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12 UNITED STATES DISTRICT COURT  
 13 CENTRAL DISTRICT OF CALIFORNIA  
 14 SOUTHERN DIVISION

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15 SECURITIES AND EXCHANGE  
 16 COMMISSION,  
 17  
 18 Plaintiff,  
 19  
 20 v.  
 21 MEDICAL CAPITAL HOLDINGS,  
 22 INC.; MEDICAL CAPITAL  
 23 CORPORATION; MEDICAL  
 24 PROVIDER FUNDING  
 25 CORPORATION VI; SIDNEY M.  
 26 FIELD; and JOSEPH J.  
 27 LAMPARIELLO,  
 28  
 Defendants.

Case No. SACV 09-818 DOC (RNBx)  
 RECEIVER'S OMNIBUS RESPONSE  
 TO NOTEHOLDER OBJECTIONS  
 Date: October 15, 2012  
 Time: 8:30 a.m.  
 Ct Rm: 9D  
 Judge: Hon. David O. Carter

Docket  
 10/2/12

1 **I. INTRODUCTION**

2 Thomas A. Seaman, Federal Equity Receiver (the “Receiver”) for Medical  
3 Capital Holdings Inc., Medical Capital Corporation, Medical Provider Funding  
4 Corporation VI, and their subsidiaries and affiliates in this matter (the  
5 “Receivership Entities”) has received approximately ninety objections from  
6 individual Noteholders to the settlement reached between the Receiver and Wells  
7 Fargo Bank, N.A. (“Wells Fargo”) and Bank of New York Mellon (“BNYM”)  
8 (collectively, the “Trustees”). Many of these objections have been filed with and/or  
9 sent to the Court, but a few have not.<sup>1</sup> The Receiver here provides an Omnibus  
10 Response to Noteholder Objections and incorporates by reference his Reply to the  
11 Motion for Approval of Settlement with Wells Fargo and BNYM.

12 The Receiver is sympathetic to the losses suffered by Noteholders and  
13 understanding of the frustration voiced by Noteholders who provided objections.  
14 The Receiver’s duty and desire has always been to maximize the return of losses  
15 suffered by the Receivership Entities and thus to maximize the return of losses to  
16 the Noteholders. The Receiver would like nothing more than to provide the  
17 Noteholders with a distribution that provides a 100% return of their losses. But the  
18 Receiver is constrained by the law and the facts, in particular the law regarding the  
19 duties of indenture trustees and the provisions of the NISAs. The Receiver entered  
20 into settlement discussions with the Trustees and ultimately secured a \$106 million  
21 settlement because the Receiver sought to maximize the return of funds to the  
22 Receivership Entities while avoiding the delays, risks, and costs of litigation,  
23 against indenture trustees who receive significant protection under the law and  
24 under the terms of contracts that were designed to insulate them from liability.

25  
26  
27 <sup>1</sup> The Receiver submits those objections that he has received but that have not  
28 been previously filed as exhibits to the Declaration of Joseph V. Mauch in Support  
of the Receiver’s Omnibus Response to Noteholder Objections filed herewith.

1 **II. DISCUSSION**

2 The approximately ninety Noteholders' oppositions come in a variety of  
3 formats. Some are emails and handwritten letters from individual Noteholders,  
4 while some are form letters and pleadings that appear to have been drafted by one  
5 person and signed by others. Despite their variety of formats, nearly all of these  
6 objections repeat, in some form and combination, the same principal arguments:

- 7
- 8 • The Trustees were guardians of the Noteholders' investments and they  
9 should not be allowed to avoid their fiduciary duties;
  - 10 • Promises were made to the Noteholders at the time of investment about  
11 the role of the Trustees that the Noteholders relied on and that were  
12 instrumental in their decision to purchase the notes;
  - 13 • The settlement should not be approved because the settlement amount  
14 only represents 10% of the Noteholders' total losses;
  - 15 • The settlement should not be approved because the Receiver does not  
16 represent the Noteholders and he should not be allowed to settle their  
17 claims.<sup>2</sup>

17 By way of example, an objection from Darryl Lane states that "I was told not to  
18 worry or have any concern about these investments because of the backing of Wells  
19 Fargo Bank." Maurice Yenni likewise states, "The whole marketing and sales  
20 premise on this offering was based on the fact that the two major banks were the  
21 trustees and therefore would monitor the financial activities of Med/Cap." Paul and  
22 Rosemary Boriello state, in turn, that "[b]oth of these banks had as trustees, a  
23 fiduciary relationship to act on behalf of all of the investors in Medical Capital."

24 The Receiver is deeply sympathetic to the frustration and the anger that these  
25 victims have expressed about their plight. These people were induced to invest in

26 \_\_\_\_\_  
27 <sup>2</sup> One trade creditor, Stratose Inc., has also filed an objection to the settlement.  
28 Stratose's objection, unlike those of the Noteholders, is based on the proposed  
distribution of the settlement funds, an issue which has already been presented to  
the Court and which the Court has reserved ruling on. *See* SEC Doc. No. 841.

1 Medical Capital on false pretenses that included the claim that Wells Fargo and  
2 BNYM would have far greater responsibilities than they actually did. In some if  
3 not many cases, those lies cost Noteholders their life savings.

4 The objections also demonstrate, however, that these Noteholders do not  
5 understand the true role of the indenture trustees, the limitations on the duties and  
6 liabilities of indenture trustees under the law and the NISAs, and the effect of the  
7 Court's prior rulings acknowledging and enforcing those limitations. This lack of  
8 understanding is not surprising, as (with only one or two exceptions) these  
9 Noteholders are neither lawyers nor securities professionals. The Objections rest  
10 on a lack of information or understanding regarding (1) the difference between a  
11 common-law trustee and an indenture trustee, (2) the Court's prior dismissal of  
12 claims based on promises or representations made to Noteholders, in the Private  
13 Placement Memoranda ("PPMs") or otherwise, regarding the purpose or duties of  
14 the Trustees, (3) the Receiver's role in this proceeding and the effect of the  
15 settlement, and (4) the difference between the Noteholders' total losses and the  
16 potential liability of the Trustees.

17 **A. The Limited Duties of Indenture Trustees.**

18 Many of the Noteholders' objections refer to Wells Fargo and BNYM as  
19 "trustees" and explicitly or implicitly refer to their fiduciary duties. But as this  
20 Court has previously held, in accord with the great majority of courts, that as  
21 indenture trustees Wells Fargo and BNYM did not owe fiduciary duties to the  
22 Receivership Entities or to the Noteholders. *See* MDL Doc. No. 143 at 12 ("Under  
23 the law of all three states, indenture trustees owe no pre-default fiduciary duties.  
24 *See Meckel v. Cont'l Res. Co.*, 758 F.2d 811, 816 (2d Cir. 1985) ('Unlike the  
25 ordinary trustee, who has historic common-law duties imposed beyond those in the  
26 trust agreement, an indenture trustee is more like a stakeholder whose duties and  
27 obligations are exclusively defined by the terms of the indenture agreement.')).  
28 The Court has likewise held, again in accord with the great majority of courts, that

1 as indenture trustees Wells Fargo and BNYM are only obligated to perform those  
2 duties explicitly set forth in the Note Issuance and Security Agreements (“NISAs”).  
3 *See id.* at 6 (“As discussed above, the duties of indenture trustees arise solely from  
4 the terms of the contract. Plaintiffs may not recast a suit for breach of those contract  
5 duties as a tort suit for negligence.”). In other words, not only are the Trustees not  
6 subject to the heightened standards of a fiduciary, but the Receiver’s and the  
7 Noteholders’ ability to hold the Trustees liable for the losses that the Medical  
8 Provider Funding Corporations (“MPFCs”) suffered is significantly circumscribed  
9 by the governing contracts – contracts that were designed in large part to minimize  
10 the Trustees’ exposure to claims.

11 Again, it is entirely understandable that individual Noteholders believe that a  
12 “trustee,” as Wells Fargo and BNYM were called in the relevant documents,  
13 actually has the fiduciary obligations that “trustees” are commonly known to have.  
14 But that belief is not correct, as settled law and the Court’s rulings establish. The  
15 Trustees duties here are defined by the NISAs and cannot be expanded. *See Abbate*  
16 *Doc. No. 227* at 13 (“The result is the same under both California and Colorado  
17 law. Under Colorado law, ‘an implied covenant cannot be used to rewrite,  
18 contradict, or add to the express terms of the contract.’ . . . Similarly, under  
19 California law, ‘it is universally recognized [that] the scope of conduct prohibited  
20 by the covenant of good faith is circumscribed by the purposes and express terms of  
21 the contract.’”)(citations omitted). The Court’s rulings were based on well-  
22 established legal principles, and while it is fair to question whether those legal  
23 principles are reasonable or appropriate, the Receiver, like the Court, is required to  
24 take the law into account when considering the risks and rewards of litigation  
25 against the Trustees.

26 **B. No Claims Against Plaintiffs Based on PPMs or Other**  
27 **Misrepresentations.**

28 The same is true regarding the claims based on promises or representations

1 made to Noteholders, in the PPMs or otherwise, relating to the purpose or duties of  
2 the Trustees. The Objections suggest that at least some Noteholders still believe  
3 what the principals of MedCap told them: That the Trustees would act as  
4 fiduciaries to the Noteholders overseeing the business operations of MedCap, that  
5 they would be the “guardians” of the investors’ money, and that they would  
6 “monitor” all the decisions made by the MPFCs. But, as discussed above, the  
7 Court has held that the Trustees did not have any such obligations, in rulings that  
8 comport with established law. The statements made by the principals of Medical  
9 Capital and others to the Noteholders regarding the role of Wells Fargo and BNYM  
10 cannot change that fact.

11 The Court has also held that the representations in the PPMs and other  
12 promises made to Noteholders by the perpetrators of the Ponzi scheme and others  
13 are not a basis for claims against the Trustees. *See Abbate* Doc. No. 227 at 13  
14 (“Perhaps investors relied on MedCap’s statements, but Plaintiffs have not  
15 connected such statements to Defendants’ alleged conduct.”). The Trustees did not  
16 have the duties that the perpetrators of the Ponzi scheme falsely represented them to  
17 have, and the Trustees cannot be held liable by the Receiver or the Noteholders for  
18 the making of those false representations. Any reasonable evaluation of the  
19 Receiver’s settlement with the Trustees must take these legal realities into account.

20 **C. The Receiver Did Not Settle the Noteholders’ Claims.**

21 The Noteholders appear to misunderstand the Receiver’s position about what  
22 claims he has settled and what the settlement achieves. While the Noteholders will  
23 ultimately benefit from the Receiver’s settlement with the Trustees, this does not  
24 mean that the Receiver is representing them or settling their claims. The Receiver  
25 does not, and does not purport to, directly represent the Noteholders. The Receiver,  
26 in turn, has not pursued and settled, and does not purport to have pursued and  
27 settled, any claim on behalf of the Noteholders. The Receiver’s position is not that  
28 he has settled the Noteholders’ claims or that he has taken over the role of their

1 attorneys. Rather, as the Court knows, the Receiver's position is (1) that, once he  
2 actually pursues claims against the Trustees for breach of the NISAs, only he has  
3 the authority to pursue and resolve those claims, and (2) that the legal effect of a  
4 fair and reasonable settlement by the Receiver of the Receivership Entities' claims  
5 is the extinguishment of all the Noteholders' derivative claims against the settling  
6 parties.

7 **D. The Difference Between Losses and Liability.**

8 The great majority of the Noteholders' objections refer to the fact that the  
9 settlement amount of \$106 million represents a return of only about 10 cents on the  
10 dollar when compared to the total losses suffered by Noteholders. Such a  
11 comparison is wholly understandable, but unfortunately is not legally relevant.  
12 Ultimately, the Trustees are responsible only for the losses that they caused through  
13 breaches of their contractual duties. Some of the losses suffered by the  
14 Receivership Entities, and thus in turn by the Noteholders, were caused by the  
15 Trustees' breaches, but some losses were caused by other factors, including market  
16 conditions, poor investment decisions by the Medical Capital principals, and, most  
17 importantly, the fraud perpetrated by those same principals. The Trustees are not  
18 liable for all of these losses and any evaluation of the settlement must take that into  
19 account.

20 To compare the amount achieved by the settlement with the Trustees to the  
21 amount of total losses is to compare the settlement to an unattainable goal. The  
22 only appropriate comparison is to compare the settlement to a realistic amount that  
23 could be achieved at trial, discounted for both the risks and costs of litigation. As  
24 discussed in detail in the Receiver's Motion for Approval and his Reply to the  
25 Motion, the Receiver believes that the settlement fares very favorably when  
26 evaluated in this correct light. Indeed, the Receiver is not aware of any case where  
27 any party has secured nearly so much money from indenture trustees as the  
28 Receiver has secured here — and the Receiver, like the Court, is well aware of the

1 many cases in which indenture trustees ultimately paid nothing.

2 **III. CONCLUSION**

3 As the objections demonstrate, many Noteholders were misled into investing  
4 in Medical Capital by, among other things, false representations about the roles and  
5 duties of the Trustees. Those false representations have, in turn, affected some of  
6 the Noteholders' views about the nature and strength of the claims against the  
7 Trustees and the extent of Trustees' liability. But the Trustees were not fiduciaries.  
8 Their responsibilities were determined by the NISAs, not by the PPMs or any other  
9 statements about them. They cannot be held liable for the false statements that  
10 others made about them. The Receiver sympathizes with the Noteholders, not only  
11 because they were defrauded in a massive Ponzi scheme but also because the terms  
12 of the NISAs and the provisions of the law greatly limit their ability to recover their  
13 losses against the Trustees. But the Receiver's settlement must be evaluated in  
14 light of the legal and factual realities of this case, and not against what might be  
15 possible if the Trustees actually had the duties and obligations that the perpetrators  
16 of the Medical Capital scheme claimed they had.

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DATED: October 1, 2012.

SHARTSIS FRIESE LLP

By: /s/ Frank A. Cialone

FRANK A. CIALONE

Attorneys for Plaintiff THOMAS A. SEAMAN,  
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## Responses, Replies and Other Motion Related Documents

8:09-cv-00818-DOC-RNB Securities and Exchange Commission v. Medical Capital Holdings Inc et al

(RNBx), DISCOVERY

### UNITED STATES DISTRICT COURT for the CENTRAL DISTRICT OF CALIFORNIA

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#### Docket Text:

**RECEIVER'S OMNIBUS RESPONSE TO NOTEHOLDER OBJECTIONS re MOTION for Settlement Approval[721] filed by Receiver Thomas A Seaman. (Cialone, Frank)**

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