

1 Thomas W. McNamara (SBN 127280)
mcnamarat@ballardspahr.com
2 655 West Broadway, Suite 1600
San Diego, California 92101-8494
3 Telephone: (619) 696-9200
Facsimile: (619) 696-9269

4 *Court-Appointed Receiver*

5 Andrew W. Robertson (SBN 62541)
robertsona@ballardspahr.com
6 Daniel M. Benjamin (SBN 209240)
benjamind@ballardspahr.com
7 Chrysta L. Elliott (SBN 253298)
elliottc@ballardspahr.com
8 Ballard Spahr LLP
9 655 West Broadway, Suite 1600
San Diego, California 92101-8494
10 Telephone: (619) 696-9200
Facsimile: (619) 696-9269

11 *Attorneys for Court-Appointed Receiver*

12
13 **UNITED STATES DISTRICT COURT**
14 **CENTRAL DISTRICT OF CALIFORNIA**

15
16 FEDERAL TRADE COMMISSION,

17 Plaintiff,

18 v.

19 FORENSIC CASE MANAGEMENT
20 SERVICES, INC., et al.,

21 Defendants.

CASE NO. LACV11-7484-RGK (SSx)

**FIRST INTERIM REPORT OF
RECEIVER**

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1 Thomas W. McNamara, as the court-appointed receiver, hereby submits this
2 First Interim Report to update the Court on the current status of the receivership and,
3 in particular, the course taken since entry of the Court’s Minute Order granting in
4 part and denying in part the motion for approval of a wind down.

5
6 I. Background

7 A. TRO

8 The Federal Trade Commission filed this action against defendants on
9 September 12, 2011. The Court issued its Temporary Restraining Order on
10 September 13, 2011 (“TRO”) (Docket No. 9) appointing me receiver (“Receiver”)
11 with the “full equity powers of a receiver.” Pursuant to that TRO, on September 15,
12 2011, my team took control of the two locations at which the Receivership
13 Defendants were doing business.

14 The TRO authorized and directed me to “[c]ontinue and conduct the business
15 of Receivership Defendants in such manner, to such extent, and for such duration as
16 the Receiver may in good faith deem to be necessary or appropriate to operate the
17 business profitably and lawfully, if at all; provided, however, that the continuation
18 and conduct of the business shall be conditioned upon the Receiver’s good faith
19 determination that the business can be lawfully operated at a profit using the assets
20 of the receivership estate[.]” (§ X(N)).

21 B. Receiver’s Preliminary Report

22 On September 26, 2011, I filed a Preliminary Report (Docket No. 43) in
23 which I reported that “[b]ased on my investigation to date, my conclusion is that
24 deceptive practices – as to clients and debtors alike – are so ingrained in this
25 business that it cannot be operated lawfully, at least in the context of this
26 Receivership.” (Report at 25). I further concluded that “[i]n the context of this
27 Receivership, that model is not salvageable as a lawful business going forward.”
28 (*Id.* at 26).

1 As the business operations were tainted with deceptive business practices, all
2 components of the business must be regarded as tainted – debt assignment
3 arrangements between Receivership Defendants and creditor clients; arrangements
4 between Receivership Defendants and attorneys to whom assigned debts were
5 forwarded; and debt-collection communications between Receivership Defendants
6 and debtors. Given the conclusion that fraud and deception were ingrained in the
7 Receivership Defendants’ operations, it would be impossible to now audit all
8 transactions to isolate any that may not have been directly tainted.

9 C. Preliminary Injunction

10 The Court issued its Preliminary Injunction on September 27, 2011 (Docket
11 No. 38 and 47-1). It reaffirmed that the business should not be operated by the
12 Receiver unless it could be accomplished lawfully and profitably. (§ X(N)).

13 The Preliminary Injunction also contains specific directives that have affected
14 my recent decisions regarding the receivership:

15 • The Receiver is directed to “[c]onserve, hold, and manage all receivership
16 assets, and perform all acts necessary or advisable to preserve the value of
17 those assets, **in order to prevent any irreparable loss, damage, or injury to**
18 **consumers or to creditors** of the Receivership Defendants...” (§ X(D), at
page 18, emphasis added).

19 • The Receiver is directed to “[p]revent the inequitable distribution of assets
20 and determine, adjust, and **protect the interests of consumers and creditors**
21 who have transacted business with the Receivership Defendants.” (§ X(G), at
page 19, emphasis added).

22 • The Receiver is also subject to an important limitation as the Preliminary
23 Injunction recites that “the Receiver shall not attempt to collect or receive any
24 amount from a consumer if the receiver believes the consumer was a victim of
25 the unlawful conduct alleged in the complaint in this matter”. (§ X(B) at
pages 17-18).

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1 D. Ex Parte Application for Approval of Wind Down

2 Given that it was not possible for the business to proceed lawfully, on
3 October 18, 2011, my counsel filed an *Ex Parte* Application for approval of a wind
4 down and liquidation of the office. The premise of this Application was that such a
5 procedure was appropriate to protect the rights of consumers and third-party
6 creditors, and maximize the assets of the receivership given the businesses could not
7 be operated lawfully and profitably going forward. Defendants opposed that
8 Application as premature (Docket No. 52). Plaintiff FTC filed a Statement In
9 Support (Docket No. 51).

10 While this application was pending, my staff responded to specific requests as
11 they came into our office from consumers and attorneys and posted a section on
12 Frequently Asked Questions (“FAQs”) on the receivership website to address most
13 of the common questions. To keep them advised, we sent a global email to all
14 attorneys retained by Receivership Defendants in collection matters to update them
15 on the status of the receivership, to suggest that they advise their respective courts
16 that the matters are stayed by virtue of the receivership, and to contact the
17 Receiver’s office with specific situations needing resolution.

18 E. Data Base to Quantify the Universe of Clients, Attorneys and Debtors

19 Also while the *ex parte* application was pending, we quantified the universe
20 of creditor clients, attorneys and debtors. This universe is large and diverse. During
21 the period November 3, 2011 through November 11, 2011, a team of three – two
22 former employees of Defendants’ and one member of the Receiver’s team –
23 compiled the following databases:

24 a. Creditor Clients. We identified creditor clients who had assigned
25 debt claims to Defendants Commercial Recovery Authority (“CRA”),
26 Rumson, Bolling & Associates (“RBA”) or Commercial Investigations,
27 Inc. (“CII”). This database includes all pertinent contact information
28 about the client (address, phone number, fax, and e-mail) and the

1 principal amount of debts assigned and amounts collected to date. This
2 database includes a large universe - approximately 2,220 for CRA,
3 8,830 for RBA, and 16,690 for CII. Of these clients, we have identified
4 a total of 23,572 who have some form of active claim(s) being
5 processed by Defendants.

6 b. Debtors. We identified all debtors associated with debts
7 assigned to Receivership Defendants. This database includes pertinent
8 contact information for each debtor (phone number, fax and e-mail),
9 the creditor client associated with each debtor, the principal amount of
10 each debt, and any amounts paid to Receivership Defendants by each
11 debtor. The database is sorted into sub-categories of debtors as
12 follows:

13 i. Active Debtors. These are debtors from whom
14 Receivership Defendants were actively attempting to collect as
15 of September 14, 2011 – approximately 2,824 for CRA;
16 approximately 12,321 for RBA; and approximately 22,212 for
17 CII. While some debtors may have multiple debts owed creditor
18 clients of Receivership Defendants, we have not further
19 segmented this database into specific debts. Such an exercise
20 would not be cost-effective and would not materially enhance
21 our knowledge while the businesses remain inoperable.

22 ii. Payment Plans. We have categorized all debtors who
23 were still subject to payment plan agreements with Receivership
24 Defendants.

25 iii. Closed Debtors. These are debtors from whom
26 Receivership Defendants had ceased collection efforts as of
27 September 14, 2011 – approximately 867 for CRA;
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1 approximately 5,900 for RBA; and approximately 10,066 for
2 CII.

3 c. Receiving Attorneys. We identified all attorneys to whom
4 Receivership Defendants had forwarded collection cases for litigation.
5 This database includes all pertinent contact information (address, phone
6 number, fax, email) for each receiving attorney and the creditor client
7 associated with each attorney. We identified approximately 171
8 attorneys to whom Receivership Defendants have forwarded cases
9 representing roughly 1,598 creditor clients.

10 d. Invoices and Statements. Finally, we compiled a database of all
11 client statements generated on the first of each month reflecting
12 transactions on a client's account during the preceding month. This
13 database includes the date each statement was generated, the amount
14 that was paid to Receivership Defendants on each account during that
15 statement period and the amount that was to be remitted to the client
16 during that statement period.

17 F. February 28, 2012 Minute Order Re Motion on Wind Down

18 In the absence of a ruling on the *ex parte* application, my counsel filed a
19 formal noticed "Motion to Approve Wind Down of Receivership Defendants'
20 Business, Liquidation of Furniture and Equipment and Return of Premises to
21 Landlord" on January 6, 2012 (Docket No. 91). The FTC filed a Response in
22 Support (Docket No. 98). Receivership Defendants filed an Opposition raising their
23 due process concerns that such a remedy was premature and requesting that the
24 Court appoint a monitor to "strike a balance between allowing a Defendant to
25 operate its business pending trial and ensuring compliance with the Court's orders"
26 (Docket No. 99, page 2).

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1 By a Minute Order entered February 28, 2012 (Docket No. 120), the Court
2 ruled on that motion, finding that “the suspension of business operations and release
3 of all employees are appropriate” and concluding as follows:

4 In light of the foregoing, the Court **GRANTS in part and**
5 **DENIES in part** the Receiver’s Motion. Specifically, the Court finds
6 that (1) Defendants’ business should remain inoperative, (2)
7 Defendants’ lease on office space at 14532 Friar Street should be
8 terminated, and (3) Defendants’ office furniture and equipment should
9 not be liquidated, but rather placed in storage by the Receiver”.

10 The Court also found Defendants’ arguments “insufficient” to rebut
11 conclusions stated in the Preliminary Report as to unlawfulness.

12 II. Receivership Activities Since February 28, 2012 Minute Order

13 In moving forward, our goal is to cost-effectively proceed with the
14 receivership of an “inoperative” and “unlawful” business whose operations have
15 been suspended and simultaneously protect the interests of consumers defrauded by
16 the Receivership Defendants. Set forth below are the steps we have taken and plan
17 to take since the February 28, 2012 Order.

18 A. The Friar Street Office

19 We are implementing a procedure whereby the leased offices will be returned
20 to the landlord and Receivership Defendants’ assets and documents on site will be
21 broken into four categories – paper business records (most filed in metal file
22 cabinets); computer CPU boxes (with hard drives still installed); other office
23 equipment; and furniture. The paper business records and CPU boxes will all be
24 stored in a nearby self-storage facility which will be accessible as needed as the FTC
25 litigation proceeds; all other office equipment and furniture will be stored in less
26 expensive storage involving containers in a warehouse near the Friar Street facility.

27 Prior to removal, the records and computers will be carefully labeled and
28 inventoried. To the extent possible, we will undertake to return any personal
property to Receivership Defendants and/or employees. We will have this
procedure completed by the first week of April, 2012.

1 B. Creditor Clients

2 The businesses must, at a minimum, remain inoperative until at least trial of
3 the FTC case, which is presently set for January 2013. The Receivership
4 Defendants who operated as debt collectors are, therefore, unable to provide
5 services to the creditor clients who assigned debts to them until at least January of
6 2013. This obviously leaves these consumers without the services for which they
7 contracted with the Receivership Defendants until, at least, January 2013.

8 We are communicating with creditor clients to inform them that the
9 Receivership Defendants will not be in a position to assist until at least January of
10 2013, if ever. We are instructing the creditors to take whatever steps they feel
11 appropriate to protect their rights. If they wish to await the outcome of the trial,
12 they need take no action. On the other hand, if they wish to pursue the debts
13 through another channel, the creditors are being offered the opportunity to “Opt
14 Out” of their assignment agreements with Receivership Defendants. By such a
15 procedure, consumers who Opt Out are free to pursue their debtors directly with no
16 obligation to any Receivership Defendant. Many creditors are already doing this as a
17 “self help” remedy and, indeed, some of the assignment documents used by the
18 Receivership Defendants give creditors the right to withdraw if there is no active
19 debt collection efforts.

20 Some creditor clients have had their assigned claims “forwarded” to an
21 attorney. For these creditor clients who choose to Opt Out, we will provide them the
22 attorney contact information so they may contact the attorney directly if they wish.

23 These procedures provide protection and guidance to consumers who are
24 creditor clients consistent with the Court’s instructions to me in the Preliminary
25 Injunction.

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1 C. Attorneys

2 Our primary message to attorneys handling litigated debt collection cases for
3 Receivership Defendants has been that these cases are “stayed” by the terms of the
4 Preliminary Injunction. This message was relayed in a global email letter to all
5 attorneys in December, 2011.

6 We are following up that letter with a further notice that advises attorneys that
7 (1) cases brought in the names of Receivership Defendants are still stayed by the
8 Preliminary Injunction; (2) Receivership Defendants are unable, until at least
9 January of 2013, to provide them any support for their cases (*e.g.* respond to
10 document production requests and other information about debtors); (3) that we
11 have notified all creditor clients that the Receivership Defendants will remain
12 inoperable until at least January of 2013 and explained the right to Opt Out of
13 assignment agreements with Receivership Defendants; (4) if a creditor client whose
14 case has been forwarded to any attorney opts out, we will provide the attorney that
15 creditor’s contact information so they may contact the creditor directly; and (5) we
16 will continue to respond to individual requests from attorneys for guidance.

17 D. Debtors

18 The Preliminary Injunction (Section X(D) at page 18-19) makes it clear that
19 the Receiver “shall not attempt to collect or receive any amount from a consumer if
20 the Receiver believes the consumer was a victim of the unlawful conduct alleged in
21 the complaint...”. Consistent with this directive, the receivership is making no
22 collection efforts as we regard the entire debtor pool as tainted.

23 E. Processing of Mail

24 The mail of Receivership Defendants is being forwarded to the Receiver’s
25 office by the UPS-type mail drops to which Receivership Defendants had their mail
26 delivered. We are reviewing this mail as it comes in and preserving it in a
27 chronological file system.

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F. In-coming Payments

The mail of Receivership Defendants has included checks which we have handled as follows:

i. Remittance checks from attorneys who have successfully collected on a debt for a creditor client. In most cases, the attorneys have first deducted their fee (usually 25%). We have deposited these checks to the receivership bank account, subject to further determination as to the ultimate rightful owner of these funds;

ii. Checks from attorneys for unexpended costs. We have deposited these checks to the receivership bank account as they represent, in effect, a refund of Receivership Defendant funds previously advanced to these attorneys;

iii. Checks from debtors payable to a Receivership Defendant as payment of a debt owed to a creditor client. We have returned these checks uncashed to the debtors as we must deem them to be tainted by the unlawful collection activities of Receivership Defendants.

III. Financial Summary

To date, the receivership has collected cash funds from frozen accounts of Receivership Defendants totaling \$111,567 with court-approved disbursements of \$94,921, leaving a cash balance of \$17,015. In addition, we have deposited approximately \$74,000 in checks payable to Receivership Defendants which have been delivered to the receivership as described above at Section II(F).

Dated: March 26, 2012

BALLARD SPAHR LLP

By: /s/ Thomas W. McNamara
Thomas W. McNamara
Court-appointed Receiver