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

UNITED STATES OF AMERICA, Plaintiff, vs. RAPOWER-3, LLC, INTERNATIONAL AUTOMATED SYSTEMS, INC., LTB1, LLC, R. GREGORY SHEPARD, NELDON JOHNSON, and ROGER FREEBORN, Defendants.	Civil No. 2:15-cv-00828 DN **UNITED STATES' REPLY ON ITS MOTION TO VACATE, IN PART, THE JULY 5, 2018, ORDER** Judge David Nuffer Magistrate Judge Evelyn J. Furse

This Court may enter a final opinion and order in this matter notwithstanding the automatic stay that arose when RaPower-3 filed its Chapter 11 bankruptcy petition. Defendants have offered neither facts nor law to contradict this showing.

I. This Court has the authority to decide this motion.

This Court has the authority to determine whether proceedings in this case are excepted from the automatic stay under § 362(b)(4).[1] The United States filed its motion based on its misimpression that this Court had entered a stay of *this litigation* in light of RaPower-3's bankruptcy.[2] The motion explicitly does *not* seek relief from the automatic stay[3] because continued proceedings here are largely excepted from the automatic stay under § 362(b)(4).[4] A party is not required to file a motion to establish its right to proceed with a case under the (b)(4) exception; it simply proceeds.[5]

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[1] *E.g. Dominic's Rest. of Dayton, Inc. v. Mantia*, 683 F.3d 757, 760 (6th Cir. 2012); *S.E.C. v. Wolfson*, 309 B.R. 612, 617-18 (D. Utah 2004) ("The Court finds that it has jurisdiction to determine its own jurisdiction, as well as to decide whether the automatic stay is applicable to the instant litigation."); *see generally United States v. Moore*, No. 2:12-CV-04196-NKL, 2013 WL 7873535, at *1 (W.D. Mo. Mar. 27, 2013) ("Count V of the United States' Complaint is exempt from this automatic bankruptcy stay that arose when Defendants filed their bankruptcy petitions."); *United States v. Fisher*, No. CIV.A.3:03-CV-2108-G, 2004 WL 62583, at *1-3 (N.D. Tex. Jan. 9, 2004).

[2] *See* ECF No. 431.

[3] *Contra* ECF No. 434 at 2, 5.

[4] Even if this motion *did* seek relief from the automatic stay, this Court would have jurisdiction to decide that motion. *E.g.*, *N.L.R.B. v. Edward Cooper Painting, Inc.*, 804 F.2d 934, 939 (6th Cir. 1986) ("The court in which the litigation claimed to be stayed is pending has jurisdiction to determine not only its own jurisdiction but also the more precise question whether the proceeding pending before it is subject to the automatic stay." (quoting *In re Baldwin-United Corp. Litig.*, 765 F.2d 343, 347 (2d Cir.1985)); *Broadcast Music, Inc. v. Game Operators Corp.*, 107 B.R. 326, 327 (D. Kan. 1989).

[5] *See Eddleman v. U.S. Dep't of Labor*, 923 F.2d 782, 783 (10th Cir. 1991), *overruled in part on other grounds by Temex Energy, Inc. v. Underwood, Wilson, Berry, Stein & Johnson*, 968 F.2d 1003, 1005 n.3 (10th Cir. 1992) (Department of Labor filed administrative proceedings against debtors already in bankruptcy without making a motion to proceed under § 362(b)(4); on debtors' motion, the court granted an injunction against that action and

(continued...)

II. Bankruptcy's automatic stay does not apply to cases like this one, to enforce a governmental unit's police or regulatory power.

Defendants agree that § 362(b)(4) excepts from the automatic stay "the commencement or continuation of an action or proceeding by a governmental unit . . . to enforce such governmental unit's . . . police and regulatory power."[6] Where "a governmental unit is suing a debtor to prevent or stop violation of fraud, environmental protection, consumer protection, safety, or similar police or regulatory laws, or attempting to fix damages for violation of such a law, the action or proceeding is not stayed under the automatic stay."[7] Defendants also agree that the Tenth Circuit has identified two tests to determine whether a governmental unit is exercising its "police or regulatory power," such that proceedings are excepted from the automatic stay under § 362(b)(4): the "public policy" test and the "pecuniary purpose" test.[8] An action need meet only one test to be excepted from the automatic stay under § 362(b)(4).[9]

(…continued)

damages for willful violation of the automatic stay; Tenth Circuit held that "[o]n the merits of DOL's challenge, . . . the enforcement action at issue was exempt from the automatic stay under 11 U.S.C. § 362(b)(4)," reversed the court's holding and remanded with instructions to dissolve the injunction).

[6] 11 U.S.C. § 362(b)(4).

[7] H.R. Rep. No. 595, 95th Cong., 1st Sess. 343 (1977), reprinted in 1978 U.S. Code Cong. & Ad. News 5963, 6299, *quoted in Martin v. Occupational Safety & Health Review Comm'n*, 941 F.2d 1051, 1054 n.2 (10th Cir. 1991); *Eddleman*, 923 F.2d at785-86 ("It is clear from the legislative history that Congress intended to give government even greater protection from unfair application of the automatic stay than it gave to private creditors."); *Wolfson*, 309 B.R. at 618-19 ("[T]he [SEC's] prosecution of this civil fraud action is excepted from the automatic stay under the Bankruptcy Code Section 362(b)(4) . . . .") (Kimball, J.).

[8] *Eddleman*, 923 F.2d at 791.

[9] *Lockyer v. Mirant Corp.*, 398 F.3d 1098, 1108 (9th Cir. 2005) ("A suit comes within the exception of § 362(b)(4) if it satisfies either test."); *see Eddleman*, 923 F.2d at 791 (after concluding that an action met the "pecuniary purpose" test, the court noted that it was not "bound to [also] apply" the "public policy" test).

This Court's entry of the final opinion and order for injunction and disgorgement in this matter is excepted from the automatic stay under § 362(b)(4) because this action meets *both* the public policy and the pecuniary interest tests.[10] Although RaPower-3 acknowledges that the "public policy" test exists, it does not address the reasons that this case *passes that test* in its opposition brief.[11] In this case, the United States is enforcing public policy by exercising its police or regulatory power to stop all Defendants from engaging in fraudulent conduct that violates the internal revenue laws.[12] The primary purpose of this case is to stop all Defendants – including RaPower-3 – from continuing to run a "fraud on the American people who have effectively paid to operate defendants' enterprise;" an enterprise that "has no sound scientific basis as a whole; has no demonstration of economic viability, not even the barest evidence; and does not qualify lens buyers for federal tax credit or depreciation deductions."[13] Having already

[10] *See, e.g.*, *F.T.C. v. Unified Glob. Grp., LLC*, No. 15-CV-422W(F), 2016 WL 489897, at *2 (W.D.N.Y. Feb. 9, 2016); *S.E.C. v. Vaughn*, No. CV 10-0263 MCA/WPL, 2010 WL 11441819, at *1-2 (D.N.M. Nov. 16, 2010); *In re D'Angelo*, 409 B.R. 296, 298-99 (Bankr. D.N.J. 2009); *In re Nelson*, 240 B.R. 802, 803-07 (Bankr. D. Me. 1999); *see also In re Bilzerian*, 146 B.R 871, 873 (Bankr. M.D. Fla. 1992).

[11] *See* ECF No. 434 at 3-5.

[12] *See, e.g.*, 26 U.S.C. § 7402(a) ("The district courts of the United States at the instance of the United States shall have such jurisdiction to make and issue in civil actions . . . orders of injunction, . . . and such other orders and processes, and to render such judgments and decrees as may be necessary or appropriate for the enforcement of the internal revenue laws."); *United States v. Elsass*, 978 F. Supp. 2d 901, 941 (S.D. Ohio 2013) ("[Section] 7402(a) is undoubtedly designed to prevent individuals from undermining the Nation's tax laws through exploiting loopholes in the [Internal Revenue Code's] overall regulatory scheme."); *Fisher*, 2004 WL 62583, at *2 ("Certainly, enjoining a debtor in bankruptcy from committing or promoting tax fraud is congruent with the purposes of § 362(b)(4) and furthers the public welfare by protecting taxpayers as well as the United States Treasury."); *see also In re Universal Life Church, Inc.*, 128 F.3d 1294, 1297 (9th Cir. 1997), *as amended on denial of reh'g* (Dec. 30, 1997) ("The question in this case is whether an IRS letter revoking the tax exempt status of a religious corporation meets either [the public policy or the pecuniary purpose test]. We hold it meets both. . . . [T]he revocation was an exercise of the IRS's police or regulatory power because revocation promotes public welfare by assuring the public and potential donors that contributions will be used for legitimate charitable purposes.").

[13] Tr. 2415:5-18 (*see* ECF No. 429-1).

concluded that the Defendants have perpetrated a "massive fraud"[14] and entered an interim injunction, the Court's anticipated "complete set of [final] findings and conclusions . . . will support much broader relief"[15]. That broader relief is necessary and appropriate to prevent Defendants' ongoing fraud against the U.S. Treasury.[16] Therefore, entering the final opinion and order in this case will effectuate a core public policy purpose for these proceedings generally: prevention of fraud and enforcement of the internal revenue laws by stopping the promotion of an abusive tax scheme. This meets the "public policy" test.[17]

Our request that this Court enter the final order fixing the amount of disgorgement for which all Defendants, including RaPower-3, are liable also meets both the public policy and the pecuniary interest test.[18] A final order would not "protect" the United States' interest in any property of RaPower-3's bankruptcy estate.[19] In its bankruptcy filings, RaPower-3 has already identified the United States as a creditor with a purportedly "[c]ontingent[,] [u]nliquidated[, and] [d]isputed" claim for an amount up to $32 million.[20] An order fixing the disgorgement amount

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[14] Tr. 2515:5-6.

[15] ECF No. 413 at 1.

[16] *See* 26 U.S.C. §§ 7402(a), 7408.

[17] *See Moore*, 2013 WL 7873535, at *1 (injunctive relief under 26 U.S.C. § 7402(a) to compel defendants to withhold and timely pay over to the IRS all taxes required by law, including federal income, FICA and FUTA taxes was exempt from the automatic stay under 11 U.S.C § 362(b)(4)); *Fisher*, 2004 WL 62583, at *1-3 (action under 26 U.S.C. §§ 7402, 7407, and 7408 to prevent defendants from promoting allegedly illegal tax schemes exempt from the automatic stay under 11 U.S.C § 362(b)(4)).

[18] *Perez v. Cargill Heating & Air Conditioning Co.*, No. 14-CV-228-JDP, 2014 WL 5325372, at *3 (W.D. Wis. Oct. 20, 2014); *Vaughn*, 2010 WL 11441819, at *1-2; *see also Wolfson*, 309 B.R. at 619.

[19] *Eddleman*, 923 F.2d at 791.

[20] *In re RaPower-3, LLC*, No. 18-24865, Docket No. 6, List of Creditors Who Have the 20 Largest Unsecured Claims and Are Not Insiders, at 2 (June 29, 2018) (Pl. Ex. 917 (*see* ECF No. 429-2)).

for each Defendant, including RaPower-3, will not "confer any advantage on the [United States] vis-à-vis other [RaPower-3] creditors."[21] Instead, it will simply resolve any contingency or dispute and provide clarity as to the precise amount of disgorgement comprising the United States' claim with respect to RaPower-3. Once this Court enters the order fixing the disgorgement amount, the United States will turn to the bankruptcy proceedings to address its claim against RaPower-3 for RaPower-3's portion of disgorgement.[22] Accordingly, this Court may fix the amount of disgorgement for which RaPower-3, and all other Defendants, are liable.[23] Defendants have not cited facts or law that requires a different conclusion.

III. Defendants have not shown that proceeding with the asset freeze and receivership as to non-RaPower-3 Defendants will affect property of RaPower-3's bankruptcy estate.

All Defendants complain (without citation to facts or law) that the United States is asking this Court to exercise control over property of the RaPower-3 bankruptcy estate.[24] That is simply not true. Since RaPower-3's bankruptcy filing, the United States has never suggested that this

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[21] *Solis v. SCA Rest. Corp.*, 463 B.R. 248, 254 (E.D.N.Y. 2011); *accord Eddleman*, 923 F.2d at 791 ("[T]he back-pay claimants would not receive any extra priority by virtue of the DOL action. Actual collection of the back-pay claims must proceed according to normal bankruptcy procedures."); *Perez*, 2014 WL 5325372, at *3, 5; *In re Bilzerian*, 146 B.R. at 873.

[22] *Eddleman*, 923 F.2d at 791; *Solis*, 463 B.R. at 254; *In re Nelson*, 240 B.R. at 805 n.8; *In re Bilzerian*, 146 B.R. at 873.

[23] *Martin*, 941 F.2d at 1053-54 ("While it is abundantly clear that we may not direct enforcement of a money judgment against CF & I, we may review the Commission's order insofar as the Secretary sought abatement of a safety violation (prospective enforcement) and a monetary penalty."); *Edward Cooper Painting*, 804 F.2d at 943 ("We thus affirm entry of a money judgment, but do not enforce that money judgment.") (emphasis in original); *Wolfson*, 309 B.R. at 619 ("Courts have explicitly held that the exception to the automatic stay provision 'extends to permit an injunction and enforcement of an injunction, and to permit the entry of a money judgment, but does not extend to permit enforcement of a money judgment.'").

[24] ECF No. 434 at 4-5, ECF No. 435 at 3 (incorporating by reference RaPower-3's arguments).

Court should freeze its assets or appoint a receiver for it.[25] And this Court is contemplating moving forward with an asset freeze and receivership with respect to all Defendants *other than* RaPower-3. This is permissible because "[i]t is universally acknowledged that an automatic stay of proceeding accorded by § 362 may not be invoked by entities such as sureties, guarantors, co-obligors, or others with a similar legal or factual nexus to the Chapter 11 debtor."[26]

Although Defendants cite no facts or legal authority, they appear to be arguing that freezing the assets and ordering a receivership for all Defendants other than RaPower-3 will exercise control of, or deplete property of, RaPower-3's bankruptcy estate in violation of § 362(a)(3).[27] First, the United States' claims for disgorgement (and for an asset freeze and receivership) against all Defendants other than RaPower-3 are not "dependent" upon any claim made against RaPower-3.[28] This Court has already made factual findings that show each Defendant's independent, albeit coordinated, role in perpetrating their fraud. For example, Neldon Johnson "is the center. He has a central control of every entity in his solar energy enterprise, which has any business activity and has interest in other entities which are managed by other persons, but those entities have been shown to have no business activity. He alone

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[25] *Contra* ECF No. 434 at 4-5.

[26] *Lynch v. Johns-Manville Sales Corp.*, 710 F.2d 1194, 1196 (6th Cir. 1983); *accord Oklahoma Federated Gold & Numismatics, Inc. v. Blodgett*, 24 F.3d 136, 141 (10th Cir. 1994) ("While § 362[(a)(1)] extends the stay provisions of the Bankruptcy Code to [judicial proceedings against] the "debtor", the rule followed by this circuit and the general rule in other circuits is that the stay provision does not extend to solvent codefendants of the debtor.").

[27] *See* ECF No. 434 at 4-5.

[28] *In re Peeples*, 553 B.R. 892, 900 (Bankr. D. Utah 2016), *aff'd Matter of Peeples*, 566 B.R. 68 (D. Utah 2017), *aff'd in part, vacated and remanded in part on other grounds by In re Peeples*, 880 F.3d 1207 (10th Cir. 2018) ("[I]f the basis for the action is independent of the claim against the debtor, then the action is not stayed. Put another way, even though a creditor may have a claim against the debtor, a creditor is free to pursue its claim against a non-debtor so long as there is an independent basis for the creditor to pursue that claim.").

makes decisions about businesses."[29] "Greg Shepard ignited Neldon Johnson's enterprise with multilevel marketing. . . . The combination of incentives from multilevel marketing fees and tax benefits energized sales. Johnson, the claimed scientist, engineer and project designer distorted tax issues to fit his plan, and Shepard experienced in marketing overstated the tax and scientific issues and operational facts and misstated and exaggerated this bad advice in volume and content."[30]

Second, in exceptional circumstances, "[t]he automatic stay can apply to non-debtors, but normally does so only when a claim against the non-debtor will have an immediate adverse economic consequence for the debtor's estate."[31] "The non-debtor must prove that its interests are so closely related to the debtor party's that [an order freezing assets and appointing a receiver] against the non-debtor will in effect be [an order freezing assets and appointing a receiver] against the debtor."[32] Defendants have not shown that this Court's proposed asset freeze and receivership will affect, in any way, RaPower-3's bankruptcy estate – much less that it will have

[29] Tr. 2519:8-13.

[30] Tr. 2518:15-24.

[31] *Queenie, Ltd. v. Nygard Int'l*, 321 F.3d 282, 287 (2d Cir. 2003); *accord* In re Nat. Century Fin. Enterprises, Inc., 423 F.3d 567, 578 (6th Cir. 2005) ("[A]n action taken against a nondebtor which would inevitably have an adverse impact upon the property of the estate must be barred by the [§ 362(a)(3)] automatic stay provision." (quotation omitted).

[32] *Deem v. Baron*, No. 2:15-CV-00755-DS, 2017 WL 2623840, at *2 (D. Utah June 16, 2017) (Sam, J.); *Fid. & Deposit Co. of Maryland v. Tri-Lam Co.*, No. SA-06-CA-207-XR, 2007 WL 1091311, at *3 (W.D. Tex. Apr. 9, 2007) (if non-debtors wish to have § 362(a)(3)'s automatic stay applied to their assets, they must seek relief in the bankruptcy court); *see also Fisher Sand & Gravel Co. v. W. Sur. Co.*, No. CV 09-727 WPL/RLP, 2009 WL 4099768, at *5 (D.N.M. Oct. 20, 2009) ("If the automatic stay could be deemed to apply to entities affiliated with the debtor without the necessity of an order extending the stay, it would be difficult for creditors of the affiliated entities to know whether attempts to collect from those entities would violate the automatic stay.").

"an immediate adverse economic consequence" on it.[33] Defendants have not shown that the order freezing assets and appointing a receiver as to all other Defendants will have the effect of freezing RaPower-3's assets and appointing a receiver for it.[34] Instead, all Defendants are attempting to use RaPower-3's bankruptcy filing to escape this Court's forthcoming order freezing their assets and appointing a receiver – *without* shouldering the obligations of disclosing, under penalty of perjury, information about their assets and debts (as RaPower-3 must do in bankruptcy).[35]

IV. Conclusion

Under 26 U.S.C. § 362(b)(4), entry of a final opinion and order, and enforcement of the injunctive relief that will be part of that order are excepted from the automatic stay. This Court has already established a new schedule for the parties to submit and review the draft opinion and

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[33] *See Deem*, 2017 WL 2623840, at *2 ("Although an automatic stay may, on occasion, be applied to parties not in bankruptcy, such application is rare and requires special circumstances."); *In re All Seasons Resorts, Inc.*, 79 B.R. 901, 904 (Bankr. C.D. Cal. 1987); *In re Otero Mills, Inc.*, 21 B.R. 777, 778 (Bankr. D.N.M. 1982).

[34] *See* Patton v. Bearden, 8 F.3d 343, 349 (6th Cir. 1993) ("Some courts have held that the debtor's stay may be extended to non-bankrupt parties in 'unusual circumstances.' Such circumstances usually include when the debtor and the non-bankrupt party are closely related or the stay contributes to the debtor's reorganization. . . . [S]uch extensions, although referred to as extensions of the automatic stay, were in fact injunctions issued by the bankruptcy court after hearing and the establishment of unusual need to take this action to protect the administration of the bankruptcy estate. Even if we were to adopt the unusual circumstances test, the bankruptcy court would first need to extend the automatic stay under its equity jurisdiction pursuant to 11 U.S.C. § 105. Moreover, the Beardens have not brought forth any evidence of unusual circumstances which would justify extending the automatic stay to their protection.")

[35] *Deem*, 2017 WL 2623840, at *3 (D. Utah June 16, 2017) (holding that the automatic stay applied to only the entities that had filed for bankruptcy, in part because "[a]s Plaintiffs state in their brief, it appears that the defendant is 'seeking bankruptcy protection for all of his companies without submitting all of his assets to bankruptcy supervision. He seeks a selective, one-sided approach to bankruptcy.... He seeks to stop all creditors from proceeding in any fashion against him or any of his assets through application of the bankruptcy rules, but does not want those same bankruptcy rules to apply to himself.'").

order.[36] Once the parties finish their work, for all of the reasons cited in our opening brief, this Court is well within its authority to promptly enter the final opinion and order in this matter, including fixing the amount of disgorgement for which each Defendant is liable, to trigger the appeal clock and allow the United States to enforce the injunction with respect to *all* Defendants.

Dated: July 20, 2018

Respectfully submitted,

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[36] ECF No. 432.

CERTIFICATE OF SERVICE

I hereby certify that on July 20, 2018 the foregoing document and its supporting documents were electronically filed with the Clerk of the Court through the CM/ECF system, which sent notice of the electronic filing to all counsel of record.

/s/ Erin Healy Gallagher
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