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11  
12 UNITED STATES DISTRICT COURT  
13 DISTRICT OF OREGON

14  
15 **SECURITIES AND EXCHANGE  
COMMISSION,**

16 Plaintiff,

17 vs.

18 **CAPITAL CONSULTANTS, LLC, f/k/a  
19 CAPITAL CONSULTANTS, INC.,  
20 JEFFREY L. GRAYSON and BARCLAY  
GRAYSON,**

21 Defendants.

Case No. CV00-1290 KI

AMENDED FIRST INTERIM REPORT OF  
RECEIVER (RECEIVED BY THE COURT)

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1 **I. INTRODUCTION**

2 Thomas F. Lennon, the receiver ("Receiver") of Capital  
3 Consultants, LLC ("CCL"), and of any trust, partnership, joint  
4 venture or other entity controlled by CCL, submits this amended  
5 initial report ("Amended Initial Report") in compliance with  
6 Paragraphs VII(C), (D), (F) and (G) of the Stipulation and Order  
7 Re Preliminary Injunction, Asset Freeze and Appointment of a  
8 Permanent Receiver entered in SEC v. Capital Consultants, LLC,  
9 et al. ("SEC Order") and Paragraphs 7(A), (B), (C) and (E) of the  
10 Stipulation and Order Re Preliminary Injunction and Appointment  
11 of Receiver entered in Department of Labor v. Capital  
12 Consultants, LLC., et al. ("DOL Order"). This Amended Initial  
13 Report is to provide this Court and all interested parties with  
14 the status of the Receiver's activities, investigations,  
15 analyses, opinions and conclusions to date. The Receiver and his  
16 retained professionals have met with many people and reviewed  
17 countless documents and records over a 30-day period. **The volume**  
18 **of material and information acquired, the shortness of time, the**  
19 **complexity of the matters analyzed and the need for additional**  
20 **information, verification and analysis requires that this Amended**  
21 **Initial Report be considered preliminary; the Receiver may need**  
22 **to materially modify its contents after further consideration.**  
23 **Furthermore, the Court has not yet determined the probative value**  
24 **of the information contained in this Amended Initial Report nor**  
25 **determined the admissibility of such information in any future**  
26 **proceeding.**

27 The Receiver's duties, responsibilities and activities fall  
28 generally into four categories: (i) securing, protecting and

1 recovering assets, including tangible assets, intangible assets  
2 and choses-in-action; (ii) investigating the who, when, how and  
3 why of the basis for the receivership proceedings;  
4 (iii) analyzing and developing, with Court approval, an equitable  
5 approach for distribution of assets and losses to investors; and  
6 (iv) the liquidation of assets and the review and allowance of  
7 claims against the receivership estate. This Amended Initial  
8 Report touches on each of these four categories in varying detail  
9 and degree in relation to the focus of the Receiver during the  
10 first 30 days of this case.

## 11 **II. EXECUTIVE SUMMARY**

12 CCL was in the business of managing investments for its  
13 clients. CCL was very successful in attracting clients. As of  
14 September 21, 2000, CCL had 301 clients. The amount of  
15 investment money under management grew dramatically over the last  
16 six years to \$927 million. CCL's management fees grew also, from  
17 \$4.8 million in 1994 to \$12.0 million in 1999.

18 CCL chose a variety of investment vehicles on behalf of its  
19 clients. Some selections did not comply with the provisions of  
20 the individual investment advisor agreements ("IAA's"). CCL  
21 placed approximately \$442 million into public equities and cash  
22 ("Public Investments"), and approximately \$485 million into  
23 private investments including loans and private equities  
24 ("Private Investments").

25 Investments in the Public Investments portfolio generally  
26 produced returns in the range of expectation for such types of  
27 investments. In contrast, investments in the Private Investments  
28 portfolio selected by, created by, and serviced by CCL produced

1 substantial losses. The management fees charged by CCL for  
2 Private Investments substantially exceeded the management fees  
3 generated by the Public Investments portfolio. Thus, CCL was  
4 faced with the dilemma of growing its business and protecting its  
5 major revenue source in the face of substantial investment  
6 losses.

7 CCL had over \$450 million invested in various forms of  
8 private secured loans, but the Receiver found no evidence of  
9 thorough or valid credit underwriting due diligence by CCL with  
10 respect to its borrowers. As a result, it holds a large number  
11 of the equivalent of "junk-debt;" borrowers who are incapable of  
12 ever repaying principal and collateral that has little or no  
13 value. Problem loans were frequently the subject of  
14 restructurings, maturity extensions, new advances, debt-for-  
15 equity swaps and the like. Few loans were declared to be in  
16 default. The Receiver found no evidence that CCL clients were  
17 aware of problems in the Private Investments portfolio.

18 Although the extent of the losses are not yet known, it  
19 appears that little to none of the over \$450 million in  
20 outstanding loans are of high enough quality to be worth anything  
21 near the amount of client dollars invested by CCL. The  
22 WCC/Sterling loans suffered particularly substantial losses as a  
23 result of the release of some collateral, the consumption of  
24 other collateral, the substitution of marginal value collateral,  
25 the release of guarantors, and the substitution of the original  
26 borrower with a new non-operating entity indirectly owned by CCL  
27 itself. During 1999 and through September 2000, despite the  
28 losses in the Private Investments portfolio, Jeffrey L. Grayson

1 personally withdrew from CCL in the form of salary and other  
2 distributions over \$3.6 million.

3 The Receiver took control of CCL on September 21, 2000. He  
4 immediately secured the premises and company assets, reduced  
5 staffing and began evaluating how best to protect investments  
6 under management. He also commenced a thorough investigation of  
7 CCL operations. Public Investments are in the process of being  
8 assigned to new investment management firms, and with Court  
9 approval, the Receiver has arranged for Merrill Lynch to contact  
10 clients in need of a new manager. Private Investments are being  
11 evaluated and a liquidation proposal is being developed.

### 12 **III. BACKGROUND**

#### 13 **A. Procedural Background**

14 On the afternoon of September 21, 2000 (the "Appointment  
15 Date"), this Court (by the Honorable Garr M. King) entered the  
16 SEC and DOL Orders appointing Thomas F. Lennon as permanent  
17 receiver for CCL and affiliates under CCL's control.  
18 Concurrently with the SEC and DOL Orders, at the request of the  
19 Receiver, the Court entered its Order Staying All Proceedings  
20 (the "Stay Order") to protect the receivership estate from  
21 adverse actions against its assets and from having to respond to  
22 litigation while the Receiver discharged his duties.

23 Among the specific tasks the Receiver is required to  
24 undertake pursuant to Paragraph VII of the SEC Order and  
25 Paragraph 7 of the DOL order are:

- 26 • to conduct such investigation and discovery  
27 as may be necessary to locate and account  
for all of the assets . . . ,
- 28 • to take such action as is necessary and  
appropriate to preserve and take control of

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and to prevent the dissipation, concealment or disposition of any assets . . . ,

- to make an accounting, . . . of the assets and financial condition . . . ;
- to employ attorneys and others to investigate and, where appropriate, to institute, pursue and prosecute all claims and causes of action of whatever kind and nature . . . .

**B. Glossary of Key Names**

520 SW Yamhill LLC	A limited liability company established in January 1998, wholly-owned by CCL and used as a collection agency by CCL to own loans in foreclosure/default.
A-Fem	A-Fem Medical Corporation, a Nevada corporation located in Portland, Oregon. A publicly traded medical technology company targeting women's health needs. A-Fem was incorporated in Nevada on December 9, 1986, as Xtramedics, Inc. In June 1994, it changed its name to ATHENA Medical Corporation and in July 1997, to A-Fem Medical Corporation. A-Fem is publicly traded over-the-counter (OTC) under stock symbol is AFEM.OB.
Beacon	Beacon Financial, LLC, a limited liability company founded on November 30, 1999. Owned by Norman Madan, Anne Byer, Kenye Echantenthal, Timothy Gamwell and Marie Durham, who also own (with the exception of Marie Durham) Brooks, FAFCO and Creditmart.
Brooks	Brooks Financial, LLC, a limited liability company founded on June 4, 1999, as a wholly-owned subsidiary of FAFCO. Owned by Norman Madan, Anne Byer, Kenye Echantenthal and Timothy Gamwell, who also own Creditmart and Beacon.

1 Byer Funding Byer Funding, LLC, a Florida  
2 limited liability company. An  
3 automobile finance company whose  
4 managing member is Timothy Gamwell  
5 and to which \$701,910 in loans were  
6 funded by CCL on its own behalf  
7 between March and June 2000 under a  
8 \$20 million commitment.

9 CCI Capital Consultants Inc., an Oregon  
10 S-corporation formed in 1968 to  
11 provide investment and money  
12 management services. CCI assigned  
13 all of its assets and liabilities  
14 to CCL in exchange for 100% of the  
15 membership interest in CCL,  
16 effective August 31, 1999.

17 CCL Capital Consultants LLC, an Oregon  
18 limited liability company  
19 registered with the Securities and  
20 Exchange Commission as an  
21 investment advisor under the  
22 Investment Advisor's Act of 1940.  
23 On August 31, 1999, CCL assumed all  
24 of the assets and liabilities of  
25 CCI. CCL's current ownership  
26 structure is as follows: Jeffrey  
27 L. Grayson - 62.50%, Barclay L.  
28 Grayson - 18.75%, Blake J. Grayson  
- 18.75%.

Capital Center Capital Center, an Oregon General  
Partnership owned 49% by CCL and  
51% by the Jeffrey L. Grayson  
Trust. The primary business  
purpose of CCP is to hold the  
Capital Center Plaza building at  
2300 SW First Avenue, Portland,  
Oregon.

Creditmart Creditmart, Inc., a Nevada  
corporation operating in Miami,  
Florida. Owned by Norman Madan,  
Anne Byer, Kenye Echantal and  
Timothy Gamwell, who also own  
Beacon, Brooks and FAFCO.

1 CJM Planning CJM Planning Corporation, a New  
2 Jersey corporation, a financial  
3 planning firm established in 1974  
4 that conducts business via a  
5 network of independent agents in 31  
6 states. Oxbow Partners acquired  
7 majority control of the company in  
8 July 1998.

9 CWH Capital Wilshire Holdings, Inc., a  
10 Nevada corporation resulting from  
11 the merger of CWH Mergco Sub Corp.  
12 with WCC and the replacement  
13 borrower to WCC.

14 Dyer Daniel Dyer, the managing director  
15 of Oxbow Partners, Oxbow Fund B and  
16 Oxbow Fund I.

17 FAFCO Florida Auto Finance Company, a  
18 Florida corporation. A sub-prime  
19 auto finance company founded in  
20 1986 and located in Miami, Florida.  
21 Owned and operated by Norman Madan,  
22 Anne Byer, Kenye Echantenthal and  
23 Timothy Gamwell, who also own  
24 Creditmart, Beacon and Brooks.

25 Gamwell Timothy Gamwell, an individual  
26 residing in Florida who is a member  
27 in Brooks, Beacon, Creditmart and  
28 Byer funding.

Huish R. Court Huish, Matthew B. Huish  
and Craig B. Huish, founders of  
Sterling.

Oxbow Fund B Oxbow Capital 1999 Fund B, LLC, a  
New Jersey limited liability  
company established on July 15,  
1999, to invest in long-term equity  
and equity equivalent investments.  
Oxbow Partners is the managing  
member; Dyer is the managing  
director of both companies.

1	Oxbow Fund I	Oxbow Capital 1999 Fund I, LLC, a
2		New Jersey limited liability
3		company established on January 12,
4		1999, by Oxbow Partners. Oxbow
5		Partners is the managing member;
		Dyer is the managing director of
		both companies.
6	Oxbow Partners	Oxbow Capital Partners, LLC, a
7		Washington limited liability
8		company which was formed in 1998.
9		The managing member of both Oxbow
		Fund B and Oxbow Fund I. Dyer is
		the managing director.
10	PSC	Portland Servicing Corporation, a
11		Nevada corporation formed in 1993
12		and a sister corporation to WCC
		with the same owners and
		management.
13	Sterling	Sterling Capital, LLC, a New Jersey
14		limited liability company formed on
15		or about November 24, 1998, by
16		R. Court Huish (managing member),
		Matthew B. Huish and Craig B.
		Huish.
17	VIS	VIS Holding Corporation, a Florida
18		corporation, founded in 1992 by
19		George M. Scopetta and John R.
		Scopetta.
20	WCC	Wilshire Credit Corporation, a
21		Nevada corporation originally
		formed in 1989.
22	WFSG	Wilshire Services Financial Group,
23		Inc., a Delaware corporation,
24		formed to acquire loans to be
		serviced by WCC.

25 **C. Summary of Receiver's Activities to Date**

26 **1. Security**

27 The CCL offices at 2300 SW First Avenue, Portland, Oregon,  
 28 were secured by the Receiver and his staff on the afternoon of

1 the Appointment Date. A professional security firm was  
2 immediately engaged and provided 24 hours per day, 7 days per  
3 week coverage. A guard was positioned at the main elevator  
4 entrance to the primary administrative area of the company with  
5 instructions to limit access to current employees and visitors as  
6 specified by the Receiver. All written material and equipment  
7 being removed from the premises is subject to inspection and  
8 approval by the security guards and the Receiver.

9 On the Appointment Date, a locksmith was hired and all doors  
10 were re-keyed and new master keys made. New keys are controlled  
11 by the Receiver. For purposes of safeguarding computer memory  
12 devices, a single office was selected and keyed separately with  
13 the keys in the exclusive possession of the Receiver's computer  
14 consultants, PricewaterhouseCoopers. No master keys were issued  
15 to this room. All computer memory devices were shut down with  
16 access denied until the Receiver was informed by  
17 PricewaterhouseCoopers that access would not jeopardize the  
18 memory.

19 Access to the CCL office is controlled by an electronic pass  
20 card system. That system is in the control of the Receiver and  
21 all existing pass cards were confirmed, deleted or reissued  
22 depending on the status of the holder.

23 The company maintains off site storage for over 1,500  
24 storage boxes. The Receiver has established the procedures to be  
25 utilized in the placement or retrieval of boxes in storage. A  
26 copy of the Court's order appointing the Receiver was given to  
27 the operators of the facility and instructions were issued so  
28 that all transactions are under the sole control of the Receiver.

1                   **2. Staff Reductions**

2           On the Appointment Date, the Receiver initiated a review of  
3 the staff positions and the current organization chart of CCL  
4 with the Chief Financial Officer and other supervisory personnel.  
5 At that time, there were 40 employee positions. Three  
6 supervisory positions were vacant as a result of resignations  
7 immediately prior to the Receiver's appointment by Jeffrey L.  
8 Grayson, Chairman of the Board; Barclay Grayson, the President;  
9 and Dean Kirkland, the Senior Vice President of Marketing. The  
10 Receiver determined that the positions that were vacant would not  
11 be filled. In addition, the Receiver evaluated the remaining  
12 positions and the personnel and reduced the staffing as follows:

<u>Description</u>	<u>Positions Eliminated</u>
Marketing and Client Services	3
Operations and Finance	3
Private Investments	4
Administrative	7
Public Investments	<u>5</u>
Total Positions Eliminated	22

18 With these reductions and the prior resignations, CCL presently  
19 has 15 employees. It is the Receiver's intention to continue to  
20 reduce staff as the need for various services are eliminated.

21                   **3. Professionals Employed by the Receiver**

22           The Receiver has engaged qualified professionals to assist  
23 him and his staff.

24           **Allen Matkins Leck Gamble and Mallory LLC** was employed as  
25 general receivership counsel. Since the Appointment Date, Allen  
26 Matkins has assisted the Receiver in fulfilling his duties under  
27 the SEC and DOL Orders, including: (i) appearing at all hearings  
28 in the SEC and DOL cases; (ii) representing the estate's

1 interests in connection with litigation commenced by certain  
2 trustees of CCL's pension fund clients, styled Hazzard et al. v.  
3 Capital Consultants, LLC et al.; (iii) interviewing interested  
4 parties including current and former employees of CCL and  
5 representatives of certain clients and borrowers of CCL;  
6 (iv) negotiating, drafting, preparing and arguing the Receiver's  
7 motion relating to the Referral Agreement with Merrill Lynch;  
8 (v) negotiating and documenting the terms of sale of Jeffrey  
9 Grayson's interest in a limited liability company owning an  
10 airplane; (vi) negotiating several potential loan workouts with  
11 current borrowers; (vii) reviewing loan files re outstanding  
12 legal and enforcement issues; (viii) investigating potential  
13 claims and causes of action held by CCL and its affiliates;  
14 (ix) assisting the Receiver and his other professionals in  
15 reviewing and analyzing CCL's operations and business affairs;  
16 (x) reviewing and representing the Receiver in ongoing litigation  
17 in which CCL is the plaintiff; (xi) providing general advice to  
18 the Receiver regarding his rights, powers and duties under the  
19 SEC and DOL Orders and general equity receivership law; and  
20 (xii) assisting the Receiver prepare this Amended Initial Report.

21 **Foster Pepper & Shefelman PLLC** was employed as local Oregon  
22 counsel for the Receiver. Since the Appointment Date, assistance  
23 has included: (i) appearances and representation of the Receiver  
24 in all pending state-court litigation; (ii) providing advice on  
25 Oregon and Washington State law for transactions and  
26 debtor/creditor matters; (iii) coordinating file turnover from  
27 CCL prior counsel and substitution of attorneys; and  
28

1 (iv) assisting Allen Matkins with the variety of matters it is  
2 handling.

3 **KPMG LLP** was employed as forensic accountants and financial  
4 consultant to the Receiver. Since the Appointment Date,  
5 assistance has included: (i) analysis of loan portfolio  
6 activity; (ii) preparation of loan data summaries; (iii) analysis  
7 of certain other private investments; (iv) investigation of  
8 alleged fraudulent activity; (v) transaction and asset tracing;  
9 (vi) analysis of CCL financial position and results;  
10 (vii) preparation of information for the Amended Initial Report;  
11 and (viii) other accounting and financial support to the Receiver  
12 and his counsel.

13 **PricewaterhouseCoopers** ("PWC") was employed as computer  
14 consultants. PWC's tasks are focused on the collection,  
15 preservation, recovery and analysis of CCL's electronic data.  
16 PWC has taken action to freeze the electronic data contained in  
17 CCL's servers, personal computers and laptops. PWC has  
18 implemented the following security measures to prevent access to  
19 the CCL's servers: (i) disconnected all cables and modem lines  
20 to prevent remote access; (ii) disabled all user accounts;  
21 (iii) changed the servers' administrator passwords; and  
22 (iv) barred physical access to CCL's servers. PWC has downloaded  
23 all electronic information contained in CCL's file and e-mail  
24 servers to magnetic tape for review. Additionally, PWC has taken  
25 physical custody of all electronic back-up tapes of CCL's file  
26 and e-mail servers. Regarding CCL's employees' personal  
27 computers and laptops, PWC has (i) taken physical custody of the  
28 personal computers and laptops belonging to CCL officers and

1 certain other employees of CCL; (ii) downloaded all electronic  
2 information contained in these computers; and (iii) copied this  
3 information to a centralized computer for analysis.

#### 4 4. Initial Investigation and Steps to Take Possession 5 of Assets

6 The Receiver, with the assistance of his retained  
7 professionals and certain CCL employees, has (i) taken possession  
8 and control of known CCL assets; (ii) investigated and analyzed  
9 the operations of CCL; and (iii) analyzed and evaluated the  
10 present status of CCL's Private and Public Investment portfolios.

11 The Receiver has taken physical custody of all known  
12 personal property assets and records other than files in the  
13 possession of CCL outside attorneys and accountants, and  
14 downloaded CCL's computer systems and records. The Receiver has  
15 contacted banks and others holding funds on behalf of CCL and has  
16 either frozen such funds or asserted rights to those funds.

17 The Receiver has taken inventory of the physical assets  
18 owned by CCL and has also consulted with present and former CCL  
19 staff concerning the location and identification of CCL assets.  
20 The Receiver has met with and talked to, in certain instances  
21 frequently and extensively:

- 22 • Counsel for the SEC;
- 23 • Counsel for the DOL;
- 24 • Representatives of the Department of Labor, Federal  
25 Bureau of Investigation, Internal Revenue Service and  
26 U.S. Attorneys Office;
- 27 • Former counsel for CCL;
- 28 • Barclay Grayson and his counsel;

- 1 • Counsel for Jeffrey Grayson;
- 2 • Dyer and his counsel;
- 3 • Gamwell and his counsel;
- 4 • Counsel for and a representative of Oregon Auto
- 5 Center (one of CCL's borrowers);
- 6 • Counsel for and a representative of Washington Alder
- 7 LLC (one of CCL's borrowers);
- 8 • Some of CCL's former employees;
- 9 • All of CCL's current employees;
- 10 • Certain creditors of CCL;
- 11 • Numerous representatives of CCL clients;
- 12 • Representatives of Merrill Lynch and other investment
- 13 advisors; and
- 14 • Representatives of CB Richard Ellis.

15 The Receiver has also contacted all known parties involved  
16 in litigation with CCL and has filed notice of this Court's stay  
17 order in all known proceedings. The Receiver has filed notices  
18 of the SEC Order and DOL Order in the following jurisdictions  
19 pursuant to 28 U.S.C. § 754: District of Oregon, Western  
20 District of Washington and Eastern District of Washington. The  
21 Receiver has also recorded the Stay Order in the following  
22 counties: Multnomah County, Oregon.

#### 23 **IV. CCL BUSINESS INFORMATION**

##### 24 **A. Overview of CCL**

25 Since 1968, CCL and its predecessor, CCI, provided  
26 investment management services to corporations, single and multi-  
27 employer pension and other retirement plans, foundations and  
28 wealthy individuals. As of the Appointment Date, CCL's assets

1 under management were valued by CCL at approximately \$1.0 billion  
2 and were managed on behalf of approximately 301 clients. Located  
3 in Portland, Oregon, CCL had 40 employees prior to the Receiver's  
4 appointment.

5 CCL managed a broad range of investments which can generally  
6 be classified as either Public or Private Investments. Public  
7 Investments include stocks, mutual funds and fixed-income  
8 securities such as government and corporate bonds. Private  
9 Investments include loans secured by real estate and non-real  
10 estate collateral, real estate ownership, and unregistered stock.  
11 As of the Appointment Date, the cost and claimed market value<sup>1</sup>  
12 reported by CCL<sup>2</sup> for portfolios under management included:

13 **As of September 21, 2000**

	<u>Cost</u>	<u>Claimed Market Value<sup>1</sup></u>	<u>% of Total Market Value</u>
14 Public Investments	\$ 407,826,008	\$ 495,224,288	49%
15 Private Investments	484,990,270	487,789,527	48%
16 Cash and Equivalents	33,737,731	33,737,731	3%
17 Total Portfolio	<u>\$ 926,554,009</u>	<u>\$ 1,016,751,547</u>	<u>100%</u>

18 CCL represented that it provided the following comprehensive  
19 investment management services:

20  
21  
22 <sup>1</sup> These amounts have not been subjected to testing or  
23 verification by an independent third party. With respect to  
24 the Private Investments, the market value is substantially  
25 less.

26 <sup>2</sup> CCL performed certain valuation and reconciliation procedures  
27 at month end for each of the portfolios. These procedures were  
28 completed as of August 31, 2000, but have not been performed  
for the interim period ending September 21, 2000. CCL's  
employees utilized available information to estimate amounts  
for cost and market value as of September 21, 2000. As such,  
these amounts represent a less precise, yet reasonable estimate  
of amounts which would have been reported by CCL using its  
standard accounting and valuation procedures for this time  
period.

- 1 • Investment research and analysis - Extensive analysis  
2 of private investments including evaluation of the  
3 company's market position, financial performance,  
4 management team, credit strength and collateral and  
the liquidity risks, exit strategy and anticipated  
return of the investment.

5 *The Receiver found no evidence to date that this*  
6 *activity was undertaken by CCL.*

- 7 • Investment selection - Investment selections made by  
8 "asset-specific investment committees each consisting  
9 of 10+ investment professionals ensuring that your  
assets are under constant supervision and review."

10 *The Receiver found no evidence to date that this*  
11 *activity was undertaken by CCL.*

- 12 • Portfolio management - Investments subject to ongoing  
13 analysis and active monitoring and collateral values  
14 and market information consistently reviewed by  
15 either CCL or third-party auditors. Client  
portfolios reviewed on an ongoing basis with respect  
to asset diversification, sector/securities  
concentrations, and compliance with client investment  
guidelines.

16 *The information found by the Receiver to date indicates*  
17 *that these activities may not have been competently,*  
18 *systematically nor uniformly done.*

- 19 • Valuation and reporting - "Portfolio appraisals" to  
20 clients on a quarterly basis indicating the cost,  
market value and yield of each investment in that  
client's portfolio.

21 *The Receiver found evidence that the market values*  
22 *reported to clients were not determined properly and*  
23 *were inaccurate.*

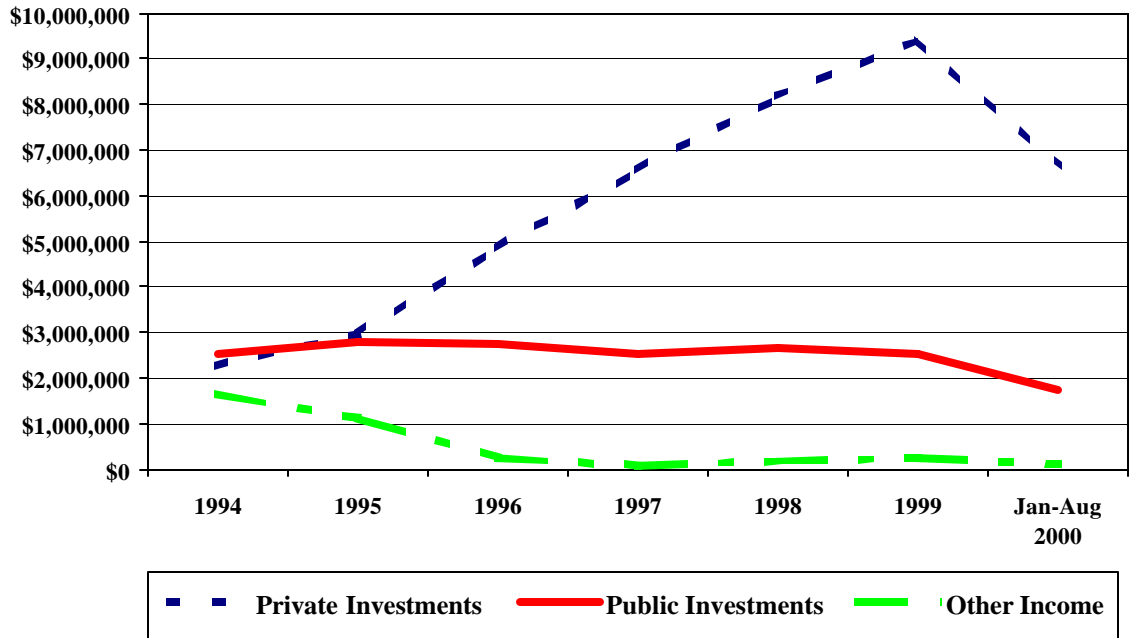
24 CCL charged its clients annual management fees calculated as  
25 a percentage of the CCL-reported market value of the assets under  
26 management. Fees ranged from 0.2% to 1.0% for Public  
27 Investments, 1.0% to 3.0% for Private Investments, and 0.5% for  
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1 cash and equivalents. The Receiver's preliminary research  
2 suggests that these fees may exceed industry norms, particularly  
3 in regard to the Private Investments.

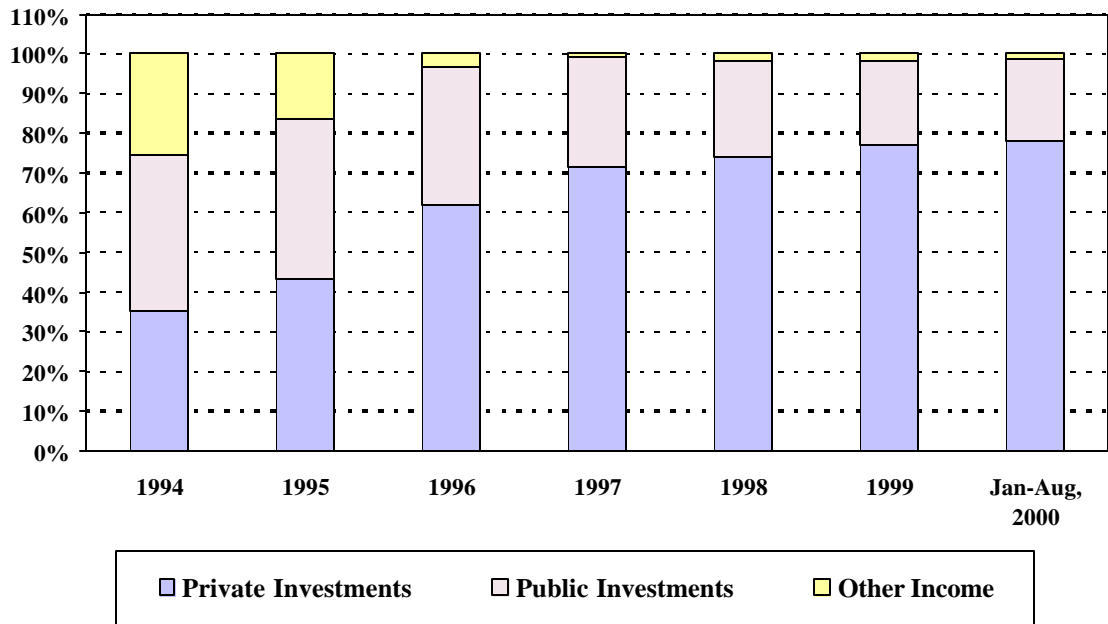
4 Total CCL fees more than doubled from \$4.8 million in the  
5 year ended December 31, 1994, to \$12.0 million in the year ended  
6 December 31, 1999. Management fees for Private Investments  
7 quadrupled over this six plus year period. Management fee  
8 revenues from Private Investments expanded from 36% of total  
9 revenues in the year ended December 31, 1994, to 78% of total  
10 revenues for the eight months ended August 31, 2000.

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Capital Consultants, LLC  
Annual Revenue



Capital Consultants, LLC  
% of Total Revenue



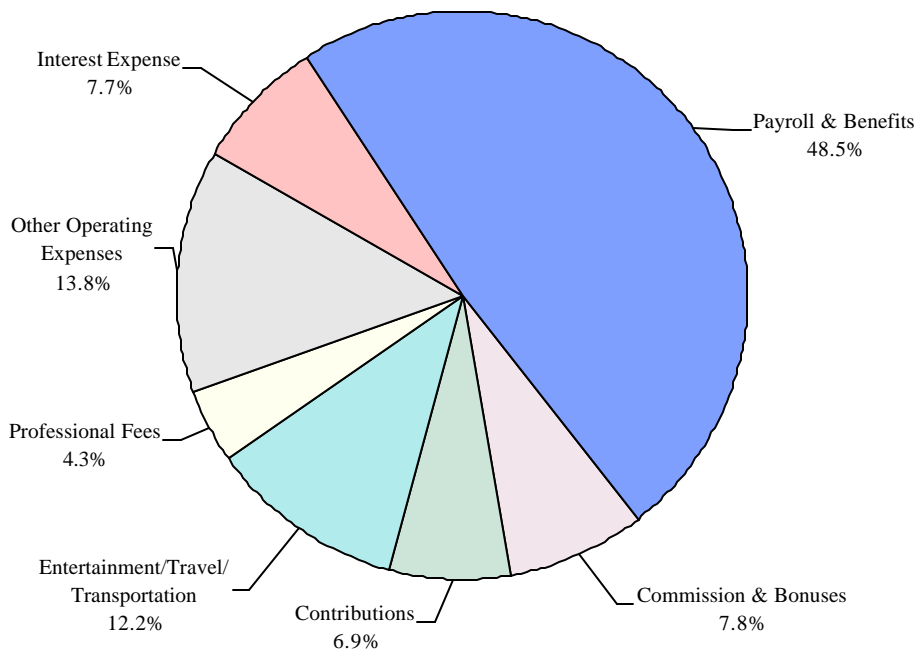
Payroll, benefits, commissions and bonuses comprised over half of CCL's expenses in the year ended December 31, 1999, and

1 the eight months ended August 31, 2000. Other significant  
2 operating expenses included entertainment/travel/transportation,  
3 contributions, professional fees and interest expense. According  
4 to the internal books and records, total net income of CCL (prior  
5 to consolidation with Capital Center) for the year ended  
6 December 31, 1999, and the eight months ended August 31, 2000 was  
7 \$1.3 million and \$0.7 million, respectively.

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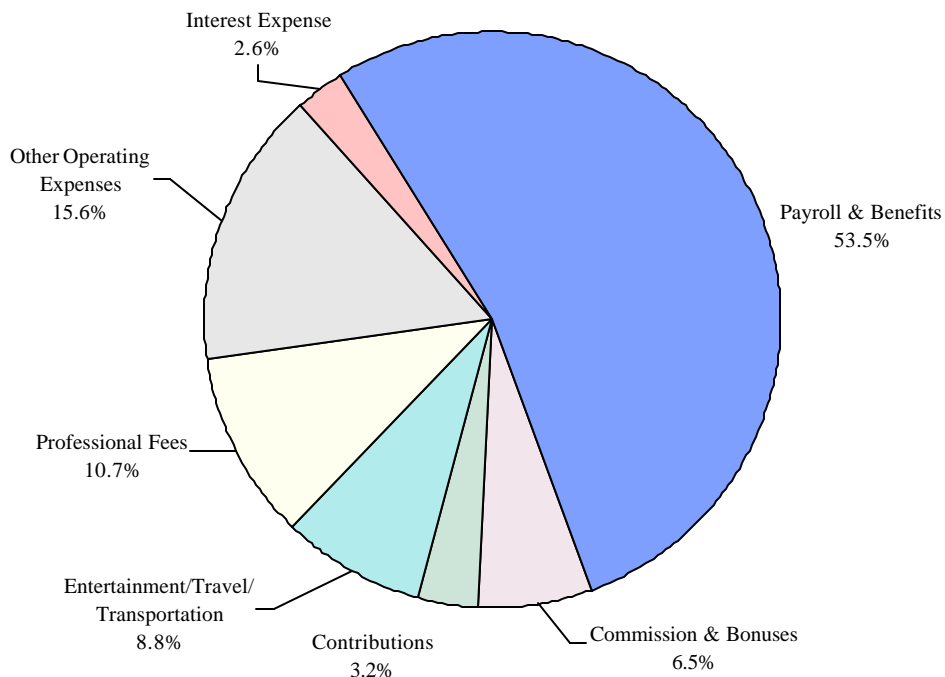
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### Capital Consultants, LLC Expense Summary 1999



Source: CCL internal accounting records

### Capital Consultants, LLC Expense Summary 2000



Source: CCL internal accounting records

1           **B. ASSETS AND LIABILITIES OF CCL AND AFFILIATES**

2           **1. Financial Statement Reporting**

3           The financial statements of CCL and its predecessor, CCI,  
4 were audited by Arthur Andersen & Co. for the year ended  
5 December 31, 1993. Moss Adams LLP audited the financial  
6 statements between 1994 and 1998. PWC was named as auditor for  
7 the year ended December 31, 1999, but disclaimed an opinion on  
8 CCL's financial statements. The financial statements of CCL and  
9 Capital Center were consolidated for annual reporting purposes.  
10 However, CCL and Capital Center maintain separate internal  
11 accounting records. The information described below is derived  
12 from the unaudited, internal accounting records of CCL and  
13 Capital Center as of August 31, 2000.

14           **2. CCL Assets and Liabilities**

15           Current Assets - As of August 31, 2000, CCL held cash of  
16 \$249,095 in six operating and money market accounts. On the  
17 Appointment Date, the balance in those accounts was \$176,939.  
18 CCL's accounts receivable for billed and accrued management fees  
19 were \$1,230,866. The aging indicates that 92% were between 31  
20 and 60 days, and only 2% were greater than 90 days. However,  
21 since the Receiver's appointment, the collection of management  
22 fees has slowed substantially. Other current assets included  
23 deposits and prepaid expenses of \$349,561, some of which relate  
24 to prepayments for hunting and other adventure excursions, and  
25 related-party receivables of \$46,627.

26           Fixed Assets - Fixed assets consist of furniture and  
27 fixtures, fine art, computer and office equipment, software, and  
28

1 leasehold/tenant improvements with a total cost of \$2,140,146 and  
2 a depreciated net book value of \$462,774 as of August 31, 2000.

3       Loans/Notes Receivable - CCL holds a note receivable from  
4 Byer Funding to which \$701,910 in loans were funded in four  
5 advances between March and June 2000 under a \$20 million  
6 commitment. CCL records and employees describe the loans as  
7 being subsequently restructured on an "informal" basis due to  
8 issues regarding CCL's line of credit. The amount outstanding at  
9 August 31, 2000, was \$597,054. CCL also holds a 20% interest in  
10 a note receivable from Cascade General; the other 80% is held by  
11 Evanston Insurance Company. The note resulted from the  
12 restructuring of prior loans made to Cascade General and related  
13 companies as part of the private loan portfolio. CCL receives  
14 monthly principal and interest payments, and the amount  
15 outstanding as of August 31, 2000, was \$143,469.

16       Investments - As of August 31, 2000, CCL held several  
17 investments with a total book value of \$852,389. CCL owns a 50%  
18 interest in two beach houses in Seaside, Oregon. Joel Grayson is  
19 the co-owner. CCL's share for both houses, recorded at  
20 historical cost, is \$463,465. CCL has an investment with a  
21 recorded claimed market value of \$40,558 in A-Fem Series A  
22 Convertible Preferred Stock, held as part of CCL's 401(k) profit-  
23 sharing plan. CCL owns a 49% interest in Capital Center. CCL  
24 holds a 40% interest in Forest Heights, a limited liability  
25 company engaged in the development of residential real estate in  
26 Portland, Oregon. This investment is accounted for using the  
27 equity method and had a book value of \$188,941. CCL also owns  
28

1 520 SW Yamhill LLC, the book value for which consists only of  
2 organizational costs.

3 Current Liabilities - CCL's payroll payable, including  
4 salary, vacation, commissions, benefits and related taxes, was  
5 \$170,239 as of August 31, 2000. Accounts payable were \$203,444,  
6 consisting primarily of rent, 401-k contributions, legal fees,  
7 and advance payments for hunting and other adventure excursions.  
8 The aging indicates that approximately 64% of the accounts  
9 payable were current, and the remainder were less than 30 days  
10 past due. CCL's reported accrued expenses and miscellaneous  
11 payables/deposits of \$411,933 included legal fees of \$235,062,  
12 plus business and property taxes, travel and entertainment  
13 expenses, insurance premiums and lease deposits.

14 Deferred Income - CCL's balance sheet at August 31, 2000,  
15 included \$531,465 and \$202,572 in deferred income related to  
16 management fees charged in advance for Private and Public  
17 Investments, respectively.

18 Bank of the West Line of Credit - The outstanding balance of  
19 \$1,550,000 at August 31, 2000, represents a full extension of  
20 amounts available under the Bank of the West line of credit,  
21 which expired on September 30, 2000, and bore interest at prime  
22 plus 1%. This obligation has fully matured, and Bank of the West  
23 has given notice that it intends to enforce its rights  
24 thereunder.

25 Long-Term Liabilities - Total long-term liabilities on the  
26 CCL balance sheet at August 31, 2000, were \$1,068,034. The note  
27 of \$257,295 to the family trusts of Barclay and Blake Grayson is  
28 payable upon a 395-day written notice, bears interest at prime

1 plus 1%, and is amortized over 15 years. The beach house  
2 mortgage of \$129,398 on the property at 50 12th Avenue, Seaside,  
3 Oregon, is amortized on a monthly basis through July 2027 with  
4 interest at 8.5%. A note to Joel Grayson is payable upon 90  
5 days' written notice, bearing interest payable monthly at prime  
6 plus 1%. Between April and July 2000, CCL repaid \$240,000,  
7 resulting in an outstanding balance of \$556,750 at August 31,  
8 2000, \$500,000 of which is subordinated pursuant to terms of the  
9 Bank of the West line of credit. The balance of the capitalized  
10 lease payable to PacificOne for computer equipment was \$124,591.  
11 A note payable to a former stockholder, Gregory J. Houser, had a  
12 balance of \$204,677 at December 31, 1999, and was payable in  
13 monthly installments of \$27,000, including interest at 9%, with  
14 the final installment paid in August 2000.

### 15 3. Capital Center Assets and Liabilities

16 Current Assets - As of August 31, 2000, Capital Center's  
17 balance sheet reflected cash held in an operating account of  
18 \$63,895, accounts receivable of \$40,009 for rent owed by CCL, and  
19 prepaid property taxes of \$19,075.

20 Fixed Assets - The primary asset owned by Capital Center is  
21 Capital Center Plaza located at 2300 SW First Avenue, Portland,  
22 Oregon. As of August 31, 2000, the balance sheet reflected  
23 building and improvements with a cost of \$1,592,742 and a net  
24 book value of \$572,957; land with a cost of \$300,000; and  
25 amortized loan costs with a net book value of \$37,332. The  
26 property was appraised on September 16, 1999, at a value of  
27 \$3,255,000.

28

1           Current Liabilities and Deposits - As of August 31, 2000,  
2 Capital Center's balance sheet reflected accounts payable of  
3 \$3,849 and refundable deposits of \$1,292.

4           Long-Term Liabilities - The outstanding mortgage owed to  
5 National Mortgage is payable in monthly installments of \$17,041,  
6 including interest at 8.25%, and is due November 2009. The  
7 balance as of August 31, 2000, was \$1,969,573.

#### 8           4.   Other Assets and Liabilities

9           The assets of Jeffrey L. Grayson and Barclay Grayson are not  
10 presently assets of the receivership estate, although they have  
11 been frozen as a result of the SEC Order. However, CCL has paid  
12 for the purchase, use and/or expenses for many assets in the  
13 personal possession of the Graysons. The Receiver has met with  
14 representatives of the Graysons in order to explore whether some  
15 of the Graysons' assets should be claimed by the Receiver as  
16 property of the Receivership estate. The Graysons have been  
17 cooperative to date in providing information requested by the  
18 Receiver.

19           Shortly after his appointment, the Receiver received notice  
20 that Jeffrey Grayson proposed to sell an interest he held in B/G  
21 and Associates, LLC ("B/G") to one of the other members of B/G,  
22 the Meisenbach Company, for \$138,625.00. B/G is an entity formed  
23 to own and operate a Cessna airplane. Since Jeffrey Grayson's  
24 personal assets are subject to a freeze under the SEC Order, the  
25 Receiver's and the SEC's consent were required in order to  
26 complete the sale.

27           Based upon an insurance company estimate of value, the  
28 Receiver was satisfied that the proposed sale price was

1 reasonable. However, the Receiver discovered through his review  
2 of CCL records that CCL funds had been used to pay Grayson's  
3 share of B/G's expenses. Accordingly, the Receiver concluded  
4 that part or all of Grayson's LLC interest and the sales proceeds  
5 therefrom were rightfully the property of CCL.

6 Thus, the Receiver agreed that the Grayson B/G interest  
7 could be sold as proposed, but only on the condition that the  
8 full amount of the sales price be held by the Receiver. The  
9 Court has advised that as long as the Receiver, Grayson and the  
10 SEC so stipulate, the purportedly personal assets, such as the  
11 B/G interest, can be sold, and the proceeds sequestered by the  
12 Receiver subject to later resolution of appropriate distribution.  
13 At the time of this Amended Initial Report, a purchase and sale  
14 agreement and corresponding stipulation have been signed and it  
15 is anticipated that the sales proceeds from the B/G interest will  
16 be received by the Receiver within days.

### 17 **C. Overview of CCL Clients**

18 Taft-Hartley plans (pension, defined contribution, health  
19 and welfare, vacation and training trust accounts) and other  
20 union clients provided 77% of the assets under management.  
21 Approximately 301 clients had investments under management as of  
22 the Appointment Date. The average client had \$3.4 million under  
23 management. But, half the clients had less than \$400,000 under  
24 CCL management. The largest client had \$165.4 million under  
25 management.

26 Taft-Hartley and union clients hold approximately  
27 \$407.7 million of the \$487.8 million in Private Investments. CCL  
28 had 715 total client accounts as of the Appointment Date. Sixty-

1 two pension accounts (9% of all accounts) totaled over half of  
 2 the total assets under management. The 20 largest accounts of  
 3 all investors (3% of all accounts) each had balances in excess of  
 4 \$10 million, and totaled almost half (48%) of total assets under  
 5 management. The largest 140 accounts (20% of all accounts) each  
 6 had balances in excess of \$1 million and totaled 87% of the  
 7 assets under management.

8 Below are summaries of the clients and accounts managed by  
 9 CCL as of September 21, 2000:

CCL Clients as of September 21, 2000					
	Client Type				Total
	Taft Hartley/ Unions	Corporations	Individuals	Other	
Number of Clients	97	56	156	14	323
Percent of Total	30%	17%	48%	4%	100%
Public Investments	\$ 350,228,005	\$ 100,739,566	\$ 29,844,541	\$ 14,412,178	\$ 495,224,288
Private Investments	407,706,443	24,504,494	53,442,672	2,135,918	487,789,527
Cash and Equivalents	26,203,436	4,436,467	2,921,095	176,734	33,737,731
Total	<u>\$ 784,137,883</u>	<u>\$ 129,680,526</u>	<u>\$ 86,208,308</u>	<u>\$ 16,724,829</u>	<u>\$ 1,016,751,547</u>
Percent of Total	77%	13%	8%	2%	100%
Average Client Investment	\$ 8,083,896	\$ 2,315,724	\$ 552,617	\$ 1,194,631	\$ 3,147,838
Median Client Investment	\$ 639,282	\$ 142,695	\$ 137,403	\$ 697,952	\$ 387,809
Largest Client Investment	\$ 108,599,113	\$ 26,137,777	\$ 5,984,572	\$ 5,078,309	\$ 108,599,113
<b>Source:</b>					
CCL portfolio management system; client groupings estimated for presentation purposes.					

**CCL Accounts as of September 21, 2000**

	<u>Account Type</u>				<u>Total</u>
	<u>Pension</u>	<u>401(k)/IRA/ Profit Sharing</u>	<u>Health &amp; Welfare</u>	<u>Other</u>	
Number of Accounts	62	312	26	315	715
Percent of Total	9%	44%	4%	44%	100%
Total Account Balance	\$ 516,798,188	\$ 248,737,409	\$ 80,709,773	\$ 170,506,178	\$ 1,016,751,547
Percent of Total	51%	24%	8%	17%	100%
Average Account Size	\$ 8,335,455	\$ 797,235	\$ 3,104,222	\$ 541,289	\$ 1,422,030
Largest Account	\$ 86,496,569	\$ 17,572,453	\$ 17,836,611	\$ 8,022,709	\$ 86,496,569

	<u>Account Balances in Excess of</u>				<u>Total</u>
	<u>\$500,000</u>	<u>\$1 million</u>	<u>\$5 million</u>	<u>\$10 million</u>	
Number of Accounts	241	140	47	20	715
Percent of Total	34%	20%	7%	3%	100%
Amount in Accounts	\$ 955,779,949	\$ 884,664,045	\$ 674,147,279	\$ 489,536,442	\$ 1,016,751,547
Percent of Total	94%	87%	66%	48%	100%
Average Account Size	\$ 3,965,892	\$ 6,319,029	\$ 14,343,559	\$ 24,476,822	\$ 1,422,030

**Source:**  
CCL portfolio management system; account groupings estimated for presentation purposes.

**V. THE PUBLIC INVESTMENTS PORTFOLIO**

**A. Description of Investments**

The following is a summary of CCL Public Investments on the Appointment Date.

	<u>Value in \$ Millions</u>	<u>% of Asset Class</u>	<u>% of Public Investment</u>
<u>Public Equities</u>			
Large Cap	\$ 125	58 %	
Small Cap	90	42 %	
Total	<u>215</u>	<u>100 %</u>	<u>43 %</u>
<u>Public Fixed Income</u>			
Short-Term	24	23 %	
Intermediate	75	71 %	
Core	6	6 %	
Total	<u>105</u>	<u>100 %</u>	<u>21 %</u>
<u>Mutual Funds</u>			
Prudential	135	77 %	
Schwab	40	23 %	
Total	<u>175</u>	<u>100 %</u>	<u>35 %</u>
<u>Grand Total</u>	<u>\$ 495</u>		

1 The Receiver reviewed selected representative accounts in  
2 both the Small Cap and Large Cap investment portfolios for the  
3 period from the Appointment Date through October 17, 2000. The  
4 sample tested from the Small Cap portfolio outperformed CCL's  
5 benchmark, the Russell 2000 Index, by 9.1%. The sample tested  
6 from the Large Cap portfolio outperformed CCL's selected  
7 benchmark, the S&P 500 Index, by 2.6%.

## 8 **B. Public Investment Program**

### 9 **1. Public Investment Committee**

10 As reported to the Receiver, CCL managed the Public  
11 Investments portfolio through the Public Investment Committee,  
12 chaired by the head of Public Investments Roger Thomas. The  
13 Public Investment Committee consisted of Public Investment  
14 personnel plus Jeffrey L. Grayson and Barclay Grayson.

### 15 **2. Public Equities**

16 As of the Appointment Date, 113 accounts, held by  
17 89 clients, were invested to some extent in public equities,  
18 predominately common stock. As reported to the Receiver, for  
19 each of CCL's large cap and small cap equity products, CCL  
20 utilized the following strategy: a "concentrated portfolio" (25  
21 to 30 stocks), "low turnover" (three to five stocks per year),  
22 and a "buy and hold" (expected holding period of three to five  
23 years).

### 24 **3. Public Fixed-Income Securities**

25 As of the Appointment Date, 58 accounts, managed on behalf  
26 of 47 clients, included publicly traded fixed-income securities.  
27 CCL's stated philosophy was to purchase high quality (generally  
28 A-rated, or better) corporate securities on a "buy and hold (to

1 maturity)" basis while minimizing the interest rate-related risk  
2 of the portfolio (i.e., prudent duration management vs. each  
3 product's designated benchmark). Benchmarks included: 3-Month  
4 Treasury Bills; the Merrill Lynch 1-3 Year Treasury Index; the  
5 Lehman Intermediate Government/Credit Index; and the Lehman  
6 Aggregate Index.

#### 7 **4. Third-Party Mutual Funds**

8 As of the Appointment Date, 85 accounts, managed on behalf  
9 of 82 clients, were invested at least partially in third-party  
10 mutual funds (e.g., Prudential). With respect to this asset  
11 class, on an annual basis, CCL's Public Investment Committee met  
12 to evaluate if there was a need to (1) change the allocation  
13 percentages related to particular asset classes or risk/reward  
14 options and (2) change the selection of any specific mutual fund  
15 currently in use for a given asset class.

#### 16 **C. The Receiver's Activities**

17 Under the SEC and DOL Orders and federal equity receivership  
18 law, the Receiver is authorized and directed to take all  
19 necessary action to collect and preserve the assets of CCL, act  
20 as a prudent fiduciary and wind down and liquidate the assets of  
21 CCL. Consistent with these responsibilities, upon his  
22 appointment, the Receiver froze trading in all Public  
23 Investments, including the specific stocks and fixed-income  
24 investments that were in client accounts as of the Appointment  
25 Date.

26 As noted earlier, given the significant allegations of fraud  
27 that led to the Receiver's appointment and the need to conserve  
28 resources, he terminated the majority of CCL's employees.

1 Consequently, the Receiver could not actively manage the stock  
2 and fixed-income investments. Nor is it appropriate in the  
3 context of a federal receivership for the Receiver to attempt to  
4 provide that type of service.

5 Leaving the portfolio of stocks and fixed-income investments  
6 frozen, however, is not a long-term management strategy,  
7 particularly for investments in individual stocks. On the other  
8 hand, liquidating stock and bond holdings is expensive and may  
9 not be consistent with specific allocation strategies adopted by  
10 CCL on behalf of clients. Mindful of these facts, the Receiver  
11 contacted several major investment management firms in an effort  
12 to find a manager willing to promptly manage this large and  
13 diverse portfolio. Those firms included Goldman Sachs, Wells  
14 Capital, a division of Wells Fargo Bank, A.G. Edwards, and  
15 Merrill Lynch Investment Managers and its affiliates ("Merrill  
16 Lynch").

17 As a result of these contacts, and after careful  
18 consideration, the Receiver requested Court authority to provide  
19 client information on the stock and fixed-income portfolio  
20 exclusively to Merrill Lynch. The Receiver selected Merrill  
21 Lynch because it is well-qualified, large enough to effectively  
22 manage this volume of investments, and was the most responsive to  
23 the Receiver's desire for immediate action. Merrill Lynch was  
24 prepared to use its best efforts to promptly contact each CCL  
25 client with investments in the stocks and fixed-income portfolio.  
26 Merrill Lynch was also prepared and willing to offer the CCL  
27 clients its standard form of investment management agreement and  
28

1 to manage these accounts subject to executing new client  
2 contracts.

3 In return, Merrill Lynch agreed to compensate the  
4 receivership estate for each client employing the firm. If a  
5 client hires Merrill Lynch to render investment advisory  
6 services, Merrill Lynch will pay a fee equal to 15% of its annual  
7 advisory fee rate multiplied by the market value of the assets  
8 committed to management. One-half of such fee shall be payable  
9 after 90 days. No fee shall be payable if the account terminates  
10 before expiration of the first 90 days. One-half of such fee  
11 shall be payable after 180 days. The second half of the fee  
12 shall not be payable if the account terminates before expiration  
13 of the first 180 days. Merrill Lynch estimates that its annual  
14 management fee will typically be approximately 1% of the value  
15 under management.

16 On October 12, 2000, the Court approved the Merrill Lynch  
17 Agreement. That Agreement and the order approving it do not  
18 obligate clients to select Merrill Lynch as their investment  
19 manager and do not affect termination notices given by clients to  
20 the Receiver. On October 13, 2000, the Receiver sent a Court-  
21 approved letter to all clients who had not notified the Receiver  
22 of termination and identified a replacement manager, notifying  
23 them of Merrill Lynch's interest. As of that date, clients  
24 representing less than one-third of the total value of the stocks  
25 and fixed-income portfolio had submitted notices of termination  
26 and had identified a new investment manager for transfer. On  
27 October 18, 2000, the Receiver sent further notices to all  
28 clients of their rights to transfer the management of their

1 publicly-traded investments without further notice to the  
2 Receiver.

3 The Receiver anticipates that by the time of the first  
4 status conference, or shortly thereafter, management of all  
5 Public Investments will have been transferred to Merrill Lynch or  
6 another qualified advisor. The Receiver will therefore have  
7 satisfied his goal to facilitate an expeditious and convenient  
8 transfer of management to a competent financial manager and, to  
9 the extent possible, generate some revenue for the receivership  
10 estate to defray the administrative expenses of the receivership.

11 **VI. THE PRIVATE INVESTMENTS PORTFOLIO**

12 **A. Summary of Private Investments**

13 The Private Investments portfolio includes private debt  
14 investments, private equity investments and real estate equity  
15 interests. Below is a table detailing the amount invested and  
16 the CCL-estimated market value according to the CCL portfolio  
17 summary as of the Appointment Date.

18  
19 **Private Investments as of September 21, 2000**

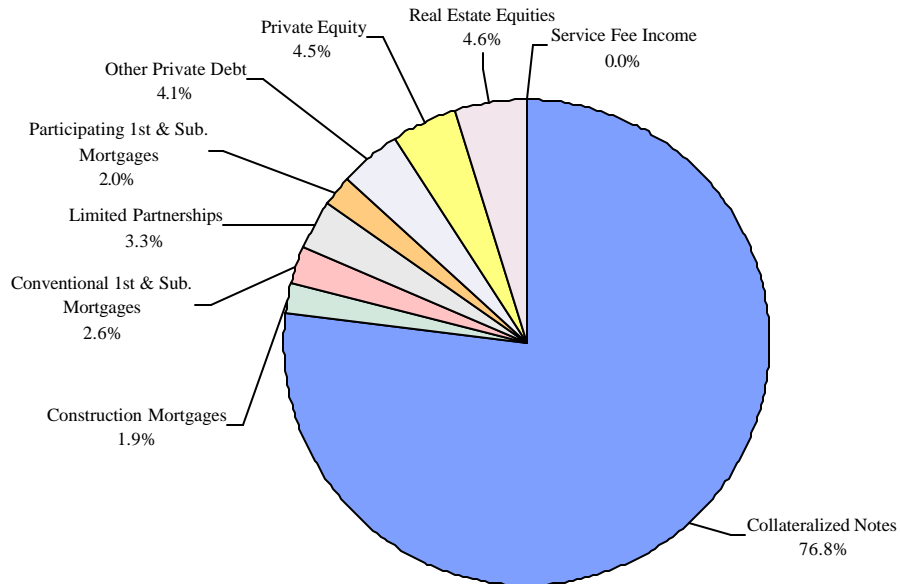
<u>Security Type</u>	<u>Cost</u>	<u>Claimed Market Value<sup>3</sup></u>
Private Debt Investments	\$387,726,015	\$404,903,607
Private Equity Interests	31,360,992	30,492,493
Real Estate Equity Investments	65,903,262	52,393,428
Total Private Investments portfolio	<u>\$484,990,270</u>	<u>\$487,789,527</u>

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22  
23 Following are two charts that depict the sources of Private  
24 Investment revenues for the year ended December 31, 1999, and for  
25 the eight months ended August 31, 2000. The charts indicate that  
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27  
28 <sup>3</sup> These amounts have not been subjected to testing or  
verification by an independent third party. The Receiver  
believes the market value is substantially less.

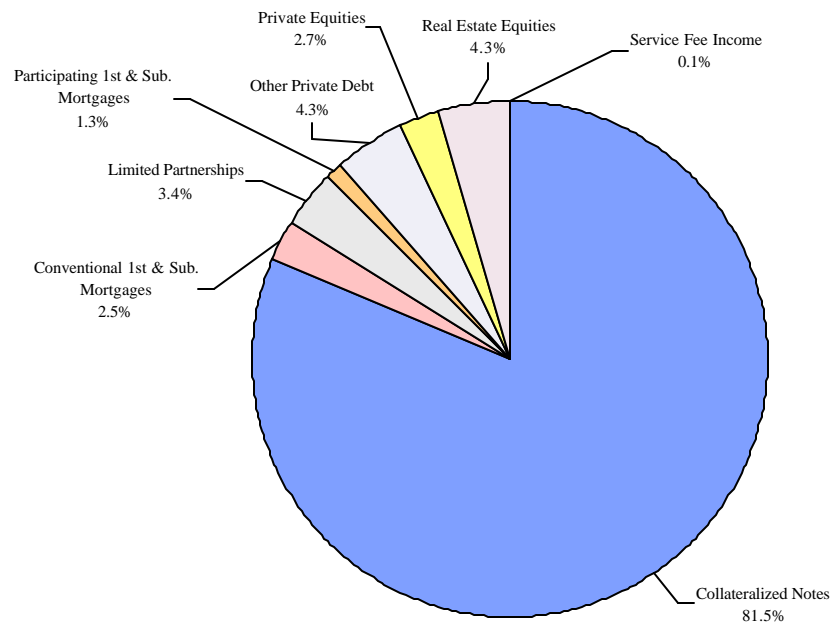
1 over 75% of the Private Investment revenues are derived from the  
2 non-real estate loan investment program marketed by CCL as  
3 "Insured and/or Collateralized Notes."

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5 **Sources of Private Revenue**  
6 **Year Ended December 31, 1999**



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## Sources of Private Revenue Eight Months Ended August 31, 2000



### B. Private Debt Investments

The private debt investments are investments in loans to an individual or company collateralized by real estate, stock, inventory, receivables or other assets. The private-debt investments are categorized into different types of loans: non-real estate secured loans and real estate secured loans.

The largest loan program was entitled the "Insured and/or Collateralized Note Program." Approximately \$157 million of the total outstanding principal under the Insured and/or Collateralized Note Program is attributable to the WCC/Sterling Notes, which are discussed in further detail below.

Approximately \$80 million of the total outstanding principal balance is comprised of a series of loans to Beacon, Brooks, and

1 Creditmart, entities controlled by Timothy Gamwell, which are  
2 also discussed in further detail below.

3 The remaining \$83 million of the Insured and/or  
4 Collateralized Note Program outstanding principal is comprised of  
5 13 loans to various other borrowers. For the most part, such  
6 loans call for monthly payments of interest only at prime plus 3%  
7 to 5%. Collateral is generally a lien on the borrowers' loan  
8 receivables or other contract rights. In certain instances, real  
9 estate is pledged as additional collateral. The current value  
10 of the non-real estate collateral is not yet known, but is  
11 suspect. Certain of these loans are personally guaranteed by  
12 principals of the borrowers. The net worth of the guarantors or  
13 their ability to personally repay the debt should the borrowers  
14 default and the collateral prove to be of insufficient value is  
15 also not yet known.

16 As of the Appointment Date, 13 private-debt investments were  
17 in default, totaling \$13,478,174 in outstanding principal. As of  
18 the Appointment Date, certain litigation and other foreclosure  
19 efforts had already been commenced on behalf of CCL. Where the  
20 loans have recently fallen into default, the Receiver has served  
21 notices of default to the borrowers. Although many borrowers are  
22 current on their monthly interest payments, there are serious  
23 questions whether several large borrowers will ever be able to  
24 pay off the principal balance.

### 25 **C. Private Equity Investments**

26 The private equity investments are direct investments in the  
27 ownership of companies. Of the 13 private equity investments  
28 included in the portfolio balance as of the Appointment Date,

1 four resulted from the conversion of nonperforming loans (a total  
2 conversion of \$1,352,205 in outstanding principal), and the  
3 remaining nine were acquired as original equity investments.  
4 Ninety-one percent of private equity investments are in A-Fem  
5 (discussed in more detail below), Pacific Capital, LLC and  
6 American Physicians Network.

#### 7 **D. Real Estate Interests**

8 The major private real estate equity interests include  
9 Legends Condominiums, AT&T Cellular One Building and the Smiths  
10 Consolidated Real Estate Holdings (SCREH) buildings. Legends and  
11 SCREH resulted from postdefault enforcement of a loan (Legends)  
12 and restructuring of a nonperforming loan (SCREH).

#### 13 **E. History of Operation - Private Debt Investments**

##### 14 **1. Lack of Underwriting**

15 CCL represented that it would perform an extensive  
16 evaluation of the borrower before underwriting a loan. The  
17 evaluation was supposed to include assessing the economics of the  
18 borrower's business, analyzing the projected cash flow, assessing  
19 the borrower's repayment plans and analyzing the credit reports,  
20 collateral, tax returns and financial statements of the borrower.  
21 The evaluation process was supposed to end in a review of the  
22 investment proposal by a Loan Committee comprised of CCL's  
23 professionals including portfolio managers, investment analysts,  
24 loan administrators and servicing individuals. The Loan  
25 Committee was supposed to ensure that all aspects of the  
26 investment were thoroughly analyzed and that client funds were  
27 put to the highest and best use within the client's investment  
28 guidelines.

1 The Receiver's review of CCL's loan files and his interviews  
2 with employees did not substantiate that the promised  
3 underwriting process took place. CCL employees were not aware of  
4 any specific credit or borrower analyses prepared or maintained  
5 by the investment analysts. Additionally, according to both the  
6 Uniform Application for Investment Adviser Registration dated  
7 March 30, 2000, and discussions with CCL staff, Jeffrey Grayson  
8 and Barclay Grayson were the only two voting members of the  
9 Private Investment Committee, as opposed to the "10+ investment  
10 professionals" described as making up the asset-specific  
11 investment committees on CCL's promotional web site.

12 Additionally, the Receiver's initial review has revealed  
13 that most of the loans are to high-risk borrowers. These  
14 borrowers are either new companies with no operating or financial  
15 history to support loan repayment requirements, or are involved  
16 in economically-risky industries such as sub-prime auto loans,  
17 South American wood products and travel agencies.

## 18 2. The Insured and/or Collateralized Note Program

19 The Insured and/or Collateralized Note Program represented  
20 82% of the total private debt investments outstanding. These  
21 loans were described by CCL as loans made to a borrower secured  
22 by an assignment of the borrower's loan receivables or contract  
23 rights. The loans were to have typical maturities of between two  
24 to five years and provide a return based upon an interest rate  
25 spread above the prime interest rate. The loans were represented  
26 to provide high current income combined with preservation of  
27 capital. These loans either required a holdback of loan proceeds  
28 equal to 15% of the loan balance, called "cash collateral,"

1 marketable securities or cash equivalent collateral or required  
2 credit insurance. All of the outstanding Insured and/or  
3 Collateralized Notes are or were collateralized by cash  
4 collateral and none by credit insurance. CCL employees could  
5 identify only one past loan which involved credit insurance.  
6 However, correspondence received by the Receiver indicates that  
7 certain clients understood these loans to be insured by third-  
8 party insurance companies.

### 9 **3. Defaults**

10 Of the total private debt investments, there are currently  
11 13 loans totaling \$13,478,174 that CCL has identified to be in  
12 monetary default as of the Appointment Date. Loans in monetary  
13 default were defined by CCL as those loans on which the payments  
14 of interest and/or principal have not been made. As described in  
15 detail below, the Restructured WCC/Sterling loans and Brooks and  
16 Beacon loans appear to be impaired as to value and CCL waived  
17 certain nonperformance by WCC and Sterling, but no default was  
18 declared.

19 The Receiver's initial review has identified many other  
20 loans in addition to those in monetary default that may be  
21 impaired as to value. For example, many loans were restructured  
22 to require payments only equal to cash flow, thus precluding a  
23 payment default. Other loans involved additional funding  
24 advances to permit the borrower to make required payments. Some  
25 loans involved postponed maturity dates or postponed principal  
26 payments. Additionally, the Receiver has identified several  
27 instances similar to the circular nature of the  
28 WCC/Sterling/Brooks/Beacon arrangement, described in detail

1 below, in which funding from new loans to an affiliate of the  
2 borrower becomes the source of payments on an existing loan.

#### 3 4. Areas of Concern

4 The Receiver's initial review of the private debt  
5 investments identify serious issues including: (i) the lack of  
6 adequate documentation and/or tracking of the loan status;  
7 (ii) the infrequent placing of loans in default/foreclosure;  
8 (iii) the lack of diversification; (iv) the number of  
9 interrelationships between loans and borrowers; (v) the  
10 antiquated database system used to maintain the loan information;  
11 and (vi) the structure of management fees and the lack of  
12 accurate appraisals for certain loans.

13 Many loan files do not have any recent financial statements  
14 and are not in compliance with the respective loan agreements  
15 regarding the production of monthly or quarterly financial  
16 statements. Additionally, the payment of property taxes was not  
17 being tracked by CCL and, as a result, tax liens may exist on  
18 real property collateral.

19 CCL infrequently placed a loan in default or pursued  
20 foreclosure. Many loans were restructured/modified numerous  
21 times to extend maturity dates, decrease monthly payments, or  
22 capitalize accrued interest to prevent a default. Once a loan  
23 was placed in foreclosure/default by CCL, ownership was assigned  
24 to 520 SW Yamhill LLC to avoid negative publicity for CCL. As of  
25 the Appointment Date, four loans were assigned to 520 SW Yamhill  
26 LLC, although those loans continued to be reported by CCL as part  
27 of the CCL loan portfolio.

1 The loans included in the Insured and/or Collateralized Note  
2 Program were not significantly diversified. Most of the 238  
3 loans in the Insured and/or Collateralized Note Program involve  
4 only a few borrowers. The major borrowers are WCC progeny:  
5 including Sterling (\$156,985,137), Beacon (\$40,328,494), Brooks  
6 (\$31,177,274) and Creditmart (\$8,328,749). Together these  
7 borrowers represent approximately 74% of the total amount  
8 (\$319,453,710) of the Insured and/or Collateralized Note Program  
9 and 61% of the total private debt investments.

10 As demonstrated by the Creditmart, Brooks and Beacon loan  
11 relationship described below, many loans and borrowers in the  
12 loan portfolio are interrelated through common ownership. There  
13 are also many examples within the loan portfolio of the same  
14 guarantors and owners being involved in numerous loans for  
15 different borrowing entities, including personal loans to the  
16 owners and guarantors and loans to affiliated entities.

17 During the period of recent scrutiny by the SEC, CCL reduced  
18 its management fee on certain questionable loans. On July 1,  
19 2000, CCL reduced the management fee from 3% to 1.5% on the  
20 Sterling loans, and then again on September 20, 2000, the day  
21 before the Appointment Date, reduced the fee from 1.5% to 0%.  
22 CCL also reduced the management fee on the Bayside loan on that  
23 same date from 3% to 0%. The reduction in management fees  
24 appears to correspond to the questionable value of the loans and  
25 collateral.

26 Significant inadequacies were identified within CCL's loan  
27 administration system. Little, if any, security was programmed  
28 into the computer system. The computer files were not password

1 protected, and the integrity of the data was not maintained. It  
2 does not appear to be possible to determine whether files/records  
3 were edited or deleted without extensive manual checking against  
4 hard copy records. Furthermore, the system does not appear to  
5 track the identity of users updating or deleting a record.  
6 According to CCL's programmer, the machines were left on for days  
7 on end, and anyone who had access to an on-line terminal could  
8 make a change. Finally, the age and difficulties associated with  
9 FoxPro 2.0, an old DOS-based application, make the interface  
10 awkward for extracting information and requires someone with a  
11 knowledge of the application, query language, and obtuse  
12 programming code. The application appears to have many  
13 "patches," and several of the reports would not run to  
14 completion. The CCL programmer had presented a proposal to  
15 rewrite the application during the first quarter of 2000, but the  
16 proposal was not accepted.

17 **5. WCC and Its Progeny, The Major Private Debt**  
18 **Problem**

19 WCC is a Nevada corporation originally formed in 1989.  
20 Prior to the last quarter of 1996, WCC was in the business of  
21 acquiring and servicing performing and nonperforming loan  
22 portfolios and mortgage-backed securities. Funding for  
23 acquisitions of loan portfolio and mortgage-backed securities was  
24 historically provided by third-party investors who held  
25 participating interests in cash flows from specified portfolios  
26 and securities or who extended credit to WCC with specified  
27 portfolios and securities pledged as collateral.

1 a) The Master Loan Agreement and Amendments

2 On or about July 6, 1995, CCL entered into a Master Loan and  
3 Security Agreement-1995-1 (the "Master Agreement") with WCC.<sup>4</sup>  
4 Pursuant to the Master Agreement, CCL agreed to make loans to WCC  
5 in an amount equal to the lesser of: (i) the sum of 90% of the  
6 net present value of pledged servicing rights plus 85% of certain  
7 eligible loan receivables plus the face amount of certificates of  
8 deposit held by CCL for the benefit of WCC; or (ii) \$10,527,500  
9 (the "Maximum Amount"). In determining the net present value of  
10 servicing rights, the Master Agreement required the use of a  
11 fixed discount rate of 9%. Advances under the Master Agreement  
12 were originally at an interest rate of prime plus 4% and were  
13 made in a series of 11 separate loans, each individually  
14 documented and secured by discrete loan pools and servicing  
15 rights. Wiederhorn and Mendelsohn personally guaranteed the  
16 loans.

17 Beginning on July 21, 1995, only days following the Master  
18 Agreement's execution, WCC and CCL entered into the first of a  
19 series of modifications to the Master Agreement as follows:  
20  
21  
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24 \_\_\_\_\_  
25 <sup>4</sup> Prior to entering into the Master Agreement, CCL had already  
26 made several loans to WCC and its affiliate, Portland Servicing  
27 Corporation ("PSC"). As of the Appointment Date, only one loan  
28 to WCC in the original principal amount of \$4,169,763 and one  
loan to PSC in the original principal amount of \$3,500,000  
remain outstanding. For purposes of discussion, the Receiver  
has included these loans together with loans made under the  
Master Agreement.

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Date	Agreement	Modifications
July 21, 1995	First Amendment to Security Agreement-1995-1	Increased the Maximum Amount to \$24,300,000.
October 1, 1995	Second Amendment to Master Loan and Security Agreement-1995-1	Increased the Maximum Amount to \$100,000,000.
December 26, 1995	Third Amendment to Master Loan and Security Agreement-1995-1	Clarified WCC's obligation to post as collateral for each loan a certificate of deposit in a principal amount not less than 15% of the outstanding principal balance of the Loans.
April 11, 1996	Fourth Amendment to Restated and Amended Master Loan and Security Agreement-1995-1	Increased the Maximum Amount to \$150,000,000; Changed the formula for determining the net present value of servicing rights. Discount rate was reduced to the prime rate.
May 23, 1996	Fifth Amendment to Restated and Amended Master Loan and Security Agreement-1995-1	Extended the maturity date for the loans.
March 31, 1997	Sixth Amendment to Master Loan and Security Agreement-1995-1	Increased ability to borrow against servicing rights to 100% of present value of contracts and clarified that loans could be secured by servicing rights only.
April 2, 1997	Letter dated April 2, 1997 countersigned by WCC	Clarified outstanding disputes between the parties.
December 30, 1997	Letter dated December 30, 1997 countersigned by WCC	Established that CCL is not required to make loans to extent borrowing base attributable to servicing contracts is less than \$116,500,000.

Date	Agreement	Modifications
May 7, 1998	Letter dated May 7, 1998 countersigned by WCC	Established that CCL is not required to make loans to extent borrowing base attributable to servicing contracts is less than \$129,000,000.
October 15, 1998	Seventh Amendment to Master Loan and Security Agreement-1995-1 (the "Seventh Amendment")	Released \$19,300,000 in cash collateral held by Bear Stearns & Co. to pay certain obligations of WCC and First Bank of Beverly Hills. Wiederhorn, Mendelsohn and WFSG to pledge all of their respective stock in WFSG and Wilshire Real Estate Investment Trust, Inc. ("WREIT") to secure the loan. WCC pledged a \$12.3 million promissory note made by Wilshire Real Estate Partnership, L.P. and a \$2,000,000 promissory note made by Wilshire Funding Corporation to secure the loan. WCC agreed to reimburse the cash collateral on or before December 31, 1998.
October 16, 1998	Eighth Amendment to Master Loan and Security Agreement-1995-1 (the "Eighth Amendment")	Agreed to make an additional loan of \$6,000,000 in exchange for Wiederhorn's and Mendelsohn's pledge of their stock in WCC.

A schedule of each of the loans made pursuant to the Master Agreement, and amendments, is attached hereto as Exhibit "A." As of October 23, 1998, WCC owed CCL approximately \$159,000,000 under the terms of the Master Agreement. Moreover, as of this date, CCL's loans to WCC accounted for roughly 68% of the entire Insured and/or Collateralized Note Program.

1 Investing such a large percentage of the total Insured  
2 and/or Collateralized Note Program in WCC was risky. The  
3 Receiver found no evidence that CCL considered the risk caused by  
4 this lack of diversification. CCL's files contained a  
5 rationalization of this approach by asserting that each  
6 individual loan made under the Master Agreement was diverse in  
7 and of itself since it was separately documented and had separate  
8 loan pools and/or servicing rights serving as collateral.

9 **b) Due Diligence Issues**

10 The Receiver's review of the WCC files revealed limited  
11 financial background information concerning WCC's financial  
12 history, including WCC's audited financial statements prepared by  
13 Deloitte & Touche LLP. However, the Receiver has been unable to  
14 locate files demonstrating that CCL engaged in any significant  
15 underwriting analysis prior to entering into the Master  
16 Agreement. More significantly, there appears to be no CCL due  
17 diligence prior to amending the Master Agreement to dramatically  
18 increase the Maximum Amount by 1,400% from roughly \$10,000,000 to  
19 \$150,000,000 or prior to funding new loans under the Master  
20 Agreement secured exclusively by servicing rights as collateral.

21 **c) Collateral Valuation Questions**

22 Under the terms of the Master Agreement, WCC was required to  
23 provide to CCL on a quarterly basis independent appraisals  
24 verifying the value of CCL's collateral. These appraisals were  
25 initially provided by Consilium and later by Moss Adams LLP,  
26 CCL's own auditors. For reasons not contained in the files or  
27 known to remaining employees, the Master Agreement dictated that  
28 the valuations be performed using either a fixed 9% discount rate

1 or using the prime rate as the discount rate. Given that the  
2 resulting value of the collateral was greatly dependent on the  
3 discount rate used, the use of a mandated low discount rate may  
4 have led to a significant overvaluation of the servicing rights  
5 collateral.

6 **d) Wilshire's First Restructure**

7 At the time CCL originally entered into the Master  
8 Agreement, WCC was in the business of acquiring and servicing  
9 loan portfolios and mortgage-backed securities. As originally  
10 contemplated, CCL, in making loans to WCC, would take as  
11 collateral all of WCC's receivable rights in the loan pools  
12 acquired within a portfolio, as well as all servicing rights  
13 related thereto. This relationship, however, changed sometime  
14 prior to 1997 when CCL began to make loans to WCC under the  
15 Master Agreement secured exclusively by WCC's pledge of  
16 servicing rights for loan portfolios. This switch was apparently  
17 precipitated by the reorganization of WCC in late 1996.

18 Because of an alleged need for additional capital,  
19 Weiderhorn and Mendelsohn, the principals of WCC, decided to take  
20 one of their companies, WFSG, public through an initial public  
21 offering. Following the initial public offering, WFSG and its  
22 subsidiaries would acquire loan portfolios and mortgage-backed  
23 securities instead of WCC. WCC, on the other hand, would only  
24 service loans for WFSG. It would no longer directly purchase any  
25 loan portfolios.

26 In accordance with this strategy, in the fourth quarter of  
27 1996, WFSG underwent an initial public offering and formed new  
28 subsidiaries to undertake the loan acquisition and servicing

1 business then conducted by WCC and its affiliates. Shortly  
2 before the initial public offering, WCC and WFSG entered into  
3 that certain Loan Servicing Agreement dated November 15, 1996  
4 ("Loan Servicing Agreement"). Under the terms of the Loan  
5 Servicing Agreement, WFSG agreed that WCC would service loans  
6 owned by WFSG and its affiliates. Importantly, the Loan  
7 Servicing Agreement contained no restriction on WFSG selling or  
8 otherwise transferring loan pools to third parties, who could then  
9 use someone other than WCC to service the loans. WFSG also could  
10 transfer the servicing rights from WCC to its own wholly-owned  
11 affiliate, WSC, within two to three years following the execution  
12 of the Loan Servicing Agreement.

13 As originally drafted, the Loan Servicing Agreement had no  
14 provision for payment to WCC following the transfer of servicing  
15 rights to WSC. On or about October 22, 1997, WFSG and WCC  
16 entered into an Amended and Restated Loan Servicing Agreement  
17 (the "Amended Loan Servicing Agreement") that provided in the  
18 event servicing rights were transferred to WSC, WCC was  
19 nevertheless entitled to a share of the servicing fee, following  
20 the deduction of WSC's average cost of servicing the loans, until  
21 the termination of the Loan Servicing Agreement (as early as five  
22 years following the transfer of loans to WSC).

23 During the process of the restructuring, WCC made CCL aware  
24 of its intended restructure and apparently requested CCL to  
25 continue to make loans to WCC following the restructure. **WCC**  
26 **"threatened" to pay off its outstanding loans under the Master**  
27 **Agreement unless CCL agreed to continue to fund new loans**  
28 **following the restructure and accept as collateral WCC's pledge**

1 of its remaining servicing rights. However, because WFSG could  
2 terminate WCC's servicing operation or sell the servicing rights,  
3 WCC's servicing rights were largely compromised following the WCC  
4 restructure.

5 The Receiver has found no evidence of serious due diligence  
6 or analysis by CCL of the impacts of WCC's 1996 restructure upon  
7 CCL's collateral value or loan repayment risk. As indicated on  
8 Exhibit "A," following the restructure, CCL lent over \$81,000,000  
9 in new additional loans to WCC secured by WCC's servicing rights.

10 e) The Second Wilshire Restructure

11 Following its initial public offering, WFSG used the funds  
12 raised to significantly expand its acquisition of loan pools and  
13 mortgage-backed securities. Reportedly, as of October 1998, WFSG  
14 was indebted to its bondholders in the principal amount of  
15 approximately \$184.2 million.

16 According to CCL files, adverse interest rate fluctuations  
17 in the fourth quarter of 1998 caused WFSG to liquidate a  
18 substantial portion of its loan portfolios to pay capital calls  
19 imposed by its lenders. In addition, because of WFSG's practice  
20 of using certain funds collected on account of loans it serviced  
21 for its wholly owned banking subsidiary, First Bank of Beverly  
22 Hills, F.S.B ("First Bank"), WFSG was forced by the Office of  
23 Thrift Supervision to immediately return approximately  
24 \$15 million in funds to First Bank. WFSG and WCC came to CCL for  
25 assistance with this alleged financial crisis.

26 For reasons not contained in CCL's files, CCL loaned WCC an  
27 additional \$25.3 million to cover margin calls and monies owed to  
28 First Bank. These new loans were evidenced by the Seventh

1 Amendment dated October 15, 1998, wherein CCL agreed to release  
2 to WCC and WFSG \$19.3 million of CCL's cash collateral for  
3 existing CCL loans to WCC. Soon after, on October 16, 1998, CCL  
4 agreed to an Eighth Amendment to loan WCC an additional  
5 \$6 million. As a result of these transactions, CCL released most  
6 of the cash collateral it held to secure WCC's performance under  
7 the Master Agreement and increased WCC's debt by \$25 million.

8 Despite the receipt of over \$25 million from CCL, WFSG's  
9 financial condition continued to decline. According to CCL, by  
10 November of 1998, WFSG's public bondholders threatened to  
11 immediately shut down and liquidate WFSG's operations unless  
12 Wiederhorn and Mendelsohn agreed to turn over the company. By  
13 December of 1998, WFSG, certain of its affiliates, CCL, and  
14 WFSG's public bondholders agreed to a new comprehensive  
15 reorganization of WFSG, WCC, and affiliated companies.

16 A restructure of the WCC loans was to be accomplished in  
17 conjunction with a prepackaged bankruptcy reorganization filing  
18 by WFSG that would exchange the bond debt for 99% of the stock in  
19 WFSG.

20 i) Step One

21 CCL's borrowers, PSC and WCC, merged with WCC becoming the  
22 surviving entity. Wiederhorn and Mendelsohn, the sole  
23 shareholders of PSC and WCC, transferred all of their existing  
24 shares in the surviving WCC to W-M LLC, an Oregon limited  
25 liability company ("W-M LLC"), of which Mendelsohn and Wiederhorn  
26 were the sole members.

27 Contemporaneously, CCL formed a new wholly-owned subsidiary,  
28 CWH Mergco Corp., an Oregon corporation ("CWH Mergco Parent"),

1 which in turn formed its own wholly-owned subsidiary, CWH Mergco  
2 Sub Corp., a Nevada corporation ("CWH Mergco Sub"). CWH Mergco  
3 Sub thereafter merged with WCC, with WCC becoming the surviving  
4 entity: the name of the corporation was changed to Capital  
5 Wilshire Holdings, Inc., a Nevada corporation ("CWH") following  
6 the merger. As a result of the merger, CCL became the owner of  
7 99% of the issued and outstanding shares in CWH Mergco Parent,  
8 the 100% owner of CWH, and W-M LLC became the owner of the  
9 remaining 1%. **Notably, as a result of these transactions, CCL**  
10 **became the 99% shareholder of the 100% owner of CCL's borrower,**  
11 **now known as CWH. No change in collateral had yet occurred.**  
12 Charts graphically depicting the corporate structure of CCL, WCC  
13 and WFSG prior to these transactions as well as depicting step  
14 one of the restructure are attached hereto as Exhibits "B" and  
15 "C," respectively.

16 **ii) Step Two**

17 The restructure continued, and the collateral for CCL's  
18 loans was diminished.

19 CCL released its lien on the existing collateral now held by  
20 CWH (i.e., the servicing rights pledged to CCL under the terms of  
21 the Master Agreement) and released Wiederhorn and Mendelsohn from  
22 their guarantees. CWH and WCC Inc., a newly-formed Nevada  
23 corporation ("New Servicer"), entered into an agreement whereby  
24 CWH transferred to New Servicer all of its assets and  
25 liabilities, with the exception of its obligations to CCL owed  
26 under the Master Agreement. The transfer included the former  
27 collateral, that is, the servicing rights under the Loan  
28 Servicing Agreement. New Servicer granted to CWH (CCL's new

1 borrower) 1,000 shares of Class B Non-Voting Stock in New  
2 Servicer (the "Class B Stock"). The Class B Stock was entitled  
3 to participate pro rata with other common stock (Class A) in  
4 dividends and was entitled to a minimum liquidation guarantee of  
5 \$19.3 million. The Class B Stock held by CWH represented 49.99%  
6 of the equity interests in New Servicer. Moreover, the Class B  
7 Stock was convertible into such number of Class A Stock as would  
8 represent 49.99 % of the outstanding shares of Class A Stock in  
9 New Servicer. Finally, pursuant to certain exchange rights, the  
10 Class B Stock was convertible into up to 42% of the stock of WFSG  
11 no earlier than June 2001.

12 WFSG contributed to New Servicer all of its outstanding  
13 shares of WSC stock, in exchange for 900 shares of Class A Stock  
14 in New Servicer. WFSG delivered to CCL a \$350,000 promissory  
15 note. WFSG also delivered to CCL a \$2,200,000 promissory note.  
16 Wiederhorn and Mendelsohn each personally guaranteed the  
17 \$2,200,000 promissory note delivered by WFSG to CCL. CWH then  
18 pledged its Class B Stock in New Servicer to CCL as collateral to  
19 secure the outstanding indebtedness to CCL of \$160 million under  
20 the Master Agreement. WFSG also executed a liquidation bond in  
21 favor of CCL that guaranteed that CCL would be paid at least  
22 \$19.3 million upon the liquidation of New Servicer. The  
23 liquidation bond was to be secured by certain assets of WFSG.  
24 CCL then also released Wiederhorn and Mendelsohn from liability  
25 for any claims not covered by directors and officers liability  
26 insurance. The WCC loan restructure was now complete.<sup>5</sup> A chart

27 \_\_\_\_\_  
28 <sup>5</sup> The WCC loans as restructured shall be referred to as the  
"Restructured WCC loans."

1 graphically depicting step 2 of the restructure is attached  
2 hereto as Exhibit "D."

3 The foregoing two steps were consummated contemporaneously  
4 with the effective date of WFSG's prepackaged plan of  
5 reorganization.<sup>6</sup>

6 **iii) Restructure Impact**

7 The net effect of the restructure transaction on CCL loans  
8 to WCC was to change the nature of CCL's collateral and borrower;  
9 CCL's loans totalling \$160 million became secured only by  
10 (i) CWH's Class B stock in the New Servicer; and (ii) the  
11 liquidation bond. Moreover, CWH, the new borrower, was owned by  
12 an entity that CCL owned 99% of, and was no longer an operating  
13 company with assets or cash flow. Accordingly, the transaction  
14 essentially converted CCL's loan collateral into an equity  
15 interest in New Servicer and its borrower into a company with no  
16 demonstrated ability to repay principal.

17 The Receiver can find no legitimate business explanation for  
18 the extraordinarily complex form of the restructure. The form of  
19 the restructure did not reveal to CCL clients that the WCC loans  
20 had little repayment prospects and the value of the collateral  
21 was severely diminished.

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27 <sup>6</sup> WFSG filed a voluntary petition for relief under chapter 11 of  
28 the Bankruptcy Code in the United States Bankruptcy Court for  
the District of Delaware on March 3, 1999. WFSG confirmed its  
plan of reorganization on April 12, 1999, and the plan became  
effective on June 10, 1999.



1 Sterling intended to obtain funding for the acquisition from  
2 Oxbow Fund I.

3       Although Sterling had agreed to purchase the Restructured  
4 WCC loans, no purchase payments were due until March 25, 1999.  
5 WCC made its last payment of interest in November 1998 and, under  
6 the terms of the restructuring agreement, CCL had agreed to toll  
7 WCC's obligations through the closing of the restructuring.  
8 Thus, the WCC loans should have gone into payment default no  
9 later than December 1998. In order to avoid declaring a payment  
10 default, CCL used the remaining cash collateral securing such  
11 loans to make the December 1998, and January and February 1999  
12 interest payments due on the WCC loans.

13       The March and April 1999 interest payments under the WCC  
14 loans should have been covered by Sterling's \$2,500,000 monthly  
15 payments due under the terms of the Purchase Agreement on  
16 March 25, 1999. Sterling, however, never made these payments and  
17 once again CCL used remaining cash collateral securing the WCC  
18 loans to make the March 1999 interest payment. The same  
19 circumstances occurred for the April 1999 payment due under the  
20 WCC loans.<sup>8</sup>

21       On May 25, 1999, CCL and Sterling entered into a First  
22 Amendment to Master Loan Purchase Agreement (the "First  
23

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24 <sup>8</sup> The current balance of the cash collateral account maintained  
25 at First Security Bank relating to the Restructured WCC Loans  
26 is now \$161,390 as of September 30, 2000. Most of the original  
27 cash collateral was drained through releasing \$19,282,070 to  
28 WCC in November 1998, funding \$7,989,844 in interest and  
principal payments on the Restructured WCC loans from December  
1998 through April 1999, and funding \$1,700,099 in legal and  
consulting expenses incurred from December 1998 through  
September 2000.

1 Amendment"). The First Amendment reduced Sterling's monthly  
2 payment obligation by almost \$1 million to \$1,533,333.33. CCL  
3 also waived any rights to recover the March and April 1999  
4 payments. Sterling, through Oxbow, paid in April by three checks  
5 the amount of \$1,500,000, which was applied to replenish the cash  
6 collateral account.<sup>9</sup>

7 Following the April payments, Sterling reportedly told CCL  
8 that it would not fund any more payments under the Purchase  
9 Agreement. Thereafter, the parties entered into yet another  
10 amendment, the Second Amendment to Master Loan Purchase Agreement  
11 dated June 7, 1999 (the "Second Amendment"). Under the terms of  
12 the Second Amendment, CCL agreed to allow Sterling to assign  
13 66.66% of its interest in the Purchase Agreement to Brooks.  
14 Brooks would thereafter be responsible to fund approximately  
15 \$1,000,000 per month to CCL on account of the Restructured WCC  
16 loans.

17 **g) Brooks and Beacon Acquisition of the**  
18 **Restructured WCC Loans**

19 Brooks was formed to acquire and service (through servicing  
20 agreements with other companies) portfolios of auto loans and  
21  
22  
23  
24  
25

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26 <sup>9</sup> The Receiver is presently investigating Oxbow Partner's source  
27 of funding for the April payments. Specifically, CCL made an  
28 additional advance in the amount of \$2,000,000 to Oxbow  
Partners under the CJM loan in April 1999, which may have been  
the source of the payment.

1 furniture/household inventory receivables.<sup>10</sup> Brooks entered into  
2 a Master Loan and Security Agreement with CCL on June 4, 1999,  
3 providing for a loan of up to \$50 million. The proceeds of the  
4 loan were to be used to purchase or payoff existing first lien  
5 interests in approved credit card, auto loan and  
6 furniture/household inventory receivables, as well as to acquire  
7 a specific portion up to \$108 million of Sterling's position in  
8 the Restructured WCC Loans. Brooks was to be advanced 90% of the  
9 computed "value" of the pools of installment contracts. The  
10 value was generally calculated as the present value of the total  
11 expected cash flow from the loan pools. The interest rate  
12 charged on the Brooks loans was prime plus 3%.

13 CCL made loans to Brooks totaling \$38.1 million between June  
14 1999 and December 1999, explained in detail at Exhibit "E." Some  
15 of the proceeds of the advances were used to acquire pools of  
16 sub-prime auto loans and furniture/household inventory  
17 receivables (\$20.0 million). The remaining proceeds were  
18 distributed as follows:

- 19 • to Brooks (\$4.9 million);

---

20  
21 <sup>10</sup> Creditmart was the predecessor to Brooks. Creditmart entered  
22 into a Master Loan and Security Agreement with CCL on May 15,  
23 1998 providing for a loan of up to \$50 million. From May 1998  
24 through March 1999, CCL loaned Creditmart \$17,246,000, of which  
25 \$8,328,749 was outstanding as of September 21, 2000. The  
26 proceeds of the loan were used to purchase pools of auto loan  
27 receivables, which secured the loan along with a pledge of  
28 stock of FAFCO. Creditmart was to be advanced 80% of the  
computed "value" of the pools of installment contracts, less  
than the "normal" 90% advance rate subsequently provided to  
Brooks and Beacon. The value was calculated as the net present  
value expected cash flow over the life of the auto loans. The  
interest rate charged on the Creditmart loans was prime plus  
3.75%. This Master Loan and Security Agreement was terminated  
in June 1999 as Brooks entered into its loan agreement with  
CCL.

- 1 • to CCL in order to acquire a portion of Sterling's
- 2 purchase of the Restructured WCC loans (\$7.4 million),
- 3 which funds were described by CCL to client as interest
- 4 payments on the sold Restructured WCC loans;
- 5 • to Oxbow Fund B (\$4.5 million) and to First Security Bank
- 6 (\$1.2 million) to fund the 15% cash collateral on the new
- 7 Brooks loan; and
- 8 • to other parties for transaction costs (\$.1 million).

9 The Brooks loans are secured by first priority liens in the  
10 auto and inventory receivable pools purchased with the loan  
11 proceeds and by a Put and Call Agreement dated July 7, 1999,  
12 between Brooks and VIS. The Put and Call Agreement provides that  
13 Brooks may, upon default on the Master Loan Agreement with CCL,  
14 require VIS to purchase the entire membership interests of Brooks  
15 for \$4.5 million. In an amendment to the Put and Call Agreement  
16 dated October 1, 1999, Broward Truck & Equipment Co., Inc. and  
17 Palm Beach Trucking Co., Inc. joined VIS as parties and the put  
18 price of Brooks' membership interests was revised to  
19 \$8.7 million. Broward Truck & Equipment Co., Inc. and Palm Beach  
20 Truck Co., Inc. are commercial truck dealerships owned by John R.  
21 Scopetta and Robert Dollar that obtained a \$1.7 million revolving  
22 line of credit on December 31, 1999, from Beacon in relation to  
23 the inclusion of the dealerships as parties to the Put and Call  
24 Agreement securing the Brooks loans.

25 Once the maximum borrowing amount by Brooks was reached,  
26 Beacon entered into a similar Master Loan and Security Agreement  
27 with CCL on January 3, 2000. CCL agreed to a loan to Beacon up  
28 to \$50 million. The proceeds of the loan were to be used to

1 purchase or pay off existing first lien interests in approved  
2 financing agreements, notes, loans or lease receivables. This  
3 Master Loan and Security Agreement was amended on February 9,  
4 2000, to express that Beacon had no obligation to purchase or  
5 acquire any interest in the Restructured WCC loans and that a  
6 decision to purchase such an interest was not a condition to CCL  
7 making any advances to Beacon under the Master Loan and Security  
8 Agreement.

9 CCL made advances to Beacon totaling \$43.6 million between  
10 January 2000 and August 2000, explained in detail at Exhibit "E,"  
11 and as of the Appointment Date, was preparing to fund an  
12 additional \$1,020,000. The proceeds of the advances were  
13 distributed as follows:

- 14 • to certain bank accounts for FAFCO and other parties in  
15 order to acquire sub-prime auto, furniture and credit card  
16 loans (\$23.7 million);
- 17 • to Beacon (\$3.3 million);
- 18 • to CCL in order to acquire a portion of Sterling's  
19 interest in the Restructured WCC loans and as a holdback  
20 (\$10.2 million) which funds were described by CCL to  
21 clients as the payment of interest on those same loans;
- 22 • to Oxbow Fund B (\$5.0 million) and to First Security Bank  
23 (\$1.3 million) to fund the 15% cash collateral  
24 requirement; and
- 25 • to other parties for transaction costs (\$.1 million).

26 These loans are secured by first priority liens in the auto,  
27 credit card and inventory receivable pools purchased with the  
28 loan proceeds and by a Put and Call Agreement dated June 15,

1 2000, between Beacon and PNB Holdings, Inc., a real estate  
2 company. The PNB Put and Call Agreement provides that Beacon  
3 may, upon default on the Master Loan Agreement with CCL, require  
4 PNB to purchase the entire membership interests of Beacon for  
5 \$2.8 million.

6 As of September 21, 2000, the outstanding amounts of these  
7 related loans and their respective cash collateral are as  
8 follows:

9	<u>Loans</u>	<u>Balance</u>	<u>Collateral</u>
10	Sterling/Restructured WCC	\$156,985,137	\$161,390
11			at First Security Bank;
12			and Restructured WCC loan
			collateral
13	Brooks	31,177,274	\$1,322,130
14			at First Security Bank;
15			\$4,483,700
			in Oxbow Fund B; and the
			purchased loan pool
			collateral <sup>11</sup>
16	Beacon	40,328,494	\$1,265,472
17			at First Security Bank;
18			\$5,030,000
19			in Oxbow Fund B; and the
			purchased loan pool
			collateral <sup>12</sup>

20 The cash collateral for the Beacon and Brooks loans were  
21 placed in Oxbow Fund B. According to the Amendment to  
22 Subscription Agreement dated January 6, 2000, Beacon has the  
23 right to "put" 100% of its equity ownership in the Oxbow Fund B  
24 to the Oxbow Fund B or any and all of the existing or future  
25 funds managed by Oxbow Partners or any of its affiliated entities  
26 at its sole discretion. The "put" is to be paid in an amount

27 \_\_\_\_\_  
28 <sup>11</sup> Value to be determined by audit.

<sup>12</sup> Value to be determined by audit.

1 equal to the total original investment within 30 days. Brooks  
2 has a similar agreement in its loan files dated July 30, 1999.

3 According to a letter from Dyer dated June 9, 2000, Brooks'  
4 investment in Oxbow Fund B at that point in time was \$4,105,700  
5 with an estimated value of \$5,315,249. Similarly, according to  
6 another letter from Dyer dated June 9, 2000, Beacon's investment  
7 in Oxbow Fund B at that point in time was \$3,445,000 with an  
8 estimated value of \$4,306,249.

9 **6. Private-Equity Investments: A-Fem**

10 Available information indicates that CCL initially invested  
11 for clients in the common stock of ATHENA Medical Corporation  
12 while it was privately held. The ATHENA Medical Corporation  
13 stock was then converted to series A preferred convertible stock  
14 and warrants in A-Fem beginning on August 31, 1998. The warrants  
15 become exercisable two years after the date issued and expire 10  
16 years after the date issued. Shares of preferred stock are  
17 convertible into shares of A-Fem common stock on a one-for-one  
18 basis, subject to adjustment under certain circumstances to  
19 prevent dilution.

20 Prior to August 31, 1998, CCL paid \$8,296,857 to A-Fem to  
21 purchase 4,316,405 preferred shares of A-Fem and 50,000 warrants  
22 with a stated exercise price of \$4.25. CCL paid \$1,248,000 on  
23 August 31, 1998, to purchase 650,000 preferred shares and 130,000  
24 warrants with a stated exercise price of \$1.92. No warrants have  
25 been exercised to date.

26 In a memo dated July 22, 1998, Jeffrey Grayson indicates  
27 that he told Stephen Frankel, A-Fem's President, that CCL was not  
28 in a position to invest any more money in A-Fem. As of that

1 date, CCL had already funded \$8,296,857. Nevertheless, an  
2 additional \$6,097,403 was funded by CCL through fifteen separate  
3 installments starting on August 31, 1998, and ending on  
4 September 21, 2000. On these funding dates, the closing market  
5 prices of the A-Fem common stock ranged from \$.938 to \$2.25 per  
6 share.

7 As of the Appointment Date, CCL had purchased 47.5%, or  
8 8,696,147 shares, of A-Fem's total outstanding preferred stock  
9 and exercisable warrants.

10 The Receiver's initial review indicates that CCL may have  
11 charged management fees on inflated values of A-Fem's preferred  
12 stock. CCL valued the A-Fem preferred stock for fee calculation  
13 purposes using the closing market price of A-Fem's common stock,  
14 ignoring appropriate discounts related to valuation of restricted  
15 preferred shares.

16 Going concern opinions for A-Fem were issued by independent  
17 auditors for the years ended December 31, 1998 and 1999. The  
18 financial statements indicate that A-Fem experienced significant  
19 operating losses during the years ended December 31, 1997, 1998,  
20 and 1999, and continued to incur losses and experience financial  
21 deterioration in 2000. Further, A-Fem has never generated  
22 significant revenues from operations. The financial statements  
23 also indicate that A-Fem management may be required to curtail A-  
24 Fem's activities and A-Fem may be forced to cease operations if  
25 the company is unable to obtain adequate additional financing.

26 Available information indicates that James E. Reinmuth, A-  
27 Fem's Chairman and Director, was also at one time a member of  
28 CCL's advisory board. In addition, Mr. Reinmuth is a guarantor

1 on a \$3.5 million loan originated by CCL in the name of Watershed  
2 Holdings and a co-borrower on another \$1.2 million loan  
3 originated by CCL in the name of Schott/Reinmuth.

4 An A-Fem press release dated July 1, 1999, indicates that A-  
5 Fem had entered into a letter of intent for a private placement  
6 of \$10 million in equity with Oxbow Partners to be completed over  
7 the next nine months.

## 8 **7. Real Estate Equity Interests**

9 The marketing materials prepared by CCL imply that real  
10 estate equity investments were selected for the benefit of  
11 clients' portfolios for either current income or future market  
12 value appreciation. It is the Receiver's understanding, however,  
13 that CCL never specifically purchased real estate equity  
14 investments for its clients. The current real estate equity  
15 interests held by CCL result from loans converted to equity  
16 through loan restructurings or from post default deeds in lieu of  
17 foreclosure.

18 According to CCL records, as of September 21, 2000, the real  
19 estate equity interests had a cost of \$65,903,262 and a claimed  
20 market value of \$52,393,428. The two major real estate equities  
21 in CCL's Private Investments portfolio are Legends and SCREH.  
22 Both have a market value significantly less than their investment  
23 cost.

### 24 **a) Legends**

25 The Legends project started as a \$16.4 million construction  
26 loan for the development of Portland senior luxury condominiums.  
27 An additional \$1.1 million of client funds were advanced by CCL  
28 to cover losses. No take-out financing was in place to replace

1 the construction loan upon completion, although at least one CCL  
2 client claims that take-out financing was misrepresented to be in  
3 place. Thirty units were sold, but the project failed and the  
4 remaining 50 unsold units were obtained by CCL through a deed in  
5 lieu of foreclosure. No units have been sold for a year prior to  
6 the Appointment Date, and it is estimated that the bulk sale  
7 value of the project is \$5 to 7 million--a loss of about 50%.

8 **b) SCREH**

9 The other major real estate equity investment is SCREH.  
10 SCREH was formed on May 26, 1995, by CCL on behalf of its clients  
11 through a limited liability company agreement with Glen Grodum  
12 (president and CEO of Smith's Home Furnishings), Frank Piacentini  
13 and Wayne Rembold. SCREH was formed in an effort to restructure  
14 Smith Home Furnishings' debt to CCL. CCL contributed its  
15 existing debt of \$6.4 million and an additional \$5 million in  
16 cash. The other three members contributed the seven real estate  
17 properties in which Smith's Home Furnishings was a tenant.

18 Smith's Home Furnishings filed for bankruptcy on August 22,  
19 1995, less than three months after the restructure. Due to the  
20 closure of Smith's Home Furnishings by mid-October 1995, the  
21 properties were left vacant. These retail spaces have been  
22 difficult to lease.

23 As of the Appointment Date, one of the retail properties  
24 included in SCREH has been sold and the other six are still owned  
25 and managed by CCL. Three of these properties are fully  
26 occupied; the rest have substantial vacancies, with current  
27 occupancy rates as low as 47% at one site. As of the Appointment  
28 Date, the portfolio appraisal for the remaining SCREH properties

1 indicates a cost of \$26.1 million and a market value of  
2 \$12.5 million, representing a loss on investment exceeding 50%.

3 **VII. EQUITABLE ALLOCATION OF ASSETS AND LOSSES**

4 **A. Relevance of Possible Misrepresentations**

5 Whether CCL made misrepresentations regarding the quality  
6 and type of the Private Investments it offered to its clients is  
7 relevant to an eventual Court determination of how assets and  
8 losses should be distributed.

9 **B. CCL Control Over Investment Selection**

10 Under the typical IAA, CCL was given complete discretion to  
11 select investments, subject only to broad diversification  
12 parameters. For example, under one IAA for "Client A," CCL was  
13 free to invest the client's money, including switching it from  
14 investment to investment, however and whenever CCL desired, so  
15 long as it adhered to the following diversification parameters:

- 16 • no more than 40% in common stocks
- 17 • no more than 20% in corporate bonds
- 18 • no more than 20% in fixed income instruments
- 19 • no more than 17% in real estate equity investments
- 20 • no more than 45% in real estate mortgages
- 21 • no more than 15% in private placements
- 22 • no more than 10% in cash and cash equivalents

23 Thus, under this IAA, CCL could allocate up to 77% of Client  
24 A's money to Private Investments and only 23% to Public  
25 Investments and cash. Alternatively, CCL could allocate 90% of  
26 Client A's money to Public Investments and cash, and only 10% to  
27 Private Investments. As discussed previously, CCL favored  
28

1 Private Investments because it could earn a higher management  
2 fee.

3 Even so, the Receiver's investigation has revealed that  
4 clients were not treated the same by CCL. Certain clients were  
5 more heavily invested in Private Investments than other clients  
6 with similar IAA-diversification parameters.

7 **C. Inconsistent Compliance With IAA Allocation**

8 Not only did CCL have virtually unfettered discretion to  
9 select investments for its clients, but it appears that in  
10 certain instances CCL violated the diversification parameters.  
11 For example, under Client B's IAA, CCL could allocate up to 55%  
12 of its assets to Private Investments. However, as of the  
13 Appointment Date, over 95% of that client's assets were held in  
14 Private Investments.

15 **D. Non-Uniform Losses from Private Investments**

16 Not all of CCL's Private Investments generated the same  
17 returns (or losses). Thus, depending on what CCL had chosen as  
18 an investment for any particular client, different clients with  
19 similar IAA's have suffered significantly different losses. For  
20 example, CCL's investment in the WCC/Sterling notes will likely  
21 turn out to be worth very little. An investment in a real estate  
22 secured loan, even if in default, may yield a somewhat better  
23 return, provided that the real property has some significant  
24 value. At the other end of the spectrum, certain loans were  
25 fully performing and have actually been paid in full, such as the  
26 Oregon Power loan which recently paid off on a principal balance  
27 of \$1.8 million.

1 To a large extent, it was the luck of the draw whether one  
2 client's funds were invested in a WCC note that turned out to be  
3 worth little or nothing, versus an Oregon Power loan which was  
4 paid off in full.

5 **E. Equitable Loss and Dividend Distribution**

6 Based on his investigation to date, the Receiver has  
7 concluded that CCL had wide-ranging and total control over the  
8 investment selection for clients. CCL did not uniformly comply  
9 with IAA diversification parameters for all clients. CCL clients  
10 are not all invested in the same Private Investments and the  
11 various Private Investments will likely have a wide range of  
12 losses. Therefore, the Receiver is evaluating whether or not it  
13 would be equitable to distribute assets to clients in strict  
14 conformity with the record investment allocation according to  
15 CCL's files as of the Appointment Date. Alternative equitable  
16 distribution approaches are being examined. The Receiver intends  
17 to request the Court to approve a distribution approach after the  
18 Receiver's examination is completed.

19 The Receiver, granted the full powers of an equity receiver  
20 and directed to take such steps as may be necessary to protect  
21 the investors' interests, may consider the interests of CCL's  
22 clients as a group in evaluating distribution approaches. Any  
23 distribution plan must be equitable and fair, and treat similarly  
24 situated investors similarly. Securities and Exchange Commission  
25 v. Elliot, 953 F.2d 1560, 1570 (11th Cir. 1992) rev'd. in part on  
26 other grounds, 998 F. 2d 922 (11th Cir. 1993).

27 With very few exceptions, CCL's clients vested wide  
28 discretion and control in CCL to select investments. As a

1 result, the makeup of any particular client's portfolio as of the  
2 Appointment Date was largely a matter of chance. It is clear  
3 from the Receiver's investigation to date, however, that CCL's  
4 total assets will be insufficient to make all clients whole.  
5 Where the struggle over receivership assets is between equally  
6 innocent parties and those assets were obtained or retained by  
7 fraudulent conduct, "tracing should not and will not apply" or  
8 control. U.S. v. Real Property, 89 F. 3d 551, 553 (9th Cir.  
9 1996). See also U.S. v. Durham, 86 F.3d 70, 73 (6th Cir. 1996)  
10 (although particular claimant would be permitted to trace funds  
11 and impose a constructive trust under state law, district court  
12 refused to permit tracing because fraud victims were in equal  
13 positions and should be treated as such.); Commodity Futures  
14 Trading Commission v. Richwell Int'l. Ltd., 163 B.R. 161 (N.D.  
15 Cal. 1994) (Court approves pro rata distribution plan based on  
16 account balances which do take into account profits and losses  
17 made by investors because company had detailed accounting records  
18 which made it possible to segregate customer accounts.)

19 Even where the pre-receivership operations are not  
20 fraudulent, courts have refused to allow tracing of assets where  
21 to do so would promote unequal treatment of similarly situated  
22 creditors. Torres v. Eastlick (In re North American Coin &  
23 Currency, Ltd.), 767 F.2d 1573, 1579 (9th Cir. 1985) amended by  
24 order, 774 F.2d 1390 (1985) cert. denied 475 U.S. 1083 (1986)  
25 (In the bankruptcy context, tracing gives way to ratable  
26 distribution where "we fail to discern the equitable principle  
27 that requires us to protect the plaintiffs' investments fully, at  
28 the expense of these other creditors.")

1           The Legends condominium project provides one example of why  
2 it may be inequitable to simply distribute a particular  
3 investment to its "record beneficial owners." The Legends  
4 started as a construction loan secured by a first trust deed in  
5 real estate. Four clients' funds were selected by CCL to make  
6 the loan. Over \$17.5 million of these clients' funds were  
7 invested, some without clients' knowledge or consent.  
8 Eventually, the loan fell into default and CCL took title to the  
9 property via a deed in lieu of foreclosure.

10           As of the Appointment Date, CCL had invested \$4.9 million  
11 and \$4.8 million for two clients in the Legends loan, "Client C"  
12 and "Client D" respectively. Client C was invested for 28%, and  
13 Client D was invested for 27% of the total advanced. It has been  
14 estimated that the net sale price for this asset could be in the  
15 range of \$5 - \$7 million. Clients C and D could receive  
16 distributions from the net sales proceeds according to the  
17 respective percentage Legends investments CCL put them in.  
18 However, in light of CCL's use of these clients' funds for other  
19 investments, a strict pro rata distribution of the sale proceeds  
20 from this particular asset may not be equitable, even as to one  
21 another.

22           As of the Appointment Date, investments made by CCL on  
23 behalf of Clients C and D were allocated as follows:

	Legends	Total Private	Total Public/Cash	IAA Diversification to Private Investment
Client C	\$4.9	\$88.9	\$4.2	≤ 55%
Client D	\$4.8	\$63.0	\$64.5	≤ 77%

8 If Client C (28%) and Client D (27%) received their  
 9 percentage shares of the estimated \$5 million net sales price,  
 10 they would receive dividends of \$1.4 and \$1.35 million,  
 11 respectively. Previously, these clients, along with all other  
 12 clients, obtained release of all Public Investments. Client C  
 13 received \$4.2 million in Public Investments, and Client D  
 14 received \$64.5 million in Public Investments. Thus, after a  
 15 percentage distribution per CCL's records of the Legends  
 16 proceeds, Client C would have received a total distribution of  
 17 \$5.6 million against its total funds invested of \$93.1 million,  
 18 or 6 cents on the dollar. In contrast, Client D, with its  
 19 \$1.35 million Legends distribution and its prior \$64.5 million  
 20 Public Investment distribution, would have received a total  
 21 dividend of \$65.85 million against a total investment of  
 22 \$132.5 million, or 49.7 cents on the dollar.

23 On its face, a total dividend of 6% to one investor and  
 24 49.7% to another appears inequitable, especially when CCL had  
 25 comparable investment discretion under each of their IAAs, and  
 26 CCL violated the diversification parameters for Client C.  
 27 Further, because the Receiver has released the Public Investments  
 28 without any equitable reallocation or adjustment, the Receiver

1 must be careful not to overpay dividends from the liquidation of  
2 Private Investments in order to minimize the need to seek  
3 disgorgement of funds from clients.

4 Thus, after further investigation and analysis, the Receiver  
5 will propose a plan to equitably distribute the proceeds from the  
6 liquidation of the Private Investments portfolio. That proposal  
7 may be a strict investment-by-investment approach based on CCL  
8 records of beneficial interest, or it may be based on a pooling-  
9 of-losses approach. Until it is determined by the Court how  
10 losses and assets should be equitably distributed, the Receiver  
11 has declined, at least for the time being, to simply turnover  
12 Private Investments to clients with record interests.

13 **VIII. CONTINUING INQUIRY AND ACTIVITY**

14 The Receiver is continuing his investigation in  
15 contemplation of submitting future reports and to seeking Court  
16 authority to undertake certain actions. He plans to do the  
17 following:

18 1. Finalize analysis of the private-loan portfolio and  
19 obtain a valuation thereof. Initiate efforts to package and,  
20 subject to Court approval, sell the private loan portfolio.

21 2. Audit the loan pools pledged as collateral for the  
22 private-debt investments.

23 3. Obtain and analyze all files and records in the  
24 possession of CCL's prior outside attorneys and accountants.

25 4. Replace CCL as asset manager on all real estate  
26 properties.

27 5. Subject to Court approval, market and sell CCL's office  
28 building and other tangible assets.

1           6.     Analyze and, where appropriate, subject to Court  
2 approval, pursue causes of action against third parties who  
3 contributed to client losses.

4           7.     Establish a secure document repository for CCL's  
5 extensive documents and files. Provide long-term access to  
6 parties involved in litigation.

7           8.     As appropriate, segregate and liquidate individual  
8 defendant's assets and determine whether to seek inclusion of the  
9 personal assets of defendants within the receivership estate.

10          9.     Recommend to the Court an equitable allocation of the  
11 assets and losses for distribution that reflects the facts about  
12 CCL representations and CCL control of investments.

13  
14 Dated this \_\_\_ day of November 2000

15                                   ALLEN MATKINS LECK GAMBLE &  
16                                   MALLORY LLP

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