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7 Chapter 11 Trustee

8 UNITED STATES BANKRUPTCY COURT
9 DISTRICT OF NEVADA

10 In re)
11 AMERICAN PACIFIC FINANCIAL)
12 CORPORATION,)
13 Debtor.)

CASE NO. BK-S-10-27855-BAM
Chapter 11
DECLARATION OF CHRISTOPHER R. BARCLAY IN SUPPORT OF SECOND STATUS REPORT OF CHAPTER 11 TRUSTEE
Date: December 6, 2011
Time: 10:00 a.m.
Ctrm: BAM - Courtroom 3
Foley Federal Building
300 Las Vegas Blvd. South
Las Vegas, NV 89101
Judge: Hon. Bruce A. Markell

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24 I, Christopher R. Barclay, declare as follows:

25 1. I am the duly appointed Chapter 11 trustee of the bankruptcy estate of American
26 Pacific Financial Corporation ("Debtor"). In this capacity, I have taken certain actions and
27 undertaken an investigation and review of the Debtor's assets and liabilities as well as of its financial
28

1 relationships with various related and affiliated entities and other insiders and its creditors. My
2 investigation and review is not complete, nor have I identified resources readily available to me
3 sufficient to fund and conduct a full scale forensic accounting investigation.

4 2. Based on my review and investigation to date, it is apparent that the Debtor has, at
5 best, only nominal operations at present. Although the Debtor's schedules list a great number of
6 purported investments, with an attributed book value of more than \$16 million, it appears that only a
7 very small number of the scheduled investments (less than six) are reasonably characterized as
8 performing investments. Of these investments, the single largest investment is the Debtor's
9 investment in Capital Foods, LLC. This investment however generates no current income or cash
10 flow and the Debtor's voting interest in this entity is a non-controlling interest. The remaining
11 performing investments include an oil & gas interest that currently generates monthly royalties of
12 between \$1,500 and \$5,000 and loans or promissory notes that provide approximately \$10,000 per
13 month of interest income. As all of these investments are passive holdings that are in various stages
14 of liquidation, the Debtor has no ongoing operations beyond collecting and depositing remaining
15 investment returns.

16 3. The Debtor reports that it currently holds a minority (26.5 percent) ownership of voting
17 class shares (Class A membership units), together with an 87 percent ownership share of Class B
18 preferred non-voting, but preferred return, membership units in Capital Foods. Unfortunately, it is
19 far less clear as to what, if any, current market or liquid value these ownership interests may have,
20 particularly given the many layers of debt, encumbrances, liens and cross guarantees under which
21 these interests and related interests in affiliated entities and investments suffer. According to the
22 Debtor's most recent plan filing (Docket #301 at page 2), the Debtor contends that the future net
23 worth of these Class A and Class B units in Capital Foods may be as much as \$45.5 million extended
24 out six or seven years to 2017.

25 4. I have spent time, as has my counsel, reviewing available documentation of the Debtor's
26 interests, claims and investments in Capital Foods in an attempt to reconcile discrepancies, if not
27 outright contradictions, between documents which purport to support the Debtor's statements in its
28 last plan filing (Docket #301) to the effect that the "[o]wnership interests in Capital Foods have

1 remained the same since 1998.”

2 5. On June 2, 2011, I met with Mr. Larry Polhill at the Debtor’s offices. I interviewed Mr.
3 Polhill regarding the Debtor’s operations and performing investments. I also met the Debtor’s
4 controller, Ms. Marilyn Donegan and another staff member, Ms. Juanita (“Jeanie”) Aranda at this
5 time.

6 6. On June 13, 2011, I met with a number of the members of the Official Committee of
7 Creditors (“OCC”) in this case at my offices in Irvine, California. Some members attended in
8 person, and others attended by telephone conference connection, including the OCC’s counsel, Louis
9 Bubala of the Armstrong Teasdale law firm. At this meeting, the attendees shared their perspectives
10 and observations about the case to date as well as some of their histories of dealing with the Debtor
11 and Mr. Polhill in various financial transactions through the Debtor and through related and
12 affiliated entities. We also discussed the members’ differing views about case alternatives and
13 possible resolutions.

14 7. I then met on June 15, 2011, with Mr. Polhill, his personal counsel, Michael Heyman,
15 the Debtor’s counsel Ms. Thomas, and my counsel, Mr. Hill at the offices of the Sullivan Hill law
16 firm in San Diego, California to review the Debtor’s financial history, its financial affairs and its
17 assets and liabilities, as well as to gain an understanding of the Debtor’s perspective of the Chapter
18 11 case, the dynamics with its creditors, its proposed plan and its perspective as to a resolution in the
19 case in light of the challenges it faced in the case as well as in the business markets in which its
20 assets resided.

21 8. On July 20, 2011, at my request I met with my counsel and Mr. Polhill and his counsel,
22 Michael Heyman, and for part of the meeting, with Marilyn Donegan, at the offices of the Debtor in
23 Grand Terrace, California to further review the Debtor’s business affairs. At this same meeting, I
24 devoted time to further identifying the Debtor’s files and records. Prior to the meeting, I instructed
25 Mr. Polhill and his staff to assemble, protect and maintain the Debtor’s books and records in
26 preparation of an anticipated turnover of those records.

27 9. From the beginning of my tenure as Trustee, I attempted to obtain access to the report
28 prepared by the OCC’s forensic accountant, Craig L. Greene, who was appointed by order of this

1 Court. Based on my visits at the Debtor's business premises, my very preliminary viewing of its
2 records and record keeping practices, and my interviews with Mr. Polhill and certain of his staff, I
3 felt it was prudent for me to view Mr. Greene's report and interview Mr. Greene himself in order to
4 confirm what records were turned over to him, what analysis he made and what conclusions, if any,
5 he had drawn from his work, particularly to ascertain whether I had been given at least equal access
6 to similar files, records and materials, and to confirm that I was addressing the same subjects of
7 concern that had previously warranted Mr. Greene's attention. Because of its practice of transferring
8 investors from one asset to another, multiple levels of ownership, and the Byzantine nature of the
9 Debtor's accounting records and documentation, I concluded that it is extremely difficult to gain a
10 clear understanding of the Debtor's business affairs without considerable effort and likely
11 extraordinary expense.

12 10. I instructed my counsel to file a motion with this Court seeking authorization to take Mr.
13 Greene's Rule 2004 examination, and to compel his attendance at that exam with his report and his
14 work papers and all documents given to him to support his work. The OCC opposed my motion and
15 attempted to deny me access to Mr. Greene on the grounds that his report and opinions were
16 privileged. The Court granted my motion over the objection of the OCC. I obtained a copy of Mr.
17 Greene's report, which I reviewed, and I attended Mr. Greene's examination on September 20, 2011.

18 11. On September 30, my counsel (Mr. Hill) wrote an email to the Debtor's counsel (Ms.
19 Kaaran Thomas) and Mr. Polhill's counsel (Michael Heyman). Mr. Hill wrote:

20 "Trustee Barclay is still grappling with understanding the interrelationships among the
21 entities involved with the Capital Foods interests and investments of APFC, directly and
22 indirectly. What we need to get is better identification of the liens, claims and
23 encumbrances, or guarantees, business agreements, or subordination agreements, that in
24 anyway impair or limit the ability of APFC to market and sell, or encumber, its interests in
25 any of the Capital Foods related interests or investments, or to realize value out of any such
26 interests on an interim basis. In our prior discussions with Mr. Polhill, he indicated that there
27 were such limitations, but they were not specifically identified to us, at least not yet in
28 writing. If and to the extent there are such limitations, re [sic] request that we also receive
copies of all documents that evidence such limitations."

12. On September 30, I wrote to Mr. Polhill to inform him that I made arrangements to

1 retrieve the Debtor's records in his possession.¹ I also inquired about the availability of a schedule
2 of the investments/loans made by the Debtor that I might use to determine that the records turned
3 over constitute the complete records of the Debtor.

4 13. On October 4, I wrote an email to Mr. Polhill following up on my September 30 inquiry
5 as no response had been forthcoming. A short time later, Mr. Polhill responded and indicated that he
6 would speak to Ms. Donegan and provide a reply the next day.

7 14. On October 5, I wrote again to Mr. Polhill and inquired about the availability of a
8 schedule of the investments/loans made by the Debtor that I might use to determine that the
9 inventory of records to be turned over is complete. A short time later, Mr. Polhill responded and
10 wrote "we have the accounting schedules in quick books [sic] and the schedules of the chapter 11
11 petition."

12 15. On October 6, I exchanged emails with Mr. Polhill. I inquired about his and Ms.
13 Donegan's availability for a meeting at his office on October 7. I told Mr. Polhill that I wanted to
14 review the documents concerning the Debtor's transactions with Midwest Business Credit, LLC
15 ("MWBC")² and also the documents relating to transactions with Café Valley, Inc. (one of the two
16 principal Capital Foods, LLC investments). Mr. Polhill confirmed his and Ms. Donegan's
17 availability and willingness to meet with me.

18 16. On October 7, I met with Mr. Polhill and Ms. Donegan at their offices. In this meeting,
19 we reviewed the schedule of investments available from the Debtor's QuickBooks records. We had
20 a wide ranging discussion touching on some of the investments made by the Debtor that were later
21 recorded as a loss. In my observation, both Mr. Polhill and Ms. Donegan responded at times with
22 equivocation and appeared to evade direct responses to simple questions about why particular entries
23 were recorded in the Debtor's books and records, which at all times relevant were maintained by Ms.
24 Donegan.

25 _____
26 ¹ There are other records in the Grand Terrace office that Mr. Polhill and Ms. Donegan claim are not APFC records, but
27 rather books and records of affiliates. Mr. Polhill and Ms. Donegan remain in possession of these records and I have
reserved all rights regarding the issue of ownership of them.

28 ² MWBC is an asset-based lender with offices in Illinois. The Debtor's records reflect that the Debtor made loans to
MWBC and at one time owned an interest in MWBC. At all relevant times, Mr. Polhill was a manager of MWBC.

1 17. In the course of the review, I observed and made inquiries about certain accounts that
2 appear under the heading "Owner Draws". One account reflects payments made by the Debtor to
3 Party A and another reflects payments made by the Debtor to Party B.³ The Party A owner draw
4 account is entitled "Lincoln Draw-Party A" and the Party B owner draw account is entitled "Party B
5 Draws".

6 18. In lay terms, the balances accumulated in these general ledger accounts are a cumulative
7 total of payments made by the Debtor to Party A and Party B, each, on account of a particular third
8 party investment made by Party A and Party B through the Debtor. The Debtor's QuickBooks
9 records reflect that the balances in these accounts were written off as a loss during the fiscal year
10 ended July 31, 2007.⁴ At the time of the write-off in 2007, Party A's owner draw account had a
11 balance of \$951,713.51 and Party B's owner draw account had a balance of \$714,785.24. Additional
12 losses were recorded in 2008.

13 19. I asked Mr. Polhill to explain why the Debtor's accounting records reflect "owner draw"
14 accounts in the name of Party A and Party B. Mr. Polhill's response is that the accounts were a form
15 of income tax reporting accommodation made by the Debtor for these parties. According to Mr.
16 Polhill, Party A and Party B each invested more than \$500,000 through the Debtor in a Limited
17 Liability Company (Lincoln Estates, LLC) that owned real property in Bluffton, Indiana. I
18 understand that the real property in question comprised a facility of some kind that was leased to
19 Inventure Foods (fka Poore Brothers, Inc.).

20 20. Apparently, the Debtor's view was that by treating the payments as an "owner draw"
21 and structuring the payments so that they were made by the Debtor and not by the LLC, the Debtor
22 believed that the payments in question could be made without requiring any disclosure by either the
23 Debtor, the LLC, or Party A and Party B to any governmental entity for income tax reporting
24 purposes. The payments in question were not reported on the tax returns of the LLC or the k-1
25

26 ³ The identities of Party A and Party B are intentionally omitted. Both Party A and Party B are members of the OCC.
27 Party B holds an interest in at least one investment that is presently actively managed by Mr. Polhill.

28 ⁴ The actual date that the balances were written off and recorded as a loss is subject to further investigation as the
accounting program used by the Debtor, QuickBooks, permits the backdating and alteration of accounting data without
evidence of an accounting trail of changes made.

1 forms issued by the LLC to Party A and Party B annually. According to Mr. Polhill, in his own
2 words, helping the Debtor's investors avoid payment of income taxes on their purported investment
3 gains on account of investments made by or through the Debtor was "all part of the game" for those
4 investors who requested it.

5 21. I also made inquiries of Mr. Polhill and Ms. Donegan about purported loan transactions
6 that appear in the Debtor's QuickBooks records involving MWBC. Mr. Polhill explained that at one
7 time MWBC was majority owned (60%) by Stillwater Capital, LLC, Dakota Farms, LLC and the
8 Debtor. I obtained documents that described Mr. Polhill as the manager for MWBC. I observed that
9 the Debtor's records reflect that the outstanding balance of the loans to MWBC (\$335,000) was
10 written off and recorded as a loss on July 10, 2009.⁵ Mr. Polhill and Ms. Donegan were not able to
11 explain why the charge off was recorded. Mr. Polhill questioned the fact that the Debtor ever loaned
12 money to MWBC, notwithstanding what the Debtor's QuickBooks records showed. I inquired about
13 the availability of accounting records for MWBC and Mr. Polhill stated (in Ms. Donegan's presence)
14 that those records were prepared by and maintained by MWBC's Illinois-based management and not
15 available at the Grand Terrace office.

16 22. In the course of our discussion about the Debtor's transactions with MWBC, I made
17 inquiries about documentation surrounding apparent borrowing and lending transactions in 2005
18 involving an Illinois-based bank, Capital Foods, MWBC, Mr. Polhill and the Debtor. Based on Mr.
19 Polhill's explanation, I understand that the Debtor sought to raise money that it intended to lend to
20 Café Valley, Inc. Capital Foods and Mr. Polhill, individually, arranged to borrow \$500,000 from the
21 Illinois bank. As collateral for the loan, Capital Foods pledged 900,000 shares of Inventure Foods
22 stock and a note receivable from MWBC for \$500,000. I inquired why Capital Foods had loaned
23 \$500,000 to MWBC. Mr. Polhill equivocated and after providing a series of evasive responses, he
24 finally admitted that the loan from Capital Foods to MWBC existed in paper only – no \$500,000
25 loan by Capital Foods to MWBC was ever made. I asked Mr. Polhill why documentation was
26 prepared to create the appearance of a loan between Capital Foods and MWBC and he explained that

27 _____
28 ⁵ The Debtor's transactions with MWBC are especially pertinent to my investigation because they relate, in part, directly
to transactions involving Capital Foods, LLC.

1 the reason was because the Illinois-based bank required Illinois-based collateral.

2 23. Based on my review of the Debtor's QuickBooks records, I noted that the Debtor
3 recorded an obligation owed to the Illinois-based bank in the amount of \$500,000. The Debtor made
4 monthly payments to the bank in connection with the 2005 loan through January 2010. Other entries
5 recorded on the Debtor's books, which appear to have been backdated to 2008, show the bank loan
6 removed along with amounts due to the Debtor from Café Valley, Inc. According to Mr. Polhill and
7 Ms. Donegan, the loan was removed from the Debtor's books because the Debtor was not the
8 borrower. My investigation of these transactions and related matters is ongoing.

9 24. Among other inquiries, I also asked Mr. Polhill to tell me about AP Venture Fund. The
10 Debtor's QuickBooks records reflect that the Debtor had a more than \$5.0M interest in this entity
11 that terminated January 1, 2010.

12 25. According to Mr. Polhill, AP Venture Fund was set up as a form of hedge fund,
13 although he personally did not like the term hedge fund. He explained that the idea was that AP
14 Venture Fund would raise money from investors and use that money to make investments in entities
15 or deals, where in addition to a stated return, the fund would also participate through some means in
16 any upside in the underlying investment performance, such as through an "equity kicker".

17 26. Mr. Polhill explained further that the funds that AP Venture Fund raised from investors
18 were later transferred to the Debtor. I understand that these transfers were accounted for as a loan
19 from AP Venture Fund to the Debtor. Additionally, according to Mr. Polhill, accounting entries
20 were made on the books of the Debtor reflecting that it transferred certain equity interests and other
21 investments to the AP Venture Fund in exchange for an ownership interest in AP Venture Fund.

22 27. Mr. Polhill explained that, notwithstanding the accounting entries made, in reality the
23 equity interests and other investments remained in the name of the Debtor and those interests were
24 never legally transferred by the Debtor to AP Venture Fund. Mr. Polhill and Ms. Donegan explained
25 that in contemplation of the Debtor filing its petition for bankruptcy, the accounting for the
26 purported asset transfers was essentially unwound whereby entries were made on the Debtor's books
27 reflecting the termination of its interest in AP Venture Fund and a reduction of the loan payable by
28 the Debtor to AP Venture Fund.

1 28. During the course of the October 7 meeting, I requested and I was provided with certain
2 documents and written information. For items not readily available, I asked Ms. Donegan and Mr.
3 Polhill to locate or otherwise obtain the information and to provide it to me. At the conclusion of the
4 meeting, I expressed to Mr. Polhill my disappointment in the condition of the Debtor's accounting
5 records and in particular Ms. Donegan's inability to fully explain entries that she made in those same
6 records. Mr. Polhill stated that he recognized that the records were poorly maintained and that Ms.
7 Donegan had performed poorly. I observed that Mr. Polhill had requested that the Debtor's estate
8 pay his company for Ms. Donegan's services, which was the practice prior to my appointment. I
9 noted, however, that in light of Ms. Donegan's inability to fully explain the records she maintained
10 and admitted significant errors in those records, it was problematic for the bankruptcy estate to
11 provide compensation for her services. Mr. Polhill said that he understood my position.

12 29. On October 11, Rosemary Nguyen one of the members of the OCC contacted me to
13 request a face to face meeting.

14 30. I later received a similar meeting request from another OCC member, Mr. Joseph
15 McCoy. I responded to these meeting requests and a meeting was scheduled for October 27.

16 31. On October 12, 2011, I wrote an email to Mr. Polhill and Ms. Donegan and requested
17 certain records, including copies of the tax returns for Lincoln Estates, LLC. In this same email, I
18 requested a follow-up meeting with Mr. Polhill and Ms. Donegan on October 18. Mr. Polhill later
19 informed me that he would be out of town on the 18th, but agreed to permit the meeting to go
20 forward, although his own participation would be by telephone. We agreed that I would travel to the
21 Grand Terrace office where Ms. Donegan would be present and that Ms. Donegan would facilitate
22 Mr. Polhill's participation by phone.

23 32. Prior to the October 18 meeting, I received copies of the 2005 to 2008 income tax
24 returns for Lincoln Estates, LLC and certain other documents and records that I requested.

25 33. On the morning of October 18, before our meeting, I wrote an email to Ms. Donegan,
26 with a copy to Mr. Polhill to request copies of the Lincoln Estates, LLC tax returns for 1997 to 2004.
27 Mr. Polhill replied a short while later in an email copied to his counsel (Mr. Heyman) wherein he
28 wrote "...per your earlier request, I don't know if we have the prior tax returns that far back for

1 Lincoln, prior to 2004,...I will look into Lincoln further when I return". In a separate email to Ms.
2 Donegan on the same morning, with a copy to Mr. Polhill, I wrote to request copies of the tax returns
3 for MWBC for the years 2005 to 2008.

4 34. When I met with Ms. Donegan (in-person) and Mr. Polhill (telephonically) on October
5 18, I renewed my request for the identified tax returns for Lincoln Estates, LLC and MWBC. I was
6 told at this time that the records either had not been located or they were not available. I directed
7 Mr. Polhill and Ms. Donegan to locate or obtain the documents requested.

8 35. On October 19, I wrote an email to Mr. Polhill and Ms. Donegan in follow-up to our
9 October 18 meeting. Among other inquiries, I renewed my request for tax returns and other records
10 relating to Lincoln Estates, LLC and MWBC.

11 36. On October 25, I wrote an email to Mr. Polhill and Ms. Donegan. In this email, I
12 requested an update regarding the status of their response to the items of information that I had
13 requested but that I had not received from them.

14 37. On October 27, I met with members of the OCC and their counsel (Lou Bubala, Esq.)
15 who, along with my counsel and some members of the committee, participated by telephone. The
16 members of the committee requested a report on the status of my efforts and the direction that I
17 believed the case was headed. The sense that I received from this meeting is that some members of
18 the committee were quite anxious to see progress with the case. I reported that since the time of my
19 last meeting with the committee, I had met with Mr. Polhill on a number of occasions. I explained
20 also that I had made requests in writing for production of records and information by Mr. Polhill, but
21 that I had not received a full and complete response. I also explained to the members present that
22 my investigation of the Debtor's books and records underlying its financial affairs had been
23 hampered by the poor condition of the Debtor's records and the inability of the Debtor's
24 representatives to provide complete explanations to my questions; I described the Debtor's records
25 as akin to a house of mirrors. I cautioned the members present that I was concerned about factors
26 that complicated the ability to obtain value from the Debtor's interest in Capital Foods, LLC.

27 38. On the evening of October 27, I wrote an email to Mr. Polhill to advise him of my plans
28 to go to his Grand Terrace office to review and complete an inventory of the APFC records there that

1 had been set aside for turnover to me. Mr. Polhill responded to indicate that while both he and Ms.
2 Donegan would be out of town and unavailable, he would nonetheless make arrangements for my
3 access to the records.

4 39. On October 28, I went to Mr. Polhill's Grand Terrace office. While I was present at the
5 office, I spoke to Mr. Polhill by phone. In this call, Mr. Polhill reported to me that the tax return and
6 other records I had requested were not available. Mr. Polhill suggested that perhaps an alternative
7 would be to write to the Internal Revenue Service to request copies. In my mind, this was not an
8 acceptable alternative as tax return copies are generally only available for the last seven years and
9 the tax returns I sought included those for periods beyond seven years. I told Mr. Polhill that I
10 wanted to review certain of the files in Ms. Donegan's office while I was present and I requested that
11 he authorize access to her office. Mr. Polhill agreed to my request.

12 40. On October 28, I reviewed certain of the files in Ms. Donegan's office. I was generally
13 familiar with how the records were kept and where particular records were located within Ms.
14 Donegan's office. This is because Ms. Donegan had shown me and others present the manner in
15 which the files were organized in her office during the meeting that occurred at the Grand Terrace
16 office on July 20, 2011. Based on my review of the records present in Ms. Donegan's office on
17 October 28, I confirmed that records I had requested and that I had been told were not available were
18 in fact easily accessible in Ms. Donegan's office.

19 41. After I returned to my office on October 28, I wrote an email to Mr. Polhill. I advised
20 Mr. Polhill that I had met with members of the OCC and their counsel and that I had informed the
21 committee members that although I had requested records and documents, certain of the items that I
22 had requested were not forthcoming. Specifically, no documents had been forthcoming in response
23 to Mr. Hill's September 30 email to Ms. Thomas and Mr. Heyman requesting documents relating to
24 Capital Foods, LLC. I requested a meeting with Mr. Polhill at his office on either November 7 or
25 November 8.

26 42. On November 3, I wrote another email to Mr. Polhill. In this email, I reminded Mr.
27 Polhill that I had not received a response to certain of the inquiries and information requests in my
28 October 19 email to him and, as well, nor my October 28 email regarding the lack of response to Mr.

1 Hill's September 30 email regarding Capital Foods, LLC. Later in the day on November 3, Mr.
2 Polhill responded and stated that he had delivered some additional information to Mr. Heyman
3 regarding Capital Foods, LLC. He stated further that Mr. Heyman and Mr. Hill would need "...to
4 connect and work on the balance of the process."

5 43. On November 7, 2011, Mr. Heyman wrote a letter to Mr. Hill enclosing certain of the
6 requested documents responsive to Mr. Hill's September 30 email. Mr. Heyman also wrote "In the
7 future, please direct all requests for documents and other information directly to me."

8 44. On November 17, 2011, I called Mr. Polhill to discuss with him the status of the renewal
9 of the insurance coverage that the Debtor has in place. In this call, I suggested to Mr. Polhill at face-
10 to-face meeting at his Grand Terrace office for the purpose of reviewing the available information
11 relating to Capital Foods, LLC and issues relating to its financing arrangements. Mr. Polhill stated
12 that he would need to confirm with his counsel first and would let me know. We later exchanged
13 emails and reached agreement to meet on November 22.

14 45. On November 21, Mr. Polhill wrote an email to me and informed me that on the advice
15 of his counsel he needed to cancel the meeting set for November 22. Mr. Polhill proposed instead
16 that the November 22 meeting be combined with a meeting that was tentatively set for December 1
17 when counsel would be present.

18 46. On November 21, Mr. Hill wrote an email to Mr. Heyman on my behalf to request
19 access to documents present at the Grand Terrace office. Mr. Hill wrote (in part):

20 "Michael:

21 Give me a call to discuss the documents that the Trustee is still requesting be made available
22 for him to review and copy as necessary. I left you a voice mail message earlier today. I will
23 be in the office a bit longer today and then fly to Vegas for hearings tomorrow in other cases,
but I will be available when not actually in the air.

24 The documents that the Trustee needs to review, and discuss with Mr. Polhill when he is
25 available, are documents that we are informed and believe are located in Grand Terrace, CA
under the possession and control of Larry Polhill, as follows:

- 26 1. All documents that refer or relate to Lincoln Estates, LLC
27 2. All documents that refer or relate to Capital Foods, LLC
28

1 3. All documents that refer or relate to Midwest Business Credit, LLC

2 Per the Trustee, based on his prior discussions with Mr. Polhill and staff in Grand Terrace,
3 there should be no burden imposed to produce these records as they are principally kept by
4 Marilyn Donegan in the filing cabinets in her office. If Mr. Polhill is not available to meet
5 with the Trustee in Grand Terrace as earlier scheduled, the Trustee is okay with starting the
6 review of the documents with questions to Mr. Polhill to follow if someone (Marilyn or
7 otherwise) can simply make them available to the Trustee in Grand Terrace tomorrow.”

8 47. Later in the evening on November 21, I wrote an email to Mr. Heyman. In this email, I
9 advised Mr. Heyman that I had made multiple requests for records and information regarding
10 Lincoln Estates, LLC and MWBC and that on more than one occasion I was advised by Mr. Polhill
11 and Ms. Donegan that the requested information was not available. I also provided Mr. Heyman
12 with copies of and excerpts from my email communications with Mr. Polhill prior to November 7
13 regarding my requests for records relating to Lincoln Estates, LLC and MWBC.

14 48. I understand that Mr. Hill and Mr. Heyman spoke on November 22. Following this
15 conversation, Mr. Heyman sent an email wherein he stated:

16 “All:

17 I had a productive conversation with Jim this morning. As a follow-up, Mr. Barclay is
18 welcome to visit the Grand Terrace office for a two-hour document review tomorrow before
19 noon or next Tuesday all day (morning preferred). Larry probably does not know where
20 specific documents are located, but, based on the prior emails, Mr. Barclay has good idea of
21 where to look for the documents he is seeking, so it should not be an issue.”

22 49. On November 29, 2011, I went to Mr. Polhill’s Grand Terrace office. When I arrived,
23 Mr. Polhill told me that he was prepared to discuss the Capital Foods, LLC financing arrangements.
24 Mr. Polhill stated that not all of the records and information that I had requested relating to Capital
25 Foods had been produced to me. I advised Mr. Polhill that my visit had been arranged through Mr.
26 Heyman and my intention was to review and copy records that I had requested from him previously.

27 50. I commenced a review of the records in Ms. Donegan’s office. As Mr. Polhill and Ms.
28 Donegan made no effort to produce the documents that I had requested, it was incumbent on me to
locate the records based on my familiarity, such as it was, with how they were maintained by Ms.
Donegan. Under the circumstances, it may well be the case that there are other records that Mr.

1 Polhill or Ms. Donegan have that are responsive to my document requests but which records I have
2 not yet seen.

3 51. Mr. Polhill closely supervised my review of the records. While I was reviewing the
4 records, Ms. Donegan volunteered that she had succeeded in locating the missing records relating to
5 Lincoln Estates, LLC that I had requested. In fact, these records are among the records that I
6 previously observed on October 28, 2011 among the files maintained by Ms. Donegan in her office.
7 I inquired about the MWBC records that I had requested be produced and Mr. Polhill responded by
8 indicating that they were unavailable.

9 52. In the course of my review of the Lincoln Estates, LLC tax returns and other records, I
10 asked Mr. Polhill if in fact Lincoln Estates, LLC ever held title to the Bluffton, Indiana property.
11 After some equivocation, Mr. Polhill admitted that the Debtor held title to the property at all relevant
12 times and that title was not transferred to Lincoln Estates, LLC. This is contrary to what was
13 reported in the LLC tax returns filed on behalf of Lincoln Estates, LLC.

14 53. I also inquired of Mr. Polhill regarding a transaction in 2003 purportedly between Party
15 C⁶ and Lincoln Estates, LLC. According to documentation contained in Party C's investor file, in
16 2003 Party C acquired a 44.3% interest in the Bluffton, Indiana property from Lincoln Estates, LLC.
17 Thereafter, the Debtor commenced making payments to Party C on account of the alleged interest in
18 the Bluffton, Indiana property.

19 54. I showed Mr. Polhill the documentation contained in Party C's investor file maintained
20 by the Debtor. Mr. Polhill stated that he could not recall the transaction specifically or whether it
21 was ever consummated. I asked Mr. Polhill to explain how the purchase price for the 44.3% interest
22 was determined. Mr. Polhill explained that Party C was attempting to arrange an IRC Section 1031
23 exchange from a sale of an unrelated property. Mr. Polhill explained further, that the purchase price
24 was dictated by the amount that Party C needed the price to be in order to avoid the recognition of
25 any gain on the sale of the other unrelated property. In Mr. Polhill's own words, it was an
26 accommodation by the Debtor to Party C. In response to a further question that I asked, Mr. Polhill

27 ⁶ The identity of Party C is intentionally omitted. Party C is a close business associate of Mr. Polhill and a member of
28 the OCC.

1 confirmed that although the documentation for the exchange transaction makes reference to a note
2 for the balance of the purchase price over the amount of cash deposited by Party C, there was never
3 any expectation that Party C would make payment on the note. It was simply part of the
4 accommodation.

5 55. After reviewing a number of documents, I informed Mr. Polhill that I wanted to have
6 photocopies of certain of the documents.⁷ Mr. Polhill personally made each copy and handed them
7 to me. In the course of photocopying documents, I asked again about the availability of the MWBC
8 records. Mr. Polhill stated again that the records in question were unavailable.

9 56. Later, while I was returning documents to Ms. Donegan's office and reviewing others, I
10 inquired a final time about the existence of the MWBC records. I asked Ms. Donegan directly if she
11 had the records and would she produce them. With a groan, she got up from her desk, went to one of
12 the filing cabinets in her office and removed two large files containing MWBC records. These files
13 included tax returns and financial statements among other items. I showed Ms. Donegan the
14 financial statements and asked her if she had prepared the reports. Ms. Donegan stammered a bit
15 and then admitted that not only had she prepared the reports, in fact she had personally maintained
16 the books and records of MWBC from 2004 to 2008. Ms. Donegan also confirmed that she
17 maintained a QuickBooks file for MWBC on her computer and that her data file also included some
18 information (albeit incomplete data) for periods after 2008. I requested a copy of the MWBC
19 QuickBooks files.

20 57. From the outset, my review of documents on November 29, 2011 was subject to a 2-
21 hour time limit. After I had completed my review of the available records within the available time,
22 I prepared to leave the office. As I was in the process of departing the office, Mr. Polhill approached
23 me and asked me to wait. As if to take a page from the OCC's own playbook in this case, Mr.
24 Polhill explained that he had spoken to Mr. Heyman and requested that I not leave with the
25 documents that he had photocopied and delivered to me after my review of them as Mr. Heyman

26 _____
27 ⁷ I had arranged for a copy service to accompany me to the Grand Terrace office. While the copy service scanned certain
28 documents that I reviewed and identified for copying, I accepted Mr. Polhill's offer to also use the copier in the Grand
Terrace office to make photocopies of other documents.

1 wanted to (quite belatedly) review the documents to determine if any were subject to the attorney-
2 client privilege. I instructed Mr. Polhill to request that Mr. Heyman contact Mr. Hill to discuss the
3 matter and I departed the Grand Terrace office with the documents already provided and reviewed
4 by me.

5 58. Later on November 29, I agreed to place the documents that I obtained that day with
6 Knox Attorney Service acting as a third-party repository pending resolution of any disputes
7 concerning the attorney-client privilege. Accordingly, at this time, I will not describe my findings
8 based on the documents that I reviewed. Notwithstanding the foregoing, I believe that the
9 documents I reviewed on November 29 pertain to very substantial issues that are likely to have a
10 direct bearing on the recoveries for creditors in this case.

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

13 Executed this 5th day of December, 2011 at Irvine, California.

14
15 By:



16 Christopher R. Barclay
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