motion.

5 THE COURT: I don't think you need it if you work  
6 for a government agency.

7 MS. ASHBAUGH: I am not sure.

8 Your Honor, this is some background so that we  
9 understand why we are having this audit in the first place.  
10 Our allegation in the SEC's complaint is that A&B was an  
11 unregistered investment company for eight years. Had they  
12 been registered with the Commission they would have been  
13 required to have an audit completed each year. So the  
14 completion of this audit is nothing more than what they  
15 should have done in the first place on a yearly basis.

16 THE COURT: So what? What has that got to do  
17 with anything?

18 MS. ASHBAUGH: Just as a matter of background, so  
19 we understand how we got here today.

20 THE COURT: Don't give me irrelevant background.

21 MS. ASHBAUGH: One way to distinguish between  
22 this case and the Telfran case which you heard last week is  
23 simply that this case involves \$450 million, and the Telfran  
24 case involved approximately --

25 THE COURT: In that case they were asking until

1 the end of February.

2 MS. ASHBAUGH: They were asking until the end of  
3 February.

4 THE COURT: And now he says they came in this  
5 week.

6 MS. ASHBAUGH: Apparently they have.

7 THE COURT: So maybe people can do what they are  
8 made to do.

9 MS. ASHBAUGH: In that case there is only \$90  
10 million, in this case there is \$450 million, and it is our  
11 understanding from reading the auditors' papers that --

12 THE COURT: Then they won't give an opinion; too  
13 bad.

14 MS. ASHBAUGH: It is our understanding that part  
15 of the reason that they haven't been able to perform their  
16 audit or complete their audit, which they expected to  
17 complete within two weeks, was that they expected that Mr.  
18 Avellino and Mr. Bienes, who are certified public  
19 accountants, had prepared financial statements and had kept  
20 books and records.

21 THE COURT: Then you bear your burden under the  
22 law of obtaining whatever relief that you think you are  
23 entitled to by me and not with their consent. What I am  
24 saying is, to the extent that they have consented on a  
25 certain basis, I am not going to enlarge the parameters of

1 what they agreed to. If you think you have some other basis  
2 to get the relief you request, make the appropriate showing  
3 and I will let them oppose it.

4 MS. ASHBAUGH: I think my point here is simply  
5 that they should not be allowed to circumvent the completion  
6 of the audit simply by refusing to --

7 THE COURT: What they did is consent to it. If  
8 you have an argument that they were unreasonably interfering  
9 with that, that is fine. I don't hear that argument being  
10 made.

11 MS. ASHBAUGH: I believe that the auditors in  
12 their report have made some argument that --

13 THE COURT: If you make that argument -- and I  
14 will schedule it for a hearing -- you had better be prepared  
15 to prove that, because if you can't prove it, the cost of  
16 the hearing will be imposed upon you personally. We don't  
17 waste their money with your frivolous applications. If you  
18 have evidence to show that they have willfully obstructed  
19 Price Waterhouse's audit, I will reconsider your application  
20 for an extension of time after an appropriate hearing, but  
21 if that hearing proves to be a waste of my time and their  
22 money, your bank account will shrink accordingly. Is that  
23 clear?

24 MS. ASHBAUGH: Yes, your Honor.

25 THE COURT: Now, with that in mind, do you want a

1 hearing?

2 MS. ASHBAUGH: At this time we won't request a  
3 hearing.

4 THE COURT: I suggest you think about it before  
5 you do. Anything else you want to say that is relevant?

6 MS. ASHBAUGH: No, your Honor.

7 THE COURT: Sit down. When do you want me to  
8 hear your application for fees? Do you want a hearing on  
9 that?

10 MR. RICHARDS: I think Mr. Sorkin may. We don't  
11 need to have a hearing, but we will get our papers in by the  
12 end of the week and then if the Court needs to hear it we  
13 will be available for the Court's hearing.

14 THE COURT: Do you want an oral argument or a  
15 hearing? Do you want testimony on this issue?

16 MR. RICHARDS: Normally I would not expect  
17 testimony.

18 THE COURT: Do you want discovery on this issue?

19 MR. RICHARDS: We don't, your Honor. It is up to  
20 Mr. Sorkin.

21 THE COURT: They may.

22 MR. SORKIN: Your Honor, I would like to see  
23 their papers before I make the decision, but I think, your  
24 Honor, if the issues as we read them in these papers that we  
25 were served with are continued to be raised, live testimony

1 may be relevant. We have found, and I will put them on  
2 notice right now, inconsistencies with respect to some of  
3 the material items represented in the papers.

4 THE COURT: When you get their papers, I will  
5 give you two weeks to respond to them. If pursuant to that  
6 response you think a hearing and/or discovery is required,  
7 make that request in your papers and then I will decide  
8 whether to schedule oral argument and/or a hearing.

9 MR. SORKIN: Thank you, your Honor.

10 THE COURT: But on the same ground rules. Don't  
11 ask for a hearing unless it is colorably based. I don't let  
12 people waste my time and their opponent's money. Anything  
13 else?

14 MR. SORKIN: Nothing from me.

15 THE COURT: When is your next regularly scheduled  
16 conference in this case?

17 MR. SORKIN: I don't think we have one.

18 THE COURT: Maybe I should schedule one. How  
19 about March 5?

20 MR. SORKIN: Fine, your Honor.

21 THE COURT: March 5 at 1 o'clock. This case  
22 always seems to take more time than most.

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25