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1 UNITED STATES DISTRICT COURT
2 SOUTHERN DISTRICT OF NEW YORK

3 -----x
4 SECURITIES AND EXCHANGE COMMISSION,

5 Plaintiff,

6 - against -

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

9 Defendants.

10 -----x
11 SECURITIES AND EXCHANGE COMMISSION

12 Plaintiff

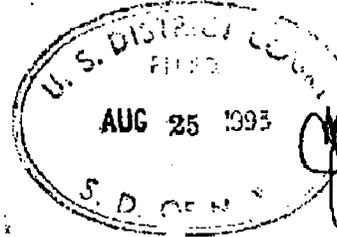
13 - against -

14 TELFRAN ASSOCIATES, LTD.,
15 TELFRAN ASSOCIATES CORP.,
16 STEVEN MENDELOW, and
17 EDWARD GLANTZ,

18 Defendants.

19 -----x

92 Civ. 8314 (JES)



92 Civ. 8564 (JES)

New York, N. Y.
April 21, 1993
11:45 a.m.

20 Before:

21 HON. JOHN E. SPRIZZO,

22 District Judge

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APPEARANCES

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Attorney for Price Waterhouse

1 THE COURT: Does anybody have any witnesses they
2 want to put on? Nobody?

3 MR. SORKIN: Your Honor --

4 THE COURT: I have the affidavits of witnesses.
5 Does anybody want to cross-examine the affidavits?

6 MR. SORKIN: Let me say, your Honor, we have
7 witnesses here. I think the application made by Price
8 Waterhouse, from memory, and we are more than delighted to
9 see what they have to say --

10 THE COURT: They have put in their testimony by
11 affidavit.

12 MR. SORKIN: So did we.

13 THE COURT: The question is, do you want to
14 cross-examine the deponents?

15 MR. SORKIN: At least from our perspective, we
16 responded in our affidavits and we have the witnesses here.
17 If your Honor has any questions, we would be more than happy
18 to address that.

19 THE COURT: Who is here from your side?

20 MR. SORKIN: Everybody.

21 THE COURT: You are objecting to the fees, so I
22 guess it is your burden to go forward.

23 MR. SORKIN: Your Honor, we can do that, or you
24 can hear argument, whatever your Honor wishes. We objected
25 through the affidavits, the affidavits Mr. Avellino, Mr.

1 Bienes, Mr. Glantz.

2 THE COURT: Obviously your affidavits raise
3 questions as to the reasonableness of the order. There are
4 two questions. One is, did they do too much work doing what
5 they did? Two is, did they do what they should have, or
6 should they have come back to me and to you and said: Since
7 your records are in such bad shape, we can't do an audit,
8 therefore we can't give an opinion earlier. Those are the
9 issues.

10 MR. SORKIN: If I can be heard for just a moment,
11 your Honor, I can respond to their position. As I
12 understand from their papers, your Honor, Price
13 Waterhouse -- and I will address the Avellino & Bienes
14 first -- wants \$414,902 in fees and \$13,777 in
15 disbursements.

16 Your Honor, when they entered the case on
17 November 18, 1992, the issue, and really the only issue
18 encompassed in the order, was to perform an audit, which is
19 a term of art, to determine, one --

20 THE COURT: No, it is not so limited. The order
21 says an audit. That is what the order says. You keep
22 changing the order but that is not what it says.

23 MR. SORKIN: In that case, your Honor, I am
24 prepared to put Mr. Avellino on the stand to advise this
25 Court under oath as to precisely what books and records were

1 available, what he told Price Waterhouse, what Price
2 Waterhouse knew on November 18 with respect to what records
3 were available, what records were not available, what
4 records did not exist, what records were provided to them.
5 I will say, your Honor, that between the 18th and the 30th
6 the fees were \$125,000 --

7 THE COURT: There are two questions. Mr. Glantz
8 sharpens the first question more than you do. Mr. Glantz
9 says they spent too much money doing what they were doing.
10 He doesn't so much question what they were doing, but that
11 they come to Florida with three lawyers -- and that is
12 argument -- and he asks, why do you need three lawyers to go
13 to Florida for the first meeting? That is what you may do
14 if you have General Motors as a client, not necessarily what
15 you may do in terms of a trustee.

16 MR. SORKIN: That is with respect to Telfran. I
17 understand that, your Honor.

18 THE COURT: The thrust of Mr. Glantz's affidavit
19 is that we don't need an accountant at \$200 an hour to
20 supervise the mailing of checks. That can be done by
21 clerical people. So, to the extent that there are claims
22 for that, he says they should not have been incurred, not
23 because the audit was wrong or because what they did was
24 wrong, but because they spent too much money doing things
25 that could have been done cheaper. That is one aspect of

1 it.

2 To some extent he does question what they did,
3 more particularly with respect to the \$317,000 claim as to
4 Telfran-A & B. He says, "I told them it was not valid, and
5 then they spent a month investigating it, having all kinds
6 of conferences about it, and then took my deposition and
7 found out it was invalid because the only way they could
8 prove it is if I supported it." He says, "They might just
9 as well have taken my word in the first place."

10 One can make an argument that taking his
11 deposition should not have taken more than twenty minutes
12 and they should not have spent all that time pursuing it.

13 The other argument they make, as I read the
14 affidavits, is that, with respect to the transfer of these
15 personal funds, there are all kinds of moneys spent
16 consulting. There is an argument that there is some water
17 in the law firm's bill when it comes to that. But your
18 client, I take it, is not really challenging the
19 reasonableness of Mr. Richards' fee.

20 MR. SORKIN: That is correct.

21 THE COURT: And you are not claiming that they
22 did work through professional people that should have been
23 done by clerical, which was what Mr. Glantz is claiming.
24 But you are claiming that the whole audit was unnecessary in
25 the first place because it greatly exceeded -- you don't say

1 this expressly, but I think that is the thrust of your
2 affidavit -- what the parties contemplated at the time the
3 consent order was entered into, and to the extent that it
4 was going to go well beyond what the parties contemplated,
5 any further application should have been made or further
6 notice should have been given to you as to how much this was
7 going to cost. I think that is basically the thrust of your
8 argument as I see it.

9 MR. SORKIN: But I will go one step further, your
10 Honor -- that's correct -- but I will also add to that, your
11 Honor, that even to the extent that they did an audit under
12 the view that it was more expansive than it should have
13 been, the work was duplicative, they did things that were
14 totally unnecessary because they knew records did not exist.
15 They were auditing phantom books. They knew from the
16 get-go, from the moment they went in, that certain records
17 did not exist.

18 THE COURT: But that is the same claim. That is
19 a claim that they knew from the beginning that the company's
20 financial records, if you will, or financial statements were
21 essentially unauditible, and therefore they were going to
22 have to do what they say they did, which was in effect
23 become an office manager, which is not what the order
24 contemplated. So it is still the same argument.

25 Your argument is, basically, that once it became

1 apparent to Price Waterhouse that the financial statements
2 of this company or records were in such condition as to make
3 it highly likely that no opinion could ever be given, they
4 should have said, "We can't audit the company's records, and
5 that's it." They should not have gone ahead and tried to do
6 what was essentially undoable, as ultimately concluded.

7 MR. SORKIN: I would also add, your Honor, that
8 in terms of the audit, number one, they received in Telfran
9 98 percent confirms in very short order, and number two,
10 with respect to Avellino-Bienes, it was almost 100 percent.
11 I would also add to that, your Honor, that at a point in
12 time, November 24, with respect to Avellino & Bienes, all
13 the money was there.

14 THE COURT: I know, but they are right when they
15 say they can't take your word for it, they have to test it.

16 MR. SORKIN: I understand that. But there came a
17 point in time where they tested it, your Honor.

18 THE COURT: The question is, do you have to test
19 100 percent?

20 MR. SORKIN: Even beyond 100 percent, the SEC had
21 advised them that all the money was there. We were prepared
22 from the records, the minimal records that --

23 THE COURT: It doesn't appear from the papers
24 that the SEC advised them that all the money was there.

25 MR. SORKIN: There is testimony, your Honor, at

1 least an SEC representative is quoted as saying, that on
2 November 24 all the money was there and they were very
3 surprised. I would add, your Honor, by the time we arrived
4 on December 30 we had objected. And we had objected on
5 November 30 to \$125,000 in twelve days. We continued to
6 voice our objection as to why do you continue to go further
7 when you have no complaints, when all the money has been
8 delivered, all principal and interest has been made. What
9 further audit do you want to take?

10 THE COURT: I know, but that is a basic error in
11 your approach. You seem to think that the only purpose of
12 the audit was basically confirming the identity of the
13 noteholders and whether they got the money they were
14 supposed to get. The order is broader than that. The order
15 says, since you had no financial records which you were
16 required to keep under the law, since you were an
17 unregistered company, there was an additional thing you
18 consented to, which was an audit of your financial
19 statements from 1984 to 1992. That is something separate
20 and apart from whether or not the money was all there and
21 noteholders were identified or whether the noteholders in
22 the company were valid.

23 The problem with this case is that normally, when
24 an accounting firm takes on an engagement, it usually gives
25 an estimate to a client as to what it is going to cost for

1 the engagement. When the time comes that the cost of the
2 engagement appears to greatly exceed the estimates given by
3 the accountant, the procedure is like any other profession.
4 If you go to the TV repairman and he says, "I will fix your
5 set for \$100, that is an estimate," then they also normally
6 say, "Well, it is going to cost \$200 more." At that point,
7 if you were dealing with a tradesman or car mechanic, they
8 give you a written estimate. If the work is going to
9 greatly exceed that estimate, they are supposed to tell you.
10 In the ordinary accounting engagement, there is then another
11 conference between the client and the accountant, where the
12 accountant then says, "Your books and records are in such
13 shape that I cannot do the audit within the price parameters
14 that I have previously discussed with you. Therefore, we
15 are going to have to expand the audit, it is going to cost
16 you more, and you decide whether you want us to audit you or
17 whether you want us to give you no opinion." In the context
18 of a trustee and in the context of an SEC consent order
19 accounting, maybe that practice doesn't follow and it
20 doesn't work that way.

21 So I see this, from your point of view, as
22 largely an argument as to whether or not Price Waterhouse
23 and/or the SEC and/or the trustee brought to your attention
24 as soon as they should have that the audit was going to cost
25 a lot more than the parties intended. As I read your

1 papers, you are saying that the consent order contemplates
2 the return of any sums not needed for that purpose to you
3 and therefore some indication that the parties estimated
4 that this would cost something less than \$250,000.

5 MR. SORKIN: That is correct.

6 THE COURT: It seems to me the only issue I have
7 to resolve, from your point of view, since most of the audit
8 seems to deal with that aspect of the problem as far as your
9 claims are concerned, is whether or not the accountant
10 should have gone back to you and the trustee and the SEC and
11 said, "This is going to cost a lot more money than we
12 planned. Do you still want to do it? And you should have
13 then said, "Well, we don't want to do it." But that choice
14 was never made.

15 MR. SORKIN: Your Honor, let me say that we made
16 timely objection all along. We made the timely objection on
17 the 30th when we appeared in court --

18 THE COURT: But you never withdrew your consent.

19 MR. SORKIN: I understand.

20 THE COURT: Which is your problem. In other
21 words, once it became apparent to you that the audit was
22 going to cost a lot more than the \$250,000, you had the
23 ability to come into court and say to me, "Judge, we
24 consented upon one assumption. That assumption is no longer
25 viable. Now we withdraw our consent because we are not

1 going to pay this money." That is not what you did.

2 MR. SORKIN: To some extent we did, your Honor.
3 You recall when we appeared here on January 16, when they
4 put in the affidavit in violation of your rules, we said at
5 that point in time that the cost --

6 THE COURT: That is after the work had already
7 been done.

8 MR. SORKIN: Not so, your Honor.

9 THE COURT: Most of it. Something like \$116,000
10 of it was done after that.

11 MR. SORKIN: Your Honor, with all due respect,
12 that is not accurate. If I may refresh the Court's
13 recollection, with due respect, by the end of December it
14 had risen to approximately \$280,000. When we appeared in
15 court, on January 16, some two weeks later, there was
16 another \$50,000 between --

17 THE COURT: So that is \$330,000.

18 MR. SORKIN: 330. And then when your Honor
19 said --

20 THE COURT: How much is their bill?

21 MR. SORKIN: \$414,000.

22 THE COURT: That is about \$110,000 that was done
23 thereafter. That is what I was saying. You agree with me.
24 After the 16th there was an additional \$110,000 incurred.
25 Correct?

1 MR. SORKIN: I think it is a little less. I
2 think about \$75,000.

3 THE COURT: My figures are not completely off the
4 wall.

5 MR. SORKIN: Between the 16th and the 25th, your
6 Honor, some nine days, there was another 50 that was
7 incurred.

8 THE COURT: But you could have said back on the
9 16th that we withdraw our consent, and I would have had a
10 hearing on it. That is not what you said. You said we will
11 object to the fees when the time comes. Then they spent
12 \$116,000 more. At that point they could have gotten out and
13 said we are not going to do any more work unless we are sure
14 we will be paid. You both left it to me. I didn't have a
15 clear-cut revocation on either side's part. Both sides left
16 it to me. Now I am left to decide whether I should pay them
17 the money or not pay them the money when this whole problem
18 could have been avoided if people had just said, we want the
19 consent order vacated because the cost of the audit exceeds
20 our expectations.

21 MR. SORKIN: Your Honor, I may not have used the
22 precise words that your Honor suggested, but when they asked
23 until the end of February to continue, both in Telfran and A
24 & B, we specifically said, your Honor, they have run up
25 costs here that are exceeding anything imaginable. They are

1 not finding anything that they didn't know in November with
2 respect to this audit. They are duplicating things. That
3 is why we objected to continuing this audit to the end of
4 February.

5 THE COURT: But you didn't say, "We withdraw our
6 consent to the order."

7 MR. SORKIN: I did not, that is correct.

8 THE COURT: And you didn't do that for a very
9 good strategic reasons: because had you said that, the SEC
10 might have become more aggressive in its enforcement action
11 against you.

12 MR. SORKIN: Absolutely not, your Honor.

13 THE COURT: Why did you consent in the first
14 place? Because you are a good guy?

15 MR. SORKIN: No, because we believed, your Honor
16 that there is nothing more that the SEC can do here with
17 respect to this case. Every penny was paid, principal and
18 interest.

19 THE COURT: Then you didn't need to consent to
20 the order. You could have let the SEC do its own
21 investigation and they would have paid for it.

22 MR. SORKIN: No, we consented to the order, your
23 Honor, with the expectation, as your Honor said, that it
24 would be \$250,000.

25 THE COURT: I know that.

1 MR. SORKIN: For the purpose of determining, when
2 we banged out this order, as the express intent of this
3 order was, are there any noteholders that haven't been paid?
4 Do any exist? That was clearly the intent.

5 THE COURT: The order doesn't say that.

6 MR. SORKIN: Your Honor, it may not say it in
7 those specific words. It said, do an audit and --

8 THE COURT: It says the opposite in very specific
9 words.

10 MR. SORKIN: With all respect, opine on whether
11 there are additional noteholders and whether everyone was
12 paid.

13 THE COURT: That is not what it says. It says
14 audit the financial statements.

15 MR. SORKIN: Subparagraph 1 says audit the
16 financials. Subparagraph 2, opine as to whether anyone --

17 THE COURT: 1 and 2. You seem to think it only
18 says 2. It says 1 and 2. The reason was that, I take it,
19 you were supposed to be doing this all along, and that is
20 one of the things they are going to charge you with, not
21 maintaining adequate books and records.

22 MR. SORKIN: I don't think so, your Honor. I
23 think they are going to charge us with running an
24 unregistered investment company, and then they will
25 bootstrap and say we should have had records for an

1 investment company that wasn't registered. That is what
2 they will probably to do.

3 THE COURT: Why did you consent to this in the
4 first place?

5 MR. SORKIN: We consented to this because we
6 wanted to satisfy the SEC -- I could rehash it -- without
7 coming in with freeze orders and without putting any kind of
8 freeze on the continuing business. We believed that they
9 were entitled to satisfy themselves that in fact there were
10 no additional noteholders and everyone had gotten what he
11 was owed. We had sent out on November 16, your Honor, \$90
12 million. We were then told not to send out any more money
13 because the SEC specifically said, "We don't know where you
14 are sending the money. You could be sending it to nominee
15 accounts and it could be dissipated." I said, "That is
16 fine, we will stop sending out the money." On November 17
17 we held up another distribution of 113 million. When Price
18 Waterhouse came in, that week on the 18th, and between the
19 18th and the 24th did something very quickly and determined
20 that, yes, all the money is there, you can send it out, it
21 was all sent out on November 24 and everybody got satisfied.
22 From November 24 on, your Honor -- they wanted to go on
23 forever -- until you finally stopped them on January 5, they
24 incurred another \$325,000 in fees.

25 THE COURT: Doing something you consented that

1 they do.

2 MR. SORKIN: Your Honor, we consented to an
3 audit. We did not consent to the procedures that they
4 instituted in the audit and duplicated --

5 THE COURT: An audit means an audit conducted in
6 conformity with generally accepted auditing standards, and
7 that means an audit which satisfies the accountant that he
8 can give an opinion until such point as he is satisfied he
9 cannot.

10 MR. SORKIN: We do not believe, your Honor, and I
11 think Mr. Avellino's papers and Mr. Glantz's papers indicate
12 they do not think, that they followed generally accepted
13 auditing procedures. We think there was duplication. Your
14 Honor, I can point to specifics. I don't want to get into
15 minutiae, but it is relevant. They have five hours meeting
16 with Dori Hanswirth in Miami on a day when Ms. Hanswirth was
17 in New York.

18 THE COURT: That is not your problem.

19 MR. SORKIN: That is their problem.

20 THE COURT: That is Glantz's problem. When I say
21 Glantz, Glantz has some arguments that maybe there is a
22 little bit of water in that bill. I am not saying that I am
23 going to give them everything they say that they are
24 supposed to get, because I think there is a little water in
25 that bill. I see a lot of time charges which, in my view,

1 are not specific enough to justify the charges made and
2 which raise an inference that the attorneys' claim to fees
3 should be cut to some degree.

4 MR. SORKIN: Your Honor, we consented --

5 THE COURT: That is not the issue I am discussing
6 with you. I don't know why they had three lawyers go to
7 Florida.

8 MR. SORKIN: Your Honor, I think, without
9 belaboring it, we consented, that is correct, to what was to
10 end on December 30, and they repeatedly came back. In the
11 interest, your Honor -- I must say this -- of satisfying the
12 SEC that there were no further noteholders here and everyone
13 had been paid, the SEC said and Price Waterhouse said, "Will
14 you consent," I believe, "until the 19th?" "Fine."

15 THE COURT: You are arguing an irrelevant
16 question. I am not dealing with the time it took to do the
17 audit. I am dealing with the issue of whether or not you
18 timely pressed your claim that the audit they were
19 conducting was beyond what the parties contemplated and
20 therefore they should give no opinion, period, and stop
21 working. That is the issue. It just seems to me that an
22 accounting firm has that option always, and if Price
23 Waterhouse had said back in January -- you know, their
24 record isn't perfect either -- or December, "If you are
25 going to object to our fees, we are not going to do any more

1 work and we are not going to give an opinion," they would
2 not have spent \$116,000 more. I am thinking that both don't
3 have the best record on that.

4 MR. SORKIN: Your Honor, I think we did timely
5 press it. We did not come to this Court and say we withdraw
6 our consent, but we timely pressed it by advising Mr.
7 Richards on November 30 that we object to \$125,000 for a
8 twelve-day period. We objected when we said we do not want
9 this to go beyond December 30. We were asked if we consent.
10 No way did we believe, your Honor, by consenting for another
11 nineteen days --

12 THE COURT: But you never withdrew your consent;
13 that is the problem.

14 MR. SORKIN: I understand that, your Honor. I
15 clearly understand what the Court is saying. Your Honor is
16 correct, we never formally came to court and objected and
17 sought to withdraw our consent. But we made timely
18 objection to Mr. Richards. When we appeared on January 16,
19 we made timely objection. We made timely objection in the
20 conference calls we had with this Court that this has gone
21 on too long.

22 THE COURT: Therefore, the only issue left to me
23 is not whether the accounting firm expanded or spent more
24 money than the parties contemplated, because I think that
25 issue is foreclosed at this point; the only issue then is

1 whether the records of the company justified the expanded
2 order and additional expense. If I conclude that is so, you
3 lose.

4 MR. SORKIN: We are prepared at this time to
5 address that issue.

6 THE COURT: But you don't even want to
7 cross-examine them on that issue. I have no expert
8 testimony from you as to why this audit did not correspond
9 with GAAS. I read the affidavits. I have had a lot of
10 experience with accounting. It seems to me what they did
11 was perfectly rational, given the records of the company.

12 MR. SORKIN: Your Honor, I am prepared to put
13 witnesses on to say that what the company did, and that part
14 of the auditing work was duplicative and excessive and not
15 necessary.

16 THE COURT: But they are not experts on
17 accounting

18 MR. SORKIN: Your Honor, both my clients, Mr.
19 Avellino and Mr. Bienes, are CPA's.

20 THE COURT: Are they auditors?

21 MR. SORKIN: They have done audits.

22 THE COURT: I will hear from them. Then I will
23 also hear from the Price Waterhouse.

24 MR. SORKIN: That is fine.

25 THE COURT: Looking at the papers, I think what

1 they did was perfectly rational, but I will see what your
2 witnesses have to say.

3

4 F R A N K J. A V E L L I N O, called as a witness in his
5 own behalf, having been duly sworn, testified as
6 follows:

7 MR. SORKIN: May I proceed, your Honor?

8 THE COURT: Yes.

9 DIRECT EXAMINATION

10 BY MR. SORKIN:

11 Q. Mr. Avellino, how old are you?

12 A. 56 years old.

13 Q. Could you tell us something of your education?

14 A. I was educated in New York City at City College.

15 I received a degree in accounting, became certified in New
16 York, and practiced accounting in New York for twenty-six
17 years.

18 Q. How long were you certified?

19 A. I was certified in 1964, I believe.

20 Q. How long did you perform as an accountant?

21 A. From 1957.

22 Q. In your experience did you do audits?

23 A. Yes, I did.

24 Q. How many audits would you estimate for us that
25 you did?

1 A. In my experience, maybe 100, 200.

2 Q. What type of audits were they, just generally?

3 A. They were extensive. They were including public
4 companies, department stores, labor unions.

5 THE COURT: Whom did you work for?

6 THE WITNESS: I worked for a firm that was called
7 Alpert & Heller, which was the predecessor of Avellino &
8 Bienes.

9 THE COURT: Were you ever an audit manager?

10 THE WITNESS: I was a senior auditor and a
11 partner auditor.

12 THE COURT: All right.

13 Q. Mr. Avellino, did there come a time in this
14 particular issue, this case, where you had a conversation
15 with representatives for the first time in Price Waterhouse?

16 A. Yes. I believe it was on either the 17th of
17 November or the 18th of November in our office in New York.

18 Q. Who did you speak to?

19 A. I was in the presence of, I believe, Lee Richards
20 or Linda Imes, the trustees, and Fred Warblow from Price
21 Waterhouse, and I believe Joel Whitman was there too. I
22 don't remember whether he was or not.

23 Q. Tell us, please, the conversation, what you said
24 to them, what they asked of you, to the best of your
25 recollection.

1 A. Basically, I told them at that time what books
2 and records we did have. I told them that our books and
3 records were always prepared for income tax return purposes
4 and no other purpose. I told them that as far as I could
5 recollect at that time that the records I did have were the
6 open years of tax returns which are probably 1989, 1990,
7 '91. And I knew that there were no other books or records
8 for the consent order that said 1984 through 1992. So that
9 they had '89, '90 and '91.

10 Q. Were those records provided to them?

11 A. Yes.

12 Q. Were there any records, Mr. Avellino, that you
13 did not provide to Price Waterhouse at any time when
14 requested?

15 A. I gave them all the records I did have in my
16 possession in New York and in Florida.

17 Q. Did there come a time in one specific instance
18 where they kept making reference to a particular lease that
19 you did not produce for them?

20 A. That lease, the New York office lease, was
21 brought up many, many times. They had asked me about it,
22 and I did supply it to a Geoffrey Cook, who I believe was
23 the managing auditor. I Fed Ex'd it to him from Florida.
24 And then it was asked of me another three times, and every
25 time we referred to it I kept saying that I already sent it.

1 I believe Mr. Cook agreed that he had possession of it, but
2 some other partners or other people in the firm kept saying
3 they didn't have it. That is one of many instances of
4 duplication.

5 Q. Mr. Avellino, can you tell us, please, what
6 records were asked of you that never existed of Avellino &
7 Bienes that you were asked to re-create during the course of
8 this so-called audit?

9 A. I was asked at one point, and maybe more than one
10 time, to re-create, number one, financial statements for
11 1984 through 1988, and I called them phantom records because
12 they didn't exist. As a matter of fact I said, how can I
13 create something that there are no books and records for?
14 And I was asked again, I believe in one of the last letters
15 that I received, please re-create or develop financial
16 statements for those particular years. And we never had
17 them. I kept saying there are no books and records, So I
18 don't even know what you are auditing.

19 Q. Mr. Avellino, in your experience as an auditor,
20 did you ever ask a client on an engagement to re-create
21 records or to create records that never existed?

22 A. When the client tells me that the books and
23 records are not there, I would try to satisfy myself by
24 trying to get some other data that might re-create, if not
25 in full, at least some substantial amount or numbers for

1 particular years that are not in existence.

2 Q. Could you tell us, please, what the scope, as you
3 understood it, was of this audit, in your conversation with
4 Price Waterhouse, and what they advised you they understood
5 the scope to be?

6 A. Well, basically it was my saying to them, and I
7 had a lot of nods over and over again from all Price
8 Waterhouse people involved, I said, as far as I am concerned
9 and from what I see and what I understand, the whole thing
10 here is to determine the liabilities as far as lenders are
11 concerned, the interest owed until November 16, and maybe
12 any undisclosed or unrecorded lenders that may exist. And
13 when I kept saying that, I never got any correspondence or
14 any statements stating, no, it is not so.

15 We went on and on over the same points. The
16 bottom line was that unrecorded liabilities, which is
17 basically the lenders in this case, was a primary object.
18 We go back to the audit which was in that number 1 item of
19 that consent, and I find that "audit" is a generic term in
20 accounting, as we all know. It does have accounting
21 auditing procedures to follow. Never once, even though I
22 know I wasn't the client in this case, was anything
23 presented to me that looked like any form of engagement
24 letter. I was told at one point that the engagement letter
25 was really the consent that I signed, which I agreed to, and

1 it is fine with me, but there was never any definition, I
2 have never seen an engagement letter anywhere, which doesn't
3 make sense to me.

4 Q. Did you ask Price Waterhouse at any time whether
5 there were --

6 THE COURT: Maybe it will make more sense if you
7 thought about the fact that they were not engaged by you.

8 THE WITNESS: No, that I agree with, your Honor.

9 THE COURT: So why would there be an engagement
10 letter?

11 THE WITNESS: Well, because when we are disputing
12 something and we are saying that the dispute is about what
13 is this engagement for, I thought that since I am still
14 paying the bills, that out of courtesy I would at least go
15 back and look at it and see.

16 THE COURT: But they were hired by the trustee
17 and not you and therefore, as you quite correctly state, the
18 engagement letter is a court order?

19 THE WITNESS: True.

20 Q. Mr. Avellino, when you consented to the \$250,000
21 set-aside, if you will, and agreed to that, based upon your
22 experience, did you understand that whatever had to be done
23 would not in any way exceed the \$250,000, since you had the
24 most knowledge of what records existed and did not exist?

25 A. Not only did I think that it was adequate; I

1 thought that in all honesty we would be basically getting
2 some money back.

3 THE COURT: But the audit does not say, as I
4 understand it, that the costs of this audit shall be limited
5 to \$250,000?

6 THE WITNESS: Not that I recall.

7 Q. At what point in time, Mr. Avellino, were you
8 advised that Price Waterhouse received confirms for almost
9 100 percent?

10 A. I believe that by the time -- I am going back by
11 memory, of course -- but I know that when we first started
12 to look at the invoice that came with the bill that came
13 from Mr. Richards' office to you, if I recall, that at that
14 time there was a number and it was probably November 30.
15 And if I recall correctly, as Geoff Cook told me, how much
16 of the
17 responses --

18 Q. Who is Geoff Cook?

19 A. Geoffrey Cook was the managing partner in this
20 audit, who managed this audit.

21 Q. At Price Waterhouse?

22 A. At Price Waterhouse. I recall he told me, I
23 think it was 67 percent, and that was November 30, and
24 remember the checks and the confirmation which were attached
25 to the check went out on November 24.

1 Q. Did there come a point in time when you
2 understood that it had risen even higher than 67 percent?

3 A. In December when we objected again, the numbers
4 were in the 90 percent returns, which I thought was
5 unbelievable.

6 THE COURT: Unbelievable? What do you mean up
7 believable?

8 THE WITNESS: The numbers of any response, in my
9 experience as an auditor in confirmations, when I got back
10 50 to 60 percent, that was a good response, especially on
11 this type of matter. That was a satisfactory test.

12 Q. Did you ask Price Waterhouse at any time
13 thereafter what else they had to do to complete their audit
14 or to satisfy themselves that no other lenders existed and
15 in fact the existing lenders had received all their
16 principal and interest? Did you have conversations with
17 them?

18 A. Well, on December 22, Michael Bienes and I came
19 up to New York, because they had made a request of certain
20 ledgers and papers that they had made copies of, the
21 receipts and disbursements, and the general ledger. That
22 didn't make sense to them because there were items which
23 would be deductible items, negative items in a general
24 ledger, and when they added it up, it wouldn't be add up
25 because it looked like a positive.

1 So I brought up the original books again on
2 December 22, and I had posted the general ledger up until
3 November 30, and gave it to Geoffrey Cook and his associate.
4 They looked at it and they kept it for the day. At that
5 point there were questions that they had asked me in their
6 conduct of the audit, which I thought I had satisfactorily
7 answered. There was a whole list. Some of those answers
8 were already given before, but we clarified it again to make
9 sure that we understood each other. As I recall, I spent
10 that day in New York at the New York office with the
11 auditing staff going over those questions.

12 Q. How many times, Mr. Avellino, after December were
13 you asked to produce documents that you had already advised
14 Price Waterhouse (a) did not exist, (b) did not exist and
15 never existed, or (c) you had already produced for them?

16 A. I believe, after my December 22 meeting, at which
17 I thought I had answered a lot of the questions, I think
18 there was a letter dated January 5 -- I am going by
19 memory -- asking some of the same items that I already had
20 done probably in November and on December 22. And it looked
21 like they made light of some of it, and I was annoyed
22 because making copies and sending voluminous pieces of paper
23 up to New York, when I do it all by myself, was rather
24 annoying when I kept saying to myself, what is it now? And
25 at that same time, I think January 5, they again, knowing

1 that on November 18 that the books and records from '84 to
2 '88 did not exist, had the audacity to say to me again,
3 "Prepare financial statements for those years." I kept
4 saying to myself, what are they talking about? They don't
5 exist.

6 I did supply them with tax returns. Mr. Bienes,
7 in his personal file, attached to his personal tax return,
8 was very smart in keeping a tax return for Avellino & Bienes
9 that corresponded to his personal tax return. And he said,
10 "I do have the returns." I said, "Well, let's stop this
11 now, let's send them the returns." And I even said, "If you
12 are going to audit anything or review anything, look at the
13 tax returns. I write them, I sign them. I tell the United
14 States Government they are accurate and they are correct,
15 with the penalty of going to jail if they are not. And I
16 think they are as good as anything else that anybody would
17 have." So those records were sent.

18 Q. When were they sent?

19 A. I think I sent them on that January 5 request,
20 right after that.

21 Q. Are you aware that Price Waterhouse waited until
22 the end of February to do whatever they were doing?

23 A. Yes, I was.

24 Q. Do you know, from January 5, if anyone from Price
25 Waterhouse told you what they were intending to do that they

1 had not already done?

2 A. No, no.

3 Q. Did they ever say to you why they needed an
4 additional almost two months?

5 A. Nobody ever said why they needed anything for any
6 period of time or for what reasons other than auditing.

7 Q. Did you object to Price Waterhouse continuing to
8 do what you knew they had already done?

9 A. Yes.

10 Q. How often did you object to it?

11 A. Every time I thought that -- when I knew, by the
12 way, the confirmations were in at such phenomenal numbers --
13 and let me add to that, not only were the confirmations sent
14 out to each individual lender via Federal Express, mail
15 which they controlled; it was publicized in every major
16 newspaper in the United States. And I had calls from
17 friends from England that saw it. It was one of those
18 things that I said, this is probably the best confirmation
19 anybody could send out, because if any person saw the name
20 Avellino & Bienes and had lent me money, in 1984, if you
21 will, they would have a great opportunity to call up Mr.
22 Richards and tell him, "We have a loan out there." And what
23 surprised me is that even the phonies and the crazies out
24 there didn't do it. And maybe they did, but I am not aware
25 of it.

1 THE COURT: Did you ever tell Price Waterhouse
2 unequivocally that you would rather have no opinion as to
3 your financial statements than to have them continue to do
4 more work?

5 THE WITNESS: I never said that. I think your
6 Honor said that very well the day I was here in court, I
7 believe on January 16.

8 THE COURT: But you never said, "Look, we don't
9 have the financial statements. If you can't audit it, you
10 can't audit it. Give us no opinion and stop working." Did
11 you ever tell them that?

12 THE WITNESS: I probably never did, but maybe my
13 attorney did, because they never talk to me about anything.

14 THE COURT: Your attorney is not a witness. I am
15 asking you.

16 THE WITNESS: No, I never did.

17 Q. Do you know if Mr. Bienes did?

18 A. Not that I know of. Maybe he did. I don't know.
19 I can't answer for him.

20 Q. There was an issue with respect to \$317,000 that
21 was to be sent to Mr. Glantz and Mr. Mendelow of Telfran.
22 Could you tell us please how much time Price Waterhouse
23 spent trying to resolve that particular issue and what steps
24 you took to help them to try to resolve it?

25 A. Well, \$317,000 was a dispute that I believe was

1 brought by the trustees for Telfran, and at that time when
2 it was brought to my attention I immediately said I don't
3 understand it only because Mr. Levey, the late Mr. Levey and
4 I, who conducted all of our business and nobody else ever
5 did for Telfran or Avellino & Bienes, and Mr. Mendelow being
6 aware of this, that this \$317,000, that so-called in
7 dispute --

8 Q. Who is Mr. Mendelow?

9 A. Mr. Mendelow is a partner of Telfran Associates.

10 Q. Go ahead.

11 A. There was never a dispute as far as the
12 principals of Avellino & Bienes and Telfran Associates were
13 concerned. A major issue is made of the 317,000. We never
14 could understand why. We were told that if we gave
15 affidavits, or depositions that the money wasn't owed and
16 the money wasn't a receivable, that everything would be OK.
17 And even after we did that and spent time and my money and
18 Mr. Glantz's money and Mr. Mendelow's money, there was still
19 an issue until the date as a matter of fact that his Honor
20 released our money on January 25, it was held by Mr.
21 Richards, our trustee, and was finally released even after
22 the 25th of January, even when the Court said that he had to
23 release it.

24 Q. How much time do you recall, from reading the
25 papers of Price Waterhouse, did they spend in trying to

1 resolve an issue that was resolved in your mind by the
2 depositions?

3 A. Well, I think the issue came up --

4 THE COURT: How much time they spent at
5 depositions?

6 MR. SORKIN: Yes.

7 THE COURT: All right.

8 A. At least a month and a half.

9 THE COURT: How much in dollars of time?

10 Q. Do you recall how much in dollars?

11 A. I recall that there were invoices, probably
12 twelve to fifteen thousand dollars.

13 Q. Are you familiar with a gentleman by the name of
14 Joseph Licht?

15 A. Yes, I am.

16 Q. Who is Mr. Licht?

17 A. Mr. Licht is the chief computer principal at
18 Optus Information Systems, Inc.

19 Q. What did Optus Information Systems do, if
20 anything, with respect to Avellino & Bienes?

21 A. Optus Information did our quarterly reporting to
22 our lenders, they prepared the checks, they prepared the
23 statements. On a quarterly basis, on the last day of each
24 quarter, the checks were mailed out by the Optus operation.

25 Q. How long did Price Waterhouse spend with respect

1 to the operations that Mr. Licht performed for Avellino &
2 Bienes in sending out checks and preparing envelopes and
3 doing what Mr. Licht had been doing?

4 A. My recollection is that they went out to Optus
5 offices in Somerset, New Jersey, and did an audit of
6 familiarization of what the program looked like. They must
7 have questioned Mr. Licht to what the procedures were. And,
8 in speaking to Mr. Licht, I think he said they spent either
9 two hours or three hours with him at that time at Optus.

10 Q. And in their affidavit how many hours do they
11 claim that they spent with Mr. Licht?

12 A. Twenty hours.

13 Q. Your partner, Michael Bienes, and maybe we could
14 move this along, could you tell us, please, his background.

15 A. Mr. Bienes is a certified public accountant. He
16 graduated from New York University. He went to work with
17 the Internal Revenue Service. At the time he was hired by,
18 I believe at that time, the firm was Alpern, Heller &
19 Avellino. He was a group chief, the youngest group chief in
20 the history of its time in the Brooklyn office. He has
21 conducted all of our tax examinations, including going up to
22 cases to appellate. He was an expert in taxes. And he did
23 many of the audits that I needed another partner on as we
24 conducted them.

25 Q. Just a few more questions, your Honor.

1 Mr. Avellino, after November 24, when the \$441
2 million was returned to the lenders, were there any books
3 and records that you had which had not as yet been turned
4 over to Price Waterhouse?

5 A. All I could answer is that whatever was asked of
6 me as of November 24, they had. Everything that I owned,
7 everything I had in my possession, my files, my papers. I
8 had made requests of Chemical Bank and the brokerage house
9 to send them statements that I did not have.

10 Q. Between November 18 and November 30 how many
11 people did you utilize -- withdrawn -- in the business of
12 Avellino & Bienes, how many people did you employ to take
13 care of receiving moneys, sending checks out, and keeping
14 books and records on computer, as well as on ledgers?

15 A. It was the existing staff that I had of three
16 people in the New York office, and Mr. Licht, his staff at
17 Optus, and my staff in Florida.

18 Q. Between November 18 and November 30, how many
19 Price Waterhouse people descended, if you will, upon your
20 office in New York which incurred fees of almost \$125,000 in
21 that twelve days?

22 A. On any given day there were anywhere between five
23 to seven people on an average day.

24 Q. In one of the affidavits, Mr. Avellino, there is
25 a reference to them spending 1 1/2 to 2 hours, approximately

1 seven people looking through the files of the individual
2 lenders. Do you recall that?

3 A. Yes.

4 Q. How thick were these files that required, as they
5 say, between 1 1/2 and 2 hours per file to look through?

6 A. The average file has the original letter from a
7 certain lender, it probably has a receipt that goes back to
8 the lender after they sent a check to Avellino & Bienes, and
9 it might have any other correspondence which relates to we
10 need some withdrawals, we need a change of address, we now
11 will enclose something that will leave this money to my
12 child, my grandchild or whatever.

13 So the file, any file, the normal files, other
14 than the Telfran file which they relate to, is anywhere from
15 three to four or five pieces of paper. That is about it.

16 MR. SORKIN: May I have just a moment, your
17 Honor.

18 (Pause)

19 Q. Do you recall at some point in time, Mr.
20 Avellino, Price Waterhouse submitting an affidavit to this
21 Court which his Honor, Judge Sprizzo, said had been
22 submitted in violation of his rules?

23 A. Yes.

24 Q. Do you recall in the papers submitted by Price
25 Waterhouse how much they want for the affidavit that was

1 submitted in support of their fee application, how much time
2 they put in, in preparing such an affidavit?

3 A. I may not remember the time, but I remember it
4 was about \$30,000 in preparation.

5 Q. And that is what they are asking for in
6 preparation?

7 A. Yes.

8 Q. There is also a reference to them spending some
9 time supervising Mr. Licht in sending out checks. Do you
10 recall that in their papers?

11 A. Yes.

12 Q. Do you know how much time they spent supervising,
13 if at all, Mr. Licht, according to your information and
14 discussions with Mr. Licht?

15 MR. SORKIN: Your Honor, I am trying to move this
16 a long. Mr. Licht is in court today.

17 THE COURT: I know. I read the affidavit.

18 A. I don't know time. All I know is that when I
19 read the first papers that were not accepted by the Court,
20 that it said that somebody supervised Mr. Licht in the
21 printing of checks. And I laughed at it only because I know
22 that the printer prints the checks and nobody has to
23 supervise once the input is in, and that it would take at
24 least a 24-hour to a 36-hour time to print checks. As a
25 matter of fact, you could almost go to sleep while the

1 printer is on. When I called up Mr. Licht about that, I
2 said, "Was anybody with you when you gave the command to the
3 computer to print checks?" He said, "No one was with me. I
4 was here by myself." And I said, "I don't understand,"
5 because they said they were there supervising the printing
6 of the check. And I think their invoice shows that they
7 were there supervising the printing of the checks.

8 Q. Do you recall how much they are charging or they
9 claim in fees for the supervising and distribution of the
10 checks?

11 A. If I recall correctly, \$5,000 or \$5,700.

12 Q. Would it refresh your recollection if I told you
13 \$23,000?

14 A. It would.

15 Q. Does that refresh your recollection?

16 A. Yes, it does.

17 Q. Is it \$23,000?

18 A. It can't be. I don't see how. It is \$23,000,
19 but I don't see how.

20 Q. I am asking you, is your recollection refreshed
21 as to what their claim is?

22 A. Yes. \$23,000.

23 MR. SORKIN: I have no further questions of Mr.
24 Avellino.

25 THE COURT: Who represents Price Waterhouse? .

1 MR. BRESLOW: Richard Breslow, your Honor, Price
2 Waterhouse, Assistant General Counsel.

3 THE COURT: Just a question for you before you
4 start.

5 Do we have a claim for the affidavits in
6 connection with this application in addition to the \$30,000
7 for the last one?

8 MR. BRESLOW: No, Judge.

9 THE COURT: So it is one or the other and not
10 both.

11 MR. BRESLOW: That is correct, your Honor.

12 THE COURT: All right. I will not deny you the
13 \$30,000 if I think the \$30,000 is reasonable and if you are
14 not seeking fees in connection with this application.

15 MR. BRESLOW: That's correct, Judge.

16 THE COURT: I am not going to do it twice. But I
17 won't deny you fair payment for what had to be done in any
18 event.

19 MR. BRESLOW: Thank you, your Honor.

20 CROSS-EXAMINATION

21 BY MR. BRESLOW:

22 Q. Mr. Avellino, you mentioned on direct you are an
23 accountant, is that correct?

24 A. Yes.

25 Q. And you have done a couple of hundred audits?

1 A. Yes.

2 Q. Are you familiar with the term "financial
3 statements"?

4 A. Yes.

5 Q. Can you describe to the judge what in your
6 judgment financial statements mean?

7 A. Balance sheet, profit and loss or income and
8 expense statement, and the attached notes and comments to
9 the financials.

10 Q. You were aware, were you not, sir, in the middle
11 November, at the time the consent order was being
12 negotiated, that the consent order contained a provision
13 requiring the trustee to oversee audits of Avellino & Bienes
14 financial statements --

15 THE COURT: You have to talk a little slower. I
16 know I am the worst person in the world to tell you. The
17 court reporter may be used to me but he may not be used to
18 you.

19 MR. BRESLOW: Understood.

20 Q. Were you aware, Mr. Avellino, in the middle of
21 November that the consent order your firm was about to sign
22 contained a provision stating the firm would consent to
23 audits of your firm's statements from 1984 to 1992?

24 A. Yes.

25 Q. Were you aware at the time that your firm didn't

1 have financial statements for those years?

2 A. Yes.

3 Q. You mentioned also in your direct that in early
4 November or the middle of November, after the order was
5 signed, you had a meeting with people from Price
6 Waterhouse -- Mr. Werblow, Mr. Whitman, perhaps Mr. Cook; is
7 that right?

8 A. Yes.

9 Q. Didn't the people from Price Waterhouse at that
10 meeting tell you they intended to conduct an audit of A &
11 B's financial statements?

12 A. I met them on November 17 or 18, when I knew that
13 they were going to be engaged by Mr. Richards to conduct an
14 audit. That is the time.

15 Q. And didn't they tell you, sir, at that meeting
16 that they intended, in accordance with the order, to do an
17 audit of A & B's financial statements from 1984 to 1992?

18 A. They told me nothing.

19 Q. No one told you?

20 A. No. They sat there. They said nothing. The
21 testimony will probably show it was a deposition and it
22 was --

23 THE COURT: I don't think you have to worry about
24 that. The order says it.

25 MR. BRESLOW: Thank you.

1 THE COURT: I am not going to be receptive to an
2 argument that you had any obligation to tell them what was
3 in the written order which he had signed or his lawyer had
4 signed in his behalf.

5 Q. Mr. Avellino, did there come a time in late
6 November or early December of '92 when you became aware that
7 Price Waterhouse was trying to do an audit of A & B's
8 financial statements?

9 A. Yes.

10 Q. When did that happen, sir?

11 A. It probably happened the day they walked out of
12 my office on November 17.

13 Q. Am I correct, sir, that you never told anybody
14 from Price Waterhouse face to face that they should stop
15 trying to do an audit of A & B's financial statements?

16 A. No, I never had any discussion like that.

17 Q. Did there come a time when the people from Price
18 Waterhouse asked you to create financials from A & B?

19 A. Yes.

20 Q. What was your response, sir?

21 A. My response was that I couldn't create what
22 wasn't available and what didn't exist.

23 THE COURT: But did you tell them -- and this is
24 important from my point of view -- that you could not create
25 the financial statements because adequate records for the

1 preparation of those statements did not exist?

2 THE WITNESS: Yes, your Honor. That is exactly
3 what I told them. And they were aware of it.

4 THE COURT: That is not what you said on direct
5 and it is not what you said just now. So what I want to
6 find out is, did you say you wouldn't do it because the
7 statements didn't exist or did you say that the company did
8 not have adequate records upon which the preparation of
9 financial statements nunc pro tunc could be made?

10 THE WITNESS: I can't recall exactly, but the
11 intent was that the records were --

12 THE COURT: I don't care what your intent was.
13 What I want to know is what you said. Twice you testified
14 in a certain way, and I want to be sure that that testimony
15 is accurate. My question is very specific. Would you like
16 to have it read back?

17 THE WITNESS: Yes, your Honor.

18 (Record read)

19 THE WITNESS: I said I could not prepare
20 financial statements because I didn't have any books,
21 records, or data to prepare financial statements for 1984
22 through 1988.

23 THE COURT: All right. Go ahead.

24 THE WITNESS: That is exactly what I said.

25 THE COURT: It is not what you said on direct.

1 THE WITNESS: You are right.

2 THE COURT: I have to resolve the inconsistencies
3 insofar as they bear upon your credibility as a witness.

4 Q. Mr. Avellino, do you recall sending a letter to
5 Mr. Cook at Price Waterhouse on or about January 5 of this
6 year?

7 A. Yes.

8 Q. And that was a letter in response to Mr. Cook's
9 request for information from you, is that right?

10 A. Yes.

11 Q. And one of the things Mr. Cook had asked you is
12 to prepare financial statements, is that right?

13 A. Yes. By the way, it wasn't the first time he had
14 asked me to do that.

15 Q. Let me read a paragraph of the letter to you,
16 sir.

17 A. Please.

18 Q. See if this refreshes your recollection.

19 "Item 11. I spent a long time explaining to Mr.
20 Stalmanis that this task is a long and tedious one from the
21 point of accuracy. In the past I spent a long time of labor
22 to accomplish this preparation of income and expenses for
23 income tax purposes. With not all of the information
24 available, for the checks and balances to prepare a true and
25 accurate statement, I am prone to not attempt this task at

1 this time. My experience has taught me to not commit any
2 figures to scrutiny when, as in this case, it can be
3 construed as 'bible' and subject to criticism."

4 Did you follow that?

5 A. I definitely do.

6 THE COURT: Now you recall seeing it in the
7 papers?

8 THE WITNESS: Could I add to that? The inference
9 I --

10 THE COURT: No. Your lawyer can deal with it on
11 redirect. He is bringing this out as an inconsistency. If
12 your lawyer thinks it is not correct, he can bring it out.

13 Q. Mr. Avellino, it is your testimony that you never
14 told anyone that you had agreed to prepare financial
15 statements for A & B?

16 A. Repeat that, please?

17 Q. Is it your testimony, sir, that you never told
18 anybody, whether it was the trustee, your counsel, anybody
19 at Price Waterhouse, you never told anybody at any point in
20 time that you had agreed to prepare financials for A & B?

21 A. I don't recall.

22 Q. You also mentioned, sir, in your direct testimony
23 that you had attended a meeting in New York on December 22,
24 I believe?

25 A. Yes.

1 Q. Were people from Price Waterhouse at that meeting
2 with you?

3 A. Yes.

4 Q. Do you recall at that meeting that people at
5 Price Waterhouse stated that because of the lack of books
6 and records they couldn't do an audit of the financial
7 statements and proposed instead to do an audit based upon
8 your tax returns? Do you recall that?

9 A. I think I told them that. They didn't tell me
10 that.

11 Q. Do you recall agreeing with them that that was a
12 good idea?

13 A. Yes.

14 Q. So you know then in the middle of December that
15 Price Waterhouse was continuing to do an audit based upon
16 your tax returns?

17 A. Yes.

18 Q. And you agreed with that, right?

19 A. Yes, I knew it on November 17.

20 Q. You also mentioned on your direct, Mr. Avellino,
21 that you talked about what the average file looked like at
22 Avellino & Bienes. But you are aware that Price Waterhouse
23 wasn't looking at just the average files? Aren't you aware
24 of that?

25 A. They had all of the files.

1 Q. Do you know which ones Price Waterhouse looked to
2 review?

3 A. No, they never told me.

4 Q. Did you ever ask them?

5 A. No, I had no reason to. They had 3,200 files.

6 It was their files and they could do whatever they want. I
7 assumed they could look at the 3,200 if they wanted to.

8 THE COURT: Did you see what files they reviewed?

9 THE WITNESS: No, because I was not present. And
10 every time one of their people came and pulled files from
11 the drawer, they would walk back to the back room with the
12 files.

13 Q. So you don't know which files Price Waterhouse
14 looked at?

15 A. I have no idea.

16 MR. BRESLOW: I have no further questions, your
17 Honor.

18 THE COURT: Anything further?

19 MR. SORKIN: Yes.

20 MR. LEVINE: Your Honor, David Levine from
21 McDermott, Will & Emery, counsel for the trustee.

22 THE COURT: You are not involved in this one.

23 MR. LEVINE: I am not, your Honor, except there
24 were some questions raised on the issue of the \$317,000. I
25 don't want to interrupt, but that is also an objection that

1 has been made to our fee application in the Telfran case.

2 THE COURT: But I think their objection is more
3 specific. Their objection is to the time that Price
4 Waterhouse spent after the depositions. I think that was a
5 very specific claim which I will have them explain to me.
6 But I don't really understand why it was necessary to spend
7 \$15,000 or so after the depositions that confirm that the
8 claim was for one reason or another not provable.

9 MR. LEVINE: Your Honor, I can withhold this
10 until the Telfran issues come up. My questions to Mr.
11 Avellino would be related to the issue of \$317,000 and how
12 that issue arose and what the documents showed.

13 THE COURT: I will allow that.

14 MR. LEVINE: We can save time if I could just ask
15 him.

16 CROSS-EXAMINATION

17 BY MR. LEVINE:

18 Q. Mr. Avellino, can you tell the Court, please, who
19 Mr. Aaron Levey was?

20 A. Mr. Levey was the partner of Telfran Associates.

21 Q. When did he die, sir?

22 A. I believe he died in September.

23 THE COURT: 1992?

24 THE WITNESS: 1992.

25 Q. After his death, sir, were there statements

1 generated from Avellino & Bienes, through the Optus system
2 or otherwise, to Telfran showing a commission payable by
3 Avellino & Bienes to Telfran of \$317,000?

4 A. Probably, yes.

5 Q. Do you know, sir, whether or not those statements
6 were generated after Mr. Levoy's death?

7 A. They may have been, yes.

8 Q. Did you, sir, prepare an affidavit in opposition
9 to the trustee of Telfran's claim for that \$317,000?

10 A. Yes, I did.

11 Q. Who prepared that affidavit for you?

12 A. I believe my attorneys did.

13 Q. That would be the firm of --

14 A. Ira Sorkin, I think, prepared it, and Dori
15 Hanswirth.

16 Q. In accounting parlance, this would be an
17 intercompany claim if it existed between Telfran and A & B
18 or Avellino & Bienes; is that correct?

19 A. It is not intracompany because Telfran has
20 nothing to do with Avellino & Bienes. That would be an
21 intercompany if it were represented.

22 THE COURT: That would be intercompany if it were
23 between two unrelated companies.

24 Q. Between the two companies?

25 A. It would just be a payable.

1 Q. Was that law firm, at the time this claim arose,
2 also representing Telfran, to the best of your knowledge?

3 A. Yes.

4 Q. In your affidavit, on what basis did you dispute
5 the claim by Telfran against Avellino & Bienes?

6 A. I think we have to backtrack and talk about the
7 memo that everybody has been referring to. There was always
8 some type of memo coming from Avellino & Bienes to Telfran,
9 for preparation for September 30, in this case being a
10 quarter ending. So that Telfran would know how much money
11 it needed to pay its people, its lenders, interest, etc.
12 And Optus, because of a tool that we used, that I used with
13 Mr. Levey, rather than sitting on the phone, which I had
14 done in previous years hour after hour after hour, I decided
15 why don't we just automatically say: Send a memo to Telfran
16 stating what the approximate dollars will be that they will
17 need to pay the lenders for any particular quarter. So that
18 Optus, not knowing any other agreements or internal affairs
19 of Avellino & Bienes or Telfran, would just normally,
20 without my directing it, would send some papers to Telfran
21 periodically, in this case probably on a monthly basis.

22 THE COURT: The question is, why what did you say
23 in your affidavit about it?

24 Q. Did you refer, sir, to an oral agreement with the
25 man who is now dead, Aaron Levey?

1 A. Yes. All of my agreements with Mr. Levey, by the
2 way, were oral, going back to 1960.

3 Q. Did you say, sir, based on this alleged oral
4 agreement, that the relationship on this \$317,000 had
5 changed?

6 A. Yes. It had changed. It wasn't owed, it wasn't
7 existent.

8 Q. Was there anything in writing to reflect that?

9 A. No.

10 Q. Just one other question. Who were the owners of
11 the Optus Company?

12 A. Optus Information Systems is owned by Joseph
13 Licht, if I recall, and I think maybe my son is part of
14 Optus Information Systems.

15 Q. Your son has an interest in Optus?

16 A. Yes. It's a computer company.

17 THE COURT: When you say it is a computer
18 company, what do they do? Do they handle the bookkeeping?

19 THE WITNESS: No, they just handled my quarterly
20 interest lenders' statements. That is all they did.

21 THE COURT: So they basically processed the
22 information and sent out the bills?

23 THE WITNESS: Exactly. They programmed and
24 processed all the quarterly statements.

25 THE COURT: All right.

1 Q. So, in other words, at the time that you were
2 suggesting by your testimony that Price Waterhouse relied on
3 Optus generated records, your son at that time had an equity
4 interest in Optus?

5 A. He always had, yes.

6 MR. LEVINE: Thank you.

7 THE COURT: Anything further? Mr. Richards do
8 you have any questions?

9 MR. RICHARDS: No, your Honor.

10 THE COURT: Go ahead.

11 REDIRECT EXAMINATION

12 BY MR. SORKIN:

13 Q. You now have the opportunity to add to that
14 letter, Mr. Avellino, that was read to you in part. What
15 did you want to add?

16 A. Well, I wanted to add that if you hear the
17 testimony today or the questions today, it looks like it
18 refers to 1984 through 1988. When I made a blanket
19 statement that I would put nothing in financial form --
20 because they never, by the way, and the record must show
21 that, financial statements never ever existed -- and to
22 facilitate an audit to create a financial statement that
23 never existed, is like just doing something that is
24 whitewashing something they could audit from the tax
25 statement.

1 THE COURT: But the question is, what did you say
2 in the letter about it?

3 THE WITNESS: The letter refers to all of the
4 years, including 1989, 1990, 1991. I don't want the
5 inference --

6 MR. SORKIN: I don't have the letter with me. I
7 would have to find it.

8 MR. BRESLOW: It is attached as a copy of one of
9 the exhibits to the affidavits in the record.

10 THE COURT: I will look at it.

11 THE WITNESS: The letter refers to the fact that
12 I refused to prepare financial statements. And I say why I
13 do. Basically, that is what it is. It is for all the
14 years. It wasn't that I was going to prepare phantom
15 statements for '84 on when everybody knew they didn't exist.

16 THE COURT: I don't think that was the point of
17 the question. I think the point of the question was, the
18 justification you gave for not doing it was not the one you
19 have testified about today but the fact that you were
20 concerned lest it be used against you?

21 THE WITNESS: Oh, yes, your Honor.

22 THE COURT: That is the point.

23 THE WITNESS: Yes.

24 Q. Were you being asked to create financials out of
25 memory from records that did not exist?

1 A. Evidently when everybody knew they didn't exist.

2 Q. You were asked by Mr. Levine about an Aaron
3 Levey. At paragraph 26 of McDermott, Will & Emery's
4 affidavit, did there come a time when they came to you or
5 are you aware that they came to Mr. Glantz and Mr. Mendelow,
6 said they were going to subpoena Mr. Levey's records from
7 his estate?

8 A. I heard mention of it, yes.

9 MR. SORKIN: Your Honor, I could go into this now
10 or wait for Mr. Mendelow?

11 THE COURT: You might as well wait for Mr.
12 Mendelow. In view of this witness's testimony that all of
13 his arrangements with Mr. Levey were oral, I doubt whether
14 that would make any difference. In the other case there is
15 a suggestion that you should not have subpoenaed because we
16 offered to produce them. This witness's testimony would
17 tend to indicate that was in effect what we call a
18 grandstand gesture because there would probably be no
19 records to produce and Mr. Glantz probably knew it, number
20 one. Number two, an oral request for records obviously,
21 from the trustee's point of view or anyone else's point of
22 view who is charged with the duty of conducting an
23 investigation in a prudent fashion, they would prefer to put
24 the power of the Court behind the request rather than just
25 take your word that you are going to produce it.

1 MR. SORKIN: That may be so, your Honor, but the
2 amount of money that was spent with respect to Levey --

3 THE COURT: That is a different question, how
4 much time it should have taken them.

5 MR. SORKIN: That is the only issue I was going
6 to.

7 THE COURT: That is an issue in the other case
8 and that they will have to explain to me. From what I know
9 of the law, it is a simple process. I don't think it
10 requires a lot of consultation.

11 MR. SORKIN: I am not contesting the use of the
12 subpoena. I am contesting the manner in which it was done
13 and how much money was charged for something that in
14 effect --

15 THE COURT: But Price Waterhouse had no part of
16 that. The only argument I have heard you make on direct
17 examination is that Price Waterhouse should not have spent
18 \$15,000 after the depositions in reconciling something that
19 they already knew they could not verify one way or the
20 other. I got that point. I will ask them to explain it.

21 MR. SORKIN: Then I can wait, your Honor. That
22 was the only reason.

23 THE COURT: So far as whether the law firm spent
24 more money, that is not your concern.

25 MR. SORKIN: I understand.

1 THE COURT: You are not challenging Mr. Richards'
2 fees.

3 MR. SORKIN: No, this is McDermott, Will & Emery,
4 your Honor.

5 THE COURT: But you don't represent that client,
6 I assume.

7 MR. SORKIN: We do.

8 THE COURT: Do you?

9 MR. SORKIN: We represent Telfran.

10 THE COURT: Then, read it in that context. Mr.
11 Richards' fees are uncontested and therefore will go forward
12 as proposed.

13 MR. SORKIN: But Mr. Richards had nothing to do
14 with Telfran. It was McDermott, Will & Emery.

15 THE COURT: But that has nothing to do with this
16 witness.

17 MR. SORKIN: I only raised it, your Honor,
18 because the Levey subpoena was raised.

19 THE COURT: He only asked about the records.

20 MR. SORKIN: Very well, your Honor, I will wait.

21 THE COURT: And that relates to Price Waterhouse,
22 not to McDermott.

23 BY MR. SORKIN:

24 Q. I believe you were asked by Judge Sprizzo, Mr.
25 Avellino, what Optus did. I think he may have said, with

1 all due respect, incorrectly that they send out bills.

2 THE COURT: I think he corrected me on that. He
3 said they were not bills.

4 THE WITNESS: Statements.

5 THE COURT: They were statements.

6 Q. Were they also checks?

7 A. Checks and statements. That is one and the same.

8 Q. The instant payments.

9 A. Yes.

10 MR. SORKIN: No further questions.

11 THE COURT: Anything further? You may step down.

12 (Witness excused)

13 THE COURT: You may call your next witness.

14 MR. SORKIN: Mr. Joseph Licht, your Honor.

15 THE COURT: I take it Mr. -- is it Bienes?

16 MR. SORKIN: Bienes.

17 THE COURT: -- Mr. Bienes' testimony would be
18 cumulative of what we have already heard?

19 MR. SORKIN: Yes.

20 THE COURT: You may not choose to call him if you
21 don't want to. Go ahead.

22

23 J O S E P H L I C H T, called as a witness by the
24 defendants, having been duly sworn, testified as
25 follows:

1 MR. SORKIN: May I proceed, your Honor?

2 THE COURT: Yes.

3 MR. SORKIN: One thing. There is about two
4 minutes' testimony that I think I am going to need from Mr.
5 Bienes.

6 THE COURT: All right.

7 DIRECT EXAMINATION

8 BY MR. SORKIN:

9 Q. Mr. Licht how are you employed, sir?

10 A. I am president of Optus Financial Services.

11 Q. Would you just tell us quickly what Optus did
12 with respect to Avellino & Bienes?

13 A. With respect to Avellino & Bienes, we operated as
14 what is commonly referred to as a data processing firm.

15 Q. Does Optus have other clients or did it have
16 other clients or does it have other clients today other than
17 Avellino & Bienes?

18 A. We have. We still have other clients.

19 Q. How many clients would you estimate you have?

20 A. Roughly twenty.

21 Q. You have heard testimony that Optus prepared
22 statements and checks, is that correct? You have heard
23 that?

24 A. Yes, I did hear that.

25 Q. Did you do anything else for Avellino & Bienes

1 besides that?

2 A. Other than the quarterly processing, which was
3 the checks and statements and check registers, or resultant
4 of that, we didn't do any other work for Avellino & Bienes.

5 Q. You were visited at one point in time in
6 connection with this case by representatives of Price
7 Waterhouse?

8 A. Yes. I recall Mr. Joel Whitman was there and Mr.
9 Curt Headke visited my office at Somerset.

10 Q. What did Price Waterhouse do? Tell us everything
11 they did with respect to Optus that you can recall.

12 A. Well, at my office, basically what they wanted to
13 know was how information flowed from Avellino & Bienes to
14 Optus, and vice versa, how the information flowed, deposits,
15 things of that nature.

16 Q. How long did you spend with him on this first
17 occasion?

18 A. Well, I would say it is a first and only occasion
19 at Optus, and we spent -- it was under two hours.

20 Q. Were there any other occasions, Mr. Licht, where
21 representatives of Price Waterhouse visited the premises of
22 Optus?

23 A. Yes. They had someone come by to pick up checks
24 after we had finished printing them.

25 Q. Where is Optus located?

1 A. In Somerset, New Jersey. That's central.

2 Q. To the best of your knowledge, Mr. Licht, did
3 Price Waterhouse have anything to do with the preparation of
4 the checks?

5 A. They weren't there when we printed them or when
6 we calculated the interest, so I would have to answer no to
7 that.

8 Q. Did they supervise the printing of the checks or
9 the calculation, or did they render any supervisory support
10 for Optus?

11 A. No. Basically Optus did what we always do. We
12 calculated the interest, printed the checks, and a
13 representative of Price Waterhouse came back to pick them up
14 after they were completed.

15 Q. How long did that take?

16 A. To have someone pick them up?

17 Q. Yes.

18 A. Five minutes, I suppose. The box was there.

19 Q. In the ordinary course of your business, how long
20 did it take to compute the interest, prepare the checks, and
21 send them out to the various lenders of Avellino & Bienes?
22 Can you give us an estimate in the ordinary course, before
23 this case was brought to court?

24 A. In the ordinary course, with that volume of
25 checks, we are talking about three days or 24 to 36 hours.

1 We work odd hours if we have to, because we have to make a
2 deadline for the post office.

3 Q. Is that around the clock?

4 A. When I say three days, I don't mean three days
5 around the clock.

6 Q. That is what I am asking you. Can you break down
7 how much time is actually spent in calculating the interest,
8 preparing the checks, preparing the statement, and then
9 sending it out?

10 A. I would say 30 hours.

11 Q. Are you aware of how much time Price Waterhouse
12 claimed it spent in visits with you?

13 A. In their original affidavit they claim that they
14 were at my office for 20 hours.

15 Q. Is that the two hours that you say --

16 A. I have to assume. I don't know what else they
17 could be referring to.

18 Q. And you say they were at your office on another
19 occasion for about five minutes to pick up the checks?

20 A. Yes.

21 Q. Do you recall any other time that they spent at
22 Optus or any other work that they performed?

23 A. Not at Optus, no.

24 MR. SORKIN: No further questions, your Honor.

25 THE COURT: You may cross-examine.

1 CROSS-EXAMINATION

2 BY MR. BRESLOW:

3 Q. Mr. Licht, was Avellino & Bienes the biggest
4 client of Optus?

5 A. Yes.

6 Q. By the way, there was testimony about Mr.
7 Avellino's son being a principal at Optus. Is he your boss,
8 basically?

9 A. I would not -- I would call him more of a
10 partner. Even though we are a corporation, I would not
11 refer to him as my boss.

12 THE COURT: How much stock does he hold
13 percentagewise?

14 THE WITNESS: It is more than me, your Honor.

15 THE COURT: How much more?

16 THE WITNESS: I don't know in exact amount.

17 THE COURT: How much do you hold?

18 THE WITNESS: Roughly 10 percent.

19 THE COURT: Does he hold less?

20 THE WITNESS: No. There are other partners.

21 THE COURT: Who?

22 THE WITNESS: Robert Chiclo is also another
23 partner. I should say principal in the corporation.

24 THE COURT: Who is the majority shareholder?

25 THE WITNESS: Joseph Avellino, I believe, is

1 the --

2 THE COURT: So at meetings, if and when the
3 corporation has its annual meetings, I take it the vote is
4 cast basically along the lines of what Mr. Avellino wants?

5 THE WITNESS: Basically, if you wanted to say
6 that.

7 THE COURT: That is what he is trying to
8 establish. It goes to interest and bias.

9 THE WITNESS: Thank you, your Honor.

10 Q. You mentioned earlier on your direct that you had
11 a meeting with Mr. Whitman of Price Waterhouse and other
12 persons at Price Waterhouse?

13 A. Kerry Haedke.

14 Q. And that lasted for a couple of hours, do you
15 recall?

16 A. It was under two hours.

17 Q. Did you have any other telephone conversations
18 with Price Waterhouse over the next week or ten days?

19 A. Certainly a lot of telephone conversations.

20 Q. Anybody ask you questions or questions about
21 Optus, and so on and so forth?

22 A. No, the questions on the telephone at that point
23 were how they were to try to set up their systems to mimic
24 what we did at Optus.

25 Q. Can you estimate, sir, how much time you spent in

1 phone calls, people at Price Waterhouse, over that week or
2 ten days?

3 A. I would say at least four hours on the phone.

4 Q. You also mentioned, sir, on your direct the
5 printing of the checks. Did you have any contact at all
6 with people from Price Waterhouse in connection with
7 printing the checks?

8 A. Well, I had to get a go-ahead from them on when
9 to start. They were in control at that point.

10 Q. Than did you get calls periodically from people
11 at Price Waterhouse asking you how it was going?

12 A. I might have gotten one late call asking when the
13 checks would be ready so that they could pick them up.

14 Q. Don't you recall getting calls from Mr. Cook and
15 the Price Waterhouse people about the progress of the check
16 printing?

17 A. I remember getting calls from them on the
18 progress of the statements and how they were to be formatted
19 well before the actual printing, not during the actual
20 process.

21 Q. You don't recall getting any calls during the
22 printing?

23 A. No.

24 Q. You weren't present, Mr. Licht, were you, at any
25 meeting of the trustee and Price Waterhouse?

1 A. I have been at some meetings. I don't know what
2 you are referring to.

3 Q. You weren't present at any meetings where the
4 trustee discussed with Price Waterhouse what work the firm
5 was supposed to be doing on its work with A & B?

6 A. No.

7 MR. BRESLOW: No further questions, your Honor.

8 THE COURT: Anything further?

9 MR. SORKIN: No further questions, your Honor.

10 THE COURT: You may step down.

11 (Witness excused)

12 THE COURT: Call your next witness.

13 MR. SORKIN: I call Mr. Bienes.

14

15 M I C H A E L B I E N E S, called as a witness in his own
16 behalf, having been duly sworn, testified as follows:

17 MR. SORKIN: May I proceed, your Honor?

18 THE COURT: Go ahead.

19 DIRECT EXAMINATION

20 BY MR. SORKIN:

21 Q. Mr. Bienes, how old are you, sir?

22 A. 56.

23 Q. Mr. Bienes, could you tell us something of your
24 educational and professional background?

25 A. Yes. I have a B.S. degree from NYU, an M.B.A.

1 from CCNY. I am a CPA in New York State since 1969. I was
2 an auditor and agent and group chief with the IRS from 1960
3 to 1968. I was an instructor in accounting at CCNY,
4 graduate and undergraduate, from 1970 to 1977. From 1977 to
5 1980, I was an associate professor at the Graduate School at
6 Pace University.

7 Q. What course did you teach?

8 A. Accounting and auditing.

9 Q. Mr. Bienes, have you had experience in the tax
10 side of auditing?

11 A. Yes, sir.

12 Q. Did you do that while you were a CPA, while you
13 practiced as a CPA?

14 A. Yes, sir.

15 Q. Mr. Bienes, could you tell us, sir, you heard
16 testimony that tax returns were given to Price Waterhouse.

17 A. Yes. I supplied them, in fact.

18 Q. Were those the tax returns of Avellino & Bienes,
19 the partnership?

20 A. Yes, sir.

21 Q. Did you supply personal tax returns?

22 A. Yes, sir.

23 Q. Did you supply the personal tax returns of Mr.
24 Avellino as well?

25 A. No, sir.

1 Q. Do you know if Mr. Avellino supplied his personal
2 tax returns?

3 A. I think he did.

4 Q. Mr. Bienes, in your experience, what information
5 can one derive from the partnership tax return that can be
6 utilized as a financial statement?

7 A. The partnership tax return, federal tax return,
8 Form 1065, is in all aspects a complete financial statement.
9 It contains a profit and loss showing various income and
10 expense items. It contains a balance sheet well classified
11 of the current and previous year. It contains a
12 reconciliation of partners' capital accounts. It is a more
13 or less complete financial statement.

14 Q. When did you turn over the A & B partnership tax
15 return 1065 to representatives of Price Waterhouse?

16 A. Mr. Sorkin, I really am afraid to answer that
17 question. I remember making copies and being so happy that
18 I found them all, even going back to 1983. I am not sure if
19 it was December or January.

20 Q. Of 1992, 1993?

21 A. Yes, sir.

22 Q. Did you in fact turn over tax returns to
23 representatives of Price Waterhouse 1065 going back to 1983?

24 A. Yes, sir.

25 Q. How far back did you turn in your tax return,

1 your personal return?

2 A. I think the same amount of time.

3 Q. Is there anything on a financial statement
4 reflecting profit and loss, capital account reconciliation,
5 that you could not get from a tax return, the information?

6 A. As referring to Avellino & Bienes, no. It would
7 be exactly the same.

8 MR. SORKIN: I have no further questions.

9 THE COURT: I have a couple.

10 Did you prepare those returns?

11 THE WITNESS: No, your Honor.

12 THE COURT: They were prepared outside?

13 THE WITNESS: No, your Honor. My partner
14 prepared them.

15 THE COURT: Who was that?

16 THE WITNESS: Frank Avellino.

17 THE COURT: So you are in no position to tell us
18 upon what he relied in preparing those statements?

19 THE WITNESS: Yes, your Honor, I am. I checked
20 the tax returns after he prepared them.

21 THE COURT: Against what?

22 THE WITNESS: Books, records. We always kept
23 books and records, worksheets. We kept a cash receipts
24 book, a cash disbursements book, and a general ledger, your
25 Honor.

1 THE COURT: That is what I am trying to find out,
2 because we have heard, you have heard, Mr. Avellino say
3 there weren't adequate records upon which to prepare a
4 financial statement. I wonder, if there were adequate
5 records to prepare a tax return, why there were not adequate
6 records to prepare a financial statement if you say they
7 contain the same information.

8 THE WITNESS: That is why, they are one and the
9 same. But not before 1988. We didn't have the books and
10 records.

11 THE COURT: You had discarded the books and
12 records?

13 THE WITNESS: Yes, sir.

14 THE COURT: So there was no way to test the
15 accuracy of returns prior to 1988 against the books and
16 records of the company?

17 THE WITNESS: That is right, your Honor.

18 THE COURT: So the job was impossible?

19 THE WITNESS: Your Honor, that is what I even
20 said one evening to Geoffrey Cook: How are you going to
21 audit and satisfy yourself prior to 1988 when we have
22 already told you we have no books and records?

23 THE COURT: When did you tell him this?

24 THE WITNESS: I was working with him one night in
25 December.

1 THE COURT: You heard Mr. Avellino's testimony
2 that he suggested that they do the audit from the tax
3 returns? Do you remember that testimony? I just heard it.

4 THE WITNESS: I just heard it too.

5 THE COURT: So Mr. Avellino was suggesting to
6 Price Waterhouse that they do something which he knew was
7 not possible to do with respect to years prior to 1988?

8 THE WITNESS: You couldn't audit, no.

9 THE COURT: You couldn't audit.

10 THE WITNESS: No. You could not audit.

11 THE COURT: All right.

12 BY MR. SORKIN:

13 Q. Mr. Bienes, could you use the tax return as a
14 financial statement?

15 A. Yes.

16 THE COURT: What good is that if you couldn't
17 test it? The whole purpose of an audit is to test the
18 accuracy of it. To suggest that you could use the tax
19 returns as a financial statement when the means for testing
20 it are not available would be an empty gesture.

21 Q. Did you turn over everything that you possibly
22 could that was requested of you?

23 A. Everything.

24 MR. SORKIN: No further questions.

25 THE COURT: We are back to the same question, Mr.

1 Sorkin: If you thought an audit was impossible, you should
2 have had said, "Give us no opinion."

3 MR. SORKIN: Your Honor, if I may add.

4 THE COURT: That is the match point here, isn't
5 it.

6 MR. SORKIN: With all due respect, why we didn't
7 withdraw our consent is --

8 THE COURT: It is not a question of withdrawing
9 your consent. Just say, "We will take no opinion." You
10 didn't want to do that.

11 MR. SORKIN: Your Honor, it was our --

12 MR. BRESLOW: Your Honor, I have a question. I
13 want to check with my client.

14 THE COURT: I think you should know where I think
15 the match point is.

16 MR. BRESLOW: May I have a moment, Judge.

17 I have no questions, Judge.

18 THE COURT: You may step down.

19 (Witness excused)

20 THE COURT: I take it that completes your
21 witnesses on this phase of the case?

22 MR. SORKIN: That is correct.

23 THE COURT: Does Price Waterhouse have any
24 witnesses they want to call?

25 MR. BRESLOW: Yes, Judge. Mr. Joel Whitman.

1 THE COURT: From your point of view, I am only
2 interested in two aspects of the case: (1) Why you
3 continued to audit after the depositions indicated that a
4 further audit would be useless; and (2) the issue of the
5 supervision of the checks, which I think creates substantial
6 credibility questions as to that one item, and therefore
7 theoretically may cast some light on the prior audit.
8

9 J O E L W H I T M A N, called as a witness by Price
10 Waterhouse, having been duly sworn, testified as
11 follows:

12 DIRECT EXAMINATION

13 BY MR. BRESLOW:

14 Q. Mr. Whitman, could you please tell the Court how
15 old you are?

16 A. I am 56 years old.

17 Q. Could you please give us a brief description of
18 your educational background?

19 A. Yes. I am a graduate of the City College of New
20 York. I am a CPA of the State of New York. I have been an
21 auditor at Price Waterhouse where I have been for 31 years,
22 and I have been a partner for eighteen years.

23 Q. Is there a certain field, Mr. Whitman, that you
24 specialize in accounting and auditing?

25 A. I would say I am an auditor and presently I do

1 specialize in the investment company industry.

2 Q. For how long have you specialized in the
3 investment company industry, sir?

4 A. Probably close to twenty years.

5 Q. Mr. Whitman, did there come a time when you heard
6 that it was being contemplated that Price Waterhouse might
7 be hired to work on an engagement with the trustee of
8 Avellino & Bienes?

9 A. Yes.

10 Q. When did you first hear of that, sir?

11 A. I had received a phone call from an associate at
12 the Squadron, Ellenoff firm on a Saturday afternoon at home
13 asking if Price Waterhouse would be interested in being
14 involved in a particular special engagement.

15 Q. Did that person ask you what you thought it might
16 cost to do an audit of A & B's financial statements?

17 A. No. In fact, as I recall the conversation, there
18 was mention that money would be no object, because I had
19 stated, not having seen books, records, financial
20 statements, or anything of the sort, it would be rather
21 ludicrous to try and give any type of fee estimate. And I
22 believe it was represented that there would be ample escrow
23 deposit, since it related to a court case.

24 Q. Are you aware, Mr. Whitman, that the consent
25 order of this case lists a figure, I believe it is a quarter

1 of a million dollars, that was held in escrow to pay the
2 trustee's fees and the Price Waterhouse fees?

3 A. Yes, I am.

4 Q. Is it correct that Price Waterhouse didn't have
5 any opinion as to what that number ought to be?

6 A. That is correct.

7 Q. Mr. Whitman, when you saw the order and saw that
8 it said an audit of financial statements, what did you take
9 that to mean, sir?

10 A. Just as I would any other audit of financial
11 statements, a complete audit in accordance with generally
12 accepted auditing standards.

13 Q. And that is what Price Waterhouse was to do from
14 the order, is that right?

15 A. It was very clear to me that that was the charge.

16 Q. Do you recall attending a meeting on November 17
17 or 18 with representatives of the trustee and the SEC and
18 Avellino & Bienes?

19 A. Yes, I do. In fact, that was the morning
20 immediately after I received a phone call advising us that
21 we had been accepted and appointed to be the auditor in this
22 case. As I recall, we met at the offices of the Securities
23 and Exchange Commission, and the trustee was present, and I
24 believe counsel for the defendants were present, a number of
25 SEC staff were present, and I, with my colleagues, Mr.

1 Werblow and Mr. Cook, was also present.

2 Q. Do you recall, sir, whether anyone made a
3 statement at that meeting to the effect that when the order
4 said audit the financial statements, it really meant audit
5 and not only the matter of the notchholders?

6 A. There was no such comment at all. In fact, a
7 part of the discussion did go into the necessity to do a
8 careful and a thorough audit of the financial statements.

9 Q. Did anyone at Avellino & Bienes representing
10 Avellino & Bienes complain about that, that was mentioned at
11 the meeting?

12 A. No. There was no such complaint nor any
13 discussion whatsoever.

14 Q. Did there come a time Mr. Whitman when Price
15 Waterhouse learned that A & B didn't have financial
16 statements?

17 A. Yes, there was. Following the meeting at the
18 SEC, we adjourned to the offices of Avellino & Bienes, and
19 Mr. Avellino sat with us and attempted to explain what his
20 business was all about. I believe at that time he did
21 mention that he kept very -- not precise records, I don't
22 think those are his exact words, but that he still kept
23 manual, old-fashioned ledgers, and he did at that time
24 mention that he wasn't sure if he had all his books and
25 records, that he generally kept whatever was necessary for

1 income tax purposes, which would have been three years.

2 Q. Did there come a time when Price Waterhouse asked
3 Mr. Avellino or Avellino & Bienes to create financial
4 statements?

5 A. Yes. In fact, I remember that very vividly
6 because, contrary to some of the things that have been
7 stated by the defendants, we indeed tried to keep our time
8 charges at a minimum and not to run up bills. I think in my
9 professional opinion that is how I have always served
10 clients. So in that spirit I had suggested, and I discussed
11 it with the trustee, that in situations like this, where
12 there is less than adequate and complete records, that
13 perhaps if Mr. Avellino, who is a CPA, would prepare the
14 financial statements and accumulate the information we would
15 need, that would eliminate the need for Price Waterhouse to
16 do what we would call a bookkeeping exercise at our billing
17 rates. So it was discussed, I did discuss it with the
18 trustee, and my understanding was, it was returned to us
19 that it was a good idea. And Mr. Avellino did indeed agree
20 to assist in that way because he would be saving his own
21 money.

22 Q. When do you recall getting that response back
23 from the trustee, sir?

24 A. I cannot fix a very specific date on that.
25 Perhaps my colleague, Geoff Cook, might know.

1 Q. Can you fix it generally as to whether it was in
2 December or January or some other time?

3 A. Well, I would say it was clearly in December,
4 because there is a sheaf of correspondence that goes back
5 and forth between Price Waterhouse and Avellino & Bienes.
6 In fact, as I recall, through the middle of January, and up
7 until that date, there was never one mention in any of the
8 communications from Mr. Avellino that we should not be doing
9 any audit or that he wasn't prepared to prepare the
10 financials until such time, again, as the middle of January
11 rolled around. By that date, of course, we were coming to
12 what would be the concluding part of our work, since we had
13 to be done by the end of the month.

14 THE COURT: But I take it you knew very early in
15 the game there were no records available prior to 1988
16 because they said that they didn't keep them longer than
17 they were required to for tax purposes?

18 THE WITNESS: Well, your Honor, that is partly
19 correct. We were aware, though, that there were records. I
20 should add I spent a dozen years in our small-business
21 department, and it's amazing how one can complete an audit,
22 given enough hours and energy. We did attempt to get bank
23 statements from the banks and brokerage statements from the
24 broker. I at no point in time would say that because you
25 are missing a general ledger, that it might be impossible to

1 do an audit.

2 THE COURT: Maybe the basic question I am asking
3 is why you were not able to conclude relatively early in the
4 game that the likelihood of being able to give an opinion
5 was not very promising as to the years certainly prior to
6 1988.

7 THE WITNESS: Well, because I truly believed that
8 we would have sufficient opportunity, once our requests were
9 complied with in terms of providing checks. There are more
10 than one type of audit and audit opinion that can be given.
11 In addition to the GAAP audit that is most common with
12 public companies, with small companies like these, very
13 often there are cash basis audits of financials and
14 income-tax basis. My charge, as I saw it, was to audit the
15 financial statements and not to give up until I determined
16 that it was impossible to do.

17 THE COURT: When was that determination made?

18 THE WITNESS: Well, I would say probably we were
19 into January and still very optimistic about receiving the
20 documents that we had requested in our letters.

21 THE COURT: No one ever told you that you should
22 stop because they didn't want an opinion of any kind, either
23 a GAAP opinion or any other kind of opinion?

24 THE WITNESS: Your Honor, I never heard anything
25 like that, and I am sure my colleague, Mr. Cook, had he been

1 advised of that, would have promptly advised me.

2 THE COURT: All right. I guess it is a GAAS
3 opinion, not a GAAP opinion?

4 THE WITNESS: Well, GAAS, the generally accepted
5 auditing standard, is the procedures, and the GAAP is the
6 accounting principles.

7 MR. BRESLOW: Judge, I can move on to this Optus
8 issue.

9 THE COURT: Go ahead

10 BY MR. BRESLOW:

11 Q. Mr. Werblow -- I am sorry -- Mr. Whitman, there
12 came a time when you met with people from Optus?

13 A. Yes, there was.

14 Q. Do you recall the first time that that happened?

15 A. I do. It was rather early on when we had to try
16 and establish the procedures that would be carried out in
17 this very, very limited time frame with which to disburse in
18 excess of \$300 million. I and a computer specialist
19 colleague of mine made arrangements to go out to Somerset,
20 New Jersey. Our office is in midtown Manhattan. The two of
21 us did take a car and go out there. As I recall, it took
22 pretty close to an hour and a half for us to get to the
23 place. As Mr. Licht testified, we probably didn't spend
24 more than two hours there. That would be my estimation of
25 how long we were there. And, of course --

1 THE COURT: Do your bills reflect that you spent
2 more than two hours there?

3 THE WITNESS: Your Honor --.

4 THE COURT: I haven't checked them in that
5 detail, but do you claim more than two hours for that
6 meeting itself?

7 THE WITNESS: No, your Honor. In fact, our bill
8 doesn't go into that specific, but in our affidavit we made
9 statement which unfortunately I believe the defendants as
10 well as Mr. Licht have read very much out of context. As I
11 recall, our statement said that, in making a visit with Mr.
12 Licht, and in follow-up with conversations with Mr. Licht,
13 and performing such other work related to the computer
14 technology, yes, that we spent 20 hours on. We never said,
15 and if the document could be produced you would see it, we
16 never said that we spent 20 hours sitting with Mr. Licht on
17 the day that we visited him.

18 THE COURT: All right.

19 MR. BRESLOW: Just for the record, Judge, Mr.
20 Whitman is referring to paragraph 12 of the Werblow
21 affidavit.

22 THE COURT: I read that one yesterday. Go ahead.
23 Paragraph 12?

24 MR. BRESLOW: Paragraph 12 on page 8, the very
25 bottom of the page.

1 MR. SORKIN: May I read it to the Court?

2 THE COURT: I have it.

3 MR. SORKIN: I am sorry, I thought you didn't
4 have it.

5 Q. Mr. Whitman, are you generally familiar with the
6 work Price Waterhouse did in the printing of checks and
7 sending notes to the noteholders?

8 A. Yes.

9 Q. Are you aware of what work was done to supervise
10 the printing of checks?

11 A. Yes. Mr. A. J. Kothari, who is, again, another
12 one of our computer specialist types, participated with our
13 team, and I am aware, since Mr. Kothari lived in Edison, New
14 Jersey, we arranged for him to go out to Somerset, since it
15 was rather close. As far as I recollect, the evening, the
16 Saturday evening that the checks were being printed at my
17 instruction, Mr. Kothari was to have gone out to Optus to
18 ascertain that the proper file would be run so that the
19 checks would be printed, since it happened over the midnight
20 and early mornings. I then understand that Mr. Kothari
21 returned to his home and through the evening had made at
22 least one or perhaps more phone calls to Mr. Licht to learn
23 when the printing job was near completion, because we wanted
24 to be there to obtain the checks and immediately bring them
25 into New York on Sunday morning. So that would be, you

1 know, the procedure that we were following regarding that.

2 THE COURT: How much time is claimed for that?

3 Is that separate or is that part of the 20 hours?

4 THE WITNESS: I can't answer that, your Honor.

5 MR. BRESLOW: I don't believe we broke it down
6 quite that far in the affidavit. There is a section in the
7 affidavit that talks about the work done generally in terms
8 of getting the checks and supervising signing and stuffing
9 envelopes and getting them all out, and so on and so forth.

10 THE COURT: It doesn't appear to be a major
11 point.

12 MR. BRESLOW: I don't think so.

13 THE COURT: Any cross-examination?

14 MR. SORKIN: Yes, your Honor.

15 CROSS-EXAMINATION

16 BY MR. SORKIN:

17 Q. Mr. Whitman, I am going to show you copy of the
18 consent order.

19 THE COURT: One more thing I want to ask you
20 about before you finish. There was some reference to a
21 \$15,000 charge for auditing Telfran's claim against A & B
22 after the deposition took place. What was that about?

23 THE WITNESS: Your Honor, I don't know where
24 anybody got that number. It resembles the same 20 hours
25 where we are alleged to have sat in Mr. Licht's office for

1 20 hours, and our affidavit never said that. Similarly, on
2 the Telfran work, it is my recollection there is nowhere in
3 any of the bills or affidavit that we rendered that says we
4 incurred \$14,000 to audit the Telfran situation, even before
5 or after the affidavit. So I can't really address that
6 number.

7 THE COURT: I take it, as an accounting
8 proposition or as an auditing proposition, if you have a
9 claim and somebody tells you that it is an oral agreement
10 that supports the claim or disproves the claim, you either
11 believe the testimony of management or you don't, and when
12 it is given under oath, you believe it or you don't, but
13 there is nothing more an auditor can do at that point, there
14 are no other written records to be reviewed?

15 THE WITNESS: Well, again, written documentation
16 is only one level and degree of audit work and audit
17 procedures, your Honor.

18 THE COURT: But you either accept what you are
19 told orally or you don't accept what you are told orally;
20 correct?

21 THE WITNESS: Well, I think we then make
22 inquiries of people, etc.

23 THE COURT: But in this particular case Mr. Levey
24 is dead. The only person who could support the claim or not
25 support the claim is Mr. Avellino, and he says he doesn't

1 owe it. There is no contrary evidence. Whether you believe
2 it or not, as an auditor you can't go any further than that?

3 THE WITNESS: Actually, in fact, your Honor, I am
4 thinking now, I was probably in Mr. Avellino's, Avellino &
5 Bienes's office on the afternoon that Mr. Glantz made a
6 phone call. As I recall, I was rather irate and I did not
7 speak with him, but I believe he spoke with Ms. Imes, the
8 counsel for the trustee.

9 THE COURT: Who is that? Mr. Avellino?

10 THE WITNESS: Mr. Glantz was irate. He was
11 calling from Florida and I guess upset about this \$317,000.
12 And I know I don't like to use the word but it sort of shook
13 up the office a little bit, because there was some shouting
14 on the phone, so I know that this claim was certainly
15 something that was ferociously contended at the initial.

16 THE COURT: But an auditor has to look at
17 documents and if the documents don't confirm the claim, then
18 you go to the oral testimony, and if the oral testimony
19 doesn't do it, you really are at sea, aren't you?

20 THE WITNESS: Yes. But keep in mind, your Honor,
21 we were engaged in multiple roles. We were auditors and we
22 were also assisting the trustee. As I recall it, at all
23 times we acted under the direction and supervision of the
24 trustee. We were not there solely in the role of an
25 auditor.

1 THE COURT: I understand that. But there is very
2 little auditing work that can be done, auditing work as
3 such, once it is obvious that what you have is an oral
4 agreement which is alleged to be sufficient to disprove the
5 claim and no way to verify or contradict that oral
6 agreement, because the other party to it is dead.

7 THE WITNESS: I agree, your Honor. And again, as
8 I said earlier, I don't believe we stated any place how much
9 time we spent on Telfran.

10 THE COURT: Go ahead.

11 BY MR. SORKIN:

12 Q. Mr. Whitman, let me read to you, and I am quoting
13 from the order: "The trustee shall engage and employ Fred
14 Werblow and the accounting firm of Price Waterhouse to (1)
15 conduct an audit of A & B's financial statements from 1984
16 to the present; (2) express an opinion confirming the
17 identity of all noteholders in A & B notes and the amount of
18 principal and accrued interest owed to each such noteholder
19 as of November 16, 1992, and as of the date of distribution
20 of principal and accrued interest in such noteholder."

21 Where did you get in your mind, Mr. Whitman, that
22 you had to render an opinion on the financial statements?
23 The order does not say anything having to do with --

24 THE COURT: That is not for him. That is for me.
25 The question is, what does the word "audit" mean? He has

1 already testified to what the word "audit" means. Why don't
2 you cross-examine him on that? Not what you intended by the
3 order, because he is not a party to that. He has testified
4 that there are various types of audits that --

5 MR. SORKIN: I am going to get to that.

6 THE COURT: Why don't you get to that. Your
7 question is objectionable and I am sustaining it. Ask
8 another.

9 Q. What type of audit did you conduct?

10 A. We conducted --

11 Q. You said there are various types of audits.

12 A. Yes. Our audit was conducted on the basis of our
13 being able to render a report on the basis ultimately of the
14 income-tax basis of accounting.

15 Q. For what purpose?

16 A. For the purpose that was stated in the order: to
17 do an audit of the financial statements.

18 Q. Did you believe, Mr. Whitman -- and I don't mean
19 to defy the Court; I think it is another question -- did you
20 believe you had to render an opinion with respect to the
21 validity of the financial statements?

22 A. I would say that it would be rather difficult for
23 any CPA who holds himself out to be in conformity with
24 professional standards to do an audit and not render an
25 opinion. In fact, if you could show me one, I would be very

1 interested in seeing it. Every examination of an
2 independent auditor, once he associates himself with any
3 type of financial statement, must render an opinion. And, I
4 would add, a disclaimer is a form of opinion.

5 Q. When did you realize for the first time that you
6 could not render an opinion with respect to the financial
7 statements?

8 A. I personally never came to that conclusion. Had
9 his Honor given us more time beyond January 31, we would
10 have been able to complete the audit on the income tax
11 basis. Although we wouldn't have had the cooperation of the
12 defendants, we would have reconstructed the financial
13 statements ourselves, and we could have completed it and
14 rendered an opinion.

15 Q. You just said the cooperation. Where did Mr.
16 Avellino and Mr. Bienes not cooperate with you in producing
17 records?

18 A. Well, I mean, I think --

19 Q. Give me one example.

20 A. I think it is clear that --

21 Q. Mr. Whitman --

22 THE COURT: Don't interrupt his answer.

23 A. -- that originally he had agreed to assist and
24 prepare the financial statements. In fact, the most current
25 period, the 1992 year, which again we probably could have

1 done it beyond the time, had we had more time under the
2 order, I would say the fact that he determined not to
3 produce it, I wouldn't categorize that as cooperating.

4 Q. Mr. Whitman, you said "not produce," and you
5 used, before that, "create." Mr. Whitman, when, if ever,
6 did Mr. Avellino or Mr. Bienes refuse to produce any
7 document for the perusal of Price Waterhouse? Do you know
8 any one instance that they refused to produce a document?

9 A. I am aware that we have a number of letters
10 requesting data, and even right through January 31 there
11 were certain items we had requested which we felt are
12 essential to do an audit that were never turned over to us.

13 Q. And that is because the audit ended January 24 at
14 the direction of the Court, is that correct?

15 A. Yes.

16 Q. You asked originally until the end of February to
17 continue your audit; correct?

18 A. Yes.

19 Q. What did you expect to learn additionally on
20 February 28 or by February 28 that you didn't know on
21 January 16 when we appeared before Judge Sprizzo?

22 A. I don't think it is a question of what I expected
23 to learn. It was a question of, had we been provided the
24 information we requested, we would have been able to
25 complete our work, do the audit, and render an opinion.

1 Q. You asked for leases, did you not, Mr. Whitman?

2 A. Yes, we did.

3 Q. How would a lease for an office that was no
4 longer have added to your audit of the financial statements?

5 A. Since we are hired and paid to verify numbers and
6 not to accept the numbers that would be on a check or in
7 some sort of statement, it is a traditional, customary audit
8 procedure, when one looks at rent expense and it is a
9 significant expense, that one asks to see the lease to see
10 that the payments are made in conformity with the lease
11 terms.

12 Q. Mr. Whitman, is it your testimony that at no
13 point in time, even if you were given an unlimited period of
14 time, could you ever render an opinion as to the validity of
15 the financial statements?

16 Let me put it this way: Was there ever a time in
17 your mind and in all the people who worked at Price
18 Waterhouse that if given an infinite amount of time you
19 could have rendered an opinion?

20 A. I think we could have continued the work on the
21 three current years and rendered an opinion.

22 Q. Is there any record that you did not get that
23 would have assisted you in reaching that opinion? What
24 record that you didn't have in December, or by December 31,
25 any one record you could point to now, that you didn't have

1 by December 31?

2 A. I believe Mr. Werblow's affidavit lists pages of
3 items that were needed.

4 Q. Can you tell us one now from Mr. Werblow's
5 affidavit that you didn't have by December 31 that would
6 have permitted you, at some point in time, to stop what you
7 were doing and finish the audit and render an opinion or a
8 disclaimer?

9 A. I am sorry, could you rephrase your question?

10 Q. Yes. Is there any document in Mr. Werblow's
11 papers or letters that you felt that you needed, so that
12 once you had it you could then say that you could now finish
13 this audit and render either a disclaimer or an opinion, any
14 one document or documents?

15 A. Well, again, as I recall, on those several pages
16 of items, we even went as far as putting an asterisk next to
17 each item that we said was essential, in our opinion, to
18 complete the audit, and not every item had an asterisk.

19 Q. Can you sit here today and tell us --

20 THE COURT: Why should he? He sent you a letter
21 which told you what they were. I am not going to sit here
22 and have you test his memory. You are wasting my time. Get
23 to some relevant examination.

24 Q. Mr. Whitman, at what point in time did you feel
25 you could express an opinion with respect to item 2 of this

1 order that you had in fact identified all the noteholders?

2 A. I would say that at such time as we advised the
3 trustee that --

4 Q. When was that?

5 A. Let me just go back a moment. After the checks
6 were disbursed to the noteholders, we were still in process
7 of trying to ascertain through the confirmation process
8 whether or not we had the list that was provided to us was a
9 valid list, and of course that is the list on which we had
10 done significant amounts of testing, but in only six or
11 seven days we couldn't complete that thoroughly. So that in
12 fact I would have to state that probably sometime later in
13 December when we wound up concluding on the circularization
14 results that we did and the notice had gone out, and I
15 believe perhaps it may have been a date in January when the
16 public had an opportunity to come back and say, I am a
17 noteholder, I wasn't paid, at that time we sort of felt
18 there is nothing more we could do.

19 I should point out that at the very inception it
20 was my opinion that no auditing procedures in the world
21 would guarantee if there were some noteholders some place,
22 perhaps a family member, an insider person, perhaps that
23 might not ever surface.

24 Q. The question was, Mr. Whitman, at what point in
25 time did you feel comfortable that you could express an

1 opinion, pursuant to the order, that all the noteholders had
2 been identified and in fact there were no other additional
3 noteholders and all the noteholders who had been identified
4 had received all their principal and interest? Was there a
5 date? Give me a date, please.

6 A. As I said, I thought I said that it was probably
7 sometime in January.

8 Q. In your experience, Mr. Whitman, have you ever
9 had a confirmation return rate of 98 percent in any audit
10 that you have ever done?

11 A. Well, since I have been doing auditing 31 years,
12 my guess is I probably did.

13 Q. Can you recall any one at this time?

14 A. In cases that we would have perhaps been
15 circularizing 100 percent, as in this case, but I can't
16 recall by name.

17 Q. Mr. Whitman, you believe that you were retained
18 by the trustee, is that correct, and not the defendants in
19 this case?

20 A. Yes, I do.

21 Q. Do you know whether the defendants ever
22 complained to the trustee at any time about how much this
23 was costing? Did the trustee ever tell you that the
24 defendants were complaining that there seemed to be no end
25 to what you were doing?

1 A. Yes. I am aware that the trustee mentioned that
2 there was an objection raised about our bill.

3 Q. When was that objection first made known to you,
4 what point in time?

5 A. Well, as I recall, although it has been referred
6 many times by yourself that on November 30 the bill was
7 rendered, in fact for the record our bill is dated December
8 11 and it probably wasn't received until after December 11
9 by you, so we were already in the middle of December. And
10 it would be my guess that shortly after the middle of
11 December we were probably made aware of this fact. We did
12 have lengthy discussions with the trustee about it. In
13 fact, I recall questioning the trustee as to whether or not
14 we would be paid, and that perhaps should we be considering
15 not continuing to do any work. And again at all times the
16 decision was that we should continue to go forward with the
17 work.

18 Q. Do you know whether the trustee ever communicated
19 your concerns or the questions you are raising with the
20 defendants?

21 A. I had no concerns and I don't know what the
22 trustee communicated.

23 Q. When did you realize for the first time, Mr.
24 Whitman, that your, whatever you were doing, however you
25 phrased your audit, would exceed the \$250,000 which you had

1 learned had been escrowed for this engagement?

2 A. I would have to say that that was probably at
3 around the time that we rendered our first bill, the middle
4 of December.

5 Q. So by the middle of December you knew you would
6 be exceeding \$250,000?

7 A. It was my opinion that we would, yes.

8 Q. And that first bill was \$125,000?

9 A. Yes, it was.

10 Q. Did you realize at the time that you would exceed
11 it by nearly \$300,000 more, put an estimate on it?

12 A. In fact I did.

13 Q. Did you communicate that to anyone?

14 A. Yes, I discussed with the trustee that this work
15 would indeed be much more difficult than anyone might
16 imagine.

17 Q. Talking about a dollar amount. Did you put an
18 estimate on it?

19 A. No, I did not.

20 THE COURT: I take it that was part of your
21 concern that you wouldn't be paid, because obviously you
22 were concerned that the bill would exceed the escrow?

23 THE WITNESS: Yes.

24 THE COURT: To the extent that the bill did not
25 exceed the escrow, you were sure you would be paid.

1 THE WITNESS: I can't answer that, your Honor.

2 THE COURT: Isn't that logical?

3 THE WITNESS: I suppose it is, but I understood
4 that we would have to go to court to get the bill approved.

5 THE COURT: In any event, you obviously were more
6 concerned because you thought your bill was going to exceed
7 \$250,000?

8 THE WITNESS: Yes.

9 Q. When did you learn, Mr. Whitman, that the
10 brokerage firm for which Avellino & Bienes traded had
11 brokerage records reflecting all transactions of the
12 partnership Avellino & Bienes?

13 A. Well, as I recall, I visited the firm of Bernard
14 Madoff and sat in Mr. Madoff's office and discussed with him
15 and made our request --

16 Q. Can you tell me when?

17 A. It probably was within the first two weeks of our
18 engagement.

19 Q. So between November 18 and perhaps December 2,
20 you were aware that Bernard Madoff had broker records
21 reflecting every single transaction engaged in by the
22 partnership of Avellino & Bienes?

23 A. Well, I could actually go one step further. You
24 have referenced this to Mr. Madoff in meeting him. Probably
25 I was aware of that on the first meeting with Frank

1 Avellino, who stated that Mr. Madoff was his broker and kept
2 the records.

3 Q. But when did you get the records and review them?

4 A. I cannot give you an answer. We made requests.
5 They were not forthcoming as rapidly as we wanted them.

6 Much of it was on microfiche or on computer --

7 Q. When did you --

8 THE COURT: Wait.

9 A. You have asked a question.

10 THE COURT: I will let him finish his answer
11 because it will help me. Since I am the fact-finder, that
12 is a decision I make.

13 MR. SORKIN: I apologize, your Honor.

14 THE COURT: Go ahead, finish.

15 A. So, as I was saying, the records, to the best of
16 my recollection, were not forthcoming all at once. Mr.
17 Madoff was forthright. He said he would have to check with
18 his computer people, since they are high technology and much
19 was on tape. As I recall, it did take some time until we
20 got all the statements.

21 Q. Mr. Whitman, when did you get the statements of
22 Madoff? When?

23 THE COURT: When did you get all of the
24 statements?

25 Q. When did you get all the statements of Madoff

1 reflecting all the transactions engaged in by --

2 THE COURT: I want to be sure that that
3 assumption is correct. Do you agree with his assumption
4 that getting the records of Madoff, all of Madoff's records,
5 would reflect all of the transactions of the company?

6 THE WITNESS: Your Honor, you are correct, it
7 wouldn't necessarily reflect all of the transactions of the
8 company. The Madoff statements purportedly would represent
9 the securities transactions of the accounts that were
10 registered under A & B's name with the Madoff firm.

11 THE COURT: Which would then have to be tested
12 against company records?

13 THE WITNESS: Yes.

14 THE COURT: When did you get all of the Madoff
15 records?

16 THE WITNESS: I would have to defer to my
17 colleague who might know that answer. I don't have the
18 specifics.

19 THE COURT: Do you an idea as to approximately
20 when it was?

21 THE WITNESS: Well, I know we got some within a
22 week to ten days, and then others had to be dug out from
23 their archives. My recollection is, it perhaps didn't come
24 to us until maybe early January, everything that Mr. Madoff
25 had to offer. But, again, that is a speculation on my part.

1 THE COURT: All right.

2 Q. Mr. Whitman, wasn't Mr. Madoff on computer and
3 his computer reflected all the transactions and all the
4 lenders and all the --

5 A. He represented that his records were on computer,
6 yes.

7 Q. Did you ask -- he represented that?

8 A. Yes.

9 Q. And your best recollection is early January you
10 got all of his records?

11 A. All the records that we had requested that Mr.
12 Madoff had available. We had requested records going back
13 through 1984, and ultimately Mr. Madoff came back to us,
14 advising us that he himself learned from his computer people
15 that they didn't have the records, the statements going back
16 that far.

17 Q. Did you ask Mr. Avellino and Mr. Bienes whether
18 they had accounts in any other firms?

19 A. I personally did not.

20 Q. Do you know if anyone from Price Waterhouse did,
21 to make sure you had, as the Judge said, all the trading
22 records?

23 A. Well, we were relying on the representation of
24 Mr. Avellino that he had a broker, Mr. Madoff, who kept the
25 securities transactions for Avellino & Bienes.

1 Q. Mr. Whitman, did you ask Mr. Avellino or Bienes
2 whether they had trading records in any other brokerage
3 firms?

4 A. I did not.

5 Q. Do you know if anyone in Price Waterhouse did?

6 A. I cannot answer that.

7 Q. Did the SEC advise you at any time that they had
8 brokerage records in any other firm in order to look there
9 as well?

10 A. I do not recollect that.

11 Q. So, as far as you knew, that was the only place,
12 both from your questioning or your associates' questioning
13 and the SEC's representations, that that was the only place
14 where they had records?

15 A. Yes.

16 Q. Is that a fair statement?

17 A. Securities records, yes.

18 Q. Were you led to believe that they had any other
19 kind of records reflecting transactions accounting for the
20 441 million?

21 A. Well, they had noteholder records.

22 Q. No, reflecting transactions in the stock market
23 for securities that were purchased on behalf of the
24 noteholders, the lenders. That is my question.

25 A. I am sorry, because you switched -- could you

1 please repeat the question?

2 Q. You understood, Mr. Whitman, that Avellino &
3 Bienes had borrowed money, had given it to Mr. Madoff, and
4 Mr. Madoff had executed securities transactions. Is that
5 correct?

6 A. Yes.

7 Q. Did you understand whether they had taken any of
8 that money, Mr. Avellino and Mr. Bienes, and given it to any
9 other broker? Did anyone ever tell you to look elsewhere --
10 the SEC, your associates, the trustee or anyone else?

11 A. I thought I answered that by saying I don't
12 recollect that anybody told us to look elsewhere.

13 Q. Were you in court, Mr. Whitman, on January 16,
14 1993, where you heard the defendants complain about the
15 costs being incurred?

16 A. Yes, I was.

17 Q. Mr. Whitman, are you aware that the Judge
18 indicated that you should end the audit by January 24?

19 A. Yes, I was.

20 Q. Can you account, Mr. Whitman, how between January
21 16 to January 24 the fees from Price Waterhouse increased
22 from approximately \$330,000 to \$414,000, how it went up
23 approximately \$84,000 in about seven days?

24 A. Well, I think we provided --

25 Q. Or nine days, I apologize.

1 A. I thought we provided you with detailed records
2 with the day-by-day number of hours, by the specific person.
3 In fact, I would expect that that should be sufficient, that
4 you would see from that record where and which person spent
5 the time.

6 MR. SORKIN: I have no further questions, your
7 Honor.

8 THE COURT: Anything further?

9 MR. BRESLOW: No, your Honor.

10 THE COURT: You may step down.

11 (Witness excused)

12 THE COURT: Any further witnesses?

13 MR. BRESLOW: No further witnesses.

14 THE COURT: I will break on this matter until
15 3:30.

16 (Luncheon recess)

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AFTERNOON SESSION

4 p.m.

(Hearing resumed)

THE COURT: Any witnesses?

MR. SORKIN: We have three short rebuttal witnesses.

THE COURT: Do you want to cross-examine Mr. Glantz?

MR. SORKIN: We haven't called Mr. Glantz.

MR. BRESLOW: I think Mr. Sorkin is talking about the rebuttal witnesses on the A & B case. I am done with my part of the case.

THE COURT: Do you want to cross-examine Mr. Glantz on his affidavit? It might save time.

MR. BRESLOW: That is fine.

THE COURT: I will take the affidavit in lieu of his direct testimony, to save time, unless there is anything else you want to add to it.

MR. SORKIN: Just three short points I want to add to it.

THE COURT: Then put him on.

MR. SORKIN: Does Mr. Levine want to cross-examine? We are dealing now with McDermott, Will & Emery, your Honor.

THE COURT: Both of them, I guess, now.

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1 MR. LEVINE: That is what I thought, yes. Your
2 Honor, I submitted a reply affidavit, so I am willing to
3 rest on Mr. Glantz's affidavit. I submitted my reply.

4 THE COURT: All right. You don't want to
5 cross-examine him?

6 MR. LEVINE: No.

7 MR. SORKIN: I have two.

8 THE COURT: Put him on for your two questions.

9 MR. SORKIN: It is in his affidavit, your Honor,
10 so I think it is all taken care of, if you are going to
11 accept his affidavit.

12 THE COURT: I will take it as his direct
13 testimony.

14 MR. SORKIN: Fine. Then I have two short
15 rebuttal witnesses and that's it, your Honor.

16 THE COURT: All right. Let's find out: do you
17 want to cross-examine him on his affidavit?

18 MR. BRESLOW: One moment, your Honor and I will
19 let you know.

20 (Pause)

21 MR. BRESLOW: Just a couple of questions, Judge.
22
23
24
25

1 EDWARD R. GLANTZ, called as a witness by the
2 defendants, being first duly sworn, testified as
3 follows:

4 CROSS-EXAMINATION

5 BY MR. BRESLOW:

6 Q. Mr. Glantz, just a very few brief questions
7 about your affidavit, sir.

8 A. Will you speak a little louder, please?

9 Q. Certainly. You said, sir, in your affidavit, and
10 I am referring to paragraphs 12 and 13, you talk about the
11 time that Price Waterhouse spent testing noteholder
12 accounts?

13 A. Pardon me? I didn't hear the question.

14 Q. You spoke in your affidavit, sir, about the time
15 that Price Waterhouse spent testing noteholder accounts at
16 Telfran?

17 A. I assume it is there.

18 Q. A couple of questions for you on that, sir. Were
19 you aware of the assignment that the trustee for Telfran
20 gave Price Waterhouse in connection with noteholder
21 accounts?

22 A. I saw the consent order that I signed.

23 Q. Apart from that, sir, are you aware of any
24 specific assignments the trustee for Telfran gave to Price
25 Waterhouse in connection with noteholder accounts?

1 A. No, I am not.

2 Q. Do you know what Price Waterhouse did to test
3 noteholder accounts at Telfran?

4 A. Not specifically.

5 Q. You say, sir, in paragraph 23 of your affidavit
6 that you maintained a hard copy of all current computer
7 records?

8 A. Yes.

9 Q. How far back did Telfran keep its records, sir?

10 A. Two years.

11 Q. So you did not have records going back to the
12 inception of Telfran?

13 A. We have records since the computer service, which
14 is approximately two years ago.

15 Q. So there was a period of time before you had a
16 computer, you don't have records for now; is that right?

17 A. Right. We had other records, not computerized
18 hard records.

19 MR. BRESLOW: I have no further questions, your
20 Honor.

21 THE COURT: Anything further?

22 MR. SORKIN: Yes, one question.

23 REDIRECT EXAMINATION

24 BY MR. SORKIN:

25 Q. Mr. Glantz, when did Telfran begin?

1 A. Telfran Ltd. commenced in 1989.

2 Q. Did you have records from 1989?

3 A. Yes.

4 Q. Were those records produced to Price Waterhouse?

5 A. We produced the records we had.

6 MR. SORKIN: No further questions.

7 THE COURT: He had records but not all on
8 computer, as I understand.

9 MR. SORKIN: That is correct. That is what I
10 thought he said.

11 THE COURT: All right.

12 MR. SORKIN: I have no further questions, your
13 Honor.

14 THE COURT: Anything further?

15 MR. BRESLOW: No, your Honor.

16 THE COURT: Do you have any questions?

17 MR. LEVINE: I will ask him one question.

18 RE-CROSS-EXAMINATION

19 BY MR. LEVINE:

20 Q. Mr. Glantz, when did Aaron Levey die?

21 A. September 1992.

22 Q. Who were the principals in Telfran besides Mr.
23 Levey?

24 A. Telfran Ltd.?

25 Q. Yes.

1 A. Steve Mendelow, myself, and Joel Levey and
2 Telfran Associates Corp.

3 Q. Prior to the time that Mr. Levey died in
4 September of 1992, who managed the day-to-day affairs
5 business affairs of Telfran?

6 A. Mr. Levey.

7 Q. Would it be fair to say that you were totally
8 inactive prior to that time?

9 A. Not totally.

10 Q. Were you at all involved in the day-to-day
11 affairs of the company?

12 A. No.

13 THE COURT: That is Mr. Aaron Levey, not Mr.
14 Joel?

15 THE WITNESS: Aaron Levey.

16 MR. LEVINE: Thank you.

17 FURTHER REDIRECT EXAMINATION

18 BY MR. SORKIN:

19 Q. Mr. Glantz, do you recall an affidavit of
20 McDermott, Will & Emery or Mr. Levine saying that they
21 reviewed records of the Levey estate and they were billing
22 you five hours for that?

23 A. To the best of my recollection, part of the five-
24 or six-hour charge included reviewing Levey's records.

25 Q. Were there any records of Mr. Levey that were

1 reviewed?

2 A. Not to my knowledge.

3 Q. Do you know whether they were subpoenaed?

4 A. They were not subpoenaed.

5 Q. Do you know how McDermott, Will & Emery was able

6 to say they reviewed Levey records that they never

7 subpoenaed?

8 A. I feel it was impossible for them to review Mr.

9 Levey's records without the records.

10 Q. How old are you, Mr. Glantz?

11 A. I am going to be 79 in July.

12 Q. Are you a certified public accountant?

13 A. I am.

14 Q. How long did you practice as a certified public

15 accountant?

16 A. 40-plus years.

17 Q. When did you retire?

18 A. Approximately twelve years ago.

19 Q. On the first day that McDermott, Will & Emery

20 appeared in your office, how many lawyers came down?

21 A. Three.

22 THE COURT: That is in his affidavit.

23 MR. SORKIN: No further questions, your Honor.

24 MR. LEVINE: Your Honor, if I may.

25 FURTHER RECROSS-EXAMINATION

1 BY MR. LEVINE:

2 Q. Mr. Glantz, I assume what Mr. Sorkin is
3 referring to are the time records of McDermott, Will & Emery
4 that were attached to our application for compensation. Can
5 you point out where in those time records McDermott
6 representative reviewed records of the Levey estate?

7 A. If I have my files there, in my affidavit I
8 stated, I quoted you. I quoted in my affidavit. There is a
9 quote from your invoice.

10 MR. LEVINE: Your Honor, I think we can deal with
11 that in argument. Can I ask one more question?

12 THE COURT: All right.

13 Q. Mr. Glantz -- and for the Court's information --
14 where was the McDermott, Will & Emery office that was
15 responsible for the engagement on the Telfran matter?

16 A. Miami.

17 Q. So when three lawyers came to Telfran's premises
18 shortly the day before Thanksgiving, if I recall, was that a
19 car trip from Miami as opposed to New York?

20 A. What is the question?

21 Q. Was that a trip from Miami as opposed to New
22 York?

23 MR. SORKIN: Objection. I am not sure he knows
24 where the lawyers came from. They may have lived in Fort
25 Lauderdale. I don't know either.

1 THE COURT: Were you billed for travel expense in
2 connection with that first trip? Is there any claim for
3 travel expenses for that first trip?

4 MR. LEVINE: No, your Honor.

5 THE COURT: So obviously they didn't come from
6 New York.

7 MR. LEVINE: From one of the Court's questions,
8 the impression might have been left that three lawyers came
9 down from New York.

10 THE COURT: Though it was more a question of why
11 do you need 3? .

12 MR. LEVINE: I can give you that in argument.

13 THE COURT: When you have three lawyers, there
14 are some cases that get staffed that way. I am not sure
15 this case gets staffed that way.

16 MR. SORKIN: I have no further questions, your
17 Honor.

18 THE COURT: You may step down.

19 (Witness excused)

20 THE COURT: Any other witnesses?

21 MR. SORKIN: Yes, your Honor. I call the
22 trustee, Lee Richards.

23

24

25 L E E R I C H A R D S, called as a witness by the

1 defendants, having been duly sworn, testified as
2 follows:

3 DIRECT EXAMINATION

4 BY MR. SORKIN:

5 Q. Mr. Richards, you are the trustee in the case of
6 Avellino & Bienes?

7 A. Yes, I am.

8 Q. Mr. Richards, in approximately the first or
9 second week of December, 1992, did counsel for Avellino &
10 Bienes express to you their objection to the amount that was
11 billed, approximately \$125,000, for the period November 18
12 through November 30 by Price Waterhouse?

13 A. I am sorry, Mr. Sorkin, what was the time
14 reference in your question?

15 Q. The first week or two of December, whenever the
16 bill became known.

17 A. My recollection is that sometime in the second or
18 perhaps the third week, you and I spoke and you indicated
19 you thought the bill for November was excessive.

20 MR. SORKIN: Your Honor, forgive me, I don't want
21 to insert myself as a witness, but I will try to phrase it.

22 Q. Mr. Richards, did counsel for Avellino & Bienes,
23 either myself or Ms. Hanswirth, express to you in January,
24 after you learned the fees were now up, through December 31,
25 to about \$250,000, that Avellino & Bienes was not going to

1 pay any further beyond that, or words to that effect?

2 A. My recollection is that you indicated on both
3 occasions in December and probably in January -- my
4 recollection is more hazy about that -- that you would be
5 objecting to the fees.

6 Q. Did at any time counsel advise you that it would
7 not consent to any further work being performed by Price
8 Waterhouse on the grounds that counsel and Avellino & Bienes
9 felt Price Waterhouse was spending unnecessary time and
10 counsel and Avellino & Bienes were objecting to any
11 additional work without any end to this engagement?

12 A. Well, your question has different language in it.
13 My recollection is, you indicated that you objected to the
14 bills that you had seen, and I either inferred or you said,
15 I don't remember which, that you would be objecting to
16 anything more that wasn't reasonable. That is my
17 recollection, Mr. Sorkin.

18 Q. Were you advised that, on January 16, Avellino &
19 Bienes would agree to no more extensions on grounds that
20 Avellino & Bienes believed that Price Waterhouse would never
21 finish its engagement, or words to that effect, unless they
22 were told to stop?

23 A. I don't remember all of that language, Mr.
24 Sorkin, but I do remember that you would not extend beyond
25 the 16th, and it was because you thought that Price

1 Waterhouse's work was excessive.

2 Q. Was it ever expressed to you, Mr. Richards, that
3 counsel should deal through you and not Price Waterhouse,
4 since you had retained the accountant to perform this
5 particular engagement under the order?

6 A. Was that ever expressed to me?

7 Q. Yes.

8 A. I don't recall that. My recollection is that
9 there were numerous dealings that I was hearing about
10 between your clients and Price Waterhouse, that that is
11 where most of the communication was occurring.

12 MR. SORKIN: I have no further questions, your
13 Honor.

14 THE COURT: Any cross?

15 MR. BRESLOW: No, your Honor.

16 MS. IMES: No.

17 (Witness excused)

18 MR. SORKIN: One further rebuttal witness, your
19 Honor. Mr. Avellino I would like to recall to the stand.

20 THE COURT: What does it have to do with this
21 phase of the hearing?

22 MR. SORKIN: It has to do with questions that
23 your Honor pointed to me and various witnesses and which
24 your Honor thought was the match point in this particular
25 case.

1 THE COURT: Yes, it is.

2

3 F R A N K J. A V E L L I N O was recalled and testified
4 further as follows:

5 DIRECT EXAMINATION

6 BY MR. SORKIN:

7 Q. Mr. Avellino, you are still under oath.

8 Mr. Avellino, you signed a consent to permit
9 Price Waterhouse to conduct an audit, among other things, is
10 that correct?

11 A. Yes, I did.

12 Q. Why did you consent to permit Price Waterhouse,
13 or indeed any accounting firm, whoever was chosen, to engage
14 in an audit?

15 A. Because the specific purpose was to conduct an
16 audit and to have an audit, so that we could exonerate
17 ourselves by showing the SEC and the world that we were
18 telling the truth, that everybody had been paid, that all
19 people that were owed money were the people we said they
20 were.

21 Q. Would you believe that if you had withdrawn your
22 consent at any time, it would be left out there, Mr.
23 Avellino, that there were some open issues with respect to
24 money that the SEC was claiming might have been dissipated
25 by you and had been taken by you that may have been not paid

1 to noteholders?

2 A. Definitely.

3 MR. SORKIN: I have no further questions.

4 THE COURT: I don't know why you put that on. It
5 tends to to confirm my view that your decision not to cut
6 off an opinion was a strategic one designed for your own
7 benefit.

8 MR. SORKIN: I can respond to your questions
9 right now or save it for argument.

10 THE COURT: It doesn't help you, if you think it
11 does.

12 MR. SORKIN: I do, your Honor. I certainly do.

13 THE COURT: You may step down.

14 (Witness excused)

15 THE COURT: Mr. Levine, do you want to put on any
16 witnesses on your side of the case?

17 MR. LEVINE: No, your Honor.

18 THE COURT: We have your affidavit and he hasn't
19 asked to cross-examine you, so I guess I can take your
20 argument to the extent that it doesn't go beyond your
21 affidavit, and even if it does, you are an officer of the
22 court and I can assume that you can testify without being
23 sworn. So why don't you go ahead. You seem to be the main
24 party in interest on this phase of the proceeding anyway.

25 MR. LEVINE: Thank you, your Honor.

1 Your Honor, let me first point out that our time
2 in the application only covers through the end of February.
3 So the time since February has been primarily involved in
4 preparing our fee application, responding to the objection,
5 and travel here today. So at the appropriate time we
6 probably would want to submit a supplement.

7 Your Honor, McDermott, Will & Emery was requested
8 to become involved in this case, as was Price Waterhouse, a
9 couple of days before Thanksgiving. The first distribution
10 to noteholders was supposed to be made three business days
11 effectively after that, December 2. Your Honor may recall
12 you continued that to December 3 because Mr. Glantz had made
13 an investment of part of the funds that matured on December
14 3.

15 We staffed this case, "we" being McDermott, Will
16 & Emery, primarily with two lawyers and one paralegal. The
17 second lawyer, aside from myself and Mr. Bonacquisti, who is
18 present in court today, he is an associate of the firm, the
19 trustee, Mr. Schultz, one of my partners. We literally
20 dropped what we were doing when the order came down and we
21 were appointed, and worked over the Thanksgiving holiday and
22 of course beyond that, to get the distribution out to
23 noteholders.

24 So I don't take too much of the Court's time, the
25 gist of Mr. Glantz's objection, if I understand it, is that

1 with 20/20 hindsight, after the investigation was done by
2 McDermott and by Price Waterhouse, it turns out that
3 apparently all noteholders were accounted for --

4 THE COURT: That argument is not persuasive to
5 me. I don't think you have to worry about that one. I am
6 not going to reduce your fee application on the theory that
7 everything turned out all right and therefore you didn't
8 have to do the work. I think that the only issue you have
9 to address is whether the time you spent was reasonable and
10 whether it was adequately documented.

11 MR. LEVINE: Your Honor, we are in the habit of
12 keeping detailed time records. Most of our work is in the
13 receivership and bankruptcy field. As your Honor knows, we
14 have to submit applications for court approval of fees in
15 most of our cases. We consciously did not overstaff the
16 case. However, there were two problems. One, Aaron Levey
17 died in September of 1992. The business of Telfran up to
18 September of 1992 had been run almost exclusively by Mr.
19 Levey. Mr. Levey was no longer around. A second problem
20 was that the records -- and I know your Honor has seen the
21 Price Waterhouse report, and of course it is in our
22 affidavit and application -- the records of Telfran were
23 virtually nonexistent. What we were given essentially, I
24 think almost on day one of the case, was a computer run of
25 the alleged noteholders of Telfran. There were minimal

1 records at that point to back up that computer run.

2 THE COURT: I know, but there is an accountant's
3 role and there is a lawyer's role, and it is the
4 accountant's job to, in effect, look at the records. The
5 inadequacies of the records seem to bear more upon the time
6 the accountants had to spend. They don't seem to have any
7 particular bearing on what time the lawyers had to spend,
8 because the lawyers' function is not an accounting function.
9 You don't have to go over there and check the records
10 yourself. You just have to maintain a supervisory presence
11 over the work done by the accountants. Therefore, it is a
12 little surprising that your bill is almost as large as
13 theirs is. What is theirs, \$127,000 and yours is --

14 MR. LEVINE: Our bill is \$80,000.

15 THE COURT: Theirs is \$127,000 and yours is
16 \$80,000, two-thirds the size of their bill, in a situation
17 in which much of the labor seems to me to be an accounting
18 function rather than a legal function. I don't know why it
19 cost so much.

20 MR. LEVINE: I think what we saw our function as
21 and what the trustee saw our function as was to verify as
22 much as possible, given the state of the records, in a legal
23 fashion whether there were additional noteholders. That
24 involved discovery and --

25 THE COURT: But it doesn't involve going out

1 there and checking the records of the company.

2 MR. LEVINE: No.

3 THE COURT: That is what I am saying.

4 MR. LEVINE: Correct. Your Honor has heard
5 several times that by a certain date, 90-some-odd percent
6 confirmations had come in verifying the Telfran or the
7 Avellino & Bienes noteholders. I want to put that in
8 context for you. Those confirmations came in from
9 noteholders who, we were told, represented the universe of
10 noteholders in Telfran. The problem was, there were really
11 not adequate records to determine, other than the statements
12 by Mr. Glantz or Mr. Mendelow, that these were all the
13 noteholders in Telfran. So what we were required to do, in
14 addition to taking deposition discovery, was to publish a
15 notice of the claims deadline and publish that in various
16 newspapers, and allow a sufficient amount of time to elapse,
17 even though we got the distribution out on December 3, to
18 see if any other noteholders came forward.

19 Beyond that, your Honor, if you give me a moment,
20 I would like to address the issue and clear up, I think, the
21 issue of the \$317,000. The very first day that we went to
22 Telfran's offices, Mr. Glantz handed us, and it is attached
23 to my affidavit in reply, a computer run from the Optus
24 System, I believe, showing a commission payable, now we know
25 to Bienes, of \$317,000.

1 THE COURT: How much of your fee is attributable
2 to that situation? I want to be sure that I am given the
3 accurate numbers on this.

4 MR. LEVINE: Your Honor, we haven't gone and
5 exactly computed that, but I would say probably between ten
6 and fifteen thousand dollars is a guesstimate, of the
7 \$80,000.

8 THE COURT: What did that entail? Taking
9 depositions?

10 MR. LEVINE: Let me tell you what that entailed.
11 There were several requirements. First, that piece of paper
12 showed the commission payable. Mr. Giantz at his deposition
13 that I took, and I asked him specifically if this was the
14 commission, said no, to the best of his recollection it was
15 interest payable. Beyond that, your Honor, we were
16 required -- and, of course, then there was a dispute whether
17 or not there was some oral agreement with Mr. Levcy -- but
18 we were required to produce a proof of intercompany claim to
19 preserve our rights that that 317 should come back to
20 Telfran. Now, at that time we didn't know that we knew all
21 the Telfran customers. Yes, on the existing noteholder
22 list, the funds in Telfran would have been sufficient to pay
23 the known noteholders. But until that expiration date, we
24 were able to publish in various newspapers and other
25 noteholders could have stepped forward. In the meantime,

1 had we not pursued the issue of \$317,000 and filed a claim
2 against Avellino & Bienes, we would have lost the right --

3 THE COURT: I am not saying you shouldn't have
4 filed a claim, don't get me wrong. I think you had to file
5 a claim. The only question is whether or not it should have
6 cost \$15,000 to find out that the claim was essentially
7 unverifiable or unprovable.

8 MR. LEVINE: Your Honor, we think the time is
9 reasonable. Your Honor, the reason we backed off the claim
10 is not because we don't still believe that that claim has
11 validity.

12 THE COURT: You can't prove it.

13 MR. LEVINE: Your Honor, we thought we had enough
14 to prove it. The only reason that claim is not being
15 pursued is now, after the publication notice, we still had
16 enough money to pay the existing noteholders. So if we had
17 brought that \$317,000 at that point into Avellino & Bienes,
18 it would have gone right back to the defendants. So clearly
19 at that point we stopped and said, there is no reason to
20 pursue this any longer, now that we believe we have the
21 universe of noteholders. So I want to put that in context
22 with the Court. Because again, if you read the Glantz
23 affidavit closely, many times things -- and I think this
24 sounds like the case in Avellino also -- are taken out of
25 context.

1 THE COURT: That is what I want to find out. I
2 just read the affidavits and I, quite frankly, don't go back
3 and check every particular item in the time sheet because
4 that is really just not what I normally do as to an issue
5 raised with respect to a specific item. I am talking more of
6 the overall structure of the time spent. If you find that
7 one item was overbilled, at least you have a conclusion that
8 maybe more time was spent. I am not going to go through
9 each item and nickel and dime you to death. It is like an
10 accountant, in a sense. A court basically does a test check
11 of four or five or six or seven items which are disputed.
12 If you resolve those one way or the other, then I am not
13 going to sit down and worry about every nickel and dime in
14 the time charges if those are not raised to me. But there
15 were very specific ones raised to me. One was the \$317,000
16 item. One was why three lawyers on the first trip went down
17 there. Why was there five or six or seven thousand dollars
18 spent to decide whether to subpoena records? These are the
19 issues they raise. They may not be characterizing what you
20 did accurately.

21 If you persuade me on those three or four, quite
22 frankly I am not going to hear much from them on anything
23 else. They put four or five arguments forward. If those
24 are spurious, I am not going to spend my time looking
25 through the audit sua sponte to find errors that they have

1 not called to my attention. So you need only respond to the
2 four or five precise issues raised as to you in that
3 affidavit. If they are not raised in that affidavit, as far
4 as I am concerned, the objections to them are waived.

5 MR. LEVINE: Let me respond, then, to those
6 issues specifically, your Honor.

7 THE COURT: Just for my information, what has Mr.
8 Richards billed here which they have not objected to?

9 MR. RICHARDS: Your Honor, the total, including
10 the amount that we have added, with the supplemental
11 affidavit, is \$115,000. That includes disbursements.

12 THE COURT: Which is about 25 percent of what the
13 accountants are seeking.

14 MR. RICHARDS: Roughly.

15 THE COURT: And you have two-thirds of what the
16 accountants are seeking. Therefore, right off the bat, if
17 he has in effect the major client, which is A & B, and he is
18 spending \$30,000 more than you are spending, it raises a
19 question as to whether \$88,000 is necessary as to the tail
20 end of the transaction, which is Telfran.

21 MR. LEVINE: Your Honor, I can't look into the
22 other proceeding, but I can tell you that, whether there was
23 \$800 million at stake or \$88 million at stake, I think the
24 attorneys' functions in either case would be the same. It
25 is unfortunate, but I think that is the case. In addition,

1 Price Waterhouse had already been involved in Avellino &
2 Bienes for some time prior to the time the Telfran case hit.
3 I think obviously their fees were lower in Telfran. They
4 can speak for themselves. But one of the reasons, I would
5 imagine, is that the issues were very similar and that they
6 had already been working on Avellino & Bienes for some time
7 before Telfran hit. So that may explain why their fees are
8 lower.

9 THE COURT: I really can't go through every item
10 and do my own audit on a 100 percent basis. I have to get
11 an overview of the case. Why don't you just respond to the
12 four or five objections they made. If you persuade me on
13 those, then, quite frankly, I will be satisfied.

14 MR. LEVINE: Your Honor, we feel the time spent
15 on the \$317,000 issue is reasonable. I think the SEC feels
16 the same way. I understand your question. Your question
17 is, is it excessive time on that issue? I think the gist of
18 Mr. Glantz's objection was: We told you there was no claim
19 there --

20 THE COURT: That argument I reject. I am
21 assuming that you had to spend a reasonable amount of time
22 to verify or not verify (a) whether the claim should be
23 filed and (b) whether or not it should be persisted in. I
24 am not going to accept that argument and I do reject it, so
25 let's not waste time with an argument I am rejecting: the

1 argument that you did not have the obligation to spend legal
2 time and accounting time satisfying yourself as a lawyer for
3 the trustee that everything was according to Hoyle, merely
4 because it turned out that way. That is a silly argument.
5 If we did that, then we would never award fees in any case
6 where, for one reason or another, the audit exonerated the
7 defendant. That is ridiculous. The whole point of this
8 audit, as I heard Mr. Avellino just testify, was to satisfy
9 the SEC that they had done nothing wrong. So then the whole
10 point of the audit is to satisfy independent examiners that
11 there is nothing wrong. To argue that you should not be
12 paid because there is nothing wrong is, in my view,
13 nonsense, and I reject out of hand that portion of Mr.
14 Glantz's affidavit. Don't waste your time with that.

15 MR. LEVINE: Thank you, your Honor.

16 On the issue of sending three people on the first
17 day to Miami, we were presented with this case, we weren't
18 involved in the negotiation of the consent order, we didn't
19 really know what we would find. This was, to our way of
20 thinking, an \$88 million problem. There may have been
21 missing noteholders. There may have been key records that
22 were moved out of the premises. We didn't know if there
23 were employees on the premises. We had just gotten
24 involved. Plus, it was the day before Thanksgiving. The
25 only time any attorneys from McDermott, Will & Emery

1 proceeded to Telfran offices in Fort Lauderdale was the
2 first two days of the case.

3 THE COURT: You say you were operating under very
4 strict time parameters which made perhaps more manpower
5 necessary.

6 MR. LEVINE: Your Honor, we had to get out a
7 distribution of \$88 million in three business days from the
8 time we were appointed. When I say "we," I am really
9 talking collectively Price Waterhouse and McDermott. Plus,
10 the case hit us the day before Thanksgiving. And you can
11 imagine that not a lot of staff is around that Thursday and
12 Friday. The distribution was supposed to go out December 2.
13 We went up there to organize Price Waterhouse, to find out
14 where the records were, where the computers were, who the
15 personnel was that knew about this issue so we could get a
16 distribution out by December 2. The order was pretty firm
17 about a lack of granting an extension of that date. The
18 only reason we got a date extension is some of the funds
19 were invested to mature on December 3. We had one partner,
20 one associate, the trustee whose time in this case after
21 that was minimal, and the Price Waterhouse people. And we
22 are dealing with \$88 million. We didn't know if this was a
23 fraud case, if there were records missing, personnel
24 missing. Again, we will hear that we should have taken the
25 defendants' -- I don't want to depart -- the defendants'

1 word that everything was fine. Obviously, we couldn't do
2 that, as your Honor has acknowledged.

3 The other issue about subpoenaing records from
4 the Levey estate is kind of a Catch-22 argument. Based on
5 the objection that had been filed --

6 THE COURT: How much time was actually spent on
7 the issue of whether or not you should subpoena records?

8 MR. LEVINE: Minimal time.

9 THE COURT: How much in dollars?

10 MR. LEVINE: I believe probably ten or twelve
11 hours, average, probably \$2,000.

12 THE COURT: Why should it take ten or twelve
13 hours to decide whether you subpoena records? That is a
14 decision you make in fifteen minutes.

15 MR. LEVINE: Your Honor, we had some initial
16 conflicting evidence about whether or not the Levey estate
17 had any records in this case.

18 THE COURT: But you had to decide to issue a
19 subpoena, which costs nothing to do, or not issue a
20 subpoena. You don't spend a lot of time thinking about it.

21 MR. LEVINE: Your Honor, I agree with that.

22 THE COURT: That is the one that I have a hard
23 time even following.

24 MR. LEVINE: The only issue, though, is, we did
25 not go ahead and spend a lot of time subpoenaing records

1 from the Levey estate.

2 THE COURT: I know that, but that decision is
3 one, with all due respect, a reasonable lawyer should make
4 within a matter of twenty minutes. Either you conclude that
5 there is no point in doing it, in which event you don't do
6 it, or you conclude that there is a point in doing it, in
7 which event you do do it. But you don't need to spend
8 twelve hours thinking about it. That one I have a hard time
9 trying to justify.

10 That is maybe a small item, but if that is
11 reflective of the overall approach that some people in the
12 firm were taking to this matter, which was maybe overkill
13 and overthinking, maybe there is a point to what Mr. Glantz
14 is saying, that there ought to be some reduction in the
15 overall structure of the bill, on a more or less
16 across-the-board percentage basis, rather than on a
17 line-by-line basis. That is what I am concerned about.

18 I am really taking an overview of it and trying
19 to form an opinion as to whether maybe there are people in
20 your firm who may be either more nervous than they should be
21 or think more than they should, and I have to decide what is
22 a reasonable fee. If that is an example of the way some of
23 these people proceeded, then maybe there ought to be some
24 reduction in your overall bill.

25 MR. LEVINE: Your Honor, obviously you are going

1 to determine that, and I will tell you it was our conscious
2 effort not to overbill --

3 THE COURT: It may be. I used to be in a law
4 firm, too. There are associates that you had in your law
5 firm who for one reason or another you had to write off time
6 because, although they were very conscientious and diligent,
7 they spent more time on it than the client was willing to
8 pay for.

9 This is not a situation where a client is paying
10 for it voluntarily. Therefore, the client is paying for it
11 almost pursuant to a consent order, but basically the Court
12 is deciding what is reasonable. That is always a judgment
13 call. I doubt very much whether I could have justified to
14 my clients, when I was practicing law, what amounts to
15 twelve hours to decide whether to issue a subpoena or not,
16 or \$15,000 to decide whether you are going to accept or not
17 accept a \$317,000 item. For \$15,000 a lot of firms write
18 briefs.

19 MR. LEVINE: Your Honor, the 317, I think, with
20 all due respect, is totally justified, given all the
21 circumstances here.

22 THE COURT: All you did is take a deposition.

23 MR. LEVINE: That is not all we had to do.

24 THE COURT: What else did you have to do?

25 MR. LEVINE: We had to file a claim in the

1 Avellino & Bienes case.

2 THE COURT: Lawyers prepare complaints sometimes
3 in a matter of two or three hours. It seems to me offhand
4 that a \$15,000 fee with respect to a \$317,000 item as to
5 which there is very little documentary support and is
6 resolved on the basis of oral testimony is more than it
7 should have been to resolve. Just looking at it as honestly
8 as I try to, it seems to be hard to justify. If I were
9 billing my clients for it, I would have a hard time doing
10 it. What kind of claim did you file? How much paperwork
11 was involved?

12 MR. LEVINE: Your Honor, maybe the best way to
13 answer this is that I guarantee you that much time was put
14 into responding to affidavits of Glantz and Avellino to this
15 \$317,000 issue. Until they submitted those affidavits and
16 until it was clear that we had enough money to satisfy the
17 noteholders in Telfran, it was from that point that we
18 dropped the issue. So the time was incurred in good faith.

19 THE COURT: What affidavit did you have to file
20 in response? That is what I want to know.

21 MR. LEVINE: We didn't have to file any affidavit
22 in response. But what I am saying is that the defendants
23 took the claim seriously enough to spend a significant
24 amount of time and effort on their own behalf contesting the
25 claim.

1 THE COURT: Because it was being asserted against
2 them. But my concern is not what time they spent but what
3 time you spent. What time did you spend in doing what?

4 MR. LEVINE: Your Honor, I raise that to show
5 that the claim is --

6 THE COURT: I am not suggesting that you are in
7 bad faith. I don't know you. But from what I have seen of
8 you, you are obviously a competent lawyer. You don't waste
9 my time, your arguments are cogent, your presentation is far
10 above the level of 90 percent of the lawyers I see. So I am
11 not faulting your good faith or bad faith or that of anybody
12 else in your firm. In fact, I find your performance quite
13 impressive, I will tell you that. There are few lawyers I
14 say that to. But I am not talking now about your good faith
15 or your bad faith. What I am saying is, good or bad faith,
16 was it reasonable? Sometimes people can disagree as to what
17 is reasonable. I have to make that decision. I don't like
18 to do it, but it does seem to me that \$15,000 effort on his
19 claim which should have been resolved by filing a claim,
20 which doesn't take that much time, and taking a deposition,
21 which shouldn't take that much time, addressed to a fairly
22 narrow issue, should not have cost more than five or six
23 thousand dollars at best. \$15,000 seems excessive to me.
24 That is what he is complaining about. I think I have to
25 take that into consideration in deciding whether I am going

1 to reduce the bill across-the-board. That has nothing to do
2 with your being a bad lawyer or good lawyer, bad faith or
3 good faith. It has to do with whether or not mainly,
4 perhaps, you did more work than was reasonably necessary.
5 That is just a hindsight judgment, which I am not even
6 comfortable making in these cases, but the law requires me
7 to do it. I can't get around it.

8 MR. LEVINE: Your Honor, I think those are the
9 three areas, I understood.

10 THE COURT: I am satisfied on the three lawyers.
11 I am not quite satisfied on the others. Therefore, my view
12 of it is -- and I will hear from Mr. Sorkin on it -- that I
13 will reduce the fee by 20 percent, which I think is a fair
14 reduction, given the overall structure of the case, because
15 I certainly don't think I could find that \$60,000 is an
16 unreasonable fee, given the nature of the case. If Mr.
17 Sorkin wants to be heard, that is fine. If he doesn't want
18 to be heard, that is my ruling.

19 MR. LEVINE: May I just add one thing, not to
20 question your ruling.

21 THE COURT: As far as Price Waterhouse is
22 concerned, my feeling is that Mr. Sorkin can address both
23 cases at once. Allowing for all the challenges to the
24 orders and allowing for all the arguments they make with
25 respect to what should or should not have been done, dealing

1 only with the question of the reasonableness of the work
2 they did and not whether they should have done it, factoring
3 all of those things into the hopper, and also considering
4 the fact that no time was charged at overtime rates, I think
5 the fees from Price Waterhouse in terms of the
6 reasonableness of the fee for the work they did, balancing
7 all of the factors, is sufficient to satisfy me that it
8 ought to be approved. I will let Mr. Sorokin address those
9 questions. But, as far as you are concerned, I don't think
10 I would be disposed to reduce your fees by a factor in
11 excess of 20 percent.

12 MR. LEVINE: Your Honor, may I just ask one
13 question. Obviously, there are disbursements that are
14 separate from that.

15 THE COURT: Disbursements I am not going to
16 quarrel with because they haven't.

17 MR. LEVINE: Your Honor, one other question. We
18 do have -- I am guessing -- probably by now close to 30
19 hours subsequent to the cutoff date dealing exclusively with
20 this fee issue, and responding to the application,
21 responding with our affidavit, and appearing today and the
22 cost of coming up here. I don't want to take any more of
23 your time --

24 THE COURT: Quite frankly, they have been
25 partially successful and probably entitled to argue that I

1 should make the same discount on those applications, which I
2 am prepared to do, unless they think I should do more, but I
3 doubt very much whether I accept that.

4 MR. LEVINE: That will be fine with us, your
5 Honor. Maybe the best way to take the least amount of your
6 time is for us to submit that statement to defendants, and
7 see if there can be an agreement on that.

8 THE COURT: Allowing for the fact that they are
9 20 percent victors on this application, I will give them a
10 20 percent reduction on the next one, because I think that
11 is rational. All I can do is what is reasonable. If they
12 want more than that, they can perhaps take this one
13 elsewhere. I will hear his arguments. Mr. Sorkin?

14 MR. SORKIN: Thank you. Your Honor, the only
15 thing --

16 THE COURT: I am satisfied, based upon the
17 testimony I have heard -- I don't need any argument on that
18 aspect of the case -- that the time spent, assuming that
19 Price Waterhouse correctly understood their engagement
20 responsibilities, was in my view reasonable. If I were to
21 weigh your specific challenges to the time spent against the
22 fact that they didn't bill you for as much in other areas as
23 they could for overtime and whatnot, I think the overall fee
24 which they submitted was reasonable. The only issue I have
25 to resolve now is whether you are correct or incorrect in

1 your legal argument that they should not have done more than
2 they did or as much as they did.

3 MR. SORKIN: May I add one thing, with respect to
4 that, for the record. Your Honor spoke on the three
5 lawyers. I want to point out that the three lawyers showed
6 up the second day and billed another \$6,000.

7 THE COURT: As far as I am concerned, given the
8 time parameters, given the structure of the case, given the
9 fact it was their first appearance, that was not
10 unreasonable, in the situation where they were forced to act
11 within a very short period of time. I am satisfied that
12 that time was well spent.

13 MR. SORKIN: Your Honor, let me address the Price
14 Waterhouse issue, if I may. Mr. Levine brought something up
15 which I think is terribly significant in respect to this.

16 If your Honor views the Telfran situation as
17 essentially the tail of Avellino & Bienes, the
18 \$441 million --

19 THE COURT: But he made a fairly persuasive
20 argument that I shouldn't look at it that way, and I accept
21 that argument.

22 MR. SORKIN: I would like you to focus in on
23 Price Waterhouse, because, of that 441, approximately 85
24 million was Telfran money, in that Avellino & Bienes would
25 take the money, send it in one check or a few checks to

1 Telfran, and Telfran would then distribute it to its
2 lenders.

3 The point I want to make, your Honor, is that,
4 that being the case, for Price Waterhouse to come in and ask
5 for \$414,000 in fees on Avellino & Bienes, and \$117,000 more
6 on Telfran, when Telfran, your Honor, was one office, with
7 Mr. Glantz and Mr. Mendelow --

8 THE COURT: Given the state of the records of
9 these companies, I am not persuaded that their expenditure
10 of time was unjustified or unreasonable. I think they could
11 have billed you for more. I accept Mr. Whitman's testimony
12 that they were consciously trying not to run the clock on
13 you, and had they really tried to run the clock on you, they
14 would have asked for overtime, which they didn't do. Taking
15 all those facts into consideration, I don't find those
16 numbers unreasonable. The only thing I need argument on
17 from you is whether, after your failure to tell them that
18 you wanted to, in effect, get out from under the consent
19 order, or tell me or anybody else that you wanted to get out
20 from under the consent order because it was costing more
21 than you thought it would, I should now let you come in and
22 say that they should have said that, based upon the state of
23 the company's records, based upon the fact that there were
24 no records for certain years, it is not likely that we are
25 going to be able to give any kind of an auditing opinion,

1 and therefore we stop sua sponte. That is really the issue.

2 It seems to me that if you and your client wanted
3 them to stop work, and you had made an unequivocal demand
4 for them to stop work and had said, "Frankly, we don't care
5 if you don't give us an opinion," you might be in a better
6 spot here in arguing that Price Waterhouse's continuing
7 efforts to try to give some kind of opinion was their own
8 decision for which they should be hanged. But you did not
9 make that kind of unequivocal demand on them.

10 MR. SORKIN: Let me address that, your Honor.

11 THE COURT: That is the issue.

12 MR. SORKIN: Let me address that issue. Your
13 Honor, I think, with all due respect, you are placing too
14 much of a burden --

15 THE COURT: I am not placing a burden on you at
16 all. You are objecting to the fees. I have a court order
17 which says you consent to an audit. You may have an
18 argument that the order makes it appear as though everybody
19 thought it was going to cost less than \$250,000, but you
20 consented to the audit. The word "audit" is a term of art.
21 Were there any ambiguity in the agreement itself or your
22 intentions under the agreement, that could have been brought
23 to me to be resolved at an appropriate hearing with parol
24 testimony. No hearing was requested. In fact, you never
25 even suggested that the consent order should be vacated.

1 You never moved to vacate the consent order or ever sought
2 to vacate the consent order.

3 What I have here is your consent that they
4 perform an audit of your company's financial statements for
5 a certain period of time. You never withdrew that consent.
6 You did consent. You are now objecting to their work and
7 making an argument that, if I give it the best reading I
8 can, it was unauditably anyway and therefore they shouldn't
9 have done all this extra audit work.

10 MR. SORKIN: Your Honor, I didn't mean the burden
11 in that sense. What I meant to say is that you are placing
12 the burden on Avellino & Bienes if we, Avellino & Bienes,
13 had hired --

14 THE COURT: But you did consent. You did not
15 have to consent to the audit. If you didn't consent to the
16 audit, the Commission could have pursued other remedies.
17 They would have asked for a hearing, they would have asked
18 for discovery, they would have asked for a TRO. There were
19 all kinds of things you avoided by this consent judgment.

20 MR. SORKIN: That is true.

21 THE COURT: So you got the benefit of it. The
22 burden you got from it was that if the audit costs more than
23 you thought it should, you had your right to object to the
24 cost of the audit. However, do you have the right to make
25 the argument to me that they should not have continued to

1 audit the company when it was plain that the company did not
2 have enough records to make it auditable in a cheap way?

3 MR. SORKIN: Your Honor, if I may?

4 THE COURT: That is the issue.

5 MR. SORKIN: I understand that. I would like to
6 address the issue. Let me put this back in the context in
7 which we consented. The sole issue, when we consented to
8 this, your Honor, was whether 441-odd million dollars was in
9 fact there.

10 THE COURT: Had your consent been so limited, you
11 would have had some very good arguments here today. But
12 your consent was not so limited, and you keep trying to
13 change the contract.

14 MR. SORKIN: No, I am trying to get a thought
15 out, with all due respect.

16 THE COURT: No, no, you have done it in your
17 papers, you have done it in your oral argument, you have
18 done it in your questioning, which I find a colossal waste
19 of my time. The fact of the matter is that you keep arguing
20 as though the primary purpose of the audit was the only
21 thing you agreed to. That argument is rejected, so don't
22 spend one minute more of my time addressing that question.

23 MR. SORKIN: I am not, your Honor.

24 THE COURT: Don't.

25 MR. SORKIN: I am not. What I am trying to say

1 to the Court is that we were in no position to tell this
2 accounting firm, who we did not retain, it was retained by
3 the trustee --

4 THE COURT: You were surely in a position to
5 write a letter to them, with a copy to me, saying, we
6 withdraw our consent and we are going to move to have the
7 consent order vacated. You surely had the power to do that.

8 MR. SORKIN: Your Honor, we complained to Mr.
9 Richards, who was our contact. We told him that we thought
10 that this audit was going nowhere.

11 THE COURT: You can kvetch all you want, but you
12 don't take the ultimate step because you don't want to. You
13 don't want to come into my court and move to vacate the
14 consent order. You don't want to come in and send a letter
15 to the trustee withdrawing your consent, because you know
16 that if you do that, the Commission or somebody else might
17 do something to you. You try to walk the middle line. Like
18 all people who walk the middle line, you end up getting your
19 throat cut.

20 MR. SORKIN: Your Honor, with all due respect, I
21 cannot disagree more. By the end of November, your Honor,
22 we were satisfied, as was the Commission, that all the money
23 was there. This is the end of November.

24 THE COURT: So why don't you just come in with
25 the Commission and make a joint application to vacate the

1 consent order and vacate the need for the audit?

2 MR. SORKIN: For the simple reason that we had
3 heard and we agreed that Price Waterhouse ought to spend
4 more time trying to prove the negative. When we began
5 complaining to Mr. Richards --

6 THE COURT: All I know is that you never made a
7 motion to vacate the order. That is the bottom line for me.

8 MR. SORKIN: We objected, your Honor. We could
9 do no more.

10 THE COURT: Objecting to the reasonableness of
11 the fees is one thing. Moving to vacate on the ground that
12 the audit was no longer necessary or possible is another.

13 MR. SORKIN: Your Honor, at some point in time we
14 drew the conclusion. If we are to be faulted for not making
15 the appropriate motion, I accept the Court's reprimand.

16 THE COURT: It is not a reprimand. What I am
17 saying to you is that your arguments would have had more
18 persuasive force had you come to me in December or January
19 and said, "Judge, we move to vacate the order because this
20 order is not possible or necessary and therefore we want to
21 withdraw our consent." I would have heard the arguments in
22 opposition, but at least you would have made a record. You
23 have not made that record. All I am saying is that I am not
24 going to listen to you tell me now that the audit was
25 unnecessary or not feasible.

1 To the extent that you are making an argument
2 that the audit should have been discontinued because the
3 records of the company were not adequate to permit any
4 opinion in any event, as it ultimately turned out, although
5 Mr. Whitman said had I given him more time he could have
6 done it -- maybe that is true. But what I am saying to you
7 is that I made the decision then that it was going to be no
8 opinion. I made that decision. You didn't make even that
9 one. I made that one.

10 What I am saying to you is that I am not being
11 persuaded by the argument that the audit should not have
12 continued because it couldn't possibly work because the
13 records were not adequate for that purpose. I am also not
14 going to be persuaded by the argument that the audit should
15 not have been continued because it was no longer necessary.
16 To the extent that the consent order called for it, in the
17 absence of a vacation of the consent order, the accounting
18 firm was entitled to conclude that it was still necessary
19 because the order was still in effect. I might have vacated
20 the consent order if you had all come to me with the
21 Commission and said, "This audit is costing more money than
22 it is worth and we don't think we should go forward with
23 it." I would have vacated the order, we wouldn't be here,
24 and Price Waterhouse wouldn't have done all this work.

25 MR. SORKIN: Your Honor, I am under the belief,

1 and it was not by formal papers, but when we approached the
2 Court and we had a telephone conference call and we said
3 enough, they are not finding anything more, and when we
4 appeared here on January 16 and made the same argument to
5 this Court, I did not phrase it --

6 THE COURT: All you said to me is that I should
7 not give them an extension, and I rejected that argument.
8 But you never said to me that that portion of the consent
9 order which called for an audit of the financial statements
10 of the company should be modified or not continued because
11 the financial records of the company were such that the
12 audit could not be completed in any event and therefore
13 there was no sense trying. All you said to me was that they
14 shouldn't have more time. I agreed with you to the limited
15 extent of giving them one more week.

16 MR. SORKIN: Your Honor, I thought implicitly,
17 and explicitly, the reason we didn't give them any more time
18 is because they were spinning their wheels, to put it in the
19 vernacular. They had not shown anything from November when
20 they had identified all the noteholders. They had not come
21 up with anything new and were trying to show a negative.

22 THE COURT: That is a danger in not making
23 arguments explicit. If you had said to me, "Judge, we will
24 take no opinion. We will take a statement from the
25 accountants that they can't opine on the financial

1 statements" --

2 MR. SORKIN: It was not for us to ask for that.
3 It was for the trustee, your Honor.

4 THE COURT: You said that to me. No, no. You
5 are the one who would be prejudiced by the accounting firm
6 coming back and saying, "We can't give any opinion about
7 this company. The records are in such bad shape that we
8 can't give an opinion on it." If you had said to me, "We
9 will take that, Judge," I would have told Price Waterhouse
10 to stop work, they don't want an opinion. Mr. Whitman would
11 have been very happy with that; we would all be very happy
12 with that. You didn't say that. Maybe you intended to say
13 it, but you didn't say it. If you had said it, I might have
14 told them to stop work. I would not have made them spend
15 another week working when you said to me you didn't want the
16 opinion anyway because you would live with no opinion.

17 MR. SORKIN: I must say, your Honor, after they
18 had identified all the noteholders and all the money could
19 have been returned, we could have lived with any opinion.

20 THE COURT: You didn't tell me that.

21 MR. SORKIN: I apologize, your Honor, but the
22 trustee --

23 THE COURT: It is too late to apologize now.
24 They had already done the work.

25 MR. SORKIN: But it was the trustee, your Honor,

1 with all due respect, that we had to deal with.

2 THE COURT: The trustee was operating under the
3 consent order too, and until vacated he had to comply. If
4 he doesn't comply with the consent order, he is in trouble
5 as a fiduciary. So if you had all come to me and said,
6 "Vacate the consent order because it is no longer
7 necessary," I don't see why I would have continued it in
8 effect if I had been told that the time spent in trying to
9 give you an opinion would be more costly than it was worth.
10 I don't think Price Waterhouse would have been bothered by
11 that. They have other clients. This is not a major
12 moneymaker for them, you know.

13 MR. SORKIN: Your Honor, with all due respect,
14 \$439,000, for about eight weeks' work.

15 THE COURT: They already earned \$300,000 of it in
16 January, so we are talking about another 120. They could
17 have lived without the other 120 and not done the work,
18 especially during the tax season.

19 MR. SORKIN: Your Honor, I appreciate that, and
20 if I had asked your Honor to simply focus on the
21 excessiveness of it, which your Honor says you are not going
22 to consider --

23 THE COURT: I find the work they did was
24 eminently reasonable, given the financial condition of this
25 company. If your clients choose to keep their company in

1 that fashion, with records in that fashion, with no records
2 going back three years, and exercise their rights under the
3 law and don't even want to provide the assistance of
4 drafting the financial statements, your clients being
5 certified public accountants, to save costs, I say too bad
6 for you.

7 MR. SORKIN: We turned over tax returns going
8 back ten years, which we felt would be more than adequate.
9 A partnership tax return, your Honor, is more than adequate
10 to create a financial statement.

11 THE COURT: Let me say something. You want me to
12 make a credibility finding? I don't believe your client. I
13 heard his testimony, I saw his demeanor, I heard his
14 inconsistencies on direct and cross, I noted the
15 inconsistency in the position he took in the letter and the
16 position he took on trial. I don't believe him. So, to the
17 extent there are credibility issues to resolve, I resolve
18 them against your client.

19 MR. SORKIN: With respect to what issue?

20 THE COURT: With respect to the issue of the
21 first conversation with Price Waterhouse; with respect to
22 the reasons why he did not prepare the financial statements.
23 I think he was worried about self-incrimination. That is
24 why he didn't prepare the financial statements. To the
25 extent he gave a different version on the stand today, I

1 don't believe it.

2 MR. SORKIN: I will have to go back and look.

3 THE COURT: Read the record.

4 MR. SORKIN: I will do that, your Honor, and I
5 believe --

6 THE COURT: There was a very subtle change
7 between direct, cross, and my question.

8 MR. SORKIN: Your Honor, I don't believe -- well,
9 I won't argue the issue because that is not before your
10 Honor. We will save that for another day, I believe.

11 THE COURT: Given the way your company kept its
12 records, given their unwillingness to provide their own time
13 as a substitute for the accountant's time, given the nature
14 of the audit that had to be conducted, given what I consider
15 the virtual nonexistence of records in relevant periods, I
16 say the money that Price Waterhouse spent auditing your
17 company was entirely rational. If you think my decision is
18 an abuse of discretion, that is why there is a Circuit
19 Court.

20 In any event, to the extent that you object to
21 the Price Waterhouse fees, for the reasons given on the
22 record those objections are overruled.

23 With respect to the objections as to the
24 attorneys' fees in your case, Mr. Levine, I will order an
25 across-the-board reduction of 20 percent, based on the

1 testimony I have heard. You have satisfied me on one of the
2 items contested, but you haven't satisfied me on the other
3 two. I think that is a reasonable approach. If there is an
4 issue as to that, let me know.

5 MR. LEVINE: Your Honor, we have no problem with
6 that. The only thing I would request is that: again, do we
7 have the same ruling on our supplementary time after
8 February 28 through today?

9 THE COURT: It is a rule-of-thumb ruling. I
10 think the Circuit Court requires me to do no more. I don't
11 think the Circuit Court requires me to sit down and count
12 beans, but just to make a general assessment as to whether
13 your fees are reasonable. I think they are, for the most
14 part, reasonable, but I will order a proportionate reduction
15 because I am not entirely sure that some of the time spent
16 was rational.

17 MR. LEVINE: That is fine with us. All we are
18 anxious to do is -- it has been five months -- to get some
19 money into the firm on this.

20 THE COURT: If you give me an order, I will sign
21 it within the next few days.

22 MR. LEVINE: Thank you, your Honor.

23 THE COURT: Where do we go from here in this
24 case?

25 MR. SORKIN: We would like to set a discovery

1 order with respect to Telfran, your Honor.

2 THE COURT: There has been no discovery cutoff?
3 Has there been a cutoff with the other?

4 MR. SORKIN: Yes, your Honor.

5 THE COURT: When?

6 MR. SORKIN: June 14.

7 THE COURT: Is that realistic or not?

8 MR. SORKIN: I am not quite sure, your Honor. We
9 are into it now.

10 THE COURT: When is your next status conference?
11 Do you have one?

12 MR. SORKIN: I week before that, your Honor, June
13 7.

14 THE COURT: Do you want to extend the cutoff date
15 in both cases?

16 MR. SORKIN: Yes.

17 THE COURT: July 31. Is that reasonable?

18 MR. SORKIN: That is fine.

19 THE COURT: I will see you for a conference in
20 July and we will talk about it. Is this a jury case or
21 nonjury case?

22 MR. SORKIN: Nonjury case.

23 THE COURT: This one we may be able to try, since
24 the Congress is not giving us the funds to try jury cases.
25 July 23.

1 MS. ASHBAUGH: I believe there is a jury demand
2 in this case.

3 THE COURT: If there is a jury demand, then we
4 won't be able to try you until Congress lifts the ban on
5 juries for civil cases. Put it this way: Our appropriation
6 has been cut so substantially that funds are no longer
7 available for juries in civil cases. That leaves me with
8 several alternatives if this becomes an issue. They are
9 supposed to let us know on May 12 whether or not that is
10 going to change. If it doesn't change, that leaves me with
11 several alternatives: to compel Congress to appropriate the
12 funds, which I guess some judges have done; to try this case
13 with jury volunteers, if you find people willing to do that;
14 and the other suggestion, which I guess no one has ever
15 quite explored, is the possibility that the parties can pay
16 the jury fees. If all the parties pay them, then I guess no
17 one can argue the jury is one way or the other.

18 MR. SORKIN: I am not sure the SEC can pay.
19 Their appropriation comes from Congress.

20 THE COURT: Then you will have an advantage with
21 the jury.

22 MR. SORKIN: As long as your Honor instructs them
23 that way.

24 THE COURT: Let's not worry about that until we
25 see what happens. But this case won't be tried before the

1 fall anyway. Let's see where we go.

2 MR. SORKIN: Thank you, your Honor.

3 THE COURT: See you on July 23.

4 MR. LEVINE: Not to belabor one procedural
5 issue -- again, this is really to save more time on issues
6 like this -- for our supplement, is it satisfactory if we
7 submit time and disbursements to the defendants, assuming
8 the same --

9 THE COURT: If they have no objection, I will
10 sign it by stipulation.

11 MR. LEVINE: -- assuming the same 20 percent
12 ruling.

13 MR. SORKIN: Your Honor, can we have some idea
14 now of what the additional amount is going to be?

15 MR. LEVINE: Your Honor, we don't have our March
16 run. I am guesstimating probably a total of something
17 approaching 25 to 30 hours, at a rate of \$200, which is
18 something in the range of five or six thousand dollars, plus
19 the expenses of the flights and hotel room.

20 THE COURT: What about Price Waterhouse? Are you
21 finished with your fee application?

22 MR. BRESLOW: There may be, Judge, one small one
23 for \$2,000.

24 THE COURT: I think those you can agree on. They
25 are relatively minor. If you need another hearing, I will

1 give you one. We have had one today.

2 MR. BRESLOW: By the way, your Honor, shall we
3 prepare an order to be signed, submit it on the other side?

4 THE COURT: It is better to do it that way.

5 MR. RICHARDS: Your Honor, if I may, there is one
6 issue, since the time on this is so sensitive. The order
7 requires the trustee, not simply Price Waterhouse, but the
8 trustee to issue a report. We haven't done that because of
9 sensitivity with respect to fees. I am not sure whether the
10 parties are prepared to respond or the Court wishes to give
11 us any guidance. But under the order we technically still
12 have an obligation to issue a report to the Court. I am not
13 sure this is the time to get the guidance, but we have that
14 obligation.

15 THE COURT: Whose fees would those be? Those
16 would be your fees, I assume.

17 MR. RICHARDS: Those would be fees from us and
18 from Mr. Levine's firm.

19 MR. LEVINE: That is a very good point. I am not
20 sure in the Telfran matter, but Price Waterhouse has issued
21 a fairly comprehensive report. It would seem to be gilding
22 the lily, and obviously there will be additional fees for
23 the trustee. We are perfectly willing to issue the report,
24 but there will be additional fees to do that. The report
25 will say basically what we said in our application, what

1 Price Waterhouse has already found, and I am sure Mr.
2 Richards would do that in his case.

3 MR. RICHARDS: I am not sure we have any more
4 than that.

5 MR. LEVINE: We have to sit down.

6 THE COURT: Work it out by agreement.

7 MR. SORKIN: I am not sure what the report would
8 say other than what we have explored fully today and what is
9 before this Court.

10 THE COURT: I don't know what kind of report we
11 are talking about.

12 MR. LEVINE: Your Honor, just to refresh your
13 memory, it is in the consent order, I assume. In both cases
14 there is a requirement for the trustee of Avellino & Bienes,
15 and Telfran, to issue a trustee's report.

16 THE COURT: Which is what? It says what?

17 MR. RICHARDS: There is not much said, your
18 Honor. I assume the contemplation of the parties was that
19 we would simply take the Price Waterhouse report and put it
20 into our own report, but there is not much guidance in the
21 order about it. It simply requires us to report on the
22 foregoing to the Court, and the foregoing is a description
23 of the duties that we had as trustees.

24 MR. SORKIN: Your Honor, it seems to me, again,
25 why is it necessary to do so? I would be more than happy to

1 talk to Mr. Levine and Mr. Richards, But it just seems to be
2 more expense. I assume their report is going to say that no
3 opinion could be reached and all the money was returned as
4 far as they know and there are no additional notcholders.
5 If they are going to say they did all of these things in
6 connection with their duties, I think it is a waste of time.

7 THE COURT: I don't think you have to do anything
8 more than to refer to your affidavit submitted with the
9 motion. All I would do is draft a report which says that I
10 am filing this report, the details are set forth in my
11 affidavits, and that should do it.

12 MR. RICHARDS: If for any reason we think of
13 anything else, we will report to the parties and see if they
14 object.

15 THE COURT: If you have an argument, see me, but
16 if not, do it in that fashion.

17 MR. SORKIN: I would suggest before they
18 communicate with the Court they talk to us.

19 THE COURT: I strongly suggest that people talk
20 to one another.

21 MR. LEVINE: Yes. We didn't receive any comments
22 to our application before we received the objections.

23 THE COURT: All I am saying is that all you need
24 to do is cross-reference your affidavits and the Price
25 Waterhouse report, since they have already paid for that.

1 They shouldn't have to pay for it twice. Fair enough?

2 MR. RICHARDS: That is fine with us.

3 THE COURT: Keep your report as short as possible
4 and the fees in connection therewith as minimal as possible.

5 MR. RICHARDS: That is perfectly all right, so
6 long as the parties and the Court agree.

7 THE COURT: I don't want any more, and it is to
8 report back to me.

9 MR. RICHARDS: Yes.

10 THE COURT: Take care.

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