

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

**UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA**

SECURITIES AND EXCHANGE
COMMISSION,

Plaintiff,

v.

PACIFIC WEST CAPITAL GROUP,
INC.; ANDREW B CALHOUN IV;
PWCG TRUST; BRENDA CHRISTINE
BARRY; BAK WEST, INC.; ANDREW B
CALHOUN JR.; ERIC CHRISTOPHER
CANNON; CENTURY POINT, LLC;
MICHAEL WAYNE DOTTA; and
CALEB AUSTIN MOODY (dba SKY
STONE),

Defendants.

Case No. 2:15-cv-02563-FMO (FFMx)

**PROPOSED ORDER TO EXTEND
RECEIVER'S AUTHORITY TO
USE EXISTING RESERVES TO
COVER UNFUNDED PREMIUM
PAYMENTS FOR 30 DAYS**

Date: November 1, 2018
Time: 10:00 a.m.
Ctrm.: 6D
Judge: Hon. Fernando M. Olguin

1 The Court, having considered the motion to extend receiver's authority to use
2 existing reserves to cover unfunded premium payments for 30 days ("Motion") of
3 Thomas C. Hebrank ("Receiver"), Court-appointed receiver for PWCG Trust, and
4 good cause appearing therefor, hereby orders as follows:

5 1. The Motion is granted.

6 2. The Receiver's authority to use existing reserves to cover unfunded
7 premium payments, as described in the Motion, is extended for 30 days to
8 November 30, 2018.

9
10 Dated: _____

11 Hon. Fernando M. Olguin
12 Judge, United States District Court
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

1 ALLEN MATKINS LECK GAMBLE
MALLORY & NATSIS LLP
2 DAVID R. ZARO (BAR NO. 124334)
865 South Figueroa Street, Suite 2800
3 Los Angeles, California 90017-2543
Phone: (213) 622-5555
4 Fax: (213) 620-8816
E-Mail: dzaro@allenmatkins.com

5 ALLEN MATKINS LECK GAMBLE
MALLORY & NATSIS LLP
6 EDWARD G. FATES (BAR NO. 227809)
One America Plaza
7 600 West Broadway, 27th Floor
8 San Diego, California 92101-0903
Phone: (619) 233-1155
9 Fax: (619) 233-1158
E-Mail: tfates@allenmatkins.com

10 Attorneys for Receiver
11 THOMAS HEBRANK

12 UNITED STATES DISTRICT COURT
13 CENTRAL DISTRICT OF CALIFORNIA

14
15 SECURITIES AND EXCHANGE
COMMISSION,

16 Plaintiff,

17 v.

18 PACIFIC WEST CAPITAL GROUP,
19 INC.; ANDREW B CALHOUN IV;
PWCG TRUST; BRENDA CHRISTINE
20 BARRY; BAK WEST, INC.; ANDREW B
CALHOUN JR.; ERIC CHRISTOPHER
21 CANNON; CENTURY POINT, LLC;
MICHAEL WAYNE DOTTA; and
22 CALEB AUSTIN MOODY (dba SKY
STONE),

23 Defendants.
24

Case No. 2:15-cv-02563-FMO (FFMx)

**DECLARATION OF THOMAS C.
HEBRANK IN SUPPORT OF
MOTION TO EXTEND
RECEIVER'S AUTHORITY TO
USE EXISTING RESERVES TO
COVER UNFUNDED PREMIUM
PAYMENTS FOR 30 DAYS;
MEMORANDUM OF POINTS AND
AUTHORITIES**

Date: November 1, 2018
Time: 10:00 a.m.
Ctrm.: 6D
Judge: Hon. Fernando M. Olguin

1 I, Thomas C. Hebrank, declare:

2 1. I am the Court-appointed receiver for PWCG Trust. I make this
3 declaration in support of my Motion to Extend Receiver's Authority to Use Existing
4 Reserves to Cover Unfunded Premium Payments for 30 Days ("Motion"). I have
5 personal knowledge of the facts stated herein, and if called upon to do so, I could
6 and would personally and competently testify to them.

7 2. When fractionalized interests in insurance Policies were sold to
8 investors by Defendants Pacific West Capital Group, Inc. ("Pacific West") and
9 Andrew Calhoun ("Calhoun"), Pacific West and Calhoun calculated a specific
10 amount of the total sale proceeds that was allocated as the reserve to be used to fund
11 premium payments for a specific period of time. The remaining funds were retained
12 by Pacific West. The reserve funds were deposited into a bank account maintained
13 by Mills Potoczak & Company, as Trustee.

14 3. The reserves set aside for the Policies were insufficient because the
15 reserve periods calculated by Pacific West and Calhoun were too short and therefore
16 most Policy reserves have been exhausted notwithstanding the fact that premium
17 payments continue to come due.

18 4. Starting in 2012, Defendants Pacific West and Calhoun funded the
19 shortfalls necessary to make premium payments on some of these policies and, by
20 doing so, were able to avoid (a) using the Secondary Reserve and Tertiary Reserve,
21 which they had represented to investors had never been touched, and (b) making
22 "cash calls" to investors to fund their shares of the shortfalls. Accounting records
23 provided by MPC reflect that Pacific West transferred approximately \$5 million to
24 PWCG Trust to be used to pay premiums between 2012 and 2017.

25 5. Shortly after the SEC filed its Complaint, Pacific West and Calhoun
26 instructed PWCG Trust, through MPC as Trustee, to make cash calls on investors to
27 contribute funds necessary to cover the shortfalls. Some investors paid cash calls
28 and some did not. Pacific West and Calhoun continued to fund the shortfalls from

1 cash calls. They also treated the fractionalized interests of investors who did not
2 pay in response to cash calls as "forfeited," meaning ownership of the interests
3 reverted to Pacific West with no compensation paid to investors.

4 6. Then, in July 2017, Pacific West purportedly sold certain of the
5 forfeited investor interests to Cook Street Master Trust, which is managed by an
6 investment firm called BroadRiver Asset Management ("BroadRiver"). Under the
7 Agreement, BroadRiver paid \$1.5 million to Pacific West to acquire the forfeited
8 investor interests, which collectively have the right to receive over \$28 million in
9 death benefits.

10 7. According to BroadRiver's principal, it has since paid an additional
11 approximately \$875,000 to fund premium payments for the forfeited interests it
12 acquired in July 2017, as well as additional forfeited interests acquired when
13 investors subsequently failed to meet cash calls. Due to the acquisition of additional
14 forfeited interests since July 2017, BroadRiver now claims to hold forfeited interests
15 entitling it to approximately \$32 million in death benefits. In other words,
16 BroadRiver purportedly stepped into the shoes of Pacific West in terms of funding
17 premium shortfalls and taking forfeited interests from investors who did not pay
18 cash calls. I refute BroadRiver's claims to the fractionalized interests.

19 8. The complexity of pricing and valuation of the Policies has been
20 exacerbated by the failure of PWCG and Calhoun to use timely life expectancies as
21 the touchstone for their original selection of policies and the setting of reserve
22 amounts. The absence of timely LE Reports, the failure of PWCG and Calhoun to
23 develop realistic cash flows for the policies, and failure to optimize premium
24 payments based on concrete data resulted in woefully inadequate reserves and, in
25 some cases, policies which have nominal or no value.

26 9. My analysis of the appropriate path forward with regard to the ongoing
27 management, servicing and possible sale of this complex portfolio has been
28 significantly impacted by PWCG's and Calhoun's failure to complete the complex

1 analysis that was required to create a portfolio of self-sustaining valuable policies.
2 For example, 21st had to start from scratch with regard to LE Reports and the lack
3 of reserves has led to some further complexities with regard to the cash flow
4 analysis in order to develop a program for short term borrowing or possible
5 liquidation of certain policies in order to sustain the overall portfolio.

6 10. At the beginning of the receivership, the balance of existing reserves
7 was approximately \$8.6 million. At that time, many of the Policies were in their
8 "grace periods" and MPC had been making the minimum payments to prevent the
9 policies from lapsing. Without the benefit of premium optimization schedules,
10 which Pacific West and Calhoun had not obtained, I maintained the status quo and
11 continued making the grace period payments necessary to keep all Policies in force.
12 In connection with his motion to engage 21st and for authority to use existing
13 reserves to cover unfunded premiums through October 2018 (Dkt. No. 153), I
14 projected that the existing reserves would cover premiums coming due until
15 approximately March 2019.

16 11. Although making grace period payments reduces cash needed on a
17 short-term basis, it increases the cash required to maintain the Policies over the
18 long-term and therefore reduces the net recovery from the Policies. For this reason,
19 obtaining premium optimization schedules is standard in the industry to determine
20 how to maximize the net recovery from each policy in terms of the cash required for
21 premiums, the cash value in the Policy, and the death benefit at maturity. One of the
22 valuation services 21st was engaged to provide was a new premium optimization
23 schedule for each Policy. These schedules were completed in August and the
24 premium payments pursuant to the schedules were commenced in September.

25 12. As noted above, this change will increase the net recovery from the
26 Policies over the long-term (and enhance their value to potential buyers in the short-
27 term), but also increases the cash needed in the short-term. The balance of existing
28 reserves as of September 30, 2018 was approximately \$3.28 million. I now project

1 the existing reserves will cover premiums coming due for the Policies (based on the
2 new premium optimization schedules provided by 21st) until approximately mid-
3 January 2019. I am also holding \$5,073,730.88 in death benefits received from
4 Policies that have matured since my appointment.

5 13. 21st's preliminary data indicates that, even if all assets of PWCG Trust
6 are pooled together into a common fund, a significant amount of additional funding
7 will be needed to maintain the policies until their projected maturities. Additional
8 work to analyze and project the cash flow for the portfolio is needed, however. This
9 includes what is known as a "Monte Carlo" analysis, in which a simulation of
10 possible maturities for the Policies (and the resulting effects on premiums and death
11 benefits) is run numerous times to produce a more accurate and reliable projection.
12 This type of statistical analysis, which will be provided by 21st, is commonly used
13 for projecting cash flow for a portfolio of life insurance policies and is of critical
14 importance here given the lack of adequate reserves. In this case, I need these
15 projections in order to more accurately determine the timing and amount of
16 borrowing and the prospects for funding premiums from the sale of certain policies.

17 14. Possible sources of funding future premium payments include a loan or
18 line of credit secured by the Policies and/or selling certain Policies to sustain the
19 remainder of the portfolio. It is also possible that selling the entire portfolio in the
20 short term would provide the best overall recovery for investors, considering the
21 time value of money, costs of selling Policies and/or borrowing against Policies, and
22 other administrative costs.

23 15. In addition, as noted above, the preliminary data from 21st indicates
24 that a small number of policies may not be worth maintaining. For some policies,
25 for example, the projected premiums required to maintain the policy until maturity
26 may exceed the death benefit. For other Policies, there is considerable risk that the
27 insured could live beyond the maturity date and there would be no death benefit at
28

1 all.¹ With the assistance of 21st, I need to gather additional information, examine
2 each of these Policies more closely, prepare cash flow projections, and evaluate
3 options such that I can make an informed recommendation to the Court as to the
4 best course of action.

5

6 I declare under penalty of perjury under the laws of the State of California
7 that the foregoing is true and correct.

8 Executed this 4th day of October 2018, at San Diego, California.

9


THOMAS C. HEBRANK

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

26

27

28 ¹ I understand from 21st that certain of the Policies mature when the insured reaches 100 years of age and there is no death benefit at all once that occurs.

1 ALLEN MATKINS LECK GAMBLE
MALLORY & NATSIS LLP
2 DAVID R. ZARO (BAR NO. 124334)
865 South Figueroa Street, Suite 2800
3 Los Angeles, California 90017-2543
Phone: (213) 622-5555
4 Fax: (213) 620-8816
E-Mail: dzaro@allenmatkins.com

5 ALLEN MATKINS LECK GAMBLE
MALLORY & NATSIS LLP
6 EDWARD G. FATES (BAR NO. 227809)
One America Plaza
7 600 West Broadway, 27th Floor
8 San Diego, California 92101-0903
Phone: (619) 233-1155
9 Fax: (619) 233-1158
E-Mail: tfates@allenmatkins.com

10 Attorneys for Receiver
11 THOMAS HEBRANK

12 **UNITED STATES DISTRICT COURT**
13 **CENTRAL DISTRICT OF CALIFORNIA**

14
15 SECURITIES AND EXCHANGE
COMMISSION,

16 Plaintiff,

17 v.

18 PACIFIC WEST CAPITAL GROUP,
19 INC.; ANDREW B CALHOUN IV;
PWCg TRUST; BRENDA CHRISTINE
20 BARRY; BAK WEST, INC.; ANDREW B
CALHOUN JR.; ERIC CHRISTOPHER
21 CANNON; CENTURY POINT, LLC;
MICHAEL WAYNE DOTTA; and
22 CALEB AUSTIN MOODY (dba SKY
STONE),

23 Defendants.
24

Case No. 2:15-cv-02563-FMO (FFMx)

**NOTICE OF MOTION AND
MOTION TO EXTEND
RECEIVER'S AUTHORITY TO
USE EXISTING RESERVES TO
COVER UNFUNDED PREMIUM
PAYMENTS FOR 30 DAYS;
MEMORANDUM OF POINTS AND
AUTHORITIES**

Date: November 1, 2018
Time: 10:00 a.m.
Ctrm.: 6D
Judge: Hon. Fernando M. Olguin

1 **TO ALL PARTIES AND THEIR ATTORNEYS OF RECORD:**

2 **PLEASE TAKE NOTICE** that on November 1, 2018, at 10:00 a.m. in
3 Courtroom 6D of the above-entitled Court, located at 350 W. 1st Street, 6th Floor,
4 Los Angeles, California 90012, Thomas Hebrank ("Receiver"), the Court-appointed
5 receiver for the PWCG Trust, will and hereby does move the Court to extend the
6 Receiver's authority to use existing policy reserves to cover unfunded premium
7 payments for 30 days until November 30, 2018 ("Motion").

8 This Motion is based on this Notice of Motion and Motion, the attached
9 Memorandum of Points and Authorities, the documents and pleadings already on file
10 in this action, and upon such further oral and documentary evidence as may be
11 presented at the time of hearing.

12 **Procedural Requirements:** If you oppose this Motion, you are required to
13 file your written opposition with the Office of the Clerk, United States District Court,
14 350 W. 1st Street, Suite 4311, Los Angeles, California 90012-4565, and serve the
15 same on the undersigned not later than 21 days prior to the hearing.

16 **IF YOU FAIL TO FILE AND SERVE A WRITTEN OPPOSITION** by the
17 above date, the Court may grant the requested relief without further notice. This
18 Motion is made following the conference of counsel pursuant to L.R. 7 3.

19

20 Dated: October 4, 2018

ALLEN MATKINS LECK GAMBLE
MALLORY & NATSIS LLP

21

By: /s/ Edward Fates

22

EDWARD G. FATES
Attorneys for Receiver
THOMAS HEBRANK

23

24

25

26

27

28

1 **MEMORANDUM OF POINTS AND AUTHORITIES**

2 **I. INTRODUCTION**

3 The Receiver requests authority to continue his use of existing reserves to pay
4 unfunded premiums until November 30, 2018 in order to complete his valuation and
5 cash flow analysis. As detailed below, the need for additional life expectancy
6 information and complexity of the cash flow analyses required to assess the
7 appropriate course of action has given rise to this request for an additional 30 days.

8 Since the Court authorized the Receiver to engage consultant ITM
9 Twentyfirst ("21st") to provide life expectancy ("LE") and valuation services for the
10 policies held by PWCG Trust ("Policies"), 21st has been working (a) to obtain the
11 necessary medical releases from the insureds, (b) gather the necessary medical
12 records to provide reports showing the life expectancies of each insured under the
13 Policies ("LE Reports"), and (c) analyze the Policies and their payment histories in
14 order to provide new premium optimization schedules. 21st was able to complete
15 the majority of this work within the relatively short time budgeted (June through
16 September 2018), but is still working to obtain medical records for certain insureds,
17 complete a small number of LE Reports, and make adjustments to others.

18 Although the work being done by 21st is not complete, the preliminary data
19 indicates that the overall PWCG Trust portfolio has positive value, but there will be
20 interim funding needs that will need to be addressed. In a simple cash flow analysis,
21 additional funding will be needed to prevent the policies from lapsing before their
22 projected maturity dates. In order to more accurately forecast these cashflow needs,
23 additional statistical and probability analysis will need to be performed to better
24 quantify the portfolio's cashflow needs.

25 In addition, the preliminary data indicates that a small number of policies may
26 not be worth maintaining. For example with some of the policies, the projected
27 premiums required to maintain the policy until maturity may exceed the death
28 benefit to be received.

1 With the assistance of 21st, the Receiver needs to gather additional data and
2 examine these policies so he can make an informed proposal to the Court as to the
3 best course of action, including, but not limited to proposing short-term borrowing
4 in order to maintain and service the Policies through their maturities or the
5 possibility of selling some or all of the Policies.

6 In order to complete the remaining LE work, cash flow analysis, and
7 valuation, and have his long-term proposal considered by the Court, the Receiver
8 asks that the Court extend his authority to use existing reserves to cover unfunded
9 premium payments for 30 days to November 30, 2018. Without this relief, the
10 Receiver would be forced to make important decisions affecting the ultimate
11 recovery from the Policies without key information and analysis that will be
12 gathered and performed over the next 30 days.

13 II. BACKGROUND FACTS

14 When fractionalized interests in insurance Policies were sold to investors by
15 Defendants Pacific West Capital Group, Inc. ("Pacific West") and Andrew Calhoun
16 ("Calhoun"), Pacific West and Calhoun calculated a specific amount of the total sale
17 proceeds that was allocated as the reserve to be used to fund premium payments for
18 a specific period of time. The remaining funds were retained by Pacific West. The
19 reserve funds were deposited into a bank account maintained by Mills Potoczak &
20 Company, as Trustee. Declaration of Thomas Hebrank filed herewith ("Hebrank
21 Declaration"), ¶ 2.

22 The reserves set aside for the Policies were insufficient because the reserve
23 periods calculated by Pacific West and Calhoun were too short and therefore most
24 Policy reserves have been exhausted notwithstanding the fact that premium
25 payments continue to come due. Hebrank Declaration, ¶ 3. In fact, as insurance
26 expert Professor Daniel Bauer found, in light of Pacific West's failure to set aside
27 adequate reserves based on realistic life expectancies, the total reserves are not
28 adequate as to the vast majority of Policies. Professor Bauer's expert report and

1 exhibits were attached to the Parties' Joint Evidentiary Appendix in Support of
2 Cross Motions for Summary Judgment and Partial Summary Judgment at Tab
3 No. 101. Dkt. No. 106-103. As discussed below, the Receiver's work with 21st and
4 its initial LE and valuation work have validated the importance of the LE Reports
5 and the impact upon the reserves of Calhoun's failure to use them.

6 Starting in 2012, Defendants Pacific West and Calhoun funded the shortfalls
7 necessary to make premium payments on some of these policies and, by doing so,
8 were able to avoid (a) using the Secondary Reserve and Tertiary Reserve, which
9 they had represented to investors had never been touched, and (b) making "cash
10 calls" to investors to fund their shares of the shortfalls. SEC Complaint, Dkt. No. 1,
11 ¶¶ 62-64. Accounting records provided by MPC reflect that Pacific West
12 transferred approximately \$5 million to PWCG Trust to be used to pay premiums
13 between 2012 and 2017. Hebrank Declaration, ¶ 4.

14 Shortly after the SEC filed its Complaint, Pacific West and Calhoun
15 instructed PWCG Trust, through MPC as Trustee, to make cash calls on investors to
16 contribute funds necessary to cover the shortfalls. Some investors paid cash calls
17 and some did not. Pacific West and Calhoun continued to fund the shortfalls from
18 cash calls. They also treated the fractionalized interests of investors who did not
19 pay in response to cash calls as "forfeited," meaning ownership of the interests
20 reverted to Pacific West with no compensation paid to investors. Hebrank
21 Declaration, ¶ 5.

22 Then, in July 2017, Pacific West purportedly sold certain of the forfeited
23 investor interests to Cook Street Master Trust, which is managed by an investment
24 firm called BroadRiver Asset Management ("BroadRiver"). Under the Agreement,
25 BroadRiver paid \$1.5 million to Pacific West to acquire the forfeited investor
26 interests, which collectively have the right to receive over \$28 million in death
27 benefits. Hebrank Declaration, ¶ 6.

28

1 According to BroadRiver's principal, it has since paid an additional
2 approximately \$875,000 to fund premium payments for the forfeited interests it
3 acquired in July 2017, as well as additional forfeited interests acquired when
4 investors subsequently failed to meet cash calls. Due to the acquisition of additional
5 forfeited interests since July 2017, BroadRiver now claims to hold forfeited interests
6 entitling it to approximately \$32 million in death benefits. In other words,
7 BroadRiver purportedly stepped into the shoes of Pacific West in terms of funding
8 premium shortfalls and taking forfeited interests from investors who did not pay
9 cash calls. The Receiver refutes BroadRiver's claims to the fractionalized interests.
10 Hebrank Declaration, ¶ 7.

11 The complexity of pricing and valuation of the Policies has been exacerbated
12 by the failure of PWCG and Calhoun to use timely life expectancies as the
13 touchstone for their original selection of policies and the setting of reserve amounts.
14 The absence of timely LE Reports, the failure of PWCG and Calhoun to develop
15 realistic cash flows for the policies, and failure to optimize premium payments
16 based on concrete data resulted in woefully inadequate reserves and, in some cases,
17 policies which have nominal or no value. Hebrank Declaration, ¶ 8.

18 The Receiver's analysis of the appropriate path forward with regard to the
19 ongoing management, servicing and possible sale of this complex portfolio has been
20 significantly impacted by PWCG's and Calhoun's failure to complete the complex
21 analysis that was required to create a portfolio of self-sustaining valuable policies.
22 For example, 21st had to start from scratch with regard to LE Reports and the lack
23 of reserves has led to some further complexities with regard to the cash flow
24 analysis in order to develop a program for short term borrowing or possible
25 liquidation of certain polices in order to sustain the overall portfolio. Hebrank
26 Declaration, ¶ 9.

27
28

1 **A. The SEC Complaint**

2 The SEC's Complaint, which was filed over a year before BroadRiver began
3 acquiring forfeited investor interests, alleges that Pacific West and Calhoun, in
4 selling fractionalized interests in insurance policies, told investors that (a) in the
5 three-tiered reserve system established by Pacific West, the second and third tiers of
6 reserves had never been touched, (b) cash calls had never been made for investors to
7 fund premium payments, and (c) insurance policies in PWCG Trust were selected
8 because, in Pacific West and Calhoun's estimation, they would mature in four to
9 seven years, despite the fact that life expectancies of the insureds were years longer.
10 SEC Complaint, Dkt. No. 1, ¶¶ 16-46, 61-92. The SEC further alleged that Pacific
11 West and Calhoun misrepresented and omitted material facts in selling
12 fractionalized interests to investors, including failing to disclose that Pacific West
13 had funded premium payments for policies where the primary reserve had been
14 exhausted, misrepresenting the amount of policy premiums on the disclosures forms
15 provided to investors, failing to disclose that such premiums would increase
16 substantially over time, and failing to disclose that only a small percentage of
17 policies held by PWCG Trust had actually matured in the seven years following
18 their purchase. *Id.* at ¶¶ 75-79, 83. The SEC also alleges that Pacific West and
19 Calhoun had no reasonable basis to believe the insurance policies acquired would
20 actually mature in four to seven years. *Id.* at ¶¶ 30, 81.

21 PWCG Trust, Pacific West and Calhoun, as well as Andrew Calhoun, Jr.,
22 have entered into Consents with the SEC and Final Judgments have been entered
23 against them. Dkt. Nos. 145, 165, 166, 168.

24 **B. Expert Report of Professor Daniel Bauer**

25 The SEC engaged Insurance and Risk Management Professor Daniel Bauer of
26 Georgia State University¹ to perform an analysis of the sale of fractionalized
27

28 ¹ The Receiver understands that since issuing his expert report, Professor Bauer
has left Georgia State University and is now the Dai-ichi Life Insurance

1 interests in life insurance policies by the Defendants and the reserves set up by
2 Defendants and held by PWCG Trust, including how the reserves were calculated,
3 whether they are adequate, and the accuracy of various representations made by
4 Defendants. As noted above, Professor Bauer's expert report and exhibits were
5 attached to the Parties' Joint Evidentiary Appendix in Support of Cross Motions for
6 Summary Judgment and Partial Summary Judgment at Tab No. 101. Dkt.
7 No. 106-103.

8 In his report, Professor Bauer makes a number of findings that help explain
9 the shortfalls from the reserves held by PWCG Trust, including:

- 10 • Although it is standard in the life settlements industry to use
11 actuarially-based life expectancy estimates for the insured in setting
12 premium reserve periods, Pacific West did not do so for policies held
13 by PWCG Trust. Pacific West also did not use standard analytical tools
14 to evaluate the length of its primary reserve periods. Bauer Expert
15 Report, Dkt. No. 106-103, ¶¶ 10, 53-61, 89-98.
- 16 • Pacific West set premium reserve periods that were significantly
17 shorter than the life expectancies of the insureds for the policies held by
18 PWCG Trust. As a result, PWCG Trust's insurance policies are
19 maturing much more slowly than the premium reserve periods. On
20 average, only 28.9% of the policies held by PWCG Trust have matured
21 within the premium reserve periods, which is an extremely low average
22 for the industry. *Id.* at ¶¶ 12, 99-102.
- 23 • Pacific West miscalculated and underfunded the amounts necessary to
24 pay policy premiums during the premium reserve periods it set,
25 exacerbating the underfunding of the reserves. *Id.* at ¶¶ 13, 103-110.

26
27
28 _____
Company Endowed Chair in Actuarial Science and Risk Management at the
University of Alabama, Culverhouse College of Commerce.

- 1 • The second and third tiers of reserves established by Pacific West
2 (known as the secondary and tertiary reserves) are very small in
3 relation to the premiums owed on the policies and insufficient to cover
4 the shortfalls from premium reserves. *Id.* at ¶¶ 15, 118-134.
- 5 • The policies held by PWCG Trust, which totaled 133 at the time, were
6 purchased between 2004 and 2015, and began to reach the end of their
7 premium reserve periods in 2011. By February 2012, Pacific West was
8 covering shortfalls from premium reserves itself. In December 2014,
9 Pacific West instructed PWCG Trust to start drawing on the secondary
10 reserve. In August 2015, Pacific West instructed PWCG Trust to start
11 making investor cash calls. The secondary and tertiary reserves were
12 depleted as of February 2016. *Id.* at ¶¶ 132-133.
- 13 • As of 2017, there were 77 Policies that had reached the end of their
14 premium reserve periods. It is estimated that the number will go up to
15 82 in 2018, 94 in 2019, and 110 in 2020. *Id.* at Exh. 5.

16 Accordingly, Professor Bauer's analysis shows the reserves held by PWCG
17 Trust are substantially underfunded and woefully insufficient to keep the policies in
18 force through their maturities.

19 **C. Interim Relief Granted by the Court**

20 Shortly after his appointment, the Receiver sought immediate, *ex parte* relief
21 to address the issue of Unfunded Premium Payments coming due in March, April,
22 and May 2018. The Receiver sought and obtained permission to borrow from
23 existing reserve funds to pay Unfunded Premium Payments coming due during this
24 initial three-month period. Dkt. Nos. 146, 147. The Receiver then learned that
25 Pacific West did not obtain LE Reports or other policy valuation information on an
26 ongoing basis as necessary to value the policies and evaluate long-term options for
27 covering Unfunded Premium Payments. Accordingly, the Receiver sought and
28 obtained permission to engage 21st to, among other things, provide LE Reports and

1 premium optimization schedules. Dkt. Nos. 153, 161. The Court also extended the
2 time during which the Receiver could use existing reserves to cover Unfunded
3 Premium Payments through October 31, 2018. Dkt. No. 161.

4 **D. Current Status of Reserves**

5 At the beginning of the receivership, the balance of existing reserves was
6 approximately \$8.6 million. At that time, many of the Policies were in their "grace
7 periods" and MPC had been making the minimum payments to prevent the policies
8 from lapsing. Without the benefit of premium optimization schedules, which
9 Pacific West and Calhoun had not obtained, the Receiver maintained the status quo
10 and continued making the grace period payments necessary to keep all Policies in
11 force. In connection with his motion to engage 21st and for authority to use existing
12 reserves to cover unfunded premiums through October 2018 (Dkt. No. 153), the
13 Receiver projected that the existing reserves would cover premiums coming due
14 until approximately March 2019. Hebrank Declaration, ¶ 10.

15 Although making grace period payments reduces cash needed on a short-term
16 basis, it increases the cash required to maintain the Policies over the long-term and
17 therefore reduces the net recovery from the Policies. For this reason, obtaining
18 premium optimization schedules is standard in the industry to determine how to
19 maximize the net recovery from each policy in terms of the cash required for
20 premiums, the cash value in the Policy, and the death benefit at maturity. One of the
21 valuation services 21st was engaged to provide was a new premium optimization
22 schedule for each Policy. These schedules were completed in August and the
23 premium payments pursuant to the schedules were commenced in September.
24 Hebrank Declaration, ¶ 11.

25 As noted above, this change will increase the net recovery from the Policies
26 over the long-term (and enhance their value to potential buyers in the short-term),
27 but also increases the cash needed in the short-term. The balance of existing
28 reserves as of September 30, 2018 was approximately \$3.28 million. The Receiver

1 now projects the existing reserves will cover premiums coming due for the Policies
2 (based on the new premium optimization schedules provided by 21st) until
3 approximately mid-January 2019. The Receiver is also holding \$5,073,730.88 in
4 death benefits received from Policies that have matured since his appointment.
5 Hebrank Declaration, ¶ 12.

6 III. PRELIMINARY DATA FROM 21ST

7 21st's preliminary data indicates that, even if all assets of PWCG Trust are
8 pooled together into a common fund, a significant amount of additional funding will
9 be needed to maintain the policies until their projected maturities. Additional work
10 to analyze and project the cash flow for the portfolio is needed, however. This
11 includes what is known as a "Monte Carlo" analysis, in which a simulation of
12 possible maturities for the Policies (and the resulting effects on premiums and death
13 benefits) is run numerous times to produce a more accurate and reliable projection.
14 This type of statistical analysis, which will be provided by 21st, is commonly used
15 for projecting cash flow for a portfolio of life insurance policies and is of critical
16 importance here given the lack of adequate reserves. In this case, the Receiver
17 needs these projections in order to more accurately determine the timing and amount
18 of borrowing and the prospects for funding premiums from the sale of certain
19 policies. Hebrank Declaration, ¶ 13.

20 Possible sources of funding future premium payments include a loan or line
21 of credit secured by the Policies and/or selling certain Policies to sustain the
22 remainder of the portfolio. It is also possible that selling the entire portfolio in the
23 short term would provide the best overall recovery for investors, considering the
24 time value of money, costs of selling Policies and/or borrowing against Policies, and
25 other administrative costs. Hebrank Declaration, ¶ 14.

26 In addition, as noted above, the preliminary data from 21st indicates that a
27 small number of policies may not be worth maintaining. For some policies, for
28 example, the projected premiums required to maintain the policy until maturity may

1 exceed the death benefit. For other Policies, there is considerable risk that the
2 insured could live beyond the maturity date and there would be no death benefit at
3 all.² The Receiver, with the assistance of 21st, needs to gather additional
4 information, examine each of these Policies more closely, prepare cash flow
5 projections, and evaluate options such that he can make an informed
6 recommendation to the Court as to the best course of action. Hebrank Declaration,
7 ¶ 15.

8 IV. ARGUMENT

9 "The power of a district court to impose a receivership or grant other forms of
10 ancillary relief does not in the first instance depend on a statutory grant of power
11 from the securities laws. Rather, the authority derives from the inherent power of a
12 court of equity to fashion effective relief." *SEC v. Wencke*, 622 F.2d 1363, 1369
13 (9th Cir. 1980). The "primary purpose of equity receiverships is to promote orderly
14 and efficient administration of the estate by the district court for the benefit of
15 creditors." *SEC v. Hardy*, 803 F.2d 1034, 1038 (9th Cir 1986). As the appointment
16 of a receiver is authorized by the broad equitable powers of the court, any
17 distribution of assets must also be done equitably and fairly. See *SEC v. Elliot*,
18 953 F.2d 1560, 1569 (11th Cir. 1992).

19 District courts have the broad power of a court of equity to determine the
20 appropriate action in the administration and supervision of an equity receivership.
21 See *SEC v. Capital Consultants, LLC*, 397 F.3d 733, 738 (9th Cir. 2005). The Ninth
22 Circuit explained:

23 A district court's power to supervise an equity receivership
24 and to determine the appropriate action to be taken in the
25 administration of the receivership is extremely broad. The
26 district court has broad powers and wide discretion to
determine the appropriate relief in an equity receivership.
The basis for this broad deference to the district court's
supervisory role in equity receiverships arises out of the

27 _____
28 ² The Receiver understands from 21st that certain of the Policies mature when the
insured reaches 100 years of age and there is no death benefit at all once that
occurs.

1 fact that most receiverships involve multiple parties and
2 complex transactions. A district court's decision
concerning the supervision of an equitable receivership is
3 reviewed for abuse of discretion.

4 *Id.* (citations omitted); see also *CFTC v. Topworth Int'l, Ltd.*, 205 F.3d 1107,
1115 (9th Cir. 1999) ("This court affords 'broad deference' to the court's supervisory
5 role, and 'we generally uphold reasonable procedures instituted by the district court
6 that serve th[e] purpose' of orderly and efficient administration of the receivership
7 for the benefit of creditors."). Accordingly, the Court has very broad discretion in
8 the administration of receivership estate assets.

9 Here, the Receiver seeks a 30-day extension of his authority to use existing
10 reserve funds to cover unfunded premium payments. In its order dated May 29,
11 2018, the Court authorized the Receiver to use existing reserves in this fashion
12 through October 31, 2018. With critical data and analysis being gathered and
13 performed by the Receiver and 21st over the next 30 days, including assessing short-
14 term borrowing needs and funding sources and the possibility of selling certain
15 Policies, the Receiver will be in a position to make informed recommendations to
16 the Court and file his long-term proposal by November 1, 2018, with a
17 November 29, 2018 hearing date. Accordingly, the Receiver asks that his interim
18 authority to use existing reserves to cover unfunded premium payments be extended
19 by 30 days to November 30, 2018.

20 V. CONCLUSION

21 For the foregoing reasons, the Receiver requests an order extending his
22 authority to use existing reserves to cover unfunded premium payments for 30 days.

23 Dated: October 4, 2018

24 ALLEN MATKINS LECK GAMBLE
25 MALLORY & NATSIS LLP

26 By: /s/ Edward Fates

27 EDWARD G. FATES
Attorneys for Receiver
28 THOMAS HEBRANK