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9 UNITED STATES DISTRICT COURT
10 CENTRAL DISTRICT OF CALIFORNIA
11 SOUTHERN DIVISION

12 SECURITIES AND EXCHANGE
COMMISSION,

13 Plaintiff,

14 v.

15 MEDICAL CAPITAL HOLDINGS,
16 INC.; MEDICAL CAPITAL
CORPORATION; MEDICAL
17 PROVIDER FUNDING
CORPORATION VI; SIDNEY M.
18 FIELD; and JOSEPH J.
LAMPARIELLO,

19 Defendants.
20
21
22

Case No. 8:09-cv-0818-DOC (RNBx)

**RECEIVER'S REPLY TO
OPPOSITIONS/RESPONSES TO
RECEIVER'S OMNIBUS
OBJECTION TO NOTEHOLDER
CLAIMS**

Date: March 12, 2012
Time: 8:30 a.m.
Ctrm: 9D
Judge: Hon. David O. Carter

1 **I. INTRODUCTION**

2 Thomas Seaman, Permanent Receiver ("Receiver") for Medical Capital
3 Holdings, Inc. ("MCH"), Medical Capital Corporation ("MCC"), Medical Provider
4 Funding Corporation VI ("MP VI"), and their subsidiaries and affiliates
5 (collectively, "Medical Capital") submits this reply to oppositions/responses
6 submitted to the Receiver's Omnibus Objection to Noteholder Claims ("Omnibus
7 Objection").

8 The Omnibus Objection was filed by the Receiver to establish a consistent
9 approach to Noteholder claim calculation that is both workable and fair, and to
10 obtain Court approval of that approach. Pursuant to the Order Approving Receiver's
11 Ex Parte Application For Extension of Period to File Evidentiary Support for
12 Claims, and Setting Further Briefing and Hearing Schedule entered on December
13 21, 2011, the Receiver filed a Status Report Summarizing Responses to Claim
14 Objections ("Status Report") on February 20, 2012 (Dkt. No. 649). Here, the
15 Receiver addresses the merits of the responses/oppositions, formally and informally
16 communicated to the Receiver by Noteholders.

17 **A. Overview of Noteholder Claim Objections, Responses and**
18 **Resolutions**

19 Pursuant to the Court's order approving the claim process (Dkt. No. 470), the
20 Receiver sent out over 11,200 Claim Information Forms to Noteholders, which
21 included the amounts each Noteholder had invested and the amounts each had
22 received in interest and principal. Approximately 7.345 Noteholders returned their
23 Claim Information Forms indicating that they did not dispute the Receiver's records.
24 3151 Noteholders did not return their Claims Information Forms. Of those, only
25 710 were Noteholders who ultimately had positive claim amounts. Approximately
26 704 Noteholders disputed the principal and interest set out in the forms or failed to
27 respond to additional amended information provided by the Receiver.

28

1 To date, the Receiver and his staff his staff have resolved 351 disputes and
2 reached agreed upon claim amounts. Attached as Exhibit A to the Supplemental
3 Declaration of Thomas A. Seaman in Support of Objections to Trade Creditor,
4 Employee, and Noteholder Claim ("Seaman Declaration") is a spreadsheet of
5 Noteholders who were previously listed as contested,¹ and who now have an agreed
6 claim amount.

7 About 404 Noteholders remain who may dispute some aspect of their claim.
8 Of those, 262 have not responded to information provided by the Receiver
9 supporting his calculation of their MIMO claim amount. Another 40 Noteholders
10 have responded but have not provided any or sufficient evidence that refutes the
11 information that the Receiver has provided. Both groups of Noteholders are listed in
12 Exhibit B attached to the Seaman Declaration. The Receiver believes that a
13 significant portion of those who have failed to respond or refuse to concede that they
14 received certain payments are doing so because they do not agree with a MIMO
15 calculation approach. The Receiver also believes that if the Court approves of the
16 MIMO claim calculation approach, it can and should rule on the allowed claim
17 amount of these Noteholders as listed in Exhibit B to the Seaman Declaration.

18 Finally, there are approximately 102 Noteholders for which an actual
19 evidentiary dispute exists about their interest or principal payments, or with whom
20 the Receiver is continuing productive discussions. These Noteholders are
21 indentified on Exhibit C to the Seaman Declaration. The Receiver believes many of
22 the Exhibit C may be resolved with further discussion, and some may need to be
23 resolved by the Court. Thus, the status and categories of Noteholder claim
24 calculation issues are as follows:

25 Claim Information Forms sent out by Receiver	11,200
26 Claim Information Forms returned as agreed and previously filed as 27 Exhibit B to Dkt. No. 601	7,345

28 ¹ Dkt. No. 601.

1	Disputed Claim Information Forms	753 ²
2	Disputes that have been resolved (Exhibit A, resolved)	351
3	Noteholders who have not timely responded additional information provided by Receiver (Exhibit B)	262
4	Noteholders who have responded but failed to provide sufficient evidence to refute Receiver's calculation (Exhibit B)	40
5	Noteholders for whom an actual evidentiary dispute may exist or with whom the Receiver is still having productive discussions (Exhibit C)	102

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8 As to those Noteholders who, after further discussions with the Receiver,
9 continue to dispute their claim calculation, the Receiver proposes that he submit a
10 report to the Court by May 11, 2012. The report will identify all Noteholders in this
11 category, as well as the number and nature of the remaining disputes. The Receiver
12 requests that the Court issue an order approving the following procedure for the
13 determination of the remaining claims: if the Noteholder so stipulates, the Court, a
14 Magistrate Judge or a Special Master shall determine the allowed claim amount
15 based on the pleadings submitted by such Noteholder and the Receiver; if the
16 Noteholder does not so stipulate, and insists on the opportunity to be heard by the
17 Court, a hearing shall be set before the Court, a Magistrate Judge or a Special
18 Master to determine such claim disputes.

19 In addition to the disputes that exist with respect to the accounting of
20 Noteholder investment and payment amounts, the Receiver received approximately
21 240 responses to the Omnibus Objection, although only about half of those were
22 solely directed at the MIMO claim approach.³ The overwhelming majority of
23 opposing Noteholders (57) took issue with the Receiver's inclusion of paid off notes
24 in the MIMO calculation. 22 Noteholders asserted that accrued but unpaid interest
25

26 ² The number of Noteholder disputing claim information increased after the initial
27 responses were received.

28 ³ The balance of the responses were directed at various aspects of the Receiver's
draft proposed Plan of Distribution (the "Draft Plan") attached to the Receiver's
Declaration in Support of Omnibus Objections. Those objections/oppositions are
premature and are briefly addressed below

1 should be added to claim amounts, and three Noteholders articulated an opposition
2 to "collapsing the MP Entities."⁴ Nine Noteholders who were also brokers involved
3 in selling the Medical Capital notes objected to their commissions being treated as
4 money-out in the MIMO calculation. The determination of Noteholder objections to
5 the Receiver's proposed approach to claim calculation is committed to the discretion
6 of the Court and briefed below.

7 II. MIMO OBJECTIONS

8 The Receiver's proposed approach to claim calculation was influenced by the
9 following factors demonstrated in the Receiver's Forensic Accounting:

- 10 • Medical Capital violated the parameters contained in the Private
11 Placement Memoranda limiting the type of lending activities in which
12 MP Entities were to engage.⁵
- 13 • Medical Capital transferred uncollectible loans and other assets with
14 nonexistent or overstated values between the MP Entities, for the
15 apparent purpose of using newly invested cash for the payment of
16 administrative fees, and principal and interest payments to earlier
17 investors.⁶
- 18 • Medical Capital's lending and investing activities were generally not
19 profitable.⁷
- 20 • The Note Issuance and Security Agreements ("NISA's) purporting to
21 grant security interests in collateral pools did not prevent the transfer of
22 assets between collateral pools and did not protect Noteholders from
23 the misuse of their funds.⁸

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25
26 ⁴ The objections articulating this argument also address related plan issues and are
premature to that extent.

27 ⁵ Receiver's Forensic Accounting Report, Dkt. No. 608; pp. 12-17.

28 ⁶ Id. pp. 17-22.

⁷ Id. p. 10.

⁸ Id. pp. 17-22.

- There will be insufficient recoveries in the Receivership estate to make 100% distributions on net claim amounts.⁹

The two overriding principles that inform judicial decision making in federal equity receiverships are: i) the District Court supervising an equity receivership has extremely broad power to determine an appropriate course of action to achieve an equitable and efficient administration of the estate for the benefit of claimants; and ii) similarly situated victims of fraud should receive roughly equal treatment. *SEC v. Hardy*, 803 F.2d 1034, 1037-38 (9th Cir. 1986); *United States v. 13328 & 13324 State Highway 75 N.*, 89 F.3d 551, 553 (9th Cir. 1996). Although the Receiver cannot and does not take the position that case law mandates the adoption of MIMO claim calculation, the case law does establish that MIMO is a permissive, appropriate, and preferred approach under similar circumstances and is a determination committed to the discretion of the supervising court where necessary to achieve equity. *CFTC v. Topworth Int'l, Ltd.*, 205 F.3d 1107, 1110 (9th Cir. Cal. 1999).

A. MIMO Claim Calculation Achieves Equity

The Ninth Circuit first recognized the appropriateness of the MIMO approach in *In re Tedlock Cattle Company, Inc.*, 552 F.2d 1351 (9th Cir. 1977). *Tedlock* involved a ponzi scheme promising large returns from the operation of cattle feedlots. After the collapse, early investors argued for a benefit-of-the-bargain claim calculation. The Court agreed with the bankruptcy trustee, that where insufficient assets existed to pay claims in full, equitable principles must override state law and limit the claims to the net amount of funds invested. To do otherwise would permit investors who had already recovered their initial investment and "false profits" to unfairly defeat the claims of later investors who had yet to receive any return on their investment.

⁹ Id. p. 41.

1 Since *Tedlock* was published, numerous courts have upheld the MIMO
2 approach to ensure that all investors receive a return on their initial investment
3 before any investors receive distributions based on profit claims. In *Topworth* the
4 Ninth Circuit affirmed a net investment approach: ". . . [d]efined as total amount
5 deposited by the claimant with the receivership entities less amounts returned to the
6 claimant from the receivership entities and less any illegal trading profits reinvested
7 by or credited to the claimant." *Id.* at 1110. See also, *SEC v. Capital Consultants,*
8 *LLC*, 2002 U.S. Dist. LEXIS 27399 (D. Or. 2002) *aff'd*, 397 F.3d 733 (9th Cir.
9 2005).

10 As demonstrated by the Forensic Accounting, the lending and investing
11 activities of the MP Entities were generally not profitable and the transfer of assets
12 between entities allowed Medical Capital to conceal the lack of profits. Moreover,
13 Medical Capital's failure to abide by parameters set out in the PPM's occurred across
14 all MP Entities. Thus, all Noteholders were victims of these practices, and whether
15 they received interest and/or repayment of principal on their notes was a fortuity and
16 a function of when they invested and whether they re-invested when their notes
17 matured. Under these circumstances, where investors are all victims of the same
18 fraud, equity requires that all recover their principal before any recover interest or
19 profits. *Topworth* at 1116. That goal is best achieved by calculating claims on a net
20 or MIMO basis.¹⁰

21 **B. Exclusion of Accrued Interest and Consequential Damages Is**
22 **Appropriate Under These Circumstances**

23 57 Noteholders submitted responses that argued for the inclusion of accrued
24 interest and/or consequential damages. While the Receiver has no objection in
25

26 ¹⁰ Several Noteholders objected to the apparent inequity of allowing Noteholders
27 who were "net winners" and therefore have no MIMO claims, to retain amounts
28 received in excess of principal. The Receiver considered the practicalities of
attempting to recover these amounts and determined that, with minor exception,
the expense of pursuing such claims was not justified given the amounts at stake
on an individual basis and the challenges of collecting any amounts awarded.

1 principal to including those elements in allowed claim amounts, as a practical
2 matter, the exercise of investigating and calculating such amounts is not warranted
3 under these circumstances, where Noteholder recoveries will be limited. The
4 aggregate amount of Noteholder claims calculated on a MIMO basis is roughly
5 \$839,303 million. The Receiver has marshaled \$99.7 million in assets. And
6 although the Receiver still holds unliquidated assets and claims against third parties,
7 it is highly unlikely that he will recover additional amounts that will approach 100%
8 of aggregate MIMO claims.

9 Soliciting, reviewing and verifying accrued interest and consequential damage
10 claims, would be a very time intensive and expensive process given that there are
11 over 8,000 Noteholders with positive MIMO claims. Incurring that expense now
12 when it will likely be unnecessary, is not in the best interests of Noteholders. If
13 recoveries do exceed aggregate MIMO claims, the Receiver can request authority to
14 modify claim amounts or simply distribute a "bonus" on existing claim amounts.

15 **C. Treating Broker Commissions As Money Out Is Appropriate**

16 Approximately 125 Noteholders were also brokers who received commissions
17 from Medical Capital for selling clients Medical Capital notes. The Receiver
18 proposes that commissions paid to these Noteholders be treated as money-out in the
19 MIMO calculation. Nine of the broker/Noteholders objected to this proposal.
20 Several objected on the grounds that they did not actually receive the full amount
21 commission deducted. To the extent that a broker/Noteholder timely objected to
22 their MIMO claim calculation, and can provide evidence that they did not receive
23 the entire commission, the Receiver is willing to adjust the money-out calculation to
24 reflect amounts actually received.¹¹ However, the Receiver believes that treating
25 commissions actually received as money-out is appropriate under the circumstances.

26 _____
27 ¹¹ The objecting broker/Noteholders are included in Exhibit C to the Seaman Dec.
28 The Receiver anticipates resolving most of these disputes prior to the March 12th
hearing. To the extent disputes remain, the Receiver proposes following the
same procedure described for all Exhibit C Noteholders.

1 The argument advanced by certain brokers that their good faith is demonstrated by
2 their own investment in Medical Capital is not compelling and doesn't change the
3 fact that additional money went out of Medical Capital to the brokers to pay
4 commissions. Broker/noteholder should not receive an advantage over entirely
5 innocent investors by ignoring these additional monies received from Medical
6 Capital.

7 **III. CLAIM CALCULATION DISPUTES**

8 As stated above, over 7,345 Noteholders returned the Claim Information
9 Forms and indicated that they agreed with the information provided by the Receiver.
10 Those Noteholders who did not respond were nevertheless included in the database
11 of Noteholders with undisputed amounts. The Receiver intends to include those
12 Noteholders in distributions. Additional Claim Information Forms were also
13 received after the bar date. To the extent that the late-filed forms agreed with the
14 Receiver's numbers the Noteholders were added to the database for undisputed
15 amounts. To the extent that Noteholders disputed the numbers in the Claim
16 Information Forms, they were added to the contested claim database.¹²

17 **IV. OBJECTIONS TO DRAFT PLAN**

18 The Receiver included for informational purposes a draft distribution plan as
19 an exhibit to the Receiver's Declaration in Support of Claim Objections.
20 Approximately 120 Noteholders wrote to object to provisions of the Draft Plan,
21 rather than to the specific amount of a claim or its calculation. The input from the
22 Noteholders concerning the Draft Plan is valuable information that will assist the
23 parties and the Court in formulating a distribution plan. The Receiver will consider
24 all of the Noteholder comments in formulating a plan for distribution, which will be
25 submitted to the Court in a noticed motion in due course. However, because a plan
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28 ¹² Seaman Declaration, ¶ 2.

1 is not before the Court, it is not necessary or appropriate to address these issues at
2 this time.

3 **V. CONCLUSION**

4 The Receiver respectfully requests that the Court approve the MIMO claim
5 calculation approach for all Noteholder claims and approve the allowed amount of
6 Noteholder claims contained in the Receiver's Exhibits A and B, to the Seaman
7 Declaration. The Receiver further requests that the Court approve the Receiver's
8 recommended approach to resolving the remaining claim calculation disputes.

9
10 Dated: February 27, 2012

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12 By: /s/ Loraine L. Pedowitz

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