Docket #0048 Date Filed: 9/2/2016

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MASSACHUSETTS

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, AND MARIA MURDOCH, ANGELA BATISTA JIMENEZ, ELISANGELA OLIVEIRA AND DIOGO DE ARAUGO, AS PUTATIVE CLASS REPRESENTATIVES, Defendants.	Adversary Proceeding No. 15-04055

TRUSTEE'S STATEMENT OF UNDISPUTED MATERIAL FACTS
IN SUPPORT OF HIS CROSS-MOTION FOR SUMMARY JUDGMENT

Stephen B. Darr as Trustee ("Trustee") of the Chapter 11 Estates of TelexFree, LLC, TelexFree, Inc., and TelexFree Financial, Inc. ("TelexFree"), pursuant to Rule 7056 of the Rules of Bankruptcy Procedure, submits the following Statement of Undisputed Material Facts:

1. On November 25, 2015, the Court, on motion by the Trustee and after notice and hearing, entered an Order, as amended on December 21, 2015, determining TelexFree perpetrated a fraud upon the public, primarily targeting the immigrant community. TelexFree's

1440987160906000000000004

fraud was premised upon the sale of membership plans to individuals and incorporated elements of both a Ponzi and pyramid scheme. Docket No. 668, annexed hereto as Exhibit A.

2. The Ponzi aspect of the fraud involved the promise of astronomical returns to all Promoters who purchased a membership plan in TelexFree, merely for posting meaningless internet advertisements. By posting these advertisements, among other things, Promoters could "earn" credits with TelexFree that were redeemable for cash. The more membership plans that a Promoter acquired, the faster that Promoter could acquire credits. Each time a Promoter purchased a membership plan he/she was assigned a "User Account." Many Promoters had multiple User Accounts. Affidavit of Stephen B. Darr in Support of His Cross-Motion for Summary Judgment, ¶ 5 (hereinafter, "Darr ¶ ____"). See also Affidavit of Special Agent John S. Soares submitted in support of Search Warrant as annexed to Document 252 in Criminal Action 4:14-cv-40028-TSH and annexed hereto as Exhibit B ¶¶ 59-62 (hereinafter, "Soares ¶ ____").

3. The pyramid aspect of the fraud was the promise to compensate Promoters for recruiting individuals into the TelexFree scheme. Although TelexFree was structured as a multi-level marketing company, there was no need for Promoters to buy or sell the internet telephone product it offered. As with most pyramid schemes, the more individuals that one recruited, the more money that the recruiting Promoter could make. For example, for each new recruit, a Promoter would receive a "fast start" bonus, either of $20 or $100, depending upon the type of membership plan that the new Promoter purchased. Further, once a Promoter was recruited into another Promoter's pyramid, the recruiting Promoter would earn credits as each of his/her 'downline' recruits purchased memberships or became Promoters themselves by bringing in their own new recruits. TelexFree encouraged this "team building" activity by offering "team builder

bonus" compensation, which a Promoter could earn by, among other things, recruiting ten (10) additional Promoters into the scheme. Darr ¶ 6, Soares ¶ ¶ 59-62, and form of Contract annexed hereto as Exhibit C.

4. The pyramid aspects of the TelexFree fraud was prominently featured in TelexFree's website content, PowerPoint presentations, internet videos, and in-person recruitment meetings. All of these materials extolled the virtues of developing a Promoter's pyramid in order to maximize compensation. Darr ¶ 7 and Exhibits to Soares Affidavit.

5. A Promoter's activity in recruiting individuals into the scheme and accounting for the membership fees collected and credits redeemed by Promoters was detailed in the Debtors' books and records (hereinafter referred to as "SIG") and reported on TelexFree's financial statements. Darr ¶ 8.

6. One of the principal methods by which TelexFree encouraged and enabled the recruitment of new Promoters was by permitting existing Promoters to earn credits by recruiting individuals into the program and redeeming those credits, referred to by TelexFree as "commissions" or "agent commission," from the fees paid by new recruits. Darr ¶ 9.

7. Pursuant to this, an individual would purchase a membership plan from TelexFree through a Promoter. TelexFree would issue an invoice for the purchase of a membership plan being sold to that individual through a Promoter. The Promoter collected from the individual the amount of membership fee set forth on the invoice as agent for TelexFree. The Promoter could redeem his earned credits from the membership fee the Promoter collected from newly recruited individuals. The Triangular Transaction was reflected on SIG, the invoice marked satisfied, Promoter credits reduced, and the new recruit became a member of the TelexFree program and could begin recruiting others.

Darr ¶ 10.

8. The economic substance of the Triangular Transaction was, in fact, a payment of the membership fee to TelexFree and a payment by TelexFree to the Promoter in exchange for recruiting a new individual into the program. Darr ¶ 11.

9. The Triangular Transaction was the predominant method of entry into the TelexFree system. Invoices associated with the sale of membership plans or phone packages had a total value of $3,073,471,326. Of this amount, approximately $2,700,000, or nearly ninety percent (90%) of the membership fees sold by TelexFree were effected through a Triangular Transaction. Darr ¶ 12.

10. The membership fee paid by an individual to a Promoter was income to TelexFree and so characterized by TelexFree on its financial statements and tax returns. Darr ¶ 13.

11. Similarly, the credits redeemed by the Promoter from the collected memberships in a Triangular Transaction was an expense of TelexFree and characterized on TelexFree's financial records as such under the category of "Agent Commission." Darr ¶ 14.

12. TelexFree's Profit and Loss Statement for 2013 expressly separated TelexFree's revenue into 2 categories: (1) "payments through bank," which is a direct payment from the individual purchasing a membership program from TelexFree, and (2) "payments through system," which is a payment of a membership fee received by TelexFree through Triangular Transactions. Darr ¶ 15.

13. The Profit and Loss Statement for TelexFree for calendar year 2013 reflects $119 million in income "paid through bank", reflecting membership fees paid by individuals directly to TelexFree to join the program. Scheduled on the Profit and Loss Statement is an additional

$572 million in income "paid through system". That entry reflects membership fees collected by Promoter from individuals through a Triangular Transaction. Darr ¶ 16.

14. The Profit and Loss Statement separately identifies expenses attributable to Triangular Transactions as commissions paid to Promoters in Triangular Transactions. The Income Statement reflects an expense of $572 million for "Agent Commission – paid through system", representing payments received by Promoters as part of a Triangular Transaction. Darr ¶ 17, and Profit and Loss Statement Exhibit D.

15. The treatment on the Profit and Loss Statement appropriately reflects the economic substance of the Triangular Transactions. The membership fees collected by a Promoter were revenue of TelexFree, e.g., property of TelexFree, and the corresponding distribution to Promoters was treated as an expense, e.g., payment by TelexFree of an "agent's commission". Darr ¶ 18.

16. TelexFree issued Forms 1099 to Promoters in calendar year 2013 for income earned by Promoters from their involvement in TelexFree for that year. Darr ¶ 19.

17. The 1099 forms reported as income to Promoters both credits redeemed directly with TelexFree and income earned by Promoters for recruiting individuals into the scheme through Triangular Transactions. Darr ¶ 20.

18. The 1099 forms provide further evidence of the economic substance of the Triangular Transaction, money paid by TelexFree to Promoters for recruiting an individual into the scheme is treated as income to TelexFree, and the payment retention by the Promoters of those membership fees is treated as income to the Promoter and an expense of TelexFree. Darr ¶ 21.

19. The Ponzi Motion describes the mechanics of the TelexFree system, including the integral nature of the Triangular Transactions. See Docket No. 623, 623-1, Ponzi Motion and supporting Affidavit annexed as Exhibit D.

20. A central premise of the Ponzi Motion as filed and approved by the Court was that claims should not be limited to payments made by individuals directly to TelexFree to join the program but needed to include fee collected from individuals and cash paid to promoters as part of the Triangular Transactions. Darr ¶ 23 and Exhibit D.

21. The Order entered by the Court directed the use of the Net Equity formula for determining allowance of claims would include both aspects of the Triangular Transactions. This formulation for allowance of claims expressly provided that fees collected by Promoters from individuals would be deemed paid to TelexFree and the amount retained by a Promoter deemed a payment by TelexFree to the Promoter. Docket entry no. 687 Order annexed as Exhibit E, and Darr ¶ 24.

22. The Net Equity formula recognized that individuals recruited into the TelexFree program through a Triangular Transaction transferred money to TelexFree in exchange for the right to participate in the TelexFree program and the right to earn credits, thereby creating an obligation between TelexFree and that recruited individual which should be treated on the same basis as an individual who had paid the membership fee directly to TelexFree. Darr ¶ 25, and Exhibit E.

23. The "Net Losers" in the scheme would thereby be treated equally under the Net Equity determination regardless of how their investment was made. Darr ¶ 26, and Exhibit E.

24. Similarly, it was important that the claims of Promoters who recruited the individuals into the program and collected a "commission" for doing so should be reduced to

reflect amounts paid to, and retained by, them through Triangular Transactions in order to avoid a windfall. Darr ¶ 27.

25. The Ponzi Motion set forth the inequities that would result if Triangular Transactions were not included in the calculation of the amount of a Promoter's claim. Darr ¶ 28, and Exhibit D.

26. First, the individual recruited by the Promoter would be denied a claim for amounts paid to the Promoter to purchase a membership plan from the Debtors. Darr ¶ 29.

27. This would have created an inequitable result since a substantial portion of Net Losers would be denied compensation because they were recruited into the scheme through a Triangular Transaction as opposed to having been recruited directly by TelexFree. Darr ¶ 30.

28. Second, the Promoter who recruited the individual into the scheme would profit by having redeemed credits through retaining the recruited individual's membership fee without a corresponding reduction in the Promoter's claim amount to reflect this payment. Darr ¶ 31.

29. This inequity is rectified by including the Triangular Transactions in the calculation of Net Winners and Net Losers. Darr ¶ 32, and Exhibits D and E.

30. The approval of the Net Equity formula for determining claims in the case appropriately addresses the equities of the case by recognizing the economic realities of the Triangular Transaction. Darr ¶ 33, and Exhibit E.

31. The PIEC recognized the inherent fairness of the application of the Net Equity determination to include the Triangular Transactions and, therefore, did not object to the allowance of claims using the Net Equity determination. Rather, the Defendants reserved their rights to argue the inconsistent position that the fees paid by individuals recruited into the scheme through Triangular Transactions constituted a claim against the Debtors, but the

corresponding payment to a Promoter by TelexFree is not a transfer of property of the Debtors. *Opposition to Certain Aspects of the Relief Sought in the Motion by Chapter 11 Trustee for Entry of Order Finding that Debtors Engaged in Ponzi and Pyramid Scheme and Related Relief*, Docket No. 649; *see also excerpts of Transcript of Hearing before the United States District Court on the Trustee's Motion to Intervene*, annexed as Exhibit F.

32. The Trustee has commenced two class actions seeking to recover from Net Winners, under theories of both fraudulent transfer and preferential transfer, amounts they received through direct and Triangular Transactions in excess of amounts they contributed into the TelexFree program. Adversary Proceeding 16-4006 and Adversary Proceeding 16-4007, Darr ¶ 34.

33. The first class action adversary proceeding, Adv. Proc. No. 16-4006, was commenced against all Net Winners who are alleged to reside within the United States. There are approximately 14,818 Net Winners falling within this category. 105 participants have been named as individual Defendants and proposed class representatives in the domestic class action, who are believed to be Net Winners in the aggregate amount of approximately $109 million. A substantial portion of the $109 million is attributable to the Triangular Transactions. Complaint, Adversary Proceeding No. 16-4006, and Darr ¶ 35.

34. The second class action adversary proceeding, Adv. Proc. No. 16-4007, was commenced against all Net Winners who are alleged to reside outside of the United States. I estimate that there are 78,487 Net Winners falling within this category. I have named 96 participants as individual Defendants and proposed class representatives in the foreign class action, who are believed to be Net Winners in the aggregate amount of approximately $76

million. A substantial portion of the $76 million is attributable to the Triangular Transactions. Complaint, Adversary Proceeding No. 16-4007, and Darr ¶ 36.

35. In these Adversary Proceedings the Trustee seeks recoveries on behalf of all Net Losers, including those who lost money through direct transactions, Triangular Transactions, or any combination thereof. A predicate to the Trustee's pursuit of recoveries from Net Winners arising from Triangular Transactions is a finding that the membership fees paid to and retained by recruiting Promoters in Triangular Transactions comprised property of TelexFree. Darr ¶ 37.

36. When the economic substance of the Triangular Transactions is considered, the payments received by the Promoters in Triangular Transactions constitutes property of the TelexFree Estate and are recoverable by the Trustee as fraudulent transfers or preferential transfers. Darr ¶ 37.

37. Each of the Defendants named in this Adversary Proceeding were plaintiffs in actions pending before the United States District Court for the District of Massachusetts or United States District Court for the District of Arizona. Each represented in their pleadings that they were Net Losers. Each further represented they were representative of Net Losers who suffered losses as a result of Triangular Transactions. Second Amended Complaint (Docket No. 144) in Civil Action Nos. 14-MD-02566-TSH and Complaint in Civil Action No. 16-CV-40018-TSH, Darr ¶ 38.

38. An examination of the Defendants' activity reveals, however, that these representations are in some instances inaccurate. Darr ¶ 39.

39. In advancing these claims, the Defendants have also alleged at various times to have had no involvement or affiliation with the TelexFree operations. Darr ¶ 40.

40. A review of the facts, however, indicates that the Defendants have in each instance been intimately involved in the TelexFree scheme. Darr ¶ 41.

41. Maria Murdoch testified in Court at an evidentiary hearing in October 2015 that she had invested approximately $25,000 in the TelexFree scheme but that she had no contact with the Debtors, never became a member of TelexFree, and never received an invoice. Darr ¶ 42, Transcript of Ms. Murdock Testimony annexed hereto as Exhibit G.

42. The Debtors' books and records reflect, however, that Ms. Murdock maintained *seventy-five* (75) accounts ("User Accounts") with the Debtors, with each User Account representing the purchase of a plan. Darr ¶ 43.

43. In fact, all of the Defendants had multiple User Accounts with TelexFree as follows: Rita Dos Santos: 12; Angela Batista Jiminez: 55; Elisangela Oliveira: 3; Diogio De Araugo: 65; and Celio Da Silva: 142. Each of the Defendants had the opportunity to earn credits and to recruit other individuals into the scheme. Darr ¶ 44.

44. In the case of Dos Santos, not only did she open multiple User Accounts with TelexFree but she received $8,035.91 in payments directly from TelexFree. Darr ¶ 45.

45. The evidence of these payments directly contradicts representations made by the Defendants in the multi-district litigation that Dos Santos never received any money from TelexFree. *In re TelexFree Securities Litigation*, MDL No. 4:14-md-2566 (D. Mass.) (hereinafter, the "MDL Action"), Docket No. 253-1, ¶ 38, and Darr ¶ 46.

46. Indeed, some of the Defendants are actually Net Winners in the TelexFree scheme. The Debtors' records indicate that Da Silva was a Net Winner in the amount of $15,343 and Jiminez was a Net Winner in the amount of $347.80. Darr ¶ 47.

47. The Defendants have made attempts to bring class actions against Net Winners in Triangular Transactions on behalf of all Net Losers in Triangular Transactions and on each occasion, their efforts fail. Docket Entry 367 in the MDL Action annexed as Exhibit H, and *Elisangela Oliveira et al. v. TelexElectric LLLP et al.*, Case No. 4:16-cv-40018 (the "Oliveira Action"), Docket No. 6 annexed as Exhibit I.

48. The Defendants' attempts, on at least two occasions, to bring Unjust Enrichment Claims in District Court, on a class action basis, against Promoters who became Net Winners based upon the receipt of membership fees from other Promoters in Triangular Transactions, have appropriately been denied. MDL Action, Docket No. 367, Exhibit H; Oliveira Action, Docket No. 6, Exhibit I.

49. In one instance, the District Court denied the Defendants' motion to amend their Complaint to sue the Net Winners in Triangular Transactions as a class. Docket No. 367 in the MDL Action, Exhibit H.

50. In the second instance, the Defendants' action was stayed because it was found to be an improper attempt to circumvent the order in the first case. Oliveira Action, Docket No. 6, Exhibit I.

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

By his attorneys,

Dated: September 2, 2016

/s/ Andrew G. Lizotte

Harold B. Murphy (BBO #326610)
Charles R. Bennett, Jr. (BBO #037380)
Andrew G. Lizotte (BBO #559609)
Murphy & King, Professional Corporation
One Beacon Street
Boston, Massachusetts 02108
(617) 423-0400
CBennett@murphyking.com

714588

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MASSACHUSETTS

In re:	)	Chapter 11
	)	
	)	Case No. 14-40987
TELEXFREE LLC, et al.,[1]	)	
	)	Jointly Administered
Debtors.	)	
	)	
	)	

AMENDED ORDER ON MOTION BY CHAPTER 11 TRUSTEE FOR ENTRY OF ORDER FINDING THAT DEBTORS ENGAGED IN PONZI AND PYRAMID SCHEME AND RELATED RELIEF

A hearing (the "Hearing") having been held on November 24, 2015, on the *Motion by Chapter 11 Trustee* (the "Trustee") *for Entry of Order Finding That Debtors Engaged in Ponzi and Pyramid Scheme and Related Relief* [# 623] (the "Motion")[2] and it appearing that this Court has jurisdiction to consider the Motion pursuant to 28 U.S.C. §§ 157 and 1334; and it appearing that venue of these jointly administered chapter 11 cases and the Motion in this district is proper pursuant to 28 U.S.C. §§ 1408 and 1409; and it appearing that this matter is a core proceeding pursuant to 28 U.S.C. § 157(b); and the Court having considered the evidence admitted and arguments made at the Hearing, the Motion and the oppositions filed thereto; and the Court having entered a Proceeding Memorandum/ Order on the Motion on November 25, 2015 [# 654]; and the Plaintiffs Interim Executive Committee having filed a motion to alter or amend the November 25, 2015 Order; and the chapter 11 trustee having filed an opposition thereto; and the Court having considered the positions of the parties; and after due deliberation thereon; and good and sufficient

---

1 The debtors (the "Debtors") in these cases (collectively, the "Chapter 11 Cases") are TelexFree, LLC, TelexFree, Inc., and TelexFree Financial, Inc.

2 Capitalized terms used but not defined herein have the meaning ascribed to them in the Motion.

cause appearing therefor; it is hereby **ORDERED** that the Motion is **GRANTED** in part and **CONTINUED FOR FURTHER PROCEEDINGS** in part as follows:

1. This Order hereby amends, and, to the extent of any inconsistency, supersedes the November 25, 2015 Order.

2. All creditors and parties in interest, including Participants, received adequate notice and an opportunity to be heard as to prayers (i) and (iii) of the Motion, and prayer (iv) as it applies to prayers (i) and (iii).

3. The relief sought by the Trustee in prayers (i) and (iii) of the Motion did not require the commencement of an adversary proceeding pursuant to Fed. R. Bankr. P. 7001.

4. Each of the Debtors in these jointly administered cases operated a Ponzi and pyramid scheme. This ruling is the law of the case in each of the jointly administered cases.

5. The Debtors shall be jointly and severally liable for the claims of Participants (as defined in the Motion) in these Chapter 11 cases. This ruling is the law of the case in each of the jointly administered cases.

6. The entry of this Order does not constitute any finding, and the Court makes no finding whatsoever, as to prayer (ii) of the Motion (including as to whether all or any part of the relief sought by prayer (ii) of the Motion required the commencement of an adversary proceeding pursuant to Fed. R. Bankr. P. 7001), or as to prayer (iv) of the Motion insofar as prayer (iv) of the Motion requests a finding related to prayer (ii) of the Motion.

7. A further non-evidentiary hearing shall be held as to prayer (ii) of the Motion, and prayer (iv) of the Motion insofar as prayer (iv) of the Motion requests a finding related to prayer (ii) of the Motion, on **January 26, 2016** at **10:00 a.m. (Prevailing Eastern Time)**. Responses, including proposed orders, shall be filed no later than **January 19, 2016** at **4:30 p.m. (Prevailing**

Eastern Time). On or before **December 7, 2015**, the Trustee shall serve notice of such hearing and response deadline as well as a plain language explanation of the relief sought on the same parties and in the same manner as the Motion was previously served, and shall file a certificate of such service.

8. The Court shall retain jurisdiction to hear and determine all matters arising from or related to the construction, performance, enforcement and implementation of the terms of this Order.

Dated: December 21, 2015
Boston, Massachusetts

Hon. Melvin S. Hoffman
Chief United States Bankruptcy Judge

62251608 v4-WorksiteUS-032276/0001

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MASSACHUSETTS

In re:	) Chapter 11
	)
	) Case No. 14-40987
TELEXFREE LLC., et al.,[1]	)
	) Jointly Administered
Debtors.	)
	)
	)

MOTION OF THE PLAINTIFFS' INTERIM EXECUTIVE COMMITTEE TO AMEND OR ALTER ORDER

Lead Counsel and the Plaintiffs' Interim Executive Committee (together, the "PIEC") appointed by the United States District Court in this District as the representative of the victims of the Debtors' Ponzi scheme by orders entered in the multi-district litigation proceedings captioned *In re TelexFree Securities Litigation*, MDL No. 14-02566 (D. Mass) (the "MDL Proceeding"), hereby move (this "Motion") to amend or alter the Court's order [Dkt. No. 654] (the "Order") on the *Motion by Chapter 11 Trustee* (the "Trustee") *for Entry of Order Finding That Debtors Engaged in Ponzi and Pyramid Scheme and Related Relief* [Dkt. No. 623] (the "Ponzi Scheme Motion") in certain limited respects as described below to more precisely follow the rulings made in open court at the hearing on the Ponzi Scheme Motion and so as to avoid the risk of later misinterpretation. In support thereof and as grounds therefor, the PIEC respectfully states as follows:

BAGKGROUND

1. On October 7, 2015, the Trustee filed the Ponzi Scheme Motion seeking entry of an order:

[1] The debtors (the "Debtors") in these cases (collectively, the "Chapter 11 Cases") are TelexFree, LLC, TelexFree, Inc., and TelexFree Financial, Inc.

(i) finding that the Debtors operated a Ponzi and pyramid scheme;

(ii) ordering that any claim or portion of claim of participants in the TelexFree scheme based upon accumulated credits in the participants' user accounts as of the Petition Date shall be disallowed and that claims should be determined on a "Net Equity" basis;

(iii) ordering that the Debtors shall be jointly and severally liable for the claims of participants in the scheme; and

(iv) ordering that the findings made pursuant to the Ponzi Scheme Motion shall be applicable throughout these proceedings, for all purposes.

Thus, the fourth prayer for relief appears to relate to each of the previous three prayers.

2. On November 12, 2015, the PIEC filed the *Opposition to Certain Aspects of the Relief Sought in the Motion by Chapter 11 Trustee for Entry of Order Finding that Debtors Engaged in Ponzi and Pyramid Scheme and Related Relief* [Dkt. No. 649] (the "PIEC Opposition"), objecting to the Trustee's second and fourth prayers for relief on the grounds, *inter alia*, that the Ponzi Scheme Motion is deficient because it appears to seek, by motion, a determination of the validity of an interest in property and, to the extent that it does seek to determine an interest in property, there are no valid legal grounds for such a determination.

3. The Court held an evidentiary hearing on the Ponzi Scheme Motion on November 24, 2015 (the "Hearing"). The Court heard argument on the Trustee's first, third and fourth prayers for relief, including as to whether the Trustee's request for a determination that the Debtors operated a Ponzi/pyramid scheme (the first prayer for relief) properly should have been brought as an adversary proceeding. See, e.g., Tr. of Nov. 24, 2015 Hr'g at 34:15-35:3.[2] The Court did not hear argument on the Trustee's second prayer for relief, including the legal basis

[2] Relevant excerpts of the transcript of the November 24 hearing are attached hereto as **Exhibit 1**.

for such a determination and the question of whether that request properly should have been brought as an adversary proceeding.

4. At the end of the Hearing, the Court made certain findings as to the first, third and fourth prayers for relief. The Court also ruled that it was making no findings whatsoever either on (i) the Trustee's second prayer for relief, as pertains to the proposed "Net Equity" calculation of claims, or (ii) the Trustee's fourth prayer for relief, inasmuch as it requested that findings on the Trustee's second prayer for relief apply throughout the case, "for all purposes." See Tr. of Nov. 24, 2015 Hr'g at 121:17-122:15. The Court likewise ruled that it was making no findings on whether the Trustee's second prayer for relief should have been brought as an adversary proceeding. The Court instead took those matters under advisement pending a further hearing.

5. On November 25, 2015, the Court entered the Order. As most relevant here, the Order (i) states that "the relief sought by the trustee in [the Ponzi Scheme Motion] did not require the commencement of an adversary proceeding pursuant to FRBP 7001," and (ii) states, without reservation, that all parties in interests and participants in the TelexFree scheme received adequate notice of the Trustee's fourth prayer for relief.

RELIEF REQUESTED

6. The PIEC respectfully requests that the Court enter an amended Order, in the form attached hereto as **Exhibit 2**, to clarify and confirm its earlier oral rulings that the Court has made no findings whatsoever as to (i) the Trustee's second prayer for relief or (ii) the Trustee's fourth prayer for relief insofar as that prayer requests a finding related to the second prayer for relief.

ARGUMENT

7. Federal Rule Civil Procedure 59(e) ("FRCP 59(e)"), made applicable to this case by Federal Rule of Bankruptcy Procedure 9023, provides that a motion to amend or alter judgment may be brought within 14 days of entry of the judgment.

8. The trial court has broad discretion in determining whether to grant a motion to amend under FRCP 59(e). See ACA Fin. Guar. Corp. v. Advest, Inc., 512 F.3d 46, 55 (1st Cir. 2008) (stating that Rule 59(e) "does not state what grounds would justify [ ] alteration" and that trial courts therefore "enjoy considerable discretion in deciding Rule 59(e) motions"); Robinson v. Watts Detective Agency, Inc., 685 F.2d 729, 743 (1st Cir. 1982) ("[A] Rule 59(e) motion is addressed the discretion of the [trial] court.").

9. In two respects, the Order may be read to appear to extend the very specific rulings made at the Hearing in a way the PIEC respectfully believes the Court did not intend. First, the Order, after making certain findings related to the first and third prayer for relief, goes on to say that "the relief sought by the trustee in [the Ponzi Scheme Motion] did not require the commencement of an adversary proceeding pursuant to FRBP 7001." This language ("the relief sought") is subject to the interpretation that *none* of the relief requested required the commencement of an adversary proceeding. But the question of whether the Trustee's second prayer for relief is an attempt to determine the validity of an interest in property, and thus requires the Trustee to commence an adversary proceeding, was not reached at the Hearing. It is respectfully submitted, therefore, that the Order should be clarified on this point to address only those matters reached at the Hearing and not reserved for further argument: (specifically, whether the Trustee's first and third prayer for relief required the commencement of an adversary proceeding).

10. Second, by its terms, the Order says that adequate notice and an opportunity to be heard was given as to the fourth prayer for relief. Because the fourth prayer for relief refers back to the previous three, this part of the Order may be read to mean three separate things:

(i) that adequate notice was given of the Trustee's request that all findings regarding whether the Debtors operated a Ponzi and pyramid scheme apply "throughout these proceedings, for all purposes" (undisputed);

(ii) that adequate notice was given of the Trustee's request that any finding that the Debtors are be jointly and severally liable for the claims of participants in the scheme likewise apply "throughout these proceedings, for all purposes" (also undisputed); and

(iii) that adequate notice was given of the Trustee's request that all findings on the "Net Equity" calculation (and any other aspects of the second prayer for relief reserved for further hearing) apply "throughout these proceedings, for all purposes."

11. This third meaning is contrary to the Court's noting at the Hearing that it was making no findings whatsoever related to the Trustee's second prayer for relief or any matters reserved for further hearing, including as to whether adequate notice was given as to the Trustee's request that any findings on the second prayer apply "throughout these proceedings, for all purposes." (Indeed, the Court has ordered extensive re-noticing of the Trustee's second prayer for relief.) Accordingly, without clarification that the Order's finding on the fourth prayer for relief does not relate to, and has no effect on, the intersection of the fourth prayer and the second prayer (or any matters reserved for further hearing), the Order

could be subject to a reading that is overly broad and permit needless and wasteful later debate and confusion. It is respectfully submitted, therefore, that the Order should be altered or amended to more precisely confirm that the Court has expressed no opinion as to whether adequate notice was given of the Trustee's fourth prayer for relief, insofar as that prayer requested that all findings made pursuant to the Ponzi Scheme Motion's second prayer for relief apply throughout these proceedings.

[Remainder of this page intentionally left blank]

CONCLUSION

WHEREFORE, for the foregoing reasons, the PIEC respectfully requests that this Court (a) amend or alter the Order to reflect that it has made no findings (i) on the Motion's second prayer for relief, or (ii) on the Ponzi Scheme Motion's fourth prayer for relief, insofar as prayer four requests a finding related to prayer two, and (b) grant such other and further relief as this Court finds just and proper.

Dated: December 8, 2015
Boston, Massachusetts

BONSIGNORE, PLLC

/s/ Robert B. Bonsignore
Robert B. Bonsignore
NH Bar 21241
3771 Meadowcrest Drive
Las Vegas, Nevada 89121
Telephone: 781-856-7650
rbonsignore@classactions.us
Interim Lead Counsel

BROWN RUDNICK LLP

/s/ William R. Baldiga
William R. Baldiga (BBO #542125)
Kiersten A. Taylor (BBO #681906)
Jill C. Wexler (BBO #691811)
One Financial Center
Boston, MA 02111
Telephone: (617) 856-8200
Facsimile: (617) 856-8201
wbaldiga@brownrudnick.com
ktaylor@brownrudnick.com
jwexler@brownrudnick.com
For the Plaintiffs' Interim Executive Committee

62251676

EXHIBIT 1

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MASSACHUSETTS - WORCESTER

IN THE MATTER OF:	:	Case No. 14-40987 14-40988, 14-40989
TELEXFREE, LLC, TELEXFREE INC., and TELEXFREE	:	(Jointly Administered)
FINANCIAL, INC.,	:	Boston, Massachusetts **November 24, 2015**
Debtors.	:	2:05:52 p.m.

: :

TRANSCRIPT OF HEARING ON:
[#623] MOTION OF CHAPTER 11 TRUSTEE FOR
FOR ENTRY OF ORDER FINDING THAT DEBTORS
ENGAGED IN PONZI AND PYRAMID SCHEME AND
RELATED RELIEF AND [#625] MOTION OF CHAPTER 11
TRUSTEE TO SET BAR DATE; AND [#635] RESPONSE
OF PLAINTIFFS' INTERIM EXECUTIVE COMMITTEE
BEFORE THE HONORABLE MELVIN S. HOFFMAN, J.U.S.B.C.

APPEARANCES:

For the United States Trustee:	Office of the U. S. Trustee BY: LISA TINGUE, ESQ. 446 Main Street, 14th Floor Worcester, MA 01608
Audio Operator:	YVONNE WOODBURY, ECRO
Transcript prepared by:	JANICE RUSSELL TRANSCRIPTS 1418 Red Fox Circle Severance, CO 80550 (757) 422-9089 trussell31@tdsmail.com

Proceedings recorded by electronic sound recording; transcript produced by transcription service.

APPEARANCES (continued):

For Interim Lead Class Counsel and Plaintiffs' Interim Executive Committee:	Brown Rudnick LLP BY: KIERSTEN A. TAYLOR, ESQ. WILLIAM R. BALDIGA, ESQ. One Financial Center Boston, MA 02111
For Stephen Darr, Chapter 11 Trustee:	Murphy & King, P.C. BY: ANDREW G. LIZOTTE, ESQ. HAROLD B. MURPHY, ESQ. CHARLES BENNETT, JR., ESQ. One Beacon Street, 21st Floor Boston, MA 02108
For Carlos N. Wanzeler and James Merrill:	Partridge Snow & Hahn LLP BY: WILLIAM MOORMAN, JR., ESQ. 30 Federal Street Boston, MA 02110
ALSO PRESENT:	STEPHEN DARR Chapter 11 Trustee 265 Franklin Street Boston, MA 02210

other than in the claims allowance process.

THE COURT: Well, I ask you the same question I asked Mr. Baldiga. What is the principal reason why a court should restrict findings that it makes and rulings that it makes that are final the way you're requesting? Why would I do that?

MR. MOORMAN: Well, this was not an action brought against Mr. Wanzeler or Mr. Merrill. If the trustee desires some relief to be binding upon them, applicable to them in this area, it should have been done by adversary proceeding.

There are other issues such as whether or not it would be a core proceeding as it relates to seeking a finding that would be binding on them and as --

THE COURT: Well, not binding on them, specifically. They're not mentioned at all in any of this. Just binding for all purposes in this case and to the extent that they want to come into this case, why shouldn't they be bound with, with notice?

MR. MOORMAN: Only to them coming into this case, that's, that's one thing, but if -- what we're questioning is extending it beyond this case and to some other case.

THE COURT: How, how altogether do these individuals have standing in this case in any way? Can you explain that to me, please?

MR. MOORMAN: As to whether or not they have standing, Your Honor?

THE COURT: Yes.

MR. MOORMAN: It appears to us that the debtor is seeking to have a, a finding that is binding upon them. If he's seeking to do that, then I think they have standing to come in and oppose that type of a finding. I think it, it comes about from --

THE COURT: Well, you have -- I think you have -- you have the cart before the horse. He's seeking a finding that is for all purposes in this case. If -- if a -- if they don't want to be bound by that finding, they can stay out of the case.

MR. MOORMAN: In terms of coming in and filing a claim or something like that.

THE COURT: Right.

MR. MOORMAN: But they might be brought involuntarily into the case by way an adversary proceeding being filed against them. If that occurs, then they should be able to litigate this issue through a proper adversary proceeding.

THE COURT: And how was this, apart from -- I'm looking at 7001, which lists ten, ten different proceedings that are called adversary proceedings. I don't see this particular one here, or anything like it. But apart from the formalities, how is this any different than an adversary proceeding in terms of your clients? They had ample notice of this. They're here opposing it. What else do they need?

MR. MOORMAN: I think the formalities are important in terms of service of service, the applicable Rules of procedure. Judge, this was done in a very quick time frame.

THE COURT: When was your motion filed, Mr. Murphy?

MR. MURPHY: October 7th, Your Honor.

THE COURT: Yeah.

MR. MOORMAN: The, the other proceedings that they are subjected to are going to take months and months of trial.

THE COURT: Not here, not with me. You know, bankruptcy moves quickly.

MR. MOORMAN: Right, but they're not, they're not parties to this proceeding. We filed this as a protective measure, Your Honor, to the extent that the trustee seeks to have them bound in some other proceeding.

THE COURT: One of the things I think you, that came up in your opposition was a comment about needing to do discovery. Can you elaborate on that? What kind of discovery would your clients need here?

MR. MOORMAN: Your Honor, I'm not sure exactly what discovery they would want to engage in here.

THE COURT: Okay. Thank you.

MR. MOORMAN: I imagine it would be extensive discovery, though, that I'm not -- I'm here for the procedural mechanism of this proceeding, the fact this was done by motion, and the fact that I --

transmitted - she would have a claim in this bankruptcy case for that $25,000 under that determination. That, that would be part of it.

And that -- those -- if you will, payments into (indiscernible) would be included in part of their claim and it would not just include direct, but it would also include what we call the triangular transactions. I'll use, probably, a different term for purposes of explaining that to people.

Is that what you want me to explain in the notice, Your Honor?

THE COURT: Yes. Thank you.

MR. MURPHY: Thank you.

THE COURT: So now let's talk about the next hearing and how much time we need for this.

MR. BALDIGA: And, Your Honor --

THE COURT: Yes.

MR. BALDIGA: -- you've addressed the first three prayers for relief. Prayer 4, is that also to be argued further at that next hearing?

THE COURT: I -- I -- Prayer 4 is the -- I, I addressed that. That's -- I -- I -- I'm finding that the Ponzi scheme, pyramid scheme finding is the law of this case. That's Prayer 4.

MR. BALDIGA: And, and the Ponzi scheme finding, yes. And -- and -- I guess I should have been more specific.

If there is to then be a ruling on the triangular aspect of it, which is not the Ponzi scheme, the only thing that people really are fighting about today is whether a finding on the triangular aspect of the proof of claim form that you're reserving on, whether that because a law of the case for purposes other than the allowance of claims.

THE COURT: Oh, okay.

MR. BALDIGA: That is, I think, the entire core of the dispute here. And I just want to be sure that's not lost in the shuffle of today's proceedings.

THE COURT: What I've done today does not affect that one was or the other.

MR. BALDIGA: That's what I understood.

THE COURT: So you still have the opportunity to address that at the next hearing.

MR. BALDIGA: Very good. Thank you.

THE COURT: And lastly, Your Honor, have you determined that the credits, the disallowance of credits for claim purposes is, is okay for today?

THE COURT: Disallowance of credits.

MR. MURPHY: That was, I think, one of the --

THE COURT: That's --

MR. MURPHY: -- one of the prongs we had, that the credits that were in the --

THE COURT: No. That, that's part of Prayer 2. That

UNITED STATES BANKRUPTCY COURT, DISTRICT OF MASSACHUSETTS
Proceeding Memorandum/Order of Court

In Re: Telexfree, LLC **Case Number:** 14-40987 (MSH) **Ch:** 11

Evidentiary Hearing
#623 Motion of Chapter 11 Trustee for Entry of Order Finding that Debtors Engaged in Ponzi and Pyramid Scheme and Related Relief (H. Murphy)
#649 Opposition of Plaintiffs' Interim Executive Committee (W. Baldiga)
#650 Opposition of Carlos N. Wanzeler (W. Moorman)
#652 Reply of Chapter 11 Trustee

COURT ACTION:

Show Cause Order _____ Released _____ Enforced
_____ Granted _____ Approved _____ Moot
_____ Denied _____ Denied without prejudice
_____ Withdrawn in Open Court
_____ Sustained _____ Overruled
_____ Continued to_____
_____ Proposed Order Submitted by_____
_____ Stipulation to be Submitted by_____
_____ Taken Under Advisement

DECISION SET OUT MORE FULLY BY COURT AS FOLLOWS:

Evidentiary hearing held on November 24, 2015. For the reasons set forth on the record of the hearing I hereby find and order that:

1. Each of the debtors in these jointly administered cases operated a Ponzi and pyramid scheme. This ruling is the law of the case in each of the jointly administered cases.
2. The debtors are jointly and severally liable for the claims of the Participants (as that term is defined in the motion) in these cases.

In addition, I find that the relief sought by the trustee in this motion did not require the commencement of an adversary proceeding pursuant to FRBP 7001 and that in any event all creditors and parties in interest, including Participants, received adequate notice and an opportunity to be heard as to prayers (i), (iii) and (iv) of the motion. As to prayer (ii), a further hearing (non-evidentiary) will be held on January 26, 2016, at 10:00 a.m. (Boston time). Responses, including proposed orders, are due by January 19, 2016, at 4:30 p.m. (Boston time). On or before December 7, 2015, the trustee shall serve notice of the hearing and response deadline as well as a plain language explanation of the relief sought in prayer (ii) of the motion on the same parties and in the same manner as the motion was previously served and file a certificate of such service.

IT IS SO ORDERED:

Dated: 11/25/2015

Melvin S. Hoffman
United States Bankruptcy Judge

AFFIDAVIT OF JOHN S. SOARES IN SUPPORT OF SEARCH WARRANTS

I, Special Agent John S. Soares, being duly sworn, state:

Introduction

1. I am an investigative or law enforcement officer of the United States within the meaning of 18 U.S.C. § 2510(7), in that I am empowered by law to conduct investigations of, and to make arrests for, offenses enumerated in 18 U.S.C. § 2516.

2. I am a Special Agent with the United States Department of Homeland Security ("DHS"), Homeland Security Investigations ("HSI"). I have served in this capacity since May 2009. My current responsibilities include conducting federal criminal investigations, including investigations of financial fraud schemes, money laundering, and violations of the Bank Secrecy Act, and participating in operations to protect the United States from exploitation of legitimate trade, travel, and financial systems. I have received specialized training in investigating financial crimes, money laundering, and asset forfeiture. During my employment with HSI, I have been involved in the investigation of financial crimes, fraud schemes, money laundering, and in identifying and seizing criminally derived proceeds and property.

3. As an agent assigned to this matter, I have personally participated in many aspects of the investigation described below. I am also familiar with the facts and circumstances of the investigation through discussions with other HSI personnel and others, and from my review of business records, reports and other materials relating to the investigation.

4. I submit this affidavit for the limited purpose of supporting an application for a warrant, in part under 18 U.S.C. § 2703(a), and Rule 41 of the Federal Rules of Criminal Procedure, to search and seize records and data from the following locations:

a. An electronic storage facility maintained by Xand Corporation, also known as Access Northeast, located at 34 Saint Martin Drive, Marlborough, Massachusetts;

b. An electronic storage facility, maintained by Exigo Office, Inc., located at 8130 John W. Carpenter Freeway, Dallas, Texas;

c. The business headquarters of TelexFree, Inc., located at 225 Cedar Hill Street, Suite 118, Marlborough, Massachusetts.

5. The facts in this affidavit are drawn from my review of documents and data obtained during the investigation, my training and experience, and information obtained from other agents. This affidavit is only intended to show that there is sufficient probable cause for the requested warrants. It does not contain all facts relevant to this matter.

Descriptions of the Properties to be Searched

6. **Xand Corporation**: Based on open source information and information provided by James Merrill, the President of TelexFree, during sworn testimony before the Massachusetts Securities Division on March 25, 2014,[1] Xand Corporation, a/k/a Access Northeast, is a business that hosts data for other companies. According to Xand's website, its Massachusetts "data center," located at 34 Saint Martin Drive, Marlborough, Massachusetts, is one of six it maintains nationwide. According to Merrill's testimony, TelexFree maintains servers at Xand's Marlborough data center; TelexFree itself owns the servers, but they are held by Xand in its facility, where Xand can provide a secure environment and service the machines as needed.

[1] In March 2014, Carlos Wanzeler and James Merrill, who ran TelexFree, were deposed by the Massachusetts Securities Division as part of that agency's separate investigation of TelexFree. The Securities Division ("MSD") disclosed some of its investigative materials to federal authorities after the U.S. Attorney's Office for the District of Massachusetts made a formal request for access on March 31, 2014.

According to Merrill, TelexFree, at least as of the date of his testimony, had begun the process of "migrating" data from Xand to Exigo, a company based in Texas.

7. **Exigo Office, Inc**.: Based on open source information and Merrill's testimony to the MSD, Exigo is a company based in Dallas, Texas, at 8130 John W. Carpenter Freeway, that markets specifically to "multi-level marketing" businesses. "Multi-level marketing" is a term for businesses that market their products through a hierarchy of people who sign up to make money pursuing that activity, and who recruit others to do so. Certain businesses that purport to be legitimate multi-level marketing ("MLM") enterprises are in fact illegal pyramid schemes. On its web site, Exigo touts its MLM "business platform." In his MSD testimony, Merrill referred to Exigo as a "more friendly environment," confirmed that TelexFree has a contract with Exigo and, as above, said that TelexFree had begun "migrating" its data to Exigo. Based on Exigo's web site, it has only one location.

8. **TelexFree Headquarters**: According to TelexFree's public filings and Merrill's testimony, TelexFree's business headquarters are located at 225 Cedar Hill Street, Suite 118, Marlborough, Massachusetts. As more fully described in Attachment A, based on surveillance by federal agents, 225 Cedar Hill Street is a multi-unit, multi-story brick façade commercial property located on the east side of Cedar Hill Street in Marlborough, Massachusetts. The number "225" is plainly visible in grey lettering and "REGUS Fully Furnished Offices" is plainly visible in blue lettering on the façade of the building. The TelexFree offices are located on the first floor within the building; "TELEXFREE INC. Employee Entrance" in white and blue lettering, as well as the company logo, is plainly visible on the glass door to the office. According to Merrill's sworn testimony, TelexFree's business is run out of Suite 118 of the building, although the business "used to be upstairs in the Regus Suite, Suite 200." Merrill

explained that the initial space became too small for the company's operations, and that the new area "downstairs" at Suite 118 had about 4,500 square feet. Merrill described the new space as having about 12 "individual spaces" and five "executive offices," a conference room and a training area. The headquarters appears to employ about 30 people.[2]

9. With regard to the search warrants to be executed at Xand and Exigo above, I am informed that warrants issued under 18 U.S.C. § 2703 do not require an officer to be present for service or execution of the search warrant. *See* 18 U.S.C. § 2703(g).[3] If the Court issues the warrants,

a. As to Xand, because it appears that TelexFree itself owns the servers maintained at Xand's Marlborough location and that, therefore, those servers are discrete storage devices containing only TelexFree data, the government intends to have agents serve the warrant on Xand personnel and, at that time, take physical possession of TelexFree's servers.[4]

b. As to Exigo Office, Inc., to minimize the level of government intrusion, the United States does not intend to execute that warrant by entering Exigo's Dallas office location, but by serving a copy of the warrant on Exigo and awaiting production of the requested data.

---

[2] "[W]e were able to re-engineer some [of the 12] cubicles to fit 30 people in the same area that there is 12."

[3] Section 2703(g) says that "[n]otwithstanding § 3105 of this title*, the presence of an officer shall not be required for service or execution of a search warrant* issued in accordance with this chapter requiring disclosure by a provider of electronic communications service or remote computing service of the contents of communications or records or other information pertaining to a subscriber to or customer of such service." (Emphasis added.)

[4] The government seeks authorization for the search warrant on Xand pursuant to both Federal Rule of Criminal Procedure Rule 41 and 18 U.S.C. § 2703.

10. The rest of this affidavit is organized as follows: The first section below explains TelexFree's operations and why TelexFree is operating a pyramid scheme in violation of 18 U.S.C. §§ 1343 & 1349. The second section further discusses the nexus between the properties to be searched and TelexFree's illegal activities.

Allegations Pertaining to Probable Cause to Believe that TelexFree is a Pyramid Scheme

I. Overview

11. TelexFree, Inc., and TelexFree LLC (collectively, "TelexFree") ostensibly provide "voice-over-internet-protocol" ("VOIP") telephone services, for which customers can sign up via a web site maintained by TelexFree. Based on our investigation, however, TelexFree is actually a pyramid scheme.

12. Based on my training and experience, and generally speaking, a pyramid scheme involves a seemingly legitimate business that purports to sell a product but actually derives its revenue not from selling the product to third parties but from recruiting new participants to pay into the system. The hallmark of these schemes is a promise of substantial returns in a short period of time for doing little beyond paying into the organization and convincing others to do the same.

13. People operating pyramid schemes usually go to great lengths to layer the program with jargon, procedural complexities, a formalized hierarchy of participation, and other trappings that create the appearance of a legitimate company pursuing a (legal) multi-level marketing program. But, as in "Ponzi"-type schemes, the organizers simply take in money from newly-invested participants and use those funds to pay the returns promised to earlier participants.

14. Again like Ponzi schemes, pyramid schemes are ultimately unsustainable because the returns promised to an ever-growing number of participants must be paid using funds deposited by a necessarily finite pool of new participants. At some point the scheme must become too big, that is, it must run out of new participants depositing sufficient cash to cover commitments to earlier participants and, because the underlying product is not in fact profitable, most of the scheme's participants lose their money.

15. In this case, between about January 2012 and March 2014, TelexFree purported to aggressively market its VOIP service by recruiting thousands of "promoters" to post ads for the product on the internet. Each promoter was required to "buy in" to TelexFree at a certain price, after which they were compensated by TelexFree, under a convoluted compensation structure, on a weekly basis so long as they post ads for TelexFree's VOIP service on the internet. What TelexFree failed to disclose, however, was that it was not concerned with advertising the VOIP service; the ad-posting requirements were a meaningless exercise, in which promoters cut and paste ads into various classified ad sites provided by TelexFree and already saturated with ads posted by earlier participants.

16. Meanwhile, as TelexFree's bank records and "back office" business data attest, it derived a miniscule amount of revenue from sales of VOIP service – less than 1% of TelexFree's hundreds of millions of dollars in revenue over the last two years. The overwhelming majority of its revenue – the other roughly 99% – came from new people buying into the scheme. In fact, TelexFree was only able to pay the returns it had promised to its existing promoters by bringing in money from newly-recruited promoters.

17. On or about March 8, 2014, TelexFree announced changes to its compensation system that appear to have been prompted by an investigation by the Massachusetts Securities

Division. Based on a review of video clips on YouTube, Steven Labriola, who is a TelexFree senior executive, openly admitted to TelexFree promoters that the changes were necessary "to come into compliance." Soon after the changes were announced, promoters began protesting at TelexFree's Marlborough Massachusetts headquarters at 225 Cedar Hill Street, because the new system required them to actually sell TelexFree's VOIP product and, as one promoter told a news reporter, "It's almost impossible to sell."

18. On April 14, 2014, the TelexFree scheme collapsed: TelexFree and its related entities filed for voluntary Chapter 11 bankruptcy protection in the District of Nevada (No. 14-12524-ABL). In a declaration filed in the bankruptcy proceeding on behalf of the company, the company said, among other things, that it changed its compensation plan in March 2014 "[b]ecause questions were raised" about the prior plan. TelexFree also admitted that it was entering bankruptcy because, after changing the compensation plan, "These discretionary payments [that is, payouts to current investors] quickly became a substantial drain on the Company's liquidity." That is, once new investor dollars stopped coming in, TelexFree was unable to pay its current investors, a hallmark of collapsing Ponzi or pyramid schemes.

19. The day of the bankruptcy filing, TelexFree's web site, which all TelexFree promoters use to manage their accounts and transfer funds paid to them by TelexFree, became inoperative, with a screen posting by the company notifying its investors that the situation was temporary and that TelexFree looked forward to reorganizing and continuing to do business.

II. The Brazilian Investigation of TelexFree[5]

20. In June 2013, open-source query about TelexFree revealed that it was under investigation by law enforcement authorities in Brazil, where TelexFree was originally based. Documents provided by Brazilian law enforcement authorities showed that they had concluded that TelexFree was a pyramid scheme, operating with the same modus operandi later used in the United States (that is, that the company ostensibly provided VOIP services, but in fact derived revenue principally from new promoter buy-in fees). The Brazilians also determined that Carlos Wanzeler, James Merrill, and Carlos Costa were connected to the Brazilian entity. For example, in 2010, Wanzeler registered a company in Brazil named "Ympactus," which began doing business as TelexFree in 2012.

21. The Brazilian investigation resulted in the Brazilian government suing TelexFree in June 2013, including seeking an injunction prohibiting TelexFree from recruiting new promoters and from taking in funds or paying money to existing TelexFree promoters. As of the date of this affidavit, the Brazilian injunction is still in effect. Also, according to sworn testimony provided by Carlos Wanzeler to the MSD, the Brazilian government has also frozen about $350,000,000 in funds that apparently belongs to TelexFree.

22. Records from the Brazilian Ministry of the Treasury showed that, since TelexFree began recruiting promoters in Brazil in 2012, TelexFree bank accounts in Brazil had received about $446,000,000 in U.S. dollars. The records also noted that on February 19, 2013, TelexFree's Brazilian bank balances totaled over $200,000,000. The Brazilian Ministry of Treasury materials also showed that transfers were made from TelexFree bank accounts to

[5] At this point, TelexFree has been investigated and prohibited from operating in several countries, including Rwanda, the Dominican Republic, and the British Crown Dependencies of Jersey and Guernsey.

Brazilian bank accounts belonging to Wanzeler, and from there to U.S. accounts in Wanzeler's name. Wanzeler's transfers to U.S. accounts totaled about $3,500,000.

23. As discussed further below, a review of filings by U.S. banks for TelexFree's banking activity in 2012 – 2013 showed a pattern similar to the activity uncovered in Brazil: significant sums deposited to TelexFree accounts, generally in small amounts, which were rapidly disbursed, again in small amounts. Meanwhile, little of the money appeared to be derived from selling a product to third parties.

III. TelexFree's Corporate Structure in the United States and Its Relationship with Other Entities

24. According to incorporation paperwork on file with the State of Massachusetts and other states, Carlos Wanzeler and James Merrill own and operate a U.S. company called TelexFree, Incorporated, and related entities.

25. Through a query on the Commonwealth of Massachusetts, Secretary of State's website I learned that TelexFree was originally known as "Common Cents Communications." Common Cents Communications was incorporated in Massachusetts in December 2002 and listed Carlos Wanzeler as President and James Merrill as Treasurer. In February 2012, Common Cents Communications filed an article of amendment with the Massachusetts Secretary of State, changing the name of the corporation to "TelexFree, Inc." The article of amendment was filed by Carlos Wanzeler in his capacity as President. In October 2012, TelexFree, Inc., filed an annual report with the Massachusetts Secretary of State, in which Wanzeler and Merrill were listed as the sole officers and directors of the company. The incorporation documents for TelexFree list a corporate address of 225 Cedar Hill Street, Suite 200, Marlborough, Massachusetts.

26. In July 2012, another entity named "TelexFree" was registered as a limited liability company ("LLC") in the State of Nevada. The company listed Carlos Wanzeler, James Merrill, and another man as officers of the LLC. In April 2013, TelexFree LLC filed an application for registration as a foreign limited liability company with the Massachusetts Secretary of State. With that application, James Merrill filed a letter of consent for TelexFree LLC to use the name "TelexFree" in Massachusetts, and signed it in his capacity as President of TelexFree, Inc. (it is not clear when Merrill replaced Wanzeler as President, if that in fact occurred).

27. In testimony before the MSD in March 2014, both men confirmed their leadership positions at TelexFree and that each of them owns 50% of the company.

28. It appears that TelexFree is also intertwined with other entities, as summarized below. The government seeks authorization to review materials pertain to these additional entities, because they may in fact contain evidence related to the activities of TelexFree, Wanzeler, Merrill, and/or other co-conspirators.

29. On October 10, 2007, Brazilian Help, Inc., was registered as a corporation in Massachusetts. Wanzeler is listed as the president, treasurer, secretary, and director of that entity, and its principal office is 225 Cedar Hill Street, Suite 200, Marlborough, MA 01742 – the same as that listed for TelexFree.

30. On March 26, 2014, in sworn testimony before the MSD, Wanzeler described the relationship among several entities, including Brazilian Help, TelexFree, Inc., and TelexFree LLC, and others called Diskavontade, Ympactus, and TelexFree Financial. Wanzeler testified that in or about 2002 he formed Brazilian Help, Inc., which does business under the name Diskavontade. Wanzeler is the president and owner of Diskavontade, and both Wanzeler and

Merrill receive profits from Brazilian Help, Inc./Diskavontade. According to Wanzeler, Brazilian Help, Inc./Diskavontade provided VOIP service and used a compensation structure that encouraged company promoters to recruit both customers and new promoters. Wanzeler then described the relationship between TelexFree and Diskavontade as "the same company for me." In an additional entanglement, on or about December 2007, Brazilian Help, Inc., entered a contract with iBasis, a carrier of international voice traffic, for VOIP services. At some point between 2007 and August 2013, the contract was modified to substitute TelexFree for Brazilian Help.

31. During his testimony, Wanzeler also discussed "Ympactus," which he described as the Brazilian incarnation of TelexFree; both companies shared the web site www.telexfree.com. Wanzeler described Ympactus as using the TelexFree brand name in Brazil.

32. When asked to describe the TelexFree corporate structure, Wanzeler stated, "Yeah, we have a TelexFree LLC in Nevada and we have a TelexFree Inc. and we have a TelexFree International we never use 'cuz everything comes to LLC and the Inc. and we have Ympactus in Brazil, that's construction." Wanzeler went on to state the he has an ownership interest in each entity and that the only other individuals with an ownership interest in them are Merrill and another man.

33. The relationships among TelexFree, LLC; TelexFree, Inc.; and TelexFree Financial are equally interwoven. Wanzeler testified that TelexFree Financial was created to pay the employees of TelexFree LLC and TelexFree, Inc., because they "have so many problems with the bank." Wanzeler testified, "We open company called TelexFree Financial just to pay our bills." Wanzeler went on to say that, "TelexFree Financial was opened not too long ago,

okay, TelexFree Financial is open because the problem we have in the banks and if all our bank shut down by TelexFree we need some bank; you know, we try get some place we can pay our employees, pay our debt, you know, and that's what TelexFree – TelexFree Financial will just let you guys know that it's another TelexFree company."

IV. TelexFree's U.S.-Based Business Operations

34. TelexFree maintains a website, www.telexfree.com. An internet registry search showed that the name was registered by Diskavontade, a company operated by Wanzeler. Again based on open-source domain name registries, in 2008 Wanzeler registered the domain name www.diskavontade.com and, based on his testimony before the MSD, he is the president and owner of that entity.

35. As further discussed below, TelexFree's VOIP product, usually called 99TelexFree, could be bought directly through the TelexFree site or the websites TelexFree provides to its promoters. A few factors, however, distinguish TelexFree and its product from the operations of a legitimate company:

a. The product, however, appears poorly designed for actually securing and keeping customers.

b. The way TelexFree compensated those who signed up to "promote" the VOIP product had little or nothing to do with actually *selling* the VOIP product, and the compensation system was not based on a sustainable business model.

c. An analysis of the bank and credit card processing accounts behind TelexFree's publicly-stated income and revenue figures shows that TelexFree was deriving less than 1% of its revenue from its VOIP products, about 99% from investments by new promoters, and that it could not meet its massive payment

obligations to existing promoters without equally large infusions of cash from new promoters.

d. TelexFree's public statements, including statements and instructions to its promoters, consistently omitted the fact that TelexFree's survival, and so promoters' profits, depended on a constant influx of new promoters, and not on selling the VOIP product.

36. These facets of TelexFree's operations, which were typical of pyramid schemes, are discussed below.

A. <u>The Product TelexFree Purports to Sell</u>

37. The 99TelexFree product allows the user to make Internet-based long distance calls to foreign countries. It is downloaded by the purchaser and installed on a computer (or, more recently, on a smartphone), after which the purchaser registers his phone number with TelexFree. The purchaser can then call a local access number from the registered phone number. When the TelexFree system recognizes a call by a registered phone number, the purchaser is alerted by a new dial tone and can then complete an international call.

38. The process for buying TelexFree's VOIP service is exceptionally cumbersome, and not indicative of a genuinely competitive product, that is, of a product that a genuine retail customer would prefer over readily available competing services. On April 9, 2014, an HSI agent acting in an undercover capacity ("UC2"),[6] bought a TelexFree VOIP package from www.telexfree.com. The initial steps in the process took over two hours.

39. UC2 was first required to provide his/her name, date of birth, Social Security number, cellular telephone number, email address, and mailing/billing address, and to create a

[6] The activities of the initial undercover agent working on this investigation are discussed below.

log-in name and password. He/She then entered a telephone "number of origin," so TelexFree could determine which local access numbers the new customer should use.

40. The TelexFree site then created an invoice for $49.90 for the VOIP purchase. But to pay that invoice, the site required UC2 to create an "eWallet," and to follow the same process summarized above – entering extensive personal information and generating a log-in name and password. The site then required UC2 to validate his/her credit card by scanning and uploading to the TelexFree site a copy of his/her driver's license and credit card, and to complete a credit card authorization form and a "pre-authorization validation" in which TelexFree tested the credit card by making "a small random temporary charge on your credit card account." A disclaimer during the validation process warned that UC2 should "please allow 1 to 2 business days to process your document."[7]

41. Beyond credit card sales, it appears that a customer could buy the VOIP service by paying the $49.90 monthly fee to a promoter, after which TelexFree subtracts that amount from what TelexFree owes the promoter in "buy back" fees or commissions (discussed below). It is unlikely, however, that significant retail sales of 99TelexFree to genuine third party customers are accomplished in this manner. First, the site itself allows for the use of a credit card for payment, an especially likely option in scenarios, like this one, where automatic monthly payments are needed. Second, paying via a promoter – instead of simply paying the site itself – implies a level of familiarity and trust between the promoter and the new customer, that is, that the promoter knows the customer, who apparently is willing to give the promoter $49.90 a month. Anyone paying for the VOIP product in that manner – even assuming they actually use

[7] Signing up for competing sites providing similar services, like Skype, takes a matter of minutes.

the product instead of simply buying it to satisfy TelexFree eligibility requirements – is most likely a newly-recruited promoter.

B. The Compensation Structure – Making Money Without Selling Anything

42. The TelexFree site, www.telexfree.com, explains how TelexFree compensates participants. TelexFree instructional videos, available on YouTube and perhaps other sources, also describe the numerous ways TelexFree pays its promoters. From approximately March 2012 to September 2012, the TelexFree site contained a "promoters" link that told potential promoters that they could, "Earn money doing announcements on Internet!" That is, the site told potential investors that, after an initial investment in the company, they could make money for a year without selling any of TelexFree's VOIP services, but simply by posting ads for the product. For example, in the summer of 2012 the website said, in part, the following:

> Be our promoter
> Earn money doing announcements on Internet!
> Through a ADCENTRAL, that you geot [sic] for the amount of US$299 (annually).
>
> The promoter will receive US$20 each week that makes 7 different announcements in websites of free announcements online, from Monday to Sunday. All in a way fast, easy, and standardized in your virtual office (BO) Telexfree.
>
> This will be for the 52 weeks of the year, of your contract, then see the simulation:
>
> 52 weeks x $20 (Putting the 7 announcements) = $ 1,040 in the year

43. The TelexFree site also contained a link, next to a photograph of James Merrill, that read, "See our opportunity presented by our President James Merrill." This link connected to a downloadable PowerPoint presentation. The presentation encouraged people to sign up as promoters and "*Earn money the smart way! Without having to invite anyone, without selling*

anything in the comfort of your own home." (Emphasis added.) It went on to explain that by placing one advertisement for TelexFree a day a promoter could earn $20 per week, $80 per month, $1,040 per year, and $741 in net profit per year. The presentation encouraged potential promoters to join under an "AdCentral Family Plan" (explained further below). This plan required an initial $1,375 payment, after which the promoter must publish five advertisements per day, every day. A promoter who published five ads each day would receive $100 per week, $400 per month, $5,200 per year, and a net profit of $3,825.

44. During his sworn testimony before the MSD, Merrill confirmed that, beyond the PowerPoint presentation being available on TelexFree's site, promoters used the presentation themselves to show others how to make money with TelexFree.

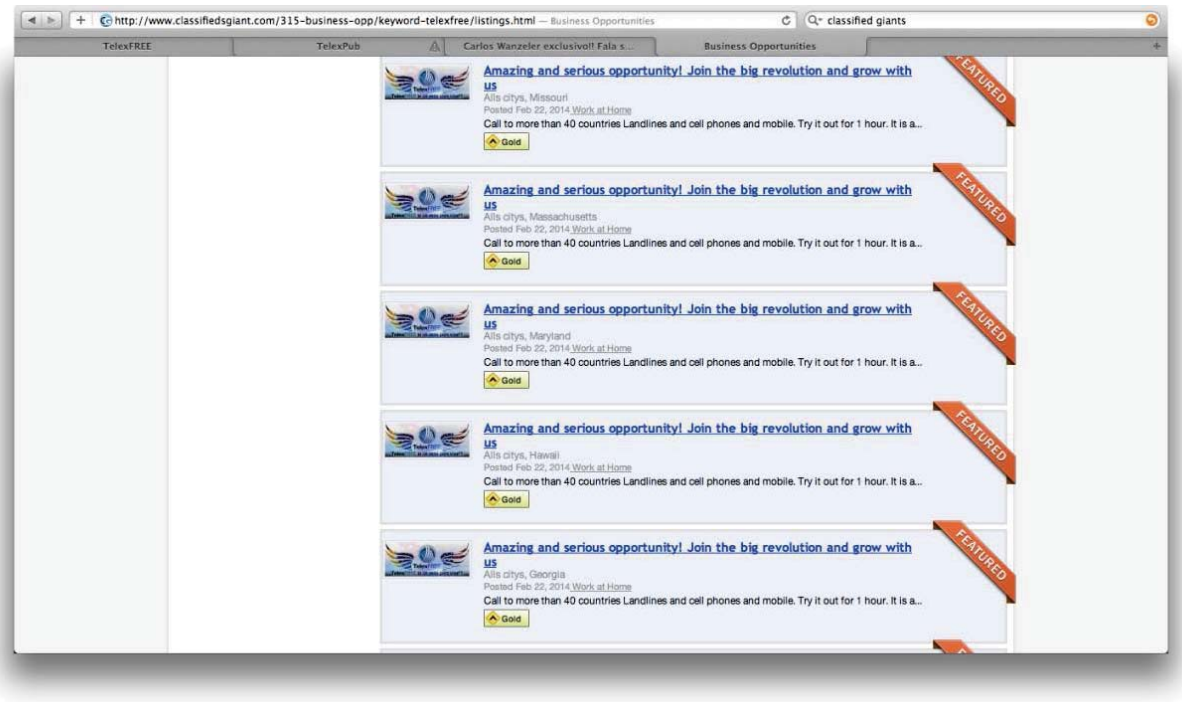
45. An analysis of the TelexFree site, made while the original compensation system was operating (about January 2012 to March 2014), showed that when a promoter joined TelexFree he was required to have a user name to access the "back office" area of the site. This was the area from which TelexFree promoters managed their sales activities. Once a promoter accessed the "back office," he was able to copy advertisements already prepared by TelexFree, after which the promoter pasted those pre-made ads into various other websites that allowed free "classified" advertising. TelexFree provided the links to those sites; the promoter could post the ads to whichever of these sites he chose.

46. After posting an ad, the promoter submitted a link to the advertisement's internet protocol ("IP") address to TelexFree, which then verified that the ad was placed. If a retail customer then decided to make a purchase of the 99TelexFree product from that IP address (that is, linking through that ad), TelexFree would have a record of which promoter posted the ad.

47. For purposes of illustration, if someone bought into TelexFree and selected the user name "Bambi," when a retail customer tried to buy the 99TelexFree VOIP product from an ad placed by "Bambi," the purchase would link the retail buyer to www.telexfree.com/Bambi. The promoter would then be notified in the back office that somebody had purchased a VOIP product or signed up as a promoter through his or her website, and the promoter would receive credit for that sale.

48. I and other agents, on multiple dates, have reviewed the sites to which TelexFree directed its promoters to posted advertisements.[8] An understanding of this ad-placing activity is important to understanding the fundamentally fraudulent nature of TelexFree as a business. These sites, each of which allowed people to post small ads for free, bear hundreds of ads for TelexFree, all of which are essentially identical. A "screen shot" of a typical site, retrieved by HSI personnel investigating this matter, appears below:

[8] The sites include www.epage.com, www.zamzata.com, www.snnap.com, www.zikbay.com, www.classifiedgiant.com, www.citynews.com, www.adpost.com, www.freeclassifieds.com, www.wantedwants.com, and www.freeadsplanet.com. In November 2013, TelexFree began referring its promoters to a site called www.telexpub.com. A review of publicly-available site registry information shows that whoever registered that site chose to make their participation anonymous by using the service Domains by Proxy which, for a fee, substitutes itself as the named registrant. As of this date, we have not yet received additional information about the true registrant for the site.



Posting ads to sites like these, which already bear hundreds of nearly identical ads, in reality could have done nothing to promote TelexFree's VOIP product. Moreover, promoters were *prohibited* from posting TelexFree ads on any site besides the ones provided by TelexFree. Finally, according Merrill's sworn testimony before the MSD, no promoter ever even asked the company for permission to do so. During the investigation, investigating agents have not found TelexFree advertising in other venues in which competing services, or Internet-businesses generally, advertise, which further indicates that actual advertising and product sales were not TelexFree's primary concern.

49. The sum of these factors is that TelexFree's ad-posting appears to have been busywork, designed to disguise what TelexFree was really offering its hundreds of thousands of promoters: a guaranteed return on an initial investment, financed by funds from later investors, for doing essentially nothing. Cutting and pasting ads from TelexFree's site to one of the above

sites which, even if performed five times a day took about two minutes to accomplish, was intended to mask this dynamic.

C. The Compensation Structure – Individual Earnings

50. Overall, between in or about January 2012 and early March 2014, TelexFree's compensation structure appeared needlessly opaque and, like the ad-posting exercises described above, had no obvious business rationale. Based on my training and experience, these are typical aspects of pyramid schemes.

51. Between about January 2012 and March 2014, a person bought into the company using cash, credit card, Internet-based payment processor (like PayPal), cashier's check, or money order, and could make the payment directly to TelexFree, or to a promoter who recruited the new participant. As discussed below, there were three buy-in levels available and, after buying into the company, a new participant could be compensated as an individual, or as part of a "team," earning additional money by recruiting new promoters. As to the buy-in levels, the greater the investment by the promoter, the higher the return.

52. The information below is based on a review of the TelexFree site, YouTube postings by TelexFree personnel and various promoters; and conversations between an HSI undercover agent and a successful TelexFree promoter (discussed further below).

1. *The Initial $50 Buy-In for All Members*

53. All new promoters were required to first pay a $50 membership fee. After paying the fee, TelexFree would set up a new "back office" site for that user. After paying this fee, the user then had the option of buying two different "AdCentral" packages, priced at $289 and $1,375.

2. *The $289 Buy-In Level (Ad Central)*

54. At the $289 buy-in level,[9] however, the promoter was compensated *regardless* of whether there were any retail sales of the VOIP product. The company called this plan "Ad Central." As with the $50 buy-in, TelexFree provided ads and free websites on which to post the ads. In the event of a retail sale based on one of those ads, the promoter received a 90% commission, that is, $44.99 out of the $49.99 the retail customer paid for the first month of TelexFree's VOIP service. As in the $50 buy-in, if that retail customer renewed on a monthly basis, that Ad Central promoter earned an additional 10% commission each time.

55. In the Ad Central plan, the company provided the promoter a "stock" of ten VOIP products to sell that week, and then each week thereafter for 52 weeks. But there was no physical product – for example, no CD or DVD containing the 99TelexFree product, or a software key for downloading it. There was only an entry in the TelexFree virtual "back office" listing the stock "available" to the Ad Central promoter. Moreover, if an Ad Central promoter posted ads for seven consecutive days, the company agreed to "buy back" any unsold stock from the promoter for $20, and to continue to do so every week for a year. This was even though the promoter paid no money to TelexFree for the stock in the first place.

56. In short, an investment of $350 (the Ad Central promoter's initial buy-in amount), results in an annual return of $1,040 ($20 x 52)– without selling a single VOIP product – so long as the promoter posted advertisements, among the hundreds of pre-existing advertisements, on a site identified by TelexFree.

[9] The cost of this buy-in level may have changed slightly over time. For example, according to Merrill's TelexFree PowerPoint presentation discussed above, the cost for this level was at some point $299.

3. *The $1,375 Buy-In Level (Ad Central Family)*

57. The third buy-in level, which required an investment of $1,375,[10] was called Ad Central Family. At this level the scheme operated the same way as the $350 Ad Central buy-in, but TelexFree gave the promoter a "stock" of 50 VOIP products (instead of 10), and instead of placing one ad per day the promoter had to place five ads per day. At the end of the seven day period, the company would then "buy back" the unsold stock from the Ad Central Family promoter for $100, and continue to do so for the remaining 51 weeks.

58. In short, if someone paid TelexFree $1,425 to become an Ad Central Family promoter, and then cut and pasted five ads per day, for seven days, from TelexFree's site to another site, TelexFree would pay that person an annual return of $5,200, regardless of the fact that the promoter has not sold a single VOIP product.

D. <u>The Compensation Structure – "Team" Earnings</u>

59. The "Ponzi" or "pyramid" aspect of TelexFree was magnified by its offer of "team" earnings. As is typical of pyramid schemes, the company's language for describing the compensation that could be earned by recruiting new members was confusing and ambiguous, using jargon like "uni-level compensation," "binary earnings," "cycle bonus," and "team builder bonus." In practice, the plan undergirded a pyramid compensation structure, in which people were incentivized to recruit other people, who then recruit additional people, and so on, while no one level of participants needed to make genuine retail sales to make money.

60. To qualify for the various team-based income streams TelexFree made available, TelexFree required a promoter to make at least one retail sale of the 99TelexFree VOIP product. Merrill's TelexFree PowerPoint presentation, noted above, and various YouTube videos by

[10] As above, this amount appears to have changed slightly over time.

TelexFree and TelexFree promoters, advised new promoters to make up a new user name and simply buy the product themselves to get credit for making a retail sale.

1. *"Binary" and "Uni-Level" Compensation Pyramids*

61. The first method of team earnings came from the direct recruitment of new promoters. For each direct recruit who bought in at the Ad Central level ($350), the recruiting promoter got a $20 "fast start" bonus. For each direct recruit who bought in at the Ad Central family level ($1,425), the bonus was $100.

62. YouTube videos the government has reviewed that explain the TelexFree compensation structure discussed a "binary" system, meaning that each promoter had two streams of recruits below him, a "left side" stream and a "right side" stream. To maximize compensation, the promoter had to ensure that both the left side and right side had *their own* recruits. For example, when a promoter ("Al") recruited a new promoter ("Ben"), Al could place Ben into Al's left or right side stream. Assume Al placed Ben on Al's left side stream. If Al recruited another person ("Chuck"), Al would then want to place Chuck in Al's right side stream, which would make Al eligible for a "cycle bonus" payment of $20 if both Ben and Chuck joined as Ad Central promoters, or of $80 if Ben and Chuck joined as Ad Central Family promoters. TelexFree would pay Al up to 22 cycle bonuses for Ad Central recruits each day, so if Al hosted an event and managed to sign up 44 Ad Central promoters, Al would receive a cycle bonus of $440 in addition to an $880 quick start bonus. If Al recruited only Ad Central Family promoters, the company would pay up to 768 cycle bonuses per day, for a daily maximum cycle bonus of $15,360.

63. To continue the left/right example, if Ben, who was recruited by Al, himself recruited a new promoter ("Dan"), Dan would appear on Al's left side stream and Ben, in turn,

would be able to choose whether Dan should appear in Ben's left or right side stream. If Chuck was able to recruit a new member ("Ed"), Ed would appear on Al's right side stream. Al would earn an additional $20 (or $80 at the Ad Central Family level) cycle bonus for the people recruited by Ben and Chuck, even though Al did not recruit them himself.

64. The YouTube videos explaining the TelexFree compensation structure also discuss "uni-level" compensation. This form of compensation was tied both to selling the 99TelexFree VOIP product and to the recruits beneath a promoter in the binary plan above. As discussed above, each individual AdCentral or AdCentral Family promoter posted free ads on the Internet, supposedly in an effort to bring in retail sales of 99TelexFree. When a promoter failed to make any retail sales, TelexFree "bought back" the unsold stock for $20 (Ad Central), or $100 (Ad Central Family). In the uni-level compensation scheme, TelexFree paid a promoter an additional 2% commission on each "buy back" for each recruit beneath him in his binary stream. For recruits who bought in at the Ad Central level, the promoter earned $.40 each week a recruit failed to sell any 99TelexFree products, and for recruits who bought in at the Ad Central Family level, the promoter earns $2.00 each week. The uni-level payment system paid the original promoter for buy backs going six levels deep.

65. According to YouTube videos posted by promoters (and corroborated by a promoter who discussed compensation with an HSI undercover agent), promoters could benefit from yet another form of "uni-level" earnings when recruits in their right or left side streams actually sold the 99TelexFree product. As noted above, 99TelexFree VOIP service was billed monthly at $49.90, and the Ad Central promoter making the direct sale earned a 90% commission on that amount in the first month. Each promoter in the binary stream above the direct seller earned a $.99 commission for each sale by a promoter in his binary stream and for

each monthly renewal. This form of uni-level compensation paid the original promoter for retail sales five levels deep.

66. The "binary" and "uni-level" systems created powerful financial incentives for promoters to recruit additional promoters, but essentially no incentive to sell TelexFree's purported VOIP product. As described above, promoters could make substantial profits without selling a thing, but merely by recruiting others to buy into the system.

2. *"Team Builder" Bonuses*

67. TelexFree's also provided "team builder bonus" compensation. To qualify for this compensation, a promoter must have made five retail sales of the 99TelexFree VOIP product, must have directly recruited 10 AdCentral Family promoters, and each of those recruits must have themselves also made five retail sales of 99TelexFree. The maximum bonus available as a team builder was $39,600.

68. It appears that, in certain instances, promoters have simply bought into the TelexFree system as team builders. That is, they themselves bought 11 AdCentral Family positions (theirs, plus the 10 they are required to "recruit") and the required five VOIP packages. For example, on one check reviewed as part of our analysis of TelexFree's bank accounts, a participant paid in $15,675 and wrote in the memo line, "team builder."

E. <u>Corroborating Information from Undercover Activities</u>

69. During the investigation, law enforcement arranged to have him/herself recruited as a TelexFree promoter, to confirm how portions of the TelexFree system operated.

70. On October 15, 2013, an HSI task force officer working in an undercover capacity ("UC") met with a TelexFree promoter ("Person A"). During the conversation, Person A told the UC that the UC could make $100 a week using an "Ad Central Family Package" to post

online ads for TelexFree, and could earn additional money by recruiting other people to join TelexFree. Person A drew out for the UC a diagram showing how "binary" recruitment would work.

71. The UC met Person A again the next day, and successfully joined TelexFree as a new promoter. The UC bought the Ad Central Plan for $1,425 (a $50 membership fee plus $1,375 for the AdCentral package), using a check made payable to the Person A. Person B, an associate of Person A, helped the UC register and verify the UC's new TelexFree "back office" account. This consisted of entering a name, date of birth, Social Security number, cellular telephone number, email address, and mailing/billing address. In order to access the back office, the UC created a unique log-in name and password.

72. Starting on October 21, 2013, using the UC's access to the TelexFree system, an HSI Intelligence Research Specialist placed online advertisements as a promoter for TelexFree. Following the system discussed above, the Specialist copied advertisements created by TelexFree and made available to her in the back office area of TelexFree's site, and pasted them to another website TelexFree recommended. As required under the Ad Central Family plan, the Specialist did this five times a day. The entire process took about 25 minutes per day.

73. Between October 21, 2013, and the date of this affidavit, the Specialist posted more than 700 advertisements. The ads have resulted in no retail sales of TelexFree's VOIP product. As described above, the sites on which these ads were posted contained page after page after page of hundreds of nearly identical ads placed by various TelexFree promoters for the identical VOIP service.

74. During a conversation with Person A on November 2, 2013, Person A told the UC that the UC did not need to sell TelexFree's VOIP product in order to make money, but just post

ads. This is in keeping with Merrill's PowerPoint presentation on TelexFree's site, discussed above. Similarly, in a meeting on December 2, 2013, Person A told the UC that, since July 2012, he had earned $1,600,000 as a TelexFree promoter, without selling a TelexFree product.

75. On December 6, 2013, the Specialist set up an "electronic wallet" (or "eWallet") through the TelexFree back office. On January 14, 2014, an undercover bank account was linked to the eWallet and, since that date, the account has received payments from TelexFree for the posting of advertisements.

76. In light of the above, from a business standpoint the TelexFree business model was nonsensical unless it was a pyramid scheme. There is no legitimate business model that can sustain "giving" inventory to it sellers at no cost; limiting advertising to a handful of classified ad sites already saturated with company ads; paying promoters a 90% commission on initial retail sales; "buying back" from promoters the unsold stock that had been provided for free in the first place; and finding ways to compensate promoters even more for recruiting other promoters.

77. As discussed further below, this is confirmed by an analysis of TelexFree revenues; did not make substantial revenue from sales of the VOIP product. TelexFree was nonetheless able to meet its massive payment obligations to existing promoters for some time, and it was only able to do that because it continuously brought in considerable investment dollars from new promoters.

F. <u>TelexFree's Revenue</u>

78. Among the documents the government has reviewed are profit and loss statements and balance sheets for both TelexFree, Inc., and TelexFree LLC, which TelexFree had provided to the MSD. The government has also reviewed financial information TelexFree submitted to

various state regulatory agencies, including Idaho, Washington, and Tennessee. There are various inconsistencies among these submissions.

79. In April 2013, a lawyer for TelexFree, Inc., and TelexFree LLC submitted to MSD a profit and loss statement for TelexFree, Inc., for the year 2012, followed by another version in February 2014. The figures on the two statements differ substantially; for example, the April 2013 statements listed about $1.8 million in total income for TelexFree, Inc., in 2012, while the February 2014 statement listed $2.8 million.

80. The government has also reviewed the 2013 profit and loss statements and balance sheets for TelexFree Inc. and TelexFree LLC, as submitted to MSD in February 2014. The Profit and Loss statements for TelexFree for the period January through December 2013 (as submitted to the MSD) report in part the following:

Description	TelexFree LLC	TelexFree Inc.	Combined
Income – Paid through Bank	$119,468,920.12	$56,195,790.54	$175,664,710.66
Income – Paid through System	$572,240,960.21	$268,930,757.53	$841,171,717.74
Total Income	$691,709,880.33	$325,126,548.07	$1,016,836,428.40
Total Cost of Goods Sold	$2,263,476.65	$397,736.51	$2,661,213.16
Agent Commissions – Paid through Bank	$50,670,290.64	$20,666,027.60	$71,336,318.24
Agent Commissions – Paid through System	$571,917,743.23	$268,930,757.53	$840,848,500.76
Total Agent Commissions	$622,588,033.87	$289,596,785.13	$912,184,819.00

81. The Profit and Loss statement for TelexFree LLC reflects additional income of $174,183,644.66 from Ympactus, TelexFree's operation in Brazil, which is not reflected here.

1. *Incoming Funds to TelexFree Bank Accounts*

82. TelexFree takes in funds from two sources: fees people pay to become TelexFree promoters and sales of the company's 99TelexFree VOIP service, which has been sold for

$49.90 per month since at least 2012. In the financial statements TelexFree has submitted to the MSD and other regulatory authorities, it reports income as either "paid through banks" or "paid through system." In our investigation, we reviewed bank account, credit card merchant, and other third-party records in an effort to determine the volume of sales of the VOIP product.

83. The investigation to date has identified and obtained records of 14 bank accounts opened and operated in the United States in the name of TelexFree Inc. or TelexFree LLC since February 2012 (not all operating at the same time). Wanzeler and Merrill are the authorized signatories on each of these accounts. In my review of the TelexFree bank accounts we have identified, a general pattern emerged. The vast majority of the thousands of deposits to these accounts appear to be buy-ins fees for TelexFree promoters. But of the thousands of cash, check, wire transfer, or money order deposits into the TelexFree accounts – totaling tens of millions of dollars in 2013 – only 19 appear to be for the purchase of TelexFree's VOIP service. For example:

a. A review of Bank of America account XXXXXXXX7408 opened in the name of TelexFree, Inc., in February 2012 revealed that between June 2012 and May 2013, the accounts received 1,133 deposits, totaling $12,203,496.48. Included in that sum were 534 cash deposits totaling $924,231.40. Between September 2012 and May 2013 there were 813 deposits in the exact amount of an Ad Central Family buy-in ($1,425 or $1,375 (the earlier requirement)) totaling $1,142,625. During that same period there were nine deposits in the amount of $49.90 – the VOIP purchase price (totaling $449.10).

b. Similarly, in September 2012 accounts were opened at TD Bank in the name of TelexFree Inc. and TelexFree LLC. In account #XXXXXX8409, in the

name of TelexFree LLC, between October 9, 2013, and January 17, 2014, there were 478 incoming wires ranging from $309 to $142,500, totaling $2,638,712. In the same period, there were 957 currency deposits ranging from $50 to $20,000, totaling $21,277,040.72. Of the deposits, there were 2,474 in the amount of $1,425, totaling $3,525,450. Deposits were made in multiple states along the eastern coast of the United States. During that same period there was one deposit for $49.90.

c. As to account #XXXXXX2808 at TD Bank, in the name of TelexFree LLC, between September 2012 and July 2013, there were 1,550 deposits by cash, check, money order or wire transfer in the exact amount of $1,425 (again, the Ad Central buy in price). During that same period there was one deposit for $49.90 (VOIP purchase price).

d. As to account #XXXXXXX334 at TD Bank, in the name of TelexFree LLC, between June and October 2013 there were 1800 deposits in the amount of $1,425. There was one deposit of $49.90.

2. *Incoming Funds Paid Through Credit Card Processing Services*

84. TelexFree also employs credit card processors to process payments to TelexFree's website, creating another potential avenue for customers to pay for VOIP service (as mentioned above, the site allows customers to use a credit card to pay for 99TelexFree). A review of the EFT deposits and payouts from the TelexFree accounts indicates credit card processors have made large deposits to TelexFree accounts, as has PayPal. Based on an analysis of the accounts, ProPay Inc., a credit card processor, processed credit card transactions for TelexFree from September 2012 to June 2013. Global Payroll Gateway Inc. (operating as Phoenix Payments),

another such processor, processed credit card transactions for TelexFree from June 2013 to September 2013, and I-Payout has recorded and tracked credit card payments processed through three other credit card processers since October 2013.

85. A review of the credit card processor records further confirms that while TelexFree in fact sold some 99TelexFree VOIP packages, the overwhelming percentage of incoming revenue was from new people investing in TelexFree to become promoters. For example,

a. I reviewed business records from ProPay, Inc. In 2013, ProPay processed 32,471 credit card sales (net of refunds and chargebacks) for TelexFree, totaling $29,150,021.19. ProPay also processed 6,098 credit card sale transactions (net of refunds and chargebacks) in the amount of $49.90 – the price of TelexFree's VOIP product. These sales totaled only $304,283.74.

b. I also reviewed business records received from Global Payroll Gateway ("GPG"). Between June 2013 and September 2013, GPG/Phoenix Payments processed total sales of $37,419,522.69 for TelexFree. Based on the records and additional information provided by GPG, GPG processed 49,656 credit card transactions for TelexFree between June 12, 2013, and September 4, 2013. Of those transactions, 7,362 (approximately 15%) were for less than $50 and, assuming every one of these transactions were to buy the VOIP product (which is unlikely), the sales revenue attributable to VOIP sales in this period was $367,363.80, or about 1% of total sales processed by GPG, a ratio similar to ProPay above.[11]

[11] There were also 31,129 credit card transactions in excess of $1,000.

c. I also reviewed records provided by i-Payout, a payment processing company that disbursed funds for TelexFree and provided record-keeping services for certain credit card payments made by promoters for buy-ins, and by purchasers of the VOIP product. The records show that in 2013 i-Payout recorded 52,562 payments to TelexFree totaling $66,036,927.99. Of these, there were 2,153 invoices for $49.90 (the monthly VOIP cost), totaling $107,434.70, or less than .2%

86. In total, in our review of TelexFree's bank account and credit card merchant account activity for the period January through December 2013, we identified approximately 15,630 payments to TelexFree, totaling $779,930.54, for monthly purchases of the 99TelexFree VOIP product. Based on TelexFree's reported sales of $1.016 billion, known sales of the 99TelexFree VOIP product represented less than 0.1% percent of TelexFree's total revenues.

3. *Outgoing Funds from TelexFree Accounts*

87. Just as sales of the VOIP product represented a fraction of TelexFree's revenue, the rest coming from new investors, the overwhelming majority of disbursements by TelexFree were to pay monies owed to existing promoters.

88. First, a review of funds disbursed from TelexFree's bank accounts showed that some funds have been paid to vendors that appear to support the necessary infrastructure for the 99TelexFree VOIP system. For example, payments, totally about $4,000,000, were identified going to iBasis, IDT Telecom, Liga Telecom, Exigo Office, Access Northeast (Xand), and Amazon Web Services. We also isolated other payments to law firms and consulting firms specializing in the "multi-level marketing" industry.

89. In the financial statements furnished by TelexFree to the MSD, the company reported Cost of Goods Sold for TelexFree, Inc., and TelexFree LLC as $2,263,476.65 and $397, $736.51, respectively, totaling $2,661,213.16. These costs of goods sold are described in the financial statements as Direct Inbound Dial & Access Numbers, Telecomm & Database Network Expense, and Termination.

90. The elephant in the room, however, is the amount paid to TelexFree's promoters. In this same period that we see $779,930.54 coming in from sales of the 99TelexFree VOIP product, TelexFree's financial statements reflect commissions paid to agents, either directly or indirectly ("through the system"), of over $912.1 million. As TelexFree has only two sources of revenue – payments to become promoters and monthly access fees for the 99TelexFree product, it is clear that the source of the company's substantial revenues and the commissions paid to TelexFree's promoters come not from sales of the VOIP product, but from the payments or buy-ins from people seeking to become promoters.[12]

91. Lastly, TelexFree, Inc., reported commissions payable of $7,642,550.42 on its balance sheet as of December 31, 2013, and TelexFree LLC reported no ($0) commissions payable at the same date. At the same time, the company has reported over a billion dollars in sales. Further, assuming for the sake of argument that even half of TelexFree's revenue came from the sale of the TelexFree VOIP product, this would leave some $500,000,000 in promoter

[12] For example, Citizens Bank account XXXXXX8206 was opened in Massachusetts on February 5, 2013, in the name of Telexfree LLC, listing James Merrill and Carlos Wanzeler as the authorized signers. A review of wire transfer data from that account showed that between February 21, 2013, and August 6, 2013, 7,340 wire transfers were made. Of those, 38 wire transfers, totaling $808,301.34, were made to entities such as iBasis, telecom companies, and electronic storage providers. The remaining 7,302 wire transfers, totaling $11,272,627.04, were made to individual persons, in amounts ranging from $270.00 to $116,650. Moreover, 1,023 of the wires to individuals were in the exact amount of $272.00, which, as explained in the "back office" portion of Telexfree's site, appears to be the minimum transfer amount TelexFree will send to promoters ($300, less transfer fees).

buy-ins during the period January through December 2013. If all of these promoter buy-ins were all at the AdCentral Family level (and the promoters sold no product but placed advertisements as required by TelexFree), this $500,000,000 would translate into 350,877 promoters, each expecting the receipt of $100 per week for 52 weeks – a payment stream aggregating $1.824 billion. After crediting the full $912 million in commissions reported as paid in 2013 by TelexFree (although some of these payments doubtless relate to contracts begun in 2012), there would still remain additional commissions owed or coming due of *$912 million*.[13]

V. Examples of TelexFree's Public Statements

92. On March 9, 2014 members of HSI, some in an undercover capacity, attended the TelexFree "New Compensation Plan" Conference at the Marriott Copley Place Hotel, 110 Huntington Avenue, Boston, Massachusetts. TelexFree periodically hosted conferences (as did successful promoters) to generate excitement for TelexFree. These events had a vaguely evangelical quality; senior TelexFree personnel tried to whip up the crowd of supporters with general exclamations about TelexFree's products and the chance to make money.

93. Merrill and Wanzeler spoke at the Boston conference, along with other TelexFree personnel and successful promoters. Several people, including a TelexFree marketing executive and the head of "IT," enthusiastically touted the quality of TelexFree's VOIP product, its

[13] Overall, TelexFree's accounts received thousands of deposits directly to its bank accounts and also through credit card processors who, after receiving payments from card users, transferred those payments in batches to TelexFree accounts. These automated clearing house ("ACH") credit transactions were transmitted via wire communications in interstate commerce. For example, on July 5, 2013, Global Payroll Gateway (also known as Phoenix Payments), recorded 176 sales transactions for TelexFree totaling $214,700.80. On July 8, 2013, the proceeds from these sales transactions were credited to a Telexfree Citizens Bank account, no. XXXXXX9078, through an ACH credit transaction originating at Phoenix Payments in Tempe, Arizona, and terminating in the bank account of Telexfree at Citizens Bank in Massachusetts. There are many similar wirings. Similarly, in 2012 and 2013 there were thousands of payments by bank-to-bank or wire transfer out of TelexFree's accounts in Massachusetts to TelexFree promoters. Citizens Bank's servers for processing banking transactions are in Rhode Island.

planned expansion, and the opportunity to "market" it. During Merrill's remarks, he first complimented the other TelexFree senior personnel at the conference, including Wanzeler, and talked excitedly about TelexFree's product and the profits to be made, saying, *e.g.*, "We can help people communicate with their friends and family overseas, for less"; "You are going to create communities of app users, each agent in here"; "You're gonna get paid"; "We are here to help you make money."

94. Later, Wanzeler took the stage, and made comments similar to Merrill's, extensively praising TelexFree's VOIP product: "TelexFree was built to change people's lives, save money for people [to] call [from] anywhere in the world to anywhere in the world"; "For over 20 years, I work in telecommunication. I was agent like you guys for big company in California. I learned the industry. I learned the product. We put our own infrastructure, okay? We changed what we done in the past 20 years and built something nobody else have. I can sit here today, please, if I'm lying here you can tell me, what company can give the opportunity for the people to call cell phone, landline, over 40 countries."[14]

95. Wanzeler continued, "We have a product and service no one else have; none of them. What company here in the U.S. can give you guys the opportunity have mobile, call from mobile phone to over 40 countries unlimited? ATT do that? Sprint? T-Mobile? Anyone do that? 40 countries? Cell and landline? Anybody? Yes? No? TelexFree only." Wanzeler also said, in the preceding month, "Over 600,000 customers paid $49.90 to TelexFree99."

96. Similarly, during the conference TelexFree's chief executive officer told the crowd, "We are here to build a long term sustainable business"; "We need your commitment to protect this opportunity for you and your families"; and "A long term sustainable business that

[14] Based on an open source internet search, Skype, for one.

can help your friends and family for years and years to come." Another TelexFree employee told the audience, "We just heard an incredible number: 580,000 retail customers [for TelexFree's VOIP product] in February."

97. During this and other conferences, Merrill, Wanzeler and the other speakers generated an excited, cheerleading atmosphere, apparently intended to give the appearance that TelexFree's VOIP product was groundbreaking and selling well. For example, in a statement recorded for public consumption on October 8, 2013, Merrill spoke about how "excited" he was about "new products about to launch." Similarly, at a TelexFree conference appearance on March 5, 2014, Merrill asked the crowd of TelexFree promoters to do "the wave," and then urged them to "get the product out there." He asked the audience to "touch people's lives" with "a billion cell phones," and told them TelexFree was trying to "put its best product together."

98. In light of TelexFree's actual financial picture, however, the repeated public statements by TelexFree personnel about TelexFree's VOIP products amounted to misdirection: Neither Merrill, Wanzeler, nor any other TelexFree executive mentioned that the company generated a miniscule amount of revenue from selling the VOIP product (about 1% or less), and instead was founded on, and depended on, generating revenue from new promoters that could be used to cover TelexFree's payment obligations to existing promoters. According to TelexFree's finances, the company was not profiting from TelexFree's legion of promoters selling more VOIP products, but instead depended on a continuous flow of new promoters, a distinction absent from TelexFree's public statements.

99. Moreover, based on extensive review of TelexFree's banking activity, credit card activity, and portions of its back office data, Wanzeler's statement to the crowd that TelexFree had brought in "over 600,000 customers paying $49.90" in or about February 2014 was false. In

their testimony to the MSD, both Wanzeler and Merrill re-affirmed that 580,000 people bought VOIP packages in February 2014. For his part, Wanzeler "guaranteed" that most of those people were "outside" retail customers, not promoters buying packages themselves, and he insisted that each of the 580,000 or so users paid $49.90 that month for the service.

100. But 580,000 customers paying $49.90 would have generated $28,942,000 in revenue from VOIP sales, and thousands of $49.90 entries in TelexFree's bank and credit card processing records. But that revenue appears nowhere in TelexFree's financial activity in that time frame. In the alternative, despite Wanzeler's representations to the MSD, the figure was derived from TelexFree promoters *themselves* "buying" the VOIP product on the TelexFree system to stay eligible for TelexFree commissions, that is, from promoters using their own "back office" credits with TelexFree (the money TelexFree owes them under the compensation system discussed above) to buy, in a virtual sense, the VOIP product. Thus, there would have been no genuine retail sales to third party customers, but only virtual purchases by people who have already invested in the TelexFree system.[15]

Further Allegations Concerning the Nexus Between TelexFree's Illegal Activities and the Properties to be Searched

101. As described above, TelexFree is a fundamentally fraudulent business. Although it maintains an actual VOIP service, only about 1% or less of the company's revenues come from that service and, at no time in its U.S. existence, could TelexFree's revenue from that service cover the massive payment obligations TelexFree had to its promoters. Meanwhile, about 99% of TelexFree's revenues came from investment dollars deposited by newly-recruited promoters,

[15] This strategy of calculating sales, revenue or other seeming legitimate figures from virtual electronic transactions is common to modern pyramid schemes.

and it is those funds – amounting to hundreds of millions of dollars – that were used to pay existing promoters.

102. Moreover, as discussed above, TelexFree's compensation system was maintained through its web site portal, and each promoter was given a "back office" location tied to the TelexFree site, through which the promoter could maintain his account, review records of what amounts TelexFree owed him, and seek transfers of funds, among other things. In short, much of TelexFree's system of managing and compensating promoters was electronically-based and, according to Merrill's sworn testimony, that promoter-related data was maintained on servers at Xand and Exigo.

103. Consequently, most or all of TelexFree's business records are evidence of an ongoing pyramid scheme, and so subject to seizure. This would include, for example, all accounting and financial records; all promoter-related records; all web site-related records (*e.g.*, instructions to promoters, advertising, etc.); and all records related to VOIP design and implementation.

I. The Marlborough Office Location

104. Based on public filings, sworn testimony by Merrill and Wanzeler, and other information, TelexFree's operations in the United States are based at 225 Cedar Hill Street, Suite 118, Marlborough, Massachusetts (the "Marlborough Office Location"). As noted above, TelexFree's registered corporate address is that address, although it states Suite 200. As Merrill explained in sworn testimony, however, the company moved from Suite 200 downstairs to Suite 118 because it needed more space.

105. As Merrill made clear during his testimony, TelexFree actually conducts business from this address. Moreover, on March 24, 2014, in a sworn filing with the Tennessee

Regulatory Authority, Merrill indicated, on behalf of TelexFree, that TelexFree has 15 employees at the Marlborough Office Location and keeps business records there.

II. The Xand and Exigo Data Storage Locations

106. As Merrill said during his testimony, TelexFree's maintains the servers supporting its business operations at Xand Corporation's data center in Marlborough, Massachusetts. Merrill noted that the company was in the process of transferring that data to Exigo, a Dallas company that appears to provide similar services, but targeted to the MLM market.

107. A review of TelexFree bank records confirms substantial payments to Xand and Exigo. For example, in 2013, TelexFree paid Xand about $77,781 by check and wire. In a similar time frame, but beginning later in 2013, TelexFree paid Exigo about $139,734 by wire transfer.

Conclusion

108. Based on the information described above, I have probable cause to believe that records and data from the three locations to be searched (as described in Attachment A), contain evidence, fruits, and instrumentalities of the crime of wire fraud, and aiding and abetting and conspiring to commit that offense (as described in Attachment B).

109. With regard to electronic data, relevant procedures for copying and reviewing the relevant records are also set out in Attachment B.

Respectfully submitted,

JOHN S. SOARES
Special Agent
Homeland Security Investigations

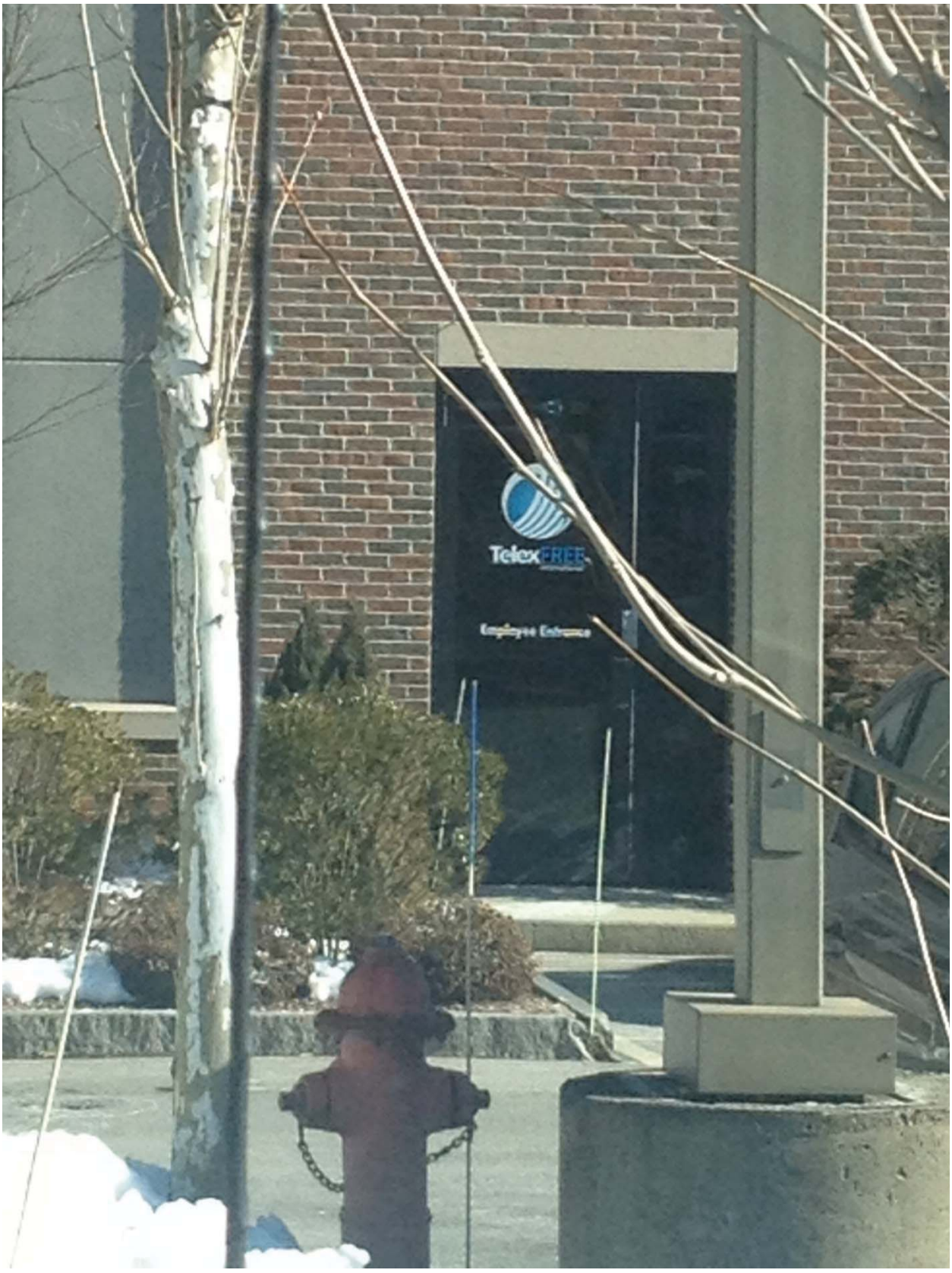
Sworn and subscribed to before me this 15th day of April 2014, at Boston, Massachusetts.

HON. DAVID H. HENNESSY
UNITED STATES MAGISTRATE JUDGE
DISTRICT OF MASSACHUSETTS

ATTACHMENT A

The premises to be searched are located at 225 Cedar Hill Street, Suite 118, Marlborough, MA 01752. Below are photographs of the premises to be searched:




TelexFREE
Employee Entrance

The following is a photograph of James Merrill in front of the office building located at 225 Cedar Hill Street. This photograph is from www.telexfree.com as it existed in or about Spring of 2013.



ATTACHMENT B

ITEMS TO BE SEIZED

I. All records, in whatever form, including but not limited to electronic data, database entries, emails, hardcopy documents, and tangible objects, that constitute evidence, fruits, or instrumentalities of violations of 18 U.S.C. §§ 1343 and 1349, including, without limitation:

A. Records and tangible objects pertaining to the following people, entities, and websites:

1. Brazilian Help, Inc.
2. Diskavontage
3. Ympactus
4. TelexFree LLC
5. TelexFree, Inc.
6. TelexFree Financial
7. www.telexfree.com
8. Carlos Wanzeler
9. James Merrill

B. Records and tangible objects pertaining to the following topics:

1. All VoIP customers and promoters including but not limited to:

a. All data concerning the names, addresses, email addresses, contact information and any other identifying information for all VoIP customers and promoters since January 1, 2012;

b. Records detailing the methods and amounts of all financial transactions involving all promoters and VoIP customers (both active and inactive) including bank, credit card, virtual credits, or any other type of payment credit or transfer, including transactions within the TelexFree back office;

c. Records detailing the amount of credit card chargebacks from VoIP customers and promoters;

C. Records and tangible objects pertaining to the payment, receipt, transfer, or storage of money or other assets by Diskavontade, Brazilian Help, Inc., Ympactus, TelexFree LLC, TelexFree Inc., and TelexFree Financial or any one of the names listed I.A above, including, without limitation:

1. Bank, credit union, investment, money transfer, and other financial accounts
2. Credit and debit card accounts
3. Tax statements and returns
4. Business or personal expenses
5. Income, whether from wages or investments
6. Loans

D. Records pertaining to the business practices of Diskavontade, Brazilian Help, Inc., Ympactus, TelexFree LLC, TelexFree Inc., and TelexFree Financial, including but not limited to any records relating to the compensation structure for promoters or other investors from the time of the respective companies' inception to the present;

E. Records pertaining to the total number of VoIP users for TelexFree's VoIP products, including but not limited to the number of unique VoIP users and the minutes used by each VoIP user;

F. Reports, data, contracts, agreements, design plans, proposals, and other documentation evidencing affiliation or business relationships with telecommunications companies;

G. Reports, data, contracts, agreements, emails, statements to or from financial institutions or other documentation concerning financial dealings with financial institutions;

H. Records, documents, written agreements, emails or notes concerning oral agreements and discussions, emails and letters from Diskavontade, Brazilian Help, Inc., Ympactus, TelexFree LLC, TelexFree Inc., and TelexFree Financial concerning or evidencing:

1. Ownership interests in and division of profits;
2. The sale and marketing of the VoIP product;
3. Promoter compensation;
4. The financial condition of the company;
5. The compensation plans for VoIP promoters;

I. Records, documents, written agreements, emails, notes, and letters, concerning or evidencing ownership interests in and division of profits from companies and stores described herein.

J. For any computer hardware, computer software, computer-related documentation, or storage media called for by this warrant or that might contain things otherwise called for by this warrant ("the computer equipment"):

1. evidence of who used, owned, or controlled the computer equipment;
2. evidence of the attachment of other computer hardware or storage media;
3. evidence of counter-forensic programs and associated data that are designed to eliminate data;
4. evidence of the times the computer equipment was used;
5. passwords, encryption keys, and other access devices that may be necessary to access the computer equipment;
6. records and tangible objects pertaining to accounts held with companies providing Internet access or remote storage of either data or storage media; and

K. Records and tangible objects relating to the ownership, occupancy, or use of the premises to be searched (such as utility bills, phone bills, rent payments, mortgage payments, photographs, insurance documentation, receipts and check registers).

II. All computer hardware, computer software, computer-related documentation, and storage media ("computer equipment"). Off-site searching of the computer equipment shall be limited to searching for the items described in Section I above.

If, after inspecting the computer equipment, the government determines that the computer equipment does not contain contraband or the passwords, account information, or personally-identifying information of victims, and the original is no longer necessary to retrieve and preserve as evidence, fruits or instrumentalities of a crime, the computer equipment will be returned within a reasonable time, if the party seeking return will stipulate to a forensic copy's authenticity (but not necessarily relevancy or admissibility) for evidentiary purposes.

If the computer equipment cannot be returned, agents will make available to the computer system's owner, within a reasonable period after the execution of the warrant, copies of files that do not contain or constitute contraband; passwords, account information, or personally-identifying information of victims; or the fruits or instrumentalities of crime.

Contents

I-THE PARTIES AND MEMBERSHIP
1.1 THE CONTRACTOR
1.2 THE CONTRACTING PARTY
1.3 MEMBERSHIP
II-PURPOSE
2.1 ACTIVITIES-AIM OF CONTRACTOR
2.2 PURPOSE OF THIS CONTRACT
2.2.1 Synthesis of legal relationship
2.2.2 Scope of services
2.2.3 Limits of the obligations of TELEXFREE
2.3 SUPPORT SERVICES AND LIABILITYDTELEXFREE
2.4 RELATIONSHIP REGIMEN
2.5 – REQUIREMENTS FOR ENTRY AND STAYING IN THE MULTILEVEL MARKETING SYSTEM
2.6.ETHICAL.PRINCIPLES
3.-.ATTRIBUTIONS.AND.DUTIES.OF.THE.CLIENT/MEMBER
4.-.REMUNERATION.AND.PAYMENT.METHOD
5.-TELEXFREE.ADVERTISING.CENTRAL.-.ADCentral.or.ADCentral.FAMILY
6.-.BINARY.PLAN.QUALIFICATION.-.Earnings.from.Binary.Cycles:
7.-.INDIRECT.EARNINGS.FROM.ADVERTISING.REVENUE
9.-.INDIRECT.EARNINGS.FROM.SERVICE.AND.QUALIFICATION
9.1.-.ACCESS.TO.VOIP.SERVICE.AND.REVENUES.THROUGH.USE
10.-.CANCELLATION.AND.BLOCKAGE.OF.REGISTRATION
11.-.INTELLECTUAL.PROPERTY.RIGHTS
12.-.LINKS.TO.SITES.OF.THIRD.PARTIES
13.-.FINAL.PROVISIONS

I-THE PARTIES AND MEMBERSHIP

1.1 THE CONTRACTOR

TelexFREE, LLC, 4705 S. Durango Dr. #100 Las Vegas, Nevada*1.2 THE CONTRACTING PARTY*

A natural person who has voluntarily filled out his particulars, including their Tax ID , registering his agreement with all these clauses after declaring that he understands the entire content of this instrument through his acceptance over the internet, at the website www.telexfree.com , by signing this contract, hereinafter referred to as the Member.

1.3 MEMBERSHIP

1.3.1 The parties identified above confirm that they are fully aware of the content of this instrument and that, pursuant to the best form of the law, by their own free and spontaneous will, to express their agreement they do sign this advertising and communications service subscription agreement, with the following clauses and conditions.II-PURPOSE

2.1 ACTIVITIES-AIM OF CONTRACTOR

2.1.1 The CONTRACTOR, doing business as TELEXFREE, is engaged in activities of business promotion, brokerage and business agent services, developing a network of promoters, providing them with training, support materials, oversight, follow-up and support, and also remunerating them based on the logical structure of binary multilevel marketing on behalf of TELEXFREE INC, pursuant to a specific contract between them.

2.1.2 TELEXFREE INC, from its headquarters in , MarlboroMassachusetts (U.S.), on the basis of an operating contract between the latter and the CONTRACTOR (YMPACTUS), has as its primary activity VOIP telephony, using its equipment installed at its headquarters in Massachusetts, where it makes the necessary connections for these calls; it also provides virtual media, through the website www.telexfree.com to associates and to the PROMOTERS that YMPACTUS/TELEXFREE coordinates and controls, including the respective publicity channels.

2.2 PURPOSE OF THIS CONTRACT

2.2.1 Synthesis of the legal relationship

The user, by accessing the website of TELEXFREE.COM can become a member through payment of the respective fee, which will provide access to the TelexFREE Multilevel Marketing network for the period of one year, without extension or renewal. At this stage, the member is called a PARTNER. The PARTNER will have the right to acquire, at an exclusive discount, products that

are offered on the website www.telexfree.com, with the principal VOIP telephony accounts called 99TELEXFREE. The PARTNER, upon acquiring them in the form of a kit (ADCENTRAL or FAMILY kit) assumes the title of PROMOTER and, as such, receives a space on the site www.telexfree.com to promote the products/services that he has acquired. He also receives training and access to materials also made available on the TELEXFREE website so that he can undertake to promote the latter and avail himself of the opportunity to be a PARTNER and PROMOTER to others in his circle of relationships. All activities are performed by the PARTNER/PROMOTER without any employment relationship, and they are able individually to manage the team and the resources it seeks to make available for such purpose, of their own free will. For the promotion of products/services he will receive a bonus in direct proportion to his results, based on the levels explained in a separate section in these GENERAL REGULATIONS. He must obey all the clauses of these GENERAL REGULATIONS so that the name of TELEXFREE and the juridical persons associated with it remain unblemished.

2.2.2 Scope of services

2.2.2.1 - Upon becoming a member, the natural person in question can acquire the kit of VOIP accounts. In doing so, he shall assume the title of PROMOTER and, at this stage, he is to be provided with a channel for virtual broadcasting - the website www.telexfree.com - so that he can post his announcements. If he wishes to post them daily, and manages to do so without interruption, he shall receive remuneration for each seven-day cycle, considering that, in addition to promoting the sale of the kits of products/services that he has acquired, he is also promoting the TELEXFREE brand. The form of remuneration is explained in a separate section of these GENERAL REGULATIONS

2.2.2.2 - While this contract is in force, the PROMOTER shall have unlimited access to the content of the tools intended for his use, as long as they are used in a manner that is in keeping with the TERMS OF USE AND THE PRIVACY POLICY available at the site of the advertisers and the CONTRACTOR, TELEXFREE.

2.2.2.3 - Access to virtual tools shall only be given to promoters who have fulfilled all the essential requirements, a process also referred to as 'qualification,' which is discussed below.

2.2.3 Limits of the obligations of TELEXFREE

2.2.3.1 - The supplying of printed material such as calling cards, pamphlets, folders or even panels, banners or variations thereof for advertising are not included in the services and materials supplied by TELEXFREE or its advertisers, and neither is underwriting provided for any meetings that PROMOTERS, individually or in groups, may organize.

2.2.3.2 - The supplying of the materials indicated above can, however, be arranged as a matter of generosity by TELEXFREE, the advertisers or any related entity, which shall not imply a binding link or the acquisition of a right. It may also provide them through reimbursement of the respective cost for all promoters, for optimization of scale, for cases in which there is an express prior agreement in writing between the parties to this effect.

2.3 SUPPORT SERVICES AND LIABILITY OF TELEXFREE

2.3.1 - THE PROMOTER shall have everything necessary so that he can commence and undertake his activities in the MULTILEVEL MARKETING system, and will be provided with oversight of the results obtained in the respective system where he is operating.

2.3.2 However, in the event of failures of public utilities to supply electricity that overwhelm TELEXFREE's own capacity to keep the energy grid for its systems up and running, and moreover, in the event of an interruption of internet services or the effects of cataclysmic events, inasmuch as *force majeure* or acts of God are involved, TELEXFREE assumes no liability for solving the problem of resuming the operation of the site and the services associated with it.

2.3.2.1 In such cases, PROMOTERS must await the return to normality of public services to recommence their activities.

2.3.2.2 For as long as situations resulting from acts of God and *force majeure* may persist that prevent the TELEXFREE site from being made available (when the site is off the air) the PROMOTERS shall not incur any loss for failure to post daily advertisements. This exception, however, does not apply in cases where a parallel situation occurs on the premises of the PROMOTER, unless the fact is commonly known or proven by a document issued by the service provider, covering all of the 24 hours in the period when the activity (posting of the advertisement) is supposed to take place.

2.3.2.3 Schedules for the posting of ads or for any operation that uses the TELEXFREE system shall be those of its servers in Boston (Eastern Time Zone).

2.3.3 - THE PROMOTER does not have any liability for the services and/or products of the ADVERTISERS, since such liability is assumed directly by the latter.

2.4 RELATIONSHIP REGIMEN

2.4.1 -PROMOTERS do not have an employment relationship, inasmuch as their working regimen is autonomous, free of any imposition of routines, goals or regularity, and there is no hierarchical relationship, since they can establish on their own the pace, routine, or geographic area, and must, however, diligently seek to preserve the good name, image and brand of TELEXFREE and its advertisers or suppliers of products and services.

2.4.2 - The remuneration received by PROMOTERS involves the bonuses and commissions earned by applying the binary system multilevel marketing methodology, in amounts that depend exclusively on the commitment of the individual and the group/network/category in which he operates; the stepped increases in pay serve as an incentive, and do not involve the imposition of a hierarchical order.

2.4.3 - The PROMOTER is expressly notified that it is prohibited for him to present himself as acting in the name of TELEXFREE in relation to public or private institutions, nor is he authorized to make purchases or sign commitments or obligations on behalf of TELEXFREE, YMPACTUS or the advertisers or suppliers of products or services offered by TELEXFREE.

2.4.4 - THE PROMOTER, upon registering and accepting the content of these GENERAL REGULATIONS, is fully aware that he will have ample ability to conduct his extracontractual activities, doing things entirely at his convenience, and able to engage in other activities, paid or not, with or without an employment relationship, with the understanding that there is no employment relationship with the CONTRACTOR.

2.4.4.1 The PROMOTER may not, however, be part of another Multilevel Marketing network whose activities are similar to TelexFREE's , or that may in any way create a conflict of interest.

2.5 -REQUIREMENTS FOR ENTRY AND REMAINING IN THE MULTILEVEL MARKETING SYSTEM

2.5.1 - Individuals interested in entering the TELEXFREE Multilevel Marketing System must become members through nomination by another PROMOTER, by: a) completely filling out the respective registration forms, b) sending in the registration form; c) payment of the membership fee.

2.5.2 - Membership must be paid for in one single installment through payment of the respective bank payment ticket, and this date will serve as the start of the 12-month period of its duration. As of the last day of expiration of the contract, it will only be possible to remain in the CONTRACTOR's Multilevel Marketing System through a **new membership**, with the following rules applying to this 2nd year, or subsequent years:

-

2.5.2.5 -PROMOTERS not applying for membership for the following year within the deadline must wait for one year from the expiration to re-enter the system, through a new membership as a PARTNER.

2.5.3 - "Position" is understood to refer to a promoter's location in the multilevel network, which qualifies him to receive the respective bonuses, pursuant to the specific rules.

2.5.4 - When a position becomes vacant because of the exclusion of a PARTNER or PROMOTER or because of the latter's not being contracted for a second (or subsequent) year, or else because of contracting for a second, the position shall belong to TELEXFREE, including the respective remuneration, and TELEXFREE may transfer the rights of the position to a promoter.

2.5.9 - As a required procedure for membership and admission into the multilevel marketing system, candidates must fill out all data requested on the application form available at: http://www.telexfree.com. No other electronic address should be used for registration or for daily access. TELEXFREE does not recognize any other electronic addresses and, moreover, hereby gives notice that the use and information provided at other electronic addresses should not be used, under any circumstances. The effects of such use, if it should take place, shall be exclusively the liability of the user as well as the assignment of passwords to third parties.

2.5.10 - The Marketing System network of TELEXFREE allows only one registration for each person based on a valid, active ID

2.5.11 - A PROMOTER may transfer his position and the respective benefits to others as long as he respects the legislation in force and adheres to the rules of the Market Network Multilevel Marketing System itself.

2.5.12 - A PROMOTER who wishes to sell his position in the marketing system network should understand that this can only be done following the analysis and acceptance of the CONTRACTOR, and, if authorized, he will be charged administrative expenses equivalent to 10% (ten percent) of the amount already received in the position of the PROMOTER conveying it, upon executing the transfer, payable to TELEXFREE.

2.6 ETHICAL PRINCIPLES

2.6.1 - Acts of discrimination on the part of promoters are at variance with the ethical principles of TELEXFREE and may entail expulsion from the system, through express communication to such effect.

2.6.2 - Upon registering at the TELEXFREE site, the PROMOTER undertakes to use the resources offered strictly within the rules and schedules established by the TELEXFREE system at its website: http://www.telexfree.com., and furthermore, undertakes to observe these terms of use and to obey all federal, state and municipal laws and regulations in force.

2.6.3 - THE PROMOTER undertakes to use the TELEXFREE site only to consult the Market Network System for his respective area, download authorized content and send invitations to participate in the group, or disseminate his announcements, it being the case that any other unauthorized commercial use is expressly prohibited, under penalty of [forfeiture] of membership.

2.6.4 - As a condition for the use of the TELEXFREE site, for all legal purposes, the PROMOTER undertakes not to use resources for any purpose that is illicit, not regulated in this contract or prohibited. In such cases, TELEXFREE reserves the right to refuse service, close accounts, remove or edit content, or to cancel orders at its sole discretion.

2.6.5 - THE PROMOTER agrees to respect all applicable local, municipal, state, federal and international laws and regulations, being exclusively responsible for any actions or omissions carried out with his password, including on the content of his transmissions through the System, agreeing moreover that in particular he must not:

a) use the TELEXFREE Network Marketing System in connection with surveys, contests, chain-mails, pyramids, spamming or unsolicited messages (whether commercial or otherwise);

b) slander, defame, disturb the peace of others, persecute, threaten or in any other way violate the rights of third parties, such as rights to privacy and publicity;

c) publish, distribute or disseminate any materials or information of discriminatory content that violates the rights of freedom of belief, or are defamatory, offensive, obscene, indecent or illegal;

d) obtain or in any way collect information about others, including e-mail addresses, without the due consent of the owner;

e) create a false identity to deceive others with regard to the identity of the sender or the source of the message;

f) attempt to obtain unauthorized access to the TELEXFREE Network Marketing System, other accounts, computer systems or networks connected to the TELEXFREE Network Marketing System, through illegal password searching or in any other way;

g) violate any applicable laws or regulations, including and without limitation, laws concerning the transmission of technical data;

h) interfere with the use and operation of the TELEXFREE Network Marketing System by another PROMOTER or with the use and operation of similar systems by other individuals or organizations;

i) violate the integrity or test the vulnerability of a data system or network security measures or violation of security or authentication;

j) interfere or try to interfere in the activities of any user, host or network, including, without limitation, through the introduction of malware into the Site, overloads, "flooding," "spamming," "mailbombing" or "break ins"; forging any headers or any part of the information in the header in any e-mail or posting;

k) use any mechanism, software, tool, agent, data or other device or mechanism (including, without limitation, browsers, spiders, bots, avatars or smart agents) to navigate or seek out sites other than those retrieved by the search engine and search agents provided by TELEXFREE or browsers generally available to the public;

l) publish, transmit or make available any material encouraging conduct that constitutes a criminal offense, or that encourages or supplies instructive information on illegal activities or activities such as "hacking,"cracking," or "phreaking";

m) use terms that distort the real meaning of products or the mechanism and functioning of multilevel marketing, including, without limitation, expressions that convey the idea of instant wealth for nothing in exchange, as well as speaking of registration costs as a "financial investment." Similarly, it is expressly prohibited to use the term "INVESTMENT" at meetings and in promotional materials in general, orally or in writing.

n) disseminating unauthorized material that has been modified or that is at variance with the rules of the TELEXFREE Network Marketing System or uses images of people without their authorization, or works protected by copyright including, site construction, blogs and spaces on social networks that could be interpreted as official corporate communications of TELEXFREE;

o) for proven sending of SPAM, that is, any kind of unauthorized message or message unsolicited by the addressee, containing information from the TELEXFREE Network Marketing System or its website;

p) for making profane or offensive comments, concerning or addressed to the System, the company that administers it or the people that run it;

q) for making profane, offensive, slanderous, obscene, indecent, defamatory comments, or comments that are otherwise at variance with the rules and conditions of the System, concerning or addressed to any of our PROMOTERS;

2.6.6 -In the event that it is ascertained by two or more elements of proof that a PROMOTER is inviting other promoters of TELEXFREE to take part in another network that also works with multilevel marketing, or is making use of the structure and contacts of the promoters of TELEXFREE to promote other events or feature other products and services not related to this activity.

2.6.7 If practices are proven that are in violation of this list of ethical behaviors, or another clause of this contract, steps will be taken pursuant to what is set forth in ARTICLE 10 of this instrument, and its respective sub-clauses.

3 - ATTRIBUTIONS AND DUTIES OF THE CLIENT/MEMBER.

3.1 - By submitting the application, the new member, whether a PROMOTER or not, agrees to receive messages in his mailbox (e-mail), via the specific tools used by the system, sent by upline and downline promoters on his line as well as those from TELEXFREE network administrators for other purposes.

3.2 - The PROMOTER agrees and hereby declares that the communications and notifications sent electronically by TELEXFREE to his e-mail address are valid for legal purposes.

3.3 - TELEXFREE reserves the right to engage in advertising, with content and format of its choosing, in any message(s) sent to its PROMOTER, who hereby agrees to receive them, without having the option of any special form of reply that would classify them as undesirable or unauthorized.

3.4 - THE PROMOTER declares, under penalty of the law, that the information provided by him on the website of TELEXFREE is true, accurate and complete, and undertakes to keep it up-to-date, especially the physical mailing address; and if such information is mistaken, incomplete or inconsistent, it shall not invalidate notifications sent by other means other than electronic ones.

3.5 - The access code and password of the PROMOTER is personal and non-transferable. TELEXFREE assumes no responsibility for the security of the data in the PROMOTER's personal computer file recorded on external media.

3.5.1 - The use of the virtual environment entitled *Back Office* can be implemented for the transfer of credit between PROMOTERS and for payment of invoices, their own, or those of third parties, and the member, whether a PROMOTER or not, should access the website only using the address www.telexfree.com, being aware that no other address is official and approved by TELEXFREE.

3.5.2 - TELEXFREE does not have any responsibility for transactions that promoters may execute using the virtual environment made available to effect such operations, the use of the password and its safekeeping being their responsibility. The member declares, whether a PROMOTER or not, that he should undertake to change its password periodically, and also that he will not use known numbers or obvious data associated with dates, relatives, or objects, for example, for his own security.

3.5.3 - With a view to protecting the image of TELEXFREE, PARTNERS, whether acting in the capacity of ADCENTRAL, FAMILY or TEAM BUILDER members, in making presentations to groups of people invited to join the TELEXFREE Multilevel network and use its products and services, must restrict themselves to the material made available in the video provided for the occasion, and may not express their own views in public. After showing the standard presentation, however, they may, addressing people individually, answer questions from the audience. No other material can be used at presentations.

3.5.4 - If at presentations a PARTNER or PROMOTER fails to comply with the instructions set forth above, he shall have his login blocked immediately and be subject to the disciplinary procedure of these GENERAL REGULATIONS, without impairment to civil and criminal liability.

4 - REMUNERATION AND PAYMENT METHOD

4.1 - The payment of bonuses and incentives to the PROMOTER, when in the form of money, shall be made by a bank check, or deposit to the checking account or savings account payable to the PROMOTER - ACCOUNT HOLDER.

4.2 - All payments by the PROMOTER to the CONTRACTOR/TELEXFREE, when made available in the financial system of the PROMOTER's country shall be made in the official currency. However, for the contract between TELEXFREE INC and YMPACTUS, the bases for calculation shall be established in U.S. dollars, always indicated by the symbol "US$" since all operational activities are conducted at the headquarters of TELEXFREE INC in the United States of America.

4.3 - In all cases, TELEXFREE reserves the right to retain the total amount of the remuneration of the PROMOTER, taxes and/or benefits, as well as administrative expenses, if any, that result from any legal issue raised, defined as follows:

a) Administrative Expense - expenses that are charged by the banking system, whose stipulated amount shall be disclosed via the website: www.telexfree.com.br; with it being up to the user to check the information.

b).

4.4 - Amounts for monthly payments charged for use of the services that are the object of this instrument, as well as credit for promotion paid by the TELEXFREE Network Marketing System to the PROMOTER, for the marketing and incentive campaigns in effect, shall be specified on the registration page of the TELEXFREE site, and should be paid in accordance with the rules established therein, which may be altered for the adjustment of the campaign in progress, or at any time that TELEXFREE may deem it necessary, with its members to be so notified forthwith.

4.5 - In the event of a change in the currency or the national monetary system, the amount shall be converted to the new standard according to the official standards of equivalency in force.

4.6 - In the event of fluctuations or alterations in the economy to the degree of compromising the contractual balance, the amounts stated herein in national currency could undergo an adjustment to re-establish the necessary balance between the parties.

5 -TELEXFREE ADVERTISING CENTRAL - ADCentral or ADCentral FAMILY

5.1 - MEMBERSHIP: A Partner who wishes to enter the TelexFREE Multilevel Marketing system must establish his MEMBERSHIP as a "Partner Member," and to such end, pay the equivalent of US$ 50.00 (fifty U.S. dollars).

5.1.1 - With membership, the PROMOTER: a) guarantees for 12 (twelve) months his position in the marketing system network and, b) is entitled to acquire the kit of VOIP accounts with exclusive discounts characterized as follows: ADCentral kit and/or Family Kit, c) the right to sell 99TELEXFREE VOIP accounts through his sub-domain, at face value, and receiving in such cases a commission of 10% on the amount of the sale.

5.2 PROMOTER: this refers to the person who, after receiving his membership, (see following clause), may acquire a kit of VOIP accounts with an exclusive discount, which may be: a)

ADCentral, with 10 99TELEXFREE accounts or b) FAMILY, with 50 VOIP accounts, and in both cases he will receive a virtual BACK OFFICE that is to be used to post ads for the sale of these products which he has acquired with the exclusive discount; and if he manages to do so without interruption for each seven-day cycle, he shall receive an additional VOIP account.

5.3 - If he so desires, the PARTNER may sponsor other member/promoters, that is, for the same Tax ID, only up to 90 days counting from the date on which he pays for his first membership, and in that case, only registering them on his downline.

5.4 -ADCENTRAL PROMOTERS: After setting up his membership, a PARTNER may acquire an "**ADCentral**" kit consisting of 10 99TELEXFREE VOIP accounts, for which he must pay the equivalent of US$ 289.00 (two hundred and eighty-nine U.S. dollars).

5.4.1 - with this qualification, the PARTNER will become a TELEXFREE PROMOTER and, accordingly, shall have his own active ad central for 12 (twelve) months, counting from the date of his membership (and not from the date of the purchase of the kit).

5.4.2 - He must also post 1 (one) announcement (prepared by TELEXFREE) per day on internet announcement sites (whether free of charge or not), so that at the end of each cycle of 7 (seven) announcements for the week, the PROMOTER shall receive one 99TELEXFREE account.

5.4.3 - If the promoter should choose to post announcements that are paid for, such expense is to be borne by the PROMOTER.

5.4.4 - The posting of announcements in numbers greater than one per day are not considered as two days, and so on, successively.

5.4.5 - After making payment for the kit, the partner becomes an ADCENTRAL PROMOTER and shall receive the right to sell the VOIP accounts at face value, as they are made available on the TelexFREE site, for the duration of his contract, without, however, earning a commission either in the upline or the downline, without this constituting an acquired right if they are not sold in this period, and the offer can be closed without any indemnification.

5.4.6 - Upon receiving the 10 VOIP accounts, if he wishes to receive the bonus of one new VOIP account per week, he must implement a posting of an announcement for each seven-day cycle without interruption.

5.4.7 - If he should fail to make the announcement, even for a single day, he shall not receive the VOIP account indicated in the preceding subclause; if he makes more than one announcement per day, he shall not be compensated for the announcement on the following day.

5.5 -ADCENTRAL FAMILY MEMBERSHIP - A PROMOTER wishing to attain the status of an "**ADCentral FAMILY Member**" must pay the equivalent of US$ 1,375.00 (one thousand three hundred and seventy-five U.S. dollars).

5.5.1 - With this membership, a PROMOTER shall have 5 (five) active announcement centrals for 12 (twelve) months, counting from the date of his activation.

5.5.2 - He must, in turn, post 1 (one) announcement (prepared by TELEXFREE) per day at internet announcement sites (whether free of charge or not) on each one of the 5 (five)

ADCentral sites. At the end of the 35 (thirty-five) announcements the PROMOTER shall receive 5 (five) 99TELEXFREE accounts as remuneration for these announcements.

5.5.3 - If for any reason the PROMOTER does not achieve the goal of 7 (seven) announcements per week, on each one of the 5 (five) ADCentral sites, the PROMOTER will not receive a 99TELEXFREE account for that particular week in which he did not meet the goal, from the respective ADCENTRAL.

5.5.4 - Other weeks begin normally and he can meet the goal and receive the compensation.

5.5.5 - Upon confirmation of payment of his membership fee, the promoter shall also receive, just once, 50 (fifty) 99TelexFREE packets that he can sell for as long as his contract remains in force, for the face value of the product, as disclosed by the TelexFREE site, and receiving credit for the sale of this product, which, however, will not generate any commission, either for the upline or the downline, and not accruing any rights if he does not put through the sale within this period, with the offer ceasing without any indemnification.

5.6 - An ADCentral can become a FAMILY ADCentral, making upgrades for each additional ADCentral with payment for this purpose of US$ 289.00 (two hundred and eighty-nine U.S. dollars), for each additional one up to a total of 4 (four).

5.7 - A PROMOTER will achieve **TEAM BUILDER** status when he is active in an ADCentral FAMILY position (in the marketing network) that has 10 (ten) ADCentral FAMILIES on the incentive plan registered directly by him on his site.

5.7.1 - As long as he is fulfilling the qualification in clause 5.9.2, a TEAM BUILDER will earn a payment of 2% (two percent) of the company's net billing in the following month, received on the 10th day following the registration of the earning; the maximum amount for this earning, by contract, which is for one year, is up to US$ 39,600.00 (thirty-nine thousand U.S. dollars), or the end of the 12- (twelve) month contract, whichever occurs first.

5.7.2 - The qualification referred to in clause 5.9.1 consists of the PROMOTER TEAM BUILDER's having sold 5 99TELEXFREE VOIP accounts as well as each one of the 10 PROMOTER ADCENTRAL FAMILIES in his network that formed the TEAM BUILDER.

5.8 - THE PROMOTER shall receive as an incentive a bonus of US$ 20.00 (twenty U.S. dollars), for each VOIP ADCentral kit that his direct lower PARTNER acquires and a US$ 100.00 (one hundred U.S. dollars) bonus for each VOIP FAMILY kit that his direct lower PARTNER acquires; in all cases, this promoter receiving the bonus must have at least one active 99TELEXFREE client plan.

5.9 - VOIP accounts acquired for each one of the plans, must be activated within the period of validity of the PROMOTER's registration, and shall not be computed as a "CLIENT" account that qualifies the PROMOTER to receive bonuses.

6 - BINARY PLAN QUALIFICATION - Earnings from Binary Cycles:

6.1 -A PROMOTER who directly registers 2 (two) new promoters, with one on the left side and the other on the right side of his marketing network, qualifies for direct and indirect binary

earnings, and for 2% (two percent) of the network from the first to the 6th level, assessed only on plans whose owners have at least one active VOIP client, that is, who have at least one active 99TELEXFREE plan.

6.1.1 - Upon qualifying in the manner described in the clause above by selling 2 (two) new ADCENTRAL kits to people in his network, with 1 (one) on the left side and the other on the right side, he shall receive an additional gratuity of US$20 (twenty U.S. dollars), called the binary cycle, with the maximum daily earning in this status being US$ 440.00 (four hundred and forty U.S. dollars), for 22 (twenty-two) binary cycles.

6.1.2 - If the sale is of 2 (two) VOIP ADCentral FAMILY kits, this cycle will yield an additional US$ 20.00 (twenty U.S. dollars), for the ADCentral principals, plus US$ 60 (sixty U.S. dollars), for 3 (three) of the 4 (four) ADCentral additionals, leaving the additional ADCentral still remaining to initiate future cycles.

6.2 - This form of revenue stream rewards the PROMOTER directly when he registers 2 (two) new sales of VOIP kits to his PARTNERS; with 1 (one) on the left side and the other on the right side, or else indirectly through the growth of his natural network (individuals registered by promoters in his downline network on the left and right sides), or by spillovers (individuals registered by promoters in his upline network on the left and right sides). The maximum daily yield in this position is US$ 15,360.00 (fifteen thousand, three hundred and sixty U.S. dollars), for the 768 (seven hundred and sixty-eight) cycles.

7 - INDIRECT EARNINGS FROM PRODUCT REVENUE

7.1 - THE PROMOTER shall receive an amount equivalent to 2% (two percent) on sales of 99TELEXFREE accounts made by the PROMOTERS in his network, both direct and indirect, up to the 5th level.

8 - ROYALTIES

8.1 - THE PROMOTER shall be entitled to a payment of 1% (one percent), in the form of ROYALTIES, from the company's net billing, if within 1 (one) calendar month (from the 1st (first) day - to the last day of the month) the PROMOTER shall have closed 22 (twenty-two) cycles in 20 (twenty) days, which need not necessarily be consecutive days.

9 - INDIRECT EARNINGS FROM SERVICE AND QUALIFICATION

9.1 - ACCESS TO VOIP SERVICE AND REVENUES THROUGH USE

9.1.1 - Promoters and other clients indicated by them can implement their communications access through VOIP - Technology for the transmission of voice signals over Internet Protocols (Voice over Internet Protocol) - using the software available for download directly from the portal *www.telexfree.com*.

9.1.2 - The promoter shall be paid directly For 99TELEXFREE accounts, and only for such accounts, the promoter shall be paid directly, For that is to say, when the client buys an individual VOIP 99TELEXFREE account on his site - he will receive a direct commission of 10% (ten percent) of the amount paid, and 2% (two percent) of indirect commission, from the 1st

(first) level to the 5th (fifth) level, for clients of his direct and indirect promoters, as long as the following requirements are satisfied:

9.1.2.1 - if each level has a direct 99TELEXFREE client with its active plan; thus, in order to receive the 2% commission at five levels, as mentioned in the previous clause, he must have five direct clients with active 99TELEXFREE; moreover, if he only has 4 direct clients with active 99TELEXFREE he shall receive a commission of 2% only on the first four levels, and so on, successively.

10 - CANCELLATION AND BLOCKAGE OF REGISTRATION

10.1 -CANCELLATION OF REGISTRATION

10.1.1 Through the procedures set forth in this section of this membership contract, TELEXFREE may cancel the registration of a PARTNER and a PROMOTER who violates the terms of the code of ethics, or fails to discharge any of the duties assigned to him, and also on grounds of material damaging to other promoters and their activities, or to other suppliers of information.

10.1.2 - A PARTNER or PROMOTER can cancel his membership within 7 (seven) days of becoming a member, and receive a full refund of what he actually paid to TELEXFREE, including the membership fee and the price of the VOIP accounts he has not activated; if the payment has been made with a credit card, he will be asked to cancel the purchase through the credit card company.

10.1.3 - To be disconnected from the TELEXFREE NETWORK Marketing System, a member must request cancellation of his participation on a specific form provided on his personal page, or in the event of absence or inability to use this resource, through a letter written and signed by him, with certified signature recognition, sent to the headquarters of the CONTRACTOR, correctly stating all of the information requested; if these data rigorously match the data reported when putting through the application, which is to be ascertained for reasons of security, the cancellation shall be approved in an irreversible manner.

10.1.4 If a PARTNER or PROMOTER seeks cancellation of membership after the legal deadline, he is aware that he will not receive any reimbursement of any amount, since his position will continue to entail expenses for its maintenance.

10.2 CANCELLATION OF PAYMENT

10.2.1 If a PARTNER or PROMOTER should cancel the payment for his membership, all logins having the same CPF/ss# or e-mail shall be suspended, and they shall be released upon payment of 10% of the amount of the purchases of the VOIP 99TELEXFREE kits (Partner, Adcentral, Family or Team Builder), in addition to reimbursement for all amounts that the promoter has received in the cancelled position.

10.2.2 Cancellation of payment shall also entail the cancellation of the amounts for the respective bonuses generated in the uplines of the binary system.

10.3 - BLOCKAGE OF REGISTRATION

10.3.1 The TELEXFREE NETWORK Marketing System can block the registration of a PARTNER/PROMOTER at any time, which becomes effective immediately, with notification to the PARTNER/PROMOTER,

if it believes that the latter has committed an act that directly or indirectly violates the provisions of this contract, in particular:

a) with the lapse of 15 (five [sic, i.e., 'fifteen']) days from the expiration of membership or the payment due date of any installment of the VOIP kits that he purchased, when purchased in installments.

b) if improper enticement of members of his own network of TELEXFREE promoters is proven.

c) if, with the lapse of 5 (five) days from the confirmation of his membership a PARTNER has not put through payment of the amounts specified for his membership.

10.3.2 Blockage consists of the total suspension of activities connected to the Back office area.

10.3.3 Concomitant with the blockage, while in this situation, the PROMOTER may not engage in any activity pertaining to his status.

10.4 - If actions are ascertained that are in violation of this contract, the PARTNER/PROMOTER shall be given the opportunity to present a written defense within 10 days, or to submit his resignation in the same manner and timeframe. If the acts in violation of this contract are confirmed, the blockage shall be converted into definitive Cancellation of Registration for membership, as well as the prohibition of a new registration/membership.

10.5 - A PARTNER/PROMOTER whose registration is cancelled by TELEXFREE as a result of what is set forth in this section, shall lose the right to all privileges offered by the TELEXFREE Network Marketing System, and cannot enjoy in any way the benefits that he held as a PROMOTER without the express consent in writing of the management of TELEXFREE.

10.6 - TELEXFREE shall not return, on any grounds or justification, the monthly payments made by the PROMOTER for the purchase of VOIP kits or other products, considering that he is fully aware that such amount was paid for the use of the resources provided by the TELEXFREE Network Marketing System as accessories in the conduct of the marketing campaign under way and/or, at the discretion of the PROMOTER himself, as an ongoing investment in the Network Marketing program made available, such that no request for reimbursement of amounts already transferred to TELEXFREE NETWORK Marketing System will be accepted.

11 - INTELLECTUAL PROPERTY RIGHTS

11.1 - The PARTNER/PROMOTER recognizes that the content, without limitation, of text, software, music, sound, photographs, videos, graphics or any other material contained in the advertising of sponsors or distributed electronically, as well as information produced commercially that has been presented to him by TELEXFREE, by advertisers of TELEXFREE or by other suppliers of content, is protected by the laws of copyright and Trademark protection. Included also in this protection are brands of advertisers or sellers of products and services that have contracted with TELEXFREE to promote and commercialize their products and services, including Computer programs, Brands and Patents, although as long as it is authorized by TELEXFREE, it possible to obtain a copy, of such content solely for its use in the non-commercial promotion of the TELEXFREE Network Marketing System, as long as the Copyright notices and other notifications of intellectual property and image are kept intact, with any modification, copying, reproduction, republication or sending of altered data to another computer or by some other manner of distribution being prohibited.

11.2 - The compilation, organization and setting up of all site content is the exclusive property of TELEXFREE and protected by U.S. and international copyright laws, also including brands and patents.

11.3 - Access to the website does not constitute a license for the PROMOTER to use its content or any rights of third parties encompassing those relating to intellectual property.

12 - LINKS TO SITES OF THIRD PARTIES

12.1 - The site may contain interactive links and functionalities that interact with the sites of third parties, including sites of social networks. TELEXFREE is not responsible and has not liability for the functionality, actions, omissions, privacy configurations, privacy policies, terms and conditions and the content of any website.

12.2 - The links and interactive functionality with third party sites at the site do not constitute an endorsement by TELEXFREE of these third party sites, moreover, it is clarified that other sites can link to the site with or without our authorization, and TELEXFREE can block any links to or from the Site.

12.3 - The use of third party sites shall occur exclusively at the expense and risk of the PROMOTER. That is to say, TELEXFREE through its employees, directors, agents, vendors or suppliers shall not be liable for any direct or indirect losses, including damages resulting from the use or incapacity of the third party links used.

13 - FINAL PROVISIONS

13.1 - TELEXFREE Network Marketing System reserves the right at any time to monitor, review, withhold and/or disclose any information, in order to comply with the applicable legislation, regulations, judicial proceeding or requirement of the competent authority.

13.2 - TELEXFREE, by its exclusive analysis, in keeping with timely and appropriate standards, may repurchase the PROMOTER'S 99TELEXFREE accounts, not, however, guaranteeing "face value" for the product, negotiating the price based on volume, demand and/or its own inventory.

13.3 - It is part of the policy of TELEXFREE Network Marketing System to respond promptly to complaints concerning intellectual property offenses. TELEXFREE shall promptly process and investigate complaints concerning infractions, taking the necessary measures pursuant to the terms of the other property laws that may apply, TELEXFREE shall take action immediately to remove or prevent access to any material subject to violation, as well as to any reference or link to the material subject to violation, also eliminating access for any subscribers and members who have been offenders.

13.4 - The information included in the TELEXFREE Network Marketing System or available thereby may contain inaccuracies or typographical errors, and it may undergo alterations; moreover, TELEXFREE and/or its respective suppliers, at any time and without the need to give prior notice, may make changes in any part of the System, including these terms of use, for which reason the PROMOTER undertakes to engage in ongoing review hereof.

13.5 - TELEXFREE Network Marketing System does not declare or guarantee that it shall not be interrupted, or that it shall be free of errors, that defects will be immediately corrected,

or that the system itself or the server that makes it available will be free of viruses or other harmful elements.

13.5.1 - It does affirm, however, that upon discovering any abnormality in its domain, it shall take the most urgent measures to regularize the situation.

13.6 - THE PROMOTER agrees to indemnify TELEXFREE and hold it harmless, along with any of its partners, subsidiaries and affiliates, as well as its offices, employees and staff, of any liability for any claims, lawsuits or losses and damages, including attorneys' fees, that may be claimed by third parties, due to or arising from their use of the TELEXFREE Network Marketing System, or conduct relating to same.

13.7 - The TELEXFREE NETWORK Marketing System reserves the right to alter the terms of use or guidelines concerning the use of the System at any time and without any need for prior notice, proceeding thereupon to publish an updated version on its website.

13.7.1 - THE PROMOTER is responsible for periodically reviewing the current content of the TELEXFREE site and of these GENERAL REGULATIONS since they may be altered, always subject to ample notification, after which alterations shall be considered tacitly accepted by those who have become members.

13.8 - Compliance with what is set forth in these GENERAL REGULATIONS by all parties at TELEXFREE is subject to the laws of the USA and the state of Nevada (With the exception of Louisiana Member/Promoters. Louisiana Promoters may choose Louisana Laws) and relevant legal procedures, and no provision thereof contravenes the right of TELEXFREE to comply with administrative or judicial requirements or orders imposed by the competent authorities, with regard to the use by the PROMOTER of the TELEXFREE Network Marketing System or the information provided by TELEXFREE, or collected by it as the result of such use, and if any provisions of this agreement are declared null or void in the light of the legislation in force, including, without limitation, provisions concerning exemption and limitation of the liabilities mentioned above, such null and void provisions shall be replaced by valid and effective provisions that respect the intention and purpose of the original provisions, with the remaining provisions of these Terms of use in full force and effect.

13.9 - Unless otherwise provided in this document, these GENERAL REGULATIONS constitute the entire agreement between the PROMOTER and TELEXFREE with relation to the use of the System itself, except with regard to the use of any software that may be governed by an end-user license agreement, and replaces any and all communications or proposals, prior or current, whether through electronic, spoken or written communication between the user and TELEXFREE with regard to the Market Network System.

13.10 - The printed version of this agreement and of any notification or notice delivered in electronic form shall be admissible in legal or administrative proceedings resulting from or related to these GENERAL REGULATIONS, and subject the same conditions as other documents and commercial records originally generated and maintained in hard copy.

13.11 - laws of the USA and the state of Nevada (With the exception of Louisiana Member/Promoters. Louisiana Promoters may choose Louisana Laws), is chosen to settle any issues arising from this instrument, with the express renunciation of any other now matter how privileged it may be, or may become, except for questions having to do with consumers, when

the jurisdiction or competency shall be established on the basis of what is provided in the Code of Consumer Protection.

13.12 - This version of this membership contract shall take effect starting February 10, 2013, rescinding any provisions of the previous membership agreement that may be at variance with this one.

Signature: the original copy of this agreement is signed.

TELEXFREE

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**

MOTION BY CHAPTER 11 TRUSTEE FOR ENTRY OF ORDER FINDING THAT DEBTORS ENGAGED IN PONZI AND PYRAMID SCHEME AND RELATED RELIEF

To the Honorable Melvin S. Hoffman, Chief United States Bankruptcy Judge:

Stephen B. Darr, the duly appointed Chapter 11 trustee (the "Trustee") of the bankruptcy estates of TelexFree, LLC, TelexFree, Inc., and TelexFree Financial, Inc. (collectively, the "Debtors"), respectfully requests entry of an order finding that the Debtors were engaged in a Ponzi/pyramid scheme and that such finding be applicable to all matters in these proceedings. The Trustee has filed simultaneously herewith the *Motion by Chapter 11 Trustee for Approval of Method of Service of Motion by Chapter 11 Trustee for Entry of Order Finding that Debtors Engaged in Ponzi and Pyramid Scheme and Related Relief* (the "Notice Motion") and the *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* ("Darr Affidavit").

In support of this motion (the "Motion"), the Trustee states as follows:

INTRODUCTION

The Debtors ostensibly operated a multi-level marketing company engaged in the sale of voice over internet service but, as detailed herein, the Debtors' operations actually were a massive Ponzi/pyramid scheme that ensnared as many as a million or more participants from multiple countries (hereinafter, parties who became members of the Debtors' scheme shall be referred to as "Participants"). Participants opened approximately 11,000,000 User Accounts (as hereafter defined) and purchased membership plans and/or Voice over Internet Protocol ("VoIP") service with a transaction value of approximately $3,070,000,000 during the approximately two years of the Debtors' operation of their scheme. An affiliate of the Debtors, Ympactus Comercial Ltda. ("Ympactus"), reportedly operated a substantially similar scheme in Brazil which was seized and shut down by the Brazilian authorities in June 2013.[1] Shortly after the Debtors' Chapter 11 filings in April 2014, the Securities and Exchange Commission and the Massachusetts Securities Division commenced litigation against the Debtors and others alleging, among other things, that the Debtors were engaged in the fraudulent sale of securities in violation of numerous securities laws. Contemporaneously therewith, substantially all of the Debtors' assets and records were seized by the federal authorities. Approximately two months later, on June 6, 2014, the Trustee was appointed.

The Trustee has conducted an extensive investigation into the operations of the Debtors' scheme and Participant involvement therein. As a result of the investigation, the Trustee has concluded that and requests a finding from the Court that the Debtors were engaged in a Ponzi/pyramid scheme, that any claim or portion of claim of Participants based upon accumulated credits arising from fictitious profits or commissions in Participants' User Accounts

[1] Reportedly, Ympactus was recently found by a Brazilian court to have been a Ponzi scheme.

as of the Petition Date should be disallowed, and that Participant claims should be determined on a "net equity" basis.

Simultaneously herewith, the Trustee has filed his *Motion by Chapter 11 Trustee for Entry of Order Fixing Bar Date for Filing Proofs of Claim, Approving Form and Manner of Notice, Directing that Claims be Filed Electronically, and Approving Content of Electronic Proofs of Claim (the "Bar Date Motion").* Pursuant thereto, the Trustee seeks, among other things, approval for the electronic noticing of a Bar Date and approval of the content of electronic proofs of claim to be filed by Participants (the "Participant ePOC") and non-Participants (the "Standard ePOC" and together, the "ePOCs").

I. CASE BACKGROUND AND PROCEDURAL POSTURE

1. On April 13, 2014 (the "Petition Date"), each of 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").

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

3. 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.

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

5. 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 (the "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 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 funds on deposit and 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.

6. 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.

7. 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.

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

9. 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.

10. On February 27, 2015, the Trustee 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 obtained from the Federal Authorities (as defined below).

11. Carlos Wanzeler and James Merrill were the Debtors' principals along with Carlos Costa, at least through Costa's alleged separation from 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 is believed to be in Brazil. Merrill was initially detained and has been released pending trial.

12. On February 3, 2015, the Trustee 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.

13. Prior to the Trustee's 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 his appointment, the Trustee 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. The Trustee has only had limited access to the Debtors' former employees.

14. Initially without access to the Debtors' books and records, the Trustee has utilized a variety of resources to obtain information regarding the Debtors' activities and the mechanics of their scheme. The Trustee filed 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").[2] 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. The Trustee also conducted informal interviews of certain former employees and consultants of the Debtors as well as several Participants.

A. Mechanics of Scheme and Methods of Compensation

15. The Debtors purported to be in the business of selling 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.

16. The Debtors ostensibly used a multi-level marketing plan, or "MLMP", to sell the VoIP Packages. An MLMP, also referred to as network marketing or referral marketing, is a direct sales strategy in which the sales force is compensated not only for sales they generate, but also for the sales generated by other sales persons that they recruit. *Whole Living, Inc. v. Tolman*, 344 F. Supp. 2d 739 (D. Utah 2004). MLMP businesses can be legitimate, and notable

[2] To date, the Trustee has deferred conducting depositions of the 2004 Motion deponents.

examples of MLMP's include Herbalife International (selling nutritional supplements, weight management, sports nutrition, and personal care products), Mary Kay, Inc. (selling cosmetics products), and Amway (selling, among other things, health, beauty, and home care products).

17. Each new distributor in an MLMP recruited by a participant, along with the recruited distributor's recruits (down to six levels in the Debtors' case), becomes part of the first participant's "network", sometimes referred to as the participant's "downline." Eventually one or more pyramid type structures is established underneath the recruiting participant. In addition to earning commission and profits on the products the participant sells, he or she is entitled to receive a commission based on the volume of products or memberships sold by his or her network.

18. Until the Debtors purported to change their MLMP contracts in an unsuccessful attempt to address the existing contract's illegality in March 2014, the Debtors provided Participants with two options (in addition to purchasing VoIP Packages) 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, for 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, for 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).

19. 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 AdCentral 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.

20. 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[3] 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.

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

21. 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.

22. 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 from the Debtors.

23. In the case of a Participant satisfying his/her own invoice 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 information entered by the recruited 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';

d. A Participant would 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 recruited 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.

24. Alternatively, a Participant could satisfy his/her own invoice directly by payment in cash to another Participant, who would, in turn, satisfy the invoice by a redemption of

accumulated credits. Thus, the recruited Participant's membership fee for TelexFree plan was paid to the recruiting Participant, rather than to the Debtors.

25. As set forth above, there are approximately 11,000,000 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.

26. Although some versions of Participant contracts contained prohibitions against Participants opening multiple User Accounts for themselves, 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 credits for themselves.

27. As noted above, a Participant could monetize accumulated credits by recruiting a Participant to join the Debtors' scheme and using his/her accumulated credits to satisfy the invoice for the later 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 to the recruiting Participant, and the Debtors redeemed the credits of the recruiting Participant in satisfaction of the invoice.

28. In fact, it was a regular practice of the Debtors' scheme that membership fees were paid by the use of accumulated credits rather than by cash. While invoices associated with the sale of membership plans or VoIP Packages had a face value of approximately $3,070,000,000, only $360,000,000, or approximately twelve percent (12%) of that amount, was paid in cash to the Debtors. The balance of these invoices was satisfied by the use of Participants' credits.

29. The Debtors also issued "manual credits" to certain User Accounts. 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, the Trustee is unable to identify any payment to the Debtors for a significant amount of manual credits that were issued to certain User Accounts. These credits issued without consideration appear to be a fraud within the larger fraud of the Ponzi/pyramid scheme. There also were exchanges of credits between User Accounts unassociated with the issuance and satisfaction of Debtor invoices.

B. SIG/Back Office

30. 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".[4]

31. 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 the Trustee to confirm Participant activity.

32. The Trustee's access to SIG was the culmination of a painstaking data recovery and analysis project implemented by the Trustee and his team of professionals with the assistance of investigators from HIS and the SEC.

33. Following the Trustee's appointment and beginning in August 2014, HSI provided copies of electronic information contained in the Debtors' computers and servers to the

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

Trustee. Once all of the data from the Debtors' computers and servers were obtained, the Trustee and his team "virtualized" (i.e., created a computer environment replicating the original configuration) the system following a multi-step process, since the Federal Authorities were in possession of the original servers.

34. Extensive testing was performed to determine that the appropriate configurations of the data were achieved. Data from 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 by the Trustee, communications with Federal 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.

35. The result was a working version of SIG, which enabled the Trustee and his professionals 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.

36. The Debtors' database was developed by programmers in Brazil and all field references are in Portuguese. The developers apparently lacked the expertise to create and manage a system of this magnitude. As a result, system modifications appear to have been done in a haphazard and disorganized fashion. In addition, the Debtors' system is permeated with unreliable data because of limited efforts at data validation of information provided by Participants in establishing User Accounts.

37. Despite all of these obstacles, as a result of the forensic efforts identified above, the Trustee and his 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.

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

39. Each User Account with the Debtors was registered with an electronic mail address (an "Email Address"). There are approximately 900,000 unique Email Addresses in SIG associated with approximately 11,000,000 Debtor User Accounts. The number of User Accounts associated with an Email Address varies widely. A particular Email Address may be associated with only 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 in excess of 1,000,000.

40. 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.

41. The Trustee and his team have taken a series of steps to confirm the accuracy and reliability of the transaction data reflected in SIG. The Trustee interviewed the Debtors' bookkeeper to understand the mechanics of SIG and how it was employed on a day to day basis. Testing was performed to reconcile balances and activity using available data, which is somewhat limited. This testing included cross-referencing data in related transactions and

conducting interviews with several Participants to confirm the accuracy of the SIG data as to their User Accounts. Based on the testing performed to date, SIG transaction data appears to have integrity and 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

42. In February 2012, Ympactus reportedly commenced operations in Brazil to operate a scheme substantially identical to the scheme that is described above. 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 Darr Affidavit, Exhibit "A",* at ¶51. 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 Darr Affidavit, Exhibit "A",* at ¶51.

43. 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. 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.[5]

[5]The Trustee is exchanging information with Brazilian authorities and is trying to develop a common protocol for administering claims and pursuing recoveries in the respective cases of Ympactus and the Debtors.

44. Upon information and belief, on or about September 21, 2015, the Brazilian court entered a decision finding that Ympactus operated a pyramid scheme.

45. Following the shutdown of Ympactus, the Debtors' cash receipts increased dramatically. The Debtors' cash receipts totaled approximately $200,000,000 in the last three full months of operation, with more than $96,000,000 in cash receipts in February 2014 alone. *See Darr Affidavit, Exhibit "A"*, at ¶53.[6]

46. The SIG system maintained by the Debtors and Ympactus operated with 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 Trustee's 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 Ympactus and the Debtors' Participants.

47. SIG includes more than 17,000,000 distinct User Accounts associated with approximately 2,000,000 Email Addresses for both the US-based and the Brazilian-based operations.

48. In creating a new User Account, each Participant was directed to identify whether such Participant would pay the initial invoices in Brazilian Reais ("Reais") or United States Dollars. Through a review of the currency field data, the Trustee 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;

[6] Attached as Exhibit 1 to the Darr Affidavit is a summary of cash receipts of the Debtors, by month, for the two years of operation of the scheme.

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.

49. The Trustee believes that the Debtors' User Accounts can be separated from Ympactus' User Accounts by the currency designation in the data fields as described above.

50. Utilizing the currency designation, it appears that approximately 11,000,000 User Accounts are associated with the Debtors' operations and approximately 4,000,000 User Accounts are associated with Ympactus operations and the remaining 2,000,000 User Accounts had no activity.

II. FINDING OF EXISTENCE OF PONZI AND PYRAMID SCHEME

51. The Debtors conducted a Ponzi/pyramid scheme, not a legitimate MLMP.

52. Pyramid schemes and Ponzi schemes share many similar characteristics and typically involve unsuspecting participants who are duped into paying money to join the scheme by unscrupulous operators promising extraordinary returns. In contrast to a legitimate investment, however, these types of schemes can only provide the promised returns if the number of participants continues to increase exponentially, as the money from later participants is the sole or primary source available to make payments to existing participants. *Webster v. Omnitrition Int'l, Inc.*, 79 F.3d 776, 781 (9th Cir. 1996); *United States v. Gold Unlimited, Inc.*, 177 F.3d 472, 479 (6th Cir. 1999); *In re First Commercial Mgmt. Grp., Inc.*, 279 B.R. 230, 232

(Bankr. N.D. Ill. 2002); *Rieser v. Hayslip (In re Canyon Sys. Corp.)*, 343 B.R. 615, 630 (Bankr. S.D. Ohio 2006); *Sec. Investor Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, 531 B.R. 439, 470 (Bankr. S.D.N.Y. 2015).

53. A Ponzi scheme is generally based upon a fraudulent investment opportunity. Typically, investors contribute funds to the organizer who promises a high return. Existing investors are paid their returns almost exclusively from the funds contributed by new investors and not from the legitimate profits of the business. *Bear, Stearns Secs. Corp. v. Gredd (In re Manhattan Inv. Fund Ltd.)*, 397 B.R. 1, 8 (S.D.N.Y. 2007); *Eberhard v. Marcu,* 530 F.3d 122, 132 n.7 (2d Cir. 2008); *accord In re Bernard L. Madoff Inv. Secs. LLC*, 654 F.3d 229, 232 (2d Cir. 2011), *cert. denied*, 133 S. Ct. 25 (2012); *see United States v. Moloney*, 287 F.3d 236, 242 (2d Cir. 2002) ("A Ponzi scheme by definition uses the purportedly legitimate but actually fraudulently obtained money to perpetuate the scheme, thus attracting both further investments and, in many cases, new investors to defraud."), *cert. denied*, 537 U.S. 951 (2002).

54. Some courts have discussed a four factor test to determine whether a Ponzi scheme exists: 1) deposits were made by investors; 2) the debtor conducted little or no legitimate business operations as represented to investors; 3) the purported business operation of the debtor produced little or no profits or earnings; and 4) the source of payments to investors was from cash infused by new investors. *Armstrong v. Collins*, 2010 WL 1141158, at *22 (S.D.N.Y. Mar. 24, 2010)(quoting *Forman v. Salzano (In re Norvergence, Inc.)*, 405 B.R. 709, 730 (Bankr. D.N.J. 2009)(quoting *In re Canyon Sys. Corp.*, 343 B.R. at 630); *accord Carney v. Lopez*, 933 F. Supp. 2d 365, 379 (D. Conn. 2013); *Wiand v. Waxenberg*, 611 F. Supp. 2d 1299, 1312 (M.D. Fla. 2009); *Kapila v. TD Bank, N.A. (In re Pearlman)*, 440 B.R. 900, 904 (Bankr. M.D. Fla. 2010); *Floyd v. Dunson (In re Ramirez Rodriguez)*, 209 B.R. 424, 431 (Bankr. S.D. Tex. 1997).

55. Other courts have identified badges that weigh in favor of finding a Ponzi scheme, including the absence of any legitimate business connected to the investment program, the unrealistic promises of low risk and high returns, commingling of investor money, the use of agents and brokers that are paid high commissions to perpetuate the scheme, misuse of investor funds, the "payment" of excessively large fees to the perpetrator and the use of false financial statements. *See In re Dreier LLP,* 2014 WL 47774, at p. 9 (Bankr. S.D.N.Y. 2014). These badges are, however, merely characteristics of many Ponzi schemes but a Ponzi scheme can exist without all of them. *Id.* At bottom, the label Ponzi scheme applies "to any sort of inherently fraudulent arrangement under which the debtor-transferor must utilize after-acquired investment funds to pay off previous investors in order to forestall disclosure of the fraud." *In re Manhattan Inv. Fund*, 397 B.R. at 12 (quoting *Bayou Superfund v. WAM Long/Short Fund II, L.P. (In re Bayou Group, LLC)*, 362 B.R. 624, 633 (Bankr. S.D.N.Y. 2007) ("Bayou I")); *see Armstrong*, 2010 WL 1141158 at * 23 ("[E]ven assuming Yagalla did not promise or represent high rates of return, this does not mean that he was not running a Ponzi scheme. 'Case law has revealed that a clever twist on the Ponzi concept will not remove a fraudulent scheme from the definition of Ponzi.'") (quoting *In re Norvergence*, 405 B.R. at 730).

56. A pyramid scheme is generally characterized by a participant's payment to an MLMP operator in return for which participants receive the right to sell a product and the right to receive rewards for recruiting other participants substantially unrelated to the sale of product to ultimate users. *Webster*, 79 F.3d at 781(*quoting In re Koscot Interplanetary, Inc.*, 86 F.T.C. 1106 (1975)).

57. A pyramid scheme is a type of Ponzi scheme in that, in both instances, the scheme can only be sustained by the continued influx of new investors/participants to fund amounts

needed to be paid to earlier investors/participants. A Ponzi scheme generally involves only a direct, linear relationship between the owner of the scheme and the investors. The pyramid scheme, however, has two additional elements: the ostensible right to sell a product, and the payment to participants for the recruitment of new participants, thereby creating the pyramid structure.

58. An MLMP is a direct sales strategy in which members are compensated not only for sales the members generates, but also for the sales generated by other members that they recruit. Whether an MLMP operates as a pyramid scheme is determined by how it functions in practice. *Whole Living*, 344 F. Supp. 2d at 745. A lawful MLMP is distinguishable from a pyramid scheme in that the primary purpose of the enterprise and its associated individuals is to sell or market an end-product to end-consumers, and not to reward associated individuals for the recruitment of more participants. *Federal Trade Commission v. SkyBiz.com, Inc.*, 2001 WL 1673645, at *28 (N.D. Okla. Aug. 31, 2001).

59. The Debtors' compensation scheme had elements of both a Ponzi and pyramid scheme.

60. Participants who purchased an Ad Central or Ad Central Family Plan received the right to generate commissions for the sale of certain VoIP Packages but also were able to receive exceedingly high returns on their investments merely by placing meaningless, pre-drafted advertisements on selected websites without the requirement of selling any product. This guaranteed return on initial investment is a hallmark of a Ponzi scheme.

61. 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 with TelexFree 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 for $1,425 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 with TelexFree for $100 weekly for 52 weeks, for a return of 265% on the initial investment.

62. 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; 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

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

64. 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.

65. 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.

66. While there were certain provisions of the Debtors' MLMP that ostensibly required the sale of VoIP Packages as a requirement for receiving credits with TelexFree, the credits that could be generated for those activities were relatively insignificant and the requirements were easily circumvented by Participants.[7]

67. The Debtors had $360,000,000 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 these 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.

68. 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

[7] While 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, as discussed above, VoIP Packages were rarely sold to third parties.

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.[8]

69. A pyramid scheme exists where payments to participants are based upon recruitment of additional participants, largely or wholly unrelated to product sales. *See Webster*, 79 F.3d at 782 (MLMP which is based principally on recruitment of new participants, as opposed to sale of the end product or service, and where product sales are an insignificant portion of the enterprise's total revenues, constitutes a pyramid scheme); *Gold Unlimited, Inc.*, 177 F.3d at 481 (company grossed $552,620 from sales of products yet took in $43,000,000); *Stull v. YTB Int'l, Inc.*, 2011 WL 4476419, at *5 (S.D. Ill. Sept. 26, 2011) (approximately 73% of cash receipts were from membership fees and not from the sales of product); *Federal Trade Commission v. Burnlounge, Inc.*, 753 F.3d 878, 888 (9th Cir. 2014)(existence of negligible amount of sales unrelated to commission opportunity does not negate evidence that commissions were the primary draw of the scheme); *In re Holiday Magic, Inc.*, 84 F.T.C. 748, 1028-30 (1974)(pyramid scheme existed where rewards were paid to participants when they recruited others, and recruits also had to purchase product).

70. 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, which is perhaps the chief hallmark of a Ponzi/pyramid scheme. *Webster*, 79 F.3d at 781; *United States v. Grasso*, 173 F. Supp. 2d 353, 357 (E.D. Pa. 2001)(all Ponzi and pyramid schemes are destined to collapse

[8] This estimate is based upon joint usage of the Debtors' and Ympactus' VoIP service for the period July 2012 through June 2013 as well as usage of only the Debtors' VoIP service from July 2013 to April 2014. Ernst & Young ("E&Y"), the consultants retained by the court in the Brazilian action, made similar findings as to use of the VoIP Packages. As part of its 220 page report issued in February 2015, E&Y also found that for the period July 2012 to June 2013, less than one percent of total VoIP Package minutes sold were actually used.

because of saturation which is the point at which investments by later participants are inadequate to sustain the scheme).

71. A calculation of the Debtors' twelve month trailing liability, that is, the amount that would be owed to Participants in 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 to the *Darr Affidavit* 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.[9] 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.[10] The unsustainability of the Debtors' MLMP is another hallmark of a Ponzi and pyramid scheme. *See Kerrigan v. ViSalus, Inc.*, 2015 WL 3679266, at *8 (E.D. Mich. June 12, 2015); *Webster*, 79 F.3d at 782; *People v. Sweeney*, 228 Cal. App. 4th 142, 152 (Oct. 15, 2014); *see also Wiand v. Lee*, 753 F.3d 1194, 1201 (11th Cir. 2014)(fact that compensation under an MLMP is almost completely dependent upon membership fees paid by new participants, and not from product sales, is a hallmark of a Ponzi/pyramid scheme).

[9] While one provision of one version of the Participant contracts ostensibly did not require the Debtors to redeem VoIP Packages issued to Participants, this contractual provision is completely undermined by the unequivocal statements in marketing materials and the Debtors' actual practice of paying the guaranteed return on investment without the need to sell any product.

[10] In its report, E&Y similarly found that the TelexFree MLMP was unsustainable. E&Y prepared income and loss projections for TelexFree over a thirty-six (36) month period using various assumptions. The projections reflect that under each set of assumptions, the projected payouts exceed projected revenue from the sale of product, in many instances by $4,000,000,000 to $5,000,000,000 over the 36 month term.

III. BECAUSE THE DEBTORS OPERATED A PONZI/PYRAMID SCHEME, CLAIMS FOR ACCUMULATED CREDITS SHOULD BE DISALLOWED.

72. The accumulated credits held by Participants in their User Accounts as of the Petition Date should not form the basis of allowed claims in these cases.

73. Claims based on the accumulated credits should be disallowed because, in a Ponzi/pyramid scheme, investors who had no knowledge that the scheme was fraudulent are generally entitled to a claim only for the net amounts invested in the scheme and not for fictitious profits.[11] *See In re Bernard L. Madoff Inv. Sec. LLC*, 654 F.3d at 242; *Donell v. Kowell*, 533 F.3d 762, 772 (9th Cir. 2008); *SIPC v. BLMIS*, 499 B.R. 416, 424-29 (S.D.N.Y. 2013); c*ompare In re Churchill Mortgage Inv. Corp.*, 256 B.R. 664, 682 (Bankr. S.D.N.Y. 2000); *In re First Commercial Mgmt Grp.*, 279 B.R. at 232; *with Bayou I* at 637-38; *In re Randy*, 189 B.R. 425, 441 (Bankr. N.D. Ill. 1995); *In re Int'l Loan Network, Inc.*, 160 B.R. 1, 12 (Bankr. D.D.C. 1993); *see also Janvey v. Golf Channel, Inc.* 780 F.3d 641 (5th Cir. 2015) (vacated and certified to the Supreme Court of Texas on this issue, *Janvey v. Golf Channel, Inc.*, 792 F.3d 539 (5th Cir. 2015), *certified question accepted* (July 17, 2015)); *Janvey v. Alguire*, 2013 WL 2451738 at *9 (N.D. Tex. 2013); *SEC v. Bernard L. Madoff Investment Securities, LLC (In re Madoff)*, 522 B.R. 41, 47 (Bankr. S.D.N.Y. 2014) ("*BLMIS II*"); *In re Taubman*, 160 B.R. 964, 980 (Bankr. S.D. Ohio 1993); *In re Bayou Grp., LLC*, 439 B.R. 284, 309 (S.D.N.Y. 2010) ("*Bayou II*").

74. Innocent investors have claims against Ponzi/pyramid schemes based in tort under the theories of rescission and restitution for the amounts they were fraudulently induced to invest. *Scholes v. Lehmann*, 56 F.3d 750, 757 (7th Cir. 1995); *Bayou II* at 309; *see also In re Int'l Mgmt. Assoc., LLC, et al.*, 2009 WL 6506657 at *9 (Bankr. N.D. Ga., Dec. 1, 2009). These

[11] This motion seeks a determination that accumulated credits as of the Petition Date should not be considered in calculating allowed claims. Aside from the disallowance of credits, the transactions that should be included in the calculation of Participants' allowed claims in these cases will be subject to separate determination of the Court.

tort claims should be reduced by amounts the Participants received from the scheme. *See In re M & L Bus. Mach. Co.*, 84 F.3d 1330, 1341 (10th Cir. 1996); *In re United Energy Corp.*, 944 F.2d 589, 595 (9th Cir. 1991); *In re Bernard L. Madoff Inv. Sec. LLC,* 424 B.R. 122 (Bankr. S.D.N.Y. 2010).

75. Innocent investors in a Ponzi/pyramid scheme should not have a claim for interest or profits beyond their initial investment because such claims are based on the fictitious profits of the scheme. *BLMIS I* at 427-29; *BLMIS II* at 47; *Scholes* 56 F.3d at 757.

76. The accumulated credits based on the posting of meaningless advertisements are equivalent to the fictitious profits promised in Ponzi schemes. The Participants were guaranteed an astronomical return by merely purchasing a membership plan and posting internet advertisements reportedly supplied by the Debtors. Participants were not required to sell a product to receive payment. Accordingly, claims based on the accumulated credits for the posting of advertisements should be disallowed. *See BLMIS I* at 427-29; *BLMIS II* at 47; *Scholes* 56 F.3d at 757; *M & L Bus. Mach. Co.*, 84 F.3d at 1341.

77. The accumulated credits based on the recruitment of later Participants should also be disallowed because the recruitment activity only contributed to and perpetuated the Debtors' scheme and provided no value to the Debtors' estates. 11 U.S.C. § 502(b)(1); *See In re Vaughan Co. Realtors*, 500 B.R. 778, 794 (Bankr. D.N.M. 2013); *Warfield v. Byron*, 436 F.3d 551, 560 (5th Cir. 2006); *In re Taubman*, 160 B.R. at 980; *Janvey*, 2013 WL 2451738 at *9; *Randy*, 189 B.R. at 441; *In re Independent Clearing House Co.*, 77 B.R. 843, 857 (Bankr. D. Utah 1987).

78. While value arguably may be provided by an innocent third party providing legitimate services to a Ponzi/pyramid operator for a reasonable fee, such is not the case here. Rather, credits that were issued to Participants for recruiting others into the scheme only

perpetuated it and deepened the pool of defrauded investors. *Compare In re Churchill Mortgage Inv. Corp.*, 256 B.R. at 682; *First Commercial Mgmt Grp.*, 279 B.R. at 232; *with Bayou I* at 637-38; *Randy*, 189 B.R. at 438-39; *In re Int'l Loan Network, Inc.*, 160 B.R. at 12; *see also* Janvey, 780 F.3d at 641.

79. Because the Debtors received no value for the accumulated credits, claims based on such credits should be disallowed. *See 11 U.S.C. §502(b)(1); Independent Clearing House*, 77 B.R. at 857; *Warfield*, 436 F.3d at 560; *Johnson v. Home State Bank*, 501 U.S. 78, 86, 11 S.Ct. 2150, 2155 (1991); *In re Muller*, 479 B.R. 508, 515 (Bankr. W.D. Ark. 2012).

80. Claims based on the accumulated credits should also be disallowed on equitable grounds, which are applicable in resolving claims allowance and distribution issues in Ponzi and pyramid scheme cases. *See Cunningham v. Brown*. 265 U.S. 1(1924); *Abrams v. Eby (In re Young)*, 294 F. 1, 4 (4th Cir. 1923); *In re Taubman*, 160 B.R. at 980; *Int'l Loan Network*, 160 B.R. at 14; *BLMIS II* at 47.

81. Equity requires the disallowance of claims for accumulated credits because these credits could only be satisfied from amounts paid by later Participants and not from earnings of the enterprise or from the sale of product. *See In re Taubman*, 160 B.R. at 980; *BLMIS I* at 427-29.

82. In reality, there are no profits to be paid out of such a scheme. *In re Young*, 294 F. at 4. As one court put it, "if a person invests money with the understanding that he will share in the profits produced by his investment, and it turns out that there are no profits, it is difficult to see how that person can make a claim to receive any more than the return of his principal investment." *Lustig v. Weisz & Assoc., Inc.*, 2002 WL 32500567 at *8 (June 21, 2002 W.D.N.Y.).

83. When a Ponzi or pyramid scheme collapses, insufficient funds remain to make distributions to later investors equal to the principal amounts they invested, such that recognition of claims for false profits would be inequitable to investors who have not and will not recover their principal investment. *In re Taubman*, 160 B.R. at 980.

84. Recognizing claims based on the accumulated credits would result in favoring Participants who were involved early in the scheme over those that invested later, since the earlier Participants had more time to accumulate the credits. *See In re Young*, 294 F. at 4 (recognizing that allowing a claim for both false profits and the original investment would not be equitable as profits had come at the expense of innocent investors). The Court should therefore disallow the claims based on the accumulated credits under its equitable powers. *Id.*; *see also Official Cattle Contract Holders Comm. v. Commons (In re Tedlock Cattle Co.)*, 552 F.2d 1351, 1353 (9th Cir. 1977).

85. Accordingly, any claim or portion of claim of Participants based upon the accumulated credits in Participants' User Accounts as of the Petition Date should be disallowed.

IV. COMPUTATION OF NET ALLOWED CLAIM OF PARTICIPANTS

86. In resolving claims and distribution issues in Ponzi and pyramid scheme cases, equitable considerations need to be taken into account to properly address the harms suffered by participants in the scheme. *See Cunningham,* 265 U.S. at 13 (all investors in a Ponzi scheme must be treated equally and that "equality is equity and this is the spirit of the bankrupt law"); *In re Young*, 294 F. at 4; *In re Taubman*, 160 B.R. at 980; *Int'l Loan Network*, 160 B.R. at 14; *BLMIS II* at 47. In order to fashion an equitable result, claims in such cases are determined based upon a "Net Equity" analysis, that is, the allowed claim is equal to amounts that a participant paid into the scheme, reduced by amounts a participant received from the scheme.

See, e.g., CFTC v. Topworth Int'l Ltd., 205 F.3d 1107, 1115-16 (9th Cir. 2000); *In re Bernard L. Madoff Inv. Sec. LLC*, 654 F.3d at 242; *Donell*, 533 F.3d at 772; *In re Tedlock Cattle Co.*, 552 F.2d at 1353; *In re Young*, 294 F. at 4; *BLMIS I* at 427-29; *Janvey*, 2013 WL 2451738 at *9; *Bayou II at* 309; *BLMIS II* at 47; *In re Old Naples Sec., Inc*., 311 B.R. 607, 616-17 (M.D. Fla. 2002). The transfers between a Participant and the Debtors must therefore comprise one component of the Net Equity determination.

87. The Debtor's scheme has elements of both a Ponzi scheme and a pyramid scheme. It is a Ponzi scheme in that Participants were guaranteed an exorbitant return on their initial investment, without the need to sell any product, which was funded from the fees paid by later Participants (since the Debtors had no legitimate business operations or earnings). *See e.g. In re Manhattan Investment Fund Ltd*., 397 B.R. at 8; *Eberhard* 530 F.3d at 132 n.7; *accord In re Bernard L. Madoff Inv. Secs. LLC*, 654 F.3d at 232. It is a pyramid scheme in that Participants had the right to receive commissions for recruiting Participants and to retain membership fees paid by those Participants. *See e.g. Whole Living*, 344 F. Supp. at 745. The Debtors created an artificial currency in the form of the VoIP Packages and credits. The principal vehicle for monetizing those credits was through the recruitment of Participants and the implementation of Triangular Transactions. Accordingly, the Triangular Transactions need to be taken into account in determining Net Equity.

88. In determining Net Equity, the recruited Participant should have a claim recognized in the bankruptcy cases for the amounts advanced to a recruiting Participant in a Triangular Transaction. Recognition of this claim is necessary to achieve an equitable result. A substantial number of those who joined the Debtors' scheme did so through participation in Triangular Transactions. The claims of these Participants should be treated the same as the

claims of Participants who paid their membership fees to the Debtors. Those later Participants who invested in the Debtors through Triangular Transactions were often at the bottom of the pyramid and were the least likely to know of the suspect nature of the Debtors' scheme. Equitable considerations require recognition of those claims to achieve a just result. *Cunningham,* 265 U.S. at 13.

89. Recognition of the claim of the later Participant in a Triangular Transaction necessitates that the claim of the earlier Participant be reduced for amounts paid to him/her by the later Participant. Otherwise, the Triangular Transaction would result in an increase in aggregate claims against the Debtors' estates even though the membership fees were retained by the recruiting Participant. If the recruiting Participant's claim is not so reduced, the calculation of the recruiting Participant's Net Equity will be overstated, thereby diminishing the recovery for other Participants. This obviously results in an inequitable outcome, perverts the distribution process, and disregards the mechanics of the scheme.

90. Recognizing the Triangular Transactions in the calculation of Net Equity of a Participant who used accumulated credits to purchase new membership plans for himself/herself through multiple User Accounts achieves a fair result as well. No cash was exchanged through these intra-Participant transactions, and there should be no claim in the bankruptcy estate on account of them. The Participant's claim for the purchase of a membership plan in one User Account will be offset by the reduced claim in the other User Account.

91. Recognizing the claim of later Participants and reducing the claim of earlier Participants reflects the economic realities of the Triangular Transactions. The substance of a transaction should prevail over its form when determining how the transaction relates to the rights of parties in a bankruptcy case. *See, e.g., In re PCH Assocs*., 949 F.2d 585, 597 (2d Cir.

1991) (*citing Pepper v. Litton*, 308 U.S. 295, 304 (1939)); *In re Adelphia Communications Corp.*, 512 B.R. 447 (Bankr. S.D.N.Y. 2014)(series of transactions may be treated as single transaction when it appears that, despite formal structure erected and labels attached, the segments comprise a single integrated scheme when considering knowledge and intent of parties involved in transaction).

92. The collapsing of transactions into an integrated transaction has been employed in varying contexts. In the case of leveraged buyouts, payments made by an acquirer to selling shareholders are considered to be transfers of estate property even though the funds were not paid directly by the debtors. *See, e.g, In re Chas P. Young Company*, 145 B.R. 131 (Bankr. S.D.N.Y. 1992); *In re OODC, LLC,* 321 B.R. 128 (Bankr. D. Del. 2005); *United States v. Tabor Court*, 803 F.2d 1288 (3rd Cir. 1986) (*cert. den. McClellan Realty Co. v. United States*, 483 U.S. 1005, 107 S. Ct. 3229 (1987)); *Wieboldt Stores v. Schottenstein*, 94 B.R. 488 (N.D. Ill. 1988); *In re O'Day Corporation*, 126 B.R. 370 (Bankr. D. Mass. 1991); *In re Jevic Holding Corp.*, 2011 WL 4345204 (Bankr. D. Del. 2011). Similarly, payments made by a purchaser of a debtor's assets to certain of the debtor's creditors are considered to have been made from property of the estate when the payment would have otherwise been part of the purchase price for the assets. *See, e.g., Warsco v. Preferred Technical Group*, 258 F.3d 557, 568-69 (7th Cir. 2001); *In re Food Catering & Housing, Inc.,* 971 F.2d 396 (9th Cir. 1992). The same rationale applies for collapsing the components of the Triangular Transaction to reflect the economic realities of the Debtors' scheme.

93. Collapsing the Triangular Transactions into one justifies the inclusion of the Triangular Transactions in the determination of Net Equity because the membership fees exchanged between Participants constituted property of the estate. The definition of property of

the bankruptcy estate is broad, encompassing all legal or equitable interests of the Debtors in property as of the commencement of the case. *See 11 U.S.C. §541; United States v. Whiting Pools Inc.*, 462 U.S. 198, 205 n. 9 (1983); H.R. Rep. No. 95-595 p. 367 (1977); S. Rep. No. 95-989, P. 82 (1978), U.S. Code Cong. & Admin. News 1978, pp. 5869, 6323. In the Triangular Transaction, the later Participant effectively paid the membership fee to the Debtors and the Debtors became liable to the later Participant for the guaranteed return. For the reasons set forth, the later Participant should have a claim in the bankruptcy cases for the amount of the membership fee. The Debtors, in turn, effectively paid the membership fee to the recruiting Participant in exchange for the redemption of credits. This payment by the Debtors to the recruiting Participant requires the reduction of the recruiting Participant's claim. To the extent recruiting Participants received more from the scheme than they invested, the Bankruptcy Code's avoidance actions provide the method to ensure equality of distribution among Participants.

94. Based upon the foregoing, the Net Equity claim of Participants should be determined as follows: the amount invested by the Participant into the Debtors' scheme, including amounts paid by the Participant pursuant to the Triangular Transactions, less amounts received by the Participant from the Debtors' scheme, including amounts received by the Participant pursuant to the Triangular Transactions.

95. The Net Equity determination will be made on a User Account basis. Many Participants appear to have maintained multiple User Accounts. In these circumstances, determination of the Net Equity for a Participant will require an aggregation of the transactions for such Participant in all of his/her User Accounts to ensure that all activity associated with that Participant has been accounted for.

V. THE DEBTORS ARE JOINTLY LIABLE FOR PARTICIPANT CLAIMS

96. 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.

97. 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 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.

98. 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.

99. The concerted actions of the Debtors in developing, marketing, and operating the Ponzi and pyramid scheme renders them jointly and severally liable for the claims of Participants. *See Aetna Cas. Sur. Co. v. P&B Autobody*, 43 F.3d 1546, 1564 (1st Cir. 1994)(joint tortfeasors can be vicariously liable for the acts of one another if there exists concerted action to commit the torts; liability requires first, "a common design or an agreement between two or more persons to do a wrongful act and, second, proof of some tortious act in furtherance of the agreement." *Id.; Restatement (Second) of Torts §876 cmt. b (1977).*

100. After the seizure and shutdown of Ympactus by the 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.

101. TelexFree Financial rendered substantial assistance to TelexFree, LLC and TelexFree, Inc. in furtherance of the Ponzi and pyramid scheme and is therefore also jointly liable to Participants as a joint tortfeasor. *See Kurker v. Hill*, 44 Mass. App. Ct. 184, 189 (Mass. App. 1998)(joint tortfeasor liability, also referred to as civil conspiracy, arises when a party knows that the "conduct [of another person] constitutes a breach of duty and gives substantial assistance or encouragement to the other to so conduct himself." TelexFree Financial, being under common ownership with TelexFree, LLC and TelexFree, Inc. had full knowledge of the actions being perpetrated by the other Debtors. *Kurker*, 44 Mass. App. Ct. at 189*; Kyte v. Philip Morris Inc.*, 408 Mass. 162 (1990); *Stock v. Fife*, 13 Mass. App. Ct. 75, 82 (Mass. App. 1982)(key to joint tortfeasor liability is the rendering of substantial assistance, with the knowledge that such assistance is contributing to a common tortious plan.)

102. The Debtors had a common design or agreement to commit a wrongful act, which was the establishment and implementation of the Ponzi and pyramid scheme. Because the

Debtors engaged in a common enterprise to further their tortious plan, the Debtors are jointly and severally liable for the allowed claims of Participants.

103. Inasmuch as the Debtors are jointly and severally liable for the claims of Participants, the Bar Date Motion proposes that Participants submit only one Participant ePOC, which shall constitute a claim against all three of the Debtors' estates. The Bar Date Motion does propose that non-Participants file a separate Standard ePOC for each Debtor against whom a claim is asserted.

104. A finding of joint and several liability for the claims of Participants does not effect a substantive consolidation of the Debtors' estates. Grounds may exist for the Trustee to seek substantive consolidation of the Debtors' estates and the Trustee reserves the right to seek same. In the event of substantive consolidation, Participants having submitted a Participant ePOC will have a single claim against the consolidated estate.

V. NOTICE

105. The Trustee has filed simultaneously herewith the Notice Motion to prescribe the form and manner for providing notice of the Ponzi Motion to interested parties.

WHEREFORE, the Trustee respectfully requests that this Court enter an Order:

(i) Finding that the Debtors operated a Ponzi and pyramid scheme;

(ii) Ordering that any claim or portion of claim of Participants based upon accumulated credits in Participants' User Accounts as of the Petition Date shall be disallowed, and that claims should be determined on a "Net Equity" basis as described herein;

(iii) Ordering that the Debtors shall be jointly and severally liable for the claims of Participants;

(iv) Ordering that the findings made pursuant to this Motion shall be applicable throughout these proceedings, for all purposes; and

(v) Granting such other and further relief as this Court finds just and proper.

STEPHEN B. DARR,
CHAPTER 11 TRUSTEE,

By his attorneys,

/s/ Andrew G. Lizotte

Harold B. Murphy (BBO #362610)
Andrew G. Lizotte (BBO #559609)
Murphy & King, Professional Corporation
One Beacon Street
Boston, MA 02108
Telephone: (617) 423-0400
Facsimile: (617) 423-0498
Email: ALizotte@murphyking.com

Dated: October 7, 2015
696114

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.

---

[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.

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**

SUPPLEMENTAL ORDER RESPECTING MOTION BY CHAPTER 11 TRUSTEE FOR ENTRY OF ORDER FINDING THAT DEBTORS ENGAGED IN PONZI AND PYRAMID SCHEME AND RELATED RELIEF

PROCEDURAL BACKGROUND

1. On October 7, 2015, Stephen B. Darr, the duly appointed Chapter 11 trustee (the "Trustee") of the bankruptcy estates (the "Estates") of TelexFree, LLC, TelexFree, Inc., and TelexFree Financial, Inc. (collectively, the "Debtors") filed a *Motion for Entry of an Order Finding that the Debtors Engaged in a Ponzi and Pyramid Scheme and Related Relief* (the "Ponzi Motion") and a *Motion by Chapter 11 Trustee for Approval of Method of Service of Motion by Chapter 11 Trustee for Entry of Order Finding that Debtors Engaged in Ponzi and Pyramid Scheme and Related Relief* (the "Notice Motion").

2. On October 14, 2015, the Court approved the Notice Motion, prescribing service of the Ponzi Motion, and scheduled an evidentiary hearing for November 24, 2015. The Trustee served the Ponzi Motion and hearing notice in compliance with the order approving the Notice Motion on or about October 19, 2015.

3. After conducting the evidentiary hearing, the Court made partial rulings on the Ponzi Motion by order dated November 25, 2015, as amended on December 21, 2015. The

Court then scheduled a continued hearing on the Ponzi Motion for January 26, 2016 to consider the balance of the relief sought. The Court directed that the Trustee provide supplemental notice of the Ponzi Motion and continued hearing notice to parties-in-interest.

4. The Trustee provided supplemental notice to Participants of the continued hearing and the additional relief sought on or about December 7, 2015. On or about such date, the Trustee filed a copy of the supplemental notice of the Ponzi Motion and filed a certificate of service.

ORDER

5. The Court, having conducted the continued hearing on the Ponzi Motion, upon the evidence submitted and the arguments of counsel made at the hearings, and the Court having reviewed all documents in connection with the Ponzi Motion, including the *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* ("Darr Affidavit"), and notice of the Ponzi Motion having been given to all parties in interest in accordance with the order dated October 14, 2015; and supplemental notice of the Ponzi Motion and continued hearing having been given on or about December 7, 2015; and the Court having considered the oppositions filed, notice of the Ponzi Motion being sufficient; and after due deliberation and consideration of all of the foregoing, and sufficient cause appearing therefor, the Court hereby orders that:

(i) In determining the amount of claims of Participants,[1] any claim or portion of claim based upon accumulated credits in a Participants' User Accounts as of the Petition Date shall be disallowed;

(ii) The claims amounts of Participants shall be determined on a Net Equity basis, which shall be defined as follows: the amount invested by the Participant into the

[1] All terms not otherwise defined herein shall have the meaning ascribed to them in the Ponzi Motion.

Debtors' scheme, including amounts paid pursuant to Triangular Transactions, less amounts received by the Participant from the Debtors' scheme, including amounts received pursuant to Triangular Transactions.

(iii) In determining the amount of a claim of a Participant who has more than one User Account, the activity in all of the Participants' User Accounts shall be aggregated and netted against one another;

(iv) The calculation of a Participant's claim using the Net Equity basis is without prejudice to the Trustee's right to object to the claim of a Participant who had knowledge that the Debtors were engaging in a fraudulent scheme and is therefore not entitled to the claims afforded innocent Participants;

(v) The relief granted herein is appropriately made by motion and does not require the institution of an adversary proceeding; and

(vi) The foregoing findings and conclusions shall be applicable for all purposes in these proceedings.

Dated: January 26, 2016

Honorable Melvin S. Hoffman
Chief United States Bankruptcy Judge

UNITED STATES DISTRICT COURT
DISTRICT OF MASSACHUSETTS

In re:
TelexFree Securities Litigation

Case No. 14-MD-02566-TSH

BEFORE: The Honorable Timothy S. Hillman

Motion Hearing

United States District Court
Courtroom No. 2
595 Main Street
Worcester, Massachusetts
December 11, 2015

Marianne Kusa-Ryll, RDR, CRR
Official Court Reporter
United States District Court
595 Main Street, Room 514A
Worcester, MA 01608-2093
508-929-3399 justicehill@aol.com
Mechanical Steno - Transcript by Computer

MR. BENNETT: It would leave January 26th still on, but the question then comes in as whether or not -- how do I treat your allowance -- how does the Court treat your allowance of the motion to amend? Are you making any substantive findings with respect to their rights to proceed? Are you making any substantive findings with respect to the claims by the trustee that this violates the stay?

09:28:54AM

THE COURT: Why wouldn't I just -- well, all right. Okay.

MR. BENNETT: And so, I mean, I would want to be heard if the Court allowed me to intervene on that basis that they should not be allowed to proceed on that -- on that action.

09:29:05AM

THE COURT: Actually, let's stay with intervention and then we can talk about what goes after that.

MR. BENNETT: All right. So, your Honor, that is the motion, the reason for requesting to intervene is to seek basically a stay of your ruling on the motion to amend until Judge Hoffman rules.

09:29:17AM

THE COURT: Thank you.

MR. BENNETT: Thank you, your Honor.

09:29:27AM

THE COURT: Who has got this for the plaintiffs? Mr. Baldiga?

MR. BALDIGA: Thank you, your Honor. And good morning. For the record, William Baldiga, Brown, Rudnick, co-counsel for the plaintiff victims here.

09:29:42AM

Your Honor, this is one of those many instances where the intersections between an ongoing MDL and bankruptcy proceedings can have rough edges. This is admittedly one. It's -- it is procedurally somewhat difficult, and unfortunately here it will -- it does present to the federal courts, and we'll -- we'll see in time which federal court decides a very difficult issue because of one of first impression as to the issue of property of the estate, which does need to be decided.

09:30:26AM Some things we don't disagree on with Mr. Bennett. There should be a court that decides that issue. The trustee has elected here to file papers both before Judge Hoffman and here. It has caused some, we think, needless confusion and expense. We -- we think we have -- we do agree that one court 09:30:55AM should decide that issue. Whichever court -- and if -- if that is Judge Hoffman, and it appears that Judge Hoffman is prepared to take that issue on, we don't oppose Judge Hoffman deciding that issue. We actually think that in the first instance at least issue of what is property of the bankruptcy estate and 09:31:13AM the extent of the bankruptcy stay is one that is well-suited especially to a bankruptcy judge, not that this court couldn't do it, and judges of a District Court do this, but much more rarely than a bankruptcy judge.

And -- but we do oppose the intervention today, and 09:31:35AM the trustee takes a view, of course, from the trustee's

perspective. He's one party, not even a party to this case, but let's assume that he is a party of some sort. He's one of only many, and the world doesn't revolve only around the trustee. And I don't want to leak into right now the -- the motion to amend, although these are obviously very much related. It is important to us that Judge Hoffman, or this court, if you decide that it should be you, it will be you, resolves the issue of property of the estate. But we also want to get on with a case that is already getting close to two years old that has the positions of the other parties as to this unjust enrichment also be heard. This -- a case this complicated and with this many parties cannot proceed in seriatim where we have to wait for one party to finish everything they have to say before we get on to whatever any other party wants to say and so forth.

09:31:57AM 09:32:16AM 09:32:39AM 09:32:55AM 09:33:11AM

These are victims for the most part who have lost their life savings. We have about $3 billion of transfers among a million victims, and we hear and respect the bankruptcy trustee wants to get some rulings that they hope will be favorable to them before Judge Hoffman, but it's not a reason to bring this proceeding to a halt.

And so just to review a little bit where we are, and obviously we appreciate the coordination between you and Judge Hoffman in terms of that's -- it's good for everyone for the two courts to be coordinated.

The -- the trustee has filed a motion for a determination that TelexFree engaged in a Ponzi scheme. We did not oppose that. The trustee has also filed in the bankruptcy case a -- a series of motions, the Ponzi scheme being one of them, the bar date motion being another, seeking to have the bankruptcy judge issue some guidance as to how proofs of claim are going to be filed in the bankruptcy case and the mechanisms that should guide the parties as to the allowance of those claims. We've not opposed those.

09:33:33AM

09:33:53AM

And so the one thing that I would start with that I would challenge Mr. Bennett on is that whatever you're being asked to do here interferes with the administration of the bankruptcy case. That's simply not the case. And that was clarified at the hearing on November 24th where Judge Hoffman asked me, "Do you oppose the bar date motion and the procedures for the setting of the claims?" We do not. And I didn't think there was really any confusion leading up to that hearing, but certainly not since that hearing.

09:34:10AM

Secondly, we do not oppose in the bankruptcy case the calculation that the trustee would use or the -- I'm sorry -- that the Bankruptcy Court would set for the determination of what is an allowable claim and what is not an allowable claim in the bankruptcy case. We do not oppose that. So there's no interference here at all with the administration of the bankruptcy case. That has to be overseen by Judge Hoffman, and

09:34:27AM

09:34:46AM

it will.

There are also a few other aspects for relief sought by the bankruptcy trustee before Judge Hoffman that the TelexFree defendants would have joint and several liability and so forth. We also did not oppose those.

09:35:02AM

There was a motion filed -- or an adversary proceeding -- the only person the trustee has sued in the Bankruptcy Court is the victims' representative. That's the only lawsuit that has been commenced by the bankruptcy trustee. That's unfortunate, but that's for another day. That -- the bankruptcy trustee has chosen for reasons known to him not to set for a hearing. So that has not yet been set for a hearing before Judge Hoffman, but we agree with Mr. Bennett that it seems that Judge Hoffman has to take that up. We would ask -- we would have liked that to have been formally put before Judge Hoffman. He seems to be getting there in his own way, and there are further arguments at the end of January that would seem to get there, but this could take a long time before it's decided before Judge Hoffman.

09:35:18AM

09:35:38AM

Technically, the specific motion filed in the bankruptcy case by the trustee on the very issue of what is property of the estate has not even been set for a hearing. And whatever -- and the issue has been briefed somewhat, and Judge Hoffman may or may not advance the ball on that on January 27th, but we don't know. And whatever is done in that

09:35:55AM

09:36:12AM

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MASSACHUSETTS - WORCESTER

IN THE MATTER OF:	:	Case No. 14-40987 14-40988, 14-40989
TELEXFREE, LLC, TELEXFREE INC., and TELEXFREE	:	(Jointly Administered)
FINANCIAL, INC.,	:	Boston, Massachusetts **November 24, 2015**
Debtors.	:	2:05:52 p.m.

: :

TRANSCRIPT OF HEARING ON:
[#623] MOTION OF CHAPTER 11 TRUSTEE FOR
FOR ENTRY OF ORDER FINDING THAT DEBTORS
ENGAGED IN PONZI AND PYRAMID SCHEME AND
RELATED RELIEF AND [#625] MOTION OF CHAPTER 11
TRUSTEE TO SET BAR DATE; AND [#635] RESPONSE
OF PLAINTIFFS' INTERIM EXECUTIVE COMMITTEE
BEFORE THE HONORABLE MELVIN S. HOFFMAN, J.U.S.B.C.

APPEARANCES:

For the United States Trustee:	Office of the U. S. Trustee BY: LISA TINGUE, ESQ. 446 Main Street, 14th Floor Worcester, MA 01608
Audio Operator:	YVONNE WOODBURY, ECRO
Transcript prepared by:	JANICE RUSSELL TRANSCRIPTS 1418 Red Fox Circle Severance, CO 80550 (757) 422-9089 trussell31@tdsmail.com

Proceedings recorded by electronic sound recording; transcript produced by transcription service.

next to the witness. I just want to make sure that we pick you up.

THE INTERPRETER: Okay. You will. Thank you.

THE COURTROOM DEPUTY: Would you raise your right hand?

MARIA MURDOCH, PIEC'S WITNESS, SWORN

THE COURTROOM DEPUTY: Could you spell her name, please?

MS. TAYLOR: It's Maria, M-A-R-I-A --

THE COURTROOM DEPUTY: Yeah.

MS. TAYLOR: -- Murdoch, M-U-R-D-O-C-H.

THE COURTROOM DEPUTY: Thank you.

DIRECT EXAMINATION

BY MS. TAYLOR:

Q Afternoon, Ms. Murdoch. Thank you for joining us.

A Good afternoon.

Q Realizing that we're short on time, I will try to keep this brief.

Do you speak -- do you speak English?

A Little bit.

Q But Portuguese is your primary language and you primarily communicate in Portuguese, correct?

A Yes.

Q Have you ever testified in court before?

A No.

Q What is your occupation?
A I'm a house cleaning.
Q And where were you born?
A Brazil.
Q Are you a permanent resident now of the United States?
A Yes. I'm an LPR.
Q And how long have you lived here?
A Sixteen years.
Q And why did you move here?
A Because Brazil was very difficult at that time and I brought my, my daughter here so she can study.
Q I'm going to ask a couple questions about your participation in TelexFree.
When did you first hear about TelexFree?
A It was about August of 2013.
Q And how were you convinced to get involved?
A It was through some friends of mine.
Q And did you pay anyone any money to get involved in TelexFree?
A Yes, I did.
Q Who?
A His name is Wagner.
Q How did you meet Mr. Wagner?
A It's through this group. They're doing some, having some meetings.

Sam, Sam Rodriguez, that's the name of the person.

Q How many times did you attend a meeting with Mr. Rodriguez, Sam Rodriguez?

A About three times.

Q Three times.

And how much money did you pay Mr. Wagner or Mr. Rodriguez to get involved in TelexFree?

A $25,000.

Q And that money was a large part or all of your savings, correct?

A Yes. Everything I had.

Q And how did you pay that money?

A Cash.

Q Cash.

And you handed that cash directly to Mr. Wagner?

A To Wagner, yes.

Q Did you ever get any money back from TelexFree?

A No.

Q And have you filed a claim in the bankruptcy case?

A No. No.

Q Do you intend to file a claim?

A Yes.

Q I'm going to ask a couple questions about the motion that's the subject of today's hearing.

Are you familiar with this motion?

A If I have the knowledge, you mean?
Q Do you know, generally, what it's about?
A Yeah, it's about TelexFree.
Q Okay. Did you receive by e-mail or by mail or by any other means a copy of the motion?
A No.
Q And did you receive any notice of today's hearing in the mail or by e-mail or by any other motion, or way?
A It was, yes.
Q It -- excuse me. I don't understand. It was.
A My daughter is the one who told me that I have to come here today.
Q Okay. But prior to your daughter telling you, you didn't -- did you get anything in the mail, you, saying that there is a hearing today?
A No.
Q Okay.
So not having had a copy of the motion, did you know that the motion, if it's granted today, would stop you or your chosen lawyer from suing to get the money back that you gave to Mr. Wagner?
A I didn't understand the question.
Q Okay. Let me try to rephrase.
Do you want to sue Mr. Wagner to get your money back?
A Yes, I do.

Q Did you know before today or yesterday that if the motion is granted you won't be able to do that?

A No, I didn't.

Q Thank you.

MS. TAYLOR: I have nothing further.

THE COURT: Just a minute, please.

Mr. Bennett, anything?

MR. BENNETT: Very briefly, Your Honor.

THE COURT: Okay.

CROSS-EXAMINATION

BY MR. BENNETT:

Q When you paid the money to this individual did you get a membership in TelexFree?

A No.

Q Did you get a user account with TelexFree?

A No.

Q Did -- does your daughter have a user account at TelexFree?

A No, she did not.

Q And how did your daughter find out about this hearing, if you know?

A Through some friends that they were supposed to be here. They told her that I, I was supposed to be here, too.

Q Thank you.

MR. BENNETT: No further questions on my part.

MS. TAYLOR: No further questions. Thank you.

United States District Court
District of Massachusetts (Worcester)
CIVIL DOCKET FOR CASE #: 4:14-md-02566-TSH

In Re: Telexfree Securities Litigation
Assigned to: District Judge Timothy S Hillman
Cause: 28:1332 - Diversity: Securities Fraud

Date Filed: 10/22/2014
Jury Demand: Both
Nature of Suit: 190 Contract: Other
Jurisdiction: Diversity

12/11/2015	367	Electronic Clerk's Notes for proceedings held before District Judge Timothy S Hillman: Motion Hearing held on 12/11/2015 re 310 MOTION (I) Modifying the Discovery Stay,266 MOTION to Intervene filed by Stephen B. Darr as Trustee of the Chapter 11 Estates of TelexFree, Inc. and TelexFree, LLC, and 252 MOTION to Amend *Complaint and File Third Consolidated Amended Complaint* filed by Plaintiffs, Case called, Counsel appear for motion hearing, Court hears arguments of counsel, Court rules taking under advisement 252 Motion to Amend; granting 266 Motion to Intervene; taking under advisement 310 Motion Modifying the Discovery Stay, (Court Reporter: Marianne Kusa-Ryll at justicehill@aol.com.)(Attorneys present: Several) (Castles, Martin) (Entered: 12/11/2015)