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IN THE UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF OREGON

UNITED STATES OF AMERICA, )  
 )  
Plaintiff, ) 3:12-cr-00485-SI  
 )  
vs. ) November 16, 2015  
 )  
JON MICHAEL HARDER, ) Portland, Oregon  
 )  
Defendant. )

(Sentencing Hearing - Phase II)

EXCERPT OF PROCEEDINGS

BEFORE THE HONORABLE MICHAEL H. SIMON

UNITED STATES DISTRICT COURT JUDGE

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1 (November 16, 2015)

2 EXCERPT OF PROCEEDINGS

3 (Open court; defendant present:)

4 MS. KERIN: Thank you, Your Honor. The Government  
5 calls Michael Esler.

6 (The witness was duly sworn.)

7 THE CLERK: Thank you. Would you please state your  
8 name for the record, spelling your last.

9 THE WITNESS: Michael Esler. E-S-L-E-R.

10 DIRECT EXAMINATION

11 BY MS. KERIN:

12 Q Mr. Esler, where are you currently employed?

13 A As an attorney in my law firm Esler, Stephens & Buckley in  
14 Portland, Oregon.

15 Q How long have you been practicing law?

16 A Since 1971.

17 Q And do you have a specialty that you practice?

18 A Yes. We handle plaintiffs' securities cases. It is  
19 probably about 50 percent of our practice. We have been doing  
20 it since I started practicing in 1971. Most of our cases are  
21 for groups of plaintiffs, not just individuals, but small  
22 private placements and some large, as large as  
23 Capital Consultants and Sunwest.

24 Q And has your practice been predominantly within the  
25 District of Oregon?

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1 A Yes. We've been local and stayed that way.

2 Q And have you practiced both in federal court and state  
3 courts throughout the state?

4 A Yes. We prefer state court, but we do visit federal court  
5 when we're called upon to.

6 THE COURT: I won't take that personally.

7 THE WITNESS: Thank you, Judge.

8 BY MS. KERIN:

9 Q And have you received any professional awards or anything  
10 of that nature because of the work that you've done?

11 A Yes. I have received the usual, you know, best lawyer,  
12 super lawyer, benchmark lawyer, those kind of things. My  
13 partners and I have spoken at numerous CLEs and done things  
14 like that. So we're recognized, I think, in the community as  
15 having spent a lot of time doing this work.

16 Q And over the 40 years that you have been practicing  
17 securities litigation on behalf of plaintiffs, has your  
18 percentage been predominantly approximately 50 percent of your  
19 time spent in this area of law?

20 A I would say, yes, 50 percent would be a good estimate.

21 Q Great. Tell the Court a little bit about your role in  
22 Sunwest and how you became involved in that litigation.

23 A Well, Phil Landstrum, who is actually in the back of the  
24 courtroom, came to see us, as I recall, in July or early August  
25 of 2008 and said that he was an investor in one of the --

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1 several of the Sunwest facilities and talked to us about the  
2 fact that they had missed a payment.

3 So we started monitoring the situation with  
4 Mr. Landstrum, and eventually other people came in. We  
5 attended the meetings -- one of my partners attended the  
6 meetings that were held by Sunwest over the Labor Day weekend  
7 in 2008 where they were explaining their cash-flow problem. So  
8 we monitored the case from that point forward, and we filed our  
9 first complaint in October 2008.

10 Q So is it fair to say that you began being involved with  
11 Sunwest sometime in July or August of 2008?

12 A Yes.

13 Q Then you attended or your partner attended a meeting in  
14 September of 2008?

15 A Right, where Mr. Gutzler spoke, and the idea was to get  
16 all of the Sunwest people together and answer their questions.

17 Q And what was the tone of that meeting? What was Sunwest  
18 saying to its investors?

19 A It was saying that things were going to work out, just  
20 wait a while. We will get back on track; we have got a lot of  
21 things in the works that are going to bail you out. The  
22 investors were panicked. This was a very unusual type of --  
23 group of investors. I think there were a lot of very, very  
24 panicked people at that point.

25 Q Why do you say this was an unusual type of investors in

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1 Sunwest?

2 A Well, it had been sold primarily to people approaching  
3 retirement or retirement age, and it had been sold to people  
4 who had generally amassed a retirement net worth in real  
5 estate. This would be people -- I think the typical person was  
6 probably 67 years old, had owned a couple of fourplexes or  
7 maybe a couple of duplexes that they bought when they were  
8 young and then refurbished and built up a little bit of a net  
9 worth, a nest egg in real estate.

10 Then as they approached retirement and wanted to turn  
11 over the property management responsibilities to someone else,  
12 they found that they could do a 1031 exchange into property  
13 managed/real estate managed by someone else and then just  
14 collect rent. So the typical investor was at a position where  
15 they couldn't do without the income stream. They counted on it  
16 as part of their retirement. They couldn't replace the income  
17 stream, and so they were suddenly living on their  
18 Social Security and, you know, had a substantial reduction in  
19 the quality of their lives. So these were very, very upset  
20 people; very alarmed people.

21 Q And you indicated in October of 2008 you filed a lawsuit,  
22 I assume, in state court, your preferred venue?

23 A Yes. We filed in state court. We filed against  
24 Davis Wright, and we had evolved a strategy. When the case  
25 came into the office, we recognized all the hallmarks of a

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1 Ponzi-like scheme. We couldn't say that it was a pure Ponzi  
2 scheme, because there were assisted living centers.

3 But in terms of what we could see, particularly in  
4 the way that Sunwest was approaching the problem, was that this  
5 had been operated as a unitary enterprise. It hadn't been  
6 operated as 300 separate assisted living centers. It had been  
7 operated as we have one common bank account, we are going to do  
8 refinancings, and then the money will go into the one common  
9 bank account. In addition, as we sell new assisted living  
10 centers to investors, the money from those are going to go into  
11 one common bank account, because that's the way they were  
12 approaching the solution to the problem. They were going to do  
13 a refinancing, or they were going to sell some assisted living  
14 centers. They were going to have a plan to put the money back  
15 into a unitary bank account and pay investors. So that's kind  
16 of what we recognized.

17 The investors, on the other hand, didn't want to  
18 recognize that they had lost everything and that everything was  
19 in jeopardy. There were people that were clinging to the  
20 belief that their unit of the unitary enterprise might have  
21 value. So in those early days there were a lot of very  
22 confused people and very anxious people, and so we had to deal  
23 with those issues.

24 Q How many investors did you represent in the lawsuit in  
25 October 2008?



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1 A I think we had five or six in the first lawsuit. We  
2 evolved a plan pretty quickly as we started to realize the  
3 scope of the problem. What we decided would be the most  
4 efficient way to handle the case was to take token cases, and  
5 so we identified three token cases that we filed against  
6 Davis Wright, and then we negotiated a tolling agreement with  
7 the law firm.

8 We didn't sue Jon Harder and his family and the  
9 principals of Sunwest because we were aware that they were in  
10 the process of filing bankruptcy. So we didn't want the case  
11 to get bogged down and stayed because one of the defendants was  
12 in bankruptcy, but we knew we were going to sue Jon Harder if  
13 he wasn't in bankruptcy in all of the cases.

14 Q I assume you made that clear to Mr. Harder and the Sunwest  
15 Enterprise as well?

16 A Yes. Pretty early on I started talking to Steve English  
17 and the people at Bullivant Houser who were representing  
18 Jon Harder at that stage of the case. So I didn't let them  
19 have any misapprehension about the fact that we would sue  
20 Harder in a heartbeat if he wasn't in bankruptcy.

21 Then we filed a token case against the Texas law  
22 firm, Thompson & Knight. They had done tax opinions, and they  
23 had done about 30 offerings. Then we filed -- because  
24 K&L Gates wouldn't agree to a tolling agreement, we filed a  
25 class action against K&L Gates and one of the accounting firms

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1 that were involved. So in total, we filed five cases before  
2 December 31st.

3 Q And what were the remedies that you were seeking and that  
4 you indicated to the Sunwest and Mr. Harder's lawyers you would  
5 seek?

6 A It was a restitutionary remedy that's provided under the  
7 Securities Act. That is, the investors get all of their money  
8 back, plus interest at the rate that was stated in the  
9 security, which was 10 percent per annum plus 2 percent per  
10 year.

11 Q What did you believe that that figure amounted to at the  
12 time that you were filing your lawsuits?

13 A Well, in terms of the entire group, we knew that the  
14 starting number was \$450 million. Harder had said that  
15 publicly, and that seemed to be consistent with the information  
16 that we were able to get in the early stages of the case, about  
17 \$450 million of investor money, TIC investor money mostly, but  
18 some of it was preferred membership money as well.

19 Q Over time -- and we will talk more about how much time was  
20 spent on this case. But over time, did the number of investors  
21 you represented increase?

22 A Yes, and that was for a variety of reasons. But by  
23 the end of the case, we had about 450 investors. When I say  
24 that, if it was a husband and wife, we are counting that as one  
25 unit. So we actually had more investors. And if you counted

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1 every limited liability company, you know, we had a lot more.

2 Q And you described your general observations about the type  
3 of investor and how they were unusual. Would it be fair to say  
4 that that description applied to the 450-plus investors that  
5 you represented over the course of the SEC proceedings?

6 A Absolutely. You can look in the courtroom and see the age  
7 of the people. This is not a program that was targeted to  
8 young people because it was going to produce income. So you'd  
9 get your 10 percent per annum. It would be rent. You would  
10 have to deal with it as ordinary income. It wasn't going to be  
11 deferred; it wasn't going to be capital gains. There were some  
12 young people, but not very many. Mostly it was for people  
13 retiring who were turning over their real estate from active  
14 management to passive management.

15 Q You've indicated that you had channeled to Mr. English and  
16 the other lawyers who represented Mr. Harder that you were  
17 refraining from suing them because you believed that they were  
18 going to go into bankruptcy?

19 A Yes.

20 Q Is it fair to say that this lawsuit that you filed really  
21 moved things along with respect to the reorganization and the  
22 filing of the bankruptcy?

23 A Well, I would like to think so. You know, the thing about  
24 that stage of the case was, there were a number of people who  
25 believed if they got their assisted living center back from

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1 Harder, that they could do better than Harder. So at that  
2 stage things were pretty confused. Then you had the added  
3 problem of -- there were people living in these assisted living  
4 centers, and they were in jeopardy. They were in harm's way.

5 So one of the concerns that we had, as plaintiffs'  
6 lawyers, having an ethical duty to sort of the universe, was  
7 that litigation couldn't become so important that the people  
8 that were actually in the assisted living centers weren't well  
9 cared for, weren't taken care of, didn't have daily meals. So  
10 I think that tempered the way in which we approached Harder a  
11 little bit.

12 Q And at the time did you understand that the Lone Star sale  
13 was already being negotiated?

14 A Yes. We didn't understand where the money was going to  
15 go. We understood that the Lone Star deal was out there and  
16 that it was going to provide some working capital to get the  
17 chief restructuring officer going, but we knew that it wasn't  
18 to last long; that the properties were operating at a negative  
19 cash flow, if you looked at them as a unit overall; and that  
20 they had been operating at a negative cash flow since 2000.

21 So we were very concerned about how this was going to  
22 continue. We called the SEC in September, shortly after the  
23 Gutzler meeting is my best recollection. We called the SEC in  
24 San Francisco and said that you really need to look at this;  
25 this needs to have a real receivership, because we didn't trust

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1 the Lone Star sale and the deal that was being worked out with  
2 Harder and the chief restructuring officer. And more  
3 importantly, our clients didn't trust it, because here they had  
4 been lied to by the people that formed Sunwest. They had been  
5 lied to by Harder, and they were concerned that the Lone Star  
6 deal and the chief restructuring officer were just a smoke  
7 screen that Harder was going to be able to hide behind: "Oh,  
8 look, I'm helping you all out, but I'm taking the money from  
9 the Lone Star deal."

10 Q So before we talk about that in a little more detail, can  
11 you describe for the Court how many hours over the course of  
12 your career have you spent understanding Sunwest and the SEC  
13 proceedings and the receivership and bankruptcy proceedings?

14 A In the space of about three years, I think I've spent over  
15 3,000 hours working on the case. It was about 50 percent of my  
16 practice. At times, it was 100 percent. You know, my firm  
17 itself spent, you know, over 4,000, 5,000 hours. I was,  
18 by far, the person who spent the most time, but our paralegals,  
19 my partners, we were all in on this case as it continued.

20 Q So back to the Lone Star sale. You've mentioned a little  
21 bit about what the investor perspective was with respect to the  
22 Lone Star sale. Once the details came out, what was the  
23 investor perspective and your perspective with respect to the  
24 Lone Star sale?

25 A Well, it was more or less a necessary evil. The idea that

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1 Harder would contribute back his interests into the unitary  
2 enterprise was not something that we accepted as being an act  
3 of generosity. He owed the money back. He didn't own Lone  
4 Star without the fact of -- the Lone Star properties -- without  
5 the fact that the rest of the enterprise had supported those  
6 properties.

7           Because of the way the thing was being operated, it  
8 should have just been an asset of the overall unitary  
9 enterprise of Sunwest. But because of the need to keep people  
10 fed, the need to keep the operations going in order for there  
11 to be any realizable value, we didn't push the buttons to try  
12 to block the Lone Star deal, and, you know, I don't know that  
13 we could have, given Judge Hogan's control of the case at that  
14 point.

15 Q    With respect to the chief restructuring agreement, what  
16 was your perspective as counsel for the investors?

17 A    Well, I didn't like the idea that it was in fact going to  
18 be treated more as a loan than it was just part of the assets  
19 of Sunwest. This operation had been commingled since -- we  
20 knew at that time -- Kraus. We knew the Kraus litigation.  
21 That was part of our individual complaint that we filed for the  
22 Landstrums. We had studied the Kraus litigations, had gotten  
23 transcripts of the hearings, and we read the testimony of  
24 Mr. Harder.

25           So we were very familiar with what he had done up to

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1 2003. Then when we saw the way the thing was unfolding in  
2 2008, you know, it appeared that he had just continued to do  
3 exactly what he had done up until Judge Mosman's trial, except  
4 he paid off Kraus before a final judgment was entered and got  
5 rid of him.

6           So we were very concerned that this would all be used  
7 as a sham to avoid what should be done, which was that any  
8 asset that Harder had should be back into the pool. It should  
9 be pooled, and it should be used by the investors and by the  
10 receiver for the interest and benefit of the investors.

11 Q    You mentioned a loan, and that's the provision in the CRO  
12 agreement where --

13 A    Yeah. Then the payment of his defense costs. I mean,  
14 that was, you know, not something that we thought was  
15 appropriate.

16 Q    And what about the monthly stipend that the CRO allowed  
17 that was eventually permitted in the bankruptcy and SEC  
18 proceedings?

19 A    That single provision was probably what created some of  
20 the most anxiety among the investors, because when they saw  
21 that -- I mean, I think that's one of the reasons why so many  
22 investors tried to get their own property. People like  
23 Hawthorne Gardens and Victory Hills and Carnegie Village were  
24 operations, and I know about those because I later  
25 represented -- I still represent the Victory Hills people.

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1 They were able to successfully get their property because it  
2 was worthless. It was worth far less than the debt against it.

3 But what drove those people was their mistrust of the  
4 chief restructuring officer, who entered a deal to pay Harder  
5 \$54,000 a month. That really was a bad move politically and  
6 otherwise. It made it very difficult to keep people involved  
7 with the receiver and not trying to get their own property. I  
8 spoke at several meetings that the chief restructuring officer  
9 held where he tried to persuade people not to sue to get their  
10 own property back but to get along with a roll-up plan where  
11 all of the assets would be disposed of for the common good. It  
12 was very difficult, given that the common good of Jon Harder,  
13 seemed to be preeminent in the restructuring plan.

14 Q Now, you have indicated that you filed the lawsuits  
15 against the professionals initially before the receivership  
16 proceedings and the bankruptcy proceedings.

17 A Yes.

18 Q What was your role and the role of the other lawyers who  
19 represented victims in these third-party recovery suits?

20 A Well, our role is a little bit different. Most of the  
21 other lawyers -- Gary Grenley and Paul Connolly were the two  
22 other principal law firms involved in bringing lawsuits. They  
23 were not seeking damages in most of their litigation. They  
24 were seeking to get the property back.

25 They had a conflict in their groups because most of



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1 their people thought that if they could get their assisted  
2 living center out, it must be able to be able to be operated  
3 profitably. They weren't right. I think perhaps \$100 million  
4 worth of assisted living centers and other projects were  
5 actually taken out of the receivership because the receiver  
6 determined that they were operating at a loss and didn't have a  
7 value to the receivership estate and the investors wanted them.  
8 So at various stages we would meet, but eventually Judge Hogan  
9 said he was going to take control of the litigation, the  
10 third-party litigation that we were operating under, and so  
11 Connolly and Grenley dropped out.

12 Q And that's a good point. Once the SEC receivership  
13 proceeding was filed, Judge Hogan took control of the  
14 bankruptcy as well as the SEC proceeding?

15 A Yes. What had happened was we had stayed in touch with  
16 the SEC. We called them in September. They began an  
17 investigation. They came up and interviewed some of our  
18 clients and then eventually took statements from them to  
19 support the filing of the complaint.

20 We had worked with the SEC pretty closely in some of  
21 our other cases, like the Capital Consultants case, and so we  
22 were familiar with the Allen Matkins firm and had a lot of  
23 respect for the people that they had that handled the  
24 Capital Consultants receivership. We saw this as being a very  
25 similar situation, where there is a lot of real estate, and we

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1 were going to have to come up with a plan and try to preserve  
2 the value as much as we could. We had worked with David Osias,  
3 who was at Allen Matkins, and who is a really brilliant lawyer.  
4 So he came up as the principal lawyer for the Sunwest case for  
5 the SEC.

6 Q At some point Judge Hogan ordered that all claims be  
7 subject to mandatory mediation; is that correct?

8 A Yes. When the SEC filed the receivership action in  
9 March 2009, they based it on the complaint that we had filed  
10 for the Landstrums back in October of 2008. Then they came up  
11 with their standard SEC receivership form of order.  
12 Judge Hogan, in Jon Harder's interests, refused -- Jon Harder's  
13 attorneys objected to the form of order. They wanted control  
14 to be in the hands of the chief restructuring officer under the  
15 CRO agreement, and that was eventually adopted by Judge Hogan,  
16 that position. So the SEC didn't get the control that they  
17 would ordinarily have in this type of receivership.

18 Q So the same benefits that were in the CRO agreement to  
19 Mr. Harder remained during the course of the receivership?

20 A Yes.

21 Q In addition, Mr. Harder had his attorneys' fees paid  
22 throughout the receivership proceeding?

23 A Yes. And, boy, you know -- we saw the attorneys at the  
24 hearings and at the meetings, and we saw the group meetings  
25 that took place at the Bullivant Houser firm, but it was an

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1     astounding amount of money.

2     Q     In your experience, your 40 years of being in securities  
3     litigation, was that an unusual provision or thing to occur in  
4     a case like this?

5     A     Yes. You know, certainly a person in the position of  
6     Harder could resist the efforts of people to take over his  
7     operation, but the SEC has extraordinary powers to protect  
8     investors by statute, and in other situations they didn't  
9     provide the assets of the estate could be used to pay the  
10    defense costs of the defendant.

11    Q     I think you testified about this before and you kind of  
12    talked about it in your last answer, but this idea of  
13    Mr. Harder contributed to his interests in the  
14    Sunwest Enterprise to the receivership. What is your response  
15    as representing more than 450 investors and being a lawyer for  
16    40 years in this area?

17    A     Well, it is nonsense. I mean -- the fact is we sued third  
18    parties as opposed to suing Harder. If we could sue a third  
19    party, Harder would be absolutely liable if the third party was  
20    secondarily liable. So Harder was faced with \$450 million  
21    worth of claims by investors and then going up at the rate of  
22    10 percent per annum paid monthly plus 2 percent per year. So  
23    it was an astonishing mountain of liability that Harder was  
24    faced with.

25                 So I didn't see how Harder had any basis to negotiate

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1 because he had no strength. His position had no strength.  
2 What we would have done in a case like this, if there was no  
3 SEC, and we have done this in other cases, we would have  
4 negotiated directly with Harder in order to try to save the  
5 assets, but we wouldn't have given the assets to Harder as a  
6 part of that process.

7 Q Thank you. I wanted to ask you a question about -- a  
8 little bit -- provide the judge a little bit of background  
9 about the mechanics of the Blackstone sale, and it is true that  
10 there was an initial lower offering to purchase the properties  
11 that became part of the Blackstone sale; is that correct?

12 A Yes.

13 Q Then what happened?

14 A Well, you know, our role was the third-party litigation,  
15 the relationship parties, but we were representing 450  
16 investors. So they would talk to me about what was going on as  
17 far as the Blackstone deal was concerned, and I had constant  
18 contact with the receiver at that stage. You know, my  
19 understanding was that Blackstone came up with a deal. The  
20 deal got worse after Blackstone came out to look, and that's  
21 not unusual with venture capital groups. They'll suck you in  
22 with what looks like a good term sheet, and then they come out  
23 and do their due diligence, and they start whittling it down.  
24 That, in fact, happened.

25 So the steering committee that was working with the

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1 receiver -- in fact, it split. Bill Brian, as I recall, and  
2 one of the other members of the committee went out to get a  
3 better offer and did find a better offer. But Judge Hogan at  
4 that stage, I think, had decided he wanted to get this done, he  
5 wanted to get it done rapidly, and refused to entertain the  
6 better offer.

7 Q What was the effect on the ultimate Blackstone response  
8 once the competitive bid that was obtained by the steering  
9 committee came forward?

10 A I think that Blackstone stopped -- they were continuously  
11 reducing the amount that they were going to pay. I think it  
12 started out at 300 million, and then it went down to  
13 277 million. It continued to go down, but I think that that  
14 maybe brought it to a conclusion.

15 Q We have heard or we have seen in the briefing that some of  
16 the investors who were able to roll over into the Blackstone  
17 investments received 100 percent of their MIMO claim.  
18 Based on what was happening at the time in the receivership,  
19 why weren't investors, based on your experience, rolling over  
20 into the Blackstone deal?

21 A My recollection is that about 11 percent of the investors  
22 rolled over into the Blackstone deal. There was no way that a  
23 responsible investment adviser or an attorney representing the  
24 investors could say rolling over to the Blackstone deal made  
25 sense. In fact, the Blackstone deal wasn't a whole lot

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1 different than the Sunwest in the first place. You had all of  
2 your eggs in one basket. You didn't have any promise of  
3 income. There would be no income stream. So the very same  
4 people who had been hurt by the original Sunwest deal, with the  
5 loss of the income and the fact that they weren't diversified  
6 were going to continue to be undiversified. So while the  
7 Blackstone deal might give a younger investor an opportunity to  
8 gamble that they could get their money back, for the older  
9 investors, it was a no-win proposition. You couldn't recommend  
10 that they continue to have their assets tied up in one sector  
11 of the economy, with a venture capitalist as a partner, any  
12 more than you could recommend that they do it with Jon Harder  
13 as a partner. You couldn't trust Blackstone.

14 Q Were there investors that you represented who needed the  
15 money at the time as well?

16 A Absolutely. There is no income stream from the Blackstone  
17 deal, and so most investors did not have a choice. They had to  
18 take the payout transaction, because sitting and hoping that  
19 maybe Blackstone will do something profitable for Blackstone  
20 and for the investors in three or four years was something that  
21 they could not do.

22 Q Based on your experience representing the victims in this  
23 matter, did it appear that some victims were simply  
24 apprehensive or didn't trust their instincts regarding  
25 additional investments at the time given their experience with

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1 Sunwest?

2 A Well, yes. This investment was sold as an affinity to  
3 an affinity group. It was basically started out as a Seventh  
4 Day Adventist offering. So many of the people that had gotten  
5 burned had really placed a lot of trust in the fact that they  
6 were all part of the same group with Jon Harder, and so they  
7 felt very betrayed. So the idea of continuing to have funds at  
8 risk anywhere was pretty scary to them. Then given the way  
9 that the Blackstone deal had come down with Blackstone starting  
10 out at a high number and then whittling it down, it didn't  
11 build up any trust with anybody either.

12 Q I want to switch topics real quick. The Court has heard  
13 testimony, and we've briefed the issue about the MIMO  
14 analysis. I know you are familiar with that, correct?

15 A Yes.

16 Q And you have read some of the letters that have been  
17 presented by Mr. Harder's lawyers in the SEC proceeding as well  
18 as the submissions in this case, correct?

19 A Yes.

20 Q And you've read Mr. VanSpeybroeck's letter wherein he  
21 indicated that the individuals who invested in Blackstone will  
22 receive more than 100 percent of their investment. Do you  
23 recall that?

24 A Yes.

25 Q What is your concern about the MIMO analysis and the

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1 representation that it has made the victims whole or that  
2 they've received 60 percent?

3 A Well, it is just not true. First of all --

4 Q Why is that?

5 A -- under the MIMO analysis that was adopted in this case,  
6 it was based on a Ponzi-scheme analysis. So what the receiver  
7 did was he said, "I'm not going to sue investors who got money  
8 between January 1st, 2006 and the date of the receivership or  
9 the date payment stopped, July 2008. I am not going to sue  
10 people to recapture the money. But what I'm going to do is say  
11 that anybody that got money after January 1st, 2006 was  
12 essentially getting money from other investors," because this  
13 was being operated as a quazi-Ponzi scheme. The investment  
14 wasn't bearing the payout to the investors. It was new  
15 investors that were bearing the payout to the investors.

16 So they adopted a MIMO approach, and that's generally  
17 the time value of money versus the idea that the money payments  
18 that you received came from other investors. It is kind of a  
19 toss-up in my mind about which one is the most fair, but a MIMO  
20 approach is recognized by courts. And as this area of  
21 litigation has evolved over the last 20 years, it has become  
22 universally accepted.

23 But it isn't the measure of damages. I mean, these  
24 were people who had invested with a promise that they get 10  
25 percent paid monthly. They thought it was real estate, so they



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1 it was secure. They thought it was diversified because they  
2 put their money in three or four different assisted living  
3 centers. They didn't understand diversification at all.

4 But they thought, "We are safe, we are secure, it is  
5 real estate. Even if Sunwest goes south, we can take our real  
6 estate and get some else to manage it." So the real measure of  
7 damages was the amount they invested plus the interests that  
8 they weren't paid from July 1st, 2008 forward.

9 You know, we all spin doctor a little bit. So when  
10 someone says there was a 61 percent recovery for the people who  
11 cashed out, and there was 100 percent recovery or better than  
12 100 percent recovery for the people in the Blackstone deal,  
13 that's really not true. The reality is that the people that  
14 cashed out probably got something along the order of 35 cents  
15 on the dollar, because they didn't get their interest, and they  
16 got deductions for any payments they received after  
17 January 1st.

18 The other thing that is misleading about all of this  
19 is that, of the money that was distributed to the people who  
20 got the 61 percent of their MIMO amount, about half of that, or  
21 maybe 40 percent of that, came from the third-party recoveries.  
22 It didn't come from the receivership pooling together the  
23 assets and selling. That was a portion of what their  
24 distribution was.

25 But the lawyers and their insurance companies put in

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1 52 and a half million dollars to that pot. Then the  
2 stockbrokers and the accounting firms put in another \$15  
3 million or \$20 million. Then we went after the officers,  
4 Mike Deines and some of the other principal officers, and they  
5 gave up their primarily preferred membership interests, but  
6 they gave up their interests, 100 percent of their interests,  
7 or 80 percent of interest, depending on the level of  
8 culpability that they had. So the reality is that it took a  
9 lot of other things to get people maybe 40 cents on the dollar,  
10 if you really measured their true damages. It took a lot of  
11 other elements.

12           Then as far as the Blackstone deal is concerned, it  
13 really was an investment into a new security of whatever your  
14 claim was worth. It wasn't worth 100 cents on the dollar when  
15 you invested. It was worth what I would call the 40-cent  
16 distribution that some people took out in cash. No economist  
17 would say, "Oh, yeah, they got all their money back." No.  
18 They made a new investment with Blackstone, where they  
19 otherwise could have taken 40 cents on their real damages.  
20 Instead of taking that off the table, they put it into a new  
21 investment that was worth 40 cents when they invested. It  
22 wasn't worth 100 cents. So it is wrong to say that.

23 Q   In addition, based on your experience in talking with your  
24 clients as the interest was being paid prior to July 2008, is  
25 it fair to say that most people were taxed on that amount as

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1 regular income?

2 A Yes. So that's another part of the equation. As they  
3 were stalled up through the fall of 2008, these are people that  
4 had paid taxes on payments they received from January 1st, 2006  
5 forward, which were really a return of principal, and it should  
6 not have been treated as interest or rent payments and treated  
7 as ordinary income. They should not have been taxable at all.

8 Now, some of the people were able to amend their  
9 returns, but I know that most people did not. So they lost the  
10 tax value -- the tax increments that they paid on the  
11 investments going back before 2006, because it was always a  
12 return of principal. It was never really income.

13 Q I have two other areas of inquiry, and then I will let  
14 counsel ask you questions. The first is something you've  
15 discussed about this return of property to investors. I think  
16 that you said that some investors were successful in obtaining  
17 the properties, correct?

18 A Yes.

19 Q How many properties do you believe were returned to  
20 investors?

21 A I think it was somewhere between 30 and 40. That's my  
22 best estimate.

23 Q Based on your 3,000 hours of reviewing Sunwest, were these  
24 investors' claims incorporated into the receiver's MIMO  
25 analysis?

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1 A No.

2 Q What did the investors have to do in order to get the  
3 properties back?

4 A They had to assign their claims back to the receiver. We  
5 spoke at public meetings that the receiver and chief  
6 restructuring officer had to tell people not to do it. But  
7 many people were so concerned and still believed that if they  
8 got their assisted living center out, as a standalone  
9 operation, it would be profitable. They thought, even though  
10 they were tenants-in-common, which when I was in law school was  
11 a malpractice to set up with tenancy in common with multiple  
12 owners, because it requires 100 percent unanimity to do  
13 anything. Despite all of those problems, they were so  
14 concerned, I think, that this receivership was going to turn  
15 into another sham that they took their property out and tried  
16 to operate it. That reduced the total claims, the  
17 \$450 million plus interest that we would have had as a starting  
18 point. That probably reduced it by close to \$100 million.

19 We've continued to represent many people. They came  
20 back. We didn't represent them when they took their property  
21 out; we refused to. But then they came to us afterwards and  
22 said, "We are stuck; we are being foreclosed." Most of those  
23 things just ended up in foreclosure. Hawthorne Gardens here in  
24 Gresham. One of the last deals that Harder did, Victory Hills,  
25 in Kansas City; Carnegie Village in Missouri, these things

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1 turned into -- I mean, the medical school up in Walla Walla,  
2 they turned into total disasters.

3 The people who ended up with them -- the people in  
4 the receiver group had anxiety. We had meetings, and we talked  
5 to them probably an average of every two to three weeks. We  
6 would have a group telephone call so they could hear what was  
7 happening and be encouraged by the fact that somebody was doing  
8 something for them. But the people that took their property  
9 back had the nightmare continuing.

10 Victory Hills, for example, we negotiated a deal  
11 because the property was worth 4 million; the bank loan was 7  
12 and a half million. The partner that Mr. Harder had in the  
13 project paid off the bank -- paid the bank \$3.6 million and  
14 then told the investors, "I am now going to foreclose; pay me  
15 seven and a half million dollars," which is what the bank note  
16 was. So the torture is continuing for many of the investors  
17 who got their own property back.

18 The other thing that you have got to remember, for  
19 many of these people, they have this hidden recapture of gain  
20 from their fourplex that they operated when they were younger  
21 and able to manage their own property. So they are facing a  
22 bankruptcy situation when, as, and if the property gets  
23 foreclosed or gets sold for what it is really worth, which is  
24 about half about what the bank debt is. So it continues.

25 Q Finally, you indicated, again, that you have been involved

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1 in cases of this size, including Capital Consultants as well.  
2 Based on your experience and knowledge of the professionals who  
3 were involved in the Sunwest case, is this recovery miraculous  
4 and unprecedented based on your experience?

5 A No. It is very similar to the recovery and maybe not even  
6 as good as the recovery in Capital Consultants. There,  
7 Judge King and the SEC worked for -- I think the case is  
8 probably still open, but it is virtually done -- but they  
9 worked long and hard at trying to sell the properties on an  
10 individual property basis and over the years. I think that if  
11 you do the same spin doctoring and use a MIMO analysis, that  
12 that recovery is 90 cents or above. And again, it was same  
13 thing. There was -- part of it came from the property and a  
14 huge part of it came from third parties, who put new money back  
15 in, so that the investors didn't suffer a complete loss. Those  
16 were lawyers, accountants, and other professionals that put  
17 together the deal.

18 MS. KERIN: Thank you, Mr. Esler. I have no further  
19 questions.

20 THE COURT: The defense may inquire.

21 MR. SCHATZ: Thank you, Your Honor.

22

23

24

25

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1 CROSS-EXAMINATION

2 BY MR. SCHATZ:

3 Q Good morning, Mr. Esler.

4 A Good morning.

5 Q You filed the lawsuit involving Mr. Landstrum, I believe,  
6 sometime in October of 2008; is that correct?

7 A Yes, October 10th, as I recall.

8 Q Were you at that time in communication with Mr. Harder and  
9 Mr. Harder's attorneys?

10 A I think I was.

11 Q Were you at that time concerned about what was going to  
12 happen with respect to the assisted living facilities in which  
13 Mr. Harder had an ownership interest across the nation?

14 A Well, yes.

15 Q Did you discuss with Steve English, Mr. Harder's attorney,  
16 the prospect of the entities going into bankruptcy?

17 A Yes.

18 Q Was the purpose of the entities going into bankruptcy to  
19 forestall them from being foreclosed against or forestall  
20 secured creditors from foreclosing against those entities?

21 A Yes.

22 Q Was that a concern of yours that these assisted living  
23 facilities, of which I take it many of your clients had  
24 interests in, were at risk of being foreclosed against?

25 A Yes.

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1 Q In the event of a foreclosure, was it not the case that  
2 your clients, the TIC investors, would basically have been  
3 flushed out? They would have lost their interest?

4 A Yes.

5 Q Were you supportive of the plan that Mr. English, on  
6 behalf of Mr. Harder, was trying to put together at that point  
7 in time in terms of reorganization of Sunwest?

8 A I was supportive of parts of the plan, and we actually sat  
9 down and mapped out where we thought the money could come from  
10 for investors to recoup some of their losses.

11 Q That being you -- "we sat down" -- that was yourself and  
12 Steve English, correct?

13 A Yes. And we saw that part of the money would come from  
14 the attorneys and accountants who had helped make this possible  
15 and that part of it would come from Harder walking away from  
16 his interests, to the extent he had really any legitimate  
17 interests. It was always my concern that Harder should not be  
18 rewarded for having created this enterprise that was a  
19 fraudulent enterprise created by him and that for him to be  
20 rewarded in any way was reprehensible.

21 Q Absolutely, absolutely, Mr. Esler. And that is your  
22 opinion, is it not, sir, today in this courtroom under oath?

23 A Yes.

24 Q Good.

25 Now, let's go back with respect to the plan that was



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1 being put together. Among the things that you were then  
2 discussing -- this is way back now in October 2008 with  
3 Steve English -- was these third-party lawsuits against law  
4 firms and accountants who were part of this whole mess, as  
5 you've described it; is that correct?

6 A Yes.

7 Q So even at that point you were thinking about, "I'm going  
8 to file lawsuits against the lawyers," Davis Wright Tremaine  
9 and the other law firms that were involved in this particular  
10 situation, that had been involved in the marketing of the  
11 investments?

12 A Yes. If you look at the first complaint we filed, we did  
13 not name Harder. We would have named Harder, but he was going  
14 into bankruptcy. That's what we understood, and so we didn't  
15 name him.

16 Q That was the Landstrum complaint. Is that what you were  
17 referring to?

18 A Yes.

19 Q When was it that you actually filed against Davis Wright  
20 Tremaine if you can recall?

21 A October 10.

22 Q October 10th?

23 A 2008. In the Landstrum lawsuit, they were named. That  
24 was our Davis Wright complaint. We filed two more Davis Wright  
25 complaints. We filed one against K&L Gates, the class action

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1 that I mentioned, and we filed one against Thompson & Knight.

2 Q Were the K&L Gates and the Thompson & Knight lawsuits all  
3 filed then in October of 2008?

4 A No. They were filed -- because it took quite a bit of  
5 time. This is a very complicated case. So as we were piecing  
6 it together, we would file each of the complaints as quickly as  
7 we could, because we were concerned that they be filed within  
8 three years of the date of sale so that we didn't have somebody  
9 arguing the date of discovery statute should have run.

10 Q And with respect to these lawsuits, Davis Wright Tremaine,  
11 K&L Gates, and Thompson & Knight, were any depositions taken at  
12 all?

13 A I don't think so.

14 Q Were any interrogatories filed?

15 A No. Most of them were in state court, so interrogatories  
16 weren't allowed. We used document production.

17 Q Were requests for admissions filed?

18 A No.

19 Q A lot of negotiation?

20 A Yes. A lot of discovery.

21 Q A lot of discovery.

22 A We spent hundreds and hundreds of hours going through the  
23 files of Davis Wright, K&L Gates, Sunwest, and Thompson &  
24 Knight. Thompson & Knight was primarily done by the SEC. We  
25 divided responsibilities for the cases. So they did the

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1 documents from Thompson & Knight, which weren't on a search  
2 engine. Actually 40 boxes of documents were produced. So  
3 Steve Walters, who was representing that part of the case for  
4 Allen Matkins, went through them and picked out the hot  
5 documents. Then so he got ill, and so I took the depositions  
6 of the two attorneys at Thompson & Knight in Texas that had  
7 been primarily responsible.

8 Q Primarily responsible for what, sir?

9 A Doing the offerings and doing the tax opinions.

10 Q Do you remember the names of those two attorneys that you  
11 took their depositions personally?

12 A Yeah -- I don't remember their names. The woman did the  
13 securities opinion for Thompson & Knight and the attorney that  
14 did the tax opinion, I did both of their depositions.

15 Q Other than the occurrence of their involvement in this  
16 case, is Thompson & Knight a credible law firm, in your  
17 opinion?

18 A Yeah. The thing about it, Oregon securities laws are far  
19 more protective than the laws of other states. Lawyers who  
20 prepare offering materials in Oregon are liable, whereas in  
21 other states, under other state law, that's not the case. So  
22 in the case of Thompson & Knight, they weren't happy with the  
23 offering materials. We found volumes of e-mails where they  
24 said, you know, that the disclosures aren't adequate, there  
25 should be a chart, they should follow the SEC Industry Guide 5.

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1 Q Who were those e-mails addressed to?

2 A To the people at Sunwest.

3 Q Like whom? Who were they addressed to? Name an e-mail  
4 recipient that you saw an e-mail that was addressed to a person  
5 at Sunwest from Thompson & Knight that you reviewed possibly  
6 used in one of these depositions. Who was it addressed to?

7 A It was addressed to Weintzen, Thurber. Those are the  
8 names that come to mind. I am sure there are others --  
9 Biesiadecki. There were a number of people at Sunwest that  
10 were direct contact people that Thompson & Knight dealt with,  
11 and they were sent to Dozois at Davis Wright.

12 Then there were e-mails back and forth between Dozois  
13 and Thompson & Knight where they discuss the inability to get  
14 information from Sunwest. In particular, they wanted  
15 performance records. They wanted Sunwest to show how well it  
16 had performed over the years, for example, from 2000 to 2006 so  
17 that you could show that there was some legitimate basis for  
18 the projections that were attached to each of the offering  
19 circulars which showed that they had a break-even point within  
20 two years. So they wanted to say, "Well, okay, if that's the  
21 case, then let's see the performance records from previous  
22 operating entities to see how long it took them to reach  
23 stabilization," I think is the term that they used.

24 And they couldn't get them. There is one e-mail that  
25 I recall where the attorney at Thompson & Knight says to

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1 Tim Dozois, "Were you able to get performance charts?" Dozois  
2 says, "Boy, you too? They wouldn't give them to me either."  
3 Then when we got into the Sunwest records, we found the  
4 performance records. They did have performance charts. They  
5 did know how badly they were doing.

6 Q What was the date of that e-mail that you just referred to  
7 where Mr. Dozois stated, "Oh, me too"?

8 A That's the fall of 2007.

9 Q Did you interview Mr. Dozois?

10 A No.

11 Q When you are talking about Mr. Dozois, he was at that  
12 point in time a partner of Davis Wright Tremaine, correct?

13 A Yes.

14 Q The lawsuits that you have filed against the third parties  
15 ultimately resulted, as you've indicated, in substantial  
16 recoveries from the law firm's insurers; is that correct?

17 A Yes.

18 Q Did Mr. Harder contribute to that recovery in any way?

19 A Not really.

20 Q Not in your opinion?

21 A Well, you know, he allowed summary judgment to be entered  
22 against him; I guess you could say that. So that established  
23 the predicate act of a seller liable. So that helped in the  
24 litigation.

25 We didn't interview Mr. Harder, as I recall, for the

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1 litigation, and the receiver had the authority to waive  
2 attorney-client privilege. So there was some assistance  
3 because he wasn't -- summary judgment had been granted against  
4 him. And so in that respect, he was of some help.

5 Q Some help because a summary judgment had been granted  
6 against him by Judge Hogan?

7 A Yes.

8 Q And when was that?

9 A My recollection is that the order entering it was about a  
10 week before we did the Davis Wright mediation, the actual  
11 physical mediation.

12 Q That resulted in the settlement?

13 A Yes.

14 Q You referred to a meeting in September of 2008 where  
15 Mr. Gutzler spoke?

16 A September 2008. I think it was Labor Day weekend.

17 Q Right. You did not attend that meeting but some --

18 A My partner did.

19 Q Your partner did. Mr. Gutzler was speaking on behalf of  
20 Sunwest?

21 A Yes.

22 Q Do you recall who else spoke at that meeting?

23 A No. I don't think Jon Harder spoke at it.

24 Q In addition to the income stream that your clients, as  
25 investors, received from their Sunwest investment, were they

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1 also deferring capital gains taxes through those investments?

2 A Yes. That was the main selling feature. What happened  
3 was, the IRS had changed the code in 2002. They issued -- they  
4 hadn't changed the code, but they issued a rev. proc. that said  
5 that up to 35 people could co-own a piece of property, as long  
6 as it wasn't a partnership. So you could go from a single  
7 ownership of a fourplex to one of 35 people owning an assisted  
8 living center without a change of character of the ownership or  
9 property, and so you didn't have to realize the capital gains.  
10 It would be buried in your next investment. You could roll it  
11 over as long as you did it according to the exchange rules.

12 Q That's rev. proc. 2002-22 that you are referring to?

13 A Yes. So then the Tenancy-In-Common Association, and I  
14 think Sunwest was a member, and I think that Jon Harder went to  
15 the meetings. The TICA association, the national association,  
16 started to publish guidelines about, okay, now that you are  
17 taking these real estate investments, here is the due diligence  
18 requirements, and you should make sure that the investors who  
19 get into them are suitable for the investments and so forth and  
20 so on.

21 One of the TICA blurbs said that you should have a  
22 due diligence report done. So what we found in the Sunwest  
23 files was that Jon Harder did have a due diligence report done  
24 by a company called MIC & Associates. They were a Kansas group  
25 that were primarily retired SEC members, and they acted as

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1 consultants. They'd come in and do a due diligence report that  
2 brokers and dealers could then rely on. So Jon Harder did have  
3 that done.

4 Q He also had the Rose report, too, didn't he, or are you  
5 not that familiar?

6 A I don't know that I have seen the Rose report.

7 Q Isn't it the case that with respect to a Section 1031  
8 capital gains deferral transaction that the deferral can be  
9 basically indefinite? You can roll it over until death,  
10 whereupon heirs can take the property and then mark it up?

11 THE COURT: A stepped-up basis.

12 BY MR. SCHATZ:

13 Q A stepped-up basis.

14 A A stepped-up basis, yes.

15 Q And that was part of the attractiveness of the type of  
16 investment that was being offered by Sunwest, was it not, to  
17 your clients?

18 A No, I don't think so. I mean, what the Sunwest program  
19 was, was that the property would be sold within two to three  
20 years. What Sunwest said was, "We have a system for operating  
21 these assisted living centers. That's why we can charge  
22 7 percent management fees. We are better than anyone else.  
23 And when we take them over, they can go from below break-even,  
24 which is 85 percent occupancy or thereabouts. They go from  
25 below break-even to above break-even within two to three years,



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1 and then we sell them."

2           What the MIC report showed was that was not true.  
3 Then when Sunwest did its own management report in 2006, it  
4 showed that that wasn't true; that they had always operated at  
5 a loss; and that the question of whether a single assisted  
6 living center operated profitably or not had nothing to do with  
7 how long Sunwest owned it.

8 Q     And I understand that. But now we understand, from your  
9 clients' perspective then, they were aware that their Sunwest  
10 investment that they bought into was going to come to an end,  
11 correct?

12 A     They were aware that within two to three years, it would  
13 be sold. Then they believed they would an option of getting  
14 into another investment or taking the money out and paying the  
15 taxes.

16 Q     Again, sensibly, it would be another Section 1031  
17 investment?

18 A     Perhaps. It just depends on the person's needs at the  
19 time.

20 Q     Did any of your clients roll over their investments within  
21 Sunwest?

22 A     Several did, but that wasn't really the actual operations  
23 of Sunwest. In fact, we tried to kind of get a picture of  
24 Sunwest. We did a chart. This is kind of a Venn diagram.  
25 What it shows is that the Sunwest sales to investors and the

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1 number of assisted living centers starting in 2005 at this low  
2 level skyrockets up through June/July of 2008. They were  
3 selling investments in June 2008, even though they didn't make  
4 the July payments. The reason for the skyrocketing, the reason  
5 it had to grow this way, is because it operated at a loss. So  
6 in 2002, it operated at a loss, a \$7 million loss, but it was  
7 made up by new sales.

8 THE COURT: Although when a new sale closed, wasn't  
9 the sales price used basically to supply the down payment for  
10 the purchase of the real property with the balance being  
11 financed? So how would a new sale bring in new money to the  
12 unitary enterprise that you've described?

13 THE WITNESS: There is \$150,000, as I recall, fee  
14 that was charged for due diligence and finding the property.  
15 That was maybe by CDE. Then there was a \$250,000 fee that was  
16 charged by CCI. Then there usually were reserves that were  
17 required by the lender. Then in many cases there were capital  
18 improvements needed, and so those would be in the budget from  
19 the lender. Those funds were all then placed into Sunwest's  
20 account.

21 It seems to me that when you have an escrow closing,  
22 and you have a lender putting in, say, \$7 million, which  
23 includes these fees, and you have the investors putting in,  
24 say, \$2 million, and it all goes into the same escrow. To  
25 parse it out and say that, Well, some of that money that was

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1 being used by Sunwest for the improvement reserve and some of  
2 it for the rent reserve and some of it for the fees only came  
3 from the lender is really kind of a fiction, because although  
4 you could say there's a paper trail created to set it up that  
5 way, it all came out of the same bank account, the same escrow  
6 account, and whether it was the investor dollar that came out  
7 or the lender dollar, it really didn't matter.

8 THE COURT: Thank you.

9 BY MR. SCHATZ:

10 Q With respect to the Lone Star sale, you were aware that  
11 that was being negotiated in the fall of 2008?

12 A Yes. We were aware that a sale of property was being  
13 negotiated. We weren't privy to the negotiations or the terms.

14 Q And the purpose of that sale, as you described it, was to  
15 provide working capital for the CRO to continue to operate the  
16 business, correct?

17 A Well, that was a secondary purpose. I think the primary  
18 purpose was to pay off GECC, because they were threatening  
19 foreclosure, and they would go after Mr. Harder, who had  
20 personally guaranteed the GECC loan.

21 Q And if the payoff of the GECC loan had not been  
22 accomplished, what would have happened to the investors in the  
23 facilities that were being operated at that point in time with  
24 live residents in them?

25 A I don't know, because the SEC receivership could have

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1 accomplished perhaps the same result. I don't know. I do know  
2 that the group of Lone Star owners who were primarily insiders  
3 that had worked with Mr. Harder for a long period of time, and  
4 we felt that one of the really outrageous side effects of a  
5 Lone Star deal was that they got paid off 100 cents on the  
6 dollar. They got paid off profits, substantial profits.

7 Q Who is "they" that are getting paid off here?

8 A My recollection is -- I don't know that I can recall the  
9 names, but there were, as I recall, eight Lone Star owners.  
10 Seven of them were kind of a small cadre. Dunn seems to be one  
11 of them.

12 Q How many of the Lone Star dollars did Mr. Harder put into  
13 his own pocket -- his pocket -- walked away with, went home  
14 with and counted the money? How many of those dollars?

15 A From the Lone Star deal?

16 Q Correct.

17 A Well, as I understand, it is over \$6 million for his legal  
18 fees.

19 Q I'm talking about what he put in his pocket.

20 A \$54,000 a month, as I recall.

21 Q How many of those \$54,000 a month checks have you actually  
22 seen?

23 A I haven't seen any of them.

24 Q How many, to your knowledge, as you sit here today, sir,  
25 on the witness stand and under oath, how many of those payments

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1 were actually made?

2 A I don't know.

3 THE COURT: Excuse me one second. May I ask the  
4 courtroom security officer, was there a problem with that  
5 gentleman wanting to come in?

6 COURTROOM SECURITY OFFICER: I was going to stick him  
7 in the overflow courtroom.

8 THE COURT: He can come in.

9 BY MR. SCHATZ:

10 Q I understand your position that there was this fraud and  
11 therefore Mr. Harder had no interest whatsoever, but back in  
12 October, November, and December 2008, as a matter of law, sir,  
13 just as a matter of law, not just saying that they are not  
14 subject to being attacked, et cetera, but just as a matter of  
15 law, did Mr. Harder have legally recognizable interests in the  
16 entities that were sold in the Lone Star sale?

17 A Yes.

18 Q Was Mr. Harder's signature needed in order for that sale  
19 to go forward to sell the properties?

20 A I don't know.

21 Q You have had 40 years of experience as a securities lawyer  
22 and are well known and very well respected in the legal  
23 community here. Given that Mr. Harder had legal interests in  
24 those properties, if he had decided to stand on them, would  
25 that have prevented the Lone Star sale from going forward?

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1 A Well, it would have delayed it, but I don't know that it  
2 could not have been accomplished simply in a receivership, an  
3 SEC receivership, or a voluntary receivership by Sunwest.

4 Q So the receivership actually came into place in March of  
5 2009; is that correct?

6 A Right.

7 Q So that would have been many months later that we would  
8 have this receivership situation arising?

9 A Yes.

10 Q And we would have then had under this kind of scenario  
11 litigation concerning each of these properties and each  
12 interest in the properties and whether they could be sold or  
13 not, again, based on your experience?

14 A Perhaps. But I don't know what the SEC would have done.  
15 I don't know how things would have played out with GECC if  
16 things had not gone the way they did go.

17 Q You were in communication with the SEC as of September of  
18 2008, correct?

19 A Yes.

20 Q You interacted with them continuously, did you not, from  
21 September 2008 all the way through March 2009, correct?

22 A Yes.

23 Q You talked about the fact that there were promissory  
24 notes -- a provision, I think, in the CRO agreement for  
25 Mr. Harder's turnover of interests, and he would receive a

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1 promissory note bearing, I think, a 9 percent interest rate.

2 Do you recall that?

3 A Well, I became aware that what Harder and the chief  
4 restructuring officer, who was selected by him, had negotiated  
5 was a deal that if Harder gave up interests, then he would have  
6 a right to recover. If he gave up money, he would have a right  
7 to recover money.

8 Q Well, the prosecutor asked you specifically about these  
9 notes. Do you remember that inquiry?

10 A Yeah.

11 Q Have you ever seen one of these notes?

12 A No.

13 Q To your knowledge, was ever such a note issued?

14 A Don't know.

15 Q Are you a tax lawyer in any way, sir?

16 A No. I mean, I have familiarity with some of the issues  
17 that were involved in 1031 exchanges. The tax code has driven  
18 much of my practice over the years. I mean, we went from  
19 investment tax credits in the 1970s to growing credits in  
20 1980s. The tax code drives a lot of litigation.

21 Q If Mr. Harder just simply gifted the money from the  
22 Lone Star sale to Sunwest, would not there have been tax  
23 consequences that the CRO and later the receiver would have to  
24 address?

25 A Well, I think the suggestion is absurd. But going down

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1 that path, I'll say maybe. But I think he probably had a  
2 greater liability than his share of the Lone Star transaction  
3 and probably would have withdrawn more capital from the  
4 entities than the Lone Star transaction.

5 Q Have you conducted yourself, sir, or accountants hired by  
6 you, have you conducted a study over the years at Sunwest of  
7 the amount of monies that, as you say, were withdrawn by  
8 Mr. Harder from Sunwest?

9 A No, we didn't. The receiver did, I think.

10 Q You think?

11 A Yes.

12 Q But you don't have any knowledge of what the result of  
13 that study was?

14 A Oh, I don't know the precise details, but I do know that  
15 one of the things that GECC said, I think, in the summer of  
16 2007, if not earlier, was that Harder can't commingle funds.

17 Q We're not talking about commingle. My question was --

18 A Mr. Harder was to --

19 THE COURT: Wait. Hold on. Since I said, "Hold on"  
20 first before you stood up, I am going first.

21 MS. KERIN: Of course.

22 THE COURT: We are trying to have a good record  
23 maintained here. Let me both ask counsel and the witness to  
24 avoid speaking over each other. So if one of you is speaking,  
25 the other one must refrain.



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1           Now that I have interrupted everything, Ms. Kerin,  
2 did you have anything to say?

3           MS. KERIN: My only objection was that the witness  
4 should be able to complete his answer before Mr. Schatz asks  
5 another question.

6           THE COURT: So both people will now refrain from  
7 speaking over the other.

8           You may continue with your next question, Mr. Schatz.

9           MR. SCHATZ: Thank you, Your Honor. My apologies and  
10 my apologies to Mr. Esler.

11           THE WITNESS: My apologies as well.

12 BY MR. SCHATZ:

13 Q My question was, just so I can recall it to myself, are  
14 you aware, as you sit here today, of any study that was  
15 conducted with respect to Mr. Harder's withdrawal of money from  
16 Sunwest over the period of time, shall we say, from 2002  
17 through 2008?

18 A I believe that the receiver did do a study.

19 Q But you are not personally aware of what result came from  
20 that study?

21 A I think I probably knew at one point, but it is not in my  
22 mind right now.

23 Q You don't know. We talked about lawyers' fees on a number  
24 of occasions. Part of the understanding that was reached  
25 ultimately, and I believe as part of the overall agreement with

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1 the receivership, is that Mr. Harder's attorneys would be paid  
2 from assets of Sunwest as they were sold; is that correct?

3 A That's my understanding and recollection.

4 Q Did you yourself file a fee application with the Court,  
5 with Judge Hogan, seeking fees in the amount of  
6 approximately -- I think it was \$1.7 million?

7 A Yes. We actually filed, I think, four fee applications.  
8 That was first. That was after three and a half years of work  
9 or three years of work on the case.

10 Q And you filed four applications?

11 A Yes.

12 Q In total, what did you request that you receive from the  
13 receivership assets in funds as attorney's fees for you and  
14 your firm?

15 A We requested a fee calculated on a common fund basis of  
16 25 percent of the funds that we had been able to recover. We  
17 estimated the total recovery from the work that we had done at  
18 about \$70 million.

19 We filed an hourly fee claim as well. I mean, we  
20 said, "Here are the hours; here is our normal billing rates."  
21 Ultimately what happened is Judge Hogan knocked out about  
22 \$50,000 worth of time and paid us at our hourly rates, of  
23 course, three and a half years after we had done the work, or  
24 some of it. So we got a recovery based on our hourly rates  
25 minus the \$50,000.

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1           Then I think as his last judicial act, because he  
2 knew we were pretty upset about the situation -- if you operate  
3 a small law firm, you can imagine the problem of lawyers  
4 devoting 50 percent of their time to a case for years and not  
5 getting paid anything for it until the very end and then only  
6 getting an hourly fee. So I think as his last judicial act he  
7 paid us an additional \$50,000.

8   Q    Wasn't it \$75,000?

9   A    It could be. Your memory could be better than mine.

10   Q   How much in total was your firm paid out of the assets of  
11 the receivership for your work?

12   A   My best recollection is about 2 million, 2,100,000,  
13 somewhere in that ballpark.

14   Q   That was on what you call your hourly rates and hourly  
15 rates of people working with you?

16   A   Yes.

17   Q   And what was your hourly rate?

18   A   \$450 an hour, I think, at that point. My partners were a  
19 little bit less, \$400 an hour.

20   Q   And those fees were paid to you for your work as approved  
21 by Judge Hogan?

22   A   Yes.

23   Q   Did Judge Hogan approve the fees that were paid to  
24 Mr. Harder's lawyers?

25   A   I think so. I think that was part of it the way the

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1 transaction worked.

2 Q Do I understand you correctly, sir, that with respect to  
3 Sunwest's rollover member LLC and the sale of assets to  
4 Blackstone, that you advised your clients not to participate in  
5 that activity?

6 A Well, we aren't investment advisers, but we were telling  
7 our clients that, among other things, putting all of your eggs  
8 in one basket and putting them in the control of somebody that  
9 owes you no fiduciary duty is a risky venture; it was when you  
10 did it with Jon Harder. You can do it, if you care to. And if  
11 you can take the risk and understand the risks, you can do it  
12 with Blackstone. We didn't advise them one way or the other  
13 that they should do it, but it would be -- you know, it would  
14 be pretty quixotic to jump from Harder to Blackstone.

15 Q So in other words, you advised your clients that the  
16 result of participating in the Sunwest rollover member LLC  
17 would be just like your investment in Sunwest, and it was going  
18 to end in an failure?

19 A No, I didn't say that. I said it was risky; it is  
20 extremely risky. Unless you have the ability to diversify,  
21 choosing to go with no income for another unlimited period of  
22 time with the hopes that Blackstone is going to treat you  
23 fairly at the end of the day is a big risk, and you should  
24 consider whether you can afford that risk. Most of the people  
25 could not afford it, in my opinion.

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1 Q Now, you indicated that most of the people couldn't afford  
2 it and didn't have a choice. How many investors/former  
3 investors of Sunwest were you representing at the time that you  
4 were giving this recommendation or advice concerning the  
5 Sunwest rollover member LLC? How many?

6 A Probably 450.

7 Q 450. How did you make the determination that most of the  
8 450 investors that you were representing didn't have a choice?  
9 Did you conduct a demographic analysis of what available assets  
10 they had at the time?

11 A No. But we were pretty familiar with the needs that they  
12 had for cash flow and the fact that they hadn't had the 10  
13 percent per annum paid monthly for years. We were aware that  
14 many of the people were ill. Many of the people were retired  
15 and living on fixed incomes. Some of them had to sell their  
16 houses. I mean, we were aware of the general plight of the  
17 people we represented, and we were aware of their ages. We did  
18 not tell anybody not to do it, and we didn't tell anybody to do  
19 it. But we did try to make sure that people understood the  
20 level of risk.

21 Q Did you, in fact, create some kind of dossier on each of  
22 your clients which listed out and identified what their asset  
23 values were separate and apart from Sunwest?

24 A No.

25 Q The MIMO analysis we discussed, was that ultimately

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1 approved by the Court?

2 A Yes.

3 Q You indicated that you conducted an analysis with respect  
4 to other principals of Sunwest; Mr. Deines, you mentioned him  
5 by name --

6 A Yes.

7 Q -- for the purpose of determining their level of  
8 culpability so as to decide how much of their interests they  
9 ought to get back, they ought to be able to take out of  
10 Sunwest; is that correct?

11 A That's one way of putting it, yes.

12 Q With respect to Mr. Deines, what was your determination  
13 concerning his level of culpability?

14 A That he was right up there close to Jon Harder in terms of  
15 culpability, but not to the same extent.

16 Q Was he allowed then, without objection from your clients,  
17 to receive funds out of the receivership?

18 A We reached a compromise with Mr. Deines and with the other  
19 principal officers that they could keep 15 percent, as I  
20 recall, of their preferred membership interests, and they could  
21 be treated on a MIMO basis if they actually put money in. But  
22 if they were just awarded as part of their retirement by  
23 Jon Harder, we felt with the cost of litigation, they weren't  
24 entitled to anything as far as we were concerned, but the cost  
25 of litigation would have exceeded the 15 percent.

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1           By that time Judge Hogan really wanted to get the  
2 plan adopted. I think it was close to the sale to Blackstone.  
3 So the issue of getting this resolved and getting it resolved  
4 very quickly was one that ran it through. So by giving them  
5 what would have amounted to the cost of defense, you know, we  
6 felt it was a reasonable thing for the investors to do.

7 Q       And in that group was Mr. Curtis Brody also involved?

8 A       Yes. I think he could have been 75 percent, but maybe he  
9 was 85 percent -- 85 percent given back to the investors. He  
10 walked away from most of his ownership interests.

11 Q       But still retaining 15 percent?

12 A       That's my best recollection. We had a chart that was  
13 prepared. The CRO and I worked on it, and then he went back  
14 and did the actual negotiations with the officers.

15 Q       How about Mr. Gutzler? Was he one of the individuals in  
16 your culpability analysis?

17 A       I don't think so.

18           THE COURT: Let me interrupt here for a moment.

19           Mr. Schatz, you are welcome to take as much time as  
20 you reasonably need. Let me ask you, can you give me an  
21 approximate or estimate of how much additional time you will be  
22 using for this examination?

23           MR. SCHATZ: Probably another 15 minutes, Your Honor.

24           THE COURT: I think we should take our 15-minute  
25 mid-morning recess now. We will be back in 15 minutes. Come

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1 back, please.

2 All right. Thank you.

3 (Recess.)

4 (Open court; proceedings resumed:)

5 THE COURT: All right. Mr. Schatz, you may continue.

6 THE WITNESS: One thing, Your Honor.

7 THE COURT: All right.

8 THE WITNESS: Mr. Schatz, you had asked about the  
9 e-mails about the prior performance tables and giving investors  
10 information. Weintzen asked for prior performance information,  
11 and Kevin Thomason was the lawyer down at Thompson & Knight who  
12 asked for prior performance information. And Tim Dozois also  
13 asked for prior performance information. They had an e-mail  
14 dialogue where Dozois says, "I vow not to repeat, once again,  
15 my admonitions to update the prior performance tables." Kevin  
16 Thomason said, "Prior performance? Do you intend to provide  
17 any past performance information? You should, but we may not  
18 have time to collect it." And then Kevin Thomason responds to  
19 Dozois later and says, "You too? You couldn't get it either?"

20 So, yes, the outside lawyers were trying to get prior  
21 performance information from Mr. Harder, and so were the people  
22 at the internal brokerage firm that was operated by Sunwest,  
23 CFF.

24 MR. SCHATZ: Thank you, Mr. Esler. Can I have an  
25 opportunity to look at the e-mail that we are referring to?



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1 THE COURT: Of course.

2 MR. SCHATZ: Mr. Esler has apparently utilized it to  
3 refresh his recollection.

4 THE COURT: Of course. Counsel for the Government is  
5 welcome to come up too and take a look, if they want.

6 THE WITNESS: What I have here is series of  
7 submissions that we put together during the mediations.

8 BY MR. SCHATZ:

9 Q I would like to see the e-mail that you just showed.

10 A I quote the e-mail. I don't have the e-mail right here,  
11 but I quote the e-mail.

12 Q So we don't have the e-mail here?

13 A No. We had it as an attachment to the document --

14 THE COURT: Wait, wait. One at a time.

15 MR. SCHATZ: Sorry. I apologize.

16 BY MR. SCHATZ:

17 Q Where is the e-mail?

18 A Well, I'm sure that it is in the computer database. I'm  
19 sure that there is probably a copy somewhere in my office, but  
20 we mostly destroyed the actual physical documents after the  
21 case was over because they were produced mostly through  
22 protective orders.

23 Q All right. So this document we are looking at, this is  
24 part of the memo you created with respect to the Davis Wright  
25 Tremaine litigation?

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1 A Yes.

2 Q And in this memo you are referring to a communication that  
3 went back and forth between Mr. Dozois and Kevin Thompson.

4 A Thomason.

5 Q Thomason, of Thompson & Knight?

6 A In 2006, yes. August of 2006.

7 Q All right. I'm missing it. I'm old, and I can't see  
8 really well. Where is Mr. Deines' name in here? The next  
9 page.

10 A Mark Weintzen's name is CCF, Canyon Creek Financial, which  
11 was the internal brokerage. "Mike Deines, the president of  
12 CCD, was concerned and raised the issue that the pro formas  
13 they were using were misleading." That's what Deines said in  
14 his internal e-mails.

15 THE COURT: Mr. Esler, if you can move the microphone  
16 a little closer to you.

17 THE WITNESS: Yes.

18 BY MR. SCHATZ:

19 Q Let's turn back for just a sec here to the Dozois/Thomason  
20 e-mail. When was that e-mail?

21 A August of 2006. It was a series of e-mails, and they were  
22 talking about the challenges that they faced in getting  
23 information from Sunwest.

24 Q Based on that information, you came to a conclusion, did  
25 you not, that you set forth in the memo?

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1 A Yes.

2 Q Is that conclusion down here at the bottom of this bolded  
3 paragraph which begins "DWT"?

4 A Yes.

5 Q Would you read that conclusion into the record, please.

6 THE COURT: Slowly, please.

7 BY MR. SCHATZ:

8 Q Please. Slowly, yes.

9 A "So after they couldn't get the information, we concluded  
10 that this was a major red flag that DWT should have stopped  
11 doing offerings. Alternatively, DWT should have warned  
12 investors that Sunwest had resisted providing prior performance  
13 information and that this was an important reason not to  
14 purchase securities from Sunwest."

15 Q Okay. Now, in your memo there, with respect to that  
16 particular paragraph, what information did you have at that  
17 time that Sunwest had resisted providing performance data?

18 A We had the Weintzen --

19 Q Weintzen --

20 A "In October of 2006, Mark Weintzen" -- so this is a month  
21 later or two months later -- "president of CCF" -- and before  
22 that, a lawyer at Davis Wright -- "asked Sunwest's finance  
23 department to provide past performance information to  
24 prospective investors that included the occupancy rate at  
25 acquisition and currently" -- because the Sunwest story was

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1 that we have a better system; we improve occupancy.

2 "Investors, Weintzen understood, knew that the financial  
3 success of Sunwest's facilities depended on occupancy. We know  
4 from statements by Dozois and the board minutes that he  
5 understood this obvious proposition as well."

6 Q Again, referring to Mr. Dozois of Davis Wright Tremaine?

7 A Yeah.

8 Q But where in there is there reference to an e-mail or to  
9 an executive decision on the part of the principals of Sunwest  
10 not to provide performance information?

11 A Well, the Mike Deines reference as well. Then what Dozois  
12 had said and what Thomason had said. Dozois answered, "I vow  
13 not to repeat, once again, my admonitions to update the prior  
14 performance tables." Kevin Thomason responded, "You too, huh?"

15 So they weren't getting it. Then when they finally  
16 did get it, they didn't use it because of what it showed was  
17 that there was no Sunwest effect and that's --

18 Q Other than a communication between the two lawyers,  
19 Mr. Dozois and Mr. Thomason, did you find an e-mail between  
20 Mr. Dozois and any of the principals at Sunwest concerning  
21 these performance valuations?

22 A Well, I think so. I think we found it in the reference to  
23 Mark Weintzen. Then ultimately he does put together a prior  
24 performance chart, or Sunwest does, and then we, in the next  
25 part of the memo, show that -- that prior performance showed

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1 that there was no Sunwest effect and that the vast majority of  
2 their assisted living centers had below an 85 percent  
3 occupancy, and so they were below break-even.

4 Q In the course of your testimony you referred to  
5 Hawthorne Gardens. Were some of your clients involved in the  
6 Hawthorne Gardens facility?

7 A We had some clients who were invested in Hawthorne Gardens  
8 as well as other facilities. We wouldn't represent them with  
9 respect to Hawthorne Gardens because the Hawthorne Gardens  
10 owners decided they were going to take over the operation of  
11 Hawthorne Gardens. That would be inconsistent with our  
12 representation of clients who wanted to pool.

13 Q Was the Hawthorne Gardens facility foreclosed against, to  
14 your knowledge?

15 A I don't know. I know that they were having incredible  
16 problems as recently as two years ago, and it may have been. I  
17 don't know.

18 Q It may have been, but you don't know?

19 A No.

20 Q So as far as you know today, sir, Hawthorne Gardens could  
21 still be in existence with its residence still operating?

22 A Right. But what we do know about Hawthorne Gardens and  
23 what I did know at the time was that Hawthorne Gardens was  
24 under water. It had a below break-even point of operations;  
25 that it was going to require additional capital to continue to

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1 keep it floating if you took it out; and that the owner of  
2 Hawthorne Gardens, which is one of the last purchases by  
3 Harder, had said to the newspapers when Sunwest first hit the  
4 news, he said, "Well, they made me an offer I couldn't refuse,"  
5 and that was consistent with what we had figured out.

6           The average assisted living center/facility cost  
7 \$65,000 a door. That's how they measure replacement costs. By  
8 the time that Harder got done in 2008, he was buying units at  
9 \$125,000 a door. In other words, more than the replacement  
10 value if you wanted to build a new one.

11 Q Do you have any training whatsoever in the evaluation of a  
12 assisted living facility in terms of its unit price per door?

13 A Well, I do, on-the-job training.

14 Q Any formal training?

15 A Well --

16 Q Have you ever assisted in an appraisal of an assisted  
17 living facility?

18 A Yes. I have worked with appraisers to get appraisals of  
19 assisted living center facilities.

20 Q So you had appraisers working for you that provided you  
21 the data?

22 A Yes.

23 Q Did you have an a appraisal done of the Hawthorne  
24 facility?

25 A No.

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1 Q You indicated that the medical school is not operating  
2 anymore. It is closed?

3 A No, I didn't say that. I said I think that the owners  
4 lost their investment in the medical school.

5 Q You think?

6 A Yes.

7 Q Do you know that as a matter of fact?

8 A Well, I have had several people that were in the medical  
9 school call me and talk about what a disaster it had turned  
10 into.

11 Q Did you represent any of those individuals?

12 A Yes, but not in the medical school, because they wanted to  
13 get the medical school out and operated themselves.

14 Q Well, sir, you are an attorney with 40 years of  
15 experience, and you know how important it is, when you testify  
16 under oath, that you be accurate.

17 A Yes.

18 Q Do you have any knowledge, as you sit here today, as to  
19 the status of the medical school?

20 A Other than what I've told you, no.

21 Q You spent many hours of analysis and investigation into  
22 the law firms that had been employed by Mr. Harder and Sunwest,  
23 and you brought lawsuits against three of the primary firms,  
24 and in particular, Davis Wright Tremaine. One of the points  
25 made in the lawsuits was that Sunwest had engaged in making

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1 loans between its facilities, and that was something that  
2 shouldn't have been allowed. In what way, in your opinion, did  
3 that activity reflect back on Davis Wright Tremaine as the  
4 primary author of the operating memorandum?

5 A Well, that's a pretty general question, but let me see if  
6 I can take it apart and answer it. What we saw was that funds  
7 from new projects were being used to pay the losses in other  
8 projects. Then we saw the Michael -- the MIC report. I don't  
9 think his first name was Michael. It wasn't Michael Mic, but  
10 it was the MIC report which corroborated that, that new funds  
11 from new investments were being used to support the old  
12 investments.

13 Then we saw the internal report that was done by  
14 management at Sunwest in 2006 for the period 2002 to 2004, and  
15 we saw the same thing; that they, in their own analysis,  
16 determined that they needed new investor money and new  
17 closings, whether they took it from the loan amount or whether  
18 they took it from the investor amount, they took it from  
19 escrow. They needed that to keep supporting, because the older  
20 operations were operating at an overall loss, and the loss kept  
21 going up every year, because as they acquired more facilities,  
22 they acquired more losses.

23 So we saw that pattern, and we said, you know, this  
24 ultimately isn't a question of whether somebody is breaching  
25 his fiduciary duty as in the Kraus case, but this is a question



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1 of disclosure. If you're operating at a loss and you're  
2 showing people projections that say you're going to be  
3 operating at a profit in two years or less, and you are telling  
4 people that you have a Sunwest plan that goes into effect when  
5 you take over these units, and they become profitable, if you  
6 are telling people that, when in fact you're operating at a  
7 loss and you're covering up the losses from new investor money,  
8 you're not making an adequate disclosure. You're misleading  
9 people. That's what we thought. It wasn't a question of  
10 whether there was a legal right to take the money. It was a  
11 question of disguising the loss.

12 Q With that in mind, sir, when you wrote in the lawsuit that  
13 name, Davis Wright Tremaine, as a defendant, at page 4, you  
14 wrote, "DWT participated and materially aided in the sales of  
15 the above-described securities to plaintiff class."

16 A Yes. They prepared the documentation that was used with  
17 the investors. Prince v. Brydon and Computer Concepts v.  
18 Brandt and Anderson v. Carden, that is participation or  
19 material aid in the sale of securities. But the seller never  
20 was Davis Wright. They got paid fees. That's all they got.  
21 The seller was Jon Harder and his companies.

22 Q In your experience had you ever seen a situation where a  
23 law firm not only developed the investment vehicle, not only  
24 prepared the offering memorandum for the investment vehicle,  
25 not only sent out the offering materials with respect to the

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1 investment vehicle, not only met with investors and discussed  
2 the investment vehicle with them, had you ever encountered a  
3 situation like that in your 40 years of experience?

4 A Yes, many times. Lawyers do that for a living. They get  
5 paid an hourly fee to do it, and they are proud when they see  
6 their client's being successful in raising capital. We find  
7 that, in particular, among younger lawyers. I classified  
8 Dozois, with less than 25 years of experience, in that  
9 category, as being a younger lawyer who was blinded by his  
10 client's avarice.

11 Q Blinded by his clients avarice. Just a mindless --

12 A He had no motive to do what happened here except to serve  
13 his client. His client was the one who was going to become the  
14 king of assisted living centers and who made charitable  
15 contributions when his operations were operating at a loss and  
16 took credit for making charitable contributions with investor  
17 money.

18 Q The same client, that is Mr. Harder, who contributed  
19 nothing to the recovery that was realized through the  
20 receivership?

21 A Harder should have contributed everything, and I don't  
22 know that he did. I know that he paid his defense costs out of  
23 the recovery that would have otherwise gone to investors.

24 Q I would like to show you a document --

25 MR. SCHATZ: May I show the document?

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1 THE COURT: Yes.

2 BY MR. SCHATZ:

3 Q If you could look at this document for a minute. Tell me  
4 if this does in fact contain your signature on the last page.

5 A Yes.

6 MR. SCHATZ: This document, for the record,  
7 Your Honor, was in fact filed in the matter entitled Securities  
8 Exchange Commission v. Sunwest Management, civil case  
9 No. 6:09-cv-6056-Hogan. It is document 1838.

10 BY MR. SCHATZ:

11 Q Mr. Esler, this is a document that you signed under  
12 penalty of perjury; is that correct?

13 A Yes.

14 Q And as one of the attorneys for various Sunwest investors,  
15 you were making this declaration based upon personal knowledge?

16 A Yes.

17 Q And paragraph 2, it is lengthy, but I'll read it slowly.  
18 Please listen carefully so I can ask you a question at the  
19 conclusion of it.

20 "In October of 2008, Jon Harder and his counsel  
21 presented a voluntary, informal reorganization plan that  
22 involved 'rolling up' all of the separate assets of the Sunwest  
23 Enterprise for the benefit of the investors. I recognized that  
24 serial foreclosures by banks or serial litigation by investors  
25 to take over control of individual properties would likely wipe

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1 out the entire asset base of the enterprise. On behalf of my  
2 clients, I supported the roll-up plan and did not file claims  
3 against Harder or the enterprise. Without his cooperation in  
4 the fall of 2008 and early 2009, I believe that the  
5 reorganization plan would have been much less likely to  
6 succeed."

7 Is that a correct reading of paragraph 2 of this  
8 declaration under penalty of perjury?

9 A Yes. Yes.

10 Q Paragraph 3 states, "Mr. Harder also assisted in the  
11 efforts to recover on claims from third-party professionals,  
12 including Davis Wright Tremaine, K&L Gates, and other  
13 professional firms. These recoveries currently top \$65 million  
14 and directly contributed to recovery for the investors. His  
15 assistance and the assistance of his attorneys reduced the cost  
16 and increased the recoveries from those third parties."

17 Have I correctly recited paragraph 3?

18 A Yes.

19 Q This declaration was signed by you January 19, 2011?

20 A Yes.

21 MR. SCHATZ: I would ask the Court to receive this  
22 declaration. It is marked as Defendant's Exhibit 1000.

23 THE COURT: Any objection?

24 MS. KERIN: No, Your Honor.

25 THE COURT: Received.

1 MR. SCHATZ: Thank you, Your Honor.

2 Nothing further, Mr. Esler. Thank you.

3 THE COURT: Mr. Esler, before we go back to the  
4 Government's questions, did I hear you correctly say that you  
5 represented approximately 450 investors in Sunwest operations?

6 THE WITNESS: Yes, that's my recollection.

7 THE COURT: Can you describe generally, and I assume  
8 you are familiar with the term, a concept of an "accredited  
9 investor"?

10 THE WITNESS: Yes.

11 THE COURT: Tell us, first, generally, what does that  
12 term mean?

13 THE WITNESS: Well, it is an SEC term that was  
14 created in about 1934 when the Securities Exchange Act was  
15 adopted or shortly thereafter. It sets a standard of an  
16 investor has to have a net worth of a million and a half  
17 dollars, exclusive of their home, and they have to -- or else  
18 they have to an income level of \$200,000 or \$300,000 a year.

19 It was originally at that stage indicative of a  
20 person who had achieved a certain relatively high degree of  
21 wealth. But as time has passed on, it has ceased to have that  
22 same meaning, because you can have that much wealth just by  
23 sitting on your house long enough if you are in the right  
24 neighborhood.

25 THE COURT: But I thought you said it has to be

1 exclusive of your primary residence.

2 THE WITNESS: Yeah. But if you sell your house, you  
3 might hit the net worth requirements. So I don't find it a  
4 very useful term in terms of evaluating the sophistication of  
5 an investor.

6 THE COURT: Do you know whether all of your 450  
7 clients met that definition of "accredited investor"?

8 THE WITNESS: No. I don't believe they all did. But  
9 because the way the sales took place, you know, we never got to  
10 the point of saying, No. 1, you didn't meet the registration  
11 requirements under Oregon securities laws; you have a  
12 three-year drop-dead statute of limitations for securities  
13 violation. So we never really approached the case from that  
14 standpoint.

15 We could have integrated the case. This was a  
16 perfect case for integrating every one of the 200 or 300  
17 offerings that took place and say it was all one big offering  
18 that didn't meet the registration requirement, but we did not  
19 think that would be an effective strategy.

20 THE COURT: Do you know from your investigation when  
21 you were representing your clients, for those who were not  
22 accredited investors, how it came to be, or what was said to  
23 them that then enabled them to be able to invest?

24 THE WITNESS: Well, I think it was the same thing  
25 that was said to everybody. It was that Sunwest is one of the

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1 best operators of assisted living centers. They have a real  
2 hands-on approach and they can --

3 THE COURT: I wasn't clear in my question. My  
4 question was, do you know whether there was any information  
5 passed on by Sunwest or any of its broker-dealers that assisted  
6 otherwise unaccredited investors in believing that they were  
7 qualified to invest under the accredited investor requirement?  
8 Do you know what I'm asking?

9 THE WITNESS: Yes, I do.

10 THE COURT: Do you have an answer?

11 THE WITNESS: I think what you are asking is  
12 oftentimes you will find that the stockbroker is telling a  
13 person to just check the box. We do believe that occurred, but  
14 it wasn't something that we tried to discern.

15 THE COURT: All right. Thank you.

16 Ms. Kerin, and then we will go back to Mr. Schatz  
17 after you.

18 MS. KERIN: I will be brief, Your Honor.

19 REDIRECT EXAMINATION

20 BY MS. KERIN:

21 Q I have three areas of inquiry, Mr. Esler. The first is  
22 regarding the filing of lawsuits against professionals in  
23 securities cases. In your 40-year experience, is it pretty  
24 common to file lawsuits against professionals, including  
25 lawyers, when you are talking about an investment fraud case?

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1 A Yes, because they have insurance. They won't run and  
2 hide. They don't hide their assets. It is very difficult --  
3 in my experience, when the business fails, either the promoter  
4 either doesn't have assets or else he has hidden the assets.  
5 If he has hidden them, he has violated IRS regulations, and if  
6 the IRS can't get them, we certainly can't.

7 Q In your experience, the fact of the culpability or  
8 negligence of the professionals, including the lawyers, does  
9 that affect whether or not the promoter or the seller is also  
10 liable or acted in a criminal manner?

11 A No, not at all.

12 Q In this case, this specific case, the fact that  
13 Davis Wright Tremaine and the other professionals that were  
14 involved may have been neglectful in their professional  
15 responsibilities, did it change your opinion about the conduct  
16 of Mr. Harder and the other professionals at Sunwest?

17 A No, absolutely not. I mean, I felt that Dozois was  
18 inexperienced and over his head and that the firm didn't have  
19 the type of back-up due diligence that K&L Gates did. That's  
20 why K&L Gates -- when Gib Masters at K&L Gates had one of the  
21 offering circulars reviewed by a peer review person at  
22 K&L Gates, and that's the guy who blew the whistle and said,  
23 "Whoa, wait a minute."

24 Q And that was the Cottonwood investment at the end of 2007,  
25 beginning of 2008; is that correct?



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1 A Yes.

2 Q In fact, in that instance, Mr. Harder made promises to  
3 Mr. Masters about the way they would conduct their business  
4 going forward, correct?

5 A Yes. And he also made them to Mr. Dozois. Mr. Dozois was  
6 involved in both sides of that, but was concerned because  
7 Masters was concerned. And because K&L Gates was concerned, he  
8 was concerned as well. So the promises were made that they  
9 were going to do rescissions for some of the offerings. They  
10 were going to stop using construction funds. They'd razed a  
11 project that they were going to build from the ground up. They  
12 had raised the construction funds from investors, and then they  
13 would spend it on the negative cash flow from the overall  
14 operation as opposed to the new construction that it was  
15 promised for.

16 So Harder promised he would stop doing that. It was  
17 a promise that was made by Harder. Mr. Wettlaufer sent the  
18 letter and said, "Jon Harder promises to do this," and then  
19 they didn't do it.

20 There is a poignant e-mail at the end of May from  
21 Tim Dozois to Kevin Thomason down in Texas where he says,  
22 "Kevin, I have got to talk to you. I have just discovered  
23 something about the client," and that's like sin on a Sunday  
24 night. You could see the lawyer's stomach eating him out.

25 So they apparently had the conversation. We can't

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1 piece together really what they said on the telephone  
2 conversation, but we know that both firms said, after these  
3 last offerings that are in the pipeline, we're not going to do  
4 any more work for you.

5 Q In your investigation, in your 3,000 hours that you spent  
6 investigating Sunwest, was it your opinion that regardless of  
7 the disclosures that were prepared by Davis Wright and all of  
8 the other professionals, that the representations, the oral  
9 representations that were made by Mr. Harder and other  
10 representatives of Sunwest, were exactly the same as those  
11 disclosures?

12 A Well, they were worse. I mean, I don't think that -- the  
13 offering circular directly says the lie. I don't ever think  
14 Davis Wright ever knew what the lie was, because they never  
15 looked at the performance data that Mr. Harder had from both  
16 the MIC report and the management report they did in 2006 that  
17 showed they were operating at a continuous loss. Most of their  
18 facilities were below the 85 percent level of occupancy, and  
19 they needed to keep raising new capital in order to keep  
20 afloat.

21 I don't think at the granular level that each of the  
22 law firms were looking at each of the separate offerings, that  
23 they could ever step back and look at it from the 35,000-foot  
24 level, which is what Mr. Harder could do, and say, "Every  
25 month, I need to have five new closings, or else I'm not going

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1 to make it." And that number kept growing. That's why you see  
2 the sharp increase in offerings and the sharp increase in  
3 prices that they are paying per unit, per door.

4 Q Thank you. I am going to move on to a second topic. That  
5 is with respect to Mr. Harder's contribution to the Lone Star  
6 proceeds. I believe that your testimony was the SEC filed a  
7 temporary restraining order and sought to instill a  
8 receivership at the beginning of the SEC proceedings, correct?

9 A Yes.

10 Q And that Mr. Harder and his lawyers objected to the  
11 receiver and to the standard SEC order; is that correct?

12 A Yes.

13 Q And there was a hearing in Eugene in March -- on  
14 March 2nd, 2009. Do you recall that?

15 A Yes.

16 Q In preparation for that hearing, Mr. Harder and his  
17 lawyers filed pleadings with the Court expressing their side  
18 and their opposition, correct?

19 A Yes.

20 Q And do you recall, was part of the opposition to  
21 Judge Hogan that there was the CRO agreement, and the CRO was  
22 in place, and the Lone Star proceeds were filling this gap; and  
23 therefore, the SEC receivership and standard order was not  
24 necessary? Is that your recollection?

25 A Yes. They did not want the full-scale receivership order.

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1 They wanted it to be subjected to the CRO agreement.

2 Q I had asked you on direct about the loan of Mr. Harder's  
3 interests in the Lone Star proceeds, correct?

4 A Yes.

5 Q Then Mr. Schatz asked you some questions to attempt to  
6 undermine whether or not this was a loan or something of a tax  
7 consequence. Do you recall that?

8 A Yes.

9 Q I'm going to hand you --

10 MS. KERIN: May I approach, Your Honor?

11 THE COURT: You may.

12 MS. KERIN: I have not marked this as an exhibit, but  
13 I'm going to show it to counsel.

14 BY MS. KERIN:

15 Q This is Docket 14 in the SEC case. You can read that in  
16 the record. What is the title of that document?

17 A "Defendants Jon Harder's and Kristin Harder's Memorandum  
18 and Opposition to the Security & Exchange Commission's Motion  
19 for a Temporary Restraining Order; Expedited Consideration and  
20 Oral Argument Requested."

21 Q If I may, I would like to show you a provision in here.

22 THE COURT: Ms. Kerin, is that from civil case  
23 9-cv-6056?

24 MS. KERIN: Yes, Your Honor. It is Docket No. 14.

25

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1 BY MS. KERIN:

2 Q Is it your understanding that part of the purpose of this  
3 was to assuage Judge Hogan not to enter the receivership and  
4 to, instead, keep the status quo?

5 A Yes.

6 Q What does Jon Harder's lawyer explain to the Court about  
7 the contribution of Mr. Harder's interest in the Lone Star  
8 sale?

9 A Well, it says, "Harder, Fisher, and Gutzler would assign  
10 to Hamstreet the entirety of their right to all cash proceeds,  
11 and other contributions payable to them on account of their  
12 equity interests. This assignment was for the benefit of  
13 Sunwest and its affiliate and was intended to fund the  
14 restructuring plan for the benefit of residents, creditors, and  
15 investors. In return, as funds were used for this purpose, the  
16 equity holders would receive promissory notes bearing interest  
17 at 9 percent from the entities receiving the cash infusions.  
18 The arrangement was structured in this manner for essentially  
19 four reasons."

20 Q You can stop there.

21 A Okay.

22 Q So essentially is it fair to say that Jon Harder's lawyers  
23 represented to Judge Hogan that the interests that he was  
24 contributing was being loaned?

25 A Yes.

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1 Q Then my final area of inquiry, Mr. Esler, you testified on  
2 direct that you submitted approximately four applications for  
3 fees in the SEC proceeding, correct?

4 A Yes.

5 Q And you also received about two and a half million  
6 dollars, maybe three?

7 A I don't think it was three.

8 Q Two and a half; is that fair?

9 A It could be that high; I don't think so. But it could be  
10 that high.

11 Q In your 40 years of experience in representing victims, is  
12 that unusual for the receivership estate to pay for the  
13 lawyers' fees who represents the victim?

14 A Absolutely. You know, all of these cases, the ones that  
15 were filed against K&L Gates, Thompson & Knight, and  
16 Davis Wright ended up as class actions. Ordinarily you would  
17 have the Court in the settlement class action determine what  
18 the fee would be. Generally it is not an hourly rate. It is  
19 usually enhanced because of the risks and the time that the  
20 lawyers put in.

21 Q But you would receive the funds from the receivership  
22 estate in most instances or what you recovered?

23 A Well, mostly we received them from clients, because there  
24 aren't receivers. Even if there are receivers, third-party  
25 litigation is generally not part of the receivership. It is

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1 generally a separate item. But in Capital Consultants and in  
2 Sunwest, there was a deviation from that norm, and the  
3 receivership was used to distribute the funds that were  
4 recovered in third-party litigation to the investors. They  
5 already had the mechanism in place. It was a lot less  
6 expensive than having to set it up as a separate type.

7 Q How many fee applications did the lawyers for Mr. Harder  
8 submit in the SEC proceeding?

9 A Well, I quit reading them all, but they came out every  
10 couple of months. They were innumerable fee applications.  
11 Then when David VanSpeybroeck moved over to Sussman Shank, then  
12 they came from that direction as well.

13 Q I am going to show you Exhibit 163. This was admitted in  
14 the Phase I sentencing. This was introduced by Allen Painter  
15 of the U.S. Trustee's Office. It was his analysis of funds  
16 from the receivership estate that went to Mr. Harder or his  
17 wife or were paid on his behalf. You will see in the far  
18 right-hand column that approximately \$6.5 million were paid to  
19 professionals on behalf of Mr. Harder or his wife. Do you see  
20 that?

21 A Yes.

22 Q Would that surprise you?

23 A Well, it is a huge figure, but we deal with big numbers in  
24 these kinds of cases. It is certainly accounted for his  
25 Lone Star equity.

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1 Q In addition, I believe Mr. Schatz asked you if you ever  
2 saw any of the money or any the checks that went to Mr. Harder  
3 during the time that the receivership proceeding was in place,  
4 and you can see the column on the left-hand side indicates  
5 payments to or on behalf of Mr. Harder directly. Do you see  
6 that?

7 A Yes.

8 Q Would that surprise you?

9 A No. I mean, I was aware of the fact that those payments  
10 were being made. I was aware of the fact that he had even  
11 prepaid his mortgage before he filed the Chapter 11. You know,  
12 it was not pretty.

13 MS. KERIN: Thank you. I have no further questions.

14 THE COURT: Mr. Schatz.

15 MR. SCHATZ: Yes, thank you, Your Honor.

16 RE CROSS-EXAMINATION

17 BY MR. SCHATZ:

18 Q Did you file an objection, Mr. Esler, to any of the fee  
19 applications filed on behalf of Mr. Harder's lawyers?

20 A No. We weren't involved in representing our investors in  
21 connection with the receivership.

22 Q Are you saying to me that was not something that you could  
23 have done?

24 A I'm saying I wasn't hired to do it, and I didn't do it.

25 Q Could you have filed an objection?



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1 A Yes.

2 Q But you weren't hired to do it, so you didn't do it?

3 A Right.

4 Q Is it also true that Judge Hogan awarded you \$74,134.94 to  
5 cover your costs?

6 A Yes. We had out-of-pocket costs, in addition to the time  
7 we spent -- the value of the time we spent. We had  
8 out-of-pocket costs.

9 Q Wasn't it the understanding that your clients were paying  
10 the costs, and you sought reimbursement so that that fund,  
11 \$74,000 and some change, could go back to your clients?

12 A Yes. Although at later stages -- what we ordinarily do  
13 when we organize a group like this, we have some contribution  
14 from each of the members for out-of-pocket costs. In a case  
15 like this, it might have started out at 1 percent or a quarter  
16 of a percent -- probably a quarter of a percent -- but at the  
17 later stages of the case, we quit bothering to try to do that.  
18 So some of that was our cost advanced and some of it was  
19 reimbursement to clients.

20 Q We have referred several times, and we have churned the  
21 ground about the SEC proceeding and the filing of injunction  
22 and the appointment of the receiver. Did you file an objection  
23 to the order ultimately entered by Judge Hogan concerning the  
24 receivership?

25 A We orally objected to it.

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1 Q Did you file a formal written objection?

2 A No.

3 Q Did you appeal from Judge Hogan's order?

4 A No. We argued the case. When he didn't issue the SEC  
5 form of order, but instead modified the form of order, we let  
6 our objections stand and moved on.

7 Q It is true, is it not, just so it can be clear, that any  
8 monies paid to anybody out of that receivership bowl or bucket,  
9 if you will, was approved by the Court?

10 A Yes.

11 Q In your lawsuit where you named Davis Wright Tremaine, was  
12 the strike of your lawsuit some failure in the lack of  
13 performance data or did it involve the inter-facility loaning  
14 back and forth that Sunwest had engaged in?

15 A I think that the thrust of our lawsuit was that Sunwest  
16 disguised the fact that individual living centers and  
17 collectively the bulk of the assisted living centers were  
18 operating at a loss and portrayed a picture that Sunwest,  
19 because of its system, operated profitably.

20 Q And that is about Sunwest, but you filed a lawsuit against  
21 Davis Wright Tremaine. How did those facts relate to what you  
22 thought was the liability of Davis Wright Tremaine?

23 A The way that I view the securities laws and the lawyers'  
24 participation, as he prepares the offering materials used in  
25 connection with the offering, is that it is the lawyer's job to

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1 do the due diligence on behalf of all the investors. It is  
2 really kind of an efficient way for the system to operate. So  
3 Davis Wright had to exercise reasonable care to make sure that  
4 the statements that were contained in the offering materials  
5 were accurate.

6 Now, the offering materials and the statements made  
7 were actually Sunwest's statements, not Davis Wright's, but  
8 Davis Wright had the duty to do the due diligence. As those  
9 segments of the performance tables that I just read to you show  
10 they fell short of their duty. They shouldn't have gone  
11 forward and done the offering unless their client gave them the  
12 performance data. If their client wouldn't give them the  
13 performance data, and they wanted to do the legal work, they  
14 should have said, "But we can't get performance data from our  
15 clients." That was all covered in SEC Industry Guide 5, which  
16 covers real estate offerings.

17 Q I see. Would you turn to pages 11 and 12 of your  
18 negotiation or mediation memorandum. The last paragraph on the  
19 page 11, top of page 12, is bolded. Do you see that?

20 A Mine aren't numbered, because I printed them off on my own  
21 computer.

22 MR. SCHATZ: May I approach again, Your Honor?

23 THE COURT: You may.

24 BY MR. SCHATZ:

25 Q I have numbered them, but who knows. I counted them, but

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1 let's see. There we go. So we're looking at the bottom of a  
2 page of your mediation negotiation memoranda that begins,  
3 "Tim Dozois."

4 A "Knew about the commingling"?

5 Q I will read it rather than have you read it since it is  
6 somewhat of an effort to do so. I will read it slowly. You  
7 make sure, Mr. Esler, that I'm reading it correctly.

8           Isn't it true, sir, that in your negotiation  
9 memorandum you wrote as follows: "Tim Dozois and DWT knew  
10 about the commingling of funds and inter-entity transfers at  
11 Sunwest from the very beginning. Those practices were a  
12 central part of a lawsuit brought against Jon Harder and others  
13 in late 2003 by Jeffrey Kraus, the former CEO of Sunwest.  
14 Kraus had argued that he breached his fiduciary duties to other  
15 LLC members by using cash from one entity to support another.

16           "The lawyers who represented Sunwest at the time,  
17 including in-house counsel and Tim Dozois, recognized the  
18 problem. As stated by Sunwest's assistant general counsel,  
19 Tom Wettlaufer, in an e-mail to Dozois and other lawyers,  
20 'Members of an LLC, which is doing well operationally, do not  
21 expect to have their cash used to fund shortfalls in another  
22 LLC in which they have no ownership.'

23           "Understanding that these transfers were not  
24 permitted by the operating agreements for these LLCs, Dozois  
25 participated in a project with Wettlaufer to obtain consent

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1 from investors and to change the operating agreements to permit  
2 this practice. Dozois knew, however, that those changes never  
3 were implemented. Instead, the Kraus litigation was settled,  
4 and Sunwest continued business as usual with Dozois as the  
5 primary outside counsel preparing offerings."

6 Is that the text in your memorandum?

7 A Yes. That text is in the section entitled "Failure to  
8 disclose that Sunwest secretly subsidized facilities to create  
9 impression that all prior projects were successful."

10 Q And that was your opinion at the time that you wrote those  
11 words, correct?

12 A That Dozois -- yes. That Dozois knew that funds were  
13 being used from other projects to create the impression that  
14 projects were successful.

15 Q From the very beginning?

16 A Yes.

17 MR. SCHATZ: Nothing further, Your Honor. Thank you.

18 THE COURT: Anything further within the scope?

19 MS. KERIN: No. Thank you, Your Honor.

20 THE COURT: Mr. Esler, thank you very much. You may  
21 step down.

22 (End of requested excerpt.)

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I certify, by signing below, that the foregoing is a correct transcript of the record of proceedings in the above-entitled cause. A transcript without an original signature, conformed signature, or digitally signed signature is not certified.

9

/s/ Dennis W. Apodaca  
DENNIS W. APODACA, RDR, RMR, FCRR, CRR  
Official Court Reporter

December 8, 2015  
DATE

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<p><b>BY MR. SCHATZ:</b>  [13] 31/1 40/11  43/8 45/8 49/11  57/7 57/15 58/17  59/6 67/1 67/9  80/16 83/23  <b>BY MS. KERIN:</b>  [5] 4/10 5/7 71/19  76/13 76/24  <b>COURTROOM  SECURITY  OFFICER:</b> [1]  45/5</p>	<p>56/6 56/25 57/3  57/13 58/14 59/5  66/25 68/22 68/24  69/2 69/6 69/10  69/24 70/5 70/19  71/2 71/9 71/14  76/10 76/21 80/13  83/22 85/17 85/19  <b>THE WITNESS:</b>  [16] 4/8 5/6 42/12  49/10 56/5 56/7  57/5 58/16 69/5  69/9 69/12 70/1  70/7 70/23 71/8  71/10</p>	<p>\$3.6 million [1]  29/13  \$300,000 [1] 69/18  \$400 [1] 51/19  \$450 [5] 10/14  10/17 19/20 28/17  51/18  \$450 million [3]  10/14 10/17 19/20  \$450 million plus  [1] 28/17  \$50,000 [3] 50/22  50/25 51/7  \$54,000 [3] 16/5  44/20 44/21</p>
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