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UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF CALIFORNIA

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

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

Defendants.

Case No.: 3:12-cv-02164-GPC-JMA

ARDIZZONE INVESTORS' REPLY TO RECEIVER'S OPPOSITION TO MOTIONS (1) FOR A STAY OF ORDERS PENDING APPEAL, (2) TO ALTER OR AMEND A JUDGMENT, AND (3) FOR RECONSIDERATION

Date: November 10, 2016
Time: 1:30 p.m.
Ctrm: 2D
Judge: Hon. Gonzalo P. Curiel

I. Introduction

The receiver, Thomas C. Hebrank ("Hebrank") has failed to address most of the issues raised by the Ardizzone Investors' motion for a stay. Space limitations prevent us from addressing all of them. While Hebrank now expressly admits two false statements in his declaration, he tacitly admits a third one with total silence. Hebrank knew he never sent any form of notice to Joseph M. Ardizzone ("Ardizzone") of the liquidation plan that strips Ardizzone of his property rights.

The Ardizzone Investors opening brief confronted Hebrank with the names of more than 1,000 investors who, like Ardizzone, never received his emails. It also projected the total number was between 1,000 and 1,200. Facing this evidence, Hebrank now admits that his May 6, 2016, email—the one giving notice of his liquidation plan—failed to reach 1,082 investors. By itself, this establishes a violation of the notice requirements in *Mullane v. Central Hanover Bank & Trust Co.*339 U.S. 306 (1950).

II. The Unsworn Hearsay Statements of Hebrank's Counsel Should Not Be Treated as Evidence When Hebrank's Sworn Statements Are Untrue

Hebrank admits his declaration (Dkt. No. 1355-1) contained untrue statements, but claims they are immaterial. Dkt. No. 1383 at 5. One covered up the fact his October 10, 2012, letter was not sent to all investors. Hebrank swore that he directed two GP secretaries to send letter to investors. Dkt. No. 1355-1, ¶ 3. In this way, any failure to send the letters to all investors—and 24 did not receive it[1]—would be placed with former Western employees. But this time, Hebrank's own email (Dkt. 1368-8 at 5, Ex. 1) impeaches his declaration. Dkt. No. 1355-1, ¶ 3.

Hebrank excuses his misstatements, because the "relevant letters and emails were sent and received several years ago, it is not surprising the Receiver's recollection of these details might be slightly off in one or two minor ways." Dkt. No. 1383 at 5. In essence, Hebrank is telling the Court that neither he nor his attorney checks the facts before

[1] See Declaration of Alice Jacobson filed herewith, ¶ 5.

Hebrank swears to them. Hebrank's explanation could defend him against a perjury charge, but it does little to restore his credibility.

A different inference could also be drawn: Hebrank may be careless with the truth, because he has no fear of contradiction. He routinely deletes his emails. Dkt. No. 967, at 3-4. This is a puzzling practice for a steward of other people's money. One might expect a steward—protective of his reputation for honesty—to preserve his emails in the event someone accuses him of an impropriety. Instead, Hebrank deletes them. Why?

Hebrank responds with silence, proof that his declaration has a third untruth: his claim that he sent emails to Ardizzone. That would be impossible. His attorney provided a copy of the email address Hebrank supposedly used to communicate with Ardizzone. Dkt. No. 1368-2, ¶ 7, Ex. 4. The email address misspells Ardizzone's name and the very first email would have bounced back. *Id*., ¶ 8 and Dkt. No. 1368-4, ¶ 2. This is easily verifiable. Thus, Hebrank knew his emails never reached Ardizzone and hundreds like him for whom Hebrank had an erroneous email address.

Hebrank would now clarify the untruths in his sworn statement with an *unsworn and inadmissible* statement, which the Ardizzone Investors address next.

III. Objection and Motion to Strike Unsworn Inadmissible Statements

The Ardizzone Investors object and move to strike the factual statements in Hebrank's opposition to this motion relating to his service of emails on investors through MailChimp (Dkt. No. 1383 at 5, l. 27 to p. 6, l. 18) on the grounds the statements are inadmissible hearsay, violate the best evidence rule (Fed. R. Ev. 1001-1008), and do not conform to the procedures for submitting evidence to oppose a motion, i.e., by affidavit or declaration. The Ardizzone Investors also submit that Hebrank should serve a proof of service identifying by name of the persons he claims to have served by his May 6, 2016, email, and any evidence available to him which of those persons opened the email. *SEC v. Global Online Direct, Inc.*, 2007 U.S. Dist. LEXIS 81803 (N.D. Ga. Nov. 5, 2007).

Further, Hebrank has chosen to offer weaker evidence—unsworn, inadmissible, and conclusory statements—instead of the hard evidence he possesses. Hebrank could

have submitted a proof of service stating the name of each person he served by email or any other way. He previously filed a list of investors by name pursuant to Local Rule ("L.R.") 66.1. He would only need one sentence: "I served the following investors by …." His failure to provide a proof of service, the strongest evidence, gives additional reason to distrust the inadmissible, unsworn, and conclusory statements he did offer. *Runkle v. Burnham*, 153 U.S. 216, 225-226 (U.S. 1894)("production of weaker evidence, when stronger might have been produced, lays the producer open to the suspicion that the stronger evidence would have been to his prejudice"); *Allen v. Matson Navigation Co.*, 255 F.2d 273, 280 (9th Cir. 1958).

IV. Hebrank's Admissions Prove A Violation of Investors' Due Process Rights

Though Hebrank postures, "the New Aguirre Investors fabricate and grossly misstate the facts regarding the percentage of investors who receive email notices from the Receiver," (Dkt. No. 1383 at 5-6) he immediately admits the Ardizzone Investors correctly projected the number of investors (between 1,000 to 1,200) who do not receive his emails, including his May 6, 2016, "notice" of his liquidation plan. Dkt. No. 1368-1 at 15. He concedes 1,086 investors do not get his emails (Dkt. No. 1383 at 6), almost the exact mid-point of the 1,000-1,200 projection by the Ardizzone Investors.

But to get the truth, one must deconstruct Hebrank's numbers, which have three components. First, he claims to have no email address for 12% of the 3,370 investors,[2] i.e., 404 investors. *Id.* Second, he admits 10% of the emails from MailChimp are not delivered to investors, i.e., another 338 investors. *Id.* Finally, he admits 344 investors have unsubscribed, another 10%. *Id.* The table below summarizes those facts:

Category	Percentage	Absolute Number
Investors who provided no email address	12%	404
Investors who do not receive emails from MailChimp	10%	338
Investors who unsubscribed	10%	344

[2] Dkt. No. 75-1 at 5.

Total investors who do not receive Hebrank's emails	32%	1,086

To satisfy the notice requirements of due process, Hebrank must comply with the mandates of *Mullane*. In *Mennonite Bd. of Missions v. Adams*, 462 U.S. 791, 796 (U.S. 1983), the Supreme Court explained how *Mullane* changed the law where property owners are divested of their rights, such as they are in this case, through proceedings *in rem*: "Beginning with *Mullane*, this Court has recognized, contrary to the earlier line of cases, that 'an adverse judgment *in rem* directly affects the property owner by divesting him of his rights in the property before the court." *Mennonite* explained the impact of *Mullane* on Supreme Court decisions over the prior three decades: "Our cases have required the State to make efforts to provide actual notice to *all interested parties* comparable to the efforts that were previously required only in *in personam* actions (emphasis added)." *Id*. at 796. On the same point, *Mennonite* continued: "In subsequent cases, this Court has adhered unwaveringly to the principle announced in *Mullane*." *Id*., at 797.

Hebrank's admissions—by themselves—demonstrate his notices fail to satisfy *Mullane*'s mandates. To begin with, Hebrank could easily "provide actual notice" to more than 99% of "all interested parties." He had the mailing address for all but 24 of the 3,370 investors. Jacobson Decl. ¶ 5. Hence, using mail to give notice, he would have been near compliant with *Mullane*, short by only 24 investors. He was obligated under *U.S. v. Ritchie*, 342 F.3d 903 (9th Cir. 2003) to use alternative means of service on these investors. *Ritchie* held that: "[W]hen initial personal notice letters are returned undelivered, the government must make reasonable additional efforts to provide personal notice." *Id*., at 911

But he did not use the U.S. mail or any other service to *send* 1,082 investors notice of his liquidation plan or the May 20, 2016, hearing. Instead, he posted the motion to his website, which he knew most investors did not visit. Dkt No. 852 at 2. Even if a Court order approved such notice, and none did, his "notices" fail to meet the mandates of *Mullane* and its progeny, which require Hebrank "to make efforts to provide actual notice

to all interested parties comparable to the efforts that were previously required only in *in personam* actions." *Mennonite,* 462 U.S. at 796.

But once again, analyzing Hebrank's numbers, it appears necessary to revise upward the projection of the number of investors *who were not* served by his emails. We have no way to confirm the accuracy of Hebrank's statement that his emails were delivered to all but 1,086 investors, except for his claim he has email addresses for all but 12% of investors, 404 investors. Dkt. No. 1383 at 6. Hebrank does not dispute our statement that Western's records in March 2015 showed he had no email address for 571 investors. He does not explain how he reduced the number of these investors from 571 to 404. The investors committee wrote 70 of these investors and 24 replied with answers to the question whether they had ever received an email from the receiver. All 24 said no. Gilman Decl. filed herewith, ¶ 6. Nor is there any letter from Hebrank to the investors for whom he has no email address or the wrong email address requesting a current email address. Aguirre Decl. ¶ 8.

Alice Jacobson filed a sworn statement that Hebrank never requested the GP secretaries to take any steps to get current email addresses for investors. Dkt. No. 1368-6, ¶ 5. She has filed a supplement to that declaration explaining why the email addresses became more stale and inaccurate with the passage of time. Jacobson Decl., ¶ 6.

Dennis Gilman has also filed a supplemental declaration stating that he has conducted a further review of the 731 undelivered emails using the Hebrank's August 2014 list. He now concludes that almost all of them were undelivered, because of an inaccurate email address. Gilman Decl. ¶ 4.

Hebrank states he "uses" MailChimp to deliver mass emails to investors. Dkt. No. 1383 at 6. Our investigation indicates the first email Hebrank sent with MailChimp was on May 6, 2016. Declaration of Gary J. Aguirre filed herewith ("Aguirre Decl.") ¶ 3. MailChimp may do a better job at sending emails to investors than Hebrank, but it cannot send emails to addresses it does not have.

And then there is one other question: how many investors do not open Hebrank's emails? On this point, Hebrank defends himself: "the Receiver has no control over whether people choose to provide their email address, choose to unsubscribe from receiving emails, or choose not to read emails they receive." Dkt. No. 1383 at 6. But he does control the form of the notice to investors. In this light, he knows—or has the information readily available to him—how many investors are opening his emails. Hebrank told the Court he uses MailChimp to send his emails to investors. MailChimp offers the following service:

> Our interactive graphs show you how many emails were delivered, how many people opened your email, what percentage clicked, and more…See which email addresses bounced and why. We'll automatically determine whether we should retry sending or permanently delete those email addresses from your list….Find out who unsubscribed from your list, and we'll keep track of them so you can't accidentally add them to your list later.

Aguirre Decl., ¶ 5, Ex. 1. Further, as discussed in our opening brief, Allen Matkins obviously knows of these types of services, since it was able to report to the court in *SEC v. Global Online Direct, Inc.*, 2007 U.S. Dist. LEXIS 81803 (N.D. Ga. Nov. 5, 2007) the percentage of investors who were opening the receiver's emails. In short, it is probable that a majority of investors were never informed by Hebrank of his liquidation plan, which divests them of their property under the GP agreements.

V. Hebrank Has All But Conceded His Violation of L.R. 66.1

Hebrank argues "the Court has discretion to modify the Local Rules and determine what notices are appropriate under the specific circumstances." Dkt. No. 1383 at 5. On this point, The Ardizzone Investors agree with the SEC that *Prof'l Programs Group v. Dep't of Commerce*, 29 F.3d 1349, 1353 (9th Cir. 1994) states the applicable legal principle: "Local rules have the 'force of law' and are binding upon the parties and upon the court, and a departure from local rules that affects 'substantial rights' requires reversal." The departure from L.R. 66.1 in the district court proceedings clearly affected

investors' substantial rights. Hebrank does not try to address the Ardizzone Investors' argument in their opening brief that he violated L.R. 66.1 in failing to give investors notice of his permanent appointment. Dkt. No. 1368 at 17-22. He has apparently left it up to the SEC to try to defend him on this issue.

In essence, the SEC is attempting to defend the indefensible. The Court's September 6, 2012, order directed Hebrank to send notice to investors as required by L.R. 66.1:

> The Court-appointed Receiver shall provide notice of this TRO and the Order to Show Cause re Preliminary Injunction and Appointment of a Permanent Receiver, by certified mail, on all receivership entities and their general partners, including but not limited to the entities listed on Schedule 1.

Dkt. No. 10 at 20. Local Rule 66.1.a.2 required that notice be sent seven days before the hearing. Since the hearing was set for September 17, 2012, the rule required Hebrank to send notice by mail no later than September 10. He failed to send it. He later stipulated to his permanent appointment with the SEC and thus no hearing was held and no notice was given. The Ardizzone Investors address this issue at more length in their reply to the SEC's opposition.

The Court's order denying the Ardizzone Investors' motion to intervene implied, as the SEC had argued, that Hebrank's May 6, 2016, email complied with the requirements of L.R. 66.1. Dkt. No. 1359 at 3. The Court appeared to adopt the SEC's argument on this point. As stated in their August 23, 2016, opposition:

> Mr. Aguirre argues that the Receiver failed to comply with Local Rule 66.1 because the Receiver's notice of the February 2016 distribution motion was not 'timely' and was by 'email.' *Id*. at p. 4. *But Local Rule 66.1 requires nothing more than two weeks' notice, and that is exactly what the Receiver provided*—a fact that Mr. Aguirre acknowledges, as he must, in his motion (emphasis added).

Dkt. No. 1358 at 9-10. In its most recent filing, the SEC has abandoned the above argument and now argues that L.R. "66.1.f.1 does not apply" (Dkt. No. 1389 at 13) and relies on Hebrank's argument that his plan does not come within the scope of L.R.

66.1.f.1. However, neither Hebrank nor the SEC disputes the language in paragraph 2 of the March 7, 2013, order (Dkt. No. 170 at 3) would require the notice be sent by mail.

The Ardizzone Investors interpret L.R. 66.1 in the same way the Supreme Court directs a statute be interpreted. “Statutory interpretation, as we always say, begins with the text,” *Ross v. Blake*, 136 S. Ct. 1850, 1856 (U.S. 2016). Local Rule 66.1.f.1 reads: "Notice of Hearings. The receiver must give all interested parties at least fourteen (14) days' notice of the time and place of all pertinent hearings of all: 1. Petitions for the payment of dividends to creditors." Hebrank's motion clearly falls within the definition of a "petition."[3] The term "dividend" does not just refer to the periodic payments by a corporation to its shareholders. When used in receivership proceedings, "dividend" means "any excess cash generated" less disposition cost and reserves met. *MBIA Ins. Corp. v. FDIC*, 708 F.3d 234, 246 (D.C. Cir. 2013). Neither the SEC nor Hebrank dispute investors are "creditors" within the meaning of L.R. 66.1.f.1. The definition of "creditors" includes investors who hold contracts and/or investment contracts of the debtor and thus includes all investors in this case.[4]

The SEC and Hebrank's argument boils down to this: Hebrank's plan “did not seek to pay any dividends or distributions to any investors or creditors and no such distributions can be made without further orders of the Court.” Dkt. No. 1383 at 3. But the language of L.R. 66.1.f does not require the payment be immediate and requires no further orders. The language is far broader: “The receiver must give all interested parties at least fourteen (14) days' notice of the time and place of *all pertinent hearings* of all: (1) Petitions for the *payment* of dividends to creditors.” The hearing decided that funds would be taken from

[3] Black's Law Dictionary defines a "petition" as: "A written address, embodying an application or prayer from the person or persons preferring it, to the power, body, or person to whom it is presented, for the exercise of his or their authority in the redress of some wrong, or the grant of some favor, privilege, or license."

[4] *In Re Los Angeles Land & Invest., Ltd.*, 282 F. Supp. 448 (D. Haw. 1968). See also: *SEC v. McGinn, Smith & Co.*, 2011 U.S. Dist. LEXIS 49548 *15 (N.D.N.Y May 6, 2011)("'creditor' is 'a person having a claim, whether matured or unmatured, liquidated or unliquidated, absolute, fixed or contingent.'")

some investors and given to all. In his own terms, Hebrank's motion requested an order "approving the One Pot Approach to distributing receivership assets." Dkt. No. 1181-1 at 25. It stated that the amount would be approximately 13.4% of the amount invested by each investor. *Id*., at 13. This Court's order specifically approved the "one pot" distribution. Dkt. No. 1304 at 31. It could not be clearer that Hebrank's motion (Dkt No. 1181) falls within the language of L.R. 66.1.f and thus Hebrank was obligated both under L.R. 66.1 and under the Court's March 7, 2013, order to send the notice by mail.

The Supreme Court also instructs that: "Text may not be divorced from context." *Univ. of Tex. Southwestern Med. Ctr. v. Nassar*, 133 S. Ct. 2517, 2530 (2013). The context of L.R. 66.1.f makes clear the receiver should give notice to investors of every significant step in the process of the receivership. None has a greater effect on investors than his proposed plan. Hence, context points to the conclusion that L.R. 66.1.f.1 applies to the liquidation plan. Consequently, Hebrank violated the order, L.R. 66.1.f, and *Mullane* by his email and website "notice."

VI. Hebrank in Effect Argues Investors Waived Their Right to Notice.

Hebrank argues that, to the extent investors did not receive the notice, it is their fault. And they should be treated as if they received it and agreed to it. This is not a claim that Hebrank gave investors notice. Rather, Hebrank argues that investors waived their rights to receive notice of his plan to divest them of their rights under the GP agreements. "Waivers of constitutional rights not only must be voluntary but must be knowing, intelligent acts done with sufficient awareness of the relevant circumstances and likely consequences." *Brady v. United States*, 397 U.S. 742, 748 (1970).

VII. Investors Are Unaware of the Existence or Effect of Hebrank's Plan

Hebrank now concedes he sent no notice to approximately one third of investors. The Ardizzone Investors have presented the different categories of investors who are likely unaware of Hebrank's plan and its operative effect. They are investors (1) for whom Hebrank has no email address, (2) for whom Hebrank has an erroneous email address, (3) who have unsubscribed to his emails, and (4) who do not open Hebrank's emails. The

Ardizzone Investors have filed the supplemental declaration of Dennis Gilman, which confirms two key facts (1) more than half of investors (for whom Hebrank has email addresses) responding to a questionnaire state they are not aware of Hebrank's liquidation plan (Gilman Decl., ¶ 8) and (2) 24 of 24 investors for whom Hebrank has no email address, according to Western's records in August 2014, have never received an email from Hebrank, even though 23 of the 24 have confirmed their email addresses. *Id*., ¶ 6. These statistics corroborate our interpretation of Hebrank's unsworn, inadmissible, and conclusory statements that less than half of investors understand what Hebrank is proposing to do.

VIII. Hebrank's Efforts to Intimidate

While defending its filing of a declaration that made three false statements, its failure to comply with L.R. 66.1, and admitting for the first time its email "notice" failed to reach one third of investors, Allen Matkins goes on the attack. It puts into play an old maxim: "The best defense is a good offense." The Ardizzone Investors will not spend their limited space responding to groundless allegations presented in violation of procedures designed to address such contentions. Nor will Allen Matkins' repeated efforts to intimidate the Ardizzone Investors' attorney deter him from their zealous representation.

DATED: October 17, 2016

Respectfully submitted,

By: /s/ Gary J. Aguirre

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