

NO. C-1-PB-14-001245

In Re: § **In the Probate Court No. 1**
§
§ **of**
§
TEL Offshore Trust § **Travis County, Texas**

**ATTORNEY AD LITEM’S RESPONSE TO CORPORATE TRUSTEES’ MOTION
TO APPROVE PAYMENTS OF ORDINARY BUSINESS EXPENSES OWED TO
THIRD PARTIES**

TO THE HONORABLE JUDGE HERMAN:

Glenn M. Karisch, as Attorney Ad Litem representing the interests of the unit holders of TEL Offshore Trust who were served by publication and did not answer or appear (“Ad Litem”) responds to the Corporate Trustees’ Motion To Approve Payments Of Ordinary Business Expenses Owed To Third Parties (“Motion”) as follows.

I. Summary

The Court entered a final judgment ordering that the funds in the segregated account could not be used to pay trust expenses. The Trustees agreed to this final judgment and it is now final and non-appealable. They certainly knew that they would incur further expenses when they agreed to this judgment.

Their Motion does not prove any changed circumstances or otherwise explain why the Trustees should not be bound by their agreement and should instead be able to use the segregated funds to pay expenses—expenses for which the Trustees did not seek Court approval before incurring.

Further, the Trustees have not complied with the Court's October 3rd order requiring them to pay the fees and expenses set forth in Ad Litem's September 26 application and have instead asked the Court to stay that order and all future fee applications. The Trust officer and representative of Bank of New York Mellon Trust Company ("BYNM") has confirmed that paying trust expenses out of the segregated account will exhaust the funds in that account, leaving nothing for the beneficiaries. The Trustees' strategy is obvious: prevent the Ad Litem from pursuing very serious breach of fiduciary claims by depriving him of his fees and expenses while simultaneously depleting the funds otherwise available to pay those expenses.

For these reasons, the Court should deny the Motion.

II. The Motion Ignores This Court's Final, Non-Appealable Judgment that the Trustees Agreed to in Cause No. C-1-PB-16-000096.

In asking to use the segregate funds to pay trust expenses, BYNM completely ignores the Court's Final Judgment it agreed to in Cause No. C-1-PB-16-000096 ("Final Judgment"). This Court ordered:

4. The Trustees hold the sales proceeds [from the sale of all of the Overriding Royalty Interest], if any, in a segregated interest-bearing account and refrain from using any of the proceeds for any purpose, including but not limited to: paying operating costs, administrative costs or the costs of this litigation, except for paying EnergyNet.com, Inc. the contractually required 4% payment for conducting the sale and paying other reasonable and necessary charges to effect such sale (excluding any attorney's fees of the Trust and payments to the attorneys, accountants or affiliates of any of the Trustees), unless an order of the Court in the Trust Proceeding is obtained;

Thus, the segregated funds cannot be used for Trust expenses. The Trustees agreed to this provision (and all other aspects of the Final Judgment). Further, the Final Judgment is final and non-appealable. If the Trustees believed that they would need to use the segregated funds to pay trust expenses they should have raised that issue before the Court entered its Final Judgment.

True, the judgment refers to the possibility of getting a subsequent Court order to allow use of the segregate funds to pay trust expenses. But that provision necessarily assumes: (a) that there is some change in circumstances from those existing when the judgment was entered that justify lifting the prohibition and (b) that the Trustees would get Court approval before incurring the expenses. The Trustees have not shown that when they agreed to the prohibition they couldn't have anticipated the expenses they now want to pay out of the segregate funds. To the contrary, they describe them as "ordinary business expenses." And BYNM unilaterally incurred the expenses it wants to use the segregated funds to pay. It did not seek Court approval to obtain these services. (In contrast, the Ad Litem has sought and received Court permission to hire outside litigation counsel and experts). Allowing the use of segregated funds to pay these expenses would reward BYNM for deliberately ignoring the Court's Final Judgment.

III. Using the Segregated Funds to Pay Trust Expenses Will Allow the Trustees to Escape any Inquiry into Their Breaches of Fiduciary Duty And Insure that the Beneficiaries Get Nothing.

While this is BYNM's first request to use the segregated funds to pay trust expenses, if allowed it most certainly will not be its last. And if the Court allows use of the segregated funds to pay trust expenses there will be nothing left.

BYNM's representative, Mike Ulrich, confirmed under oath:

Q: So the net to the trust from the Arena sell [sic] was what?

A: \$1,750,000, something like that.

Q: And ---

A: That included Chevron's .01 percent.

Q: And where is that money?

A: Sitting in a segregated account.

Q: Per the court order?

A: Per the court order.

* * * *

Q: So now we have proceeds. If the trust were allowed to pay [sic] those proceeds to pay its liabilities would there be trustee compensation among those liabilities?

A: Yes.

Q: So if you totaled all the liabilities of the trust that would otherwise be paid out of the \$1.75 million, how much are they?

A: Close to that amount. In addition -- would -- and I had just talked about the bank is owed a little over a million dollars on a note that the bank lent to the trust company.

Q: That's the Bank of New York as the bank --

A: Lent to the trust company a million dollars and change.

Q: So but for the court order, we have \$1.75 million. A million would go to payoff the bank and how much would go -- go to payoff these other liabilities?

A: Most of that, 700,000.

Q: So how much, if any, would be left to distribute to the unit holders?

A: Almost zero.

Excerpts of the deposition of Michael Ulrich (“Ulrich Dep.”), attached as Exhibit A, at 88:9-17 and 90:9-91:6 (emphasis added).

Despite this fact, the Trustees state that staying the enforcement of Ad Litem’s fee order would “serve the interests of the unitholders.” *See* Individual Trustees’ Motion to Stay Pending Mandamus (“Motion to Stay”), p. 3. Thus, while attempting to drain the segregated funds to pay their own expenses, the Trustees are simultaneously trying to prevent use of the funds to pay the Ad Litem’s expenses—even to the extent of disregarding the Court’s October 3, 2016 order. The positions the Trustees are taking benefit only themselves, not any of the Trust beneficiaries.

After an evidentiary hearing on October 3rd the Court awarded Ad Litem \$10,780.00 in fees and \$107,423.31 in expenses for a total of \$118,203.31. The Court ordered the Trustees to pay that amount from the segregated account established pursuant to the Final Judgment. The Trustees have not complied with the October 3rd Order. Instead, the Trustees have asked the Court to stay that order and all future fee applications by the Ad Litem. *See* Motion to Stay. Thus, if the Trustees have their way, their expenses will be paid, the Ad Litem’s expenses will not be paid and as a result the Trustees will avoid having to face a serious breach of fiduciary claims.

The Ad Litem’s investigation and discovery to date—including Ulrich’s sworn testimony—has revealed that the Trustees have breached their fiduciary duties in several respects:

1. By the end of 2009 the Trustees knew that as a result of Hurricane Ike the Trust was in dire financial condition. The situation was so bad they

considered resigning. They also considered selling some or all of the overriding royalty interest, borrowing money, and calling a vote of the unit holders—as allowed under the Trust Agreement—to terminate the Trust. They did not disclose any of this to the beneficiaries, however;

2. Instead of pursuing any of the options they considered—including letting the beneficiaries decide whether to sell the overriding royalty interest when it still had value and terminate the Trust—the Trustees chose to borrow money from the Corporate Trustee’s affiliate bank and sell portions of the property to make sure they themselves got paid, while the beneficiaries got nothing; and

3. The Corporate Trustee admitted that it did not follow the Trust Agreement’s formula for compensating itself; rather, it arbitrarily determined that Ulrich spent half of his time on the TEL Trust and charged the same amount of hours every year, regardless of the actual time spent.

Had the Trustees acted in the beneficiaries’ best interests and pursued a sale of all the overriding royalty interest in 2010 or even 2011, they could have reaped millions of dollars in value for the beneficiaries. Instead, they took actions to benefit themselves (and their outside counsel and accountants) while the beneficiaries received nothing. *See* Attorney Ad Litem’s Response to Trustees’ Objections to September 2016 Fee Application at 1-3 and the facts set forth in the Ad Litem’s Original Petition as Realigned Plaintiff. These breaches of fiduciary duty started in 2009 and continued until 2016.

And if the Trustees get their way, the beneficiaries will never receive another dime. As seen, if the funds in the segregated account are used to pay Trust expenses there will be nothing left for the beneficiaries. The only way the beneficiaries stand to recover anything is if the Ad Litem is free to pursue his claims. And that can only happen if the Ad Litem, his counsel and experts are paid.

But through the combination of depleting the segregated funds to pay trust expenses and preventing the use of those funds to pay the Ad Litem's expenses, the Trustees hope to skate away from any inquiry into their very serious breaches of fiduciary duty by depriving the Ad Litem of any funds with which to pursue the claims. The Court should not tolerate such gamesmanship. The only way the Trustees can be held accountable for their breaches is for the Ad Litem to be able to pursue claims for breach of fiduciary duty. And the only way for that to happen is to use the segregated funds to pay the Ad Litem's fees and expenses and not allow them to be depleted on Trust expenses that the Trustees unilaterally incurred without prior Court approval.

WHEREFORE, PREMISES CONSIDERED, Ad Litem prays that the Court deny the Motion and grant Ad Litem such other and further relief to which he may justly be entitled.

Respectfully submitted,

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Attorney Ad Litem

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing has been served on counsel of record on October 28, 2016 and will be served in accordance with the Court's orders regarding service dated September 28, 2015 and January 21, 2016.

/s/Cynthia L. Saiter

Cynthia L. Saiter

EXHIBIT A

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NO. C-1-PB-14-001245

In Re:) In the Probate Court No. 1
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) of
)
TEL Offshore Trust) Travis County, Texas

ORAL AND VIDEOTAPED DEPOSITION OF
THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A.,
CORPORATE REPRESENTATIVE

MICHAEL ULRICH

JULY 14, 2016

ORAL AND VIDEOTAPED DEPOSITION OF MICHAEL ULRICH,
produced as a witness at the instance of the
Defendants, and duly sworn, was taken in the
above-styled and numbered cause on July 14, 2016, from
9:14 a.m. to 5:08 p.m., before Kim Seibert, CSR in and
for the State of Texas, reported by machine shorthand,
at the law offices of ANDREWS KURTH, LLP, 111 Congress
Avenue, Suite 1700, Austin, Texas, pursuant to the
Texas Rules of Civil Procedure and the provisions
stated on the record or attached hereto.

1 (Exhibit No. 1 marked.)

2 THE VIDEOGRAPHER: Stand by. This is the
3 videotaped oral deposition of Michael Ulrich. Today's
4 date, July 14th, 2016. The approximate time, 9:15 a.m.
5 We're recording and on the record.

6 MICHAEL ULRICH,
7 having been first duly sworn, testified as follows:

8 EXAMINATION

9 BY MR. BITTING:

10 Q. Good morning. What is your name?

11 A. Mike Ulrich.

12 Q. Where do you live, Mr. Ulrich?

13 A. In Lakeway, Texas.

14 Q. Can you provide your address, please?

15 A. 114 Indian Bend, Lakeway, Texas.

16 Q. What ZIP code is that?

17 A. 78734.

18 Q. Do you have a cell phone?

19 A. Yes, I do.

20 Q. Would you provide that number, please?

21 A. (512) 633-9974.

22 Q. Do you have a landline?

23 A. Yes.

24 Q. Would you provide that, please?

25 A. (512) 261-9976.

1 Q. Let's start gross and then whatever -- the
2 partnership paid commission?

3 A. It was 1,830,000. And then Arena -- well,
4 that's what they paid. And then EnergyNet received a
5 4 percent commission.

6 Q. EnergyNet was the auction --

7 A. Auction house that sold the properties on
8 behalf of the trust.

9 Q. So the net to the trust from the Arena sell
10 was what?

11 A. 1,750,000, something like that.

12 Q. And --

13 A. That also included Chevron's .01 percent.

14 Q. And where is that money?

15 A. Sitting in a segregated account.

16 Q. Per the court order?

17 A. Per the court order at the bank.

18 Q. What current trust expenses are there that,
19 subject to the court ruling otherwise, you would
20 contend need to be paid out of that 1.75 million?

21 A. I'm not paying any expenses out of that.

22 MS. LUCIER: Objection, form.

23 Q. (BY MR. BITTING) Okay. Yeah, bad question.
24 Sometimes my A&M education comes out. You're going to
25 follow the court order?

1 MS. LUCIER: Objection, form.

2 Q. (BY MR. BITTING) Because in the past, as I
3 understand it, you suspended trustee compensation for a
4 period, but then paid it whenever there were proceeds
5 from a RNR sale?

6 A. Yes.

7 Q. Is that what happened?

8 A. That's what happened, yes.

9 Q. So now we have proceeds. If the trust were
10 allowed to pay those proceeds to pay its liabilities,
11 would there be trustee compensation among those
12 liabilities?

13 A. Yes.

14 Q. So if you totaled all the liabilities of the
15 trust that would otherwise be paid out of 1.75 million,
16 how much are they?

17 A. Close to that amount. In addition to --
18 would -- and I had just talked about the bank is owed a
19 little over a million dollars on a note that the bank
20 lent to the trust company.

21 Q. That's the Bank of New York as the bank --

22 A. Lent to the trust company a million dollars
23 and change.

24 Q. So but for the court order, we have
25 \$1.75 million. A million would go to payoff the bank

1 and how much would go -- go to payoff these other
2 liabilities?

3 A. Most of that, 700,000.

4 Q. So how much, if any, would be left to
5 distribute to the unit holders?

6 A. Almost zero.

7 Q. All right. Looking back at the second quarter
8 of 2009, part of Exhibit 7, we saw that the net loss
9 carry-forward had increased to \$3.1 million for the
10 Chevron properties and for a total of 3.4 million?

11 A. Correct.

12 Q. What led to that -- that's more than -- looks
13 like about -- shouldn't try to do math in my head.
14 It's more than double the loss carry-forward we saw on
15 the first quarter. Of course, it's significantly more
16 than the \$62,000 loss carry-forward that we saw at the
17 end of 2008. So what led to that increase?

18 A. Operating expenses related to
19 Eugene Island 339.

20 Q. Would that be the cleanup expenses?

21 A. Yes.

22 Q. If we look over to the third quarter of 2009,
23 that's from May, June, and July. We see that the net
24 loss carry-forward for the trust -- for the Chevron
25 properties is right close to \$4.7 million and the total