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11 **UNITED STATES BANKRUPTCY COURT**
12 **DISTRICT OF NEVADA**

13 In re:) Case No.: BK-S-10-27855-BAM
14 AMERICAN PACIFIC FINANCIAL)
CORPORATION,) Chapter 11
15 Debtor.) **U.S. SECURITIES AND EXCHANGE**
16) **COMMISSION'S STATEMENT IN**
17) **SUPPORT OF THE CHAPTER 11**
18) **TRUSTEE'S MOTION TO CONVERT**
19) **CASE FROM CHAPTER 11 TO**
20) **CHAPTER 7**
21)
22) Date: January 4, 2011
23) Time: 1:30 p.m.
24) Place: Foley Federal Building, Courtroom 3
25) 300 Las Vegas Blvd. South
26) Las Vegas, Nevada 89101

27 **TO THE HONORABLE BRUCE A. MARKELL, UNITED STATES BANKRUPTCY**
28 **JUDGE, CHAPTER 11 TRUSTEE CHRISTOPHER R. BARCLAY, DEBTOR, THE**
UNITED STATES TRUSTEE AND OTHER INTERESTED PARTIES:

The UNITED STATES SECURITIES AND EXCHANGE COMMISSION
("Commission"), appearing in this case as a creditor pursuant to 11 U.S.C. § 1109(b), files
this statement in support of Trustee's Motion to Convert Case From Chapter 11 to Chapter 7

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1 (Dkt. # 446, "Motion to Convert;" Dkt. # 447, "Trustee's Declaration Supporting Motion to
2 Convert"). The Commission respectfully states as follows:

3 I.

4 **INTRODUCTION**

5 The Commission participates in this case to protect its enforcement interest¹ and to help
6 ensure that American Pacific Financial Corporation's ("Debtor" or "APFC") investors, many
7 of whom the Debtor has listed as unsecured creditors, are treated fairly. The Commission
8 believes that the Trustee has established cause pursuant to 11 U.S.C. § 1112(b)(1) to convert
9 this case to Chapter 7 and fully supports immediate conversion of this case to a Chapter 7
10 liquidation. This Debtor is administratively insolvent. It has no active business and few
11 performing assets. Moreover, the Debtor has been grossly mismanaged by Larry Polhill
12 ("Polhill") and others reporting to him. The Motion to Convert does not raise the question of
13 whether or not the Debtor can be rehabilitated through Chapter 11 and emerge as a viable
14 business – that question has been answered by the Trustee in the negative. What is at issue here
15 is whether or not the Debtor should be liquidated through a Chapter 11 plan or through Chapter
16 7.

17 The Trustee's investigation of the Debtor, as detailed in the Motion to Convert and as
18 reported to this Court in Second Status Report of Chapter 11 Trustee Christopher R. Barclay
19 (Dkt. # 435, "Trustee's Second Status Report") and Declaration of Christopher R. Barclay in
20 Support of Second Status Report of Chapter 11 Trustee (Dkt. # 435-1, "Trustee's Declaration,
21 Second Status Report"), makes clear that any Chapter 11 plan that would put Polhill directly or
22 indirectly in control of liquidating assets of the Debtor or of affiliated entities on behalf of
23 creditors could not satisfy the feasibility requirement of 11 U.S.C. § 1129(a)(11). The Trustee's
24

25 ¹ The Commission is conducting a non-public investigation into the activities and conduct
26 of the Debtor and related persons and entities to determine whether federal securities laws have
27 been violated. Notwithstanding the pending bankruptcy case, the Commission is continuing its
28 investigation as an action by a governmental unit to enforce its police and regulatory power in
accordance with the exception to the automatic stay provided at 11 U.S.C. § 362(b)(4). The
Commission has filed a proof of claim in this case. [See Claim No. 98-1].

1 investigation also makes clear that the advantages to be gained through a Chapter 7 liquidation
2 favor conversion of this Chapter 11 case to one under Chapter 7. For these reasons, the
3 Commission believes that it is in the best interest of creditors and the estate for this case to be
4 converted to Chapter 7.

5 II.

6 DISCUSSION

7 A. The Best Interests of Creditors and the Estate Require Conversion of this 8 Case to Chapter 7 Given the Mounting Evidence of Gross Mismanagement 9 and Possible Fraud.

10 The growing body of evidence in this case indicates that Polhill and his direct reports not
11 only grossly mismanaged the Debtor but also may have conducted a large-scale fraud. The
12 evidence indicates that the Debtor and its management may have engaged in securities, tax, and
13 bank fraud and may have manipulated its books and records with respect to creditor claims.

14 1. Securities Fraud

15 On March 19, 2011, the Office of the United States Trustee filed a motion to appoint a
16 trustee and accompanying declarations, which outlined multiple misrepresentations and
17 omissions that had been made by the Debtor, Polhill, and other APFC employees, to investors.
18 [Dkt. # 233, "Motion for Trustee"]. On March 28, 2011, the Commission joined and filed a
19 statement in support of the Motion for Trustee, based on what appeared to be securities fraud.
20 [Dkt. # 246]. Specifically, the evidence outlined in the Motion for Trustee indicated that Polhill
21 signed promissory notes on behalf of the Debtor, which promised investors that their loans to the
22 Debtor would be secured by specific collateral. Unbeknownst to the investors, however, the
23 collateral was often non-existent or otherwise encumbered, leaving the investors with no security
24 for their loans when the Debtor filed for bankruptcy. [See, e.g., Motion for Trustee at ¶¶ 11-22;
25 Dkt. # 231, Declaration of Paul Hazel]. In addition, the Motion to Convert suggests that there is
26 evidence to support investor allegations that the Debtor conducted a Ponzi scheme. For example,
27 the Motion to Convert states that the Trustee's investigation, including his review of a report
28 prepared by, and the Rule 2004 testimony of, Craig Greene, a forensic accountant, lends

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1 credence to investor allegations that the Debtor may have been operating a Ponzi scheme.

2 [Motion to Convert, p. 6, ll. 14-19].

3 **2. Tax Fraud**

4 The evidence gathered by the Trustee suggests that the Debtor, under the control of
5 Polhill, also may have engaged in tax fraud. For example, the Trustee's Declaration, Second
6 Status Report states, "According to Mr. Polhill, in his own words, helping the Debtor's investors
7 avoid payment of income taxes on their purported investment gains on account of investments
8 made by or through the Debtor was 'all part of the game' for those investors who requested it."

9 [Trustee's Declaration, Second Status Report at ¶ 20].

10 **3. Bank Fraud**

11 The Trustee has presented evidence suggesting that the Debtor, under the control of
12 Polhill, also may have engaged in bank fraud. According to the Trustee's Declaration, Second
13 Status Report, in the context of discussing a loan from an Illinois-based bank to Capital Foods,
14 LLC ("Capital Foods") and Polhill individually, the Trustee inquired as to why Capital Foods
15 had loaned \$500,000 to an Illinois-based affiliate of APFC called MWBC. In response, the
16 Trustee relates, "Mr. Polhill equivocated and after providing a series of evasive responses, he
17 finally admitted that the loan from Capital Foods to MWBC existed in paper only - no \$500,000
18 loan by Capital Foods to MWBC was ever made." [Trustee's Declaration, Second Status Report
19 at ¶ 22]. The Trustee states that when he asked Polhill why documentation was prepared to
20 create the appearance of a loan between Capital Foods and MWBC, "he [Polhill] explained that
21 the reason was because the Illinois-based bank required Illinois-based collateral." [Trustee's
22 Declaration, Second Status Report at ¶ 22].

23 **4. Other Suspicious Activity**

24 Finally, the Motion to Convert indicates that, in addition to the potential misconduct
25 outlined above, the Debtor may have engaged in other suspicious activity. According to the
26 Motion to Convert, "on the eve of bankruptcy, the Debtor added more than \$20 million in
27 investor related claims to its books which had not been there before and later listed these
28 additional claims on its bankruptcy schedules as undisputed." [Motion to Convert, p. 11, ll.8-11].

1 The Motion to Convert states that these claims appear to pertain to many creditors who enjoyed,
2 and may continue to enjoy, close business and financial relations with Polhill and affiliated
3 entities. [Motion to Convert, p. 11, ll. 11-13].

4 Given the evidence of potential securities fraud set forth in the Motion for Trustee and in
5 the Motion to Convert, along with the additional evidence of other suspicious activity, including
6 potential tax and bank fraud, any plan that were to leave Polhill in charge directly or indirectly of
7 liquidating assets on behalf of creditors would be objectionable on the grounds that it lacked
8 feasibility and was not proposed in good faith, as required by 11 U.S.C. §§ 1129(a)(11) and
9 (a)(3), respectively. The Commission is strongly opposed to leaving Polhill in control to
10 manage the few assets that he has not already squandered, for the purported benefit of the very
11 creditors whose investments he procured through deceit. In addition to this concern, given the
12 especially poor accounting and documentation maintained by the Debtor of its business
13 transactions [Motion to Convert, p. 3, ll. 14-19; p. 7, ll. 11-13], the Commission would question
14 the integrity of any plan and distribution scheme that the Debtor might propose.

15
16 **B. The Costs of Liquidating in Chapter 11 and the Advantages to Be Gained in**
17 **Chapter 7 Favor Conversion.**

18 The Commission agrees with the Trustee that even a Chapter 11 liquidating plan that does
19 not involve Polhill is not practicable. For this Debtor, the costs of remaining in Chapter 11
20 cannot be justified given that Chapter 7 offers a cost-effective and, in the context of this case as
21 explained below, a superior alternative. According to the Motion to Convert, the Debtor has
22 fewer than six performing assets. [Motion to Convert, p. 5, ll. 17-20]. The Debtor's single
23 largest investment is Capital Foods, but this investment generates no current income or cash flow
24 and the Debtor's voting interest in the entity is a non-controlling interest. [Motion to Convert,
25 p.2, ll. 23-26]. The value of this investment is further undermined by the facts presented in the
26 Motion to Convert indicating that Capital Foods may have been the recipient of at least one loan
27 procured through bank fraud. [Motion to Convert, p. 8, ll. 20-28; p. 9, ll. 1-22]. Put simply, the
28 value of the assets in this case cannot support the costs of liquidating through a confirmed

1 Chapter 11 plan. Consequently, it is difficult to discern how any value would be passed on to
2 APFC creditors if the Debtor were allowed to remain in Chapter 11.

3 Furthermore, as pointed out in the Motion to Convert, a Chapter 7 liquidation has
4 significant advantages in the context of this case. Because a Chapter 7 trustee's administrative
5 expenses would be entitled to priority under 11 U.S.C. § 726(b), a Chapter 7 trustee would be
6 able to investigate further the business transactions of the Debtor and bring avoidance actions as
7 appropriate to recover assets of the estate for the benefit of all creditors with allowed claims.
8 This potentially could stop the distribution of assets to creditors who may have engaged in
9 misconduct and preserve additional assets for those who did not.

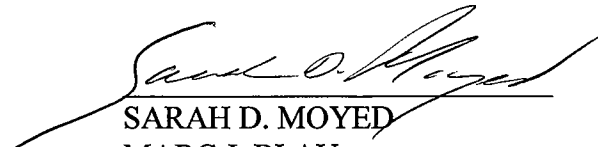
10 **III.**

11 **CONCLUSION**

12 For the reasons discussed above, the Commission supports the Motion to Convert and
13 respectfully requests that this case be converted to a case under Chapter 7.

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15 Dated: December 16, 2011

Respectfully submitted,

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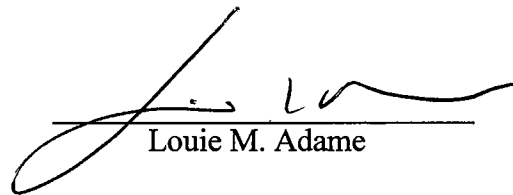
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CERTIFICATE OF SERVICE

On December 16, 2011, I served the following document(s): **U.S. SECURITIES AND EXCHANGE COMMISSION'S STATEMENT IN SUPPORT OF THE CHAPTER 11 TRUSTEE'S MOTION TO CONVERT CASE FROM CHAPTER 11 TO CHAPTER 7**. The document was served by the following means to the persons as noted on the attached service list as printed from the Court's ECF filing system.

I declare under penalty of perjury that the foregoing is true and correct.

Dated: December 16, 2011



Louie M. Adame

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Mailing Information for Case 10-27855-bam

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Manual Notice List

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Click the link above to produce a complete list of **creditors** only.

Mailing Matrix

Click on the link above to produce a list of **all** creditors and **all** parties in the case. User may sort in columns or raw data format.