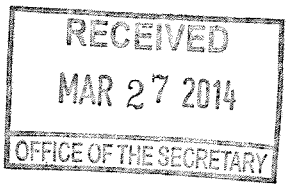
HARD COPY

UNITED STATES OF AMERICA

Before the

SECURITIES AND EXCHANGE COMMISSION



In the Matter of CLEAN ENERGY CAPITAL, LLC, and SCOTT A. BRITTENHAM, Respondents.	Admin. Proc. File No. 3-15766

ANSWER OF RESPONDENTS CLEAN ENERGY CAPITAL, LLC and SCOTT A. BRITTENHAM

Respondents Clean Energy Capital LLC ("CEC") and Scott A. Brittenham ("Mr. Brittenham"), by their attorneys, Stern, Tannenbaum & Bell LLP, for their Answer to the allegations of the Division of Enforcement (the "Division") of the Securities and Exchange Commission (the "Commission"), set forth in Section II of the Order Instituting Administrative and Cease and Desist Proceedings dated February 25, 2014 (the "OIP")(said Section II being referred to herein as the "Complaint"), allege as follows:

A. SUMMARY

1. In answer to Paragraph 1 of the Complaint, Respondents deny each and every allegation, and further allege that:

a) Until 2012, CEC was an investment advisor registered with the Commission, and Mr. Brittenham is its co-founder, president and main portfolio manager. CEC serves as the general partner of twenty limited partnerships under a "series" limited partnership formed under Delaware law, Ethanol Capital Partners, L.P.: Series A, B, C, D, E, G, H, I, J, L, M, N, O, P, Q, R, S, T and V, and Tennessee Ethanol Partners L.P. (collectively, the "ECP Limited Partnerships"). In 2012, CEC no longer met the minimum assets under management to be eligible for registration with the Commission, and thereafter filed its notice of withdrawal from registration as an investment adviser; it is now registered only with the State of Arizona.

b) As set forth more fully below, this proceeding involves no "misconduct." The Division's primary allegations focus on expense allocations, and accuse Respondents of having (i) allocated a portion of its rent, employee and office overhead expenses to the ECP Limited Partnerships as "Partnership Expenses" under their respective limited partnership agreements; and (ii) amended the ECP Limited Partnership agreements, during the depths of the financial crisis, to authorize the issuance of secured promissory notes to CEC to document past debts owed to CEC. The Division alleges these actions to be fraudulent, which it must allege in order to sustain its claims that they violated § 206 of the Investment Advisers Act of 1940. However, the Division conveniently omits these important facts:

- *First,* CEC acted so as to protect the assets of the ECP Limited Partnerships and the investors as required by its fiduciary duty obligations, and has largely succeeded in preserving those assets from what could well have been a total loss of investment in the depths of the financial crisis. CEC did so by actively participating and even changing the management of the Portfolio Companies (as defined below) to stem their operating losses and to make them more profitable, acting above and beyond the normal functions of a general partner of a passively invested private equity fund. In addition, Mr. Brittenham and CEC's co-founder put over $1 Million of their own money into CEC to keep it from collapsing when, again deep in the financial crisis, the ECP Limited Partnerships could no longer pay the fees and expenses necessary to sustain operations of CEC and the ECP Limited Partnerships.
- *Second,* CEC consulted legal counsel concerning both the allocation of expenses to the ECP Limited Partnerships and the amendment of the partnership agreements to authorize the ECP Limited Partnerships to issue secured promissory notes to CEC, and in both instances was advised that such actions were, under and subject to the partnership agreements and Delaware law, delegated to the discretion of

the general partner in the exercise of its good faith business judgment. As set forth more fully below, when CEC and the ECP Limited Partnerships found themselves in dire financial straits during the recent financial crisis, CEC exercised its discretion to take those actions that it deemed, in its good faith business judgment, to be in the best interests of the ECP Limited Partnerships and their investors and to preserve the value of their investments while riding out the economic storm. Accordingly, Respondents, far from breaching their fiduciary duties under the ECP Limited Partnership agreements or Delaware law, actually fulfilled those duties at great risk to themselves. They certainly did not engage in fraud or deception under the Advisers Act.

- *Third,* in 2007, court-appointed monitors for one of the ECP Funds, Series G, asserted on behalf of the investors that those very same allocations of expenses and issuances of promissory notes were "unauthorized" and "fraudulent." In a final order dated March 29, 2011, the United States District Court for the District of Arizona ruled on a cross-motion for summary judgment that (i) both CEC's allocation of expenses to ECP Limited Partnership Series G and its unilateral amendment of the limited partnership agreement to permit the issuance of secured promissory notes to CEC

were permitted by the Series G limited partnership agreement and by Delaware law, (ii) CEC acted in good faith exercise of its business judgment in taking both those actions, and therefore (iii) CEC did not breach the ECP Limited Partnership agreement, or engage in self dealing, or breach its fiduciary duties to the ECP Limited Partnership, and (iv) those allegations could not be the basis of a federal securities fraud claim. *Pozez, et ano. v. Clean Energy Capital, LLC, et al.,* No. 07-CV-00319-TUC-CKJ (Jorgenson, J.)(Order, March 29, 2011)(the "*Pozez* Order")(annexed hereto as Exhibit A), at 16-22. The *Pozez* Order implicitly applies to *all* the other ECP Limited Partnerships, because CEC acted with respect to all the ECP Limited Partnerships the same way it acted with respect to Series G.

c) Given these facts, the Division cannot prove a violation of any anti-fraud provision of the federal securities laws, not § 17 of the Securities Act of 1933, nor § 10(b) of the Securities Exchange Act of 1934, nor § 206 of the Advisers Act—because it cannot show either deception or *scienter*. What the Supreme Court aptly said about § 10(b) applies to all these laws: Though each may be called a catch-all provision, "what it catches must be fraud." *Chiarella v. United States,* 445 U.S. 222, 234-35 (1980). The anti-fraud provisions of the securities laws do not extend to the content of and

cannot be used to modify—in effect to federalize the governance of—Delaware limited partnerships. Here, the Division improperly labels "fraud" events that could never be more than breaches of contract or fiduciary duties under State law, and such breaches of duty are not under the purview of the federal securities laws. *See Santa Fe Industries, Inc. v. Green*, 430 U.S. 426, 476 (1977).

2. In answer to Paragraph 2 of the Complaint, Respondents deny each and every allegation, and further allege that:

a) *First*, Respondents' designation of certain expenses as Partnership Expenses properly allocable to the ECP Limited Partnerships was permitted by the limited partnership agreements and Delaware law, as the *Pozez* Order expressly found with respect to Series G. Therefore, there was no "misappropriation" of any funds by Respondents from the ECP Limited Partnerships.

b) *Second*, the ECP Limited Partnerships did not "secretly" borrow money from CEC at unfavorable rates. Rather, the ECP Limited Partnerships that were in arrears in their payment of management fees and partnership expenses under their limited partnership agreements accrued a liability to CEC, which CEC, in consultation with its accountant and legal counsel, documented through promissory notes secured by Partnership assets. That documentation was a necessary and reasonable predicate to having Mr. Brittenham and CEC's co-founder infuse over $1 Million in cash funds to

CEC, as necessary lenders of last resort after failing to obtain loans from any other source, to ensure the continued viability of CEC and the ECP Limited Partnerships and to preserve the assets of their investors during the financial crisis.

c) *Third*, CEC exercised its good faith business judgment under the ECP Limited Partnership agreements to correct its internal method for calculating the amount of distributions due to limited partners as recommended by a financial consultant in order to ensure that such partners received what the limited partnership agreements reasonably provided.

d) *Fourth*, Respondents categorically deny stating to any investor, or directing or authorizing anyone else to say to such investor on their behalf, that Mr. Brittenham or CEC's co-founder would invest any sum certain in the ECP Limited Partnership in question.

e) *Fifth*, CEC did not violate § 206(4) of the Advisers Act with respect to assets of the ECP Limited Partnerships because (a) the non-cash assets of the ECP Limited Partnerships consist of equity interests in privately held limited liability companies and thus comprised inchoate contractual rights recorded in the books and records of those companies, and not in any "original stock certificates" that needed to be, or even could have been, taken "custody" of; and (b) the cash assets of the ECP Limited Partnerships were at all times in a bank account with subaccounts maintained exclusively by such bank,

which ensured the accurate accounting of such funds in the names of each of the ECP Limited Partnerships to which they belonged.

f) *Sixth,* CEC's compliance policy contained a scrivener's error—an "or" misplaced for an "and"—which was corrected when CEC discovered it. For the Division to brand CEC's policies in the whole "inadequate" on account of this sole typographical error in the compliance manual says more about the pettiness of the Division's charges than it does about CEC's compliance regime.

g) *Seventh,* CEC's Co-Founder's prior SEC disciplinary history was omitted with respect to ECP Limited Partnership Series S, T and V—but to say it was "concealed" is absurd given that it was admittedly disclosed in the prior 17 ECP Limited Partnerships. That history was omitted from the PPMs of Series S, T and V because it was no longer required to be disclosed under the federal securities laws.

B. RESPONDENTS

3. CEC admits the allegation contained in Paragraph 3 of the Complaint.

4. In answer to Paragraph 4 of the Complaint,

a) Mr. Brittenham admits that he resides in Tucson, Arizona, that he is the co-founder, CEO, and main portfolio manager of CEC; that he has an 85% ownership interest in CEC and a 50% voting interest; that he is an investor in two ECP Limited Partnerships managed by CEC; and that he holds Series 7 and 63 licenses.

b) However, with respect to the balance of Paragraph 4 of the Complaint, Mr. Brittenham denies each and every allegation, and moreso objects to its blatant falsity and to the innuendo by which the Division seeks to besmirch his character. The Washington State Order of which the Complaint speaks is attached hereto as Exhibit B. It does *not* apply to Mr. Brittenham, and it says *nothing* about a ten year ban. It applies only to the mortgage brokerage company of which Mr. Brittenham was president, and he signed the order *only* as President of the company. That was because the conduct that was the subject of the Order was committed not by Mr. Brittenham, who never personally conducted any business in the State of Washington, but by the company's resident officer in Washington, who did in fact sign the order in *his* personal capacity.

c) But more telling than the falsity of the Division's accusation is its context in this proceeding. There is nothing in the Complaint that turns on the Washington State Order. It is not mentioned as a relevant factor to any of the stated charges. Therefore, its inclusion in this Paragraph is for rhetorical purposes only, a blatant attempt to bias the Administrative Law Judge into believing, before reading any allegations, that Mr. Brittenham is a "bad boy" unmindful of regulatory responsibility. The truth is that Mr. Brittenham's 32-year regulatory history in the securities field—extending back to 1982—has been spotless.

C. OTHER RELEVANT ENTITIES

5. In answer to Paragraph 5 of the Complaint, Respondents admit that Ethanol Capital Partners, L.P., was organized on May 27, 2004, as a "series" limited partnership, and that it continues to exist in good standing under the laws of the State of Delaware, authorized and intending to be the basis of a number of sequentially lettered limited partnerships, each making separate investments and holding separate funds and assets. Respondents admit that 19 ECP Limited Partnerships were created, each bearing Series letters A, B, C, D, E, G, H, I, J, L, M, N, O, P, Q, R, S, T and V. In addition, a separate Delaware limited partnership was created named Tennessee Ethanol Partners, L.P., on June 10, 2005. Those 20 limited partnerships are referred to herein collectively as the ECP Limited Partnerships. Each ECP Limited Partnership has fewer than 100 limited partners, and they in the aggregate invested about $64 Million into all the ECP Limited Partnerships. Respondents also admit that the ECP Limited Partnerships were not registered with the Commission as investment companies, because such registration was not required under of the Investment Company Act.

D. FACTUAL BACKGROUND

6. In answer to Paragraph 6 of the Complaint, Respondents deny each and every allegation, except allege that :

a) Mr. Brittenham co-founded CEC in order to fulfill what was seen to be a need for capital to finance the construction and operation of more efficient production plants in the Midwest designed to convert corn into ethanol for sale to gasoline producers, in order to help meet federal requirements that gasoline for sale to United States consumers include 10% ethanol content,

and further to increase the supply of ethanol for use in newer "flex-fuel" enabled automobile engines, designed to operate on gasoline with a 15% ethanol content.

b) The ECP Limited Partnerships made investments in one or more of the following seven limited liability companies that constructed and operated ethanol production facilities: Granite Falls Energy, LLC; East Kansas Agri-Energy, LLC; First United Ethanol, LLC; Advanced BioEnergy, LLC; E Energy Adams, LLC; E Energy Broken Bow, LLC; and Highwater Ethanol, LLC (collectively, the "Portfolio Companies").

c) The investment strategy of the ECP Limited Partnerships was not merely to passively invest in the Portfolio Companies, but to engage in active oversight and participation in management at the board of directors level of the Portfolio Companies so as to maximize the probabilities that the investment objectives of the ECP Limited Partnerships would be met or exceeded.

d) CEC naturally incurred reasonable and necessary expenses, including most of its rent, personnel and office expenses, in furtherance of its active oversight and participation in the management of the Portfolio Companies (the "Portfolio Expenses").

e) The Portfolio Expenses were not normal and ordinary expenses of the general partner of the ECP Limited Partnerships, which, as the Division points out, would have been minimal. Rather, they were incurred solely in order to maintain active oversight and participation in the management of the Portfolio Companies themselves.

f) Accordingly, the Portfolio Expenses were appropriately allocable to the ECP Limited Partnership as "Partnership Expenses" under their respective limited partnership agreements.

g) Average annual Portfolio Expenses amounted to less than 1% of the aggregate assets of the ECP Limited Partnerships.

7. In answer to Paragraph 7 of the Complaint, Respondents deny each and every allegation, but admit that the rights, obligations, powers and privileges of limited partners and the general partner of each of the ECP Limited Partnerships are governed by the limited partnership agreements of each such partnership, and by the laws of the State of Delaware. Those rights, obligations, powers, and privileges were summarized for the convenience of potential investors—all of whom were sophisticated and/or accredited as those terms are defined in the Rules of the Commission—in private placement memoranda, one for each limited partnership (the "PPMs") and in other documents. The initial forms of the limited partnership agreements and PPMs were prepared by experienced securities counsel for CEC. Each limited partnership agreement and each PPM was reviewed and finally approved by such counsel before being distributed to potential investors. Although as a matter of internal governance Mr. Brittenham had final authority to direct the preparation and distribution of limited partnership agreements and PPMs, he never exercised such authority without consulting legal counsel, or against the advice of legal counsel.

8. In answer to Paragraph 8 of the Complaint, Respondents deny each and every allegation, and repeat and incorporate their responses to Paragraphs 1 and 2 hereof as their response to this Paragraph.

Portfolio Expenses Were Properly Deemed "Partnership Expenses"; Their Allocation as Such to the ECP Limited Partnerships Was Authorized by the Limited Partnership Agreements, Made With the Concurrence of Accountants, and Upheld by the District Court in the *Pozez* Order

9. In answer to Paragraph 9 of the Complaint, Respondents deny each and every allegation, but admit that Portfolio Expenses were incurred annually by CEC for the benefit of the ECP Limited Partnerships, were properly deemed to be "Partnership Expenses" under the applicable partnership agreements, and were properly allocated to the ECP Limited Partnerships as such. Respondents further allege that the definition of "Partnership Expenses" under each limited partnership agreement gives the General Partner discretion, acting in good faith, to determine what constitutes a "Partnership Expense," and that the propriety of such allocations was determined in consultation with CEC's accountants, and was expressly upheld by the district court in the *Pozez* Order. As to any conduct prior to February 25, 2009, Respondents further allege that the Division is barred from any claim by the applicable statute of limitations.

10. In answer to Paragraph 10 of the Complaint, Respondents deny each and every allegation, except admit that each of the ECP Limited Partnerships is a separate legal entity and that, insofar as it simply owns Portfolio Companies, it neither has nor needs officers or employees. CEC also admits that it is entitled to a management fee as set forth in the several limited partnership agreements solely for being the general partner. However, pursuant to the investment strategy of the ECP Limited Partnerships, CEC is also engaged in the active oversight and participation in the management of the Portfolio Companies, above and beyond the normal and customary duties of a general partner, and that most of the expenses CEC incurs are Portfolio Expenses, which are properly deemed "Partnership Expenses" under the limited partnership agreements and thus allocable to the ECP Limited Partnerships as such.

11. In answer to Paragraph 11 of the Complaint, Respondents deny each and every allegation, except admit that some of CEC's expense were allocated solely to CEC, some solely to the ECP Limited Partnerships, and some were divided between them generally on an allocation of 30% to CEC and 70% to the ECP Limited Partnerships (the "Split Ratio"). The Split Ratio was used to reasonably estimate the portion of CEC's rent, compensation and office overhead expenses that was reasonably attributable to CEC's active oversight of and participation in the management of the Portfolio Companies, and therefore were Portfolio Expenses. Respondents further allege that the Split Ratio was adopted by CEC after being advised by its legal counsel that doing so was permitted by the ECP Limited Partnership agreements and Delaware law. CEC adopted the Split Ratio methodology in the exercise of its good faith business judgment that doing so was an administratively reasonable way to determine Portfolio Expenses. In the good faith business judgment of CEC as general partner of the ECP Limited Partnerships, after consultation with its accountant, (a) the administrative burden and cost of attempting to use a more precise method of allocation would have exceeded any adverse impact that using the Split Ratio may have had on any one ECP Limited Partnership, and (b) the amount of economic benefit to any one ECP Limited Partnership, if any, of using a more precise method of allocation would not have been material. The district court in the *Pozez* Order held that the use of the Split Ratio was permitted under the partnership agreements and Delaware law, and the Division does not appear to contest Respondents' use of the Split Ratio to determine Portfolio Expenses.

12. In answer to Paragraph 12 of the Complaint, Respondents deny each and every allegation, and further allege that in the good faith business judgment of CEC, after consultation with its accountant, CEC properly determined that Portfolio Expenses comprised 70% of salaries, benefits, and rent incurred by CEC, and that such Portfolio Expenses were properly deemed

"Partnership Expenses" under the applicable limited partnership agreements, and were properly allocated to the ECP Limited Partnerships as such, and further allege that the propriety of such allocations was expressly upheld by the district court in the *Pozez* Order.

13. In answer to Paragraph 13 of the Complaint, Respondents deny each and every allegation, except admit that Mr. Brittenham received compensation and benefits from CEC, that such compensation was included in Portfolio Expenses (as determined by application of the Split Ratio) properly deemed to be "Partnership Expenses" under such definition in the applicable partnership agreements, and properly allocated to the ECP Limited Partnerships as such; and further allege that the propriety of such allocations was determined in consultation with CEC's accountants, and was expressly upheld by the district court in the *Pozez* Order. Respondents expressly deny the innuendo beneath this allegation to the effect that Mr. Brittenham took advantage of the ECP Limited Partnerships for his personal gain, and further allege that Mr. Brittenham served without any pay at all for organizing and managing CEC from mid-2004 through mid-2007, and that his average annual compensation from CEC from its inception through 2013 was about $255,000 per year.

14. In answer to Paragraph 14 of the Complaint, Respondents deny each and every allegation, and further allege that the only expense listed by the Division that is arguably "improper" is whatever charges may relate to transporting, on occasion, Mr. Brittenham's daughter to and from school and that the amount of such expense would have been *de minimus*. Beyond that, the expenses identified in Paragraph 14 are properly characterized as includible in Portfolio Expenses as derived by using the Split Ratio, and therefore properly deemed to be "Partnership Expenses" under such definition in the applicable partnership agreements, and properly allocated to the ECP Limited Partnerships as such; and further allege that the propriety of such allocations

was determined in consultation with CEC's accountants, and was expressly upheld by the district court in the *Pozez* Order.

15. In answer to Paragraph 15 of the Complaint, Respondents deny each and every allegation, and further allege that the district court in the *Pozez* Order held that these expenses were permitted by the limited partnership agreements and Delaware law and therefore were not "improper" and could not be the basis of any federal securities fraud claim.

16. In answer to Paragraph 16 of the Complaint, Respondents deny each and every allegation, and further allege that the district court in the *Pozez* Order held that these expenses were permitted by the limited partnership agreements and Delaware law and therefore were not "improper" and could not be the basis of any federal securities fraud claim.

17. In answer to Paragraph 17 of the Complaint, Respondents deny each and every allegation, and further allege that the district court in the *Pozez* Order held that these expenses were permitted by the limited partnership agreements and Delaware law and therefore were not "improper" and could not be the basis of any federal securities fraud claim.

18. In answer to Paragraph 18 of the Complaint, Respondents deny each and every allegation, and further allege that the district court in the *Pozez* Order held that these expenses were permitted by the limited partnership agreements and Delaware law and therefore were not "improper" and could not be the basis of any federal securities fraud claim.

19. In answer to Paragraph 19 of the Complaint, Respondents deny each and every allegation, except admit that the Split Ratio was applied to certain CEC expenses to determine Portfolio Expenses, and that Portfolio Expenses were allocated across all the ECP Limited Partnerships pro rata the assets of each partnership; and further allege that the district court in the *Pozez* Order held that the limited partnership agreements and Delaware law permitted CEC to so

allocate those expenses, and therefore that its doing so was not "improper" and could not be the basis of any federal securities fraud claim.

20. In answer to Paragraph 20 of the Complaint, Respondents deny each and every allegation, except allege that the district court in the *Pozez* Order held that the limited partnership agreements and Delaware law permitted CEC to so allocate those expenses, and therefore that its doing so was not "improper" and could not be the basis of any federal securities fraud claim.

21. In answer to Paragraph 21 of the Complaint, Respondents deny each and every allegation, and further allege that the district court in the *Pozez* Order held that the limited partnership agreements and Delaware law permitted CEC to so allocate those expenses, and therefore that its doing so was not "improper" and could not be the basis of any federal securities fraud claim.

22. In answer to Paragraph 22 of the Complaint, Respondents deny each and every allegation, and further allege that the district court in the *Pozez* Order held that the limited partnership agreements and Delaware law permitted CEC to so allocate those expenses, and therefore that its doing so was not "improper" and could not be the basis of any federal securities fraud claim; and further allege that inasmuch as all decisions with respect to (a) the determination of Portfolio Expenses, (b) their being deemed "Partnership Expenses" under the applicable limited partnership agreements, and (c) their allocation as such to the ECP Limited Partnerships, were taken in CEC's good faith business judgment after consultation with CEC's accountant, Respondents did not act with the *scienter* required to ground a claim for fraud under the federal securities laws.

23. In answer to Paragraph 23 of the Complaint, Respondents deny each and every allegation, and further allege that

a) The district court in *Pozez* Order held that the limited partnership agreements and Delaware law permitted CEC to so allocate those expenses, and therefore that its doing so was not "improper" and could not be the basis of any federal securities fraud claim; and further allege that inasmuch as all decisions with respect to (a) the determination of Portfolio Expenses, (b) their being deemed Partnership Expenses under the several limited partnership agreements, and (c) their allocation as such to the ECP Limited Partnerships, were taken in CEC's good faith business judgment after consultation with CEC's accountant, Respondents did not act with the *scienter* required to ground a claim for fraud under the federal securities laws.

b) Moreover, the impact of the allocation of the Portfolio Expenses to the ECP Limited Partnerships was not material: Even assuming that the Division is correct that the amount of Portfolio Expenses allocated to the ECP Limited Partnerships was $3 Million across the six years spanning 2008 to the present (as alleged in Paragraph 9 of the Complaint), then CEC allocated to the ECP Limited Partnerships about $500,000 per year, amounting on average to less than 00.785% per year of the total amount $64 Million (according to Paragraph 5 of the Complaint) invested in such Partnerships. In connection with the lawsuit resulting in the *Pozez* Order, CEC engaged Rothstein, Kass & Company, LLC—ranked the country's leading auditor of alternative investment funds, serving more than 2,500 fund clients across the country, including over 500 private equity and

venture capital funds—to examine the fees and expenses of ECP Limited Partnership Series G, including the allocation of Portfolio Expenses. Their conclusion as presented to the district judge was that the combined management fees and expenses charged to Series G was not unreasonable given their observation of other private equity funds. That conclusion must hold as well for all the other ECP Limited Partnerships.

The ECP Limited Partnership Agreements Permitted Amendments to Authorize the General Partner To Be the Lender of Last Resort During the Financial Crisis

24. In answer to Paragraph 24 of the Complaint, Respondents deny each and every allegation, and further allege that

a) As the financial crisis deepened in 2008, some of the ECP Limited Partnerships' reserves for paying management fees and reimbursing Partnership Expenses to CEC had become depleted, and therefore such partnerships were or would become delinquent in paying such fees and expenses, and CEC would not have the cashflow necessary to remain in operation.

b) Neither CEC nor any of the ECP Limited Partnerships could, in the depths of the financial crisis, find any conventional source of financing. CEC on three separate occasions approached over 40 institutional and alternative lenders seeking loans on behalf of the ECP Limited Partnerships with not one of them showing any interest.

c) In order for CEC to remain viable to continue to act for the benefit of the ECP Limited Partnerships and their limited partners, either (a) CEC needed to sell all or some of the ECP Limited Partnerships' interests in Portfolio Companies, or (b) Mr. Brittenham and CEC's co-founder needed to infuse personal funds into CEC.

d) To sell interests in the Portfolio Companies on a distressed basis in the depths of the recession would have been severely detrimental to the ECP Limited Partnerships and their limited partners, possibly wiping out their investments.

e) Therefore, Mr. Brittenham and CEC's co-founder personally infused over $1 Million to keep CEC in business so that it could continue to act as general partner of the ECP Limited Partnerships, and actively monitor and participate in the management of the Portfolio Companies for the benefit of the limited partners.

f) No loans were actually made by CEC to the ECP Limited Partnerships, and no funds were actually delivered to such partnerships. Rather, the existing and accumulating debts of such partnerships to CEC on account of unpaid management fees and Partnership Expenses were *documented* by promissory notes secured by the assets of the partnerships.

g) CEC was advised by accounting and legal counsel that it was necessary to document the obligations of the ECP Limited Partnerships to CEC, and that the limited partnership agreements would need to be amended to incur the indebtedness. Afterwards, the district court in the *Pozez* Order held that the amendments to the ECP Limited Partnerships' agreements and the documenting of such debt by the giving and taking of such promissory notes were not a breach of the limited partnership agreement, not a breach of fiduciary duty, and could not be the basis of a federal securities fraud claim.

25. In answer to Paragraph 25 of the Complaint, Respondents deny each and every allegation, except admit that the nominal interest rate stated in the Promissory Notes was 10% above prime, adjusted quarterly, and further aver that the market rate of interest for debt of the

quality, risk and illiquidity of the ECP Limited Partnerships, had any such loan even been available, would have been at least that much. However, Respondents further allege that the nominal interest rate was academic inasmuch as by November 2012, CEC had written off and waived approximately $1.3 Million, being approximately 57%, of the interest that had accrued under the Promissory Notes, effectively reducing the true interest to well below market rates. Respondents also aver that Mr. Brittenham executed and delivered the Promissory Notes and Pledges as an officer of CEC both on behalf of CEC and on behalf of CEC as general partner of the ECP Partnerships.

26. In answer to Paragraph 26 of the Complaint, Respondents deny each and every allegation, and further allege that the district court in the *Pozez* Order specifically found that Respondents' conduct in creating the Promissory Notes and Pledges to document the accumulating debt of the ECP Limited Partnerships to CEC for unpaid management fees and Partnership Expenses was not self-dealing, not a breach of fiduciary duty, and not fraud.

27. In answer to Paragraph 27 of the Complaint, Respondents deny each and every allegation, except admit that the limited partnership agreements of the ECP Limited Partnerships needed to be amended to authorize CEC as their general partner to incur debt and to borrow money on their behalf, and further allege that pursuant to Section 14.2 of the limited partnership agreements CEC had "the authority to amend or modify [the] Agreement without any vote or action by the other Partners: . . . (b) to reflect any change or changes to the terms of the Agreement that the General Partner determines, in its good faith judgment, is in the best interest of the Partnership and which could not, individually or in the aggregate, have a material adverse effect on any individual Limited Partner or on the Partnership as a whole." Respondents further allege that the consequences of the financial crisis of 2008 rendered it in the best interests of the limited

partners for the ECP Limited Partnerships to borrow funds, because the only alternative at the time would have been to sell partnership assets at "fire sale" prices to the greater detriment of the partnerships and their investors. One of the ECP Limited Partnerships that took this course was Series G, and as to that Limited Partnership, the district court in the *Pozez* Order held that CEC's actions in amending the limited partnership agreement and causing that Limited Partnership to issue secured promissory notes to CEC were permitted by the limited partnership agreement and Delaware law, not self-dealing, and could not be fraud.

28. In answer to Paragraph 28 of the Complaint, Respondents deny each and every allegation. The amending of the limited partnership agreements to permit the accruing of debt, the issuance of the Promissory Notes and Pledges were all made necessary by the financial crisis of 2008 and later years, and the alternative would have resulted in the significant or total loss of the value of the assets of the ECP Limited Partnerships. All such actions were taken in consultation with accounting and legal counsel, and no actions were taken against any such advice. Therefore, these actions were not taken with any intent to deceive, but as emergency measures to salvage the ECP Limited Partnerships and their value for their investors. Under these circumstances, *scienter* does not exist.

29. In answer to Paragraph 29 of the Complaint, Respondents deny each and every allegation, and expressly allege that the limited partners of the affected ECP Limited Partnerships were given adequate disclosure of the facts and circumstances surrounding the Promissory Notes and Pledges.

30. In answer to Paragraph 30 of the Complaint, Respondents deny each and every allegation, and further repeat and reallege their responses to Paragraphs 1 through 29 of the Complaint for their further answer to Paragraph 30 of the Complaint.

31. In answer to Paragraph 31 of the Complaint, Respondents deny each and every allegation, and further allege that under these circumstances the ECP Limited Partnerships' issuance of secured promissory notes to CEC was not in connection with a purchase or sale of a security within the meaning of the federal securities laws.

32. In answer to Paragraph 32 of the Complaint, Respondents deny each and every allegation. As set forth above, the district court in the *Pozez* Order reviewed one instance of these exact transactions and held that they were permitted by the limited partnership agreement and Delaware law; they did not constitute self-dealing; they were neither breach of contract nor of fiduciary duty; and they could not be fraud. Respondents further assert that § 206(3) of the Advisers Act cannot be read so as to nullify the rights, obligations, privileges and powers of general partners of private equity funds as established by preexisting limited partnership agreements that are valid under Delaware law.

CEC Appropriately Modified its Internal Methodology for Calculating Preferential Distributions So that Limited Partners Received the Amounts to Which They Were Entitled Under the Appropriate Limited Partnership Agreements

33. In answer to Paragraph 33 of the Complaint, Respondents deny each and every allegation, except admit that in 2011 CEC (a) observed that the mathematical results of the methodology it had created to calculate preferred distributions to limited partners was yielding absurd results inconsistent with a reasonable reading of the limited partnership agreements, (b) sought professional guidance from Scott Cederburg, Ph.D., Assistant Professor of Finance at the Eller College of Management of the University of Arizona, to identify the source of the erroneous results and to determine how to correct the methodology so that the amount of distributions would be consistent with a reasonable reading of the limited partnership agreements; and (c) adopted

Prof. Cederburg's recommendations; and expressly deny that any limited partner's distribution as provided for by the relevant limited partnership agreement was impacted, and thus that nothing needed to be disclosed. Nevertheless, CEC fully disclosed its methodology to any limited partner who inquired. Respondents further contend that each limited partnership agreement is silent regarding the methodology used to calculate the preferred return. Accordingly the calculation of the preferred return hurdle is in the general partner's discretion, and the general partner, in revising the calculation, had a reasonable good faith basis for determining that it was appropriate.

34. In answer to Paragraph 34 of the Complaint, Respondents deny each and every allegation, except admit that distributions to limited partners of the ECP Limited Partnerships were governed by the terms of the various limited partnership agreements, and they respectfully refer to such agreements for the contents thereof.

35. In answer to Paragraph 35 of the Complaint, Respondents deny each and every allegation, except admit the limited partners of the ECP Limited Partnerships were entitled to a preferential return on their investments from annual distributions ahead of the general partner as specified in the limited partnership agreements, and they respectfully refer to such agreements for the contents thereof.

36. In answer to Paragraph 36 of the Complaint, Respondents deny each and every allegation, except aver that the method CEC had previously used to calculate distributable amounts yielded absurd results when distributions were deferred, due to the effects of compounding being erroneously applied. As a result, limited partners were being calculated as being due amounts greatly in excess of what was reasonably provided for under the limited partnership agreements, with the result that the preferential rate might never be achieved in future years and the general partner might never receive the distribution due to it under the agreements.

37. In answer to Paragraph 37 of the Complaint, Respondents deny each and every allegation, except admit that in or around August 2011 CEC adopted, after consultation with its accountants, the revisions to its distribution formula recommended by Prof. Cederburg in order to derive preferential distributions to limited partners that were consistent with what was reasonably due to such partners under the relevant limited partnership agreements; and expressly deny that any limited partner was deprived of any right or interest provided by the relevant limited partnership agreement.

38. In answer to Paragraph 38 of the Complaint, Respondents deny each and every allegation, except admit that in or around August 2011 CEC adopted, after consultation with its accountant, the revisions to its distribution formula recommended by Prof. Cederburg in order to derive preferential distributions to limited partners that were consistent with what was reasonably due to such partners under the relevant limited partnership agreements; and expressly deny that any limited partner was deprived of any right or interest provided by the relevant limited partnership agreement.

39. In answer to Paragraph 39 of the Complaint, Respondents deny each and every allegation, except admit that in or around August 2011 CEC adopted, after consultation with its accountants, the revisions to its distribution formula recommended by Prof. Cederburg in order to derive preferential distributions to limited partners that were consistent with what was reasonably due to such partners under the relevant limited partnership agreements; and expressly deny that any limited partner was deprived of any right or interest provided by the relevant limited partnership agreement, and therefore that any disclosure was required. Nevertheless, CEC made its distribution formulas available to any limited partner that requested information about it.

40. In answer to Paragraph 40 of the Complaint, Respondents deny each and every allegation, except admit that in or around August 2011 CEC adopted, after consultation with its accountants, the revisions to its distribution formula recommended by Prof. Cederburg to correct errors in the methodology previously used to calculate preferential distributions to limited partners so as to render the amounts of such distributions consistent with what was reasonably due to such limited partners under the relevant limited partnership agreements; and expressly deny (a) that any limited partner was deprived of any right or interest provided by the relevant limited partnership agreements, (b) that any disclosure of CEC's internal calculation methodology was required; and (c) that Respondents acted with any fraudulent intent in correcting its internal calculations methodologies.

Respondents Did Not Fraudulently Induce Steve Roth to Invest in ECP Limited Partnership Series R

41. In answer to Paragraph 41 of the Complaint, Respondents deny each and every allegation, except admit that:

a) On or about July 6, 2006, Steve Roth ("Roth") became a limited partner of ECP Limited Partnership Series I. Roth invested $2 million, which gave him a 74.76% interest in that limited partnership. Neither Mr. Brittenham nor CEC's co-founder was a limited partner of LCP Limited Partnership Series I.

b) The sole investment of ECP Limited Partnership Series I was 249,234 limited liability company interests in Advanced BioEnergy, LLC ("ABE"). Accordingly, Roth had acquired through Series I an indirect interest in approximately 186,327 LLC units of ABE at a per unit price of about $10.73.

c) By 2009, the full impact of the financial crisis had substantially eroded the value of ABE, and ABE desperately needed to raise capital. It had secured partial financing from a venture capital firm, with the result that the ownership interests of prior investors, including Series I and, indirectly, Roth, would be diluted.

d) In connection with that financing, an in order to permit existing investors the opportunity to mitigate that dilution, ABE offered in a private placement an additional 2,466,666 LLC units at a significantly discounted price of $1.50 per unit.

e) In order to allow its clients to take advantage of the opportunity to minimize dilution of their interests, and to lower the average cost of their imputed total indirect investments in ABE, CEC created ECP Limited Partnership Series R, T and V for the express purpose of acquiring some of these new ABE LLC units.

f) LCP Limited Partnership Series R, S and V acquired in the aggregate 1,187,149 of the new ABE LLC units—about 48% of the total number offered. By June 8, 2010, ABE had announced that all offered units had been sold and its full funding needs met.

g) In connection with these transactions, CEC approached the limited partners of ECP Limited Partnership Series I, including Roth, to determine their interest participating, through ECP Limited Partnership Series R, in the newly offered ABE LLC units.

h) In the course of those discussions, Roth inquired how much Mr. Brittenham and CEC's co-founder would personally invest in the new ABE LLC units through ECP Limited Partnership Series R.

42. In answer to Paragraph 42 of the Complaint, Respondents deny each and every allegation, and expressly deny that they ever represented to Roth how much Mr. Brittenham or CEC's co-founder had invested or would invest in ECP Limited Partnership Series R.

43. In answer to Paragraph 43 of the Complaint, Respondents deny each and every allegation, except admit that emails were exchanged between Steven Roth and CEC's former Chief Financial and Compliance Officer, Howard Schildhouse ("Schildhouse") concerning how much Mr. Brittenham and CEC's co-founder had invested or would invest in ECP Limited Partnership Series R, and expressly deny that Mr. Brittenham responded to such inquiries or authorized Schildhouse to so respond.

44. In answer to Paragraph 44 of the Complaint, Respondents deny each and every allegation, except admit that Schildhouse sent an email to Mr. Brittenham, while Mr. Brittenham was out of town, purporting to resign from CEC (for the third or fourth time), and respectfully refer to said email for the contents thereof. Respondents further aver that upon Mr. Brittenham's return to the office, he and Schildhouse had a conversation in which Schildhouse acknowledged that Mr. Brittenham had only authorized Schildhouse to say that he and his co-founder would invest "up to $100,000" in the ABE Units then being offered by ABE, not that each would invest $100,000 definitively. Thereafter, although relieved at his request of his position as CEC's Chief Financial and Compliance Officer, Schildhouse remained an employee or consultant of CEC for some time thereafter.

45. In answer to Paragraph 45 of the Complaint, Respondents deny each and every allegation, except admit that Roth purchased $250,000 in, and that Mr. Brittenham and CEC's co-founder each purchased $25,000 in, ECP Limited Partnership Series R. In total, $620,000 was invested by 18 investors in ECP Limited Partnership Series R, with which that partnership

acquired 318,420 ABE LLC units. Roth's investment in Series R comprised a 40% interest in the Series R, significantly less than his 75% interest in Series I, and resulted in his indirect ownership of 128,402 ABE LLC units. Thus, Roth, through his ownership of ECP Limited Partnership Series I and R, indirectly owns approximately 314,795 ABE LLC units at an approximate average cost of $7.15. Roth has not complained to CEC about his investments in Series R, which is no surprise since, on account of his $250,000 investment, he has already received $339,000 in cash distributions and his interest in Series R is currently valued to be about $230,000.

46. In answer to Paragraph 46 of the Complaint, Respondents deny each and every allegation, and further aver that (a) Mr. Brittenham did not make or authorize any statements to Roth concerning the precise amount of his own personal investments in ECP Limited Partnership Series R; (b) Schildhouse did not make any such statement to Roth, in that he purported to resign before making any such statement; (c) Roth had no reasonable basis for believing that Mr. Brittenham would invest any specific amount in ECP Limited Partnership Series R; (d) in any event, whatever Roth might claims to be personally "material" to him is irrelevant to this proceeding, as the test of materiality under the federal securities laws is normative and rests on what a reasonable investor would deem important to an investment decision, not what Roth or any particular investor claims to be important.

47. In answer to Paragraph 47 of the Complaint, Respondents deny each and every allegation, and further aver that (a) Mr. Brittenham did not make or authorize any statements to Roth concerning the precise amount of his own personal investments in ECP Limited Partnership Series R; (b) Schildhouse did not make any such statement to Roth, in that he purported to resign before making any such statement; (c) Roth had no reasonable basis for believing that Mr. Brittenham would invest any specific amount in ECP Limited Partnership Series R; (d) in any

event, whatever Roth might claims to be personally "material" to him is irrelevant to this proceeding, as the test of materiality under the federal securities laws is normative and rests on what a reasonable investor would deem important to an investment decision, not what Roth or any particular investor claims to be important.

48. In answer to Paragraph 48 of the Complaint, Respondents deny each and every allegation, and further aver that (a) Mr. Brittenham did not make or authorize any statements to Roth concerning the precise amount of his own personal investments in ECP Limited Partnership Series R; (b) Schildhouse did not make any such statement to Roth, in that he purported to resign before making any such statement; (c) Roth had no reasonable basis for believing that Mr. Brittenham would invest any specific amount in ECP Limited Partnership Series R; (d) in any event, whatever Roth might claims to be personally "material" to him is irrelevant to this proceeding, as the test of materiality under the federal securities laws is normative and rests on what a reasonable investor would deem important to an investment decision, not what Roth or any particular investor claims to be important.

CEC Did Not Have "Original Stock Certificates" Requiring a Qualified Custodian, And CEC Segregated Funds as Recommended by Bank of America, N.A.

49. In answer to Paragraph 49 of the Complaint, Respondents deny each and every allegation, and further aver that

a) The Division's allegation that "CEC kept original stock certificates for securities owned by the ECP [Limited Partnerships] in its office" is false, *because there are no original stock certificates for any such securities.* The ECP Limited Partnerships own only equity interests, acquired in private offerings, in the Portfolio Companies, all of which are limited liability companies, not corporations.

b) The ECP Limited Partnerships' membership interests in each Portfolio Company is evidenced contractually by the existence of a member's account on the books and records of each such company. There are no "original stock certificates." These equity interests are inchoate contract rights, and are not evidenced by negotiable instruments or documents of presumptive ownership that are in any way analogous to "original stock certificates."

c) While such limited liability companies typically do not issue certificates of membership interests, E Energy Broken Bow, LLC, did issue one to ECP Limited Partnership Series D; that certificate was cancelled in 2010 when E Energy Broken Bow dissolved. Another, Granite Falls Energy, LLC sent ECP Limited Partnership Series A a simple letter confirming its LLC membership. However, such documents are not negotiable nor even legally conclusive of the ECP Limited Partnerships' ownership of LLC interests; they cannot bear the importance connoted by the phrase "original stock certificate."

d) In the end, the ECP Limited Partnerships' membership interests in the various limited liability companies in which they have invested is definitively established by the proof of the investments themselves, as shown in the banking records of those Partnerships. There are no documented "securities" which a custodian could take custody of. Moreover, the membership interests in the Portfolio Companies are transferable only with the prior consent of the Portfolio Companies and issued them and/or the ECP Limited Partnerships that own them.

e) Accordingly, the assets of the ECP Limited Partnerships were not lost, were never at risk of loss, and no investors were harmed or ever put at risk of being harmed.

50. In answer to Paragraph 50 of the Complaint, Respondents deny each and every allegation, except admit that for a short time, the funds of the ECP Limited Partnerships were maintained at Bank of America, N.A., in accounts recommended by such bank for related entities like the ECP Limited Partnerships. CEC understood that under this banking program, each ECP Limited Partnership would have a separately maintained account, but that all deposits and withdrawals would occur through a master administrative account. Each deposit and withdrawal was identified to a specific ECP Limited Partnership and credited or debited from the account of such Limited Partnership. Upon being advised that the Commission staff viewed this arrangement as a violation of the Advisers Act, CEC immediately terminated it and reopened separate checking accounts for each of the ECP Limited Partnerships. At all times, the funds of each ECP Limited Partnership were under the custody and control of Bank of America, N.A.; no funds of any one Partnership were deposited into the account of any other Partnership; and no funds of any Partnership were lost or at risk of loss, and no investor was ever harmed or put at risk of being harmed.

CEC's Compliance Policies Were Created by, and Adopted By CEC Upon the Advice of, its Legal Counsel

51. In answer to Paragraph 51 of the Complaint, Respondents deny each and every allegation, except admit that its compliance policies were prepared by its legal counsel with active involvement by CEC. To claim that CEC's compliance policies were "inadequate" because an "or" was misplaced for an "and"—a minor scrivener's error of *de minimus* consequence—is ludicrous, especially as the Division admits that the error was corrected as soon as it was discovered. The existence of one minor—*one typographical*—error in a compliance manual does

not render CEC's entire compliance policies "inadequate," and the Division betrays its pettiness in even making such an accusation.

52. In answer to Paragraph 52 of the Complaint, Respondents deny each and every allegation, except admit that its compliance policies were prepared by its legal counsel with active involvement by CEC, and further allege that no investor was ever harmed or put at risk of being harmed by reason of this minor error in CEC's compliance manual.

CEC Appropriately Omitted its Co-Founder's Prior SEC Violations from Offering Documents Issued After Such Co-Founder Ceased to be a Manager of CEC In Reliance on Commission Regulation S-K

53. In answer to Paragraph 53 of the Complaint, Respondents deny each and every allegation, and further allege that:

a) By 2008, CEC's co-founder had ceased to be a manager of CEC, was not involved in the day-to-day activities of CEC and his status was reduced to a consultant of CEC. His 50% voting interest in CEC ensured that he had no voting control or power to change or influence the management of CEC. In particular, he could not under any circumstance remove Mr. Brittenham as the sole manager of CEC or counteract any of his management decisions. Accordingly, by 2008, Mr. Brittenham was the sole manager of CEC, as well as the holder of 85% of the economic interest in CEC.

b) CEC's co-founder was sanctioned by an order of the Commission, dated July 11, 2002 (the "Sanction Order").

c) As in effect in 2008, Item 401 of Regulation S-K required managers of an issuer to disclose, in certain circumstances, in private placement memoranda, orders like the

Sanction Order only for a period of five (5) years. Further, disclosure of matters set forth in subpart (f) of Item 401 of Regulation S-K applies only to managers, promoters and control persons. (See Item 401(g) of Regulation S-K.)

d) The PPMs for ECP Limited Partnership Series R and T were dated December 11, 2008, and August 26, 2009, respectively. Both offerings closed in October 2009. Those PPMs disclosed that Mr. Brittenham was the sole manager of CEC and CEC's co-founder was only a consultant. Accordingly, disclosure of the Sanction Order was not required under Regulation S-K because (a) it was more than five years old, and (b) CEC's co-founder was not a manager, control person or promoter of CEC.

e) Effective February 28, 2010, Item 401 of Regulation S-K was amended to require managers of an issuer to disclose, in certain circumstances, in private placement memoranda, orders like the Sanction Order for a period of ten (10) years.

f) The PPM for ECP Limited Partnership Series V was drafted in January and February of 2010 and was dated May 1, 2010, and the offering closed in June 2010. That PPM disclosed that Mr. Brittenham was the sole manager of CEC and CEC's co-founder was only a consultant. Disclosure of the Sanction Order was not required in that PPM under Regulation S-K because CEC's co-founder was not a manager, control person or promoter of CEC.

54. In answer to Paragraph 54 of the Complaint, Respondents deny each and every allegation, except reallege their response to Paragraph 53 of their complaint for their answer to Paragraph 54, and further allege that CEC's legal counsel reviewed the PPMs of ECP Limited Partnership Series R, T and V drafted by CEC, and that CEC relied in good faith on such

counsel's advice regarding whether disclosure of the Sanction Order was required under Regulation S-K, and therefore did not act "willfully," nor with any other form of *scienter*.

55. In answer to Paragraph 55 of the Complaint, Respondents deny each and every allegation, except reallege their response to Paragraph 53 of their complaint for their answer to Paragraph 55, and further allege that after 2008, CEC's co-founder was neither a control person nor promoter or manager of CEC.

E. RESPONDENTS DENY ALL ALLEGED VIOLATIONS

56. In answer to Paragraph 56 of the Complaint, and by reason of all of the foregoing, Respondents deny each and every allegation.

57. In answer to Paragraph 57 of the Complaint, and by reason of all of the foregoing, Respondents deny each and every allegation.

58. In answer to Paragraph 58 of the Complaint, and by reason of all of the foregoing, Respondents deny each and every allegation.

59. In answer to Paragraph 59 of the Complaint, and by reason of all of the foregoing, Respondents deny each and every allegation.

60. In answer to Paragraph 60 of the Complaint, and by reason of all of the foregoing, Respondents deny each and every allegation.

61. In answer to Paragraph 61 of the Complaint, and by reason of all of the foregoing, Respondents deny each and every allegation.

RESPONDENTS' AFFIRMATIVE DEFENSE

62. To the extent that any element of the Complaint depends on acts occurring prior to February 25, 2009, the Complaint is barred by the applicable statute of limitations and equitable principles of laches.

63. To the extent that any element of the Complaint is inconsistent with the holding of the *Pozez* Order, the Complaint is barred by the doctrines of *res judicata* and/or collateral estoppel.

* * *

THEREFORE, Respondents demand a Decision as follows:

A. That each and every allegation of the Complaint be found not to be true or not to prove a violation of any provision of the Securities Act of 1933, the Exchange Act of 1934 or the Investment Advisers Act of 1940, in each case as amended, and therefore that the Complaint be dismissed in its entirety; and

B. That no remedial actions, neither disgorgement nor civil penalties, be found to be appropriate in the public interest against any Respondent for any violation of any provision of the Securities Act of 1933, the Exchange Act of 1934 or the Investment Advisers Act of 1940, in each case as amended; and

C. That no Respondent be ordered to cease and desist committing or causing violations of and any future violations of any provision of the Securities Act of 1933, the Exchange Act of 1934 or the Investment Advisers Act of 1940, in each

case as amended, or of Section 9 of the Investment Company Act, as to which the Division alleges nothing in the Complaint; and

D. Granting such other and further relief as to the Administrative Law Judge seems just and proper.

Dated: New York, New York
March 26, 2014

STERN, TANNENBAUM & BELL, LLP

By_____
Aegis J. Frumento, Esq.
Stephanie Korenman, Esq.
Members of the Firm

Attorneys for Respondents
CLEAN ENERGY CAPITAL, LLC
and SCOTT A. BRITTENHAM

380 Lexington Avenue, Suite 3300
New York, NY 10168
212-792-8979
212-792-8980

afrumento@sterntannenbaum.com
skorenman@sterntannenbaum.com

EXHIBIT A

WO

IN THE UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF ARIZONA

MITCHELL POZEZ and NEIL KLEINMAN,

Plaintiffs/Counterdefendants,

vs.

CLEAN ENERGY CAPITAL, LLC f/k/a ETHANOL CAPITAL MANAGEMENT, L.L.C., a Delaware limited liability company; SCOTT BRITTENHAM and JANE DOE BRITTENHAM; GARY SCHWENDIMAN and JANE DOE SCHWENDIMAN; ABC CORPORATIONS I-V; XYZ PARTNERSHIP I-X; JOHN DOES I-V,

Defendants/Counterclaimants.

CLEAN ENERGY CAPITAL, LLC f/k/a ETHANOL CAPITAL MANAGEMENT, L.L.C., as general partner of and on behalf of, ETHANOL CAPITAL PARTNERS, L.P., SERIES G.,

Third Party Plaintiff,

vs.

NOK & MTP, L.L.C.,

Third Party Defendant

No. 07-CV-00319-TUC-CKJ

ORDER

Pending before the Court are Plaintiffs' Motion for Partial Summary Judgment re Count VIII – For Removal/Expulsion of CEC as General Partner of Series G; Pursuant to Del. Code Ann. Tit. 6 § 15-601(5) [Doc. 135] and Motion for Partial Summary Judgment on Issue of Allocated and Direct Expenses [Doc. 142], and Defendants' Cross-Motion to Dismiss Counts I-III and V-VIII of the Amended Complaint [Doc. 147].[1]

I. FACTUAL BACKGROUND

Clean Energy Capital, L.L.C. ("CEC") is the new name of Ethanol Capital Management, L.L.C. ("ECM"), a Delaware limited liability company, authorized to conduct business in Arizona. All relevant documents are in ECM's name; however, in light of the name change reflected in the docket, this Court adopts CEC as the general partner's proper name. CEC is the General Partner of Ethanol Capital Partners, L.P., Series G, a Delaware limited partnership ("ECP"). Defendant Scott Brittenham ("Brittenham") is the Chief Executive Officer of, and former consultant for CEC. Defendant Schwendiman ("Schwendiman") was the Chairman of CEC. Plaintiffs contend that these Defendants were, at all times relevant to this matter, managers of the General Partner Defendant CEC; however, Defendants dispute this assertion. Defendant Schwendiman retired as manager of the General Partner on June 1, 2007. Since that time, Defendant Schwendiman has not participated in the management of CEC.

Plaintiffs Pozez and Kleinman met Defendants Brittenham and Schwendiman in September 2005, when Plaintiffs were looking for an opportunity to invest in the ethanol production business. Plaintiffs' aver that "[o]ver the course of several conversations, Defendants Brittenham and Schwendiman suggested to Plaintiffs that they might personally invest in ECP's ethanol production efforts." Pls.' SOF [Doc. 136] at ¶ 5. Defendants object

[1]Also pending before the Court is Defendants' Cross-Motion for Leave to File a Motion to Compel (embedded within their Response/Cross-Motion).

to this last statement; however, Defendant Brittenham's affidavit does not clearly controvert it.[2] *See* Defs.' Exh. W at ¶ 12.

Defendants Brittenham and Schwendiman suggested to Plaintiffs that they could assist Defendants' business by identifying other potential investors for ECP's ethanol production business. Plaintiffs identified personal friends and relatives as potential investors. Plaintiffs then introduced these potential investors to Defendants for sales presentations in Tucson, Arizona. After these meetings, some of the potential investors did invest in Defendants' business. Ultimately, Defendants raised $6,000,000.00 in Series G, which included money from Plaintiffs and their friends and relatives.

Plaintiffs aver that the "venture was memorialized in two documents – the Limited Partnership Agreement ("LPA") and the Series G Private Placement Memorandum ("PPM")." Pls.' SOF [Doc. 136] at ¶ 11. Furthermore, "[t]he PPM represented to all of the potential investors/limited partners the expenses that would be allocable among the various series of similar limited partnerships, and the expenses that would be borne solely by the individual series limited partnerships." *Id.* at ¶ 12. Defendants argue that these two paragraphs misstate the evidence, because the PPM clearly states that:

> The transactions contemplated by this Private Placement Memorandum will be governed by the Limited Partnership Agreement. Any inconsistencies between this memorandum and such document are governed by the limited partnership agreement. The information contained herein should be read subject to the limited partnership agreement, a copy of which will be furnished to prospective investors prior to any commitment.

Defs.' Obj. to Plaintiffs' "SOF," Exh. "T" [Doc. 145] at 2. Regarding expenses, the PPM dictates as follows:

> The Management Company will be required to pay for all "Management Expenses". Management Expenses will mean the costs and expenses incurred

---

[2] During his deposition Plaintiff Pozez recalls meeting Defendants at Millie's Pancake House and then again at Defendants' offices; Plaintiffs Pozez and Kleinman discussed direct investment and putting together their own series. Plaintiff Kleinman's deposition is consistent with this recollection. Defendants' Answer unequivocally denies that Defendants Brittenham and Schwendiman solicited investments. This is true to the extent that Plaintiff Pozez initially reached out to Defendant Brittenham.

by the Management Company in providing for its normal operating overhead, including, but not limited to, compensation of its employees and the cost of providing relevant support and general services for its operations, but not including any Partnership Expenses described below.

The Partnership will be responsible for all reasonable and necessary Organizational Expenses and Operational Expenses (collectively, the "Partnership Expenses").

"Organizational Expenses" will mean all reasonable third-party and out-of-pocket expenses, including, but not limited to; attorneys' fees, auditors' fees, consulting fees, structuring fees, travel and other expenses incurred by the Partnership, the General Partner, the managers of the General Partner, the Management Company, the Partnership Series G Program Monitors or any affiliates thereof in connection with any activities having to do with the organization or development of the Partnership or preliminary entities to the Partnership (including the formation of such entities) any Alternative Investment Vehicle or Parallel Regulatory Vehicle and the initial and subsequent development and closings of any Series of the Partnership, any Alternative Investment Vehicle or Parallel Regulatory Vehicle.

"Operational Expenses" will mean, to the extent not reimbursed by a prospective or actual portfolio company, if any, all reasonable expenses of operation of the Partnership, including, but no limited to; Management Fees, Carried Interest Distributions, expenses of the Advisory Board, any taxes imposed on the Partnership, commitment fees payable in connection with credit facilities, accounting fees, third-party fees and expenses, attorney's fees, due diligence, research, travel, office, marketing and related expenses as well as costs related to the acquisition or disposition of securities, whether or not the transaction is consummated, insurance, indemnification expenses, and the costs and expenses of any litigation involving the Partnership and the amount of any judgments or settlements paid in connection therewith.

Partnership Expenses will be applied to an Investor's Capital Account. In all matters regarding Partnership Expenses, the General Partner has the authority, in its sole discretion, to allocate expenses as it deems proper.

Pls.' Exh. "2" at 23-4 (punctuation errors in original). Regarding expenses, the LPA states:

8.1 Partnership Expenses.

Partnership Expenses for any Series shall be paid from time to time by a reduction in the Capital Account of a Partner. Each Limited Partner's share of Partnership Expenses shall be the portion thereof which such Partner's Capital Contribution minus such Partner's Load represents of the sum of Capital Contributions of all Partners holding Interest in a Series minus the sum of Loads of all Partners holding Interest in such Series. The Partnership will be responsible for, and pay, all other reasonable expenses ("Partnership Expenses") including but not limited :

(i) all expenses incurred in connection with Partnership operations, to the extent not reimbursed by a portfolio company, if any, including, but not limited to: Management Fees, Carried Interest Distributions, if due, expenses of the Advisory Board, Program Monitor Fees, structuring fees, organizational fees, marketing fees, third party fees, fees for due

diligence, research, travel, development, marketing, office and other related expenses and costs related to decision making for the acquisition or disposition of securities, or with the purchase, holding, sale or proposed sale of any Partnership investments including all third party out-of-pocket costs and expenses of custodians, paying agents, registrars, counsel and independent accountants, unless such costs or expenses are paid for by the proposed Portfolio Company;

(ii) all costs incurred in connections with the preparation of or relating to reports made to the Partners;

(iii) all costs related to litigation involving the Partnership, directly or indirectly, including attorneys' fees incurred in connection therewith;

(iv) all costs related to the Partnership's indemnification or contribution obligations set forth in section 11;

(v) interest on and fees and expenses arising out of all borrowings made by the Partnership, including, but not limited to, the arranging thereof,

(vi) the costs of any litigation, director and officer liability or other insurance and indemnification or extraordinary expense or liability relating to the affairs of the Partnership;

(vii) all unreimbursed out-of-pocket expenses relating to transactions that are not consummated including legal, accounting and consulting fees and all extraordinary professional fees incurred in connection with the business or management of the Partnership;

(viii) all expenses of liquidating the Partnership; and

(ix) any taxes, fees or other governmental charges levied against the Partnership and all expenses incurred in connection with any tax audit, investigation, settlement or review of the Partnership.

8.2 Organizational Expenses.

(a) Allocation of Organizational Expenses Among Series. Organization Expenses will be allocated among Series, subject to the additional conditions stated below, by allocating to each Series at its closing the amount of total Organizational Expenses multiplied by a ratio consisting of the total Capital Contributions in the Series divided by the sum of total Capital Contributions in all Series. The amount paid by Series A will be paid to the Partnership, the General Partner, the managers of the General Partner, the Management Company or any affiliates thereof to cover Organizational Expenses. The amounts paid by each additional Series will be paid to previous Series in amounts that cause the total amount paid for Organizational Expenses by each Series to equal it pro rata portion of total Organization Expenses based on total Capital Contributions, except that no payments for Organization Expenses will be made that would be less then one-tenth of one percent (0.1%) of the total Capital Contributions in the Series receiving the payment.

> (b) Payment of Organizational Expenses by Partners. Organizational Expenses for any Series shall be paid from time to time by a reduction in the Capital Account of a Partner. Each Limited Partner's share of Organizational Expenses shall be the portion thereof which such Partner's Capital Commitment minus such Partner's Load represents of the sum of Capital Commitments of all Partners holding Interest in a Series minus the sum of Loads of all Partners holding Interest in such Series. The Partnership will be responsible for, and pay, all other ("Organizational Expenses") including:
>
> (i) all third-party and out-of-pocket expenses, including, but not limited to attorney's fees, auditor's fees, consulting fees, structuring fees, travel and other expenses, office expenses, personnel expenses, research expenses and development expenses incurred by the Partnership, the General Partner, the managers of the General Partner, the Management Company or any affiliates thereof in connection with any activities having to do with the organization, development and operation of the Partnership before any Series Closing Date or preliminary entities to the Partnership (including the formation of such entities) any Alternative Investment Vehicle or Parallel Regulatory Vehicle and the initial and subsequent closings of the Partnership, any Alternative Investment Vehicle or Parallel Regulatory Vehicle.

Defs.' Exh "U" at 36-8.

Plaintiffs Klein and Pozez were named in the PPM as the "Program Monitors" for Ethanol Capital Partners Series G. Plaintiffs' duties as Program Monitors were described in the PPM as follows:

> Mr. Neil Kleinman and Mr. Mitchell Pozez will serve as Program Monitors for Ethanol Capital Partners Series G. In this function, Mr. Kleinman and Mr. Pozez will observe the Partnership and the General Partner to monitor that the activities of the Partnership are generally proceeding as described in the Memorandum and the Partnership Agreement, as the same may be amended from time to time.
>
> The General Partner will cooperate fully and in good faith with the Partnership Series G Monitors by among other things, providing the Monitors with reports, memoranda, correspondence, financial information or other information concerning the General Partner or the Partnership. The General Partner agrees to make itself and its officers and agents reasonable [sic] available to answer questions and otherwise communicate with the Partnership Series G Monitors. The Monitors shall have reasonable access to books, records, reports, data and other information relevant to the Limited Partners or the Partnership for purposes of review and report. The Program Monitors will communicate to the General Partner any information from the Monitors or that the Monitors receive from Partners that may be helpful to Fund operations.
>
> The Partnership Series G Monitors will be compensated by the General Partner or its Affiliates in the form of assignment of a portion of the carried interest of the General Partner and compensation for certain expenses incurred. In addition, the Partnership will pay the Monitors together for providing Program Monitor services to the Fund a total fee annually of 1% of the capital contributions to the Partnership secured for the Partnership by the Program Monitors.

Pls.' Exh. "2" at 21-2. Plaintiff Pozez testified that in lieu of becoming general partners, the concept of Program Monitors was suggested by Defendants Brittenham and Schwendiman as a way for Plaintiffs Pozez and Kleinman to "become comfortable as a watchdog." Pls.' Exh. "4" at 17:8-13.

Aside from the 1% monitoring fee paid to the Program Monitors, the General Partner (CEC/ECM) was entitled to a 2% management fee. Realized Investments were to be allocated as follows:

> (i) Return of Capital: 100 percent to the Limited Partners until each Partner has received an amount equal to its capital contributions.
>
> (ii) *12 Percent Preferred Return.* 100 percent to the Limited Partners until cumulative distributions to each Limited Partner from either Distributions or Realized Investments or both combined represent a 12 percent per annum rate of interest compounded annually on such Limited Partner's capital contributions from the Series Closing Date, not including the amount designated as Return of Capital.
>
> (iii) *70/30 Split*: Thereafter, 70 percent to the Limited Partners and 30 percent to the General Partner as a Carried Interest Distribution.

Pls.' Exh. "2" at 20. Plaintiffs assert that "Defendants offered and Plaintiffs accepted a proposal by Defendants that Plaintiffs would receive 45% of the 30% to be received by CEC"; however, Defendant Brittenham has no recollection of any such agreement. Plaintiffs allege that Defendants "failed to include this agreement and, even though Brittenham acknowledged the agreement in his deposition, CEC has never taken any steps to memorialize the agreement." Pls.' SOF [Doc. 136] at ¶ 18. The record before this Court does not demonstrate that Defendant Brittenham ever made such an agreement. Plaintiffs also allege that "[d]uring the drafting process, an attorney for one of the eventual Series G limited partners, Art Leonard, observed that the LPA had missed some very important tax issues and, with the agreement of CEC, Leonard began to correspond with CEC's counsel in order to rectify some big tax issues. CEC verbally committed to pay for the tax work being done by Leonard, which was in the eventual amount of $40,000. However, CEC never paid for the work done by Leonard, which was, of course, available to be used by CEC in the documentation for each of the remaining Series Partnerships." Pls.' SOF [Doc. 136] at ¶ 19.

In support of this proposition, Plaintiffs rely on e-mails between Leonard and the law firm Baker & Donelson. Defendants' properly object to this evidence as hearsay. Even if the Court were to rely on the e-mails solely for the purpose of showing that such correspondence took place they do not support Plaintiffs' claims of an agreement for payment.

As outlined previously, the PPM sets forth the duties of the Program Monitors and provides how they would be compensated. The LPA delineates responsibilities of the General Partner regarding Financial Statements and Other Reports as follows:

> (a) Annual Audited Financial Information. Subject to the General Partner receiving all necessary information from third parties, after the end of each fiscal year of the Partnership, the General Partner shall send to each Person who was a Partner in the Partnership at any time during the fiscal year then ended an audited statement of assets, liabilities and Partners' capital as of the end of such fiscal year and related audited statements of income or loss and changes in assets, liabilities and Partners' capital, all prepared on the same basis used for the computation of adjustments to Capital Accounts.
>
> (b) Quarterly Financial Information. After the end of each calendar quarter in each year, the General Partner shall mail to each Person who is a Limited Partner on the date of dispatch unaudited summary financial information together with a narrative description of Partnership investment activities with respect to the Partnership.

Pls.' Exh. "7" at 39. These requirements are also reflected in the PPM, which states that "[t]he Partnership will furnish audited financial statements to the investors annually, and descriptive investment information quarterly. Each investor will also receive an annual financial report for each ethanol plant in which the Partnership is invested." Pls.' Exh. "2" at 25. With regard to the investment in a series and the payment of capital, the PPM provides:

> Portfolio Investments will be funded in Series. Each Series will be separately accounted for in the Partnership books and records. The capital accounts and return on investment of each Series will not be co-mingled with any other Series. The General Partner expects each Series will be open for investment until the General Partner believes adequate funds are available for Portfolio Investments in one or more ethanol production plants. The Series will be closed to new investors when the General Partner thinks it is appropriate to do so. Investors will be required to pay 100 percent of the capital commitment upon initial investment in a Series.

Id. at 18. As noted previously, the PPM provides for the Program Monitors having "reasonable access to books, records, reports, data and other information relevant to the Limited Partners or the Partnership for purposes of review and report." *Id.* at 22.

The current litigation arose from a denial of Plaintiffs Pozez and Kleinman access to the information they deemed necessary to fulfill their duties as Program Monitors. Moreover, Defendants' Tennessee counsel took the position that they were required to be licensed in order to act as Program Monitors. This Court in its July 20, 2009 Order [Doc. 110], granted Plaintiffs' Motion for Partial Summary Judgment, finding as a matter of law, that Plaintiffs Pozez and Kleinman were not required to hold specific licenses to act as Partnership Series G Monitors. On August 17, 2010, Plaintiffs' counsel sent a letter via facsimile to defense counsel asserting that Plaintiffs would seek to contact CEC, via Defendants Brittenham and/or Schwendiman, directly to resume monitoring. Defense counsel appropriately requested communication go through him in light of the ongoing litigation.

On September 10, 2009, this Court entered its Order [Doc. 114] compelling Defendants to disclose accounting documentation regarding "reimbursed" and "allocated' expenses. Accordingly, "Defendants produced a massive set of accounting documents." Pls.' SOF [Doc. 136] at ¶ 28.[3] Plaintiffs' counsel also outlines management fees; however, his math was incorrect.[4] Defendants submitted an affidavit by their Chief Financial Officer ("CFO"), Neil Hwang correcting these errors. As such, to the extent necessary, this Court will rely on Mr. Hwang's numbers.

---

[3]The Court finds that the remainder of Plaintiffs' statements in ¶¶ 28-30 are without foundation and largely argument. As such, the Court has not restated them here.

[4]Plaintiffs' counsel commented that "Mr. Hwang then sought to correct our math by a few pennies and a few dollars. Math is not contended to be the author's strongest suit. If it was, the author would be a surgeon." Pls.' Resp. to Cross-Mot. for Leave to File Mot. to Compel [Doc. 151]. The Court interprets this statement as an acceptance of Mr. Hwang's numbers.

Plaintiffs assert that in 2006, CEC did not "impose a 70/30% split of virtually all ordinary and necessary CEC business expenses down on the Series Partnerships and that, in 2006, CEC absorbed completely expenses that it both *should* have borne itself under the terms of the PPMs *and* which, in 2007, 2008, 2009, and 2010, it allocated to the Series Partnerships." Pls.' Exh. "18" [Doc. 137] at ¶ 39. Plaintiffs aver that the division of expenses in 2006 was approximately 91% CEC and 9% Series Partnerships. Defendants state that this is incorrect and the division was approximately 50/50. Plaintiffs further aver that "[f]or the entire year of 2007, the 70/30% division existed and the total of *all* CEC "only expenses was $360.76. (Exhibit 27, ECM 10/09 0278). This was in January 2007. By February 2008, CEC basically had its own expenses on a monthly basis near "zero," while it collected or accrued its management fees from all the Series Partnerships and paid or accrued 30% of the allocated expenses to itself. In 2008, CEC stopped the practice of having the Series Partnerships pay 70% of the lease payments for Mr. Brittenham's Lexus and for Safeco insurance (perhaps on the Lexus). (Exhibit 28, ECM 10/09 1233, 1237). Otherwise CEC bore almost none of its ordinary and necessary business expenses on its own."[5] Pls.' SOF [Doc. 136] at ¶¶ 49-50.

Plaintiffs use May 2008, as a "typical example," stating: "Benefit Plan Expenses, Compensation (Accounting, Administration, Executive, Financial Analysis, Marketing[)], Computer Services (Support, Data Base [sic] Development), Conferences and Meetings, Depreciation Expense, Employee Hiring Expenses, Employee Relations, Insurance (General Liability, Health, Professional Liability, Worker's Compensation[)], Leases of Office Equipment, Marketing, Office Equipment, Office Expenses, Office Supplies, Water Cooler, Payroll Taxes, Employer Taxes, FICA and Medicare, FUTA, Postage and Delivery, Printing and Reproduction, Professional Fees (401K Administration, Half the Baker & Donelson legal fees), Payroll Service Fees, Office Rent (Tucson and New York City), Telephone and Fax,

[5]Defendants failed to controvert these paragraphs; however, the Court notes that the last sentence is conclusory.

Temporary Help, and Travel and Entertainment (Meals and Travel) were all charged 70% to the Series Partnerships." Pls.' SOF [Doc. 136] at ¶ 51.

Plaintiffs further aver that "[i]n the fall of 2009, [Defendant] Brittenham, who held a seat on the E Energy Adams Board of Directors based upon the Series G investment into that facility, was kicked off the Board for alleged self-dealing. Brittenham hired counsel in Nebraska and filed suit. The fees associated with that litigation have been charged to Series G as so-called direct expenses. Eventually, the Nebraska suit settled, with E Energy Adams reinstating Brittenham for a nanosecond, or so, after which he resigned in favor [of] another CEC employee, CFO Neil Hwang." Pls.' SOF [Doc. 136] at ¶¶ 53-4. Defendant Brittenham describes the situation as follows:

> The E Energy Adams lawsuit referenced by [Plaintiffs] Pozez and Kleinman was in ECP's critical financial interest. E-Energy Adams, LLC (EEA) was formed in 2005 for the purpose of developing and operating a corn-based ethanol plant near Adams, Nebraska. ECP is the major (*i.e.*, largest) investor with an agreed upon right to appoint one director to the EEA Board. I was appointed to that board position in 2008. I concluded that the executive management was mismanaging the company and the Board was not properly overseeing management so I challenged it. Things came to a critical head when the Board accepted a proposal to purchase convertible notes, which would have diluted ECP's ownership interest compared to a more favorable rejected proposal. The result was that the Board removed me "for cause," *i.e.*, citing a business relationship which I had previously disclosed. The lawsuit resulted in my reinstatement as a board member by the Board of Directors followed by the appointment of CEC's CFO, Neil Hwang, to the Board. CEC has in the past taken active steps for management change in the event Mr. Brittenham in good faith believes the portfolio companies are not performing and management is unresponsive. As was the case with E Energy Adams, CEC has actively advocated for management change on another company in which case the CEO was ultimately removed. This portfolio company is now performing significantly better than when the former CEO and executive management were in charge. This activist approach takes a significant amount of time and effort on the part of CEC and its management.

Defs.' Exh. "W" [Doc. 145] at ¶ 5.

Plaintiffs state that after the resignation of former CEC CFO Howard Schildhouse in the fall of 2009, "a few expenses previously allocated among the Series Partnerships, mainly legal expenses, have now been borne strictly by CEC." Pls.' SOF [Doc. 136] at ¶ 55. Plaintiffs' argue that in February 2010, CEC "paid $600 on its own for registration." *Id.* at ¶ 56. Whereas, in February, 2007, "CEC allocated payment of the same registration among

the Series Partnerships. *Id.* at ¶ 57. Defendants object because the evidence submitted does not support these contentions. The Court agrees with this objection, and notes that although the general category "Taxes" is the same, the specific line items do not match up.

Plaintiffs further aver that with respect to the direct expenses of $944,858.22, incurred over the life of Series G, the largest single item is CEC's management fees totaling $482,944.44. The second largest item is legal fees in the amount of $275,118.80. Moreover, Plaintiffs argue that "[a] review of the basis for the legal fees shows that virtually all of the fees for which no details have ever been provided based upon a claim of attorney-client privilege – are associated with the present litigation and the aforementioned E Energy Adams litigation." Pls.' SOF [Doc. 136] at ¶ 61.

The third largest expense category is the interest charged by CEC on two (Defendants correct this to be 3) 3-year promissory notes for $275,000 each. The interest rate was 10 points over prime (15% and 13.25%), and the total amount of interest charged is $86,585.84. Plaintiffs go on to argue that there is no basis for CEC to have created promissory notes between Series G and itself at all; no basis to provide for them to be repaid in three years, given the order in which cash is supposed to flow from the plants; and no basis for the interest rate to be 10 points over prime. Pls.' SOF [Doc. 136] at ¶ 62. Defendants explain this situation as follows:

> Some of [the] 20 limited partnerships have fully expended their reserves to pay the management fees and their share of the partnership expenses. To ensure that these partnerships continue to fully operate, Dr. Gary Schwendiman and I have lent more than $3.3 million to them to date. We have loaned over $800,000 to the Series G. Those loans are authorized by Section 7.4 of the Agreement of Limited Partnership for ECP (LPA). They were made after exhaustive and extensive attempts to obtain third party loans from unaffiliated banks on a reasonable basis. Given the state of the economy, and particularly the credit markets, the loans originating from me and Dr. Schwendiman to ECP were on better terms to ECP and the other partnership than could be obtained from third parties.

Defs.' Exh. "W" [Doc. 145] at ¶ 10. Furthermore,

> Article 8.1(v) of the LPA provides that Partnership Expenses include "interest on and fees and expenses arising out of all borrowings made by the Partnership, including, but not limited to, the arranging thereof." The interest rate is prime (index) plus 10% (margin), and floats with changes in prime. The interest rate was established based on a market-based analysis of interest rates

> applicable to debt of similar size, quality and risk characteristics. . . . ECP ran out of cash because its Partnership Expenses, all inclusive, exceeded the cash it had available to pay those expenses.
>
> ECM sought but was unable to obtain third-party financing to fund Partnership Expenses for Series G. The financing requests were denied essentially because the collateral for the loan – the investments in the ethanol companies – were privately issued and illiquid, and, therefore, were no other assets to lend against by third parties. Accordingly, ECM offered ECP a revolving credit agreement based on usual and customary commercial terms. Typically, a general partner would not provide credit, but would instead liquidate all or a portion of the partnership's holdings to satisfy the cash requirement. Had ECM not provided credit, ECP would have had to liquidate a portion or all of its investments at a significant loss to its cost basis in those investments. By providing an arms-length credit agreement to ECP, ECM preserved greater value for the limited partners than they would have realized if the investments were liquidated.

Defs.' Exh. "X" [Doc. 145] at ¶ 10-11.

Plaintiffs' aver that "Series G disputes every direct expenses [sic] except the monitor fees paid to Plaintiffs in 2006 and 2007 ($47,284.72) and the management fees paid and accrued to CEC ($482,944.44), thus contesting a total of $414,649.06 in direct expenses." Pls.' SOF [Doc. 136] at ¶ 63. Additionally, "Series G disputes virtually all of the allocated expenses totaling $449,481.93." *Id.* at ¶ 64. Defendants correctly point out that Plaintiffs do not speak for Series G, as they are not General Partners and have not been designated as class representatives. As such, they can only speak for themselves.

"Plaintiffs also claim damages of $40,000 resulting from them having to pay attorney Art Leonard the fees that CEC had promised it would pay for improving the CEC documentation by adding language that would improve the tax situation for the investors." As discussed previously, there is not any evidence before this Court that such an agreement was made. "Plaintiffs also claim damages in the amount of $210,000 for the unpaid program monitor fees that CEC has refused to pay to Plaintiffs since third-quarter 2006." Pls.' SOF [Doc. 136] at ¶ 66. Plaintiffs aver that at the filing of the present Motions, the damages total $1,114,130.99.

Plaintiffs note that "[a]fter CEC exhausted the Series G cash held back from investment the direct and allocated expenses charged to Series G could no longer be withdrawn from Series G in cash infused by Series G investors, because, of the

approximately $6,000,000 invested by Series G limited partners, $5,400,000 had been directed by ECM to Series G's twin investments, one in an ethanol production facility operated/owned by E Energy Adams, in Nebraska and the second ethanol production facility called the FUEL investment located in Georgia. Once the approximately $600,000 in holdbacks had been exhausted by ECM, there was no additional cash to be taken." Pls.' SOF at ¶ 68. Additionally, "[w]ith respect to the Georgia facility (FUEL), it is noteworthy that CEC created a completely separate LLC to own the FUEL investment and, as a matter of plain fact, there is no document showing that Series G even owns a portion of the FUEL investment." Pls.' SOF at ¶ 69. Defendants correctly object, because Plaintiffs failed to attach any documentation to support this assertion.

Plaintiffs charge that "[b]ecause the expenses could no longer be withdrawn in cash, beginning in July 2008, CEC began accruing the direct and allocated expenses allegedly owed to it by Series G. CEC unilaterally decided to charge Series G an interest rate of prime plus 10%. This aside, for 2008, CEC charged Series G 15 % annual interest on each accruing amount claimed to be owed to CEC by Series G. In 2009, the rate was generously slashed to 13.25% but only because, apparently, Prime was 3.25%." Pls.' SOF at ¶ 70. On September 25, 2008 ECP gave CEC a $275,000 three-year promissory note. On March 10, 2009, a second $275,000 three-year promissory note was given.

Regarding damages, Plaintiffs recognize that "approximately $600,000 was available to CEC from [ECP] cash withheld by CEC from investment in the plants. Of this amount, the Plaintiffs cannot contest $530,229.16, meaning that, in actual cash, [ECP] lost approximately $70,000. The balance of [ECP's] losses are accruing in notes payable from [ECP] to CEC written and signed for (on both sides, as obligor and oblige[sic]) by CEC." Pls.' SOF at ¶ 72. Defendants object to this and subsequent paragraphs as without foundation and argumentative. Beyond what Plaintiffs claim as their damages, the Court agrees with Defendants' objection.

Finally, Plaintiff include a copy of their expert report, which relies on data up to October 2009. Defendants object, and properly assert that this document relies on the false premise that the PPM governs, which it does not.

On November 29, 2010, the Court heard oral argument on the motions.

II. STANDARD OF REVIEW

Summary judgment is appropriate when, viewing the facts in the light most favorable to the nonmoving party, *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 255 (1986), "there is no genuine issue as to any material fact and [] the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c). A fact is "material" if it "might affect the outcome of the suit under the governing law," and a dispute is "genuine" if "the evidence is such that a reasonable jury could return a verdict for the nonmoving party." *Anderson*, 477 U.S. at 248. Thus, factual disputes that have no bearing on the outcome of a suit are irrelevant to the consideration of a motion for summary judgment. *Id.*

In order to withstand a motion for summary judgment, the nonmoving party must demonstrate "specific facts showing that there is a genuine issue for trial," *Celotex Corp. v. Catrett*, 477 U.S. 317, 324 (1986). Moreover, a "mere scintilla of evidence" does not preclude the entry of summary judgment. *Anderson*, 477 U.S. at 252. The United States Supreme Court also recognized that "[w]hen opposing parties tell two different stories, one of which is blatantly contradicted by the record, so that no reasonable jury could believe it, a court should not adopt that version of the facts for purposes of ruling on a motion for summary judgment." *Scott v. Harris*, 550 U.S. 372, 380, 127 S.Ct. 1769, 1776, 167 L.Ed.2d 686 (2007).

A motion to dismiss pursuant to Rule 12(b)(7), Fed. R. Civ. P., may be granted when a plaintiff fails to join an indispensable party.[6] *See United States v. Bowen*, 172 F.3d 682,

---

[6]A Rule 12(b) motion must be brought prior to the responsive pleading. Fed. R. Civ. P. 12(b). Here, Defendants have already filed their Answer [Doc. 129] to Plaintiffs' Amended Complaint [Doc. 126]. As such, the Court will treat Defendants' Cross-Motion to Dismiss Counts

688 (9th Cir. 1999). "In determining whether a party is 'necessary' under Rule 19(a), a court must consider whether 'complete relief' can be accorded among the existing parties, and whether the absent party has a 'legally protected interest' in the subject of the suit." *Shermoen v. U.S.*, 982 F.2d 1312, 1317 (9th Cir.1992) (citations omitted). This is a fact specific inquiry, in which the moving party bears the burden of persuasion. *Makah Indian Tribe v. Verity*, 910 F.2d 555, 558 (9th Cir.1990).

II. ANALYSIS

A. Direct and Allocated Expenses

This Court has previously considered the express choice of law agreement contained in the LPA and found Delaware law applies in this cause of action. *See* Order 7/21/09 [Doc. 110]. The Delaware Revised Uniform Limited Partnership Act ("DRULPA") embodies the policy of giving "maximum effect to the principle of policy of freedom of contract and to the enforceability of the partnership agreements." 6 Del.C. § 17-1101(c). "DRULPA's 'basic approach is to permit partners to have the broadest possible discretion in drafting their partnership agreements and to furnish answers only in situations where the partners have not expressly made provisions in their partnership agreement' or 'where the agreement is inconsistent with mandatory statutory provisions.'" *Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, 817 A.2d 160, 170 (Del. 2002) (citations omitted). Furthermore, "the partnership agreement is the cornerstone of a Delaware limited partnership, and effectively constitutes the entire agreement among the partners with respect to the admission of partners to, and the creation, operation, and termination of, the limited partnership. Once partners exercise their contractual freedom in their partnership agreement, the partners have a great deal of certainty that their partnership agreement will be enforced in accordance with its

---

I-III and V-VIII of the Amended Complaint [Doc. 147] as one brought pursuant to Rule 12(h)(2). Fed. R. Civ. P. 12(h)(2); *Elvig v. Calvin Presb. Church*, 375 F.3d 951, 954 (9th Cir. 2004).

terms." *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 291 (Del. 1999) (citations omitted).

As an initial matter, Plaintiffs argue that only the PPM was signed, and the LPA was unsigned, when this investment opportunity began. *See* Pls.' Resp. to Defs.' Controverting SSOF at 9. Therefore, the PPM should control. The DRULPA states that a:

> "Partnership agreement" means any agreement, written, oral or implied, of the partners as to the affairs of a limited partnership and the conduct of its business. A partner of a limited partnership or an assignee of a partnership interest is bound by the partnership agreement whether or not the partner or assignee executes the partnership agreement. A limited partnership is not required to execute its partnership agreement. A limited partnership is bound by its partnership agreement whether or not the limited partnership executes the partnership agreement.

6 Del.C. § 17-101(12). Based upon the plain language of the LPA, it is the controlling document.

Plaintiffs argue that "CEC may not allocate either the costs of running CEC or certain direct expenses to Series G because they are not within the scope of the expenses for which Plaintiffs are responsible under the PPM." Pls.' Mot. Partial Summ. J. on Issue of Allocated and Direct Expenses [Doc. 142] at 6. Relying solely on the PPM, Plaintiffs assert that "[b]ecause neither the CEC Overhead Costs nor CEC Attorneys' Fees meet the definition of the types of expenses from which Plaintiffs are responsible, these expenses cannot be allocated to Plaintiffs[.]" *Id.* Plaintiffs assert that "various employee-related expenses that CEC has allocated to Plaintiffs, [as identified by Plaintiffs' expert witness,] such as payroll, payroll taxes, health insurance, pension benefits, and employee cell phones, constitute 'compensation of [CEC's] employees . . .'." *Id.* at 7.

Defendants argue that Plaintiffs incorrectly rely solely on the PPM in their argument. Rather, Defendants contend that the LPA controls. Defendants assert that Plaintiffs have failed to specifically identify which "expenses that they contend are not permitted pursuant to the LPA." Defs.' Combined Opp. to Pls.' Mot. for Partial Summ. J. on Claims re: Expenses and For Expulsion of Gen. Partner [Doc. 147] at 11. Moreover, the Business Judgment Rule "generally protects the actions of general partners, [and] affords them a

presumption that they acted on an informed basis and in the honest belief that they acted in the best interests of the partnership and the limited partners." *Id.* at 10 (quoting *Zoren v. Genesis Energy, L.P.*, 836 A.2d 521, 528 (Del. Ch. 2003)).

Delaware law provides that:

> Unless otherwise provided in a partnership agreement, a partner or other person shall not be liable to a limited partnership or to another partner or to another person that is a party to or is otherwise bound by a partnership agreement for breach of fiduciary duty for the partner's or other person's good faith reliance on the provisions of the partnership agreement.

6 Del.C. § 17-1101(e). This section is a safe harbor provision "for general partners who act in good faith reliance on the partnership agreement." *United States Cellular Invest. Co. of Allentown v. Bell Atl. Mobile Sys., Inc.*, 677 A.2d 497, 501 (Del. 1996). Similarly, Section 3.2(e) of the LPA provides:

> (e) Reliance on This Agreement. To the extent that, at law or in equity, the General Partner has duties (including fiduciary duties) and liabilities relating thereto to the Partnership or another Partner, the General Partner acting under this Agreement shall not be liable to the Partnership or to any such other Partner for its reasonable good faith reliance on the provisions of this Agreement. The provisions of this Agreement, to the extent that they expand or restrict the duties and liabilities of the General Partner otherwise existing at law or in equity, are agreed by the Partners to modify to that extent such other duties and liabilities of the General Partner.

LPA at 19.

"Undoubtedly, a corporate general partner and the directors of that general partner owe a fiduciary duty of loyalty to a limited partnership and its limited partners." *Zoren v. Genesis Energy, L.P.* 836 A.2d 521, 528 (Del. Ch. 2003) (citations omitted). General partners, however, are entitled to "a presumption that their actions are protected from judicial oversight by the business judgment rule." *Id.* "The business judgment rule generally protects the actions of general partners, affording them a presumption that they acted on an informed basis and in the honest belief that they acted in the best interests of the partnership and the limited partners." *Id.* "[A] plaintiff's mere allegation of 'unfair dealing', without more, cannot survive a motion to dismiss, averments containing 'specific acts of fraud, misrepresentation, or other items of misconduct' must be carefully examined[.]" *Rabkin v. Philip A. Hunt Chem. Corp.*, 498 A.2d 1099, 1105 (Del. 1985). In order to overcome the

presumption established by the business judgment rule, Plaintiffs have the burden of pleading sufficient facts to show that the general partners "appeared on both sides of the transaction or derived a personal benefit from a transaction in the sense of self-dealing." *Zoren*, 836 A.2d at 528. Delaware courts have recognized bad faith as encompassing not only traditional notions of bad faith in which the fiduciary is motivated by an actual intent to do harm, but also where the fiduciary's actions are the result of gross negligence, without malevolent intent, and actions which are a conscious disregard of the fiduciary's duties. *Lyondell Chem. Co. v. Ryan*, 970 A.2d 235, 240 (Del. 2009) (quoting *In re Walt Disney Co. Deriv. Litig.*, 906 A.2d 27 (Del. 2006)). "In the transactional context, [an] extreme set of facts [is] required to sustain a disloyalty claim premised on the notion that disinterested directors were intentionally disregarding their duties." *Id.* at 243 (alterations in original).

Additionally, DRULPA provides that "[e]xcept as provided in this chapter or in the partnership agreement, a general partner of a limited partnership has the rights and powers and is subject to the restrictions of a partner in a partnership that is governed by the Delaware Uniform Partnership Law." 6 Del.C. § 17-403(a). Delaware law recognizes that unless the parties agree otherwise, "[t]he only fiduciary duties a partner owes to the partnership and the other partners are the duty of loyalty and the duty of care set forth in subsections (b) and (c)." 6 Del.C. § 15-404. Section 15-404 further states in relevant part that:

> (b) A partner's duty of loyalty to the partnership and the other partners is limited to the following:
>
> (1) to account to the partnership and hold as trustee for it any property, profit or benefit derived by the partner in the conduct or winding up of the partnership business or affairs or derived from a use by the partner of partnership property, including the appropriation of a partnership opportunity;
>
> (2) to refrain from dealing with the partnership in the conduct or winding up of the partnership business or affairs as or on behalf of a party having an interest adverse to the partnership; and
>
> (3) to refrain from competing with the partnership in the conduct of the partnership business or affairs before the dissolution of the partnership.
>
> (c) A partner's duty of care to the partnership and the other partners in the conduct and winding up of the partnership business or affairs is limited to refraining from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law.

> (d) A partner does not violate a duty or obligation under this chapter or under the partnership agreement solely because the partner's conduct furthers the partner's own interest.
>
> (e) A partner may lend money to, borrow money from, act as a surety, guarantor or endorser for, guarantee or assume 1 or more specific obligations of, provide collateral for and transact other business with, the partnership and, subject to other applicable law, has the same rights and obligations with respect thereto as a person who is not a partner.

6 Del.C. § 15-404. Additionally, Section 7.4 of the LPA specifically provides that:

> The General Partner shall have the right, at its option, to cause the Partnership to borrow money from *any* Person, or to guarantee loans or other extensions of credit for the purpose of:
>
> (i) providing interim financing to cover Partnership Expenses; or
>
> (ii) providing interim financing to the extent necessary to consummate the purchase of Portfolio Investments[.]

LPA at 33 (emphasis added).

Plaintiffs have not met their burden to demonstrate that the General Partners appeared on both sides of the transaction in the sense of self-dealing. The Amended Complaint [Doc. 126] broadly alleges a failure to deal with the Program Monitors in good faith, and in the charging of allocated expenses to ECP. Defendants, however, have turned over a tremendous amount of financial information and despite Plaintiffs' averment to the contrary, nothing stands out as an extreme set of facts sufficient to sustain a disloyalty claim. The LPA specifically provides for the types of expenses about which Plaintiff complain. Furthermore, Plaintiffs do not address how the allocated expenses are not reasonably partnership operational expenses. At oral argument, counsel recognized that Series G does not maintain offices separate from CEC, nor does it have office equipment or staff solely dedicated to it. Plaintiffs' argument suggests that it is impossible for any CEC employee working on Series G business to have any portion of their salary or expenses related to their employment charged to Series G; however, this logic does not follow. Because Series G does not have its own office equipment or other employees, operations cannot be conducted without the use of individuals or items affiliated with CEC. CEC is then entitled to "charge" Series G for these expenses.

Plaintiffs also strenuously object to the payment of legal fees, and in particular those fees associated with the E Energy Adams litigation. Section 8.1 of the LPA, however, unequivocally allows for the payment of litigation expenses arising out of the Partnership, including those relating to director and officer liability. LPA at § 8.1(iii) & (vi). It is undisputed that Series G funds were invested in E Energy Adams. It is also undisputed that Series G was entitled to have an individual on the board of directors for E Energy Adams. Plaintiff argues that this litigation is strictly about Defendant Brittenham's ego; however, even if the litigation was borne out of Defendant Brittenham's feelings, it remains undisputed that once Defendant Brittenham was removed from the E Energy Adams's board, Series G was left without a representative. Defendant Brittenham, as the general partner for Series G, instigated litigation and the seat was ultimately filled by Neil Hwang. These facts are undisputed. Based upon the record before this Court, the presumption established by the Business Judgment Rule has not been overcome.

Finally, Plaintiffs allege self-dealing regarding the promissory notes signed by CEC on behalf of itself and Series G. Section 15-404(e), 6 Del. C., of the Delaware Revised Uniform Partnership Act ("DRUPA") provides that general partners can lend the partnership money. This is also consistent with the express language of the LPA. Defendants aver that they were unable to secure financing from outside sources at a better rate for the partnership. Without more, the act of loaning money to Series G does not indicate self-dealing.

Delaware law gives parties broad rights regarding their ability to contract. Furthermore, the agreements before this Court give the general partners wide latitude in the management of the partnership. As such, Plaintiffs' Motion for Partial Summary Judgment regarding Direct and Allocated Expenses must fail. Conversely, Plaintiffs' failure to meet their burden in rebutting the Business Judgment Rule means that summary judgment in favor of Defendants is proper.

. . .

. . .

. . .

B. Securities Fraud (Federal and Arizona)

Plaintiffs further allege that Defendants have committed securities fraud under both federal and Arizona statutes. With regard to securities violations, Plaintiffs' Amended Complaint states "Defendants' actions and omissions constitute breach of contract, breach of fiduciary duty, gross negligence, bad faith, intentional and willful misconduct, and knowing violations of securities and other law." Pls.' Amended Compl. [Doc. 126] at ¶ 52. A complaint does not "suffice if it tenders 'naked assertion[s]' devoid of 'further factual enhancement.'" *Ashcroft v. Iqbal*, – U.S. –, 129 S.Ct. 1937, 1949, 173 L.Ed.2d 868 (2009) (alterations in original). Based upon the foregoing discussion and the record before this Court, Plaintiffs cannot state a claim for securities fraud.

C. Removal/Expulsion of CEC as General Partner of ECP

Plaintiffs seek to have the CEC removed as general partner of ECP. Plaintiffs rely on Section 15-601 of the DRUPA as authority for this proposition. The DRULPA is the controlling statute for Delaware limited partnerships; the DRUPA applies to limited partnerships only insofar as the subject matter is not covered by the DRULPA. 6 Del.C. § 17-1105. Additionally, the DRUPA applies when the DRULPA expressly incorporates provisions thereof. *See e.g.,* 6 Del.C. § 17-403. As Defendants point out, the DRUPA § 15-601 does not fit either of these categories.

In response, Plaintiffs assert that "while Defendants would like to persuade this Court that DRUPA and DRULPA are different in spirit and cannot possibly co-exist, they fail to point out that essentially, the statutes say the same thing." Pls.' Consolidated Reply to Mot. for Summ. J. and Resp. to Defs.' Cross-Mot. for Summ. J. [Doc. 152] at 14. The DRULPA, however, contains its own provisions for removal of the General Partner, and the DRUPA, therefore, cannot apply. Section 17-402, the DRULPA, provides:

> (a) A person ceases to be a general partner of a limited partnership upon the happening of any of the following events:
>
> (1) The general partner withdraws from the limited partnership as provided in § 17-602 of this title;

(2) The general partner ceases to be a general partner of the limited partnership as provided in § 17-702 of this title;

(3) The general partner is removed as a general partner in accordance with the partnership agreement;

(4) Unless otherwise provided in the partnership agreement, or with the written consent of all partners, the general partner:

a. Makes an assignment for the benefit of creditors;

b. Files a voluntary petition in bankruptcy;

c. Is adjudged a bankrupt or insolvent, or has entered against him or her an order for relief in any bankruptcy or insolvency proceeding;

d. Files a petition or answer seeking for himself or herself any reorganization, arrangement, composition, readjustment, liquidation, dissolution or similar relief under any statute, law or regulation;

e. Files an answer or other pleading admitting or failing to contest the material allegations of a petition filed against him or her in any proceeding of this nature; or

f. Seeks, consents to or acquiesces in the appointment of a trustee, receiver or liquidator of the general partner or of all or any substantial part of his properties;

(5) Unless otherwise provided in the partnership agreement, or with the written consent of all partners, 120 days after the commencement of any proceeding against the general partner seeking reorganization, arrangement, composition, readjustment, liquidation, dissolution or similar relief under any statute, law or regulation, the proceeding has not been dismissed, or if within 90 days after the appointment without the general partner's consent or acquiescence of a trustee, receiver or liquidator of the general partner or of all or any substantial part of his or her properties, the appointment is not vacated or stayed, or within 90 days after the expiration of any such stay, the appointment is not vacated;

(6) In the case of a general partner who is a natural person:

a. The general partner's death; or

b. The entry by a court of competent jurisdiction adjudicating the general partner incompetent to manage his or her person or property;

(7) In the case of a general partner who is acting as a general partner by virtue of being a trustee of a trust, the termination of the trust (but not merely the substitution of a new trustee);

(8) In the case of a general partner that is a separate partnership, the dissolution and commencement of winding up of the separate partnership;

(9) In the case of a general partner that is a corporation, the filing of a certificate of dissolution, or its equivalent, for the corporation or the revocation

> of its charter and the expiration of 90 days after the date of notice to the corporation of revocation without a reinstatement of its charter;
>
> (10) Unless otherwise provided in the partnership agreement, or with the written consent of all partners, in the case of a general partner that is an estate, the distribution by the fiduciary of the estate's entire interest in the limited partnership;
>
> (11) In the case of a general partner that is a limited liability company, the dissolution and commencement of winding up of the limited liability company; or
>
> (12) In the case of a general partner who is not an individual, partnership, limited liability company, corporation, trust or estate, the termination of the general partner.
>
> (b) A general partner who suffers an event that with the passage of the specified period becomes an event of withdrawal under subsection (a)(4) or (5) of this section shall notify each other general partner, or in the event that there is no other general partner, each limited partner, of the occurrence of the event within 30 days after the date of occurrence of the event of withdrawal.

6 Del.C. § 17-402. Section 13.1 of the LPA states:

> (b) Removal Event. In the event of (i)(x) the General Partner's conviction of a felony, including, without limitation, any felony involving a violation of the federal securities law or (y) any act or omission to act by the General Partner that involves fraud, gross negligence, willful misconduct or a knowing violation of law with respect to the Partnership, as determined by a court of competent jurisdiction, not a government regulatory authority (the events described in clauses (x) and (y) being "Triggering Events") and (iii) the vote by Limited Partners with at least sixty-six and two-thirds percent (66 2/3 %) of the aggregate Voting Interests of all Limited Partners to remove the General Partner, the General Partner shall be removed. The General Partner shall not be removed until it is provided with written notice signed by the Limited Partners that have affirmatively voted for its removal, such notice specifying the circumstances constituting the grounds for such proposed removal, including, without limitation, the circumstances constituting the alleged Triggering Event.

LPA at 51-2.

Currently, there is nothing before the Court that indicates that (1) any of the Triggering Events has occurred or (2) that Plaintiffs have complied with the notice requirements. Plaintiffs base the removal on the allegation that the General Partner has charged unauthorized direct and allocated expenses; however, as discussed previously, this argument fails. Plaintiffs further allege that the General Partner has prevented them from "monitoring and reporting." Even if this Court accepts Plaintiffs contention that the General Partner willfully interfered with their Program Monitor duties, since the inception of this

lawsuit, Plaintiffs have received, and continue to receive, all necessary accounting documentation for the fulfillment of their Program Monitoring duties. A limited partner is one "who receives profits from the business but does not take part in managing the business[.]" Black's Law Dictionary (9th ed. 2009). Plaintiffs duties as Program Monitors are defined in the PPM, which provides that they shall "observe the Partnership and the General Partner to monitor that the activities of the Partnership are generally proceeding as described in the Memorandum and the Partnership Agreement, as the same may be amended from time to time." The collection of records provided to Plaintiffs to date has allowed them to "observe" and "monitor." Nothing more is required. As such, there is nothing before this Court to warrant expulsion of the General Partner. Plaintiffs have failed to present any admissible evidence that CEC has acted either fraudulently or with gross negligence. This Court is not required to accept conclusory statements as a factual basis. *See Soremekun v. Thrifty Payless, Inc.*, 509 F.3d 978, 984 (9th Cir. 2007) ("Conclusory, speculative testimony in affidavits and moving papers is insufficient to raise genuine issues of fact and defeat summary judgment."). Accordingly, Plaintiffs have failed to meet their burden, and summary judgment will be denied.

D. Failure to Join Indispensable Parties Pursuant to Rule 19, Federal Rules of Civil Procedure.

Defendants cross-move for summary judgment on Plaintiffs' derivative claims. Plaintiffs' Amended Complaint [Doc. 126] sets forth claims for: (1) derivative action for accounting; (2) derivative action for breach of fiduciary duty; (3) derivative action for breach of contract; (4) breach of contract; (5) derivative action for unjust enrichment/promissory estoppel; (6) derivative action for aiding and abetting breach of fiduciary duty; (7) derivative action for negligent misrepresentation; and (8) derivative action for declaratory judgment. The previous discussion regarding expulsion of the general partner partially encompasses Plaintiffs' declaratory judgment claim. Defendants seek dismissal of counts 1-3 and 5-8. As

an initial matter, Defendants argue that Rule 19, Federal Rules of Civil Procedure, requires joinder of the partnership.

Rule 19(a), Federal Rules of Civil Procedure, provides:

> (1) ***Required Party.*** A person who is subject to service of process and whose joinder will not deprive the court of subject-matter jurisdiction must be joined as a party if:
>
> (A) in that person's absence, the court cannot accord complete relief among existing parties; or
>
> (B) that person claims an interest relating to the subject of the action and is so situated that disposing of the action in the person's absence may:
>
> (i) as a practical matter impair or impede the person's ability to protect the interest; or
>
> (ii) leave an existing party subject to a substantial risk of incurring double, multiple or otherwise inconsistent obligations because of the interest.

Fed. R. Civ. P. 19(a). It is well established law that in a derivative suit "[t]he claim pressed by the stockholders against directors or third parties is not his own but the corporation's. The corporation is a necessary party to the action; without it the case cannot proceed." *Ross v. Bernhard*, 396 U.S. 531, 538, 90 S.Ct. 733, 738, 24 L.Ed.2d 729 (1970) (internal citations and quotations omitted). The court in *Urquhart v. Wertheimer*, 646 F.Supp.2d 210 (D.Mass. 2009) discussed the difference between derivative and direct action lawsuits in the limited partnership context. The *Urquhart* court stated:

> A suit is "derivative" if the source of the plaintiff's claim of right "flows from the breach of a duty owed by the defendants to the corporation: and the harm to the plaintiff thus "flows through the corporation." Examples of derivative claims include "mismanagement of funds" and "embezzlement or breach of fiduciary duty resulting in a diminution of the value of the corporate stock or assets." A suit is "direct" if "the right flows from the breach of a duty owed directly to the plaintiff independent of the plaintiff's status as a shareholder, investor, or creditor of the corporation." An example of a direct claim is one in which the plaintiff alleges that he was "misled or defrauded in the purchase" of an investment.

Urquhart, 646 F.Supp.2d at 212. Upon determination that the claims asserted by Plaintiff were derivative, the *Urquhart* court concluded that the partnership was both a "necessary"

and "indispensable" party to the cause of action. *Id.* at 213. The following discussion by the *Urquhart* court is instructive:

> Defendants have satisfied the requirements of Rule 19(a) and (b). Rule 19(a) is satisfied not only because Plaintiff's claims are derivative, but because any recovery against CHI would flow first to the Partnership and then to all its limited partners, placing a constructive trust over monies received by the Partnership would affect the Partnership's ability to manage its affairs, and removal of CHI as general partner implicates and potentially prejudices the entire Partnership.
>
> For similar reasons, the four factors of Rule 19(b) favors Defendants. Imposition of a constructive trust and removal of CHI as general partner have the potential to prejudice the Partnership. Such prejudice could not be lessened by protective provisions, shaping the relief, or other measures because it ensues from the very relief that Plaintiff seeks in this action. An adequate judgment could not be rendered in the Partnership's absence because the Partnership and other limited partners could challenge a constructive trust and removal of CHI as general partner in separate lawsuits, and any damages would flow through the Partnership in general to all the limited partners individually. Finally, Plaintiff would have an adequate remedy if this case were dismissed because Plaintiff could refile this action in state court naming the Partnership and all the limited partners, or file an action in either federal or state court against the same Defendants by asserting only direct claims.

Id. Plaintiffs do not directly contradict this authority. They do, however, point to a Ninth Circuit case in which the partnership was found not to be indispensable under Rule 19(b). *Schnabel v. Liu*, 302 F.3d 1023 (9th Cir. 2002). *Schnabel* was predicated on California law allowing suit against individual partners. *Id.* at 1031. Furthermore, all individual partners were party to the lawsuit and the partnership was found not to have its own assets. *Id.*

Here, Plaintiffs are seeking removal of the general partner as well as claims for breach of fiduciary duty, breach of contract, unjust enrichment/promissory estoppel, and aiding and abetting a breach of fiduciary duty. All of these, as discussed in *Urquhart* would result in damages flowing through the Partnership in general to all the limited partners individually. Additionally, the Negligent Misrepresentation claim is a direct action, not a derivative one. *See Urquhart*, 646 F.Supp.2d at 212 ("An example of a direct claim is one in which the plaintiff alleges that he was 'misled or defrauded in the purchase' of an investment."). The absence of the partnership in this cause of action hinders this Court's ability to render an adequate judgment. Moreover, this "prejudice could not be lessened by protective provisions, shaping the relief, or other measures because it ensues from the very relief that

Plaintiff seeks in this action." *Id.* at 213. As such, the Court finds that Plaintiffs have failed to join an indispensable party pursuant to Rule 19.

E. Failure to Meet Rule 23.1, Federal Rules of Civil Procedure, Requirements

Defendants argue that Plaintiffs cannot meet the requirements of Rule 23.1 because of Plaintiffs' conduct of personal vindictiveness against the General Partner. In light of the foregoing analysis, the Court declines to reach this issue.

F. Individual Wrongdoing on the Part of Defendant Schwendiman.

It is undisputed that Defendant Schwendiman retired as a manager of the General Partner on June 1, 2007. While Defendants are correct that the Amended Complaint [Doc. 126] was filed two and a half years after Defendant Schwendiman retired, the breach of contract claims that it contains is based upon actions that occurred prior to Defendant Schwendiman's retirement. Plaintiffs breach of contract claim remains, and as such the Court declines to dismiss Defendant Schwendiman at this time.

Accordingly, IT IS HEREBY ORDERED that:

1. Plaintiffs' Motion for Partial Summary Judgment re Count VIII – For Removal/Expulsion of CEC as General Partner of Series G; Pursuant to Del. Code Ann. Tit. 6 § 15-601(5) [Doc. 135] is DENIED;

2. Plaintiffs' Motion for Partial Summary Judgment on Issue of Allocated and Direct Expenses [Doc. 142] is DENIED;

3. Defendants' Cross-Motion to Dismiss Counts I-III and V-VIII of the Amended Complaint [Doc. 147] is GRANTED in part and DENIED in part. Defendant Gary Schwendiman remains a party and Plaintiffs' direct action claims for breach of contract and negligent misrepresentation remain pending in this action; and

. . .

. . .

4. Defendants' Cross-Motion for Leave to File a Motion to Compel [Doc. 147] is DENIED with leave to refile after consideration of this Order.

DATED this 29th day of March, 2011.

Cindy K. Jorgenson
United States District Judge

EXHIBIT B

STATE OF WASHINGTON
DEPARTMENT OF FINANCIAL INSTITUTIONS
CONSUMER SERVICES DIVISION

IN THE MATTER OF DETERMINING Whether there has been a violation of the Mortgage Broker Practices Act of Washington by: FIDELITY MORTGAGE CORPORATION, and NICHOLAS HAINES, Vice President and Designated Broker, and SCOTT BRITTENHAM, President, Respondents.	NO. C-03-172-05-CO01 CONSENT ORDER **FIDELITY MORTGAGE CORPORATION**

COMES NOW the Director of the Department of Financial Institutions (Director), through his designee Chuck Cross, Division Director, Division of Consumer Services, and Fidelity Mortgage Corporation (Respondent Fidelity) by and through its attorney Greg Cavagnaro, and finding that the issues raised in the captioned matter may be economically and efficiently settled, agree to the entry of this Consent Order. This Consent Order is entered pursuant to chapter 19.146 of Revised Code of Washington (RCW), and RCW 34.05.060 of the Administrative Procedure Act, based on the following:

AGREEMENT AND ORDER

The Department of Financial Institutions, Division of Consumer Services (Department) and Respondent Fidelity have agreed upon a basis for resolution of the matters alleged in Statement of Charges No. C-03-172-04-SC01 (Statement of Charges), entered November 12, 2004, (copy attached hereto). Pursuant to chapter 19.146 RCW, the Mortgage Broker Practices Act (Act) and RCW 34.05.060 of the Administrative Procedure Act, Respondent Fidelity hereby agrees to the Department's entry of this Consent Order and further agrees that the issues raised in the above captioned matter may be economically and efficiently settled by entry of this Consent Order. The parties intend this Consent Order to fully resolve the Statement of Charges as it pertains to Respondent Fidelity.

Based upon the foregoing:

DEPARTMENT OF FINANCIAL INSTITUTIONS
150 Israel Rd SW
PO Box 41200
Olympia, WA 98504-1200
(360) 902-8703

A. **Jurisdiction.** It is AGREED that the Department has jurisdiction over the subject matter of the activities discussed herein.

B. **Waiver of Hearing.** It is AGREED that Respondent Fidelity has been informed of the right to a hearing before an administrative law judge, and that Respondent Fidelity has waived the right to a hearing and any and all administrative and judicial review of the issues raised in this matter, or of the resolution reached herein. Accordingly, Respondent Fidelity agrees to withdraw the appeal and to inform the Office of Administrative Hearings in writing of the withdrawal.

C. **Mortgage Broker License Revocation.** It is AGREED that Respondent Fidelity's license to conduct the business of a mortgage broker is revoked.

D. **Non-Compliance with Order.** It is AGREED that Respondent Fidelity understands that failure to abide by the terms and conditions of this Consent Order may result in further legal action by the Director. In the event of such legal action, Respondent Fidelity may be responsible to reimburse the Director for the cost incurred in pursuing such action, including but not limited to, attorney fees.

E. **Authority to Execute Order.** It is AGREED that the undersigned have represented and warranted that they have the full power and right to execute this Consent Order on behalf of the party represented.

F. **Voluntarily Entered.** It is AGREED that the undersigned have voluntarily entered into this Consent Order, which is effective when signed by the Director's designee.

G. **Completely Read, Understood, and Agreed.** It is AGREED that the undersigned have read this Consent Order in its entirety and fully understand and agree to all of the same.

\\\

\\\

\\\

\\\

\\\

RESPONDENT:

Fidelity Mortgage Corporation
By:

SCOTT BRITTENHAM
President

11-4-05
Date

NICHOLAS HAINES
Vice President and Designated Broker

Date

Greg Cavagnaro, WSBA No. 17644
Attorney at Law
Attorney for Respondent Fidelity

Date

DO NOT WRITE BELOW THIS LINE

THIS ORDER ENTERED THIS 16th DAY OF NOVEMBER, 2005.

CHUCK CROSS
Director
Division of Consumer Services
Department of Financial Institutions

DEPARTMENT OF FINANCIAL INSTITUTIONS
150 Israel Rd SW
PO Box 41200
Olympia, WA 98504-1200
(360) 902-8703

RESPONDENT:

Fidelity Mortgage Corporation
By:

SCOTT BRITTENHAM
President

11-4-05
Date

NICHOLAS HAENES
Vice President and Designated Broker

Date

Greg Cavagnaro, WSBA No. 17644
Attorney at Law
Attorney for Respondent Fidelity

11/4/05
Date

DO NOT WRITE BELOW THIS LINE

THIS ORDER ENTERED THIS 16th DAY OF NOVEMBER, 2005.

DIRECTOR OF FINANCIAL INSTITUTIONS STATE OF WASHINGTON

CHUCK CROSS
Director
Division of Consumer Services
Department of Financial Institutions

DEPARTMENT OF FINANCIAL INSTITUTIONS
150 Israel Rd SW
PO Box 41200
Olympia, WA 98504-1200
(360) 902-8703

RESPONDENT:

Fidelity Mortgage Corporation
By:

SCOTT BRITTENHAM
President

Date

NICHOLAS HAINES
Vice President and Designated Broker

11/4/05
Date

Greg Cavagnaro, WSBA No. 17644
Attorney at Law
Attorney for Respondent Fidelity

Date

DO NOT WRITE BELOW THIS LINE

THIS ORDER ENTERED THIS 16th DAY OF NOVEMBER, 2005.

CHUCK CROSS
Director
Division of Consumer Services
Department of Financial Institutions

DEPARTMENT OF FINANCIAL INSTITUTIONS
150 Israel Rd SW
PO Box 41200
Olympia, WA 98504-1200
(360) 902-8703

RESPONDENT:

Fidelity Mortgage Corporation
By:

SCOTT BRITTENHAM
President

Date

NICHOLAS HAINES
Vice President and Designated Broker

11/4/05
Date

Greg Cavagnaro, WSBA No. 17644
Attorney at Law
Attorney for Respondent Fidelity

11-4-05
Date

DO NOT WRITE BELOW THIS LINE

THIS ORDER ENTERED THIS 16th DAY OF NOVEMBER, 2005.

CHUCK CROSS
Director
Division of Consumer Services
Department of Financial Institutions

DEPARTMENT OF FINANCIAL INSTITUTIONS
150 Israel Rd SW
PO Box 41200
Olympia, WA 98504-1200
(360) 902-8703