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IN THE UNITED STATES DISTRICT COURT FOR THE
DISTRICT OF UTAH, CENTRAL DIVISION

UNITED STATES OF AMERICA, Plaintiff, vs. RAPOWER3, LLC, INTERNATIONAL AUTOMATED SYSTEMS, INC., LTB1, LLC, R. GREGORY SHEPARD, NELDON JOHNSON, and ROGER FREEBORN, Defendants.	Civil No. 2:15-cv-00828-DN-EJF **OPPOSITION UNITED STATES' SECOND MOTION TO FREEZE THE ASSETS OF DEFENDANTS NELDON JOHNSON, RAPOWER-3, LLC, INTERNATIONAL AUTOMATED SYSTEMS, INC., AND R. GREGORY SHEPARD AND TO APPOINT A RECEIVER** Judge David Nuffer Magistrate Judge Evelyn J. Furse

Defendants International Automated Systems, Inc., LTB1, LLC, R. Gregory Shepard and Neldon Johnson, in opposition to the United States' Motion to Freeze the Assets of Defendants Neldon Johnson, RaPower3, LLC[1], and International Automated Systems, Inc. and Appoint a Receiver, respond as follows:

[1] RaPower3, LLC filed for Chapter 11 bankruptcy on Friday, June 29th, and, although they are mentioned in this response, an automatic stay prevents a response on their behalf for the present. Since the arguments made on behalf of the other party Defendants relate equally to RaPower3, LLC, we mention their name in this response.

ARGUMENT

I. Equitable Principles weigh against an asset freeze and receivership appointment at this time.

a. A preliminary injunction requires proof beyond acknowledgement of the grant of authority in 26 USC 7402.

As a preliminary matter, this Court should not abandon an examination of the traditional equitable principles governing the grant of a preliminary injunction despite the broad grant of authority under section 7402, and despite Plaintiff's encouragement to do so.[2] At present, there is no controlling decision that has interpreted the appropriate standard for issuing injunctive relief under Section 7402, particularly one that abandons the four-part test to merit an injunction applied in the 10th Circuit. *United States v. Colo. Mufflers Unlimited, Inc*., a case involving an injunction under Section 7402 (and cited by Plaintiff), recognized that there is "some uncertainty regarding the standards for issuance of the requested injunctive relief."[3] However, in deciding to issue a preliminary injunction, the trial court applied the "traditional equitable principles requiring proof of (1) substantial likelihood of success on the merits; (2) irreparable injury to the movant; (3) threatened injury to the movant outweighs injury to the Defendants; and (4) the injunction is not against the public interest." [4] Plaintiff's remark that *Mufflers Unlimited* suggests that this Court can abandon the traditional equitable inquiry is not well taken. It is an invitation to err.

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[2] See Doc. 414 at pg. 14 ("The statute alone provides this Court with sufficient authority to issue an injunctive order freezing Defendants' assets and appointing a receiver without examining the preliminary injunction factors.")

[3] *United States v. Colo. Mufflers Unlimited, Inc*., Civil Action No. 03-cv-1310-WDM-CBS, 2007 U.S. Dist. LEXIS 24393, at *11, 99 A.F.T.R.2d (RIA) 2052 (D. Colo. Mar. 30, 2007).

[4] *Id.*

Additionally, courts have long recognized that appointing a receiver is an extraordinary remedy.[5] This remedy is so serious that such an order – as a matter of right— is subject to an immediate interlocutory appeal with the 10th Circuit Court of Appeals.[6] While the court has authority under 26 U.S.C.S. § 7402 to appoint a receiver, that authority is limited to situations where an appointment is "necessary and appropriate for the enforcement of internal revenue laws."[7] There is no reason for such an appointment at present.

b. While Plaintiff has succeeded on the merits at trial, Defendants will appeal.

At present, this factor weighs in Plaintiff's favor given the Court's preliminary oral findings read into the record on June 22, 2018. However, Defendants intend to challenge these findings and other appealable issues preserved before and during trial. Germane to this opposition is Defendants' challenge the admissibility and adequacy of the Government's proof supporting its disgorgement request and calculation of amounts. The weakness of the proof and the absence of expert testimony regarding any financial calculations make the calculation for disgorgement dubious at best. Furthermore, even if the Court of Appeals considers Plaintiff's summary exhibits properly admitted, Defendants challenge the Government's flawed method of computation using those exhibits. The resulting numbers are not sufficiently reliable to meet the burden of a

[5] *United States SEC v. Universal Express, Inc.*, 2007 U.S. Dist. LEXIS 65009, at 37 (S.D.N.Y. Aug. 30, 2007); (appointment necessary where defendants have continued to "flout numerous aspects of the internal revenue laws and the injunction" and where court is not persuaded that defendants can remedy "their historic noncompliance or repay their substantial outstanding tax judgement without close supervision or support."); *United States v. Latney's Funeral Home, Inc.*, 41 F. Supp. 3d 24, 38 (D.D.C. 2014); *United States SEC v. Levine*, 671 F. Supp. 2d 14, ¶ 61 (D.D.C. 2009) (appointment receiver necessary where defendants have continued to violate court orders and there is "no one who is responsible, wiling, and able to manage a company in compliance with federal security laws.); *Canada Life Assur. Co. v. LaPeter*, 563 F.3d 837, 844 (9th Cir. 2009) (appointing a receiver is "an extraordinary remedy" that "should be applied with caution" to be used "cautiously and only where less onerous remedies would be inadequate or unavailable."); see also *Logal v. Stasan, Inc.*, 2000 U.S. Dist. LEXIS 12084, at *3 (N.D. Tex. Aug. 21, 2000) (A receivership is an extraordinarily harsh remedy and one that courts are particularly loath to utilize);

[6] *See* 28 U.S.C.S. 1292(a)(2).

[7] 26 U.S.C.S. § 7402(a).

reasonable approximation of Defendants' gains. Plaintiff's insistence to the contrary does not make it so. For these reasons, this factor does not fully weigh in favor of Plaintiff's request.

c. Plaintiff will not suffer irreparable injury if an asset freeze does not issue.

Plaintiff claims that Defendants continued sales of lenses to this day causes Plaintiff further harm because of the tax benefits claimed by its customers concerning those lenses.[8] To this end, Plaintiff requests an immediate asset freeze and receiver appointment. Plaintiff presumably will demand the receiver shutdown all lens sales to obtain the broadest relief possible.[9]

This argument, however, ignores Defendants' actions since trial. Defendants have entirely complied with this Court's Initial Order and Injunction After Trial. Furthermore, Defendants went even further by contacting tax preparers known to service RaPower3 customers to inform them of the order and to requested that they discontinue assisting customers with claiming tax credits and depreciation for RaPower3 lenses. Defendants were not ordered to take this step. They voluntarily took the step to end any further tax-motivated purchase of lenses. Consequently, there can be no further harm caused by Defendants. Until further order of this Court or the 10th Circuit Court of Appeals, Defendants will remain compliant with every order of this Court. Before the Court ruled, they held an honest belief and acted on it. Following the Court's announced decision, they submit and will follow the Court's direction. There is no need for coercion, nor a receiver.

Additionally, freezing Neldon Johnson's assets serves no purpose because Mr. Johnson has no assets. Where there are no assets to freeze, Plaintiff suffers no injury by not freezing Mr. Johnson's assets.

1. Defendants have not been dissipating assets.

[8] Doc 414 at pg. 17.

[9] During closing argument, the Court seemingly challenged Plaintiff on this point, stating that preventing the Defendants from selling their lenses seemed overbroad, so long as Defendants' lens sales were divorced from the promotion of any and all tax benefits related to the lenses.

Plaintiff argues an asset freeze is necessary because if the injunctive relief requested is not granted, Defendants will have full unfettered access to the funds illicitly obtained to the detriment of the United States.[10] Plaintiff argues this is likely merely because family members who work in the business have been paid for their past labor, and patents have been registered to a company located in Nevis. The patents were registered there years ago and long before this motion.

A. Defendants have transferred and spent money – only for the purpose of maintaining and progressing their business.

Plaintiff relies upon copies of bank statements of IAS between June, 2016 and January, 2017 and of RaPower3 between June, 2016 and January, 2017[11], to demonstrate that RaPower3 and IAS have been paying their employees and their legal counsel. That does not prove they are transferring assets. Plaintiff provided the Court with checks to Neldon Johnson from 2005[12], a check to NP Johnson Family Limited Partnership from 2012[13], a check from Cobblestone Centre (not a party to this action) to Randy Johnson from 2014[14] and a check to the Howard County Tax Office from 2015 from this same entity[15]. None of these checks relate to anything in this case and none show dissipation of assets is currently taking place. These payments are from years before this action began, written by nonparties or for purposes that are clearly necessary for business related activities for the benefit of the company. They do not provide this Court a basis to fear that money is being transferred out of the company for the purpose of avoiding this or any other

[10] See. Doc. 252 at pg. 12

[11] See Plaintiff's Ex. 684.

[12] See Plaintiff's Ex. 646.

[13] See Plaintiff's Ex. 647.

[14] See Plaintiff's Ex. 650.

[15] See Plaintiff's Ex. 649.

creditor. Payments to employees, including family members, results in them paying income taxes—a benefit to the government altogether unrecognized in the government's case.

The purpose for ordering a freeze of assets – or any preliminary injunction – is to deal with some exigency or emergency. It requires immediate action because something is going to happen immediately. The evidence used in the motion not only demonstrates a complete lack of urgency in this case but suggests any hasty action would be wholly unnecessary. A payment to an employee from 5 years ago for work done on the company's behalf doesn't demonstrate immediate harm. It shows quite the opposite. Hyperbole is not proof, but mere rhetoric.

B. Patents are Assigned to Companies in Nevis.

Defendants admit that for business reasons unrelated to this case, prior to the initiation of this lawsuit patents were assigned to companies in Nevis. Defendants' business is international and several foreign companies have expressed interest in Defendants' technologies. There is no exigency or emergency created by registering patents years prior to this case. Indeed, if examined carefully, with the exception of one assignment, which occurred in June, 2015, all of the assignments occurred prior to this case being filed. There have been no assignments or transfers since 2015, or three years ago. This is hardly a basis to claim an immediate harm. The argument overreaches the facts and common sense.

Plaintiff has previously called Defendants' business a "sham enterprise." They argue there is no value in it – only a tax scheme. If there is no value, then what does it matter that a valueless patent was assigned to a Nevis company? The government's position is inconsistent. If the patent has value and must be protected, then the business likewise has value, and should be protected, not put at jeopardy by a receiver working for the government who has no motivation to continue the business operations.

d. Injury to the Defendants outweighs any threatened harm to the Plaintiff.

In this latest attempt to freeze assets, Plaintiff added Mr. Shepard to its request. Plaintiff is requested that Mr. Shepard be restricted to withdrawals in the amount of $3,619.00 of which only $114.00 is allotted for out of pocket medical costs. At present, Mr. Shepard is suffering from a heart condition that may require costly medical attention, including open heart surgery within the next 30 days. This proposed allocation of funds falls well below the amount he would need to take care of his medical and living needs. Additionally, based on the government's still unliquidated claim his proposed share of the anticipated disgorgement order is comparatively small. For these reasons, the harm to Mr. Shepard greatly outweighs the threatened harm to the Plaintiff. Further, there is no evidence before the court of the extent of Mr. Shepard's assets and what injury such an order would cause to him beyond any disgorgement order (which may not be entered by the court for at least another 45 days).

Additionally, freezing the assets and appointing a receiver for the remaining Defendants would both injure all parties involved, and diminish Defendants' abilities to pay any disgorgement amount that may be ordered. Plaintiff has made clear it wants to prevent the Defendants from engaging in any business involving lens sales, even if they discontinue promotion of tax benefits and have buyers interested in purchasing without tax benefits. Freezing assets and appointing a receiver would effectively shut down all business operations in their entirety, preventing Defendants from continuing to generate any revenue to be used to pay off debts, including disgorgement. So long as Defendants make every effort necessary to earn a living without promoting tax benefits of their product, they should remain in control of their businesses and have use of their assets.

Furthermore, Defendants challenge the appropriateness of imposing such an extreme remedy before any disgorgement has issued. As of the date of this motion Defendants have not been ordered to disgorge any amount. Additionally, Plaintiff has impermissibly included amounts

involving non-parties in their unliquidated claims.[16] These non-parties cannot be subject to any disgorgement award, much less the invasive control of a receivership.

Finally, depending on the final amount determined by this court, some (if not all) of the Defendants may be able to satisfy in full a disgorgement amount without the costs, disruption, and destructiveness of appointing a receiver. For these reasons, appointing a receiver is at a minimum premature, and should be rejected outright unless something more is done to show an exigent need.

II. The case law upon which Plaintiff relies is factually and procedurally inapposite to this case.

a. Plaintiff's series of authority is distinguishable from this case.

Plaintiff relies on a series of decisions where appointing a receiver was considered "necessary and appropriate" under 26 U.S.C.S. § 7402.[17] However, all these authorities are distinguishable both factually and procedurally from this case and therefore do not support Plaintiff's argument that appointing a receiver is necessary and appropriate in this case. Each is addressed in turn.

1. *United States v. Latney's Funeral Home.*

In *United States v. Latney's Funeral Home*[18], the district court appointed a receiver only ***after*:**

(1) the court acknowledged that the defendants had consented to a preliminary injunction (issued under § 7402) that precluded defendants from committing further violations of the Internal Revenue Code,

(2) the court determined that the defendant owed over $1 million in unpaid payroll taxes and civil penalties through the government's unopposed motion for summary judgment;

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[16] *See United States v. Mesadieu*, 180 F. Supp. 3d 1113, 1123 (M.D. Fla. 2016) ("Had the Court determined that the Government established a reasonable approximation of the amount subject to disgorgement, the Court questions whether it would have had jurisdiction to order disgorgement of revenue obtained by Mesadieu's companies—entities that are not before the Court.")

[17] *See* Doc. 414 at pg. 14.

[18] *Latney's Funeral Home*, 41 F.Supp.3d at 27.

(3) the court found the defendant (by clear and convincing evidence) in civil contempt for failing to adhere to the terms of the stipulated preliminary injunction and after considering defendant's defenses of an inability to comply and good faith and substantial compliance; and

(4) the court held that the facts before it justified the "extraordinary remedy" of appointment a receiver because "ample evidence" that the defendants "continued to flout numerous aspects of the internal revenue laws and the Injunction…" and was "not persuaded that Defendants can remedy their historic noncompliance or repay their substantial outstanding tax judgments without close supervision and support."[19]

In the current matter, the circumstances could not be more dissimilar. First, unlike *Latney's Funeral Home*, Defendants here are not subject to a preliminary injunction preventing them from pursuing the conduct of their regular business operations. Second, *Latney's Funeral Home* is procedurally dissimilar: The Defendants are not subject to the judgment and ruling of an unopposed summary judgment nor are they subject to a civil contempt related non-payment of obligations arising from such an order. Defendants here fought the Government's case on the merits, and having lost, thereafter willingly submitted to the Court's decision.

2. *United States v. Bartle.*

United States v. Bartle[20], an unpublished 7th Circuit decision[21], is also factually and procedurally inapposite to the facts of this case. In *Bartle*, the district court appointed a receiver only after:

(1) the court ordered the defendant to pay an agreed upon amount of $1,378,420;

(2) the defendant had failed to make a single payment;

(3) the parties entered into a subsequent agreement that required the defendant to make installment payments to disclose to the government monthly statements;

(4) the district court heard evidence that the defendant from 2001 to 2004 had shuffled over $1 million among various accounts to thwart the government's collection efforts,

[19] *Id.*

[20] 159 Fed. Appx. 723 (7th Cir. 2005) (unpublished non-precedential decision).

[21] Rule 32.1 of the Seventh Circuit prohibit citation to its unpublished non-precedential decisions issued before 2007.

and fraudulently underreported his receipts and failed to pay the government $435,000 as required by the order;

(5) the defendant admitted to "fudging" his statements to the government;

(6) the court discussed "at length" with the parties "inability to secure Bartle's finances under the control of a court-appointed third-party; and

(7) even at this point, the court withheld appointing a receiver until the defendant ignored a subsequent payment modification and filed for bankruptcy.[22]

The 7th Circuit Court of Appeals upheld the appointment of the receiver on review.[23] It acknowledged that "a receiver is especially appropriate 'in cases involving fraud and the possible dissipation of assets since the primary consideration in determining whether to appoint a receiver is the necessity to protect, conserve administer property pending final disposition of the suit.'"[24] After noting that the district court had policed defendant's "shenanigans" over several years, listened to his excuses, and ultimately determined that the defendant was untrustworthy and intentionally avoiding the government's collection of its judgment, the panel concluded the district did not abuse its discretion in appointing a receiver.[25]

The facts in *Bartle* are glaringly dissimilar. Again, Defendants to date have not been assessed or ordered to pay any amount. Additionally, Plaintiff has not shown Defendants are incapable of following a court order requiring them to pay any amount; that Defendants have "fudged" statements to the government; or have breached subsequent agreements to fulfill payment obligations. There is no present obligation for Defendants here to pay anything. No agreed amount or default on payment of an agreed amount has happened in this case. In short, *Bartel* provides guidance that strongly suggests the Government is not entitled to a receiver in this case.

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[22] *United States v. Bartle*, 159 Fed. Appx. at 724-25.

[23] Id.at 725.

[24] Id (internal citation omitted)

[25]

Additionally, the matters are procedurally inapposite, since *Bartle* involved (once again) enforcement for non-compliance of a final court order prior to appointment of a receiver.

3. *Florida v. United States.*

Florida v. United States[26] is also factually and procedurally distinguishable. In *Florida*, the 8th Circuit affirmed the district court's appointment of a receiver, satisfied with the district court's judgement that (1) the Government made a prima facie case for some substantial tax liability, (2) further established that the tax liens were established for such liability, and (3) pursuant to applicable statutory procedure. This case has limited utility because unlike *Latney's Funeral Home* and *Bartle*, the court did not engage in any depth of analysis supporting its conclusion. Instead, it largely deferred to the district court's findings and conclusions.

4. *United States v. First Nat'l City Bank.*

Finally, *United States v. First Nat'l City Bank*[27] is factually distinguishable from this case. In *First National*¸ the IRS had ***already assessed*** $19,000,000 against a Uruguayan corporation, served notices of levy and federal tax lien to the bank in New York whose branch in Uruguay which held funds belonging to the Uruguayan corporation.[28] The IRS failed to personally serve the corporation, but had successfully served the bank.[29] The "narrow issue" before the court was whether the United States "may by injunction *pendente lite* protect whatever rights [the corporation] may have against [the bank.]"[30] The corporation had demonstrated both its willingness and ability to dissipate assets prior to issuance of the injunction by (1) a statement by

[26] 285 F.2d 596, 602 (8th Cir. 1960)

[27] 379 U.S. 378 (1965)

[28] *Id*. at 379.

[29] *Id*. at 386.

[30] *Id* at 381.

the corporation's attorney that "[it] would likely liquidate its holdings in the United States, and send the money out of the country" if the IRS persisted in attempting to collect taxes, and (2) the corporation was largely successful in liquidating its assets and transferring the funds out of county,[31] and some of the funds were actually proven to have been transferred on the day the government filed its complaint. [32]

The government's cited authority does not justify appointing a receiver, but instead teach that the request at present cannot be justified. Some act or acts following the Court's final decision would need to take place. Nothing following the Court's preliminary statements justify taking this draconian step.

Finally, the scope and breadth of the proposed Receivership Order from the Government (when it is entered) would strip Defendants from the ability to appeal this Court's final decision, much less carry out counsels' obligations ordered by this Court.[33] To preserve an opportunity to appeal, RaPower3 filed for Chapter 11 bankruptcy on Friday. After consulting with bankruptcy counsel, that step was deemed necessary to avoid the risk of losing appeal rights if a receiver is appointed as the government has requested with power to assume full control over all rights of the Defendants, including any right to appeal.

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[31] *Id.* at 386.

[32] I*d.*

[33] Doc. 414-4, in its proposed iteration, immediately discharges the Defendants' attorneys upon entry, thereby precluding the Defendants continued defense, including fulfilling obligations currently ordered by this Court (i.e., report concerning the "preservation order," and Defendants' objections to any proposed findings and order.) The overarching language is as follows:

> 5. The trustees, directors, officers, managers, employees, investment advisors, accountants, **attorneys and other agents of the Receivership Defendants are hereby dismissed** and the powers of any general partners, members, officers, employees, directors and/or managers **are hereby suspended**. Such persons and entities **shall have no authority** with respect to the Receivership Defendants' operations or assets, except to the extent as may hereafter be expressly granted by the Receiver.
>
> 6**. No person holding or claiming any position of any sort with RaPower-3 or IAS shall possess any authority to act by or on behalf of RaPower-3 or IAS**.

(emphasis added).

CONCLUSION

Neither the circumstances, timing, or the law justify a freeze of assets or appointment of a receiver in this case. Plaintiff's motion should be denied.

Dated this 2nd day of July, 2018.

NELSON SNUFFER DAHLE & POULSEN

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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing **OPPOSITION TO UNITED STATES' SECOND MOTION TO FREEZE THE ASSETS OF DEFENDANTS NELDON JOHNSON, RAPOWER3, LLC, AND INTERNATIONAL AUTOMATED SYSTEMS, INC. AND APPOINT A RECEIVER** was sent to counsel for the United States in the manner described below.

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