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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. 12 CV 2164 GPC JMA **DEFENDANTS' RESPONSE TO SECOND INTERIM APPLICATIONS FOR APPROVAL AND PAYMENT OF FEES AND COSTS (RECEIVER AND COUNSEL TO RECEIVER)** Date: May 10, 2013 Time: 1:30 p.m. Courtroom: 9 Judge: Hon. Gonzalo P. Curiel **NO ORAL ARGUMENT UNLESS REQUESTED BY THE COURT**

Defendants LOUIS V. SCHOOLER and FIRST FINANCIAL PLANNING CORPORATION (collectively "Defendants") respond as follows to the Second Interim Applications for Approval and Payment of Fees and Costs to the Court's appointed receiver, Thomas C. Hebrank, CPA ("Receiver"), and the receiver's counsel, Allen Matkins Leck Gamble Mallory &Natsis LLP ("Receiver's Counsel").

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I.

INTRODUCTION

Receiver, on behalf of himself and Receiver's Counsel, has filed a set of second interim applications for payment of fees and costs for himself and Receiver's Counsel, involving the continued receivership of Western Financial Planning Corporation ("Western") and the various general partnerships established through Western that are the subject of this litigation ("GP's") during the period of October 1, 2012 through December 31, 2012.

The Receiver and Receiver's Counsel claim to have incurred a total of $109,604.97 in fees and costs for work performed for those three months, with $61,432.65 in fees and $301.92 in costs for the Receiver, and $45,817.65 in fees and $2,052.75 in costs for Receiver's Counsel. Dkt. No. 178. Although the Receiver seeks interim payment of $55,289.38 in fees (and 100% of costs) and Receiver's Counsel seeks $36,654.12 in interim payment of fees (plus 100% of costs), the remaining amounts would be sought for recovery at the conclusion of the receivership; they are not being permanently waived or forfeited.

Defendants object to the Second Interim Applications on the same grounds as their objection to the First Interim and/or Final Applications: that the fees and costs to be recovered continue to be unreasonable and have still not benefitted Western or the GP's, and that the Receiver should not be allowed to invade GP-owned funds to pay obligations that the Receiver clearly considers to be those of Western. The Receiver has yet to provide any rationale for using GP funds to pay Western's obligations.

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II.

ARGUMENT

A. THE RECEIVER'S FEE APPLICATIONS MUST BE REASONABLE AND MUST BE CLOSELY SCRUTINIZED TO AVOID EVEN THE APPEARANCE OF A WINDFALL

Courts scrutinize fee applications to ensure they are reasonable. *Hensley v. Eckerhart*, 461 U.S. 424, 433 (1983). Even if no objection is lodged, the court must carefully examine the fee application (whether by a receiver, counsel, or affiliated professional) to determine whether the time spent, services performed, hourly rates charged, and expenses incurred are justified. The trial court is vested with discretion regarding the amount of the award of fees and costs and any reduction of the desired award. *Hensley*, *supra*; *In re San Vicente Medical Partners, Ltd.*, 962 F.2d 1402, 1409 (9th Cir. 1992); *United States Football League v. Nat'l Football League*, 887 F.2d 408, 415 (2d Cir. 1989).

The applicant has the burden of proving that the compensation request is reasonable. *In re Beverly Mfg. Corp.*, 841 F.2d 365 (11th Cir. 1988); *Matter of U.S. Golf Corp.*, 639 F.2d 1197, 1207 (5th Cir, 1981); *In re Coastal Equities, Inc.*, 39 B.R. 304 (Bankr. S.D. Cal. 1984). To meet this burden, the applicant must keep and present records from which the court may determine the nature of the work done, the need for it, and the amount of time reasonably required. *In re Coastal Equities, Inc.*, 39 B.R. at 311 ("sufficiently detailed records of time spent and on what it was spent"). "It is not unduly burdensome to set forth with specificity what the topic of research or conference was, and indeed many times the application is quite precise (e.g. 'prepare motion to dismiss,' 'prepare trial brief re injunctive relief,' 'telephone conference with [trustee's attorney] re cash flow problem of corporation')." *Id.* "[T]he district court...must not only avoid awarding 'windfall fees' but avoid every appearance of having done so." *In re Equity Funding Corp. Sec. Litigation*, 438 F.Supp 1303, 1325 (C.D. Cal. 1977).

The analysis of reasonableness, as determined by this Court in its order approving in part the Receiver's First Interim and/or Final Fee Applications, is a multi-factor test described in *SEC v. Fifth Avenue Coach Lines*, 364 F.Supp. 1220, 1222 (S.D.N.Y. 1973): (1) the complexity of problems faced, (2) the benefit to the receivership estate, (3) the quality of work performed, and (4) the time records presented. Of these factors, the extent to which the receivership estate has benefitted from the receiver's efforts is especially important. *Specialty Products Co. v. Universal Indus. Corp.*, 21 F.Supp. 92, 94 (M.D. Pa. 1937). "What is left for the class, after fees have been awarded, is always a paramount consideration." *Spicer v. Chicago Bd. Options Exchange*, 844 F. Supp. 1226, 1250 (N.D. Ill. 1993).

The award of fees is to be reduced when the receiver's and counsel's conduct prolongs or complicates the case and increases legal costs. *Nowell v. International Trust Co.*, 169 F. 497 (9th Cir. 1909); see also *United States v. Larchwood Gardens, Inc.*, 404 F.2d 1108, 1114 (3d Cir. 1968).

B. THE FEES AND COSTS CLAIMED ARE UNREASONABLE

Upon applying the *Fifth Avenue Coach Lines* factors to the fee applications, there are many areas in which the applications fall short. There is no great complexity of problems faced, and the benefit to the receivership estate is slight at best.

The problems faced were not truly complex at the beginning of the receivership and have not grown more complex since. Although there are over 100 entities each with its own bank account, 22 properties, and over 3,300 investors, the accounts are all with one bank, the entities have a common office in San Diego with common storage, and the entities hold only raw land with no day-to-day management required. Furthermore, the money in the GP accounts has come directly from the individual investors for the purpose of paying the GPs' respective property tax payments and other administrative costs such as preparation of each GP's required Form K-1's.

The GPs have been able to meet all of their obligations for years at the nominal cost of between $100 and $400 per month, and these obligations and needs did not

suddenly increase upon the appointment of a receiver. The GPs' needs have been and remain extremely basic.

The Receiver owes an obligation to the receivership entities to preserve their assets and to adequately justify any amounts paid to himself out of their accounts, yet he has not explained what value he has provided to the GPs in return.

Moreover, the GP investor-partners have yet to be given an opportunity to be heard by this Court with regard to even the existence of the Receivership, let alone money being taken directly out of their accounts to pay the Receiver. The GP accounts' money is that of the individual investors comprising each GP. The Receiver has an obligation to examine how best to preserve the assets of the entities in his receivership, not to deplete their accounts without the entities even having a chance to be heard.

As all parties recall from the Receiver's First Fee Applications, dozens of GP investors wrote the court to express their concerns about their investments being jeopardized to pay the Receiver, at lease one investor remarked that the Receiver was not responsive to their queries, and another investor was told by an employee of the Receiver that typically the investors get no money back because all of the assets get sold to pay the legal fees. See Dkt. Nos. 114, 165. Defendants doubt those concerns will be any more mollified by the Receiver's representations in the Second Fee Applications than they were by the representations in the First Fee Applications.

The Receiver simply indicates there is enough money in the GP accounts to pay their obligations and also buy back Western's units, but availability of cash is hardly a rationale to justify a payment as appropriate. The more important question, never answered by the Receiver, is on what basis does the Receiver justify using GP-owned funds to pay the obligations of Western, *which is a legally-separate entity*.

Such action not only lacks a sufficient basis, it is in fact inconsistent and contrary to the Receiver's obligation to preserve and recover assets for the benefit of the investors, not raid their funds at will without their input. At a bare minimum, the

investors, who own the cash in question, should be balloted to determine whether they want their cash, no matter how abundant, used to pay the obligations of wholly separate and independent entities.

If GP funds are used to pay the Receiver's fees, the pace accelerates at which individual investors are required to replenish their respective GP operating funds. Again, these are the bank accounts from which the GPs pay their property taxes, non-payment of which can deprive the GPs of the titles they currently hold.

The Receiver's own application indicate a lack of results obtained and a conclusion that the receivership provides no benefit to the estate whatsoever. The Receiver admits that Western's financial situation has not changed significantly in recent months and that Western continues to be short on cash (Dkt. No. 176, p. 10 of 34, ll. 23-24). To meet this monetary shortfall, the Receiver proposes the reduction to cash of Western's equity interests in the GP's to pay the Receiver, as was previously requested and granted in the First Fee Applications. Defendants do not see how such parasitic actions would benefit the GP's or the investors who are the general partners.

There is much that is missing from the fee applications. There is no accounting of what amount or portion of recovery of Western's assets, if any, were obtained through the Receiver's (or his professionals') expenditures. There has been no accounting to date of the fruits of the Receiver's or Receiver's professionals' expenditures.

The court is not "required to fix fees in total disregard of the fact that this receivership produced a very lean harvest, that all interests suffered heavily, and that the whole enterprise was not a success." *Specialty Products Co. v. Universal Indus. Corp.*, 21 F.Supp. 92, 94 (M.D. Pa. 1937). There is no indication that any assets have been recovered, and no distributions have been made to the investors.

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The result obtained by the Receiver is a critical factor. *SEC v. Elliott*, 953 F.2d 1560, 1577 (11th Cir. 1992); *United States v. Code Products Corp.*, 362 F.2d 669, 673 (3d Cir. 1966). Since there has been no indication as to the results obtained through the Receiver's labors to date, the Receiver's work "merits an 'incomplete' grade" and therefore the fee application should be denied in its entirety or else the award should be reduced significantly. *In re Alpha Telcom, Inc.*, 2006 U.S. Dist. LEXIS 79997 at *16 (D. Or. Oct. 27, 2006).

At a minimum, the Receiver should not be allowed to use GP funds to pay himself for fees he characterizes as belonging to Western, an entity separate, distinct, and independent from the GPs.

C. THE RECEIVER'S "COMPARABLE" CASES DO NOT JUSTIFY THE RATES, FEES AND COSTS IN THIS CASE, BECAUSE THEY ARE SIGNIFICANTLY DISTINGUISHABLE

Although the Receiver and Receiver's Counsel present information as to hourly rates charged by receivers and counsel in three SEC receivership cases in Southern California to support their rates, the cases cited by the Receiver and counsel - *SEC v. Lambert Vander Tuig* and *SEC v. Homestead Properties L.P.* from the Central District of California, and *SEC v. Learn Waterhouse, Inc.*, from the Southern District - are not truly comparable. In fact, they are significantly distinguishable so as to make the receivers' and counsels' rates inapplicable.

Vander Tuig involved the fraudulent sales of unregistered shares in the Carolina Company, a corporation that purported to specialize in developing resort communities surrounding prestigious golf courses.[1] The stock was sold through a "boiler room" operation in Orange County at inflated prices, with misrepresentations

[1] *Vander Tuig*, No. 06-CV-00172 (C.D. Cal.); www.carolinareceivership.com; *Six O.C. Men Charged in $52-Million Investment Scam*, Los Angeles Times, Jan. 24, 2009, http://articles.latimes.com/2009/jan/24/business/fi-ponzi24).

as to the Carolina Company's going public and owning more properties than it actually owned. Not only did the Carolina Company own less land than was claimed in the investor promotional materials, but other land it claimed to own was under contract or option. Also, the defendants did not disclose that the Carolina Company common stock was available for purchase through the "Pink Sheet" quotation system at prices below the offering price given by the boiler-room staff. The defendants also made false statements as to the amount of outstanding shares of corporate stock. Furthermore, the lead defendant, Lambert Vander Tuig, had been the subject of an injunction in a previous SEC case, in which he was subsequently barred from associating with any securities broker or dealer; this information was also withheld from prospective investors, and he used false names to conceal his identity.

Vander Tuig and his co-defendant Jonathan Carman, both of whom were members of Orange County's famous "Saddleback Church" megachurch, solicited investments from fellow churchgoers by providing copies of Saddleback Church pastor Rick Warren's best-selling book *The Purpose-Driven Life* with their promotional materials. Of the $52 million raised by Vander Tuig and his associates, over $24 million was diverted for their own use for a Ponzi scheme to pay "returns" to the initial investors (by using money from the new investors).

Learn Waterhouse, Inc. was a "prime bank" Ponzi scheme that raised over $24.5 million by the sale of unregistered securities in the form of nine-month promissory notes.[2] The scheme involved the defendant corporation purporting to pool investment funds to engage in a secret, invitation-only, bank trading program yielding returns of 5% to 50% per month. The defendants claimed that one of their

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[2] *Learn Waterhouse*, No. 04-CV-2037-W-DHB (S.D. Cal.); Office of the United States Attorney, Southern District of California, *Two Sentenced in Nationwide Multi-Million Dollar Investment Scam*, http://www.justice.gov/usao/cas/press/cas81211-Treadwell.pdf (announcing sentences of Learn Waterhouse's principal Randall Treadwell and counsel Arnulfo Acosta to 300 months' imprisonment and 87 months' imprisonment respectively).

programs earned 500% in 60 days, and that the investors' principal was secured by a "pre-funded cash-back instrument" purportedly issued by a major U.S. bank. The bank trading program was entirely fictitious, as were the "pre-funded, cash-back instruments." Of the $17.6 million paid by the defendants to investors and sales agents, at least $8.2 million came from investor funds, with another $2.5 million in investor funds misappropriated to support the defendants and finance other businesses. The corporation and its principals and attorney had been under cease-and-desist orders from the securities commissions of Alabama and Iowa. Later, the defendants operated under a different name and directed investors to wire investment funds to an account in the Netherlands Antilles.

Homestead Properties involved a limited partnership that purported to invest in mobile home park communities.[3] The owner of the limited partnership (the sole member of the limited liability company that was the general partner) raised almost $10 million from 36 investors, almost all of whom were senior citizens. However, the owner then transferred $4.5 million into a brokerage account held in the limited partnership's name without ever informing the investors, and then immediately used the money in the brokerage account for day-trading without informing the investors as to his trading strategy. The investment offering materials made various misrepresentations including an intent to conduct yearly audits (which never happened), payment of commissions to a registered broker-dealer (while the owner's co-defendant, who referred most of the investors, was not registered), and quarterly distributions of net profits (but distributions were made to some investors while the partnership reported losses in the years of distribution). The owner also misappropriated funds to pay his personal credit card bills.

The only similarities between this case and the Receiver's allegedly comparable cases are that they all took place in Southern California and involved

[3] *Homestead Properties*, No. 09-CV-01331 (C.D. Cal.); http://www.robbevans.com/html/homestead.html.

SEC civil litigation. Otherwise, the facts of the cases make them wholly inapplicable.

This case does not involve a Ponzi scheme (*Vander Tuig* and *Learn Waterhouse*), investment in improved real estate (*Homestead Properties*), promissory notes promising absurdly high rates of return (*Learn Waterhouse*), boiler-room sales of stock available elsewhere for less cost (*Vander Tuig*), radical undisclosed changes of investment strategy (*Homestead Properties*), promoters under SEC injunctions or states' cease-and-desist orders (*Vander Tuig*, *Learn Waterhouse*), offshoring of funds (*Learn Waterhouse*), or misappropriation for personal purposes (all).

Instead, as has been described time and again by Defendants, the investments at issue are general partnerships established solely for holding raw land for future appreciation on resale; there are no limited partners, the general partner-investors retain full and exclusive power over the partnerships as described in the partnership agreements, the investment strategy has remained unchanged throughout, neither Schooler nor Western have been the subject of prior injunctions for improper dealings in securities, and there has been no evidence of either offshoring of investors' money or misappropriation of investors' funds by Schooler for personal purposes.

Therefore, none of the allegedly comparable cases provide any justification for the Receiver's and counsel's rates; if anything, they demonstrate why the continuation of the receivership over the GP's has no merit and should end now.

III.

CONCLUSION

The application for fees and costs requested by the Receiver and Receiver's Counsel should be denied as the requested fees and costs are unreasonable. There is no showing as to how this work performed has benefitted Western or the GP's, and the Receiver's proposals for obtaining funds to pay his fees and costs (and those of the associated professionals) by liquidating equity interests in the GP's would be inconsistent with the purpose of preserving and recovering assets for the benefit of the investors. Also, the Receiver should not be allowed to use GP money for work

done for Western, as the GP's and Western are separate entities. Therefore, the Second Interim Applications should be denied, or in the alternative any award of fees and costs should be substantially reduced from what is claimed.

Respectfully Submitted,

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