Docket #0005 Date Filed: 10/9/2015

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MASSACHUSETTS
CENTRAL DIVISION

In re: TELEXFREE, LLC, TELEXFREE, INC. and TELEXFREE FINANCIAL, INC., Debtors.	Chapter 11 Cases 14-40987-MSH 14-40988-MSH 14-40989-MSH Jointly Administered
STEPHEN B. DARR AS TRUSTEE OF THE ESTATES OF TELEXFREE, LLC, TELEXFREE, INC. and TELEXFREE FINANCIAL, INC., Plaintiff, v. RITA DOS SANTOS, INDIVIDUALLY AND AS PUTATIVE CLASS REPRESENTATIVE, Defendant.	Adversary Proceeding No. 15-04055-MSH

MOTION FOR SCHEDULING ORDER REGARDING
TRUSTEE'S REQUEST FOR PRELIMINARY INJUNCTION

Stephen B. Darr, as he is the duly appointed Trustee of the Chapter 11 Estates of TelexFree, LLC, TelexFree, Inc. and TelexFree Financial, Inc. (the "Trustee"), moves this Court for the entry of a scheduling order with respect to the Trustee's Request for a Preliminary Injunction establishing:

(a) A date by which the Defendant must file her response;

(b) A date by which replies, if any, must be filed; and

(c) A hearing on the Request for Preliminary Injunction.

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The Trustee requests, however, that the Court not schedule a hearing for the week beginning October 26, 2015.

In support of his motion, the Trustee states as follows:

1. The Trustee has filed a Verified Complaint, in which he seeks a Declaratory Judgment that a certain Unjust Enrichment Claim which Rita Dos Santos seeks to add to the class action, currently pending in the United States District Court for the District of Massachusetts, is in violation of the automatic stay and, therefore, *void ab initio*.

2. The Trustee's Verified Complaint also seeks a Preliminary Injunction restraining and enjoining Rita Dos Santos from prosecuting her Unjust Enrichment Claim, pursuant to § 105 of the Bankruptcy Code.

3. The Trustee is seeking both to restrain and enjoin under § 105 of the Bankruptcy Code Rita Dos Santos from prosecuting the Unjust Enrichment Claim pending a determination with respect to the applicability of § 362 of the Bankruptcy Code to the action. In conjunction with the request for injunctive relief, the Trustee has also filed a Motion with the United States District Court for the District of Massachusetts in the action of *In re TelexFree Securities Litigation*, MDL No. 4-14-MD-2566-TSH seeking a stay in the prosecution of the Unjust Enrichment Claim pending a determination by this Court of the issues raised in the Verified Complaint. (Copies of the relevant District Court pleadings are annexed, excluding those exhibits consisting of Motions and pleadings previously filed with this Court.)

WHEREFORE, the Trustee respectfully prays that his Motion be allowed and the Court enter a scheduling order.

STEPHEN B. DARR AS TRUSTEE
OF THE ESTATES OF TELEXFREE,
LLC, TELEXFREE, INC. and
TELEXFREE FINANCIAL, INC.

By his attorneys,

Dated: October 9, 2015

/s/ Charles R. Bennett, Jr.

Harold B. Murphy (BBO #326610
Charles R. Bennett, Jr. (BBO #037380)
Murphy & King, Professional Corporation
One Beacon Street
Boston, MA 02108
(617) 423-0400
CBennett@murphyking.com
HMurphy@murphyking.com

CERTIFICATE OF SERVICE

I, Charles R. Bennett, Jr., hereby certify that on October 9, 2015, I caused a copy of the *Motion For Scheduling Order Regarding Trustee's Request For Preliminary Injunction*, filed through the ECF system, to be sent electronically to the registered participants as identified on the Notice of Electronic Filing and by first class mail and/or electronic mail to the following parties:

Robert J. Bonsignore, Esq.
Bonsignore, LLC.
193 Plummer Hill Rd,
Belmont, NH 03220
Email: rbonsignore@class-actions.us
(*Counsel to the Defendant, Rita Dos Santos*)

William R. Baldiga, Esq.
Brown Rudnick LLP
One Financial Center
Boston, MA 02111
Email: wbaldiga@brownrudnick.com
(Counsel to the Defendant, Rita Dos Santos)

/s/ Charles R. Bennett, Jr.
Charles R. Bennett, Jr.

696246

EXHIBIT A

[Trustee's Motion to Intervene]

UNITED STATES DISTRICT COURT
DISTRICT OF MASSACHUSETTS

In Re:	
TELEXFREE, SECURITIES LITIGATION	**MDL No. 4:14-md-2566 TSH**
This Document Relates to: ALL CASES	

TRUSTEE'S MOTION TO INTERVENE

Stephen B. Darr, the duly appointed Chapter 11 bankruptcy trustee (the "Trustee") of the bankruptcy estates of TelexFree, LLC, TelexFree, Inc., and TelexFree Financial, Inc. (collectively, the "Debtors"),[1] respectively moves to intervene for the limited purpose of moving to stay Rita Dos Santos, individually and as putative plaintiff class representative of individuals who are net losers ("Dos Santos"), in her proposed prosecution of an unjust enrichment claim (Count IV of the proposed Third Amended Complaint) against Daniil Shoyfer, individually and as putative defendant class representative of individuals who are determined "net winners" who received payments from net losers (the "Unjust Enrichment Claim").

As set forth more fully in the Trustee's accompanying Memorandum of Law in Support of this Motion, the Trustee has commenced an adversary proceeding in the United States Bankruptcy Court for the District of Massachusetts against Rita Dos Santos, individually and as putative class representative (the "Adversary Proceeding"). In the Adversary Proceeding, the Trustee is seeking a declaratory judgment that the Unjust Enrichment Claim Ms. Dos Santos

[1] The Debtors are parties to a jointly-administered bankruptcy proceeding in the United States Bankruptcy Court for the District of Massachusetts captioned as *In re TelexFree, LLC, et al.*, Chapter 11 Case No. 14-40987-MSH.

seeks to add to this civil action violates the automatic stay imposed by § 362 of the Bankruptcy Code because it seeks to exercise control over property of the bankruptcy estate. Alternatively, in the Adversary Proceeding the Trustee seeks an injunction against Ms. Dos Santos' prosecution of the Unjust Enrichment Claim pursuant to § 105 of the Bankruptcy Code because the prosecution will materially and adversely interfere with the administration of the bankruptcy case and the Bankruptcy Court's core function of determining and administering claims and distributing funds to all of the Debtors' creditors.

The Trustee should be allowed to intervene to protect and defend Dos Santos' improper encroachment on the Trustee's exclusive province to recover fraudulently transferred funds on behalf of the Debtors' bankruptcy estates for the benefit of their respective creditors. Accordingly, the Trustee respectfully requests that its Motion to Intervene be granted.

STEPHEN B. DARR AS TRUSTEE
OF THE ESTATES OF TELEXFREE,
LLC, TELEXFREE, INC. and
TELEXFREE FINANCIAL, INC.,

By his attorneys,

Dated: October 7, 2015

/s/ Charles R. Bennett, Jr.

Harold B. Murphy (BBO #326610)
Charles R. Bennett, Jr. (BBO #037380)
Peter C. Obersheimer (BBO #680187)
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LOCAL RULE 7.1(a)(2) CERTIFICATION

I, Charles R. Bennett, Jr., hereby certify that I have conferred with Plaintiff Interim Executive Committee Counsel and have attempted in good faith to resolve or narrow the issue.

Dated: October 7, 2015 */s/ Charles R. Bennett, Jr.*

CERTIFICATE OF SERVICE

I, Charles R. Bennett, Jr., hereby certify that this document filed through the ECF system will be sent electronically to the registered participants as identified on the Notice of Electronic Filing (NEF) and paper copies will be sent to those indicated as non-registered participants on this date.

Dated: October 7, 2015 */s/ Charles R. Bennett, Jr.*

696048

EXHIBIT B

[(Proposed) Trustee's Limited Motion to Stay]

UNITED STATES DISTRICT COURT
DISTRICT OF MASSACHUSETTS

In Re:	
TELEXFREE, SECURITIES LITIGATION	**MDL No. 4:14-md-2566 TSH**
This Document Relates to: ALL CASES	

[PROPOSED] TRUSTEE'S LIMITED MOTION TO STAY

Stephen B. Darr, the duly appointed Chapter 11 bankruptcy trustee (the "Trustee") of the bankruptcy estates of TelexFree, LLC, TelexFree, Inc., and TelexFree Financial, Inc. (collectively, the "Debtors"),[1] respectfully requests this Court stay Rita Dos Santos, individually and as putative plaintiff class representative of individuals who are net losers ("Dos Santos"), in her proposed prosecution of an unjust enrichment claim (Count IV of the proposed Third Amended Complaint) against Daniil Shoyfer, individually and as putative defendant class representative of individuals who are determined "net winners" who received payments from net losers (the "Unjust Enrichment Claim"),[2] pending the resolution of the related Chapter 11 bankruptcy adversary proceeding (the "Adversary Proceeding").

As set forth more fully in the Trustee's accompanying Memorandum of Law in Support of this Motion, on September 23, 2015, Dos Santos moved for leave to file a Third Amended Complaint seeking to expand her unjust enrichment claim by adding a putative class of "net

[1] The Debtors are parties to a jointly-administered bankruptcy proceeding in the United States Bankruptcy Court for the District of Massachusetts captioned as *In re TelexFree, LLC, et al.*, Chapter 11 Case No. 14-40987-MSH.

[2] The Unjust Enrichment Claim is Count IV of the Third Amended Consolidated Complaint.

winner" defendants who are to be liable to "net loser" plaintiffs. On October 7, 2015, the Trustee commenced the Adversary Proceeding in the Bankruptcy Court requesting the Bankruptcy Court determine that (a) the Unjust Enrichment Claim violates the automatic stay imposed by § 362 of the Bankruptcy Code because her action exercises control over property of the bankruptcy estate, to wit, certain causes of action to recover payments received by those Participants identified as net winners in the Debtors' scheme, and (b) an injunction under § 105 of the Bankruptcy Code because the Unjust Enrichment Claim interferes with the orderly, efficient administration of the Bankruptcy estate and seeks to effectively remove to this Court matters relating to claims determination that are core findings of the Bankruptcy Court.

This Court should stay Dos Santos' improper encroachment on the Trustee's exclusive province to recover fraudulently transferred funds on behalf of the Debtors' bankruptcy estates for the benefit of their respective creditors. The stay is essential, and will prevent Dos Santos from interfering with the Bankruptcy Court's jurisdiction to make a net winner determination. Accordingly, the Trustee respectfully requests that its Motion for Stay be granted pending the resolution of the Adversary Proceeding.

STEPHEN B. DARR AS TRUSTEE
OF THE ESTATES OF TELEXFREE,
LLC, TELEXFREE, INC. and
TELEXFREE FINANCIAL, INC.,

By his attorneys,

Dated: October 7, 2015

/s/ Charles R. Bennett, Jr.

Harold B. Murphy (BBO #326610)
Charles R. Bennett, Jr. (BBO #037380)
Peter C. Obersheimer (BBO #680187)
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LOCAL RULE 7.1(a)(2) CERTIFICATION

I, Charles R. Bennett, Jr., hereby certify that I have conferred with Plaintiff Interim Executive Committee Counsel and have attempted in good faith to resolve or narrow the issue.

Dated: October 7, 2015

/s/ Charles R. Bennett, Jr.

CERTIFICATE OF SERVICE

I, Charles R. Bennett, Jr., hereby certify that this document filed through the ECF system will be sent electronically to the registered participants as identified on the Notice of Electronic Filing (NEF) and paper copies will be sent to those indicated as non-registered participants on this date.

Dated: October 7, 2015

/s/ Charles R. Bennett, Jr.

EXHIBIT C

[Affidavit of Stephen B. Darr]

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MASSACHUSETTS
CENTRAL DIVISION

In re: TELEXFREE, LLC, TELEXFREE, INC. and TELEXFREE FINANCIAL, INC., TelexFree.	Chapter 11 Cases 14-40987-MSH 14-40988-MSH 14-40989-MSH Jointly Administered
STEPHEN B. DARR AS TRUSTEE OF THE ESTATES OF TELEXFREE, LLC, TELEXFREE, INC. and TELEXFREE FINANCIAL, INC., Plaintiffs, v. RITA DOS SANTOS, INDIVIDUALLY AND AS PUTATIVE CLASS REPRESENTATIVE, Defendant.	Verified Adversary Proceeding No.

AFFIDAVIT OF STEPHEN B. DARR

I, Stephen B. Darr, hereby submit the following affidavit in support of the contemporaneously filed *Complaint*.

1. I am the duly appointed Chapter 11 trustee (the "Trustee") in the above-captioned Chapter 11 cases of TelexFree, LLC, Case No. 14-40987, TelexFree, Inc., Case No. 14-40988, and TelexFree Financial, Inc., Case No. 14-40989 ("TelexFree" or the "Debtors"), having been appointed by order of the Court dated June 6, 2014.

2. I am a Managing Director with the Business Advisory Practice of Huron Consulting Group. I have more than 35 years of experience providing accounting, auditing and

financial consulting services to business organizations many of which are experiencing significant financial and operating difficulties. I am a Certified Public Accountant in Massachusetts and New Hampshire, a Certified Insolvency and Restructuring Advisor and hold certifications in both Financial Forensics and Distressed Business Valuation, as well as other professional qualifications.

3. The statements provided herein are based upon information and knowledge I have derived through my involvement in the Debtors' Chapter 11 cases.

4. On October 7, 2015, I filed the *Motion by Chapter 11 Trustee for Entry of an Order Finding that the Debtors Engaged in a Ponzi and Pyramid Scheme and Related Relief* (the "Ponzi Scheme Motion"). Attached as Exhibit "A" to the Ponzi Scheme Motion is the *Affidavit of Stephen Darr in Support of Motion for Entry of an Order Finding that the Debtors Engaged in a Ponzi and Pyramid Scheme and Related Relief* (the "Ponzi Affidavit"). The Ponzi Affidavit is attached hereto and is incorporated by reference.[1]

5. By order dated October 23, 2014, six class action complaints filed by Rita Dos Santos ("Dos Santos") and others, Participants in the Debtors' scheme, were transferred and consolidated in the United States District Court for the District of Massachusetts (the "MDL"). These complaints asserted claims against various financial institutions, former professionals of the Debtors, and major Participants in the Debtors' scheme for, among other things, alleged violations of Mass. Gen. Laws Ch. 93A. I did not object to the prosecution of the claims initially asserted because either the claims were not bankruptcy estate causes of action or Dos Santos was better positioned to pursue the claims as a result of, among other things, the applicability of the *in pari delicto* defense.

[1] Terms not otherwise defined herein shall have the meanings set forth in the Ponzi Affidavit.

6. On September 23, 2015, I became aware that Dos Santos had moved to file a Third Consolidated Amended Complaint in the MDL asserting a claim for unjust enrichment (the "Unjust Enrichment Action") against a class of Participants who are determined to be net winners on behalf of Participants in the Debtors' scheme who are net losers and made payments to such net winners. Unlike previous claims brought in the MDL, the Unjust Enrichment Action directly relates to causes of action of the bankruptcy estates and interferes with the administration of the bankruptcy estates.

7. I and my professionals have spent considerable time developing an understanding of the Debtors' records and establishing a methodology for determination of those who received more from the Debtors' scheme than they invested ("Net Winners"), and those who invested more into the Debtors' scheme that they received ("Net Losers"). The determination of Net Winners and Net Losers is core to the bankruptcy cases, both as it pertains to allowance of claims and the prosecution of avoidance actions. The Unjust Enrichment Action requires consideration of Net Winners and Net Losers, and continued pursuit of the action would result in duplication of effort, increase in costs, and potentially inconsistent results. Additionally, the putative class representatives in the Unjust Enrichment Action only represent a subset of potential Net Winners and Net Losers in these cases, as they do not include Participants who are Net Winners or Net Losers as a result of payments made to, or received from, the Debtors.

8. The Unjust Enrichment Action is based upon the same claim and transactions and involves the same pool of funds that will be the subject of avoidance actions to be commenced by the bankruptcy estates against Net Winners in the Debtors' scheme.

Sworn to this 7th day of October, 2015.

Dated: October 7, 2015

Stephen B. Darr,
Chapter 11 Trustee

696167

EXHIBIT A

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MASSACHUSETTS
CENTRAL DIVISION

In Re:	)	
	)	**Chapter 11**
TELEXFREE, LLC ,	)	**Case No. 14-40987-MSH**
TELEXFREE, INC.,	)	**Case No. 14-40988-MSH**
TELEXFREE FINANCIAL, INC.,	)	**Case No. 14-40989-MSH**
Debtors.	)	**Jointly Administered**

AFFIDAVIT OF STEPHEN B. DARR IN SUPPORT OF MOTION BY CHAPTER 11 TRUSTEE FOR ENTRY OF ORDER FINDING THAT DEBTORS ENGAGED IN PONZI AND PYRAMID SCHEME AND RELATED RELIEF

I, Stephen B. Darr, hereby submit the following affidavit in support of the *Motion by Chapter 11 Trustee for Entry of Order Finding that Debtors Engaged in Ponzi and Pyramid Scheme and Related Relief* (the "Ponzi Motion").

Introduction

1. I am the duly appointed Chapter 11 trustee (the "Trustee") in these cases, having been appointed by order of the Court dated June 6, 2014.

2. I am a Managing Director with the Business Advisory Practice of Huron Consulting Group. I have more than 35 years of experience providing accounting, auditing and financial consulting services to business organizations many of which are experiencing significant financial and operating difficulties. I am a Certified Public Accountant in Massachusetts and New Hampshire, a Certified Insolvency and Restructuring Advisor and hold certifications in both Financial Forensics and Distressed Business Valuation, as well as other professional qualifications.

3. The statements provided herein are based upon information and knowledge I have derived through my involvement in these Chapter 11 cases, as further set forth herein.

4. During the course of my investigative duties in these cases, my colleagues and I have examined the Debtors' books and records that were seized from the Debtors by federal authorities, electronic copies of which were provided to me, as well as documents produced by third parties in response to numerous motions for Federal Rule of Bankruptcy Procedure 2004 examinations. I and my professionals have conducted interviews of the Debtors' former employees and consultants, as well as professionals retained by the Debtors during the Chapter 11 cases. I have also reviewed the docket in these cases.

I. CASE BACKGROUND AND PROCEDURAL POSTURE

5. On April 13, 2014 (the "Petition Date"), each of TelexFree, Inc., TelexFree, LLC, and TelexFree Financial, Inc. (collectively, the "Debtors") filed voluntary petitions for relief under Chapter 11 of the United States Bankruptcy Code ("Bankruptcy Code") with the United States Bankruptcy Court for the District of Nevada ("the Nevada Bankruptcy Court").

6. The Debtors initially operated as debtors-in-possession pursuant to Sections 1107 and 1108 of the Bankruptcy Code.

7. On the Petition Date, the Debtors filed a motion for joint administration of the cases, with TelexFree, LLC designated as the lead case. By order dated April 24, 2014, the order for joint administration was approved.

8. Prior to the filings, the Commonwealth of Massachusetts, Office of Secretary of State, Securities Division ("MSD") commenced an investigation into the Debtors' business practices.

9. On or about April 15, 2014, the MSD commenced an administrative proceeding against the Debtors. Also on April 15, 2014, the Securities and Exchange Commission ("SEC") commenced an action against the Debtors and others in the United States District Court for the District of Massachusetts. The foregoing actions alleged, among other things, that the Debtors were engaged in an illegal Ponzi/pyramid scheme and the fraudulent and unregistered offering of securities. Substantially contemporaneously with the commencement of the SEC action, Homeland Securities Investigation ("HSI") seized the Debtors' assets, books, and records. In connection therewith, the federal government seized more than $107,000,000 in cash, including checks payable to the Debtors, their principals, or their affiliates. Federal authorities have also made forfeiture claims against approximately forty (40) other items of real and personal property standing in the name of the Debtors' principals and their affiliates, including automobiles, real properties, and notes secured by mortgages on real properties.

10. On or about April 22, 2014, the Office of the United States Trustee filed a motion for the appointment of a Chapter 11 Trustee based upon the allegations of illegal activity.

11. On April 23, 2014, the SEC filed a motion to transfer venue of the cases to the United States Bankruptcy Court for the District of Massachusetts (the "Court"). By order dated May 6, 2014, the motion to change venue was approved. The cases were transferred to the Court on May 9, 2014.

12. On May 30, 2014, this Court allowed the United States Trustee's motion to appoint a Chapter 11 trustee, and I was appointed on June 6, 2014.

13. The Debtors filed only a list of the alleged thirty (30) largest creditors in the cases and did not file schedules or statements of financial affairs, nor a matrix of creditors.

14. On February 27, 2015, I filed schedules of assets and liabilities and statements of financial affairs for each of the Debtors, using information obtained from documents produced pursuant to Rule 2004 examinations and Debtor records provided by the Federal Authorities (as defined below).

15. Carlos Wanzeler and James Merrill were the Debtors' principals along with Carlos Costa, at least through his alleged separation with the Debtors in the fall of 2013. Shortly after the Trustee was appointed, the United States Department of Justice ("DOJ" and, together with the SEC and HSI, the "Federal Authorities") indicted Wanzeler and Merrill based upon their involvement in the Debtors' scheme. Wanzeler has fled the country and, upon information and belief, is in Brazil. Merrill was initially detained and has been released pending trial.

16. On February 3, 2015, I submitted a comprehensive Status Report on outstanding matters in the cases. The Status Report set forth, among other things, the background of the Debtors and their affiliates, the breadth and scope of the scheme, assets recovered to date and potential additional sources of recovery, as well as efforts at coordination with governmental authorities, both in the United States and in Brazil.

17. Prior to my appointment, the Federal Authorities shut down, disconnected, and seized the Debtors' computer system, which consisted of forty-six (46) computers and servers containing more than twenty (20) terabytes of data. Accordingly, at the time of my appointment, I did not have access to any of the Debtors' records. Neither of the Debtors' principals has been available because Wanzeler fled the country and Merrill had been indicted and detained. I have had only had limited access to the Debtors' former employees.

18. Initially without access to the Debtors' books and records, I have utilized a variety of resources to acquire information regarding the Debtors' activities and the mechanics of their scheme.

19. I directed counsel to file motions for authority to obtain documents from, and conduct examinations of, twenty-nine (29) separate entities pursuant to Federal Rule of Bankruptcy Procedure 2004 (the "2004 Motions").[1] The deponents of the 2004 Motions included prepetition and postpetition professionals retained by the Debtors, financial institutions who had prepetition and/or postpetition relationships with the Debtors, multiple firms who provided payment processing services to facilitate payments between the Debtors and Participants, and firms who provided consulting services to the Debtors or who otherwise were believed to have had business relationships with the Debtors.

20. I have also conducted or supervised informal interviews of certain former employees and consultants of the Debtors as well as several Participants.

A. Mechanics of Scheme and Methods of Compensation

21. The Debtors purported to be in the business of selling a voice over internet service, or "VoIP" that cost $49.90 per month to conduct international phone calls. The sale of VoIP on a monthly basis is hereinafter referred to as a "VoIP Package". Customers who purchased the VoIP Package registered their phone numbers with the Debtors and received software that enabled their computers to place phone calls through the Debtors' computer servers in Marlborough, Massachusetts to approximately 40 countries.

22. The Debtors ostensibly used a multi-level marketing plan, or "MLMP", to sell the VoIP Packages.

[1] To date, I have deferred conducting depositions of the 2004 Motion deponents, as the focus has been on retrieving and examining documents and conducting informal interviews.

23. Until they purported to change their MLMP in March 2014, the Debtors provided Participants with two options to become members and to thereby open User Accounts:

a. "AdCentral Plan": $339 for a one-year contract ($50 membership fee plus $289 contract fee). This contract entitled the User Account holder with the right to sell ten VoIP Packages, as to which a Participant could receive a commission if the packages were sold, although there was no sale requirement. Participants were required to place one internet ad per day and, for each week in which the Participant placed the required ads, he/she was entitled to one additional VoIP Package, which could be sold or exchanged for $20 in credits with the Debtors. Thus, Participants who posted the required ads were eligible to receive $20 per week for 52 weeks, for a total return of $1,040 (a return of 207% on the investment of $339).

b. "AdCentral Family Plan": $1,425 for a one-year contract ($50 membership fee plus $1,375 contract fee). This contract entitled the User Account holder with the right to sell fifty VoIP Packages, as to which a Participant could receive a commission if the packages were sold, although there was no sale requirement. Participants were required to place five internet ads per day and, for each week in which the Participant placed the required ads, he/she was entitled to five additional VoIP Packages, which could be sold or exchanged for $100 in credits with the Debtors. Thus, the Participants who posted the required ads were eligible to receive $100 per week for 52 weeks, for a total return of $5,200 (a return of 265% on the investment of $1,425).

24. In addition to credits for posting these advertisements, the Debtors issued credits to Participants for the sale of membership plans and the establishment of new User Accounts as follows:

a. $20 in credits for each new Ad Central Plan and $100 in credits for each new AdCentral Family Plan in a Participant's network.

b. $20 in credits for each User Account in one's "network," up to a maximum of $440, as long as there were two subsidiary User Accounts.

c. 2% of all payments to each User Account within one's network, down to six "levels" of the network, provided that each User Account had a registered VoIP customer.

d. 2% of the Debtors' net monthly billing, up to a maximum of $39,600 in credits, for an AdCentral Family Plan that had ten new AdCentral Family

Plans in its network, so long as each plan had five registered VoIP customers.

25. The Debtors also issued credits to Participants for the sale of VoIP Packages as follows:

a. 90% (or $44.90 in credits) for the initial sale of a VoIP Package at $49.90.

b. 10% (or $4.99 in credits) per month for the renewal of a VOIP Package by a User Account holder directly in one's network[2] and 2% (or $0.99 in credits) per month for the renewal of a VOIP Package by a User Account holder indirectly in one's network, down to six levels of the network.

c. 2% from all VoIP Package sales in one's network, down to six levels of the network.

26. The credits issued to Participants for placing advertisements and selling membership plans and VoIP Packages could be redeemed for cash, transferred to another User Account, or applied in satisfaction of an invoice for another User Account.

27. Invoices for the purchase of a membership plan could be satisfied in one of two ways. Participants could pay the invoice in cash directly to the Debtors or Participants could pay a recruiting Participant for the purchase of a membership plan through the recruiting Participant's redemption of credits in an existing User Account.

28. In the case of a Participant satisfying his/her own invoice directly by payment in cash to the Debtors, the process worked, generally, as follows:

a. The Participant joined the Debtors' organization and created an online account with the assistance of a recruiting Participant, who needed to be identified;

b. The Debtors' database recorded the details entered by the new Participant and assigned an identification number to the new User Account;

c. The Debtors recorded the purchase, issued an invoice number, and marked the invoice as 'pending';

[2] In practice, the Debtors appear to have provided Participants with credits equal to ninety percent (90%) of the renewal fees.

d. A Participant could pay money directly to the Debtors in the form of cash, check, cashier's check, or wire transfer, or through a third-party online payment processing account. Once the Participant paid the invoice, the Debtors updated the invoice as 'paid', and the account setup would be complete;

e. The new Participant could then start building a pyramid underneath the newly created User Account by recruiting other Participants (or by purchasing new User Accounts themselves) and generating bonuses and commissions in accordance with the scheme.

29. Alternatively, as described below, a Participant could satisfy his/her own invoice directly by payment in cash to another Participant, who would satisfy the invoice by a redemption of accumulated credits. Thus, the new Participant's membership fee was paid directly to the recruiting Participant, rather than to the Debtors.

30. There are 10,987,617 User Accounts associated with the Debtors' MLMP. A new User Account was generally established each time that a membership plan was purchased, with either cash or accumulated credits.

31. Although some versions of Participant contracts contained prohibitions against Participants opening multiple User Accounts, other plan descriptions did not. In any case, any such restriction was not enforced and could not be enforced since the Debtors did not verify the Participants' identities. The Debtors' MLMP structure created incentives for Participants to open multiple User Accounts to generate commissions for themselves.

32. As noted above, a Participant could monetize accumulated credits by recruiting a new Participant to join the Debtors' scheme and using his/her accumulated credits to satisfy the invoice for the new Participant's membership plan in exchange for payment of the membership fee from the new Participant (a "Triangular Transaction"). In a Triangular Transaction, the Debtors issued the membership invoice to the recruited Participant, the recruited Participant paid

the membership invoice that was due to the Debtors instead to the recruiting Participant, and the Debtors redeemed the credits of the recruiting Participant in satisfaction of the invoice.

33. In a Triangular Transaction, the process generally worked in the same manner outlined above except that:

a. The new Participant paid the invoice amount to the recruiting Participant (in those cases where there were two separate Participants involved, that is, not an intra-Participant transaction) and forwarded the initial invoice to the recruiting Participant; and

b. The recruiting Participant, in turn, satisfied the initial invoice with accumulated credits in his/her existing User Account.

34. In fact, it was a regular practice of the Debtors' scheme for membership fees to be paid by the use of accumulated credits rather than by cash.

35. While invoices associated with the sale of membership plans or VoIP Packages had a face value of $3,073,471,326, only $359,792,242, or approximately twelve percent (11.7%) of that amount, was paid in cash to the Debtors. The balance of these invoices, totaling $2,713,679,084, was satisfied by the use of Participants' credits.

36. The Debtors also issued "manual credits" to certain User Accounts in some instances. Manual credits were credits issued to User Accounts unrelated to the purchase of a membership plan and not resulting from the placement of advertisements or other components of the compensation scheme. Although some manual credits may have been issued to User Accounts in exchange for cash payment to the Debtors, a significant amount of manual credits appear to have been issued to certain User Accounts without any payment to the Debtors. There also were exchanges of credits between User Accounts unassociated with the issuance and satisfaction of Debtor invoices.

B. SIG/Back Office

37. The Debtors maintained two computer applications for accessing and processing information from the Debtors' database relating to User Account activity, referred to as "SIG" and the "Back Office".[3]

38. SIG stands for Sistemas de Informacoes Gerenciais, which is Portuguese and translates roughly to "Information Management System." SIG tracked the activity for Participants by User Account, and the User Accounts are the only records available to confirm Participant activity.

39. Access to SIG was the culmination of a painstaking data recovery and analysis project implemented with the assistance of my professionals and investigators from HSI.

40. Following my appointment and beginning in August 2014, HSI provided copies of electronic information contained in the Debtors' computers and servers. Once all of the data from the Debtors' computers and servers were obtained, I and my team reassembled the system following a multiple step process.

41. The first step involved identification of a key server that appeared to contain much of the Debtors' 'big data'. Extensive testing was then performed to determine the appropriate configurations of the data and to restore the data in a virtual machine environment. Once the physical configuration of the hard drives was determined, the servers were 'virtualized', which was necessary because the Federal Authorities were in possession of the original servers. Additional servers were later identified that were necessary to operate the network. Once the key components of the system were identified and operating, passwords were obtained through research into document productions received, communications with Federal

[3] The Back Office was the program used by Participants to obtain information on their User Account activity.

Authorities, and a variety of investigative tools. Finally, an intensive analysis was performed to better understand the database structure, table relationships, data fields, and process flow.

42. Once access to a working version of SIG was obtained, I and my professionals were able to conduct search queries and sort data. Because SIG was complicated, written in more than one language, and poorly maintained, and system documentation was unavailable, substantial additional hurdles remained to achieving an understanding of the system and extracting usable data.

43. The Debtors' database was developed by programmers in Brazil and all field references are in Portuguese. System modifications appear to have been done in a haphazard and disorganized fashion. The Debtors' system is permeated with unreliable data because of limited efforts at data validation in establishing User Accounts.

44. Despite all of these obstacles, as a result of the forensic efforts identified above, I and my team have been able to reconstruct the Debtors' computer system in a virtual environment and obtain a working understanding of SIG and how it was used to track User Account activity.

45. Each time that a Participant purchased a membership plan or VoIP Package, an account was established with SIG (the "User Account").

46. Each User Account with the Debtors was registered with an electronic mail address ("Email Address"). There are approximately 900,000 unique Participant Email Addresses in SIG associated with 10,987,617 User Accounts. The number of User Accounts associated with an Email Address varies widely. A particular Email Address may be associated with a single User Account or may be associated with hundreds or thousands of User Accounts. Because each User Account may represent a separate Participant and some Participants entered

the scheme using the Email Address of another Participant, the number of Participants is unknown but is likely to be well in excess of 1,000,000.

47. After a User Account was established, SIG tracked the activity of the Participant in that User Account, including the accumulation of credits for bonuses and commissions 'earned', the use or transfer of credits between User Accounts, and payments made to or from the Participant directly with the Debtors.

48. SIG contains more than 100 tables of data. These tables include an Account Table (which contains a unique record for each User Account), an Invoice Table (which contains a unique record of each invoice generated by the Debtors), a Transfer Table (which contains information about each transfer of credits within the TelexFree system, including withdrawals of funds), and a Bonus Table (which contains information about each increase in credits into a User Account).

49. I and my advisors have taken a series of steps to confirm the accuracy and reliability of the transaction data reflected in SIG. My advisors interviewed the Debtors' bookkeeper, Andrea Cabral, to understand the mechanics of SIG and how it was employed on a day to day basis. Limited testing was performed to reconcile balances and activity using available data, including cross-referencing data in related transactions, conducting interviews with several Participants to confirm the accuracy of the SIG data as to their User Accounts, and reconciling payment data with third party processor records. Based on the testing performed to date, SIG provides accurate information regarding membership plan sales, issuance of invoices, accumulation and use of credits, and amounts received from and disbursed to the User Accounts.

C. Relationship with Ympactus, and Segregation of Ympactus Information and Debtor Information

50. In February 2012, Ympactus commenced operations in Brazil and reportedly operated a scheme substantially identical to the scheme that is described above. The Debtors commenced operations in April 2012. Ympactus initially grew much more rapidly than the Debtors, with growth accelerating in the fall of 2012 through the early summer of 2013. By the spring of 2013, Ympactus had cash receipts of more than $100,000,000 per month. *See Exhibit "1".* On the other hand, the Debtors' cash receipts were initially much more modest. In the spring of 2013, the Debtors' cash receipts averaged approximately $6,400,000 per month. *See Exhibit "1".*

51. On June 28, 2013, the Public Prosecutor's Office of the State of Acre, Brazil filed claims against Ympactus, Carlos Wanzeler, Lyvia Mara Campista Wanzeler, and James Merrill, alleging that the VoIP Packages marketed in Brazil were violating consumer rights, since the MLMP constituted a Ponzi/pyramid scheme. The Brazilian authorities suspended the operations of Ympactus and froze its assets in Brazil. Upon information and belief, the Brazilian authorities seized as much as $300,000,000 from Ympactus in connection with the shutdown, and civil and criminal proceedings are pending in Brazil. On or about September 21, 2015, the Brazilian court entered a decision finding that Ympactus operated a pyramid scheme.

52. Following the shutdown of Ympactus, the Debtors' cash receipts increased dramatically. The Debtors' cash receipts totaled approximately $198,500,000 in the last three full months of operation, with more than $96,600,000 in cash receipts in February 2014 alone. *See Exhibit "1".*

53. The SIG system maintained by the Debtors and Ympactus ran off a single database reflecting User Account activity for both operations. After reconstructing the computer

network and developing a working understanding of SIG, one of the first tasks was to determine how to segregate the Debtors' activity from that of Ympactus, since SIG did not clearly differentiate the User Accounts between the two.

54. SIG includes 17,016,780 distinct User Accounts associated with 2,166,955 Email Addresses for both the US-based and the Brazilian-based operations.

55. I believe that a valid basis exists to separate the Debtors' User Account data based upon the currency designation in the data fields.

56. The Debtors' system assigned a currency to be used to pay invoices based on the Participant's country of residence. Participants entering Brazil as their home address paid invoices denominated in Brazilian Reais ("Reais") and all others paid invoices denominated in United States Dollars, although for accounting purposes, all transactions in the database were recorded in United States Dollars. The Invoice Table distinguishes between invoices paid in United States Dollars and invoices converted to United States Dollars from Reais.

57. The Invoice Table contains a "cambio" or "exchange rate" field. In 99.7% of transactions, by amount, where the currency field is denominated as "D" or United States Dollars, the cambio field is populated with a "0". In 99.8% of the transactions where the currency field is denominated as "R" or Brazilian Reais, the cambio field is populated with a range of values from 1.98 to 2.37 (that is, 1.98 to 2.37 Reais for each 1 Dollar). I have confirmed that the two currencies traded in this conversion range during the time that the Debtors and Ympactus were simultaneously in operation.

58. Through a review of the currency field data, I have further determined the following:

a. Prior to the shutdown of Ympactus in June 2013, invoices in User Accounts with Brazilian contact information were denominated in Reais and invoices in User Accounts with non-Brazilian contact information were denominated in Dollars;

b. Fewer than 700 Reais-denominated User Accounts were associated with non-Brazilian addresses. Similarly, fewer than 150 Dollar-denominated User Accounts were associated with Brazilian addresses; and

c. There was relatively little activity after the shutdown of Ympactus for Reais-denominated User Accounts that were created prior to the shutdown, and all cash activity for Reais-denominated accounts ceased shortly after the shutdown.

59. Utilizing the currency designation, 10,987,617 User Accounts are associated with the Debtors' operations and 4,006,422 User Accounts are associated with Ympactus operations. The remaining User Accounts have no activity.

II. FINDING OF EXISTENCE OF PONZI AND PYRAMID SCHEME

60. Participants who purchased the AdCentral Plan became entitled to receive a VoIP Package each week by placing one internet advertisement per day. These VoIP Packages could be, and routinely were, converted into credits for $20 weekly for 52 weeks, for a 207% return on the initial investment of $339. Participants who purchased the more expensive AdCentral Family Plan were entitled to receive five additional VoIP Packages each week by placing five internet advertisements per day. These VoIP Packages could be, and routinely were, converted into credits for $100 weekly for 52 weeks, for a return of 265% on the initial investment of $1,425.

61. The repetitive posting of internet advertisements (which were reportedly supplied by the Debtors) served no legitimate purpose, because anyone who used "telexfree" as an internet search term would be led to the Debtors' own website, and the repetitive posting of similar advertisements had no discernable value. For example, one website, Adpost.com, contained more than 33,000 postings submitted by Participants for TelexFree, while another, ClassifiedsGiant.com, contained more than 25,000 postings

62. Participants did not draft the advertisements or perform any design services for their configuration, and the placing the ads could be, and often was, outsourced to third parties for a nominal fee. The requirement of posting advertisements to receive weekly payments obfuscated the true nature of the scheme – that the credits were a disguised, "guaranteed" return on the Participant's initial investment.

63. The guarantee of an astronomical return on the initial investment without the requirement to sell any product created perverse incentives for Participants. Participants opened multiple User Accounts for the sole purpose of leveraging their fictitious profits, without the need to sell any product or recruit any individuals. Some Participants appear to have invested a substantial portion of their life savings into the scheme seeking to quickly triple or quadruple their investment. Participants opened hundreds of User Accounts, ultimately resulting in an exponential rise in the number of User Accounts.

64. Participants who opened multiple User Accounts on their own behalf could generate credits by essentially recruiting themselves. Participants could receive (1) $20 worth of credits for recruitment of an AdCentral Plan member and $100 in credits for recruitment of an AdCentral Family Plan member, and (2) $20 in credits for each membership plan in one's downline, up to a maximum of $440 in credits, so long as that Participant recruited two new User

Accounts in his/her downline by either opening User Accounts in his/her own name or by recruiting new Participants.

65. While there were certain provisions of the Debtors' MLMP that ostensibly required the sale of VoIP Packages as a requirement for receiving credits, the credits that could be generated for those activities were relatively insignificant and the requirements were easily circumvented by Participants.[4]

66. The Debtors had $359,792,242 in actual cash sales during the two year operation of the scheme. Of this amount, approximately $353,000,000 was from the sale of membership plans and $6,600,000 was from the sale of VoIP Packages. Even more remarkably, seventy-seven percent (77%) of sales occurred in the six weeks before the filing in a belated attempt by the Debtors to fix their fatally flawed plan by ostensibly requiring the sale of VoIP Packages to receive bonuses and commissions in the future.

67. By and large, the few VoIP Packages that were sold were not used. Of the $6,600,000 in VoIP Package cash sales, less than one percent (1%) of available minutes contained in these packages were actually utilized, further demonstrating that the Debtors were not operating a bona fide MLMP and the VoIP Packages were not a legitimate product.[5] Approximately $477,888,000 in VoIP Packages were sold through the use of accumulated credits. Approximately eighty percent (80%) of these sales occurred in the six weeks leading up to the Petition Date in connection with implementation of the new compensation scheme.

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[4] While the generation of certain commissions required activation of VoIP Packages in a Participant's downline, this requirement was circumvented by the purchase of VoIP Packages with accumulated credits. Credits were also issued for the sale of standalone VoIP Packages but VoIP Packages were rarely sold to third parties.

[5] This estimate is based upon information contained in the Disk A Vantage database (which includes VoIP service for both the Debtors and Ympactus) for the period July 2012 through June 2013, as well as usage of only the Debtors' VoIP service for the period July 2013 to April 2014.

68. The total reliance on the sale of membership plans, as opposed to the sale of a legitimate product, made the collapse of the Debtors' scheme inevitable.

69. A calculation of the Debtors' twelve month trailing liability, that is, the amount due to Participants over the following year on account of the guaranteed return, further evidences the unsustainability of the scheme. This liability grew exponentially in the year prior to the Petition Date, eventually rising to more than $5,000,000,000 as of the Petition Date. Attached as *Exhibit "2"* hereto is a computation of the 12 month trailing liability as of the Petition Date. This trailing liability more than tripled in the five (5) months leading up to the Chapter 11 filings, far outpacing any cash generated from the sale of VoIP Packages.[6] The $5,000,000,000 trailing liability is more than seven hundred times the $6,600,000 in cash receipts from the sale of VoIP Packages since inception of the Debtors' MLMP. The sale of additional membership plans only deepened the insufficiency.

IV. THE DEBTORS ARE JOINTLY LIABLE FOR PARTICIPANT CLAIMS

70. The Debtors worked in concert with one another to develop, market, and operate their Ponzi and pyramid scheme. The Debtors had common ownership and each was controlled by Wanzeler and Merrill, as well as Carlos Costa at least through his alleged separation from the Debtors in the fall of 2013.

71. Each of the Debtors was intimately involved in the scheme. Common Cents Communications, Inc., which was owned and controlled by Wanzeler, Merrill, and Steven Labriola, changed its name to TelexFree, Inc. in early 2012 in conjunction with the marketing

[6] While certain provisions of Participant contracts did not require the payment to Participants for VoIP Packages issued to them, this contractual provision is completely undermined by the unmistakable statements in marketing materials and some of the Participant contracts promising Participants the right to a guaranteed return on investment without the need to sell any product.

and selling of VoIP Packages through the Debtors' MLMP. Shortly thereafter, in July 2012, TelexFree, LLC was formed, to conduct TelexFree's operations outside of Massachusetts.

72. TelexFree, Inc. and TelexFree, LLC worked collaboratively in furtherance of the scheme throughout 2012 and 2013, including joint marketing efforts, promotional materials, and Participant recruitment events. TelexFree, Inc. and TelexFree, LLC alternated responsibility for maintaining bank accounts, because on multiple occasions TelexFree was asked to close accounts with banks because of suspicious account activity.

73. After the seizure and shutdown of Ympactus by Brazilian authorities, TelexFree, LLC and TelexFree, Inc. saw a substantial increase in activity, which further exacerbated difficulties with banking facilities needed to conduct the TelexFree scheme. TelexFree Financial, Inc. was formed in Florida in December 2013 and opened bank accounts and paid expenses of TelexFree, Inc. and TelexFree, LLC. In late 2013, TelexFree, Inc. and TelexFree, LLC transferred more than $4,000,000 to an account at TelexFree Financial. TelexFree Financial deposited an additional $10,000,000 in membership fees and VoIP Package sales in February 2014. The only Debtor with employees was TelexFree, Inc. and these employees were being paid by TelexFree Financial.

74. TelexFree Financial rendered substantial assistance to TelexFree, LLC and TelexFree, Inc. in furtherance of the Ponzi and pyramid scheme.

75. The Debtors had a common design or agreement to establish and implement the Ponzi and pyramid scheme. The Debtors engaged in a common enterprise to further their plan.

I attest that, to the best of my knowledge, the foregoing is true and accurate.

Dated: October 7, 2015

Stephen B. Darr
Chapter 11 Trustee

695349

Affidavit of Stephen B. Darr in Support of Motion by Chapter 11 Trustee for Entry of Order Finding that Debtors Engaged in Ponzi and Pyramid Scheme and Related Relief

Exhibit 1

In re: TelexFree, LLC, *et al.*
Cash Receipts by Month - TelexFree and Ympactus

Month	TelexFree	Ympactus
February 2012	$ 150	$ 22,942
March 2012	1,884	84,503
April 2012	14,709	336,350
May 2012	43,983	1,847,443
June 2012	53,606	4,764,547
July 2012	84,986	8,948,617
August 2012	375,556	15,030,324
September 2012	768,207	34,346,283
October 2012	290,450	12,987,841
November 2012	693,672	34,128,986
December 2012	616,314	55,083,742
January 2013	1,764,966	143,425,971
February 2013	4,972,733	257,513,534
March 2013	3,800,994	121,512,314
April 2013	5,983,150	149,372,999
May 2013	9,467,356	284,144,633
June 2013	13,949,543	184,497,992
July 2013	12,180,176	-
August 2013	18,850,084	-
September 2013	9,279,178	-
October 2013	14,929,643	-
November 2013	27,738,566	-
December 2013	33,310,766	-
January 2014	48,483,827	-
February 2014	96,630,356	-
March 2014	53,385,849	-
April 2014	2,121,537	-
	$ 359,792,242	$ 1,308,049,021

Note: Determination of TelexFree vs. Ympactus based on Invoice Table data as described in Darr Affidavit.
Source: Debtors' Participant database.

Exhibit 2

In re: TelexFree, LLC, *et al.*

Trailing Liability Calculation - Advertising Bonus[1,2,3]

Trailing Liability	Outstanding ADCentral Payments	Outstanding ADCentral Family Payments	ADCentral Liability ($20 per week)	ADCentral Family Liability ($100 per Week)	Total Liability
February 2012	$ -	$ -	$ -	$ -	$ -
March 2012	-	-	-	-	-
April 2012	-	-	-	-	-
May 2012	-	102	-	10,200	10,200
June 2012	-	1,871	-	187,100	187,100
July 2012	-	2,881	-	288,100	288,100
August 2012	-	5,659	-	565,900	565,900
September 2012	1,237	5,735	24,740	573,500	598,240
October 2012	5,640	20,526	112,800	2,052,600	2,165,400
November 2012	9,989	39,832	199,780	3,983,200	4,182,980
December 2012	19,484	94,394	389,680	9,439,400	9,829,080
January 2013	31,697	182,875	633,940	18,287,500	18,921,440
February 2013	78,520	356,527	1,570,400	35,652,700	37,223,100
March 2013	164,655	506,542	3,293,100	50,654,200	53,947,300
April 2013	283,453	761,101	5,669,060	76,110,100	81,779,160
May 2013	494,359	1,261,216	9,887,180	126,121,600	136,008,780
June 2013	739,166	1,798,677	14,783,320	179,867,700	194,651,020
July 2013	1,096,143	2,411,703	21,922,860	241,170,300	263,093,160
August 2013	1,684,888	3,656,684	33,697,760	365,668,400	399,366,160
September 2013	2,559,676	5,852,955	51,193,520	585,295,500	636,489,020
October 2013	3,583,231	9,169,675	71,664,620	916,967,500	988,632,120
November 2013	4,826,215	13,775,043	96,524,300	1,377,504,300	1,474,028,600
December 2013	6,357,701	20,343,202	127,154,020	2,034,320,200	2,161,474,220
January 2014	8,284,248	31,105,685	165,684,960	3,110,568,500	3,276,253,460
February 2014	10,409,821	45,926,764	208,196,420	4,592,676,400	4,800,872,820
March 2014	10,611,602	50,826,455	212,232,040	5,082,645,500	5,294,877,540
April 13, 2014	10,021,920	48,251,878	200,438,400	4,825,187,800	5,025,626,200
April 2014	9,432,888	45,682,130	188,657,760	4,568,213,000	4,756,870,760

Notes

1. Trailing liability calculated as of the last day of each month based on the weekly Advertising Bonus as described in TelexFree Participant contracts
2. Includes purchases of AdCentral and AdCentral Family plans and excludes commission other than weekly Advertising Bonus
3. Assumes Participants purchasing AdCentral or AdCentral Family plans would place required advertisements and receive Advertising Bonus each week.

Source: Debtors' Participant database.