

1 Eric J. Hougen (SBN 258968)
2 Law Offices of Eric J. Hougen
3 624 Broadway, Suite 303
4 San Diego, CA 92101
5 Telephone: (619) 702-1000
6 Facsimile: (619) 702-1005

7 Philip H. Dyson, Esq. (SBN 097528)
8 Law Office of Philip H. Dyson
9 8461 La Mesa Boulevard
10 La Mesa, CA 91942
11 (619) 462-3311

12 Edward Patrick Swan, Jr., Esq. (SBN 089429)
13 Jones Day
14 12265 El Camino Real, Suite 200
15 San Diego, CA 92130
16 Telephone: (858) 703-3132
17 Facsimile: (858) 314-1150

18 Attorneys for Defendants

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

21 SECURITIES AND EXCHANGE
22 COMMISSION,

23 Plaintiff,

24 v.

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

Defendants.

Case No. 12 CV 2164 GPC JMA

**DEFENDANTS' REPLY BRIEF IN
SUPPORT OF MOTION FOR
MODIFICATION OF PRELIMINARY
INJUNCTION ORDER TO REMOVE
WESTERN FINANCIAL PLANNING
CORPORATION FROM
RECEIVERSHIP**

Date: June 20, 2014

Time: 1:30 p.m.

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Judge: Hon. Gonzalo P. Curiel

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STATUTES

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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 reply brief in support of Defendants’ Motion for Modification of this
5 Court’s order of October 5, 2012 (final order March 13, 2013) granting a
6 Preliminary Injunction and appointing a receiver for Western and the real estate
7 general partnerships established through Western (“GPs”).

8 I.

9 INTRODUCTION

10 Preliminary injunctions can be modified when there have been changes in law
11 or fact that mean that the original terms of the injunction are obsolete or
12 unnecessary, which are “new circumstances that have arisen after the district court
13 granted the injunction.” *Credit Suisse First Boston Corp. v. Grunwald*, 400 F.3d
14 1119, 1124 (9th Cir. 2005). Furthermore, because a receivership “is not an end in
15 itself” (*Gordon v. Washington*, 295 U.S. 30, 37 (1935)), it “must be monitored to
16 ensure it is still serving the function for which it was created.” *SEC v. Madison Real*
17 *Estate Group, LLC*, 647 F. Supp. 2d 1271, 1275 (D. Utah 2009) (citing *Gordon*, 295
18 U.S. at 37).

19 In this case, the circumstances that may have originally warranted a
20 receivership over Western no longer exist after almost two years of receivership,
21 and therefore the Preliminary Injunction should be modified to release Western
22 because the receivership no longer serves the function for which it was created.

23 Defendants moved for Western’s release from the Court-ordered receivership
24 on the grounds that no misappropriation of funds, commingling, or other financial
25 mismanagement has been identified or even alleged as to the GPs or Western,
26 thereby eliminating the need for the Receiver’s oversight of Western’s finances; that
27 the Receiver’s purpose of clarifying Western’s financial affairs has been completed;
28 that the remaining terms of the preliminary injunction will adequately protect the

1 status quo and alleviate any concerns the Securities and Exchange Commission
2 (“SEC”) has about protecting the public pending the outcome of this litigation; and
3 that Western’s remaining business operations are minimal at best, consisting of
4 collecting receivables, paying the underlying notes from Western to the original
5 sellers of the GP-held lands, maintaining the servers and archives, and paying taxes
6 and insurance.

7 Notwithstanding that Western has been rendered toothless by the other terms
8 of the Preliminary Injunction and will remain so pending the outcome of this case,
9 both the Receiver and the SEC have opposed Defendants’ motion for modification.
10 The Receiver’s vituperative opposition, which is long on factual misstatements and
11 short on evidence and law, fails to present a cogent case for continuing his presence,
12 while simultaneously displaying reasons for his removal.

13 The SEC’s opposition, while more-reasoned and much-less hyperbolic than
14 the Receiver’s, is based on incorrect assumptions about Defendants, including
15 purported conflicts of interest that have not arisen (or if so, solely through the
16 Receiver’s activities, such as the needless lawsuits against the LinMar entities) and
17 the continued practice of confusing the need for a receiver over Western with the
18 purported need for continuing the receivership over the GPs. Both oppositions fail
19 to overcome the changed factual circumstances that merit the end of the
20 receivership.

21 **II.**

22 **ARGUMENT**

23 **A. The Receiver’s Opposition Is Wildly Factually Inaccurate While**
24 **Failing to Present Plausible Grounds for His Continued Presence**

25 In his opposition, the Receiver makes various spurious, unproven, and
26 inaccurate claims that, at times, go even beyond what the SEC has alleged. Among
27 the Receiver’s purported grounds for maintaining his control of Western – all of
28 which have no cited support from the record or caselaw:

- 1 • Schooler “marked up the land sold to the General Partnerships (“GPs”) as much as 1,821%” (Dkt. No. 584, 2:13-14) when even the SEC has
2 alleged no more than a 775% markup (Dkt. No. 1, p. 12), the Receiver
3 has not provided any mathematical calculations for his purported
4 “fact,” and when no evidence of even a 775% markup – let alone any
5 explanation as to how a markup is *de jure* fraudulent – has been
6 submitted to the finder of fact;
- 7
- 8 • Schooler having “drained more than \$80 million from Western” (Dkt.
9 No. 584, 2:14-15), despite this Court having found no evidence of any
10 misappropriation, commingling, or offshoring of Western’s funds (Dkt.
11 No. 59) and that the Receiver had found Western’s financial records so
12 “accurate and reliable” (Dkt. No. 182, p. 14) that he relied on them for
13 his two-part Forensic Accounting Report (Dkt. Nos. 182, 504);
- 14 • Schooler “put[ting] investors in the position of either receiving pennies
15 on the dollar or paying operational bills for years to come in the hope
16 of one day recovering some larger percentage of their losses” (Dkt. No.
17 584, 2:16-18), when it was the *Receiver* who proposed the sale of the
18 GP-held properties for pennies on the dollar over Defendants’ objection
19 (see Dkt. Nos. 203, 210), the GPs are intended for long-term land
20 holding of unspecified duration (see Dkt. No. 14-3, ¶¶ 8, 14), and
21 dozens of GPs have sold their land for a profit that typically is four to
22 seven times the original investment by the GP investor-partners (Dkt.
23 No. 12-1);
- 24 • “The Receiver has reduced Western’s operating expenses to a fraction
25 of what they were under Mr. Schooler” (Dkt. No. 584, 3:6-7) when the
26 reduction of operating expenses can be more-accurately attributed to
27 the Preliminary Injunction’s ban on the continued marketing and sale of
28 GP interests to would-be investors (Dkt. No. 174, Part I), which would

1 have the effect of eliminating the expenses of maintaining office space,
2 paying sales and administrative staff, etc., and reducing Western's
3 operations to a minimal "caretaker" level of collecting receivables,
4 making payments on the Underlying Notes, paying taxes and insurance,
5 and preserving electronic and paper records.

6 The Receiver does not explain how his presence over Western remains
7 necessary given that the remaining terms of the Preliminary Injunction, including
8 the ban on selling GP interests, transferring or disposing of assets, or destruction of
9 records, would adequately protect the public at large from any potential harm by
10 Western pending the outcome of this case. Nor does the Receiver explain how he
11 can manage Western's remaining operations - collecting receivables, making
12 payments on the Underlying Notes, paying taxes and insurance, and preserving
13 electronic and paper records - more efficiently or more legally-compliant than
14 Western or Schooler can.

15 Many of the other tasks that the Receiver is performing, such as selling
16 Western's land holdings and suing the LinMar entities, are unnecessary to the
17 operation of Western or the preservation of assets for investors, since the main
18 assets for the investors are, and have always been, the parcels owned by the
19 investors' GPs.

20 Unlike the lion's share of securities fraud cases, in which the promoter takes
21 the investors' money and absconds with it, the investors in this case have actually
22 received something of value in return for their money - title to land for appreciation
23 and resale - and hence the liquidation of Western's land holdings and the lawsuits
24 against the LinMar entities serve no valid purpose for recovering funds for
25 investors. Rather, those actions are done for the apparent purpose of raising funds to
26 pay the Receiver; certainly the Receiver has never paid a cent to any investors.

27 Therefore, the Receiver's opposition does not provide adequate justification
28 for his continued control of Western.

1 **B. The SEC's Opposition Confuses Western with the GPs and is**
2 **Based Upon Purported Conflicts Arising Solely from the Receiver's**
3 **Actions**

4 The SEC's opposition to Defendants' Motion has three threads: (1) The
5 Receiver is necessary to perform certain administrative tasks; (2) the Receiver is
6 necessary to provide information to the GP investors; and (3) the Receiver has to be
7 present to avoid conflicts of interests that would (purportedly) result if Schooler is
8 allowed to run his own corporation again. However, all three threads are flimsy
9 because they are based upon the SEC's conflating of the GPs with Western or upon
10 self-fulfilling prophecies that the Receiver has created.

11 The list of Receiver's tasks, as described above (Part II.A, *infra*) are either
12 wholly unnecessary as not protecting the GPs or their investors (such as suing the
13 LinMar entities) or can be performed by Schooler and whomever he hires (such as
14 collecting receivables; paying the Underlying Notes, taxes and insurance;
15 maintaining records). The SEC has not advanced a sound reason for keeping the
16 receivership in place.

17 With regard to "protecting the investments of certain GPs by paying the
18 mortgages encumbering the GPs' land," Dkt. No. 587, 7:2-3, the SEC confuses the
19 receivership over *the GPs* with the receivership over *Western*. The mortgages
20 encumbering the GPs' land do not require the Receiver's presence; their payment is
21 an administrative matter. Moreover, in cases of dire necessity, such as shortfalls in
22 Western's cash (including those caused by the Receiver's claiming priority of
23 payment), the GPs can simply redirect their GP note payments directly to the
24 original sellers, bypassing Western completely. This is a protection provided to the
25 GPs under the all-inclusive deed of trust (AITD) entered into with Western when the
26 GPs purchased their interest from Western; it is a common mechanism in AITDs
27 and serves as a fail-safe protection to the GPs, allowing them to simply and easily
28 preserve their title should Western ever fail to meet its obligation. *See* Dkt. No. 14-

1 2 (example of GP AITD). Thus, the Receiver's control of Western is unnecessary
2 for the purpose of paying the mortgages. The GPs can pay the mortgages without
3 the Receiver's help, either directly or through Western.

4 The SEC's claim that the Receiver's presence is necessary to ensure that the
5 GP investors get accurate information (Dkt. No. 587, 8:10-9:6) misses the point.
6 Once again, the SEC tries to confuse the issue of whether *Western* should remain
7 under receivership with the issue of whether *the GPs* should remain in receivership
8 – an issue that is outside the scope of Defendants' motion and that is the subject of a
9 separately briefed hearing.

10 Whether *Western* is in receivership has nothing whatsoever to do with
11 providing case updates and factual information to the investors, other than for the
12 SEC to try to prove that Western "controls" the GPs by pointing to the continued
13 receivership over Western, for purposes of providing information to the investors, as
14 proof. The SEC simply dislikes that Schooler endeavors to provide accurate facts
15 to the investors in response to the Receiver's distortions or omissions of fact.

16 As previously noted by Defendants, the Receiver has done a poor job of
17 conveying information to investors; that failing certainly tilts in favor of his
18 removal. *See* Dkt. No. 407, p. 11, fn. 3 (quoting letters from investors). The SEC
19 can post documents on its website if it claims that Schooler presents inaccurate
20 information to the investors (which Defendants deny). The Receiver's control of
21 Western is unnecessary for, and unrelated to, the purpose of providing accurate
22 information to GP investors.

23 Indeed, the SEC tries to spin a report from one investor regarding the
24 repayment of amounts loaned by Western to the GPs as proof of Defendants'
25 purportedly inaccurate information. The investor's belief that "the GPs are being
26 forced to pay back loans to Western Financial that my understanding Western has
27 not requested be repaid" (Dkt. No. 587, 8:23-25) is not "mistaken" as the SEC
28 claims, but is accurate: Western did not intend for the GPs' loans to be repaid until

1 the GP-held lands sold, but that intention was upset by the appointment of the
2 Receiver. See attached Declaration of Louis Schooler (“Schooler Decl.”), ¶¶ 3-4.
3 Once the Receiver was in place, the relaxed system of repaying Western was upset.

4 With regard to the purported conflicts of interest resulting from the
5 receivership being lifted, the SEC ignores that the conflicts resulted from the
6 Receiver’s decision to pursue legal action against the LinMar entities. As with the
7 loans from Western to the GPs, there was no intention by Western to demand
8 payment of the loans to the LinMar entities upon the due dates specified in the
9 promissory notes from the LinMar entities to Western; repayment would occur
10 when the LinMar entities had sufficient cash on hand after paying all mortgages and
11 expenses. Schooler Decl., ¶¶ 5-6. It was solely the Receiver who chose to pursue
12 legal action against the LinMar entities despite having knowledge of the LinMar
13 entities’ currently-poor financial situation; the Receiver chose to expend funds
14 trying to get money that is not there, for the apparent purpose of ensuring his
15 payment. See Schooler Decl., ¶ 7. If anything, the removal of the receivership over
16 Western should lead to a reconsideration of the litigation against the LinMar
17 entities, since the litigation accomplishes nothing but generating more purported
18 justification for the Receiver’s bills in chasing activities that have been
19 demonstrated not to benefit the Receivership estate.

20 Lastly, the SEC’s claim that there is a conflict of interest between one of
21 Defendants’ counsel (Mr. Hougen) and Western ignores the realities of legal
22 malpractice law in California. The statute of limitations contains a tolling clause for
23 continuous representation involving the same subject matter; once this case ends, the
24 clock begins to run for any malpractice claims that Western may have against Mr.
25 Hougen. See Cal. Code Civ. Proc. § 340.6(a)(2); *Gurkewitz v. Haberman*, 137
26 Cal.App.3d 328 (1982). The “‘continuous representation’ rule was adopted in order
27 to ‘avoid the disruption of an attorney-client relationship by a lawsuit while enabling
28 the attorney to correct or minimize an apparent error, and to prevent an attorney

1 from defeating a malpractice cause of action by continuing to represent the client
2 until the statutory period has expired.” *Laird v. Blacker*, 2 Cal. 4th 606, 618 (1992)
3 (internal cites omitted). Keeping the Receiver in place for purposes of evaluating
4 any potential legal claims, at a time when actual injury may not have accrued and all
5 possible claims are tolled under the continuous-representation clause of Code of
6 Civil Procedure section 340.6(a)(2), would serve no constructive purpose.

7 IV.

8 CONCLUSION

9 Despite the best efforts of the SEC and Receiver for justifying the Receiver’s
10 continued control of Western, the oppositions do not rebut the facts that the
11 receivership has outlived its initial purpose. There has been no misappropriation;
12 the financial records were fair and accurate and all transactions accounted for;
13 Western’s activities are controlled by the remaining terms of the Preliminary
14 Injunction; and the investors still have the land that they invested in, through the
15 GPs. The tasks that the Receiver oversees are either simple matters not requiring his
16 expensive supervision (collecting receivables, paying Underlying Notes, paying
17 taxes and insurance, maintaining records) or are wholly unnecessary for protecting
18 the investors (such as suing the LinMar entities). For the reasons stated above and
19 in their Motion for Modification, Defendants respectfully request that this Court
20 modify the Preliminary Injunction and dissolve the receivership in its entirety as to
21 Western.

22 DATE: May 23, 2014

Respectfully submitted,

23 /s/Philip H. Dyson

24 Philip H. Dyson, Esq. (SBN 097528)

25 Law Office of Philip H. Dyson

26 8461 La Mesa Boulevard

27 La Mesa, CA 91942

28 Counsel for Defendants

