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UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of LYNN TILTON, PATRIARCH PARTNERS, LLC, PATRIARCH PARTNERS VIII, LLC, PATRIARCH PARTNERS XIV, LLC, and PATRIARCH PARTNERS XV, LLC, Respondents.	Administrative Proceeding File No. 3-16462 Hon. Judge Carol Fox Foelak

REPLY MEMORANDUM AND POINTS OF AUTHORITIES
IN SUPPORT OF RESPONDENTS' MOTION FOR SUMMARY DISPOSITION

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July 10, 2015

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INTRODUCTION

This case arises out of Patriarch's long-standing and well-disclosed practice of categorizing loans for which it has agreed to accept reduced interest as performing loans. The Division asserts that, in so doing, Patriarch failed "to abide by the terms of the deals." (Ex. 9 at 2.) But that is an allegation that sounds in contract and not in fraud. Since, of course, the Division cannot bring a breach of contract claim (which, it bears noting, no investor has ever seen fit to bring), it has attempted to wrongly shoehorn its case into one for non-disclosure.

The first problem for the Division is that what it alleges was concealed was in fact disclosed. The Division does not dispute that investors knew or could easily ascertain how Patriarch categorized loans paying reduced interest. To deal with this problem, the Division attempts to recast what was supposedly concealed. It contends that Patriarch concealed the fact that its approach to loan categorization involved "subjective" judgment rather than a supposed "objective" methodology that the Division posits. But the very fact that, as was disclosed, loans paying reduced interest were categorized as performing made plain that Patriarch was exercising discretion.

In its continuing effort to divine something — anything — that was concealed from investors, the Division also contends that investors somehow did not and could not know that the OC Ratio was affected by Patriarch's categorization approach. This new contention is false because the OC Ratio is defined in the indentures by reference to the loan categories. Because investors knew how Patriarch was categorizing loans, they also knew from the governing indentures that Patriarch's approach affected the OC Ratio.

The second problem for the Division is that there is no legal duty for contracting parties to disclose their interpretation of a contract. Conceding the point, the Division tries to side step the issue by claiming that Patriarch's interpretation is wrong as a matter of law. But whether

Patriarch's interpretation is right or wrong is irrelevant here, because the Division has not brought a breach of contract case. A nondisclosure case, by its very nature, cannot proceed on disputed contract terms that were available for all to see. Even if Patriarch's interpretation was relevant here, extensive contemporaneous evidence, cited in Patriarch's moving papers, shows that the relevant stakeholders understood the indenture the same way as Patriarch.

A final problem for the Division is that all of its claims under the Advisers Act §§ 206(1) and (2) are flawed as a matter of law. It is undisputed that Lynn Tilton is both the owner of the investment advisers, the Patriarch entities, and is the ultimate equity owner of the "clients," the Zohar CLOs. The case law is clear that Ms. Tilton could not have defrauded herself. The same result flows from agency law, which imputes to the CLOs any information known to Ms. Tilton. In the face of this dispositive case law, the Division claims that the Court should apply the "adverse interest" exception to these basic agency principles. That narrow exception, however, applies only in cases akin to "outright looting," where the defendant acts *only* in his or her interest. Here, the Division has already disavowed any challenge to Patriarch's good faith business judgment that the distressed portfolio companies could be turned around. In other words, Patriarch pursued a strategy intended to benefit all stakeholders. The "adverse interest" exception cannot apply in these circumstances, and thus the client-based claims must be dismissed.

This Court should grant Patriarch's motion.

DISCUSSION

I. THE INVESTIGATIVE RECORD CONTRADICTS THE DIVISION'S CATEGORIZATION THEORY

The Division does not dispute the central, dispositive fact requiring that Patriarch's motion be granted: Patriarch's practice of "categorizing as performing loans that do not pay the

full stated interest" was disclosed. (Pat. Br. 9-13.) The Division does not even attempt to argue or demonstrate that investors were unaware, or could not easily ascertain from Patriarch's regularly distributed reports, that Patriarch was accepting less than full interest on loans it categorized as performing.

Yet, oddly, that is exactly what the Division alleged in its OIP was improperly concealed from investors. In the Division's view, the indentures do "not permit an asset to be classified as a Category 4 [*i.e.*, performing] when contractual interest has not been paid." (Opp. 3.)

As discussed below, Patriarch disputes that contention, and with good reason. But if Patriarch's classifications were wrong under the indenture terms, they were wrong right out in the open, contained in detailed disclosure reports that the investors used to understand their investments. This is no small hole in the Division's case. The Division, realizing the obvious, has tried to recast things. What was not disclosed, it argues, was the fact that Patriarch was using a subjective rather than an objective approach to categorization. Or maybe, the Division argues, the nondisclosure is that the "true" OC Ratio was somehow hidden. Neither of these is remotely true, as can be easily ascertained from the monthly reports.

Because investors could readily see that loans that were not generating full stated interest were held as performing, it was evident that Patriarch was not using the so-called "objective" method of automatically defaulting loans in those circumstances. The inescapable conclusion was that the manager was using subjective discretion. And, indeed, the Division does not dispute that discretion was at the core of the indentures and the underlying investment strategy. After all, successful investment in deeply distressed assets requires using subjective discretion as to when to allow a borrower more time to pay and when to foreclose. (Tilton Aff. ¶ 5.)

For this reason, each of the Zohar indentures allow Patriarch to freely "enter into any amendment, forbearance or waiver of or supplement to any" loan. (Ex. 5 § 7.7(a) (PP050056); Ex. 6 § 7.7(a) (PP050399); Ex. 7 § 7.7(a) (PP001881).) The process of deciding whether or not to agree to accept reduced interest is necessarily subjective. This subjective judgment necessarily affects loan categorization because it determines whether the borrower has defaulted in the first place. When a party accepts partial payment for amounts due under a contract, as Patriarch indisputably did here, it modifies the terms of the agreement. *See Puma Indus. Consulting, Inc. v. Daal Assocs., Inc.*, No. 85 Civ. 3137, 1986 WL 10281, at *3 (S.D.N.Y. Sept. 9, 1986), *aff'd as modified*, 808 F.2d 982 (2d Cir. 1987).

The Division has no genuine answer to this critical point. The Division acknowledges that Section 7.7(a) of the indentures "does allow for loan modifications," (Opp. at 4), and that Patriarch would often use that authority granted to undertake "interest waiver, deferral, forbearance, forgiveness, modification, and amendment" of loans. (*Id.* at 15.) But without citation to any authority, it simply contends that loan modifications do not count in determining whether or not a loan is defaulted. (Opp. at 4.)

The Division notes that Section 7.7(a), which makes plain Patriarch's discretion to amend or modify loans, does not expressly reference the loan categories. But it ignores that Section 7.7(a) underscores the ability to modify or amend "*notwithstanding anything else*" in the indentures. (Ex. 5 § 7.7(a) (PP050056); Ex. 6 § 7.7(a) (PP050399); Ex. 7 § 7.7(a) (PP001881).) The law is clear that that kind of language overrides anything else in a contract. *See Int'l Multifoods Corp. v. Commercial Union Ins. Co.*, 309 F.3d 76, 90–91 (2d Cir. 2002). There is also nothing in the plain language of the definitions distinguishing performing from defaulted loans to suggest that amendments do not count.

In a related effort to find something that was not disclosed, the Division asserts that Patriarch's approach to categorization obscured what it contends was the proper OC Ratio. (Opp. 1.) But this does not advance matters for the Division. The OC Ratio is a calculation defined in the indentures. (Ex. 5 § 1.1 (PP049949); Ex. 6 § 1.1 (PP050276); Ex. 7 § 1.1 (PP001762-63) (definitions of the OC Ratio).) The Division, itself, concedes in the OIP that "[t]he category of each asset, which is published in the trustee reports, determines its value for calculating the numerator of the OC Ratio." (Ex. 1 ¶ 34.) Thus, any investor aware that Patriarch had accepted reduced interest on loans it categorized as performing, would also know that the categorization affected the OC Ratio.

If an investor agreed with the Division's post hoc interpretation of the category definitions, all the investor had to do was to treat all the loans that had not paid full interest defaulted, mark them down under the indenture definitions, and calculate the revised OC Ratio. And if that hypothetical investor agreed with the Division's view as to how the indentures were to be interpreted, the investor could decide, for itself, whether the OC Ratio met the thresholds in the indentures. Which is to say that the point the Division drives here does not move its case from a breach of contract case, which it has no authority to bring, to a fraud case.

The testimony that the Division cites also does not change that reality. All of the testimony is based on the mistaken contention, urged by the enforcement staff onto the investors, that the loans were not amended and were, in fact, in default. (*E.g.*, Opp. 11 ("Q. [W]ould you expect a company that is not current in its interest payment to be classified as" performing?).) The Division has failed to cite any testimony in which it asked investors whether Patriarch had discretion to accept reduced interest, and thereby avert defaults in the first place.

Moreover, multiple witnesses confirmed the simple and obvious: they knew that loans categorized as performing were not always generating full interest and that Patriarch was exercising discretion to avert defaults by amendment. For example, when the Division asked a witness for investor MBIA, "[D]oes an amendment affect the way in which a loan should be categorized"?, he said it would not "automatically" do so but that the amendment would be relevant insofar as what it might "impl[y]" about the "health of the company." (Ex. 19, at 122-24.) The Division ignores this testimony, and largely ignores the extensive evidence cited in Patriarch's moving papers that the investors and other stakeholders were well aware that Patriarch had the ability to enter into loan amendments that would avert borrower defaults. The Division makes only isolated criticisms of Patriarch's evidence, all of which are clearly wrong.

The Division buries in footnote its "response" to the powerful evidence that Natixis in fact also knew the obvious: "Categorization: knows its @ her discretion to categorize assets. . . . If she continues 2 fund co. it will get a high rating. They have a 100% manager risk which was disclosed." (Ex. 11, at SECNOTES000526-27.) Says the footnote: "The Division does not agree with the interpretation of those notes as set forth by Respondents." (Opp. 7 n.3.) That is hardly a real response. And, tellingly, after taking these notes, the Division chose not to interview Natixis on the record.

Patriarch cited a June 2011 email in which Barclays ascertained on its own what was supposedly concealed — that Patriarch was collecting reduced interest on performing loans. The Division attempts to step around the email by claiming the email was not "about categorization." (Opp. 6 n.2.) But that is just false. The email expressly states that Barclays calculated the missing interest by looking at the amount of "*performing* funded assets," which is a clear reference to the loan categories. (Ex. 13, at 2 (USB 00096) (emphasis added).)

Patriarch also cited a 2010 email chain among the trustee and a ratings agency clearly illustrating that they knew exactly why loans not paying full interest were "being treated as performing" (Ex. 14, at 1 (KRU00009021)). The Division's sole response to this evidence is to claim that the email does not show "the propriety" of Patriarch's approach. (Opp. 7 n.3.) But here again, the Division has brought a fraud case based upon the premise that Patriarch's approach to categorization was not *disclosed.*

Finally, the Division attempts to downplay the import of an October 2004 email chain among the bankers and ratings agencies involved in Zohar I showing that the parties considered, but rejected, a proposal to require that loans be categorized as defaulted in cases where an amendment averts a default. (Ex. 12 at 1, 3 (NNA_SEC_0009412, 14).) The Division shrugs off the email as having "occurred after the fact." (Opp. 14.) But the email preceded Zohar II and III. In any event, the manner in which parties behave after a contract is signed is "often the strongest evidence" of what a contract means, because "parties to an agreement know best what they meant." RESTATEMENT (SECOND) CONTRACTS § 202 cmt. g (1981). The Division also appears to read the email's reference to "restructur[ings]" to encompass only "formal," written restructurings. (Opp. 14.) But the email makes no distinction between the two and there is reason to do so.

* * *

Patriarch exercised the discretion expressly bargained for, provided for, and disclosed in, the indentures. It did so in plain sight of each and every investor.

II. PATRIARCH HAD NO AFFIRMATIVE DUTY TO DISCLOSE ITS INTERPRETATION OF THE ZOHAR INDENTURES

The Division's categorization case fails for the additional reason that contracting parties have no legal duty to disclose their interpretation of contracts. (Pat. Br. 13-15.) An

interpretation that ultimately proves incorrect amounts to, at most, a private suit for breach of contract. (*Id.*) The Division does not dispute this basic legal point, but argues that "what this case is about" is that the "Zohar indentures plainly require" loans to borrowers who pay reduced interest to be deemed defaulted. (Opp. 16.) In other words, the Division claims that Patriarch's interpretation of the indentures is wrong and that it breached the indentures as a matter of law.

The Division's claims in this regard are irrelevant in the context of a fraud case based on nondisclosure. In any event, Patriarch's interpretation is correct, for all the reasons discussed in its moving papers, which the Division fails to meaningfully rebut.

For example, Patriarch showed that the Division's cramped reading would doom the basic investment strategy from the start, because the portfolio companies would be starved of cash when they needed it the most. (Tilton Aff. ¶¶ 5-7.) The Division mentions in a footnote that, if the OC Ratio (calculated according to the Division's preferred methodology) caused the CLOs to default, the "controlling" investors might allow Patriarch to continue working instead of liquidating the deals altogether. (Opp. 8 n.4.) But that narrow response fails to address the larger issue, which is undisputed: under the indentures, automatically defaulting loans paying reduced interest severely constrains and often shutters further investment in companies most in need. (Tilton Aff. ¶¶ 5-7.) That would doom the disclosed business strategy and, standing alone, casts serious doubt on the Division's reading of the indentures. *See L. N. Jackson & Co. v. Royal Norwegian Gov't*, 177 F.2d 694, 700 (2d Cir. 1949) ("Business contracts must be construed with business sense.").

For this reason, as well, the Division's categorization case should be summarily dismissed.

III. THE DIVISION HAS FAILED TO ALLEGE ANY FRAUD ON PATRIARCH'S "CLIENTS"

The Division does not dispute that its claims under the Advisers Act §§ 206(1) and (2) require it to prove that Patriarch defrauded their "clients", the Zohar CLOs. Nor does the Division dispute that Ms. Tilton is the principal and ultimate owner of the "clients". (Tilton Aff. ¶ 9.) The Division nonetheless contends that Ms. Tilton somehow defrauded her own companies. The Division is wrong as a matter of law.

A. There is No Case Law Holding That an Adviser Can "Defraud" Him or Herself

Courts routinely reject claims that a sole shareholder deceived the company because, in those circumstances, the shareholder could "hardly have defrauded himself or breached a fiduciary duty to himself." *In re Doctors Hosp. of Hyde Park, Inc.*, 474 F.3d 421, 428 (7th Cir. 2007).[1] For example, in *In re Tufts Elecs., Inc.*, 746 F.2d 915 (1st Cir. 1984), a bankruptcy trustee accused a company's former sole shareholder of usurping a corporate opportunity to buy land. The First Circuit rejected the claim because "the corporate opportunity doctrine is a rule of disclosure," and the defendant could not "be accused of defrauding or concealing information from himself." *Id.* at 917.

The Division argues that this common sense proposition applies only when "the defrauder and the defrauded are identical." (Opp. 20 (emphasis in original)). The Division, however, cites no case endorsing that limitation, which is inconsistent with all the cases cited above. *See, e.g., Tufts*, 746 F.2d at 917 (dismissing nondisclosure claim while acknowledging

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[1] *See also, e.g., Tow v. Amegy Bank N.A.*, 505 B.R. 455, 467 (S.D. Tex. 2014) (sole shareholder "cannot be liable for breaching a fiduciary duty owed to himself"); *Battleground Veterinary Hosp., P.C. v. McGeough*, 2007 WL 3071618, at *17 (N.C. Super. Oct. 19, 2007) ("[T]o hold that [sole shareholder] breached a fiduciary duty would mean only that he breached a duty to himself. Because this conclusion is a *non sequitur*, the Court declines to adopt it."); *In re Gordon Car & Truck Rental, Inc.*, 65 B.R. 371, 376 (Bankr. N.D.N.Y. 1986) ("[T]he individuals cannot be accused of withholding or concealing information from *themselves* as sole shareholders and officers.").

that ownership does "not make that corporation and the individual owner identical"). Patriarch is aware of no case (and the Division has not cited one) in which an Advisers Act defendant was held liable under the peculiar theory that he or she defrauded a "client" he or she owns.

The two cases the Division cites on this point are easily distinguishable. In *SEC v. Ficeto*, 839 F. Supp. 2d 1101, 1106 (C.D. Cal. 2011) (Opp. 20), the defendant was alleged only to be the "de facto controller," not the owner, of the client funds. The decision *United States v. Sain*, 141 F.3d 463 (3d Cir. 1998) (Opp. 20) is even less helpful because the court ruled the defendant could not have entered into a "conspiracy" with his own company. *Id.* at 475. An owner "defrauding" her own company is equally impossible.

The claims under Advisers Act §§ 206(1) and (2) must therefore be dismissed.

B. Patriarch's Knowledge is the CLOs' Knowledge Under Agency Law

The Division's claims under the Advisers Act §§ 206(1) and (2) fail as a matter of basic agency law, as well. (Pat. Br. 17.)

1. There are No Allegations Akin to "Outright Looting" for Purposes of the Adverse Interest Exception

The Division does not dispute that Ms. Tilton was an agent of the Zohar CLOs, whose knowledge would ordinarily be imputed to the CLOs. Nevertheless, the Division contends that it is possible for the Zohar CLOs to have been defrauded by Ms. Tilton under the "adverse interest" exception of agency law. That is wrong as a matter of law, and is an independent ground to dismiss the client-based claims.

Under the narrow adverse interest exception, an agent's knowledge is not imputed to the principal in cases where the agent has "totally abandoned his principal's interests." *Center v. Hampton Affiliates, Inc.*, 488 N.E.2d 828, 830 (N.Y. 1985). For these purposes, *total* abandonment is required, and the exception "cannot be invoked merely because [the agent] has a

conflict of interest or because he is not acting primarily for his principal." *Id.* This "avoids ambiguity where there is a benefit to both the insider and the corporation, and reserves this most narrow of exceptions for those cases—outright theft or looting or embezzlement—where the insider's misconduct benefits only himself or a third party." *Kirschner v. KPMG LLP*, 938 N.E.2d 941, 952 (N.Y. 2010). These legal principles are not disputed. (Opp. 22 (citing *Kirschner*).).

Here, the unrebutted evidence shows that Patriarch modified loans because Ms. Tilton believed all stakeholders would benefit from the companies having more time to turn around. (Tilton Aff. ¶¶ 5-7.) The Division has *conceded* that it is not challenging Ms. Tilton's subjective judgment in this regard. (Ex. 9, at 4.)

The Division's claims that Ms. Tilton's "conduct resulted in [Patriarch's] receipt of about $200 million" in additional compensation (Opp. 22), but that bare statement is not supported by any evidence and thus should be rejected out of hand. For purposes of summary disposition, the Division must actually "produce documents, affidavits or some other evidence." *In the Matter of Jeffrey L. Gibson*, 2008 WL 294717, at *6 & n.26 (S.E.C. Feb. 4, 2008).[2]

Even if the Division had presented evidence on this point, it would not suffice. The Division's allegation is premised on the assumption that the CLOs would have terminated in 2009, when the supposedly correct OC Ratio would have failed. (Ex. 1 ¶ 44.) That Patriarch did not allow the CLOs to fail from the outset, and was compensated for the actual hard work

[2] The Division suggests that it may have additional relevant evidence in its expert reports, and urges the Court to defer this motion until then. (Opp. 9 n.5 (citing ROP 250(b)).) But deferring a motion is appropriate only if "a party, for good cause shown, cannot present by affidavit prior to hearing facts essential to justify opposition to the motion." ROP 250(b). There is no "good cause" here, since the Division made this allegation about additional compensation in its OIP in March, and has had ample time (including over five years of investigation) to support its claim. (Ex. 1 ¶¶ 6, 44.)

done managing billions in assets for the past six years, can hardly be called "outright theft" undertaken "only" to benefit itself. *Kirschner*, 938 at 952.

2. There Are Concededly No "Innocent" Fund Insiders to Whom Disclosure Would Be Made

The Division does not dispute the general proposition that the adverse interest exception is likewise inapplicable when there is no "innocent" decision maker among management to have addressed the alleged wrongdoing, nor does it dispute that there are no "innocent" insiders in this case. (Pat. Br. 17.) This is an additional reason to dismiss the client-based claims.

The Division's only response, on this point, is to contend that these principles do not apply in "the enforcement context." (Opp. 23.) According to the Division, these principles relate only to causation, which the Division need not prove. (*Id.*) But the Division cites no case adopting its position, and there is no reason to invent a limitation along those lines.

The existence of an innocent member of management is important in any case about disclosure because, otherwise, there is no true third party to whom any disclosure can be made. Here, the OIP alleges that Patriarch has not "given the Funds or investors a choice as to whether to consent" to its approach to categorization. (Ex. 1 ¶ 56.) To whom at the Zohar CLOs should Patriarch have disclosed its approach? The Division does not say. Patriarch managed all the CLOs' day-to-day affairs and cannot be accused of failing to disclose things to itself.

For this independent reason, any issue of disclosure should be focused, solely, on the outside investors, and the client-based claims must be dismissed.

CONCLUSION

For all of the reasons stated above, as well as those set forth in its moving papers, Patriarch respectfully requests that the Court grant this motion for summary disposition, and

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of LYNN TILTON, PATRIARCH PARTNERS, LLC, PATRIARCH PARTNERS VIII, LLC, PATRIARCH PARTNERS XIV, LLC, and PATRIARCH PARTNERS XV, LLC, Respondents.	Administrative Proceeding File No. 3-16462 Hon. Judge Carol Fox Foelak

REPLY DECLARATION OF CHRISTOPHER J. GUNTHER

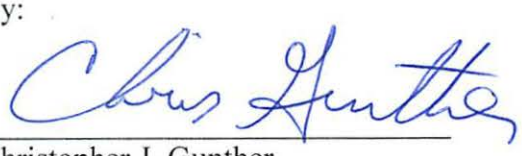
1. I am a member of the law firm Skadden, Arps, Slate, Meagher & Flom LLP, attorneys for the above-referenced Respondents I respectfully submit this reply declaration in further support the Respondents' Motion for Summary Disposition.

2. I attach as Exhibit 19 a true and correct copy of excerpts from transcript of the investigative testimony of Anthony McKiernan, taken on May 16, 2014.

I declare under penalty of perjury under the laws of the United States that the foregoing is true and correct to the best of my knowledge

Executed on June 10, 2015, in New York, New York

By:



Christopher J. Gunther
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Exhibit 19

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

In the Matter of:)
) File No. HO-11665
PATRIARCH PARTNERS, LLC) D-3350
)

WITNESS: ANTHONY McKIERNAN

PAGES: 1-144

PLACE: Securities and Exchange Commission
Brookfield Place
200 Vesey Street
New York, New York 10281-1022

DATE: May 16, 2014

The above-entitled matter came on for hearing at 9:35 o'clock a.m.

APPEARANCES:

On behalf of the Securities and Exchange Commission:

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BY: SUSAN F. DiCICCO, ESQ.
BRYAN P. GOFF, ESQ.

PROCEEDINGS

MS. SUMNER: We are on the record at 9:35 on May 16, 2014.

Will you please raise your right hand:

Do you swear to tell the truth, the whole truth and nothing but the truth?

THE WITNESS: I do.

Whereupon,

ANTHONY McKIERNAN,

appeared as a witness herein and, having been first duly sworn, was examined and testified as follows:

EXAMINATION BY
MS. SUMNER:

Q. Please state and spell your full name for the record.

A. My name is Anthony Matthew McKiernan; A-N-T-H-O-N-Y M-A-T-T-H-E-W M-c-K-I-E-R-N-A-N.

Q. Mr. McKiernan, my name is Amy Sumner. I'm a member of the staff of the Enforcement Division of the Denver Regional Office of the Securities and Exchange Commission. I am also an officer of the Commission for the purposes of this proceeding.

This is an investigation by the United States Securities and Exchange Commission in the matter of Patriarch Partners to determine whether

there have been violations of certain provisions of the Federal Securities Laws. However, the facts developed in this investigation may constitute violations of other federal or state, civil or criminal laws.

Prior to the opening of the record, you were provided with a copy of the Formal Order of Investigation in this matter. It will be available for your examination during the course of this proceeding.

Mr. McKiernan, have you had an opportunity to review the Formal Order?

A. Yes.

Q. Prior to the opening of the record, you were also provided with a copy of the Commission's Supplemental Information Form 1662. A copy of that notice has been previously marked as Exhibit 33.

Mr. McKiernan, have you had an opportunity to read Exhibit 33?

A. Yes.

Q. Do you have any questions concerning this exhibit?

A. No.

Q. Mr. McKiernan, are you represented by counsel?

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interest accrued.
Do you follow me on that?
A. Yeah, I do.
Q. And we can go through other loan facilities, but I will represent to you that this seems to be a pattern among -- across the loan facilities for American la France.
Does it surprise you to see that there are significant amounts of uncollected interest on loan facilities to American la France?
A. I would say yes. To the degree that there are amounts due that just haven't been paid and that's the fact pattern, that would be surprising to me.
Q. And why is that?
A. I would expect that, to the degree that there were -- there were changes to the loan agreement or something to that nature -- for example, we certainly see interest rates being changed in these transactions, things like that, I would expect that there would be some formal modification or amendment or waiver that would be within the scope of the documents of the transactions that would dictate why there might be changes in interest payments.
But to the degree that those items

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haven't occurred, but just funds haven't been collected, that would certainly be a concern to me from the way the transaction is structured.
Q. What about it is concerning to you?
A. To the degree that a company is simply not meeting its obligations, I'm not sure how a company could be classified as a true going concern, and I'm not sure how the company could generate audited financial statements that, you know, would certainly not depict or get a clean audit for that matter, that it was in compliance with its contracts and loan obligations if that wasn't the case.
I believe that to the degree there are changes, material changes to the loans, that there would have to be some kind of formal modification or documentation to that effect.
Q. And why do you think that?
A. I believe that is what the documents require.
Q. The deal documents?
A. Yes.
Q. Even if there were, let's say, amendments to the loan agreements, does the -- does that change the way -- does an amendment affect the way in which a loan should be categorized, in your

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mind?
A. I'm not sure that any one particular aspect would automatically -- you know, other than say, you know, if the company went into bankruptcy or something like that, there is obviously events that I think a one off basis would be clear.
I think that in the context of why an amendment was being done or why a modification was being done, what that really implied, as far as the health of the company, and to the degree that it ultimately amounted to what would be looked at as some kind of restructuring or pre-bankruptcy kind of action, might have a material impact on how that company is classified.
Q. I'm not sure I follow what you meant by that.
So an amendment -- I see. So are you saying that you need to look at the type of amendment or the circumstances?
A. I think there are requirements within the documents of how things needed to be done. To the degree that that's happening, then the question is: What is causing the need for that event to happen? So to the degree that a company can't pay its interest and the interest rate's been reduced

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five times in a year and a half or in the case you're showing me it went from a 10 percent rate to a 1 percent rate, it would seem to me that that would open -- that would be open for question as to does this company meet the definition of a category 4, or are actions being taken that would replicate a work out pre-bankruptcy or restructuring type activity that would cause one to look at the categories.
Was I clear on that?
Q. Yes. Thanks.
So are you surprised, given the lack of -- that's not what I'm trying to say.
Given the amounts of uncollected interest on American la France, are you surprised that American la France was classified as a 4 until it ceased operations in January of this year?
A. Yes.
Q. And why is that?
A. From the standpoint of looking at the financial statements of the company, discussions with the manager, and then on top of it, if this is the case that actual due interest was just not being paid and in essence the company was in default of its debt obligations, it would surprise me that the company was a category 4 until it actually filed for

CERTIFICATE OF SERVICE

I hereby certify that a true copy of the foregoing was served on the following on this 10th day of July 2015, in the manner indicated below:

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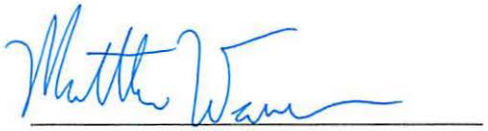
1961 Stout Street, Ste. 1700
Denver, CO 80294
(By Email pursuant to the parties' agreement)



Matthew T. Warren

FACSIMILE CERTIFICATION

I hereby certify that the enclosed filing was transmitted via facsimile on July 10, 2015 to the Office of the Secretary at the number (202) 772-9324.

Matthew T. Warren