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UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA, WESTERN DIVISION

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

CHARLES P. COPELAND, COPELAND WEALTH MANAGEMENT, A FINANCIAL ADVISORY CORPORATION, AND COPELAND WEALTH MANAGEMENT, A REAL ESTATE CORPORATION,

Defendants.

CASE NO. 2:11-cv-08607-R-DTB

MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF MOTION TO:

1. CONSOLIDATE RECEIVERSHIP ENTITIES; AND

2. POOL ASSETS AND LIABILITIES OF THE VARIOUS RECEIVERSHIP ENTITIES

DATE: November 5, 2012
TIME: 10:00 a.m.
DEPT. 8, 2nd Floor

Judge: Hon. Manuel L. Real

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TABLE OF AUTHORITIES

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I.

INTRODUCTION

This case involves a fraud perpetrated largely upon retired, or soon to be retired, professionals. The victims, most of whom were clients of defendant Charles P. Copeland's accounting practice, invested their savings and retirement accounts in various limited partnerships created and managed by Copeland. They trusted him and thought their money was being conservatively invested. However, rather than prudently managing his clients' investments, Copeland treated the entities as the "Copeland Piggy Bank", and engaged in pervasive comingling of funds from entities that had cash flow to those that did not at any given time.

Thomas C. Hebrank is the duly appointed permanent receiver (the "Receiver") pursuant to the Judgment of Permanent Injunction filed October 19, 2011 ("Judgment", [Dkt. No. 3]). The Judgment gives him full powers of an equity receiver to take custody, control and possession of the assets ("Receivership Estate") of defendants Copeland Wealth Management, a Financial Advisory Corporation ("CWM Financial") and Copeland Wealth Management, a Real Estate Corporation ("CWM Realty") (together "Defendants"), and their subsidiaries and affiliates (the "Receivership Entities").

The Receiver seeks consolidation to accelerate distribution of money he collects. Otherwise, distribution of recovered assets will be significantly delayed because unwinding the interrelated transfers will be time-consuming. Many of the victims are either elderly, or because of Copeland's actions financially desperate, or both. They have little time to wait for the distribution of assets.

Without consolidation, administration of the Receivership Estate also will be expensive. Considerable time would have to be expended

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determining exactly when, and how much, money was transferred from one entity to another. Substantial attorneys' fees would be incurred recovering improperly transferred or distributed assets. Those expenses will reduce the amount ultimately available for distribution.

Accordingly, the Receiver brings this motion on the bases that: (1) it is in the best interests of the Receivership Estate and creditors to consolidate the assets and liabilities of the various Receivership Entities, as it will ensure equitable treatment of all creditors and investors and will yield a larger return because administrative costs will be reduced; and (2) the Receiver's investigation reveals that Receivership Entities received the benefit of monies invested in other Receivership Entities, and that their assets were commingled such that they should best be treated as one.

The Receiver currently has about $2 million in the combined accounts of the Receivership Entities, and should receive between $2.5 and $3.0 million more from the sale of CP18's property, which the Court has approved. Upon consolidation, the Receiver could then have over $4 million for distribution to the investors once a method for paying claims has been approved by the Court, perhaps before the end of the year.

II.

FACTUAL AND PROCEDURAL BACKGROUND

A. Nature of the Commission's Action

The Securities and Exchange Commission (the "Commission") brought this action under various Sections of the Securities Act of 1933[1], the Securities Exchange Act of 1934[2], and the Investment Advisors Act of 1940[3]. (Complaint [Dkt. No. 1] filed 10/18/11.) Through imposition of the

[1] Sections 20(b), 20(d)(1) and 22(a), 15 U.S.C. §§ 77t(b), 77t(d)(1) & 77v(a).

[2] Sections 21(d)(1), 21(d)(3)(A), 21(e) and (f), 15 U.S.C. §§ 78(u)(d)(1), 78u(d)(3)(A), 78u(e), 78aa(a).

[3] Sections 209(d), 209(e)(1) and 214(a), 15 U.S.C. §§ 80b-9(d), 80b-9(e)(1) & 80b-14(a).

Receivership, the Commission sought to protect the Receivership Entities' creditors and investors from dissipation of the Receivership Estate's assets and to provide for payment of creditors with some return for investors. The Complaint alleged that Defendants made false and misleading statements and engaged in deceptive acts and/or practices, all in violation of the Acts. The Complaint sought permanent injunctive relief and monetary relief in the form of disgorgement and civil penalties.

The Judgment also gives the Receiver full equity powers including, without limitation, power over all funds, assets, collateral, premises, real or personal property, choses in action and other property being managed by or in the possession or control of Defendants CWM Financial and CWM Realty and their subsidiaries and affiliates.

B. The Receivership Entities

The Court determined by its Order Approving Receiver's Response ("Order" [Dkt. No. 53] filed 3/12/12), that the following limited partnerships are also included in the receivership as affiliates of CWM Financial and CWM Realty:

a. Copeland Private Equity One, L.P.; Copeland Private Equity Two, L.P.;[4]

b. Copeland Fixed Income One, L.P.; Copeland Fixed Income Two, L.P.; Copeland Fixed Income Three, L.P.;[5]

c. Copeland Properties One, L.P.; Copeland Properties Two, L.P.; Copeland Properties Three, L.P.; Copeland Properties Four, L.P.; Copeland Properties Five, L.P.; Copeland Properties Six, L.P.; Copeland Properties Seven, L.P.;

[4] The Copeland Private Equity Partnerships will be identified individually as "CPE1" and "CPE2" and together as the "Private Equity LPs."

[5] The Copeland Fixed Income Partnerships will be identified individually as "CFI1", "CFI2" and "CFI3" and collectively as the "Fixed Income LPs."

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Copeland Properties Eight, L.P.; Copeland Properties Nine, L.P.; Copeland Properties Ten, L.P.; Copeland Properties Eleven, L.P.; Copeland Properties Twelve, L.P.; Copeland Properties 13, L.P.; Copeland Properties 14, L.P.; Copeland Properties 15, L.P.; Copeland Properties 16, L.P.; Copeland Properties 17, L.P.; Copeland Properties 18, L.P.[6]

C. The Receiver's Initial Activities

The investors, who had come to trust Defendant Copeland as their accountant, were subsequently induced by him to invest in the Fixed Income LPs, the Real Estate LPs, and to a lesser extent, the Private Equity LPs. Those who invested in the Fixed Income LPs were told that the money would be used to make loans secured by real estate or stable corporate assets. Instead, the money was secretly used to fund and provide cash flow for the Real Estate LPs, and to pay distributions to Real Estate LP investors. The Fixed Income LPs raised about $14 million from investors, but they now have virtually no assets. (Receiver's Response to Order on Receivers Application and Report [Dkt. No. 47, Pg. ID #:804].)

Similarly, the Real Estate LPs made loans to and received loans from other Receivership Entities, and made other loans to investors and clients of Defendant Copeland. Some Real Estate LPs were allowed to fail (e.g. CP4 and CP6, even after CFI1 loaned $2.9 million to CP4), while other Real Estate LPs were kept afloat. (Id. [Dkt. 47, Pg. ID #810].)

When the Commission discovered the fraud, it requested the appointment of a receiver to protect the victims. Defendants Charles Copeland, CWM Financial and CWM Real Estate consented to the relief sought in the Judgment. Until that time, Copeland controlled CWM Financial and CWM Real Estate as the general partners of all the

[6] The Copeland Real Estate Partnerships will be identified individually as "CP1" through "CP18" and collectively as the "Real Estate LPs."

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Copeland limited partnerships, including the Fixed Income LPs, the Real Estate LPs and the Private Equity LPs. (Id. [Dkt. No. 47, Page ID #:804].)

The Receiver has taken over daily operations of the Receivership Entities. He is managing the properties, responding to tenants, working with brokers, leasing agents and appraisers, and negotiating terms of sale, among many other activities for the Real Estate LPs. He maintains separate bank accounts for each of the partnerships. (Receiver's Report #3 [Dkt. No. 76].)

The Receiver also has analyzed all of the notes receivable for the Receivership Entities. In conjunction with counsel, he has demanded payment and is attempting to collect all third-party notes receivable. At the inception of the receivership, the Receivership Entities had a combined total of over $22.3 million in notes receivable. Of the notes receivable, however, $15.9 million are from one Receivership Entity to another. Because all of these entities are included in the Receivership Estate, the Receiver is not attempting to collect the related-party notes receivable. The Receiver is attempting to collect the $6,414,343.34 of third-party notes receivable, but only $83,907.00 has been recovered so far ($17,907.00 of this amount is referenced in Receiver's Report #3 [Dkt. No. 76, Pg. ID #:1278-1279]; and, $66,000.00 was collected recently, and is referenced in the Receiver's Report #4, which is being filed concurrently.

The reason so little has been collected is yet another reason the Receivership Entities should be consolidated. Most of the third party notes were made by the investor-victims. These debtors argue that they should not have to repay the notes because Copeland defrauded them of more money than they owe. As a practical matter, the victims have little money to repay the notes.

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D. Receiver's Response to Objectors

At a February 6, 2012 hearing on administrative matters relating to the Receivership Estate, the Court entered the Order on Receiver's Application and Report that had been submitted by certain limited partner investors in the Real Estate LPs (the "LP Objectors"). The order required the Receiver to provide justification for including in the Receivership Estate certain of the Real Estate LPs in which the LP Objectors had invested.

The Receiver filed his response to the order on March 5, 2012, and on March 12, 2012, the Court entered its order confirming that all of the Real Estate LPs were included in the Receivership Estate together with the Fixed Income LPs and the Private Equity LPs. (Order Approving Receiver's Response to Order on Receiver's Application and Report [Dkt. No. 53].) Nevertheless, the Receiver anticipates that the LP Objectors might again attempt to exclude from the receivership certain Real Estate LPs in which they invested.

In his March 5th response to the LP Objectors, the Receiver explained that if the Real Estate LPs were excluded, he would have to immediately start efforts to collect on notes receivable among the various Receivership Entities and the investors themselves. This includes 59 separate notes receivable from individual limited partners, including some of the LP Objectors, as well as from other Real Estate LPs and Copeland related entities. (Receiver's Response to Order on Receiver's Application and Report [Dkt. No. 47, Pg. ID#:807].)

The Court, in issuing its order and rejecting the LP Objectors' efforts to exclude their Real Estate LPs from the Receivership Estate, apparently agreed that the receivership would be best served by keeping all assets in one proceeding. That would allow an equitable distribution of recoverable funds among all investors. The alternative would be a series of lawsuits

against the investors and partnerships at substantial cost to the Receivership Estate and at further indirect expense to the victims.

E. Receiver's Forensic Accounting

On June 29, 2012, the Receiver filed the first of his three expected forensic accounting reports (the "First Forensic Report"). (Receiver's Forensic Accounting Report #1 [Dkt. No. 90].) The report focused on the accuracy of the financial information prepared by Defendant Copeland and his accounting group to determine the recoverability of Receivership Estate assets. Central to that was an analysis of the related-party transactions. As stated in the report, the Receiver's key findings include:

- The Real Estate LPs were dependent upon cash from other Receivership entities to fund operations, and make mortgage payments and investor distributions, among other things.
- The Real Estate LPs loaned approximately $11.8 million to related entities, and received loans of approximately $30.3 million from related entities. This money was routinely commingled through Copeland's "piggy bank."
- The Fixed Income LPs loaned a total of $19 million, none of which went to unrelated third parties, as required by the partnership agreements, for the stated purpose of investing in real estate backed loans and corporate loans.
- Instead, 40% of the Fixed Income LP loans went to Real Estate LPs and 33% went to Copeland investors and clients. The balance went to other Receivership Entities or Defendants and their related entities.
- The Fixed Income LPs paid approximately $1 million more in distributions than cash flow supported. Despite restrictions against it in the partnership agreements, early investors were

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allowed to "cash out" with new investors paying in part for the "cash outs" and excess distributions.

- CWM Financial and CWM Realty, as the general partners of the Receivership Entities, treated the entities as a "piggy bank" with funds flowing freely among the partnerships.

Although the conclusions reached in the First Forensic Report are disturbing, the Receiver's tracing of the Copeland's accounting to supporting documentation did not indicate any inaccuracies in the financial statements. In short, Copeland's undisclosed comingling and dissipation of assets appears to be correctly documented. However, approximately 4,800 general journal entries were recorded reflecting non-bank account accounting entries. These entries are not easily verified and frequently reflect cross-over entries relating to other Receivership Entities. Whether these general journal entries reflect unsupported transactions or just reclassifications of different supported accounts was beyond the scope of the First Forensic Report. Verifying the legitimacy of these journal entries would be very costly, resulting in less money available to distribute to the victims.

F. <u>The Fixed Income LPs</u>

As stated above, the Fixed Income LPs consisted of CFI1, CFI2 and CFI3. Each has a partnership agreement which provides that the Fixed Income LPs were to engage in the business of owning real estate backed loans and corporate loans, and activities related to that business. The partnership agreements also required approval by 67% of the limited partners for transactions that involved a conflict of interest for the general partner, CWM Real Estate. [Dkt. 90, Pg. ID#:1383.] However, the vast majority of the $14 million raised through the Fixed Income LPs was loaned to related entities without the required limited partner approval.

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In his First Forensic Report, the Receiver summarized the ebb and flow of funds between the Fixed Income LPs and the Real Estate LPs. [Id. at Pg. ID#:1383–1387.] The report documents early cash contributions from the initial investors, and then outflows of cash to the Real Estate LPs and CWM Real Estate, to pay off early investors despite restrictions in the partnership agreements, and to make loans to Copeland clients and investors. The movement of funds among the various entities was characterized as "indiscriminant" and "pervasive", to the entities that required cash flow to maintain their existence and operations. [Id. at Pg. ID#:1384.]

Although the General Partner, CWM Real Estate, was required to invest only in third-party real estate backed and corporate loans, the Receiver's analysis determined that none of the Fixed Income LP funds were used for that purpose. Indeed, funds were regularly transferred to pay limited partner distributions, mortgages, and operating expenses of the Real Estate LPs. [Id. at Pg. ID#:1386-1387.]

The Fixed Income partnership agreements also provide that partners were entitled to the return of their contributions only upon dissolution of the partnership or following a noticed-sale of the interests. However, the Receiver found that $11.8 million in partner contributions were received, and approximately $2.1 million in partner withdrawals were allowed, with no documentation that the withdrawals complied with the partnership agreements. [Id. at Pg. ID#: 1387-1388.] The Receiver concluded that the manner in which funds were moved between the Fixed Income LPs and existing investor accounts was indicative of a Ponzi Scheme; i.e., "an investment fraud that involves the payment of purported returns to existing investors from funds contributed by new investors". [Id. at Pg. ID#:1388.]

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G. The Copeland Real Estate LPs

The Receivership Estate includes 18 real estate limited partnerships, CP1 through CP18. Each is or was a single asset entity. At the time the Receiver filed his First Forensic Report, only eight of the Real Estate LPs were active entities holding real property. [Id. at Pg. ID#:1388.] Two had been closed by the sale of the asset, four were lost to foreclosure or receiverships, and three were tax transfer vehicles.

As he did in his analysis of the Fixed Income LPs, the Receiver summarized all of the related-party debits in the Real Estate LPs to determine the total loans made by them. Additionally, the Receiver summarized all of the credits to the related-party notes payable accounts to ascertain the total loan proceeds received by each of the Real Estate LPs. His calculations revealed that the Real Property LPs loaned $11.8 million to related entities, but borrowed over $30.3 million. [Id., at Pg. ID#: 1390.]

The commingling of money among the related entities was clearly shown by their interconnectedness and their dependency upon one another to fund cash flow requirements. The Receiver's tabular summary highlights of some of the transfers and cogently demonstrates the commingling within the Real Estate LPs and between the other Receivership Entities and the Real Estate LPs. [Id. at Pg. ID#:1390-1391.]

In short, the Fixed Income LP funds were not used for their stated purpose of engaging in the business of owning real estate backed loans and corporate loans, but rather were improperly used to fund other Copeland entities, the Defendants, or Copeland clients and investors. The Receiver has not found a single instance where the money was loaned to a true third party. While the Real Property LPs did own real property, they were routinely used to fund loans to and from each other, and they

received regular advances from other Receivership entities to meet cash flow needs. This was done by Defendant Copeland in an arbitrary manner so that some investors would receive windfalls at the expense of others facing financial ruination unless the Receivership Entities are consolidated to allow an equitable distribution of monies recovered.

The Receiver respectfully requests an Order of the Court authorizing the administrative consolidation of the Receivership Entities into a single entity in which the assets and liabilities may be pooled, and from which all claims, as well as fees and costs of administering the Receivership Estate may be paid. The consolidation will allow fair and equal treatment of all creditors and will save money by substantially reducing administrative expenses to the benefit of all investors.

III.

ARGUMENT

A. THE COURT'S AUTHORITY TO ORDER CONSOLIDATION ARISES FROM ITS GENERAL EQUITABLE POWERS

Substantive consolidation of entities affects the combination of assets and liabilities of distinct entities and treats them as though they were a single entity. Consolidation not only pools the assets and liabilities of several entities, but also satisfies the liabilities from the resulting common fund. It eliminates inter-entity claims and combines the creditors of the various entities within the Receivership Estate.

The Court's power to order consolidation arises from its general equitable powers. A court of equity has inherent power to take possession and control of the property of an entity through imposition of a receivership, for the purpose of preserving and administering that property for the ultimate benefit of the entity's creditors, as well as those entitled to the property. *Burnrite Coal Briquette Co. v. Riggs*, 274 U.S. 208, 47 S.Ct.

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575 (1927). The power of a District Court to impose a receivership or grant other forms of ancillary relief further derives from its inherent power as a court of equity to fashion effective relief. *Securities & Exchange Commission v. Wencke*, 622 F.2d 1363, 1369 (9th Cir. 1980). A District Court has "broad powers and wide discretion to frame the scope of appropriate equitable relief." *Securities & Exchange Commission v. Lincoln Thrift Ass'n.*, 577 F.2d 600, 609 (9th Cir. 1978).

Similarly, other Federal Courts, such as bankruptcy courts, have consistently based their authority to order substantive consolidation upon their general equitable powers provided by the Bankruptcy Code. Section 105 of the Bankruptcy Code provides, in pertinent part: "The Court may issue any order, process, or judgment that is necessary or appropriate to any of the provisions of this title." *In re Auto Train Corp.*, 810 F.2d 270, 276 (DC Cir. 1987).

The United States Supreme Court impliedly approved substantive consolidation in *Sampsell v. Imperial Paper & Color Corporation*, 313 U.S. 215, 61 S.Ct. 904 (1941). Federal equitable principles also entitle victims of fraudulent conduct to a proportionate share of the assets recovered, based upon the amount of their actual out-of-pocket losses. *Securities & Exchange Commission v. Elliot,* 953 F.2d 1560, 1566-1570 (11th Cir. 1977); *In re Tedlock Cattle Co. Inc.,* 552 F.2d 1351, 1352-1353 (9th Cir. 1977).

It is readily apparent from the Receiver's Reports [Dkt. Nos. 14, 31, and 76], and the Receiver's First Forensic Report, that the Copeland Defendants through the Receivership Entities did not distinguish between the assets, liabilities and activities of the various entities. They used funds contributed to or earned by one entity to pay creditors or investors in another entity. As a result of the commingling and numerous transfers

among the Receivership Entities, all assets in the Receivership Estate should be pooled. Substantive consolidation will also ensure that all victims will be treated similarly. *In re Standard Brands Paint Company*, 154 B.R. 563, 571 (Bkrtcy. C.D.Cal. 1993).

B. IT IS IN THE BEST INTEREST OF VICTIMS AND CREDITORS TO CONSOLIDATE THE ASSETS OF ALL ENTITIES

1. Consolidation Will Ensure Equitable Treatment

Although the investors might have invested in an entity without knowing that the Receivership Entities were operating as an entwined single enterprise, all of them were part of the same fraudulent scheme. The Receiver has not had an opportunity to interview each of the nearly 200 investors, however, declarations have been obtained from several of those caught in the Copeland web. Their stories are remarkably similar: they invested in Charles Copeland, not the individual limited partnerships. The investors did little, if anything, to select the limited partnerships into which their money was placed or the property that was purchased with the funds. They handed their money to Defendant Copeland because they trusted him, and he moved the money into entities as he saw fit. True and correct copies of the declarations are attached to the Notice of Lodgment filed concurrently with this motion. The following excerpts are examples of the manner by which innocent people became entangled in this debacle.

- Declaration of Peggy Hatfield Neumann

7. I met Charles P. Copeland through his relationship with my parents. He provided personal and business accounting services to my parents beginning in the 1980's. My parents are now deceased.

9. Mr. Copeland began providing personal accounting services to Leonard and me in approximately 1991. Among other things, he prepared our annual income taxes.

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10. Leonard and I trusted Mr. Copeland wholeheartedly with our financial affairs. Mr. Copeland was my parents' accountant and advised them with regard to their financial affairs for several decades. I trusted my parents' opinion of Mr. Copeland and had no reason to doubt his competency, his moral character, or his ability to provide top notch accounting services.

16. Mr. Copeland led me to believe that the money I contributed to CFI3 would be invested in multiple sources consisting of stable tangible assets such as commercial real estate buildings and industrial buildings; however, he did not provide me with any such details. I never thought the money would be invested in Mr. Copeland's own related entities. In fact, Mr. Copeland told me he was not allowed to do this.

21. I also became a partner in CP9 based on Mr. Copeland's recommendation. At the time I signed the partnership agreement for CP9, I knew very little about the partnership and was not informed about the details of the property or assets owned by CP9. I trusted that Mr. Copeland would advise us in a conservative manner as he had always promised. He told me that I would receive an eight percent (8%) to ten percent (10%) return on my investment. I did not perform any independent investigation into the property or assets owned by CP9, or the viability of the investment. I never saw any appraisals for the property owned by CP9, which I now understand is located in Kentucky. I relied solely on Mr. Copeland's advice in making the investment and trusted that it was a conservative endeavor.

28. The impact this has had on myself and my family has been devastating. My husband and I can no longer afford to live at or operate our ranch, which is our dream come true. We have 30 horses on our ranch that we will most likely lose if we do not get some money back somehow. In fact, if we lose the ranch, which appears probable, we will probably move away from Redlands for some time. Also, as a result of our lost investments, my husband and I cannot leave any significant inheritance for our daughters as my parents did for me.

- <u>Declaration of Leonard Neumann (Peggy's Husband)</u>

6. I met Charles P. Copeland through his relationship with Peggy and Peggy's parents. Mr. Copeland was Peggy's parents' accountant for several decades. Peggy and I trusted Mr. Copeland for this reason, among others as explained below.

7. Mr. Copeland began providing personal accounting

services to Peggy and me in approximately 1991. Among other things, he prepared our annual income taxes.

8. In my initial dealings with Mr. Copeland, he seemed trustworthy and competent. Having had no professional training or experience in accounting or investments myself, I trusted him. He portrayed himself as a professional, and as a conservative investor. I never had any reason not to trust him.

11. I did not independently investigate the real properties in which the money would be invested. I saw brochures but did not research the property values or the market. I relied on Mr. Copeland's representations that the investment was a sound decision. I relied on his integrity and professionalism, as Peggy and I had always done.

- Declaration of Werdna Wayland Eure, Jr.

9. Beginning in 1999 and until about 2007, I put a lot of trust in Mr. Copeland. Over the years, I gave Mr. Copeland increasing control over my finances and investments, as it appeared he was quite competent. I understood him to be a religious man. In fact, at one point, he won the Loma Linda Chamber of Commerce of the Year Award.

10. Mr. Copeland created and controlled my business accounts. Again, until about 2007, I had no reason to believe he was anything other than trustworthy.

11. In 2004, I received approximately $3,000,000.00 from the sale of my medical practice. Around that time, Mr. Copeland approached me about investing my money in his real estate limited partnerships. He sold me on the idea as a reliable investment tactic. At this time, Mr. Copeland continued to have control over my finances and invested my money in various partnerships as he saw fit. I believed Mr. Copeland was a conservative investor and that he would protect my investments.

12. At various times, I requested information from Mr. Copeland about the investments he had made with my money. I never really got any legitimate answers or satisfactory explanations; however, I continued to rely on him and trust that he had my best interests in mind. Mr. Copeland routinely advised me that I did not need to worry about anything and that he would handle my affairs for me.

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19. The impact of Mr. Copeland's actions, and the mess he has made of my finances, has had a grave effect on my life and my future. Among other things, my wife and one of my sons blamed me for the financial disaster Mr. Copeland created. This ultimately led to my divorce and estrangement from my son. Additionally, the deterioration of my emotional health has been exacerbated by my financial instability.

- Declaration of Geoffrey A. Gardiner

8. In 2003, my tax preparer retired. Because Mr. Copeland had a good reputation as an accountant, and I was pleased with my prior interactions with him, I decided to hire him to prepare my taxes. Mr. Copeland has prepared my taxes from 2002 until 2011, and during this time I have never had any problems with my tax returns, nor have I ever been audited. I have always been satisfied with the work Mr. Copeland did as my accountant.

10. In 2007, during a meeting with Mr. Copeland, he approached me about investing some money that was in my IRA rollover account and that was paying very little interest. He knew how much money I had and where it was kept because he did my taxes.

11. Mr. Copeland told me he knew of a safe investment that would give me a regular six percent (6.0%) return on my money. I emphasized to Mr. Copeland that these funds need to be secure without any loss of capital and he assured me that this was the case. He did not give me any additional details about this proposed investment. I didn't ask because I had come to trust Mr. Copeland with my financial affairs.

12. I never thought Mr. Copeland would steer me in the wrong direction, so I agreed to invest $500,000.00 from my IRA in the investment he had proposed. Based on what he told me, I figured it was a safe and reliable investment. I would never had invested my money in the proposed investment had I known the money was going to be invested into a real estate limited partnership, as I had invested in three of these types of partnerships many years ago and lost all the money I invested.

17. I had planned on using the money in my IRA for retirement purposes, with some left over to leave to my children. Now that the $500,000.00 is gone, my wife and I will have to make do with what we have left, unless we can recover some of the money we lost through the receivership.

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- Declaration of Bruce Taber

6. I first met Charles Copeland in approximately 1992. At that time, Mr. Copeland was a Certified Public Accountant affiliated with the Soren, McAdam Christianson, CPA firm, which was the accountancy firm I retained for my dentistry practice. Work performed on my behalf by Soren McAdam Christianson was performed by Charles Copeland.

7. In approximately 1993, Charles Copeland left Soren McAdam Christianson and started his own firm. I moved my work from Soren McAdam Christianson to Charles Copeland, at his new practice.

12. I first determined that problems existed with my investments in Copeland's limited liability entities in late 2010 or early 2011. At that time, I received telephone calls and correspondence from someone in New York telling me that the loan for CP-8 was in default and that I was a guarantor. After several attempts, I finally was able to speak with Charles Copeland. Copeland divulged that, unbeknownst to me, he had caused me to execute a personal guarantee of the CP-8 loan.

13. In my initial dealings with Mr. Copeland, he seemed trustworthy and competent. Having had no professional training or experience in accounting or investments myself, I trusted him. He portrayed himself as a professional, and as a conservative investor. I never had any reason not to trust him.

- Declaration of Janet Ihde

7. I first met Charles P. Copeland in approximately 1982, during my first year out of residency. At that time, Mr. Copeland was a Certified Public Accountant affiliated with the Soren McAdam Christianson, CPA firm.

8. Over the many years that Mr. Copeland served as my accountant, he appeared to be a knowledgeable professional. I did not know much about accounting so I trusted him.

11. I continued to place my trust in Mr. Copeland. He was personable and charismatic. Ultimately, I turned over the management of my finances to him. I gave him complete control over my investments. At that time, I had no reason not to trust him. I did not know which investments he chose for me, how much he invested, or how much I was receiving in distributions.

13. I trusted Mr. Copeland so wholeheartedly that he would often give me documents to sign, last minute. He would come to my

clinic and spend 5 or so minutes with me without explaining what I was signing. I never really read the documents he had me sign because I figured he was taking care of me.

14. I later found out that one of the documents Mr. Copeland had me sign obligated me to pay $17,000,000.00 on behalf of Copeland Properties 12, L.P.

15. I also found out that Mr. Copeland took all the equity out of my house, and out of my mother's house. As a result, I had to sell my house in a short sale, and move into my mother's house.

18. As late as 2010, Mr. Copeland told me I had $1,200,000.00 in retirement funds. At that time, I had no reason to believe otherwise.

19. At this time, I am informed and believe that there is nothing left of my investments.

20. The loss of my financial stability has been devastating. I feel like I have worked hard all my life, and I have lost everything I have worked so hard to achieve

22. My current financial situation is embarrassing and humiliating. Unless I am able to recover some of the funds I lost through Mr. Copeland's actions, it is unlikely that I will be financially stable anytime soon.

- <u>Declaration of Joanne Kohut</u>

3. Charles Copeland served as the personal accountant for me and my husband for over thirty-five years.

10. I trusted Copeland. I would not have continued using him as our accountant if I did not trust him.

14. I relied on Copeland in making the investments related to the limited partnerships.

18. As far as I know, Copeland controlled the investments made in connection with the limited partnerships.

19. As far as I know, Copeland decided whether to sell a partnership or to make a loan to a partnership or other partnerships.

- <u>Declaration of John J. Kohut</u>

2. I am seventy two years old and married to Joanne Kohut.

3. Charles Copeland served as the personal accountant for me and my wife for many years.

11. I do not know what kind of limited partnership investments we made and I do not know how many partnerships we invested in through Copeland or with Copeland's assistance.

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12. I relied on Copeland in making the investments related to the limited partnerships.

23. I do not know who controlled the investments made in connection with the fixed income limited partnerships.

The common thread running through the victims' statements is that money was invested with Defendant Copeland because people trusted him, not because of the financial vitality of any particular limited partnership that they had personally investigated. Moreover, the funds, as well as returns on investments, were moved from one entity to another, on the whim of Defendant Copeland, not at the direction of an investor. The money invested into a specific partnership was never permanently segregated for purposes of that partnership alone. The funds were freely transferred among the Receivership Entities, depending upon which partnerships had money and which ones needed money.

The Receiver proposes to treat the assets of all Receivership Entities as a single estate. Likewise, the Receiver proposes to treat all proper claims as obligations of the consolidated Receivership Estate. Similar treatment will ensure equity and fairness to each investor and claimant. Dissimilar treatment would ensure inequality and injustice because some would benefit at the expense of others based arbitrarily on where the money was when the Commission became involved. Moreover, substantive consolidation would increase the pool of assets available to satisfy claims of investors and creditors.

Substantive Consolidation is an equitable doctrine; its purpose is to insure the "equitable treatment of all creditors." *In re Eastgroup Properties*, 935 F.2d 245 (11th Cir. 1991); *In re Standard Brands Paint Company*, 154 B.R. 563, 570 (Bkrtcy. C.C. Cal. 1993).[7]

[7] Although *Standard Brands Paint Company* involves consolidation in the context of a bankruptcy proceeding, Local Rule 66-8 provides that where possible the administration of a receivership is governed by bankruptcy administration principles. When acting in equity, the District Court has broad power and wide discretion to determine appropriate relief in receivership action.

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Because the various Receivership Entities likely have had different debt to asset ratios, consolidation will invariably redistribute wealth among the investors and creditors. However, it was the unauthorized redistribution of assets among the limited partnerships that created the inequities which now burden most of the investors. Though some courts have concluded that substantive consolidation should be used sparingly, the modern trend favors the remedy. The basic criteria used to evaluate substantive consolidation is whether the "economic prejudice of continued debtor 'separateness' outweighs 'the economic prejudice of consolidation'" *In re Eastgroup Properties*, 935 F.2d 245, 249 (11th Cir. 1991) citing *In re Snyder Brothers, Inc.* 18 B.R. 230, 234 (Bankr. D. Mass. 1982). "In other words, a court must conduct a searching inquiry to insure that consolidation yields benefits offsetting the harm it inflicts on objecting parties." *In re Eastgroup Properties*, at 249, citing *In re Auto Train Corp.*, 810 F.2d at 276.

Though not articulating a universal test to be applied in all situations, the Ninth Circuit has applied the doctrine of substantive consolidation in the context of an order emanating from the U.S. Bankruptcy Court. *In re Bonham*, 229 F.3d 750 (2000). In that case, the Ninth Circuit directed that a court could order substantive consolidation of two non-debtor corporations with the bankruptcy estate of a Chapter 7 debtor. The *Bonham* Court observed that two similar, yet not identical, tests have developed to assess whether substantive consolidation is proper. *In re Bonham*, at 765.

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a. The Substantial Identity Test

The *Bonham* Court explained: "In *Auto–Train*, the D.C. Circuit articulated a three-part burden-shifting test as part of 'a searching inquiry to ensure that consolidation yields benefits offsetting the harm it inflicts to objecting parties.' [Citation.] Under this test, a proponent of substantive consolidation must first show that '(1) there is a substantial identity between the entities to be consolidated; and (2) consolidation is necessary to avoid some harm or to realize some benefit.' [Citation.] When this prima facie showing is made, 'a presumption arises 'that creditors have not relied solely on the credit of one of the entities involved.'' [Citation.] The burden then shifts to an objecting creditor to show that '(1) it has relied on the separate credit of one of the entities to be consolidated; and (2) it will be prejudiced by substantive consolidation.' [Citation.] Finally, if the objecting creditor makes the required showing, 'the court may order consolidation only if it determines that the demonstrated benefits of consolidation 'heavily' outweigh the harm.' [Citation.] Each element of the *Auto-Train* test must be satisfied to properly order substantive consolidation." In re Bonham, at 765-766.

b. The Second Circuit Test

The *Bonham* Court also recognized an independent test developed in the Second Circuit, "which requires the consideration of two factors: "(1) whether creditors dealt with the entities as a single economic unit and did not rely on their separate identity in extending credit; or (2) whether the affairs of the debtor are so entangled that consolidation will benefit all creditors. [Citations.] *The presence of either factor is a sufficient basis to order substantive consolidation.*" *In re Bonham*, at 766, (emphasis added). The *Bonham* Court concluded: "[t]he Second Circuit's approach is more

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grounded in substantive consolidation and economic theory; it is also more easily applied." *In re Bonham*, at 766.

Recently, in an *unpublished* opinion, the District Court for the Eastern District of California relied upon the *Bonham* decision, also utilizing the Second Circuit test. *In re SK Foods, L.P.,* 2010 WL 5136187 (E.D. Cal. Dec. 10, 2010).[8] Guided by *Bonham*, the *SK Foods* Court observed, "[w]hen deciding whether substantive consolidation is appropriate, courts in the Ninth Circuit consider two factors: '(1) whether creditors dealt with the entities as a single economic unit and did not rely on their separate identity in extending credit; or (2) whether the affairs of the debtor are so entangled that consolidation will benefit all creditors.' Either factor may constitute a sufficient basis to order substantive consolidation."

In considering the facts of this case under either of the foregoing tests, substantive consolidation is appropriate and necessary. However here, as in *Bonham*, the Second Circuit's approach seems best tailored to the circumstances. Not only did the investors rely on Defendant Copeland (they did not perform independent due diligence before investing in the limited partnerships), but also, the affairs of the Receivership Estate are so entangled that consolidation will benefit all creditors and investors. The Second Circuit's approach is more grounded in substantive consolidation and economic theory and it is also more easily applied here.

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[8] *In re SK Foods, L.P.* is an unpublished decision. It is not authoritative, but only cited as an example of tests utilized by District Courts in the Ninth Circuit.

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2. Consolidation Allows More Efficient and Less Expensive Administration so More Money Will Be Distributed

The transfers of funds among the Receivership Entities for loans to each other, to investors and to Copeland clients, among others, are so intertwined that it would be financially prohibitive to disentangle their affairs. Without consolidation, dozens of additional lawsuits will have to be filed to collect notes receivable, many of them payable by the investors themselves. The investors as a whole also will benefit from consolidation because the costs of administration will be reduced. "Consolidation will eliminate intercompany claims and liabilities of the consolidated entities as well as duplicate claims." *In re Standard Brands*, supra, 154 B.R. 563 at 569; *FDIC v. Colonial Realty Company*, 966 F.2d 57 (2d Cir. 1992); *In re Augie-Revisto Baking Company*, 860 F.2d. 515 (2d Cir. 1998).

If the Receivership Entities are substantively consolidated, the Receiver will be able to administer the estate more efficiently, and as a result, resources that would otherwise be expended in prolonged efforts to unwind the affairs of the Receivership Entities can be substantially reduced. It would be time consuming and costly, indeed, to attempt an allocation of funds contributed by each investor to a particular partnership, especially those in the Fixed Income LPs where millions have been dissipated in numerous loans to Real Estate LPs, some successful and some not. Moreover, the assets of any Receivership Entity that received funds from another one would have to be reduced; and, the transferring Receivership Entities would need to be credited in a like amount.

Finally, consolidation will avoid the substantial accounting fees and expenses resulting from the continued preparation of separate tax returns for each of the Receivership Entities.

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IV.

CONCLUSION

Defendant Copeland was the mastermind behind this web of interconnected assets that he wove through the Receivership Entities he controlled. He placed investors' money into limited partnerships and then moved the money to related-entities without constraint or investor consent. Initially, investor funds were segregated into separate investments, but he quickly moved the assets from Receivership Entities operating in the black, to those operating in the red. For the most part the individual investors had no idea of, nor did they determine, the entities into which their investments eventually were transferred. Only Mr. Copeland knew the shells under which the investors' money was located. Tragically, by the time the shells were lifted in 2011, much of the money was gone leaving the Receiver the difficult task of determining the location and value of the remaining assets.

Due to the commingling of assets, it will be difficult if not impossible to determine the treatment of any particular investor's funds; for example, was their share of the Fix Income LPs' money used to subsidize a successful Real Estate LP or an unsuccessful one. Since the funds were commingled, and because all investors have a claim against the Receivership Estate based upon the same legal theories (i.e., fraud and conversion), the only fair and equitable procedure for the benefit of investors and creditors would be to consolidate the assets and liabilities of all the Receivership Entities, so as to create on fund from which all claims and expenses can be paid.

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Based on the foregoing, the Receiver respectfully requests:

(1) That the Receivership Entities be consolidated into one entity in which all assets and liabilities of all Receivership Entities are held;

(2) That the Receiver be authorized to treat as one fund all property of the Receivership Entities which is in, and comes into, his possession for (a) payment of the administrative fees and costs; and (b) the benefit of and distribution to the investors and creditors of the Receivership Entities; and

(3) For such other and further relief as the Court may deem just and proper.

DATED: October 5, 2012

MULVANEY BARRY BEATTY LINN & MAYERS LLP

By: /s/ John H. Stephens
John H. Stephens
Attorneys for Permanent Receiver, Thomas C. Hebrank

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