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19 and FIRST FINANCIAL PLANNING CORPORATION

20 **UNITED STATES DISTRICT COURT**
21 **SOUTHERN DISTRICT OF CALIFORNIA**

22 SECURITIES AND EXCHANGE
23 COMMISSION,

24 Plaintiff,

25 v.

26 LOUIS V. SCHOOLER and
27 FIRST FINANCIAL PLANNING
28 CORPORATION d/b/a
WESTERN FINANCIAL
PLANNING CORPORATION,

Defendants.

Case No. 12 CV 2164 GPC JMA

**DEFENDANTS' MEMORANDUM
OF POINTS AND AUTHORITIES IN
SUPPORT OF THEIR MOTION FOR
STAY OF ORDER PENDING
APPEAL**

Date: November 15, 2013

Time: 1:30 p.m.

Courtroom: 2D

Judge: Hon. Gonzalo P. Curiel

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1 Defendants LOUIS V. SCHOOLER (“Schooler”) and FIRST FINANCIAL
2 PLANNING CORPORATION d/b/a WESTERN FINANCIAL PLANNING
3 CORPORATION (“Western”) (collectively “Defendants”) respectfully submit the
4 following Points and Authorities in support of Defendants’ Motion for Stay of Order
5 Pending Appeal, to wit, this Court’s order of August 16, 2013, granting in part and
6 denying in part Defendant’s Motion for Modification of Preliminary Injunction
7 (Dkt. No. 470) (“Order”). Defendants are appealing Section II.G.2 of the Court’s
8 Order that mandates that all of Western’s equity interests in the real estate general
9 partnerships (“GPs”) formed through Western’s real estate syndication activities be
10 liquidated before the receivership over the GPs is lifted (Dkt. No. 470, pp. 25-26)
11 and request a stay of Section II.G.2 pending the Ninth Circuit’s decision.

12 I.

13 INTRODUCTION

14 Following extensive briefing and over an hour of oral argument on July 26,
15 2013, the Court on August 16, 2013 issued its Order regarding Defendants’ motion
16 for modification of the preliminary injunction of March 13, 2013.

17 Although the Court granted Defendants’ motion to have the receivership
18 released over the GPs, the Court’s Order imposed several “equitable” conditions
19 precedent on the removal of the receivership. The main condition, which is the
20 subject of Defendants’ appeal and this Motion for Stay of Order Pending Appeal, is
21 quoted in its entirety (Dkt. No. 470, 25:20-26:9):

22 First, the Court first orders a pro rata reduction of Western’s equity interests
23 in the GPs according to the properties’ current fair market value as set forth in
24 the appraisals obtained by the Receiver. To the extent a GP account has a
25 zero balance or insufficient funds to meet an obligation due within ninety
26 days from the date of the reduction of Western’s interests, such interests shall
27 nonetheless be formally liquidated with no payment to Western. Before the
28 GPs are released from the receivership, all of Western’s equity interests in the
GPs shall be liquidated to ensure that Western will have no future
responsibility for any liability incurred by the GPs. Additionally, given the
enormous disparity between the purchase prices of the GP properties and the

1 funds Western raised from the GPs, the Court finds it equitable to preclude
2 Western from receiving a share of any proceeds received from any future sale
3 of the GP properties.

4 Under the Court's Order, Western would be permanently stripped of at least
5 \$11 million of assets and likely millions of dollars of future investment returns
6 before the underlying claims have been tried, and without any judgment of liability
7 against Western having been entered first, if at all. If the Court's Order is not
8 stayed, Western will be deprived of the opportunity to present evidence to the trier
9 of fact why it is entitled to retain its equity interests in the GPs, and it will have been
10 deprived of due process.

11 There is no need or justification at this time to liquidate Western's equity
12 interests in the GPs. In fact, the caselaw mandates the opposite: *the primary*
13 *purpose of injunctive relief is to preserve and maintain the status quo until a full*
14 *trial can be held.* Liquidating the equity interests at this time will unalterably
15 change the status quo before the case on the merits can be heard, to the benefit of
16 none of the parties or the investors.

17 Enforcement of the Order and summary liquidation of Western's equity
18 interests, prior to review by the Court of Appeals, would cause irreparable harm to
19 Western and violate its due process rights. Therefore, a stay of Section II.G.2 is
20 warranted pending a decision on appeal.

21 II.

22 ARGUMENT

23 A. Standard of Review

24 Defendants seek a stay of Section II.G.2 of the Court's Order pursuant to Rule
25 62(c) of the Federal Rules of Civil Procedure (FRCP) and Rule 8(a)(1) of the
26 Federal Rules of Appellate Procedure (FRAP), whereby "a party must...move first
27 in the district court for...a stay of the judgment or order of a district court pending
28 appeal...[or] an order suspending, modifying, restoring, or granting an injunction

1 while an appeal is pending.”

2 There are four factors to be considered before a stay can issue under FRCP
3 62(c) or FRAP 8(a)(1), namely (1) whether the party applying for the stay has
4 shown a strong showing that it is likely to succeed on the merits, (2) whether the
5 applicant will be irreparably injured without a stay, (3) whether issuance of a stay
6 will substantially injure the other parties, and (4) where the public interest lies.
7 *Hilton v. Braunskill*, 481 U.S. 770, 776 (1987) (four-factor test applies to both
8 rules). “A probability of success on the merits” or “that serious legal questions are
9 raised and the balance of hardships tilts sharply in...favor” of the moving party. *See*
10 *Maharaj v. Ashcroft*, 295 F.3d 963, 966 (9th Cir. 2002). The first two factors –
11 strong showing of likelihood of success on the merits, and whether irreparable
12 injury will result – are the most critical. *Nken v. Holder*, 556 U.S. 418, 434 (2009).

13 **B. Defendants Have Shown a Probability of Success on the Merits**

14 To satisfy the first factor for a stay pending appeal, Defendants need not show
15 that it is more likely than not that they will win on the merits, but merely that there
16 is a “substantial case” for relief. *Leiva-Perez v. Holder*, 640 F.3d 962, 966 (9th Cir.
17 2011) (*citing Nken v. Holder*, 556 U.S. 418, 432 (2009) (“The whole idea [of a stay]
18 is to hold the matter under review in abeyance because the appellate court lacks
19 sufficient time to decide the merits”).

20 Defendants present such a case here. The Court’s Order is a premature finding
21 of liability on the part of Western that violates Western’s right, as a litigant and
22 property owner, to due process before it can be permanently deprived of its
23 property. Western is being treated as if it has already been tried and found liable for
24 fraud, with the resulting punishment of disgorgement of ill-gotten gains, despite no
25 proof that Western’s equity interests are legally illegitimate. Therefore, the Order
26 mandating permanent and total liquidation of Western’s equity interests is in excess
27 of jurisdiction.

28 ///

1 While federal courts have broad discretion to supervise an equity
2 receivership, the courts' supervisory actions must still comply with due process.
3 *SEC v. Basic Energy & Affiliated Resources, Inc.*, 273 F.3d 657, 668 (6th Cir.
4 2001). As the Supreme Court has noted, in employing its broad equitable powers a
5 federal court must "exercise '*the least possible power* adequate to the end
6 proposed.'" *Spallone v. United States*, 493 U.S. 265, 280 (1990) (quoting *Anderson*
7 *v. Dunn*, 19 U.S. (6 Wheat.) 204 (1821)) (emphasis added). "Courts of equity can
8 no more disregard statutory and constitutional requirements and provisions than can
9 courts of law." *Hedges v. Dixon County*, 150 U.S. 182, 192 (1893).

10 The broad supervisory discretion does not empower the Court to order the
11 permanent liquidation of at least \$11 million of property interests – and an
12 enormous, unrecoverable investment loss for Western - at this early stage of
13 litigation, particularly when it benefits none of the parties or the investors. No trial
14 has been held in this case, and no final judgment of liability has been imposed upon
15 Western. Such action would be an abuse of the Court's discretion that likely would
16 not pass muster on appeal.

17 The primary purpose of a preliminary injunction is to preserve the status quo
18 pending determination of the action on its merits. *Chalk v. United States Dist. Ct.*
19 *Cent. Dist. Of Calif.*, 840 F.2d 701, 704 (9th Cir. 1988); *Six Clinics Holding Corp. II*
20 *v. Cafcomp Systems Inc.*, 119 F.3d 393, 400 (6th Cir. 1997). Accordingly,
21 injunctions that alter the status quo are "subject to a heightened scrutiny" and are not
22 appropriate unless "extreme or very serious harm will result." *Dahl v. HEM Pharm.*
23 *Corp.*, 7 F.3d 1399, 1403 (9th Cir. 1993); *Marlyn Nutraceuticals, Inc. v. Mucos*
24 *Pharma GmbH & Co.*, 571 F.3d 873, 879 (9th Cir. 2009).

25 The forced liquidation of Western's property interests would violate this
26 clearly established principle, permanently curtailing the status quo without any
27 showing that extreme or very serious harm would result if Western maintains its
28 units in the GPs until trial. It would also contradict the Court's direction that the

1 purpose of the receivership over Western was solely “to clarify Western’s financial
2 affairs.” Dkt. No. 59, 9:27.

3 “We tolerate some exceptions to the general rule requiring predeprivation
4 notice and hearing, but only in ‘extraordinary situations where some valid
5 governmental interest is at stake that justifies postponing the hearing until after the
6 event.’” *United States v. James Daniel Good Real Property*, 510 U.S. 43, 53 (1993)
7 (quoting *Fuentes v. Shevin*, 407 U.S. 67, 82 (1972)) (seizure of real property in civil
8 forfeiture cases requires pre-deprivation notice and hearing); *see also Fuentes*, *supra*
9 (loss of kitchen appliances and household furniture requires pre-deprivation
10 hearing).

11 The only fraud allegation made to date is with regard to the pricing of the GP
12 units. That allegation has not been proven at trial, and Western has not been given
13 an opportunity to show that it met all of its duties and obligations under the law,
14 including providing investors with all required material disclosures. The SEC has
15 made allegations, but has not proven its case. Defendants are entitled to an
16 opportunity to present their own evidence showing that investors not only were
17 provided with all material disclosures, but that the real estate market data will
18 support the conclusion that investors purchased their property interests at fair prices.

19 The Court points to the disparity in price between what Western paid for the
20 property and what the GPs paid for the property as a rationale for divesting Western
21 of its property interests, but that is not a sufficient reason for this drastic action. The
22 Court assumes – solely on the allegations of the SEC – that the price differential was
23 nothing but pure profit for Western. However, the Receiver’s (albeit sparse)
24 information shows that *while Western received approximately \$80.2 million in*
25 *investor deposits between 2005 and 2012, Western’s costs* – including payroll, sales
26 commissions, taxes, legal fees, rent paid for its office space, and other operational
27 expenses related to the investigation, selection and acquisition of the real estate that
28 was sold to the GPs – *totaled \$95.8 million, or a shortfall of \$15.6 million.* Dkt.

1 No. 484, p. 18 (Receiver's summary of Western's sources and uses of cash).¹

2 Furthermore, the Receiver has stated that Western's accounting records were
3 "accurate and reliable," Dkt. No. 182, at 14, and there has been no proof whatsoever
4 of any offshoring or concealment of money. Therefore, the price differential is not
5 indicia of fraud, but of regular business practices with no nefarious intent. This is
6 especially true in light of the 63 GPs that have successfully sold their title to end-
7 users for significant profits, returning in excess of 10% annualized returns for the
8 investors in those 63 GPs.

9 The SEC's burden of proof in this matter will require them to show much
10 more than simply a difference in the price to acquire the property versus the price at
11 which the GPs acquired the property. The mere existence of the difference in price
12 paid by the entities does not rule out the Defendants' ability to show at trial that
13 investors not only purchased their property at fair prices, but that they also were
14 provided with all material disclosures regarding the investment. Equity demands the
15 status quo to be preserved until there is a full trial on the merits.

16 No trial on the merits has been held, yet Western is being completely
17 deprived of all of its equity interests without a judgment entered against it. Thus,
18 the Order is such "a plain usurpation of power" that Defendants have a substantial
19 case for relief on appeal. *Hoult v. Hoult*, 57 F.3d 1, 6 (1st Cir. 1995).

20 Because Defendants have a substantial case for relief, the first factor of a
21 strong showing of likelihood of prevailing on the merits is in Defendants' favor, and
22 therefore the stay should issue.

23 _____
24 ¹ By citing the Receiver's data here, Defendants do not concede its overall accuracy
25 and reserve their right to challenge and clarify it. For example, although Western
26 ended 2012 with \$65,324.50 in cash (Dkt. No. 484, p. 18), the \$15 million that
27 offset the shortfall consisted of \$4.5 million in cash on hand as of January 1, 2005,
28 ***including approximately \$1.2 million loaned by Schooler in 2012, about \$270,000
of which was contributed after the receivership over Western began.***

1 **C. Defendants Will Be Irreparably Injured Without a Stay**

2 For Defendants to prevail on the second factor of irreparable injury,
3 Defendants must show a probability of irreparable injury, with the court to
4 “anticipate what would happen as a practical matter following the denial of a stay.”
5 *Leiva-Perez*, 640 F.3d at 968.

6 In this case, without the issuance of a stay, the Receiver would be required to
7 liquidate all of Western’s GP equity interests without any adjudication of liability
8 against Western for fraud. The equity interests cost Western \$11 million, and – as
9 noted above – Western’s \$80.2 million in investors’ initial deposits is offset by its
10 expenses of \$95.8 million including payroll, sales commissions, rents, taxes, and
11 other operational expenses. If the interests are liquidated, Western will have no
12 opportunity to recoup its costs, let alone make any profit, which it can only do by
13 maintaining its equity interests until the prices of the underlying properties can be
14 sold at an opportune time -- as is the case for *all* GP investors.

15 Such a massive deprivation of property interests could not be remedied,
16 particularly since no judgment of liability has been entered against Western. In
17 particular, if Western prevails at trial, it would have no recourse to recover its equity
18 interests that have been stripped. Such an act of confiscation would be a taking by
19 the government without just compensation, let alone due process – a double dose of
20 Fifth Amendment violations.

21 The liquidation of Western’s assets at this time, without the issuance of a stay,
22 would serve only to deprive Western of a property right long before it has been
23 proven responsible for any wrongful action. As the Supreme Court has noted:

24 Moreover, the availability of a postseizure hearing may be no recompense for
25 losses caused by erroneous seizure. Given the congested civil dockets in
26 federal courts, a claimant may not receive an adversary hearing until many
27 months after the seizure. And even if the ultimate judicial decision is that the
28 claimant was an innocent owner, or that the Government lacked probable
cause, this determination, coming months after the seizure, “would not cure
the temporary deprivation that an earlier hearing might have prevented.”

1 *United States v. James Daniel Good Real Property, supra*, 510 U.S. at 56,
2 quoting *Connecticut v. Doehr*, 501 U.S. 1, 15 (1991) (striking down state statute that
3 authorized prejudgment attachment of real estate without prior notice or hearing, in
4 the absence of extraordinary circumstances).

5 Therefore, without the issuance of a stay pending appeal, Defendants would
6 be irreparably harmed because the Receiver would be free to liquidate Western's
7 property rights.

8 **D. Issuance of a Stay Will Not Substantially Injure the SEC or the**
9 **Receiver**

10 The last two parts of the four-factor test require a balancing of the public
11 interest against the harm to the SEC and Receiver as the opposing parties. *Nken*,
12 556 U.S. at 435; *Leiva-Perez*, 640 F.3d at 964-66.

13 Neither the SEC nor the Receiver would suffer *any* injury, let alone a
14 substantial injury, if the stay were to issue. The Court's Order does not affect the
15 SEC's ability to litigate the case, because the Order affects only the ancillary issues
16 of the receivership over Western and the GPs, not the key issues of the litigation
17 (whether Defendants sold unregistered securities and committed fraud in doing so)
18 on which the SEC would still be able to proceed.

19 Similarly, the Receiver will maintain control of Western and will be able to
20 proceed with winding up his duties over the GPs through the publication and
21 distribution of an information packet to the GP investors, a part of the Order that
22 Defendants do not challenge. A stay of the Receiver's ability to liquidate Western's
23 equity holdings *en masse* would not cause substantial injury to him, particularly now
24 that the Receiver has filed suit against three businesses to recover money loaned by
25 Western, and will be presumably seeking his fees and costs if he prevails. *See*
26 *Hebrank v. LinMar Management, Inc.*, 13-CV-2179-W-WVG (S.D. Cal.); *Hebrank*
27 *v. LinMar III, LLC*, 13-CV-2180-W-WMC (S.D. Cal.); *Hebrank v. LinMar IV, LLC*,
28 13-CV-2181-JM-BLM (S.D. Cal.).

1 Moreover, the investors in the GPs would not be affected in any way by a stay
2 here. Whether or not Western's interests in the GPs are liquidated, the GPs will still
3 be responsible for all the same ongoing obligations they have under the partnership
4 agreements. There is simply no harm to the SEC, the Receiver, or the investors for
5 Western to continue to simply hold its minority non-voting units during the
6 pendency of this litigation.

7 **E. The Public Interest is in Favor of a Stay**

8 The public interest in this case is the upholding of the constitutional right of
9 due process and ownership of property, by halting the proposed liquidation of a
10 defendant's assets pending an interlocutory appeal. The broad discretion of the
11 Courts in fashioning injunctive relief has its limits – especially when it bumps up
12 against the well-established due process that is required before private property
13 rights can be forcibly taken away.

14 In this case, Western, as a corporation and litigant, is as entitled to due
15 process as anyone else is before it can be permanently deprived of its property. *See*
16 *Santa Clara County v. Southern Pac. R.R.*, 118 U.S. 394 (1886) (corporations
17 protected by Fourteenth Amendment's Equal Protection Clause); *Covington &*
18 *Lexington Turnpike Co. v. Sandford*, 164 U.S. 578 (1896) (corporations are
19 "persons" under Fourteenth Amendment's Due Process Clause); *Green v. Bock*
20 *Laundry Mach. Co.*, 490 U.S. 504, 510 (1989) (civil litigants and criminal
21 defendants in federal court are equally protected by Fifth Amendment's Due Process
22 Clause).

23 While a stay is in effect, the heart of this litigation – the SEC's claims against
24 Defendants – can move forward, through discovery and pretrial motions, toward an
25 evidentiary trial on the merits.

26 The public interest would not be harmed by the issuance of a stay, but rather
27 protected. If the intent in liquidating Western's GP interests is to provide funds for
28 injured investors as the Receiver appears to claim, waiting until the appeal has run

1 its course would not harm things. If Western is found at trial to have committed
2 securities fraud, liquidation at that point in time would still be possible. However,
3 there is no benefit to the public interest by ordering the liquidation of the GP
4 interests *before* trial.

5 **III.**

6 **CONCLUSION**

7 Based on the foregoing, Defendants respectfully request that this Court issue
8 a stay of Part II.G.2 of its Order of August 16, 2013, with regard to the liquidation
9 of all Western-held equity interests in the GPs, pending the outcome of Defendants'
10 appeal of the Order to the Ninth Circuit Court of Appeals.

11
12 DATE: September 26, 2013

Respectfully submitted,

13 /s/Philip H. Dyson

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CERTIFICATION

I hereby certify that on the 26th day of September 2013, I electronically filed the foregoing with the Clerk of the District Court using the CM/ECF system, which sent notification of such filing to the following counsels of record:

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