

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF FLORIDA
WEST PALM BEACH DIVISION

IN RE: Lead Case No.: 12-30081-BKC-EPK
CLSF III IV, Inc., *et al.*, Chapter 7
Debtor. (Jointly Administered)

**TRUSTEE’S AMENDED MOTION FOR SUBSTANTIVE CONSOLIDATION
OF THE JOINTLY ADMINISTERED BANKRUPTCY ESTATES AND
MEMORANDUM OF LAW IN SUPPORT**

Trustee Deborah C. Menotte, (“Trustee”), by and through undersigned counsel, and pursuant to 11 U.S.C. § 105, files this Amended Motion seeking substantive consolidation of Debtor CLSF III IV, Inc.’s bankruptcy estate with that of: (a) the bankruptcy estates of the thirty-two jointly administered bankruptcy estates of the affiliated Debtors (“Affiliated Debtors”): Behl Corporation, a Florida corporation; BGI 3 Life, Inc., a Florida corporation; BGI 5 Life, Inc., a Florida corporation; BGI 6 Life, Inc., a Florida corporation; BGI XVII Corporation, a Florida corporation; BGI XX Corporation, a Florida corporation; CLSF I, Inc., a Florida corporation; CLSF VII, Inc., a Florida corporation; CLSF VIII, Inc., a Florida corporation; CLSF XIV, Inc., a Florida corporation, CLSF XL, Inc., a Florida corporation; CLSF XLI, Inc., a Florida corporation; CLSF XV, Inc., a Florida corporation; CLSF XVI, Inc., a Florida corporation; CLSF XVII, Inc., a Florida corporation; CLSF XX, Inc., a Florida corporation; CLSF XXI, Inc., a Florida corporation; CLSF XXII, Inc., a Florida corporation; CLSF XXIII, Inc., a Florida corporation; CLSF XXIX, Inc., a Florida corporation; CLSF XXV, Inc., a Florida corporation; CLSF XXXI, Inc., a Florida corporation; CLSF XXXV, Inc., a Florida corporation; Friedman TR Corp., a Florida corporation; LSF I, Inc., a Florida corporation; LSF III, Inc., a Florida corporation; LSF IV, Inc., a Florida corporation; LSF VI,

Inc., a Florida corporation; RPM Life, Inc., a Florida corporation; Ryan Trust Corporation, a Florida corporation; The Gluck TR Corp., a Florida corporation; and The Sinder TR Corporation, a Florida corporation; and (b) the non-debtor trust entities, (“Non-debtor Entities”): BGI I Life, Inc., a Florida corporation; BGI II Life, Inc., a Florida corporation; BGI VII Corp., a Florida corporation; BGI VIII Corporation, a Florida corporation; BGI IX Corp., a Florida corporation; BGI X Corp., a Florida corporation; BGI XI Corp., a Florida corporation; BGI XII Corp., a Florida corporation; BGI XIV Corp., a Florida corporation; BGI XV Corp., a Florida corporation; BGI XVI Corp., a Florida corporation; BGI XVIII Corp., a Florida corporation; BGI XIX Corporation, a Florida corporation; BGI XXIX Corp., a Florida corporation; BGI XXI Corp., a Florida corporation; BGI XXII Corp., a Florida corporation; BGI XXIV Corporation, a Florida corporation; BGI XXV Corporation, a Florida corporation; BGI XXVI Corporation, a Florida corporation; BGIF 18 UA Dated 2-1-2010; BGIF 19 UA Dated 2-1-2010; CLSF IX, Inc., a Florida corporation; CLSF XII, Inc., a Florida corporation; CLSF XVIII, Inc., a Florida corporation; CLSF XXX, Inc., a Florida corporation; CLSF XXXII, Inc., a Florida corporation; CLSF XXXIV, Inc., a Florida corporation; CLSF XXXVI, Inc., a Florida corporation; CLSF XXXVIII, Inc., a Florida corporation; CLSF XXXIX, Inc., a Florida corporation; CLSF XLII, Inc., a Florida corporation; CLSF XXXXII, Inc., a Florida corporation; CLSF XLIII, Inc., a Florida corporation; CLSF XXXXIII Corporation, a Florida corporation; CLSF XXXXIV, a Florida corporation; CLSF XXXXV Corporation, a Florida corporation; CLSF XXXXVI Corporation, a Florida corporation; LSF II, Inc., a Florida corporation; LSF V, Inc., a Florida corporation; MP XXVI, Inc., a Florida corporation; Peck Associates Palm Beach, LLC d/b/a Deborah C. Peck, P.A.; The LIP Corporation, a Florida corporation; The LIP II Trust Corporation, a Florida corporation; The LIP III Trust Corporation, a Florida corporation; CLSF

1A Corporation, a Florida corporation; CLSF 3-4 A Corporation, a Florida corporation; CLSF 3-4 Corporation, a Florida corporation; CLSF 7 A Corporation, a Florida corporation; The Friedman Trust Corp., a corporation; The Feyga Darmanyans Ins. Trust UA DATED 10-07; The Guberman Trust; The Guberman TR Corp., a Florida corporation; Hassan Joher Family Insurance Trust; The Hassan Joher Family Insurance National Trust Corporation, a Florida corporation; The Hassan Joher Insurance Trust; Joher Family Trust Dated 9-10-2010; The Joher Family Aviva Insurance Trust Corporation, a Florida corporation; The Ibrahim Radadi Trust Dated 2-3-2011; The Rabadi Life Insurance Trust, Ryan TR Corp., a Florida corporation; The Ribadi TR Corp., a Florida corporation; The Klara Rosenberg Insurance Trust Dated 8-19-2012; The Spector Trust UA Dated 4-27-2010; The Spector TR Corp., a Florida corporation; The Teichman Trust Corporation, a Florida corporation; The Teichman TR Corp., a Florida corporation; The Lundvall TR Corp., a Florida corporation; and The Martha Elliott Insurance Trust Corporation, a Florida corporation, while preserving for the Trustee the right to pursue avoidance actions and/or other causes of action on behalf of individual debtors or debtor subgroups. In support, the Trustee states as follows:

Preliminary Statement

1. Substantive consolidation of the Debtor, the Affiliated Debtors and the Non-debtor Entities (with the Affiliated Debtors, the “Sub Con Entities”, each a “Sub Con Entity”) is essential to the proper administration of the Debtor and the Affiliated Debtors’ bankruptcy cases. Through the testimony of Deborah Peck before this Court on August 24, 2012, as well as facts since garnered by the Trustee’s financial advisors, Kapila and Company through their extensive review of the Sub Con Entities’ financial documents and records, it is clear that substantial grounds exist to support substantive consolidation.

2. As will be discussed in greater detail below, the Sub Con Entities were started and operated by the same individual, Deborah C. Peck, who then operated them as though they were one entity. Among other actions, Ms. Peck: comingled investor funds in trust accounts; failed to maintain separate accounting by investor; utilized funds from one policy's investors to (without authorization) pay the premiums of other policies; withdrew millions of dollars from the comingled funds accounts without investor knowledge or authorization; made payments to investors without explanation, and paid premiums on select policies while other policies lapsed (with, in some instances, investors continuing to pay premiums after their policy lapsed).

Background

3. Each of the Sub Con Entities began and was operated in a virtually identical way: Investors paid money into bank accounts established by Deborah C. Peck through her company, Deborah C. Peck, P.A., one of the Non-debtor Entities the Trustee is seeking to substantively consolidate. Watershed, LLC and/or its principal, Dennis Moens (collectively, "Watershed") would then use these funds to finance the purchase of life insurance policies by local providers in the United States that had licenses to buy and sell the policies. At times, policies were purchased directly from individual insureds. According to Ms. Peck, Watershed would then service and maintain the policies and open related escrow accounts. *See* Transcript of August 24, 2012 Hearing at 54-56.

4. Watershed packaged the policies for sale by the marketing entity, Quality Investments, located in Holland. The "package" was to include a reinsurance component. Quality Investments' job was to obtain the reinsurance, then market and sell the policies to European investors as investments in life settlements funds. Occasionally the "package" was set up even before the life insurance policy was actually purchased. Provident Capital Indemnity

(“PCI”) was to provide the reinsurance component for each of the life insurance policies. *See Id. generally* at 55-67. On January 19, 2011, the SEC filed a civil enforcement action and request for appointment of a receiver with regard to PCI. On January 21, 2011, the court in the SEC action appointed a receiver for PCI.

5. The investments sold by Quality Investments were organized into closed life insurance settlement funds under Dutch rules and law (the “CLSF Funds”), or bank guaranteed interest funds under Dutch rules and law (the “BGI Funds”), each with an agreement that governed the members’ involvement in that particular fund. *Id.* at 69-70.

6. Although Watershed did not take actual title to most of the life insurance policies, it “sold” each of the policies to a separate Florida trust with Ms. Peck as the trustee of each trust. As a result, over 55 separate trusts were formed, each of which at some point owned a policy. According to Ms. Peck, the beneficiary of each individual trust was a CLSF Fund or BGI Fund in which foreign investors had purchased participation interests. *Id.* at 69

7. Watershed was the grantor and Ms. Peck was trustee for each of the Florida trusts. *Id.* at 58.

8. Ms. Peck was an attorney admitted in New Jersey, but lived in Florida and, from 2005 forward, worked as trustee for all of the trusts out of the same office in Florida. *Id.* at 49.

9. Ms. Peck was in charge of operating and administering escrow accounts and subaccounts purportedly in the name of Watershed, as grantor for each of the trusts. Watershed had control over the accounts and would give her instructions “as to everything, including the payment of premiums, payment to providers for purchase of policies, payment to accountants that needed to be paid to care for the servicing of the trust” as well as payments for personal

items. These payments also included “fees that were required for the maintenance and servicing of the policies.” *Id.* at 73:3-8, 75:7-14.

10. “There was never an escrow account set up with each individual investor.” “[T]here was never an effort made to create individual escrow accounts either with the particular fund or with particular investors.” *Id.* at 75:21-25, 76:1.

11. Ms. Peck would give notice to Watershed regarding when premium payments were due. As payments came into the accounts, Peck would receive instructions from Watershed on how the funds were to be disbursed, including what premiums to pay and when to pay the insurance carriers. No escrow accounts were ever set up for the benefit of individual funds or individual investors. *Id.* at 73-76.

12. Corporations (the Debtor and the Affiliated Debtors) were later created, allegedly for tax purposes, to own the policies, which were transferred from the Florida trusts to the corporations. Each corporation was owned by the related trust, which became the sole shareholder, and the corporation signed a note in favor of the trust in the amount of the face value of the policy. Each of the related trusts held all of the shares of the related corporation. *See generally* August 24 Transcript at 54-60.

13. According to Ms. Peck, in 2012, Peck, purportedly concerned about the repercussions of a Dutch criminal investigation of Watershed and the PCI receivership, removed \$20 million from the escrow accounts and wired the funds to Dubai. There was no reconciliation regarding which policies and which trusts were affected by that transfer.

14. After the arrests in Europe by Dutch authorities of Moens, Laan and their attorney, and the related freezing of the Watershed accounts, Peck faced what she termed a “crisis” - she was no longer receiving money from Watershed to pay the policy premiums. The

administration of the policies was taken over by Admin QI (“QI”). Peck began writing to the individual investors in the closed funds asking them directly for money to pay the premiums on the policies. As she received the funds, she pooled them together, then used them as she deemed appropriate to pay premiums on policies on a “case by case emergency basis. If a policy was being lapsed, that’s the policy that would be paid.” *Id.* at 86-88, 96-97.

15. According to Ms. Peck, “ever since this crisis, I have pooled the policies, and have pooled the investors, so that I’m working on behalf of all of the investors, not a splintered group of investors.” *Id.* at 86:6-9. Further, “[e]ver since the portfolio became a distressed portfolio, I was obligated to do what I needed to do to preserve the assets. In order to preserve the assets I needed to collectivize the money that was coming in, and use that money on an emergency basis to pay premiums.” *Id.* at 87:25 -88:5.

Memorandum of Law

This Court Has the Power to Order Substantive Consolidation of the Debtor and the Sub Con Entities

16. This case is ripe for substantive consolidation of the Debtor and the Sub Con Entities and this Court clearly has the power to order it. Substantive consolidation is appropriate when “the economic prejudice of continued debtor separateness” outweighs “the minimal prejudice that substantive consolidation might cause.” *Eastgroup Properties v. Southern Motel Assoc., Ltd.*, 935 F.2d 245, 249 (11th Cir. 1991); *In re Murray Industries*, 119 B.R. 820, 829 (Bankr. M.D. Fla. 1990). Where, as here, there is a comingling of funds among entities, a disregard of corporate formalities, operations as if a single entity, significant financial and operational decisions being made by the same individual for all entities and arbitrary allocation of monies among the entities and to third parties, a case is clearly ripe for substantive consolidation. *See Murray Industries* at 829-830.

17. As established by the Eleventh Circuit Court of Appeals in *Eastgroup Properties*, bankruptcy courts, by virtue of their general equitable powers, have the power to order substantive consolidation of multiple debtors. *Eastgroup Properties* at 248. “Consolidation involves the pooling of the assets and liabilities of two or more related entities; the liabilities of the entities involved are then satisfied from the common pool of assets created by consolidation.” *Id.* “Substantively consolidating debtors’ claims simplifies the administration of interrelated bankruptcies by eliminating inter-company claims between related debtors and amalgamating duplicative claims ‘filed against related debtors by creditors uncertain as to where the liability should be allocated.’” *In re Pearlman*, 462 B.R. 849, 853 (Bankr. M.D. Fla. 2012).

18. The test for substantive consolidation requires a showing that “(1) there is substantial identity between the entities to be consolidated; and (2) consolidation is necessary to avoid some harm or to realize some benefit.” *Eastgroup Properties* at 249. “Once the proponent has made this prima facie case for consolidation, the burden shifts to an objecting creditor to show that (1) it has relied on the separate credit of one of the entities to be consolidated; and (2) it will be prejudiced by substantive consolidation.” *Id.*

19. The Eleventh Circuit suggested a number of factors that a proponent for consolidation could utilize to frame its argument, including the following factors outlined in *In re Vecco Construction Industries, Inc.*:

- a. The presence or absence of consolidated financial statements,
- b. The unity of interests and ownership between various corporate entities,
- c. The existence of parent and intercorporate guarantees on loans,
- d. The degree of difficulty in segregating and ascertaining individual assets and liabilities,

- e. The existence of transfers of assets without formal observance of corporate formalities,
- f. The commingling of assets and business functions, and
- g. The profitability of consolidation at a single physical location.

4 B.R. 407, 410 (Bankr. E.D. Va. 1980).

20. In discussing the *Vecco Construction* factors and others that might be presented in support of substantive consolidation, the Eleventh Circuit stressed that they were only examples and that “[n]o single factor is likely to be determinative in the court’s inquiry.” *Eastgroup Properties* at 250.

21. Utilizing these factors, the Eleventh Circuit in *Eastgroup Properties* determined that the Chapter 7 trustee had presented sufficient evidence to establish a prima facie case for consolidation of the two debtor entities, GPH and SMA. In evaluating whether consolidation was necessary to avoid some harm or to realize some benefit, the court noted certain factors that are also present here: that GPH had probably paid some of the unsecured obligations of SMA without being contractually obligated to do so, that consolidation would help see to it that GPH’s creditors would not be harmed by that action, and that GPH’s creditors would benefit “because a larger portion of each of their claims will be paid than if consolidation did not occur - both because their claims would be paid from the larger pool of assets resulting from consolidation and because substantive consolidation eliminates claims that either debtor has against the other.” *Id.* at 251.

22. Here, there is no denying the substantial identity between the Debtor and the Sub Con Entities and that consolidation is necessary both to avoid harm to individual entities and to realize a benefit to all. This conclusion is supported by many of the *Vecco Construction* factors:

- a. The financial records of the Debtor and each of the Sub Con Entities are in shambles and it would take significant time and money to unravel the finances at an individual level.
- b. The unity of ownership and interest between and among the Debtor and Sub Con Entities is clear – Peck operated and administered the Debtor, the Affiliated Debtors and each of the Non-Debtor Entities and their bank accounts.
- c. It would be extremely difficult as well as costly to the bankruptcy estates for the Trustee to segregate and ascertain the individual assets and liabilities of each Sub Con Entity.
- d. There were innumerable transfers of assets from various entities for the benefit of other entities without any observance of corporate or trust formalities.
- e. Indisputably, there was a continuous commingling of assets without a separate accounting for each entity, rendering it impossible to identify which funds belonged to which debtor and how those funds should be allocated to satisfy the claims by individual debtor.
- f. Substantive consolidation would avoid what would likely be substantial and costly litigation between and among the Debtor and the Sub Con Entities.

Chapter 7 Trustees May Seek and Obtain Substantive Consolidation

23. As did the Eleventh Circuit in *Eastgroup Properties*, bankruptcy courts in Florida, Georgia and elsewhere have recognized the ability of a chapter 7 trustee to seek and obtain

substantive consolidation. See *In re MMH Automotive Group, LLC*, 400 B.R. 885 (Bankr. S.D. Fla. 2008)(ordering substantive consolidation of separate chapter 7 estates); *In re Maxxis Group, Inc.*, 2009 WL 6527594 (Bankr. N.D.Ga. 2009)(authorizing substantive consolidation of chapter 7 debtor estates); *In re Creditors Service Corp.*, 195 B.R. 680 (Bankr. S.D. Ohio 1996)(approving substantive consolidation of chapter 7 debtor with non-debtor entities). Each of these cases had elements present here.

24. In *MMH Automotive*, the chapter 7 trustee sought, and the court approved, the substantive consolidation of three chapter 7 bankruptcy cases where, as here, there had been transfers of valuable assets from one entity to other debtor entities (both owned and controlled by the same person) for little or no consideration.

25. In *Maxxis Group*, factors in support of the trustee's successful effort to obtain substantive consolidation of five chapter 7 debtor cases also ring true here: the debtors' financial records were "in disarray and incomplete" and the debtors all operated out of one office "without a conventional accounting system." 2009 WL 6527594, * 2.

26. In *Creditors Service Corp.*, the court, at the conclusion of an adversary filed by the chapter 7 trustee, approved the substantive consolidation of a corporate chapter 7 debtor with several non-debtor entities, as well as the individual who owned and controlled all of the entities. Among the numerous factors considered by the court, were several that apply to the case at bar: the financial affairs of the entities and the individual were interdependent, there were numerous financial transactions between and among the individual, the debtor and the non-debtor entities, there were fraudulent transfers between and among the debtor and the non-debtor entities, and all operated out of the same building and shared the same computer system and phones.

This Court May Authorize the Substantive Consolidation of the Debtor with Non-debtor Entities

27. While the Trustee recognizes there is a split of authority as to whether a bankruptcy court has the authority to substantively consolidate non-debtors' assets and liabilities into a bankruptcy debtor's estate, it has been approved by bankruptcy courts in the Southern District of Florida and elsewhere, including the court in *In re S & G Financial Services of South Florida, Inc.*, 451 B.R. 573 (Bankr. S.D. Fla. 2011), whose analysis is particularly helpful.

28. In *S & G Financial*, the Chapter 7 trustee filed an adversary proceeding seeking to substantively consolidate the debtor with two non-debtor entities. The considerations in support of the trustee's arguments are similar to the factors present here, including the transfer of assets between the debtor and the non-debtors without observing corporate formalities, the comingling of assets and business functions between the debtor and the non-debtors, and the debtor and non-debtors having a sole common principal, owner and manager. As a result, the *S & G Financial* trustee argued that equity dictated their consolidation.

29. In rendering its decision, the *S & G Financial* court addressed the split among courts regarding substantive consolidation of debtor and non-debtor entities. It noted that, while the Ninth Circuit in *Bonham v. Compton (In re Bonham)*, 229 F.3d 750 (9th Cir. 2000) was the only federal circuit to hold that a court could order substantive consolidation of such entities, there was full support for that holding to be found in the Supreme Court's decision in *Sampsell v. Imperial Paper and Color, Corp.*, 313 U.S. 215 (1941), "[t]he seminal case on substantive consolidation." *Id.* at 580. In *Sampsell*, the Supreme Court held that a bankruptcy referee properly ruled that the property of a non-debtor corporation was property of the bankruptcy estate of its debtor principal shareholder, noting that "mere legal paraphernalia will not suffice to transform into a substantial adverse claimant a corporation whose affairs are so closely

assimilated to the affairs of the dominant stockholder that in substance it is little more than his corporate pocket.” *Id.*, quoting *Sampsell* at 218.

30. The *S & G Financial* court, referencing cases cited by the non-debtor defendants who argued against substantive consolidation in the underlying adversary proceeding, explained that the courts in those cited cases viewed “the application of the substantive consolidation remedy over non-debtors as an impermissible use of the court’s equitable power to take jurisdiction over a non-debtor without express statutory authority to do so.” The *S & G* court disagreed:

Conflating jurisdiction with power obscures the issue. The Eleventh Circuit, as well as many other circuit courts, has recognized that a bankruptcy court’s jurisdiction over non-debtors can be quite broad. In *Miller v. Kemira, Inc. (In re Lemco Gypsum, Inc.)*, 910 F.2d 784, 788 (11th Cir. 1990), the court held that the bankruptcy court has jurisdiction over any proceeding relating to bankruptcy if “the outcome of the proceeding could conceivably have an effect on the estate being administered in bankruptcy.” Moreover, “the proceeding need not necessarily be against the debtor or the debtor’s property.” *Id.* at 788.

Id. at 582-583.

31. The bankruptcy court correctly concluded:

[C]onsistent with the directive of *Sampsell*, **it is well within this Court’s equitable powers to allow substantive consolidation of entities under appropriate circumstances, whether or not all of those entities are debtors in bankruptcy.** Moreover, this Court holds that this Court has jurisdiction over non-debtor entities to determine the propriety of an action for substantive consolidation insofar as the outcome of such proceeding could have an impact on the bankruptcy case.

Id. at 582 (emphasis added).

32. In its opinion, the *S & G Financial* court emphasized the numerous other courts, including bankruptcy courts in Florida and Georgia, that had expressly recognized a bankruptcy court’s ability to substantively consolidate a debtor with a non-debtor entity, including *In re*

Alico Mining, Inc., 278 B.R. 586 (Bankr. M.D. Fla. 2002), *Munford, Inc. v. TOC Retail, Inc.*, (*In*

re Munford, Inc.), 115 B.R. 390 (Bankr. N.D. Ga. 1990), *Simon v. New Center Hospital (In re New Center Hospital)*, 187 B.R. 560 (E.D. Mich. 1995), *White v. Creditors Service Corp. (In re Creditors Service Corp.)*, 195 B.R. 680 (Bankr. S.D. Ohio 1996), and *Bracaglia v. Manzo (In re United Stairs Corp.)*, 176 B.R. 359 (Bankr. D.N.J. 1995).

33. In *Munford*, the debtor sought to substantively consolidate the estate's assets with those of two other non-debtor corporations. The bankruptcy court looked to *Sampsell* for a foundation, through the Supreme Court's affirmance of the bankruptcy referee's decision to bring the property of a non-debtor 'alter ego' corporation into the debtor's bankruptcy estate. In denying the non-debtor entities' motion to dismiss the debtor's complaint for substantive consolidation, the *Munford* court recognized that,

substantive consolidation may be based on a finding that it would be more equitable to all of the parties to allow consolidation under the circumstances of the case by showing that the affairs of the entities are inextricably intertwined or that creditors dealt with them as a single economic unit, and does not require a finding of fraud or intent to hinder, or delay creditors.

Id. at 394 (internal citations omitted). The *Munford* court further reasoned that substantive consolidation

must be predicated upon the estate's right to property in the hands of someone else. That right is created by Bankruptcy Code § 541, however, which provides that property of the estate includes all legal and equitable interests of the estate and § 542, which requires that all estate property must be turned over to the trustee. Substantive consolidation is essentially a complex turnover proceeding because the debtor is asking the nondebtor affiliated entity to bring into the estate assets in which the debtor asserts an unseparable interest. As long as the debtor can satisfy the pleading requirements of substantive consolidation . . . then the debtor has correctly invoked its legal rights under these Code sections.

Id. at 398.

34. In *Alico Mining*, the bankruptcy court, agreeing with *Munford*, recognized substantive consolidation as an alternative means to bring a non-debtor's assets into a debtor's

estate. 278 B.R. at 588-589. In support, it was argued by the creditor who filed the motion that both the debtor and non-debtor were controlled and dominated by the same individual and that individual determined what to do with the funds generated under an agreement for purchase of mining rights between the debtor and non-debtor. The bankruptcy court determined that it had the power to grant the requested relief under its general equitable powers.

35. Here, as with *S & G Financial* and the other cases cited above, equity demands substantive consolidation of the Non-debtor Entities with the Debtor and the Related Entities. The Non-debtor Entities are inextricably entwined in every aspect with the Debtor entities and there is no other rationale or equitable means to untangle the financial quagmire that faces the Trustee and this Court without bringing the Non-debtor Entities into the mix.

This Court Can Order Substantive Consolidation Subject to Specific Limitations and/or Preserving Particular Rights

36. The Trustee submits that substantive consolidation in this case would be ineffective unless the Court's order approving substantive consolidation also preserved the Trustee's avoidance powers as well as causes of action against third parties on behalf of individual debtors or subgroups of the Sub Con Entities. Among the Trustee's targeted sources of recovery for the bankruptcy estates are purchasers of several of the policies sold by Ms. Peck in the few months prior to the bankruptcy. There are other litigation targets as well. Preserving the Trustee's ability to pursue these litigation claims on behalf of particular debtor entities would provide substantial benefit to the Debtor and all the Sub Con Entities.

37. This Court has the authority to order substantive consolidation of the Debtor and Sub Con Entities subject to certain limitations, conditions and/or the preservation of particular rights. For example, in *In re Giller*, 962 F.2d 796 (8th Cir. 1992), the Eighth Circuit affirmed the bankruptcy court's ruling ordering the substantive consolidation of an individual debtor with six

corporations in which he was the sole or majority shareholder, but specifically preserving the trustee's avoidance powers as to any transfers made by any of the debtors to third parties for the benefit of other debtors. In that case, the individual had abused corporate form and caused the corporations to make transfers that could be subject to fraudulent transfer litigation. Only one of the corporate entities had any assets, and those assets were needed to fund the litigation. As explained by the Eighth Circuit:

We recognize that substantive consolidation normally would eliminate the justification for the exercise of the trustee's avoidance power. Nonetheless, the bankruptcy court retains the power to order less than complete consolidation. Here, eliminating the trustee's avoidance power after consolidation would also eliminate the very reason for ordering consolidation in the first place, that is, to obtain the funds required to recover transferred assets.

Geller at 799.

38. Similarly, the Ninth Circuit in *Bonham*, a Ponzi scheme case, affirmed the bankruptcy court's substantive consolidation of the debtor's estate with two non-debtor corporations, while specifically preserving the trustee's avoidance powers. "Absent express preservation of the trustee's avoidance power, an order of substantive consolidation would ordinarily eliminate that power." *Bonham* at 768. The Ninth Circuit recognized that "the bankruptcy court has the power, in appropriate circumstances, to order less than complete substantive consolidation, or to place conditions on the substantive consolidation, including the preservation of avoidance claims by the formerly separate estates." *Bonham* at 769 (internal quotations and citations omitted). *See also Creditors Service Corp.* (approving chapter 7 trustee's request for substantive consolidation of chapter 7 debtor with an individual and non-debtor entities subject to numerous special limitations and requirements); and *In re Deltacorp, Inc.*, 179 B.R. 773, 777 (Bankr. S.D.N.Y. 1995) (recognizing noting that the court was "afforded a good deal of discretion in constructing its order of substantive consolidation" and retained "the power

to order a less than complete consolidation, preserving avoidance claims by the formerly separate entities.)

39. In the case at bar, preserving the Trustee's right to bring claims and/or causes of action held by individual debtors or funds, or subgroups of same, might well lead to recoveries that would benefit all entities and help equalize the glaring inequities created by Deborah Peck's indiscriminate usage of monies comingled in trust accounts.

40. Moreover, no creditors can prove prejudice should this Court grant the relief sought herein: while creditors may attest that they relied on the individual credit of the Debtor or one of the Sub Con Entities, what they actually relied on were the representations of Peck and others, which did not legitimately reflect the credit (if any) of individual entities. Based on Peck's testimony, all funds were combined in the same accounts with monies being paid out without regard to the source of the funds. Hence, while creditors may have assumed a certain value was attributed to certain individual affiliated entities, that perceived value was, in fact, illusory.

41. Furthermore, no creditors can validly attest that they will be prejudiced by substantive consolidation. The only viable means to address the creditors of the Debtor and the Affiliated Debtors is through substantive consolidation. The only prejudice to creditors here would be to deny that relief.

Conclusion

Based on the foregoing, the Trustee submits that the Court, under its equitable powers, has the authority to substantively consolidate the Debtor with the Sub Con Entities while preserving the Trustee's avoidance powers and right to pursue claims and/or litigation against third parties on behalf of individual Sub Con Entities or subgroups.

WHEREFORE, the Trustee respectfully requests that this Court enter an order: (i) substantively consolidated the bankruptcy estates of the Debtor and the Sub Con Entities, (ii) preserving the Trustee's avoidance powers and right to pursue claims and/or litigation against third parties on behalf of individual Sub Con Entities or subgroups, and (iii) granting such other and further relief as the Court deems just and proper.

I HEREBY CERTIFY that a true and correct copy of the foregoing was served on this 23rd day of July, 2013, via electronic transmission through the Court's CM/ECF system upon all parties on the attached CM/ECF Service List, and via first class, U.S. Mail upon all creditors and interested parties on the attached Service List, to the extent that such parties were not already served electronically through the Court's CM/ECF system.

Respectfully submitted,

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