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UNITED STATES DISTRICT COURT  
DISTRICT OF OREGON

SECURITIES AND EXCHANGE  
COMMISSION,

Plaintiff,

vs.

SUNWEST MANAGEMENT, INC., CANYON  
CREEK DEVELOPMENT, INC., CANYON  
CREEK FINANCIAL, LLC, and JON M.  
HARDER,

Defendants,

Case No. 09-CV-6056-

DECLARATION OF RECEIVER MICHAEL  
GRASSMUECK IN SUPPORT OF  
DISTRIBUTION PLAN OF RECEIVER AND  
CHIEF RESTRUCTURING OFFICER FOR  
SUNWEST ENTERPRISE

DARRYL E. FISHER, J. WALLACE  
GUTZLER, KRISTIN HARDER, ENCORE  
INDEMNITY MANAGEMENT, LLC,  
SENET LEASING COMPANY, FUSE  
ADVERTISING, INC. KDA CONSTRUCTION,  
INC., CLYDE HAMSTREET, and CLYDE A.  
HAMSTREET & ASSOCIATES, LLC,

Relief Defendants.

I, Michael A. Grassmueck, declare:

1. I am the Court-appointed federal equity receiver ("Receiver") for Sunwest Management, Inc. ("SMI") and certain subsidiaries, affiliates and entities controlled by them, as defined and identified in the orders appointing me. I submit this declaration in support of the Distribution Plan ("Distribution Plan") that I have proposed jointly with the Chief Restructuring Officer, Clyde Hamstreet ("CRO") and submitted concurrently herewith. The Distribution Plan, if approved by the Court, would establish how claims against the Receivership Estate are calculated for purposes of establishing Allowed Claims, how Allowed Claims are treated with regard to priority and source of Plan Distributions, and what the sources of Plan Distributions will be and how they will be created. (Capitalized terms not defined herein shall have the meaning set forth in the Distribution Plan.)

2. I have personal knowledge of the facts stated in this declaration and could and would competently testify thereto if called upon to do so. My knowledge is based upon my personal review of documents obtained from the Receivership Entities and other sources; my interviews of and discussions with officers, employees and third parties associated with the Receivership Entities; my work and the work of my staff and professionals in carrying out the duties and obligations of the Receiver under the orders appointing me; and my involvement in the mediation sessions and discussions that have led to the proposed Distribution Plan. My knowledge and views of the Distribution Plan are also informed by my 25 years of experience serving as a trustee in bankruptcy and as a receiver. I am a Certified Insolvency Restructuring Advisor. I have been a federal equity receiver in many securities-related cases and have created and implemented distribution plans in a variety of cases and circumstances.

**Appointment of the Receiver**

3. On March 2, 2009, the Securities and Exchange Commission (the "SEC") filed its Complaint in this action ("Action") naming Sunwest Management, Inc., Canyon Creek Development, Inc., Canyon Creek Financial, LLC and Jon M. Harder ("Harder") as defendants and Darryl E. Fisher ("Fisher"), J. Wallace Gutzler ("Gutzler"), Kristin Harder, Encore

Indemnity Management, LLC, Senenet Leasing Company, Fuse Advertising, Inc., KDA Construction, Inc., Clyde Hamstreet, and Clyde A. Hamstreet & Associates, LLC as relief defendants. The SEC's Complaint alleged violations of federal securities laws. In summary, the Complaint alleged securities fraud in the offering of various investments in Receivership entities and that the parties in control of the Sunwest enterprise operated it virtually as a "Ponzi" scheme. In conjunction with the Action, the SEC requested injunctive relief and the appointment of a receiver.

4. The Court entered its Order Granting Preliminary Injunction and Appointing Receiver on March 10, 2009, appointing me as receiver over SMI and other entities identified in Exhibit A to that order. The Court subsequently appointed me as receiver over additional entities pursuant to the Unopposed Order Granting Additional Preliminary Injunction and Appointing Receiver for Additional Entities entered by the Court on May 27, 2009. The Commission currently has pending with the Court an application for Further Order Granting Additional Preliminary Injunction and Appointing Receiver for Further Entities. (The May 27, 2009 order and the pending order, together with the March 10 order, are referred to as the "Receiver Orders").

5. The Receiver Orders provide the Receiver with various rights, powers, and duties with respect to the Receivership estate. Those rights, powers and duties are more circumscribed than those often granted to a federal equity receiver, and the Receiver Orders give authority over certain matters to others, such as the CRO and Management Committee. My responsibilities and activities as Receiver in this case generally fall into four categories:

- (i) investigation of the financial condition of the Receivership Entities, the disposition of investor funds and determining the extent of commingling of funds among the Defendants, Relief Defendants and Receivership Entities;
- (ii) pursuing and resolving claims against third parties so that the proceeds will be available to satisfy investors' and creditors' claims;

(iii) advising the Management Committee and CRO as to issues concerning the bankruptcies, secured creditors, disposition of assets and restructuring and distribution; and

(iv) developing a plan for distribution of proceeds to creditors and investors.

6. In order to carry out these responsibilities, I have retained professionals to assist me including legal counsel and forensic accountants. The retained forensic accountants are the firm Financial Forensics lead by Greg Gadawski and Darrell Dorrell.

7. Upon entry of the March 10 Order, consistent with my duties as Receiver, we began researching and investigating the financial condition and operations of the Receivership entities. Our immediate focus was to determine the extent to which funds of the Defendants, Relief Defendants and Receivership entities were commingled, and the impact this commingling may have on the claims of investors and creditors. Pursuant to the Order, the Receiver was charged with completing a preliminary analysis of the Receivership entities' financial position, operations, cash flows, accounting records and cash controls. My preliminary work and findings are set forth in my First Interim Report of Receiver filed with this Court.

8. Since my First Interim Report, I have continued to carry out the duties assigned to me under the Receiver Orders. My efforts have included further investigation. Through the early analyses and meetings, it was determined that a significant forensic accounting investigation would need to be undertaken to determine the amount and source of investments, lending and borrowing between entities and Defendants and the effect on the entities. Financial Forensics undertook substantial effort to conduct a further independent forensic accounting investigation and analysis, although the Court suspended that work before a report could be issued.

9. As part of my responsibilities under the Receiver Orders, I have also worked with the CRO and Management Committee to establish procedures for disposition of certain assets of the Receivership Estate for properties identified as those to be divested. I have also participated in mediations and negotiations with secured creditors who hold liens on various properties. My team has also been communicating with regulators and addressing insurance issues regarding the

Receivership Entities. Substantial work has been done to devise an appropriate and comprehensive claims process. As set forth below, we have also been evaluating and pursuing third party claims. I, as Receiver, have also worked with the CRO and the Management Committee to establish an interim strategy to help mitigate the adverse tax consequences to TIC investors from the foreclosures by secured lenders. My work in each of these areas has informed my views of the appropriate distribution plan and restructuring options. We have also been working with the CRO and representatives of various stakeholders on a distribution plan and plan for restructuring.

10. My work includes developing a distribution plan for administering assets and claims related to the Receivership Estate. We have provided substantial input on the development of a plan for restructuring the Sunwest Enterprise that is intended to maximize the value of the business and, it is hoped, provide a substantial return to investors. Formulation of the proposed Distribution Plan has involved many days of Mediation among various parties in interest.

### **Pre-Receivership Events**

11. To understand some of the structural issues that have plagued the Sunwest Enterprise and impact the design of any restructuring and distribution plan, a brief description of the events which occurred during the 12 months immediately prior to the appointment of the Receiver is important. My investigation of the Sunwest Enterprise revealed the following:

- At the time of the filing of the SEC's Action, SMI was managing approximately 183 assisted living facilities, 85 non-assisted living facilities and other investments (collectively, the "Facilities"). The Receivership Entities consist of the entities listed on Exhibit A, Exhibit A-2 and proposed Exhibit A-3 to the Receiver Orders and additional entities that are owned or controlled by the Defendants. The Sunwest Enterprise primarily involved the management of individual Facilities by Sunwest (or, in a few cases, third-party management companies); the management of other real and personal property interests and entities which are encompassed by the Receiver

Orders; the Facilities; and the equity and membership interests in the Receivership Entities (collectively, hereinafter the "Sunwest Enterprise").

- Sunwest and many of the Facilities faced critical cash flow problems arising from the overleveraging of properties, lower than industry standard occupancy, and disruption in the capital markets. This has caused Sunwest to be in turmoil for the past year and, based on the review to date, it appears that the allegations of wrongful conduct described by the SEC are supported by substantial evidence and played a significant role in the losses suffered by the Sunwest Enterprise.
- In or around the spring of 2008, Sunwest was allegedly in default on loans and/or pools of loan with certain of its primary lenders (General Electric and Merrill Lynch). In response to this situation, General Electric required that Sunwest engage a restructuring expert, apparently in order to provide the lender with comfort that the loan default and other issues were being addressed in a professional fashion. The Alvarez & Marsal firm was engaged by SMI for this purpose.
- During the spring and summer of 2008, Alvarez & Marsal analyzed the operations and identified what it believed were possible remedies for certain problems and made proposals to management to sell specific assets in order to generate cash for operations and possible restructuring. Mr. Harder and possibly others at Sunwest did not agree to those proposals. The failure to promptly address what appeared to be severe cash flow and debt issues ran straight into the disruption of the credit markets in the fall of 2008.
- From accounting records and interviews, it is evident that by the fall of 2008, finances of the Sunwest Enterprise were in turmoil and rapidly deteriorating. Among other things, loans were maturing or in default as the Sunwest Enterprise scrambled to generate sufficient cash to both operate and forestall foreclosure actions by the lenders.

- In the midst of this turmoil and in a further effort to stave off and satisfy secured and unsecured lenders and Investors, in October 2008, Hamstreet and Associates was engaged and Clyde Hamstreet was installed as the CRO.
- Thereafter, Mr. Harder filed an individual, voluntary petition for bankruptcy on December 31, 2008, Case No. 08-37225-tmbll.
- Concurrently with these events, in an effort to avoid catastrophic foreclosures and generate much needed cash for operations, the Sunwest Enterprise pursued what became known as the Lone Star Transaction. The Lone Star Transaction involved the sale of 45 Facilities for the sum of \$364.2 million, most of which went to pay off a loan with General Electric. This sale closed in January 2009. \$82.7 million of net revenue was generated after payment of the secured debt.
- As of December 2008 and January 2009, Sunwest faced numerous foreclosure actions which were impacting valuable assets. As of January 2009, there were at least 45 foreclosure actions pending in which rents and profits receivers had been appointed to take control of the Facilities.

12. The SEC then filed this action on March 2, 2009, leading to an injunction and my appointment as Receiver.

**Commingling of Funds and Operations of the Sunwest Enterprise as a Unitary Enterprise.**

13. My investigation to the date of my First Interim Report revealed that the commingling of funds within the Sunwest Enterprise was rampant. Financial Forensics undertook substantial forensic accounting investigation following my First Interim Report. Although not completed, the work confirmed the tentative conclusions reported in the Receiver's First Interim Report that commingling among the Receivership Entities was extensive. Also, I found evidence of substantial commingling among some Receivership Entities and certain of the Defendants and Relief Defendants.

14. Based on my investigation, I have learned the following:

- The Receivership Entities were organized as discrete legal entities, but historically operated as one enterprise, and utilized cash investments and/or cash from operations in a significantly commingled manner without regard to the proper legal rights of purportedly separate entities to such funds. As a result, payments to certain Investors or to benefit certain facilities were made from funds that should have been limited to benefit other Investors or facilities.
- The Sunwest Enterprise regularly acquired distressed facilities and utilized cash from other sources to pay operating expenses, mortgages and lease payments. Furthermore, it does not appear that it was merely profitable Facilities propping up those with negative cash flow. The Receiver has received information and reviewed evidence that loans and other funds transfers were also made from distressed Facilities to those that are now profitable Facilities. Sunwest's records reflect a variety of descriptions for transfers into and out of Receivership entity accounts and into and out of Defendant Harder's account.
- The opportunistic flow of funds appears to be consistent with the alleged "all in" cash policy that has been implemented over the past few years. Sunwest management would draw cash from any available source to satisfy cash shortfalls for certain Facilities. While some thought was given to the source of funds, the ultimate decision was based on mere availability. At some point in time, we are informed that it became Sunwest's practice to merely review all account balances in the morning for overdraft positions, and then find ways to transfer monies from other accounts to cover those cash shortfalls before the banks deemed the account to be in overdraft. By mid to late 2008, funds were being utilized and paid on almost a pure "availability" and "cash flow needs basis," without regard to the source or intended or required use of the funds, and without the knowledge or consent of affected investors and creditors.

- At the time of appointment of the CRO, many of the facilities did not have sufficient cash flow to cover operating expenses and/or mortgage payments. As such, the CRO continued the practice of inter-facility "borrowing" or transfers until the closing of the Lone Star transaction. That practice has not continued post-receivership.

15. In my opinion, the extent and manner of commingling renders it excessively expensive and impracticable to trace the ultimate source and use of the funds. In order to treat the investors and creditors fairly, as well as to serve the public purpose of establishing an orderly mechanism to administer the assets of the Receivership Estate and implement an equitable mechanism to reduce the losses experienced by investors and creditors, I believe that the Distribution Plan needs to be premised on a unitary enterprise finding and the claims of investors and creditors need to be determined and allowed on an equitable basis using a modified Money-In less Money-Out approach, as set forth in the Distribution Plan.

16. I have been kept informed by the SEC, my counsel, and Harder's counsel (through my own counsel) concerning a settlement to be implemented between the SEC and Harder. In connection therewith, I have been made aware of the settlement terms, which provide, in part, for a public proceeding at which the SEC will present certain evidence that Harder has agreed to not dispute. In particular, Harder will not dispute that on certain occasions when Harder met personally with a potential investor, he encouraged the investor to purchase a TIC interest in a particular Facility, and during such conversations, Harder, at times, represented that the potential TIC investment was limited to only the risks and benefits of an investment in only that particular Facility. Furthermore, Harder will not dispute that at times, Harder directed money transfers to be made from cash flow positive Facilities to negative cash flow Facilities and from negative cash flow Facilities to cash flow positive Facilities to ensure the facilities could meet financial obligations to residents, investors, and creditors. And, Harder will not dispute that in conversations with some potential investors, Harder at times omitted material facts necessary to avoid misleading these potential investors into believing that their investment was limited to only that particular facility, and that as a result of the money transfers between facilities, the TIC

investments were not always limited to a particular facility, and were at times intertwined with other facilities also managed by SMI.

### **FORMULATION OF THE DISTRIBUTION PLAN<sup>1</sup>**

17. The purpose of the proposed Distribution Plan is to administer the assets of the Receivership Estate. The Receiver's focus has been to have a Distribution Plan that is equitable, is in the best interest of the Receivership Estate, and provides an efficient and practicable approach to administering the assets. Part of the Distribution Plan complements and relies upon implementation of a proposed reorganization plan. The Distribution Plan also encompasses a claims review process, which is the subject of a separate motion. The Distribution Plan has been the subject of multiple mediation sessions with the Receiver, CRO and various parties in interest.

18. In fulfilling my duties of formulating and proposing a distribution plan, I have worked closely with, among others, my counsel and accountants; the CRO and his professionals, including Alvarez & Marsal, counsel and special tax counsel; and the Management Committee and its constituent Unsecured Creditors' Committee and TIC Committee. I have also participated in continuing consultations with various parties in interest and many days of Mediation with respect to plan structure and terms.

19. Based on these consultations, the CRO and I early on realized that liquidation of the Sunwest Enterprise likely would provide very little recovery to investors and unsecured creditors. The projections from Alvarez & Marsal, which I find persuasive, estimate a recovery of 3% to 13% resulting from an orderly liquidation. Consequently, our focus turned to developing a structure for preserving the going concern value of the Sunwest Enterprise.

20. The first option considered was the "status quo" option, which would involve continuing with the asset disposition process to shed Facilities and properties that were burdensome to the Sunwest Enterprise, and moving forward with the profitable facilities and

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<sup>1</sup> The description of the Distribution Plan herein is for purposes of reference or illustration only, and shall not be deemed or construed in any way to amend, modify, or otherwise alter the Distribution Plan in any way. In the event of any discrepancy between the Distribution Plan and the descriptions of the Distribution Plan herein, the Distribution Plan shall control.

assets in which the Sunwest Enterprise enjoyed some equity. Implementation of this option was already underway, but that was its only clear advantage. The clear disadvantage was that investors and creditors related to unprofitable Facilities and properties likely would receive little or no distributions (perhaps only distributions funded by Avoidance Action, Disgorgement and Third Party Claim recovery), while investors and creditors related to profitable Facilities and properties would receive large distributions or possibly payment in full plus profit. Within the context of the unitary operations of the Sunwest Enterprise, such unbalanced distributions to investors and creditors would not be fair nor equitable.

21. Another option would be to substantively consolidate the Sunwest Enterprise as a single corporate entity, with securities issued to Claimants so that they could participate in realization of the going concern value. The advantage to this option would be that it is consistent with the actual operation of the Sunwest Enterprise and would allow for pro rata distribution among investors and unsecured creditors. The main disadvantage to this approach would be that the TIC Investors, who comprise the majority of the investors victimized in this case, likely would suffer adverse tax consequences as a result of such a consolidation. Many of the TIC Investors made their investments through 1031 exchanges. To the extent that consolidation would be construed as a transfer of their property interest for income tax purposes, consolidation would impair their 1031 status. Moreover, secured Creditors would object to the plan because of the violence it would do to their single purpose borrower structure.

22. To resolve these competing concerns, the proposed Distribution Plan was developed based on an equitable consolidation of the Sunwest Enterprise, confirmation of a chapter 11 reorganization plan, and creation of a REIT/MLP structure. This structure has the advantages of realizing the going concern value of the Sunwest Enterprise for the benefit of investors and creditors, the ability to make pro rata distributions of that value through issuance of securities, offers the potential for certain tax benefits for the TIC Investors, and will preserve the borrower –Secured Creditor structure except only as modified through a consensual or cramdown restructuring in the chapter 11 case. The one relative disadvantage is the

administrative burden of the additional chapter 11 process, but it is important that the Sunwest Enterprise have the opportunity to restructure certain secured loans and to issue new securities under the provisions of the Bankruptcy Code. For all of these reasons, the CRO and I support and jointly propose the Distribution Plan as the most fair, equitable, and feasible means to distribute the highest value to investors and creditors of the Sunwest Enterprise.

23. The components of the Distribution Plan include:

- The classification and treatment of claims;
- Identification of a claims process for receiving, verifying and processing claims for all claimants;
- The type and means of distributions to be made under the Distribution Plan;
- Certain exceptions to inclusion in the Distribution Plan;
- Implementation of the Distribution Plan through the parallel tasks of restructuring of the Sunwest Enterprise and the liquidation of claims, assets and the pursuit of Third Party Claims; and,
- Retention of jurisdiction by the Court for certain purposes including summary procedures for adjudicating certain matters.

24. The proposed Distribution Plan acknowledges that the Sunwest Enterprise failed to observe proper and customary legal distinctions among the various Receivership Entities. The Sunwest Enterprise effectively eliminated nominal legal boundaries among the various Receivership Entities such that they were operated as a unitary enterprise. As the Receiver, in consultation with the CRO and others in this case, I believe that the most fair and equitable method of distributing the existing value of the Sunwest Enterprise to claimants holding "Allowed Claims" is to recognize the Sunwest Enterprise as a unitary enterprise and distribute such value to investors and unsecured creditors on a *pari passu* basis with pro rata distributions. Recognition and reorganization of the Sunwest Enterprise as a unitary enterprise will allow for this most equitable means of distribution and the greatest opportunity to maximize the value of the enterprise. Accordingly, subject to certain exceptions, the proposed Distribution Plan calls

for the Receivership Entities to be judicially recognized as a unitary enterprise that can be reorganized as a single enterprise in a subsequent single bankruptcy case involving one Reorganization Plan. Notably, legal title to properties will continue to be held by the relevant Receivership Entities. The ownership of the Receivership Entities (and, therefore, the *indirect* ownership of certain Properties) may be restructured through the Reorganization Plan.

25. Through the Distribution Plan and the follow-on Reorganization Plan, a unitary enterprise will be recognized and reorganized to become REITCO with an affiliated Master Limited Partnership known as SWP Holdings, L.P. ("SWP"), for which REITCO will serve as the general partner. Cash and securities will be distributed to Claimants holding Allowed Claims. The cash will be generated from the operations of properties affiliated with REITCO and SWP, the sale of certain properties, and the recoveries/settlements on Third Party Claims. Securities will be issued as REITCO shares and SWP units. Interests of the Receivership Entities and any co-owners in "Holdco Properties" will be sold or conveyed to REITCO or SWP in exchange for securities as determined by the Receiver. REITCO will be a public reporting company. I anticipate that REITCO eventually may have an initial public offering that will enable its shares to be traded on an exchange. Alternatively, and perhaps more likely, the value of the Reorganized Company (including REITCO) will be realized through a sale or a merger of REITCO with a third party entity. The goal is to accomplish the sale, merger, or initial public offering within seven years of the effective date of the Reorganization Plan.

26. For purposes of the Distribution Plan and the Reorganization Plan, all claims and all assets, with certain exceptions, will be equitably consolidated. Claims against any Receivership Entity, employees of a Receivership Entity arising from the employee's course and scope of work, claims against assets and Sunwest-related claims against the HFG Parties will be treated and resolved pursuant to the Distribution Plan. Claims of Secured Creditors will remain against the relevant Receivership Entity borrower and will remain as liens and security interests in their respective collateral, subject to treatment through the Reorganization Plan. On the asset side, all assets owned, co-owned or in the control or possession of any Receivership Entity and

any Sunwest-affiliated assets owned or co-owned by the HFG Parties, as well as any recovery on Third Party Claims, will be utilized to create Plan Distributions for Allowed Claims.

### **Claims**

27. Claims will be classified into different types, which will then determine their source of payment. Claim types include:

- administrative claims (including the fees and expenses of professionals employed by the Receiver, CRO and certain others, subject to approval by the Court; and certain approved interim operating expenses and advances);
- investor claims (including TIC investors, preferred membership investors, LLC members and non-institutional unsecured noteholders);
- unsecured creditor claims (including trade and employee claims of the Receivership Entities, lender deficiency claims, creditors of Harder, Fisher and Gutzler, and unsecured non-contractual creditor claims);
- secured creditor claims (including real estate lenders, personal property lenders, secured creditors against the assets of Harder, Fisher and Gutzler, and secured non-contractual creditors); and
- claims by the HFG Parties.

28. The Distribution Plan establishes a methodology for evaluating the claims of each class of claim. In general, Plan Distributions to Investors and certain unsecured creditor claims will be determined on a "MIMO" basis, meaning "Money In, Money Out." Preferred membership and LLC investors will have a one-time opportunity to elect to retain their interests in lieu of having an Allowed Claim, and TIC Investors will be given the option to retain bare legal title, subject to certain conditions including a new and superseding master tenant lease. These elections are to be made concurrently with the submission of Proofs of Claim.

29. For *pro rata* Plan Distribution purposes, Claims of employees' and trade creditors' claims will be calculated as the principal amount owed under a contract or judgment as of March 2, 2009.

30. As to Secured Creditors, the Distribution Plan does not alter, amend, modify or otherwise affect the terms of the loan documents between a Secured Creditor and a Receivership Entity, other than certain changes in ownership or control of the Receivership Entity. Secured Creditors will retain their liens with respect to their existing collateral. Loan restructuring and loan cram downs, if necessary, with respect to Holdco and Trustco Properties will be accomplished through the Reorganization Plan. The injunction against Secured Creditors' enforcement of rights and remedies under the Receiver Orders will, upon approval of this Disposition Plan, be deemed coterminous with an automatic stay in the follow on reorganization case.

31. Finally, claims by the HFG Parties have been resolved pursuant to a settlement reached through court ordered mediation, subject to Court approval of the settlement and other terms and conditions.

32. I have worked with parties in interest in the case to establish a claims procedure. Numerous potentially-affected classes of claimants have been identified and a comprehensive mailing matrix for all known potential claimants is being compiled. I anticipate noticing tens of thousands of potentially-affected parties. A comprehensive Proof of Claim form has been design to facilitate submission of Claims. I continue to seek input from all parties to ensure that the information received through the claims process allows the Receiver to evaluate and audit all claims fairly and accurately. I will be filing a motion to approve claim procedures, establish a bar date, approve the claim form and other matters related to the claims process. My intent is to make the claims process as efficient and transparent as possible so that claimants can understand how their claims will be classified and consequently what Distribution Plan treatment they are entitled to and what Plan Distributions they could reasonably expect. Processing claims is necessary in order for me as Receiver to determine the maximum amount of claims that will be entitled to Plan Distributions of cash and securities. Determinations of Allowed Claims will be subject to Court review and approval and claimants will be afforded the opportunity to review and object to their proposed allowed claim amounts.

## Distributions.

33. The Distribution Plan addresses how distributions will be made. First, no distributions will be made on an Allowed Claim where the holder of the allowed claim is liable for Disgorgement of Ill-Gotten Gains, an Avoidance Action or other Third-Party Claims until such liability is paid in full to the Receiver. This is equitable and promotes efficient administration of the Receivership Estate, since it does not require that I take affirmative recovery action against such parties to prevent them from receiving valuable Plan Distributions.

34. The second major feature is that within a class, distributions generally will be made *pari passu* and *pro rata*.

35. Distributions of cash (generated from any net income from asset sales and Third Party Claims) will be made from time to time, subject to the Receiver's discretion, when material amounts are available and as far as reasonably practical. The Receiver also will establish certain reserves for contingencies including disputed claim amounts and administrative claims and operating costs.

36. Securities will also be distributed to certain Claimants holding Allowed Claims. Those securities will be an interest in REITCO or SWP. Those securities are described in more detail in the Reorganization Plan pursuant to which they will be issued.

37. Appreciation of value associated with the Trustco Properties will also be shared *pro rata* by *Pari Passu* Distributions to Investors and Unsecured Creditors.

38. Based on the operation of the Sunwest Enterprise as a unitary enterprise, and the fact that most Investors are similarly situated with respect to their relationship to the Sunwest Enterprise, I believe that *pro rata* sharing of value and *pari passu* distributions are the most fair and equitable means of distribution.

### Distribution Plan Exceptions

39. The Plan also provides for certain Distribution Plan exceptions that allow for certain investors to retain their interests in real property under the terms of the Plan. These exceptions have been developed through Mediation and other discussions with interested parties.

Based on the conditions set forth in the Distribution Plan, I believe that the exceptions are fair and equitable because such conditions would establish that Investors subject to the exceptions may not be similarly situated to other Investors and because the exceptions require that the Receivership Estate's interest in such properties be resolved for the exceptions to apply.

### **Effectuation of the Plan**

40. Implementation of the Distribution Plan will take place on two parallel tracks: (i) the Restructuring of the Sunwest Enterprise; and (ii) liquidation of claims and certain assets of the Receivership Estate and the pursuit of Third Party Claims.

#### **Restructuring**

41. The Restructuring will be a three-step process. The first step is approval of the Distribution Plan which recognizes the unitary enterprise and the equitable consolidation of Claims and Assets, the Claims Allowance Methodology and the sources and priorities for distribution of Plan Distributions. The second step is the confirmation of the chapter 11 Reorganization Plan that creates REITCO as a REIT with SWP as the affiliated MLP, and creates REITCO shares and warrants and SWP MLP interests for the Receiver to distribute as Plan Distributions consistent with the Distribution Plan. The third step is the employment by REITCO and SWP of new professional management to increase value, leading to an eventual sale, merger or public offering resulting in a final Plan Distribution, closing of the Receivership case and discharge of the Receiver.

#### **Pursuit of Third Party Claims**

42. The potential assets of the Receivership Estate include certain claims against third parties. I believe there are numerous and potentially valuable Third Party Claims. These include potential claims against third parties brokers, lenders and the professionals for the various Receivership Entities including attorneys and accountants. My initial focus has been on third party claims for negligence, malpractice and securities violations by professionals representing the Receivership Entities. As Receiver, I hold and control all third parties' claims that any Receivership Entity has, but without any *in pari delecto* defenses being applicable.

43. As Receiver, to date I have initiated legal actions against the law firms Davis Wright Tremaine ("DWT"); K&L Gates; and Thompson & Knight. These firms acted as attorneys for Receivership Entity securities offerings. We have also initiated an action against Grove Miller & Swank, an accounting firm that provided services to the Receivership Entities. Each of these actions has been filed in this District Court. As these claims are being pursued through litigation, it is not possible at this time to state with accuracy when such litigation might be resolved or the potential recoveries in such litigation. It does appear that each of the professional firms against whom an action has been brought to date carries some level of professional malpractice insurance. Mediation has been scheduled with DWT for Autumn 2009.

44. I am in the process of investigating and analyzing additional potential claims against brokers, lenders, and others who performed services for the Receivership Entities in connection with the securities offerings or otherwise received ill-gotten gain that should be disgorged.

45. Those pursued for recoveries are highly likely to vigorously oppose the claims. There is the prospect for some insurance coverage for certain claims, but such insurance is not likely to be sufficient to cover all the claimed damages, and insured amounts are likely to be reduced by litigation costs. Litigation could be slow and expensive, although mediation has started on some of the claims and we are cautiously optimistic about reaching some settlements. In light of all this, I estimate that the range of recoveries on Third Party Claims could be from approximately \$50 million to several times that amount, although no holder of an Allowed Claim should rely on Plan Distributions in that amount or in any amount.

46. Third Party Claims, to the extent not resolved earlier, and Avoidance Actions would be assigned to a litigation trust for which I, as the Receiver, would serve as the sole trustee. As Third Party Claims and Avoidance Actions are pursued, and as recoveries or settlements occur, proceeds would be distributed from the litigation trust as Cash Plan Distributions.

47. Proceeds from Disgorgement of Ill Gotten Gains and Avoidance Actions will be shared *pro rata* by *Pari Passu* Plan Distributions to all Investors and Unsecured Creditors. Recoveries premised on injuries to investors, such as securities fraud, fraud in the inducement or other non-derivative claims, will be shared *pro rata* by *Pari Passu* Plan Distributions only to Investors in the Receivership Entities or investors with the HFG parties. In the case of mixed recoveries, the adjudicating court or mediator will be asked to apportion the recovery among the relevant types of third party claims so that distributions can be made consistent therewith.

#### **Liquidation of Divestco and Trustco Properties**

48. Divestco Properties will be released from the injunction established by the Receiver Orders as soon as practicable after Court approval of the Distribution Plan.

49. Trustco Properties will be sold as the markets recover and the net proceeds of such sales will be distributed as cash Plan Distributions.

50. Such liquidation is in the best interest of the Receivership Estate because the Divestco Properties generally are burdensome to the Estate and because Trustco Properties generally do not currently generate net income for the benefit of the Receivership Estate.

#### **Retention of Jurisdiction**

51. The Distribution Plan also calls for the Court to retain and have exclusive jurisdiction of matters arising out of the Receivership Action and the Distribution Plan. This would include jurisdiction for, among other things, the summary procedures proposed in our Claims Process and for the pursuit of Disgorgement of Ill Gotten Gains and Third Party Claims where suitable. I believe that it is necessary and appropriate for this Court to retain such jurisdiction in order to efficiently administer the Receivership Estate.

#### **The Proposed Distribution Plan is in the Best Interest of the Receivership Estate**

52. Based on my review and understanding of the Sunwest Enterprise and the nature of claims of Investors, unsecured creditors, and secured creditors, I believe the Proposed Distribution Plan represents the most fair and equitable approach to resolving such claims and making distributions to Claimants. Moreover, I believe that the Distribution Plan is the most

efficient and practicable approach to administering the assets of the Receivership Estate. I believe that the administration and distribution of the receivership assets as set forth in the Distribution Plan is in the best interest of the Receivership Estate.

53. Many of the material terms of the Distribution Plan including, without limitation, the HFG Settlement, have been negotiated through Mediation and with the encouragement of a Mediator very experienced in complex litigation and with particular experience before this Court. With respect to these settlements, I have considered the claims and positions of the various parties, the input from the Mediator, and the relative likely costs and benefits to the Receivership Estate of agreeing to the settlements or pursuing the Estate's rights through litigation or otherwise. I believe that the settlements reflected in the Distribution Plan are, collectively, in the best interests of the Receivership Estate. It is important to note that under the HFG Settlement, the HFG Parties' Sunwest-related assets will be contributed without need for litigation or collection, and the HFG Parties will not realize value from the Reorganized Company until the Reorganized Company has generated new value for interest holders (Investors and certain unsecured creditors) of at least \$500 million.

I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

Executed this 25<sup>th</sup> day of August, 2009, at Portland, Oregon.



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MICHAEL A. GRASSMUECK,  
Federal Equity Receiver