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The Thief, His Wife & Her Lawyer

Marc Miles successfully defended the widow of an alleged Ponzi schemer; but the case wasn't over

BY MICHAEL ESTRIN
PHOTOGRAPHY BY DUSTIN SNIPES

MARC MILES FRAMES THE STORY WITH both hands, cautioning that there are “no winners here.”

He flips his left hand back and forth to chronicle each twist and turn of the multiyear saga. When he has to pause for questions, he keeps this hand motionless, as if to keep his place in the narrative, while using the right hand to augment the answers to the follow-ups. Sidestepping legal jargon, he explains things with a low-key, Southern California charm. He's plain-spoken without being folksy; clear without sounding overly polished. But always he returns to the story.

It was late on a Friday afternoon in May 2009 when the phone rang in Miles' Orange County office. The caller was John Otto, an elderly businessman who lived in Palm Desert.

“He explained that he had some investors who were anxious because he had missed a dividend payment,” Miles recalls. Agreeing to represent Otto, and taking his new client at his word, Miles

drafted a letter to shareholders explaining that he had been retained as counsel, and that the missed payments were only temporary because Otto was in the process of selling the company. In order to represent Otto effectively, however, he needed to get a better sense of the man's business; so Otto agreed to meet Miles at his office the following Wednesday.

“There were no red flags then,” Miles says, recalling the two phone calls—one lasting 25 minutes, the other much shorter—that constituted the extent of his contact with Otto. “I drafted the letter he needed, sent it to him and left. The name John Otto didn't even cross my mind that weekend.”

Had Miles lived in Fresno, he would have thought differently. In that city of 500,000, Otto was already a well-known figure. About 350 investors in Fresno, and 850 more nationwide, alleged that Otto, through his company, HL Leasing Inc., had orchestrated a massive Ponzi scheme, defrauding them of more than

\$100 million. Later, it would emerge that Otto's other two companies, Manufacturers Acceptance Corp. and Air Fred, were implicated in the fraud because he had commingled funds between all three.

That weekend, the letter Miles wrote appeared on the local news in Fresno. Otto had sent it to shareholders, and apparently one of them shared it with the local media. When Miles returned to work the following Monday, the phones were ringing off the hook with angry investors calling about their money. The calls were so numerous that he set up a dedicated line to field them.

“The messages were devastating,” Miles recalls. “There were elderly people who had lost their life savings and people on dialysis who could no longer afford treatment. There were people who were going to be evicted because their money was gone. They were all blaming John Otto. It was very sad.”

But there was a bigger problem: John Otto was dead.



"It felt like I had walked into a punch," Miles says. "I had never had a client hire me and then commit suicide. It's [the stuff of] a John Grisham novel. It was alleged that this case involved a Ponzi scheme, but at first I was not quite sure. And the one person I could ask, my client, had killed himself."

IF THERE'S A COMMON DENOMINATOR

to the kinds of cases Miles handles at Callahan & Blaine, it's that they're big. The suits are often business disputes, and the dollar amounts are such that, he says, he "can hire the right expert, not just an expert."

"He's incredibly good at taking something that's very complex and condensing it into a story that a jury can understand and believe," says Kristy Schlesinger, a senior attorney at Callahan & Blaine who worked extensively with Miles on the Otto case.

Miles found his passion for storytelling while on the trial advocacy team at Southwestern Law School in Los Angeles, where his team placed third at a national competition. After graduating, he was hired as an associate by Carpenter, Rothans & Dumont, a small firm that specializes in representing public entities—mostly small cities within Los Angeles County. The opportunities there for a young lawyer to gain courtroom experience were so good that Miles recalls his secretary administering his oath just days after getting his bar results so he could stand in front of a judge.

For five years, Miles cut his teeth as a litigator. He also developed a philosophy that serves him to this day. "I like figuring out the story like it's a puzzle," he says. "And when it's assembled, you get to show it to the jury."

But defending small cities had its limits. Budgetary constraints meant Miles didn't always get to put all of the puzzle pieces together. As a long-distance relationship grew with the woman who would become his wife, Miles took the opportunity to look for employment in Orange County, not far from UC Irvine, where he had studied criminology as an undergrad.

With fewer than 30 lawyers, Callahan & Blaine is big enough to take on

multimillion-dollar lawsuits and "not get pushed around," says Miles, but small enough that he can focus his energy on a few big cases. He's traveled thousands of miles for a single deposition and hired investigators to pick apart every aspect of a client's business.

A few years back, Miles successfully defended Wolfgang Puck's company against products liability claims when news broke that self-heating coffee containers the company had licensed its name to were allegedly exploding in people's hands. The case involved potentially millions of dollars in claims. Miles traveled to Ohio to find an expert on the use of plastics, as well as to upstate New York, where he located a Cornell University food science professor. But the real work was done in Green Bay, Wisc., where Miles and his team of experts inspected the manufacturer's plant and gathered evidence that the product had both design and manufacturing defects. From there, Miles successfully litigated claims against the product's inventor in San Diego, and against two manufacturers, one in Wisconsin, the other in South Carolina.

While such complex cases are the norm for Miles, he says the key is to remember your audience and keep it simple. Then he offers an example.

"It was alleged that Mr. Otto ran a massive Ponzi scheme," he explains, holding up his left hand. Miles' client, Kathy Otto, he adds, holding up his right hand, "is a housewife."

WHEN THE OTTO CASE WENT TO TRIAL IN

the summer of 2011, Miles knew he had an uphill battle. The trial was held in Fresno, where the atmosphere was hostile.

"The word of mouth on the Otto trial was tremendous," says Donald Fischbach, an attorney with Dowling Aaron who worked as local counsel on behalf of the California plaintiffs. "A lot of people had lost everything."

One couple living in a San Luis Obispo retirement home had invested their life savings with John Otto. With only their Social Security income left, they were forced to move. Another woman was rendered homeless. One of Fischbach's neighbors was taken for \$300,000. According to

Fischbach, stories like these were common in Fresno. On the eve of the trial, in fact, Kathy, Miles' only client in a multiparty proceeding, was receiving death threats. Miles hired a bodyguard for her and for himself, then tried to focus on the facts.

Inside the courtroom, Miles had another problem. Judge Donald Black ruled that the phrase "Ponzi scheme," which Miles felt was inflammatory, could be used in front of the jury.

That term, he says, "automatically conjures up images of guilt, or at least civil liability in this context. But the judge denied our motion to bar the use of that phrase because he said it would help the jury to better understand the case. That was like giving the other side a 20-yard head start! So from the opening, jurors heard Ponzi scheme, and the whole time everyone was thinking, *Madoff, Madoff, Madoff.*"

Except nobody could say the name "Bernie Madoff" in court. Judge Black had dealt Miles another tactical blow, forbidding any mention of the disgraced financier.

Obviously any comparison to Madoff wouldn't be favorable—except, Miles felt, for one. Ruth Madoff claimed she didn't know anything about her husband's actions. So did Kathy Otto. That was the connection Miles wanted jurors to make.

"Bernie Madoff *admitted* his wife didn't know anything about the scheme," Miles says. "Here my client was dead, and couldn't come in and say, 'My wife didn't know either.' She was a housewife who made dinner and took the dog to the groomer's. She wasn't involved in her husband's business."

But *Madoff* was out even if *Ponzi* was in. To Miles, it was like being stuck between a rock and a hard place.

The case involved four claims against Kathy Otto. However, the two breach-of-contract claims were bifurcated out because Kathy hadn't signed any of those contracts. The trial moved forward with two fraud claims: concealment and negligent misrepresentation. The plaintiffs weren't accusing Kathy of masterminding the scheme; everyone knew her husband had been the culprit. No, the plaintiffs alleged that Kathy, along with Dan Ramirez, president of HL Leasing Inc., and Andy

Fernandez, the company's chief financial officer, had helped John commit fraud.

The plaintiffs had a few facts on their side. Fifteen years earlier, Kathy had worked for one of her husband's companies, Manufacturers Acceptance Corp. Mostly, she answered phones and made coffee, says Miles. More potentially damaging were corporate reports that identified her as the company secretary.

For one month, jurors heard three stories. The plaintiffs argued that to varying degrees, all of the defendants, including Kathy Otto, had run a Ponzi scheme through HL Leasing. At each turn, lawyers for Ramirez and Fernandez rebutted that claim by shifting the blame to John Otto. The third story in the courtroom, one being told by Miles, tried to answer a question that was on everyone's mind: *How could Kathy not have known what her husband, who worked out of their home, was doing?*

Demonstrating ignorance is tricky. Miles had to prove a negative. He knew he had to get the jury to understand Kathy's world.

"In a lot of ways, the Ottos are from a different time," Miles says, explaining that his parents or grandparents might be better able to understand the way they segregated business from family life. "You may not like or understand it, but men and women of their generation are just different from us today. Their gender roles are different. John and Kathy had a deal: He took care of the business, she took care of the house. He would travel all over the country for the business, and the only time she made a business trip was to go with him to Fresno for the company Christmas party."

During closing arguments, the plaintiffs used a "classic empty chair" defense to tie Kathy and her co-defendants to John Otto. He may have been the one running the show, counsel argued, but the living defendants were trying to shift all of the blame onto a dead man.

Miles had his own theatrical stunt up his sleeve. During his closing, he removed the picture of John Otto that had been taped to the chair, and sat in it himself. From that position, Miles reminded jurors that being a wealthy widow of a fraudster wasn't the same as being complicit in fraud. Then he read a quote from Bernie

Madoff—without mentioning his name—in which Madoff explained how he had run an \$18 billion Ponzi scheme without his family's knowledge.

"I think they got it," says Schlesinger who kept her eyes on the jury while Miles spoke. "That quote had been in the news a lot, but really it was just a moment where Marc—through Bernie Madoff—was able to explain how it could be that a wife wouldn't know."

In the end, the jurors agreed with Miles. Kathy Otto was a widow, not a co-conspirator. The other defendants weren't so fortunate. The jury found that Ramirez and Fernandez had aided and abetted the fraud and hit them with \$47.22 million in damages.

That ended the case ... until it didn't.

IN 2009, IN THE IMMEDIATE AFTERMATH

of John Otto's suicide, Miles faced a number of challenges. Miles, after all, was still technically the attorney for all three companies, but they had more or less disintegrated with Otto's death.

Records culled from Otto's hard drive didn't give Miles what he had hoped for: a lead on the corporate assets that might be used to mitigate investor losses. Since the companies had disintegrated, Miles filed a motion with the court to be relieved as counsel. The motion was granted in January of 2010 and Miles thought that was the end of it. Three months later, Kathy hired Miles to defend her personally. By that time, the judge had already entered an order certifying the class, a step toward victory in a class action case.

At the end of the jury trial, the judge found that the three corporations had breached their contracts with the investors to the tune of \$114 million. That verdict didn't carry any weight at that point, says Miles, because there really were no companies anymore and they "didn't really show up to trial." But as the Otto trial moved into its second phase, that breach-of-contract verdict would come back to haunt Miles and his client.

After releasing the jury, the judge considered what corporate lawyers refer to as the alter-ego theory, which allows a judge to put a person in the shoes of a

corporation if it can be shown that they exercised "dominion and control" over that corporation.

In Kathy Otto's case, the alter-ego theory wasn't applicable. Fresno County Superior Court Judge Donald S. Black wrote, "The clear weight of the evidence at trial was that Kathleen Otto did not exercise dominion and control over any of the corporate entities."

But the same could not be said for John. The judge found that John Otto had exercised dominion and control over his corporations and that they were in fact his alter ego. Next, Judge Black found that Kathy was a successor in interest to her husband.

"She stood in the shoes of John Otto for the purpose of the lawsuit," Ara Jabaghourian, one of the plaintiff's lawyers, told *The Fresno Bee*.

In other words, she was now on the hook for \$114 million. "We felt all along that we always had an alternative theory," Fischbach says. "As far as we are concerned, we won the case, and the alter ego claim was always our second bullet."

Miles, no surprise, doesn't see it that way. He feels it's an example of judicial overreach. He's careful to remind anyone who will listen that the jury exonerated Kathy Otto. "I think there was a feeling in Fresno that the widow got away with something," Miles explains. "The judge got really creative here and tried to throw the plaintiffs a bone."

But while Miles is confident he'll prevail before an appellate panel sometime in 2013, he's cautious about calling it a win.

"There are no winners," he says. It was a refrain he repeated often to the jury in Fresno. It's how he sees the whole Otto affair. More than a thousand people lost their savings. The man most responsible killed himself. And while Miles takes solace that he was able to prove his client wasn't liable for fraud, he says Kathy Otto is a victim too.

Framing the sentence with his hands stretched a foot apart, he says, "She lost her husband; then she found out that her life was a lie." ■