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UNITED STATES DISTRICT COURT

DISTRICT OF OREGON

PORTLAND DIVISION

FEDERAL TRADE COMMISSION,

Plaintiff,

vs.

MERCHANT PROCESSING, INC.; VEQUITY FINANCIAL GROUP, INC.; DIRECT MERCHANT PROCESSING, INC.; PPI SERVICES, INC.; AARON LEE RIAN; KARLEY MCCARTHY, AKA KARLY SPEELMAN,

Defendants.

Case No. CV 07-0533-BR

MEMORANDUM IN SUPPORT OF RECEIVER'S MOTION FOR ORDER TO (I) ALLOW CERTAIN CLAIMS, (II) AUTHORIZE PAYMENT TO CERTAIN TERMINAL LEASE COMPANIES, AND (III) TRANSFER ESTATE FUNDS TO FEDERAL TRADE COMMISSION REDRESS CONTRACTOR [EXHIBITS "A"-"B"]

[Motion, Memorandum, Declaration of Michael A. Grassmueck, and Proposed Order, Filed Concurrently Herewith]

I.

INTRODUCTION

On April 30, 2007, the Court entered the Stipulated Preliminary Injunction and Order for Other Equitable Relief ("First PI"), which authorized the appointment of Michael A. Grassmueck, as receiver (the "Receiver") with regard to Merchant Processing, Inc. ("MPI"), Vequity Financial Group, Inc. Direct Merchant Processing, Inc., their respective affiliates and subsidiaries, ("MPI Receivership Defendants") under the control of any of them, including, but not limited to, Bad Boy Enterprises, Inc., dba Atlantic Hound, Bad Boy Racing, LLC, Bad Boy Investments, LLC, and Rian Racing, Inc. (collectively, the "Receivership Defendants"). Pursuant to a Second Stipulated Preliminary Injunction and Order for Other Equitable Relief, entered on November 2, 2007, ("Second PI") other defendants were added to the list of Receivership Defendants, and the Receiver's appointment as receiver was confirmed as continuing.

Pursuant to the First PI, the Receiver was empowered with all powers of a federal equity receiver which included, among others, the power to sell the assets of the receivership estate ("Receivership Estate"), determine the allowance of claims through a claims review process, and make disbursements from the Receivership Estate as necessary and consistent with the powers and duties set forth in the First PI.

On April 30, 2008, the Court entered the Stipulated Final Judgment and Order for Permanent Injunction and Other Equitable Relief ("Final Order"), which authorized judgment against the Receivership Defendants, jointly and severally, in the amount of $26,480,041, and confirmed the continued appointment of the Receiver as set forth in the Second PI Order (including, but not limited to, his powers to sell assets of the Receivership Estate). The Final Order further provided that funds from the Receivership Estate would be paid over to the Federal Trade Commission ("FTC"), and the FTC would deposit such funds in an account administered by the FTC or its agent for distribution purposes.

Based on the significant process made in the claims review and allowance process, and the existence of funds available for distribution to merchants and creditors, the Receiver has determined that it is appropriate at this time to (i) allow certain claims against the Receivership Estate (and disallow other claims), (ii) make payments from Receivership Estate funds to certain companies that leased terminal services for credit card processing ("Terminal Lease Companies") for the Receivership Defendants, and (iii) transfer certain of the Receivership Estate funds to the Federal Trade Commission (in particular, the FTC's redress contractor) ("FTC Redress Contractor") for payment on the allowed merchant claims. The FTC Redress Contractor would act as a distribution agent for the FTC and distribute funds to those holding allowed merchant claims in the full amount of the allowed claims.

By this Motion, the Receiver seeks authority to allow certain merchant claims against the Receivership Estate, to pay the Terminal Lease Companies for their services, and to transfer certain of the Receivership Estate funds to the FTC Redress Contractor for distribution to those certain merchants holding allowed claims.

The parties respectfully request that this motion also serve as the Status Report due on June 23, 2011.

II.

FACTS

A. The FTC Action

On April 11, 2007, the FTC commenced an action against the MPI Receivership Defendants and other individual defendants in this Court, for violations of Section 5 of the FTC Act, 15 U.S.C. Sec. 45. The FTC alleged in the action, among other things, that the MPI Receivership Defendants engaged in unfair or deceptive acts or practices in or affecting commerce, based on the business practices described below.

At least one of the MPI Receivership Defendants, MPI, acted as an Independent Sales Organization ("ISO"), which, in credit card business terminology, indicates that they served as a liaison between small business merchants who desired to accept credit and debit card payments and financial institutions that are members of card associations such as MasterCard and Visa. ISOs solicit merchants to establish accounts with the financial institutions into which the proceeds of merchants' card sales are deposited. For this service, merchants pay processing fees to the financial institutions, including a so-called "discount rate" that is a percentage of each sale they make.

The MPI Receivership Defendants used sales agents to solicit merchants to pay for the credit and debt card processing services ("Processing Services") through the MPI Receivership Defendants. According to the FTC, the MPI Receivership Defendants would typically quote a discount rate lower than the rate the merchants were paying for existing Processing Services, and make other representations concerning fees and rates which would purportedly result in significant savings to the merchants. The MPI Receivership Defendants also solicited merchants to lease terminal services (known as card swipe terminals), which obligated merchants to pay monthly lease payments to a third-party leasing company. The MPI Receivership Defendants made numerous claims associated with such solicitations, including that leasing the card swipe terminals through the MPI Receivership Defendants would allegedly result in substantial savings for the merchants.

Through its investigation, the FTC determined that the MPI Receivership Defendants' representations, in connection with its solicitations for Processing Services and terminal services, were deceptive in violation of Section 5(a) of the FTC Act, 15 USC § 45(a). Following completion of its investigation and findings, the FTC filed this action against the MPI Receivership Defendants (and later added, pursuant to an amended complaint, PPI Services, Inc., as a Receivership Defendant) and others.

On April 11, 2007, the FTC filed its complaint and motion for temporary restraining order ("TRO") and for appointment of a temporary receiver in this action. On April 11, 2007, the Court granted the request for TRO and for appointment of a temporary receiver, and Michael A. Grassmueck was appointed as temporary receiver as to the Receivership Defendants. On April 30, 2007, the Court issued a stipulated preliminary injunction against the Receivership Defendants and others, and continued the appointment of Michael A. Grassmueck as receiver in this action.

Pursuant to a Second PI, Defendants Karely McCarthy, a.k.a Karly Speelman and PPI Services, Inc., were added as defendants to this action. Pursuant to the Second PI, PPI Services, Inc., was added to the list of Receivership Defendants made subject to the provisions of the receivership, as outlined in the First PI.[1]

B. The First PI

Pursuant to the First PI, the Receiver was empowered with all powers of a federal equity receiver, which included, among others, the power to sell the assets of the Receivership Estate, determine the allowance of claims, through a claims review process, and make disbursements from the Receivership Estate as necessary and consistent with the powers and duties set forth therein.

C. Final Order

On April 30, 2008, the Court entered the Final Order, which authorized judgment against the Receivership Defendants, jointly and severally, in the amount of $26,480,041, and confirmed the continued appointment of the Receiver as set forth in the First and Second PIs (including, but not limited to, his powers to liquidate assets of the Receivership Estate). The Final Order further provides that the funds from the Receivership Estate will be paid to the FTC, and the FTC will deposit such funds in an account administered by the FTC or its agent for distribution purposes.

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[1] Hereinafter, the term "Receivership Defendants" is inclusive of Defendant PPI Services, Inc.

D. The Claims Motion

On February 18, 2010, in connection with his duties as equity receiver as set forth in the First PI, the Receiver filed a motion for order to approve claims procedures and for order establishing claims bar date ("Claims Motion"). Pursuant to Court order entered on March 2, 2010, the Court approved the Claims Motion, including the claims bar date of June 11, 2010 ("Claims Bar Date").

E. Merchants Claims Review and Allowance

For the Claims Bar Date, and claims procedures, the Receiver notified approximately 5,187 merchants (and other creditors) of the necessity of filing a proof of claim for the Receivership Estate in order to participate in any distributions from the Receivership Estate funds. In response to such notification, the Receiver received 124 filed proofs of claims ("First Merchant Claims"). The Receiver then began working with the FTC in checking the Receivership Estate's records to verify the correct amounts of such First Merchant Claims, and reviewing the documentary support provided to prove up the validity of the Claims.

Following the Receiver's and FTC's exhaustive and diligent review, the Receivership Estate determined that of the 124 First Merchant Claims filed, 106 should be allowed and paid in full (which total $953,104.86). The Receiver requests that the remaining 18 claims be disallowed. Attached hereto as Exhibit "A" is a reference chart showing those First Merchant Claims which will be allowed in full, and those First Merchant Claims which will be disallowed.

F. Secondary Merchants Claims Review Process and Allowance

After providing notification of the claims procedures and Claims Bar Date, the Receiver discovered that approximately 1,929 merchants ("Second Merchant Claims Group") were not notified of the requirement to file proofs of claim. The Receiver proceeded on April 4, 2011 to immediately mail proof of claim forms to the Second

Merchant Claims Group, and provided an extended Claims Bar Date of June 6, 2011 for these potential claimants.

From the second group, the Receivership Estate received an additional 23 proofs of claim ("Second Merchant Claims"), which total $58,514.78. The Receiver with the FTC's assistance is reviewing these Second Merchant Claims and determining whether these claims may be subject to allowance and payment in full. When the allowance decisions are made on the Second Merchant Claims, the Receiver will then request Court approval to transfer the appropriate amount of funds to the FTC Redress Contractor for distribution to the allowed Second Merchant Claims.

G. Terminal Lease Companies' Claims

In late 2010 through April 2011, the Receiver contacted the 7 companies that leased terminal services to merchants for credit card processing for the Receivership Defendants ("Terminal Lease Companies"). At the outset of the case, the Receiver advised the Terminal Lease Companies to stop all collection efforts against merchant customers of the Receivership Defendants.

The Receiver conferred with 5 of the 7 Terminal Lease Companies (as two of the companies were discovered not to have active mailing addresses or phone numbers). These Terminal Lease Companies agreed to cooperate with the Receiver on the amounts owed to them by the Receivership Estate, including waiving all penalties, interest and collection costs, and removing all negative credit reporting related to merchants which had engaged in business transactions with the Terminal Lease Companies (and also agreed to cooperate on any future corrections which would be needed if additional negative credit reporting is discovered). After reaching an agreement with the Receiver on payment of the Terminal Lease Companies for their services, they agreed to accept as full and final payment the amount of $760,065.05. Attached hereto as Exhibit "B" is a reference chart showing those Terminal Lease Companies, which will be paid in full for their services.

The Receiver and the FTC have approved payment of this sum to the Terminal Lease Companies, and the Receiver will pay this sum directly from Receivership Estate funds.

H. Current Cash on Hand in the Receivership Estate

The Receivership Estate is holding approximately $4.3 million in cash ("Estate Funds"). After transfer of the portion of the Estate Funds to the FTC Redress Contractor for distribution on the First Merchant Claims, and payment of the Terminal Lease Companies, the Receivership Estate expects to hold approximately $2.5 million in Estate Funds, which amounts will be available for payment of the allowed Second Merchant Claims and the Receivership Estate's administrative expenses (i.e., the Receiver's and his professionals' fees and expenses).

I. Current Status on Tax Issues

As indicated in the Status Report filed with the Court on February 10, 2011, the Receivership Estate was then awaiting the results of a refund claim in the amount of $197,000 from the IRS related to certain carryback of losses from year 2004 (related to MPI). The Receivership Estate now reports that the IRS has approved the refund claim and the Receivership Estate has received the tax refund. Final tax returns will be filed once all receivership activity is completed.

III.

THE COURT SHOULD APPROVE THE REQUESTED RELIEF

Pursuant to the Court's orders entered in this case, including the First PI, the Second PI, and the Final Order, the Receiver is authorized to seek this Court's order approving the allowance of the 106 First Merchant Claims in the amount of $953,104.86 (and the disallowance of the remaining First Merchant Claims). Based on the Receiver's review of the claims, and his recommendation to allow such claims, the Receiver requests that the Court allow these First Merchant Claims in the amount requested (and for the disallowance of the remainder of the First Merchant Claims).

With allowance of these First Merchant Claims, in the amount noted above, the Receiver requests that the Court authorize transfer of the portion of the Estate Funds necessary to the FTC Redress Contractor for payment of these claims and for payment of costs associated with redress distribution. The FTC Redress Contractor will make the distributions on such claims, pursuant to the provisions of the Final Order.

Further, pursuant to the Court's orders entered in this case, the Receiver is authorized to pay the Terminal Lease Companies in the amount of $760,065.05 for their services. Since the Receiver has determined that these services were indeed provided, and payment for these services is appropriate (based on the cooperation received from the Terminal Lease Companies, as noted above), the Court should approve the Receiver's request to pay the requested amount to the Terminal Lease Companies from the Receivership Estate funds for their services.

IV.

CONCLUSION

Based on the foregoing, the Receiver requests that this Court grant the Motion, and for such other relief as the Court deems just and necessary.

Dated: June 23, 2011

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