UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

SECURITIES AND EXCHANGE COMMISSION,	§	
	§	
Plaintiff,	§	
	§	Case No.
v.	§	3:09cv0298-N
	§	
STANFORD INTERNATIONAL BANK, LTD., ET AL,	§	
	§	
	§	
Defendants.	§	
	§	
	§	
	§	

WESTRIDGE COMMUNITY DEVELOPMENT DISTRICT'S REPLY TO RECEIVER'S RESPONSE TO MOTION FOR LEAVE TO PROCEED IN STATE COURT FORECLOSURE ACTION AGAINST STANFORD INTERNATIONAL BANK, LTD.

Westridge Community Development District (the "District"), a local unit of special purpose government of the State of Florida, by and through its undersigned attorneys, hereby files this reply ("Reply"), to Receiver, Ralph S. Janvey's ("Receiver"), response to the District's Motion for Leave to Proceed in State Court Foreclosure Action Against Stanford International Bank, Ltd., and, in support of said Reply states as follows:

Procedural History

On February 9, 2010, the District filed a motion with this Court seeking relief from an injunction established by the Court in its Order Appointing Receiver (Doc. 10), dated February 16, 2009, and Amended Order Appointing Receiver (Doc. 157), dated March 12, 2009, which enjoined all judicial, administrative, and other proceedings located in other forums with respect to Stanford International Bank, Ltd. ("Stanford"). The Motion sought leave of the Court to allow

the District to proceed in State of Florida Circuit Court to foreclose out assessments on certain real property on which the District holds a first lien, coequal with all State of Florida, County, school district and municipal taxes, and superior in dignity to all other liens, titles, and claims on the subject property. Stanford holds a junior lien in the form of a mortgage on the subject property which as a result, stays the District's foreclosure action against the owner of the Property.

On March 17, 2010, the Receiver filed a response to the District's Motion. The Response alleges that the Court should not lift the injunction granted by the Court as such relief would "render worthless SIBL's [Stanford] $85 million investment in American Leisure Group, Ltd. and would greatly disrupt the central purpose of the Receiver's work—identifying and distributing assets in an orderly, efficient and impartial manner to all the victims of the Stanford Defendant's fraud." *See* Response, pg. 1. Receiver identifies in its Response the three-prong test established in *SEC v. Wencke*, 622 F.2d 1363, 1373-74 (9th Cir. 1980), and as adopted by a myriad of other federal courts, as the determinative test on whether the Court should lift the Court ordered stay. *Id*. at pg. 3. District agrees that *Wencke* is the proper test for the Court to balance the interest of the competing parties; however, District believes that the Wencke test weights heavily in favor of the District.

Argument

1. Lifting the Injunction this early in the receivership will not interfere with the Receiver's ability to maintain the status quo and failure to lift the injunction will cause substantial injury to the District.

Receiver argues that it is important that the Court not lift the stay so as to protect the status quo. Receiver argues that failure of the Court to maintain the status quo would result in thousands of lawsuits by defrauded creditors and investors and would result in the Receiver not

spending the time needed to perform the duties requested of a receiver in these actions. Furthermore, Receiver argues that the Receiver has only had 13 months to "unravel Defendants" complicated matrix of companies, assets, and investor account transactions." *Id* at pg. 8. This argument is speculative and has no relevance to the District's cause of action in District's state court action. The District is requesting that this Court allow it to proceed in State Circuit Court on claims that are unrelated to the purpose of the Receivership. As pointed out by Receiver in its Response, the purpose of the Receivership is to protect defrauded investors and to marshal and untangle company assets without being forced into court by every investor or claimant. *Id.* at page 4. The District claims, however, are inherently different from other claims asserted against Stanford. The District is not a defrauded investor, creditor, or party to the alleged fraud that occurred between Stanford and innocent third-parties. The property sought to be foreclosed is not property which is part of the Receivership Estate. Rather, the property is subject to a junior lien in favor of Stanford Bank that was executed and recorded after all of the transactions giving rise to the District's claims. The District is seeking to foreclose a mortgage held by Stanford on a matter that is unrelated to the purpose behind the receivership, i.e. to determine how to collect, manage, and untangle assets in order to protect defrauded creditors. Regardless of the outcome of the receivership, the District has a superior claim to the collection of the assessments encumbering the mortgaged property and will be provided the right to proceed in state court against the encumbered property. It is doubtful, although argued by Receiver, that multiple other claimants have claims that are provided this super priority both by Florida Statute and the United States Bankruptcy Code. Untangling of the assets is not required with respect to District's action in order for the District to be able to proceed in District's state court action. Therefore, timing of the request of the District to lift the stay is not a critical issue, although Receiver has had ample

amount of time to determine Stanford's position with respect to the District's state court case. Receiver's actions are nothing more than an attempt to stall the District's cause of action, which is causing extreme financial hardship on the District. *See Securities Exchange Commission v. Wencke*, 742 F.2d 1230, 1232 (9th Cir. 1984), 742 F.2d at 1231 ("[A]t some point, persons with claims against the receivership should have their day in court. The receivership cannot be protected from suit forever.").

Before determining that the status quo should be maintained, the Court in *Wencke* made it clear that you must weigh maintaining the status quo to the injury the movant will suffer if the movant is not afforded the right to proceed. *United States v. Acorn Technology Fund, L.P.*, 429 F.3d 438, 443 (3rd Cir. 2005) (adopting *Wencke* and stating "[F]ar into a receivership, if a litigant demonstrates harm will result from not being able to pursue a colorably meritorious claim, we do not see why a receiver should continue to be protected from suit."). Receiver argues in its Response that the only injury District will suffer is a delay in its enforcement action under its complaint. *See* Response, page 7. Receiver, however, fails to address the District's current financial emergency. As asserted in District's Motion, the District is currently facing a financial emergency for failure to make bond debt service payments when due. *See* District's Motion, par. 24. The bonds are in default because there were insufficient funds to make the interest payment due on November 1, 2009. *Id*. Moreover, because the District is unable to levy and collect its operation and maintenance fees from the defaulting property owners, District is unable to pay its obligations as they come due and is classified by its accountants as being at risk in its ability to continue as a going concern. *Id*.

Under Florida's statutory scheme for community development districts (Fla. Stat. Chapter 190), the only type of income available to operate the District and to make required

bondholder payments is the ability to levy special assessments upon the real property within the District. Without such income, the District will be irreparably injured as the District will be forced to shut down operations, lay off staff, and will be in violation of applicable law regarding its operation. The lack of funding renders the District unable to publish required meeting notices, to keep staff to comply with reporting and auditing requirements or otherwise to conduct business. Ultimately, the District might be turned over to the Office of the Florida Governor and placed in a receivership or some form of government supervision. *See Wencke*, 742 F.2d at 1232 (lifting the stay with respect to movants claim holding that "[t]he receiver does not intend to maintain the status quo, but rather intends action that will irreparably injure the appellants.).

Financial hardship has been recognized by the Courts as a legitimate reason for lifting a stay. *See United States v. ESIC Capital, Inc.*, 685 F.Supp. 483 (D. Md. 1998). In *ESIC Capital, Inc.*, the movant requested the court to lift the stay and allow her to foreclose on real property. *Id*. at 486. The movant, albeit a single mom, argued that failure to lift the stay would result in substantial injury because the movant had no source of income to provide for her family. *Id*. at 485. The only prospective source of income the movant had was a first lien on real property that movant desired to generate income through foreclosure. *Id*. The court, weighing the interest of the receiver to maintain the status quo as compared to the injury the movant would suffer as a result of the court's failure to lift the stay, ruled in favor of the movant and lifted the stay with respect to the encumbered property only. *Id.* at 485, 486. The District, while understandably not in the same class as a single mom seeking to provide for a family, sits in an almost identical financial position. The District's only source of income is either payment of the assessments by the Receiver (and maintain the assessments current) or foreclose on the real property.

The Receiver's Response has understandably ignored this portion of the District's Motion. Instead, it argues about the prospect of a hypothetical "white knight" which might make an investment in the project and permit the Receiver to realize payment on its junior mortgage. The Receiver provides no evidence to support this idea. At a minimum, it should be required to demonstrate to this Court in an evidentiary hearing that there is a real prospect that any of this might happen.

Receiver argues that the only way for it to recover any significant value on its investment is to maintain the status quo in order to allow prospective investors to come into the project and complete construction and generate income. *See* Response, page 1. The District and the other secured creditors on the Tierra del Sol project have already seen this movie and know how it ends. The project developer and Bankruptcy Debtor, Tierra del Sol Resorts, Inc., already promised District on numerous occasions that investments funds were imminent. When those funds did not materialize, it filed a Chapter 11 proceeding (See In re: *Tierra Del Sol Resort, Inc*., Case No.: 6:09-bk-07266-ABB, Bankr. M.D. Fla.) and promised to obtain debtor in possession financing to rejuvenate the project, close condominium units and complete the amenities. None of those things happened, and, as a result, the Chapter 11 action has been converted to a Chapter 7 proceeding. The discovery which led to this conversion demonstrated that the project was a distressed property in a distressed market, that there existed no prospect of obtaining funding for the hypothetical condominium sales expected to save the project, and that the sale values projected by the developer were unrealistic in the market. Receiver's argument that investors are now ready to purchase the property and generate income is hopeful at best. Weighing the certain prospect of injury to the District against the speculative prospect that the project might be built out and sold, District would submit that the scales tip heavily in favor of the District. This Court

should not allow a stay to remain in effect that will cause irreparable injury to the District based on "hope" alone. At a minimum, the District is entitled to an evidentiary hearing on these issues.

Furthermore, Courts have recognized the importance of municipalities being able to perfect and enforce municipal liens during the time of court-ordered stays, especially, as in this instance, when a debtor is involved in a Chapter 7 proceeding.[1] *See Matter of Henry*, 173 B.R. 878 (Bankr. N.J 1993). The court was confronted with whether to lift a stay issued in bankruptcy court for "cause" under 11 U.S.C. 362(d) because of the potential inability of the debtor to pay its post-petition taxes as administrative expenses since debtor's efforts in a Chapter 11 reorganization failed, leaving doubt that the post-petition taxes would ever get paid to the municipality. *Id*. at 882. In lifting the stay to allow the municipality to perfect its post-petition taxes, the court provided the following explanation:

> *"In the first place, any hope of reorganization of the debtors has disappeared and the debtors themselves have consented to the court conversion of their case to one under chapter 7. In this regard, the court notes that it is one thing to require that the creation of a municipality's tax lien is stayed while a viable chapter 11 reorganization is moving forward. In such a situation, the fundamental principles underlying the bankruptcy code require that a debtor be entitled to treat the payment of its taxes in the chapter 11 plan, with the option of spreading out their payment, in order to facilitate reorganization. It is quite another situation entirely, however, when the court is faced with a failed chapter 11 reorganization and debtor is attempting to "sell" as asset outside the plan to its secured creditor, the result being that both the debtor and the secured creditor avoid any responsibility for the accrued real estate taxes merely by transferring title to the property of the estate.*
> *Id*. at 882. (emphasis added).

In this case, it appears that District finds itself in a similar position: Debtor in a chapter 7 proceeding and Receiver looking to avoid payment of the accrued special assessments by prolonging the Court's stay.

[1] Community Development Districts are afforded the same protection as municipalities are with tax liens with respect to priority of special assessments and enforcement of special assessments. See Florida Statutes, Chapters 190 and 170 generally.

The issue of whether the Tierra del Sol property is a viable development or has such substantial equity so as to pay off the District and other lienholders and then yield sufficient assets for the Receivership has already been substantially litigated in the Bankruptcy Court for the Middle District of Florida, which has granted a number of requests for relief from the automatic stay. At a minimum, the District is entitled to an evidentiary hearing at which the Receiver substantiates its belief in the viability of a project which the bankruptcy trustee and bankruptcy judge have not found to exist.

2. <u>District's claim in State Court Circuit Claim has merit.</u>

There appears to be no dispute that District's claim in State Circuit Court has merit and is likely to prevail on the merits. In fact, Receiver acknowledges in the Response that the District has a "superior lien" on real property that Stanford holds an interest. *See* Response, pg. 2. Furthermore, Receiver attempts to persuade this Court that such factor is "immaterial because in this case the other factors outweigh this one." *Id*. at pg. 9. However, the Court in *Wencke* expressed the importance of this factor where the receiver's claim holds little weight and the movant is likely to be prejudiced by the stay. *See Wencke* 622. F.2d at 1373, 1374. ("where the likelihood that the receiver will prevail is small, when the receiver's position is considered realistically and not in the abstract, there is less reason to permit the receiver to avoid resolving the claim; a blanket stay should not be used to prejudice the rights which innocent and legitimate creditors may have against the receivership entities.") (also stating "as the receivership progresses, however, it may become less plausible for the receiver to contend that he needs more time to explore the affairs of the entities. *The merits of the moving party's claim may then loom larger in the balance*."(emphasis added)). As stated above, the District holds a first lien, coequal with all State of Florida, County, school district and municipal taxes, and superior in dignity to

all other liens, titles, and claims on the subject property. This super priority lien, which has priority over Stanford's interest in the real property, gives the District a "colorable claim" which justifies lifting of the receivership stay. At this point in the receivership there is nothing more that the Receiver can learn with respect to the claim that District has against Stanford. This is a simple foreclosure action with respect to real property upon which Stanford holds an inferior interest. No claims of fraud, collusion, or other deviate acts have been alleged with respect to the lien that Stanford holds. There is little doubt that the District will be prevail in its state court claim and as a result, this Court should not allow the Receiver to avoid the inevitable by hiding behind the Court's blanket stay.

3. If the Court determines *Wenke* weighs in favor of the Receiver, then the Court is required to compel Receiver to keep the District assessments current.

In the event the Court determines that the factors in *Wenke* weigh in favor of the Receiver, then the Court is required to compel the Receiver to keep the District's assessments current as the Court will be treating the Property as part of the Receivership Estate. Federal courts have long held that "property in the hands of a receiver of any court, either of a state or of the United States, is as much bound for the payment of taxes, state, county, and municipal, as any other property." See *Union Trust Co. v. Great Eastern Lumber Co., et. al.,* 248 F.46, 47 (5th Cir. 1918) (noting the importance of the court's duty to "recognize as paramount, and enforce with promptness and vigor, the just claims of the authorities for the prescribed contributions to state and municipal revenue" citing reference omitted*).* In fact, courts have held that such liens are "prior to all other liens whatsoever, except judicial costs, which are first to be paid where the property is rightfully in the custody of the court." *Id.* at 47. See also *City of New Orleans v. Malone et al*., 12. F. 2d 17 (5th Cir. 1926) (holding that appellant's lien for taxes in a receivership were prior to all other liens whatsoever except judicial costs).

In *Central Vermont Ry. Co. et al v. Marsh et. al*, 59 F. 2d 59 (5th Cir. 1932), the Court was presented with the question of whether receivers were liable for the unpaid taxes that accrued during a receivership. The Court, while holding that the receiver was responsible for paying the unpaid taxes due on real estate out of the general fund of the receivership estate, relied upon two prior Second Circuit Court of Appeals decisions. *Id*. at 61. First, the Court analyzed the holding in *Carthage Sulphite Pulp & Paper Co*., 8 F. 2d 35 (2nd Cir. 1925). In that case, the Court held that a mortgagee was a general creditor only with respect to the taxes that were assessed prior to the receivership, but as to taxes that were assessed after the receivership, the mortgagee had a prior claim "as such taxes constituted one of the expenses of the receivership." *Id*. The second case the Court analyzed was *MacGregor v. Johnson-Cowdin-Emmerich, Inc.*, 39 F.2d 574 (1930). *Id*. In that case, the receivers took over as part of the receivership estate certain real estate, a part of which was a mill, that was subject to a mortgage. *Id*. The mortgagee claimed that the receivers should pay the taxes that accrued on the property before and subsequent to the receiver's appointment. *Id*. The Court held that the receivers were required to pay the taxes out of the general fund of the receivership estate and offered this following explanation:

> "The taxes accruing after the receivers entered are in a different position. They could have refused to accept the mill, if they had thought the equity a burdensome asset. Having elected to enter, they took it cum onere, and the taxes, which were a condition upon their continued occupation, were as much a part of their expenses as heat, custody or current upkeep. So far as we have found, courts have universally regarded them as part of the receivers' expenses, when the question has come up."

Id. (citing references omitted). *See also, McFarland v. Hurley*, 286 F. 365, 366 (5th Cir. 1923) (holding receiver liable for taxes as receivers "are custodians of the property for the benefit of the litigants, and the property in their hands should bear whatever tax burdens it . . ..").

In the current Receivership, at least $129 Million has been collected for payment of costs and claims of the Stanford victims, pursuant to the October 28, 2009 Interim Report [859]. As of that time, nearly $60 Million had been spent in Receivership expenses. As of February 2, 2010, another $10 Million in expenses was authorized. Unless the Receiver intends to spend all of the available funds on the costs of the Receivership, monies are available to pay current the claims of the District. Payment of those claims will also help to maximize any potential recovery related to the Tierra del Sol property, because current payment prevents acceleration of the special assessment claims under Florida law. The claims of the District should clearly be paid prior to payment of other general claims against the Receivership. A refusal of the Receiver to recognize and pay these claims is, in effect, a demand that the District bankroll the Receiver's activities. In view of the Court's findings that "the eventual size of the receivership estate will be smaller than initially hoped or expected" (Order [994]), District is entitled to prompt payment of its claims.

CONCLUSION

The District holds claims which are in the nature of local governmental tax and assessments liens. As such, it is in a position unique among the parties or claimants which may be affected by the Stay Order in this action. District's ongoing function requires that this Court permit it to assess and collect its special assessments. District believes that the claims of the Receiver that the continuation of the Stay will reap a bounty for the benefit of the Receivership Estate are hypothetical and the Receiver should be required in an evidentiary proceeding to demonstrate their viability. If the Receiver demonstrates that the Tierra del Sol property has substantial worth to the Receivership Estate, and the Court is convinced of that fact, then the

Court should require the Receiver to pay the ongoing assessments due to the District which arise from the property.

WHEREFORE, the District respectfully requests the entry of an order immediately either (i) granting it leave to proceed in the Circuit Court of the Tenth Judicial Circuit, in and for Polk County, Florida, to exercise all of its statutory rights and remedies in and to the real property subject to the SIB Mortgage, including, without limitation, foreclosing on the property, and taking actions necessary to levy and collect special assessments for District operations and maintenance budget purposes; or (ii) in the alternative, as a condition of continuing the stay, to require Receiver to pay the District all special assessments due and owing the to the District for the time period the Property is subject to the stay order. The District will, by separate filing, provide a detail of these amounts. The order should further require the Receiver to keep said assessments current while the Property remains subject to the stay. The District also requests that this Court and grant such other and further relief as this Court deems appropriate.

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on April 14, 2010, I electronically filed the foregoing with the Clerk of the United States District Court for the Northern District of Texas (Dallas Division) using the CM/ECF system which electronically sent notification of such filing to all registered users.

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