C

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

IN RE:	)	
EQUIPMENT ACQUISITION RESOURCES, INC.	)	Case No.: 09 B 39937
Debtor.	)	Hon. Susan Pierson Sonderby
WILLIAM A. BRANDT, JR., not individually but solely in his capacity as Plan Administrator for EQUIPMENT ACQUISITION RESOURCES, INC.,	)	
Plaintiff,	)	
v.	)	Adv. No. 11 A 2216
SHELDON PLAYER,	)	
Defendant.	)	

AFFIDAVIT OF PATRICK J. O'MALLEY

I, Patrick J. O'Malley, being duly sworn, depose and state as follows:

1. I am over the age of 18 and under no legal disability.

2. I work at Development Specialists, Inc. ("DSI") with William A. Brandt, Jr., who is the Plan Administrator of Equipment Acquisition Resources, Inc. ("EAR") pursuant to the Order of Confirmation entered by the Court on or about July 15, 2010 which approved the Second Amended Plan of Liquidation.

3. I have reviewed the books and records of EAR, which were turned over to Mr. Brandt in his capacity as Chief Restructuring Officer ("CRO") on or about October, 2009.

4. EAR was incorporated in 1997 under the laws of Illinois. EAR purportedly operated as a refurbisher of special machinery, a manufacturer of high-end technology parts, and a process developer for the manufacturing of high-technology parts. The bulk of EAR's revenue

was allegedly derived from the refurbishing and selling or leasing high-tech machinery. As set forth below, this revenue was almost universally the result of false, fraudulent sales transactions which occurred while EAR was insolvent.

5. The review of the books and records of EAR undertaken by me and others in my office under my supervision has revealed that the fraudulent transactions were the primary basis of EAR's revenue from as early as March of 2004.

6. EAR's fraudulent scheme generally involved it purchasing high-tech equipment near the end of its life-cycle at extremely low prices relative to the cost of a new unit. EAR then sold that same piece of equipment to a shill company at dramatically more than the price EAR had paid for the piece of equipment.

7. EAR concurrently entered into purchase and lease transactions with financial institutions interested in obtaining a better rate of return than is available in public markets. The shill company would sell the piece of equipment to the financial institution purchaser and then EAR would enter into a lease whereby EAR would pay lease payments to the financial institution purchaser. The purchase price was dictated by the artificial, high invoice issued by the shill company. Further, EAR commonly sold the same piece of equipment to multiple financial institution purchasers, and thus pledged that piece of equipment to the multiple financial institution purchasers or created fictitious pieces of equipment.

8. In 2009, after receiving numerous notices of default from its creditors, EAR sought the assistance of outside counsel and turn-around specialists in order to assist in the company's rehabilitation. After some investigation, EAR's outside counsel and consultants discovered evidence of potential fraud in the sale/leasing activity. The officers and Board of Directors resigned from their positions at EAR on October 8, 2009 and William A. Brandt, Jr. of

Development Specialists, Inc. was elected as sole member of the board of directors and as the Chief Restructuring Officer ("CRO").

9. The CRO was vested with the power to assume full control of all operations of EAR and all the powers and duties of the President, Chief Executive, and Treasurer of EAR. Pursuant to these powers, on October 23, 2009, the CRO filed EAR's voluntary Chapter 11 bankruptcy petition to manage EAR's assets for the benefit of all creditors.

10. Mr. Brandt is now the plan administrator of EAR's confirmed plan.

11. Under my supervision, Mr. Brandt's staff at Development Specialists, Inc. conducted a thorough analysis of the books and records of EAR and found the fraud to be extensive, primarily relating to recording fraudulent sales and purchasing activity that resulted in the massive overstatement of values for inventory, equipment, sales and stockholders' equity.

12. I have performed an analysis of the historical financial statements of EAR as of December 31, 2008, 2007, 2006 and 2005. EAR recorded equipment related assets on those financial statements in two ways: Equipment and Parts Inventory and Property Plant and Equipment. Our investigation and review of the assets of EAR has demonstrated that these two categories both describe the equipment controlled by EAR, including the equipment subject to lease and fraudulent equipment.

13. Exhibit 1 to this affidavit sets forth my solvency analysis, submitted in a different adversary proceeding but applicable to this proceeding, and supports my conclusion that EAR was insolvent since October 2005 and for all periods thereafter.

14. As a starting point, the creditors of EAR had a valuation completed of the inventory/equipment of EAR on hand as of the date Mr. Brandt became CRO. The current market value of the inventory/equipment held by EAR was estimated at approximately $3

million. This is less than 2.5% of the financial statement value of the inventory and equipment at December 31, 2008 of over $132 million. The reason for the large discount to book value is that most of EAR's transactions were fraudulent in nature and many of the assets identified on the financial statements were not, in fact, real. The inventory and equipment may have declined in value somewhat from 2005 until the date of the appraisal, but that decline is not material for purposes of my solvency analysis.

15. I subtracted valueless assets from the reported stockholders equity as of each of those dates. I then compared the remaining stockholders' equity to the value of equipment related assets recorded in the financial statements to determine how much value would need to be attributed to the equipment related assets in order for the company to be considered solvent.

16. The line titled "Valuation Percentage of Net Book Value of Equipment Related Assets Required for Solvency" indicates the percentage of the financial statement value of the equipment-related assets necessary for EAR to be solvent. With a market value as of December 31, 2009 of $3 million, it is clear that EAR was not even close to solvent from 2005 until its bankruptcy filing in 2009. The actual value of the equipment related assets is substantially less than what would be required for EAR to be considered solvent as of those dates.

17. Mr. Brandt has amended the tax return for the year ended December 31, 2006 to remove the fraudulent entries from the tax returns. The retained earnings included in the December 31, 2006 tax returns were reduced by $49,471,743 resulting in a negative shareholders' equity balance of $23,419,089.

FURTHER AFFIANT SAYETH NOT.

Executed on this 16 day of March, 2012.

Patrick J. O'Malley
PATRICK J. O'MALLEY

SUBSCRIBED and SWORN to before me
this 16th day of March, 2012.

Bethany J. Davies
NOTARY PUBLIC

OFFICIAL SEAL
BETHANY J. DAVIES
NOTARY PUBLIC, STATE OF ILLINOIS
MY COMMISSION EXPIRES 6-6-2015

EXHIBIT C-1

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION**

IN RE:	)	
EQUIPMENT ACQUISITION RESOURCES, INC.	)	Case No.: 09 B 39937
Debtor.	)	Hon. John H. Squires
WILLIAM A. BRANDT, JR., not individually but solely in his capacity as Plan Administrator for EQUIPMENT ACQUISITION RESOURCES, INC.,	)	
Plaintiff,	)	
v.	)	Adv. No. 10 A 2166
HARRAH'S ENTERTAINMENT, INC.	)	
Defendant.	)	

EXPERT REPORT OF PATRICK J. O'MALLEY

ASSIGNMENT

I have been asked to determine whether Equipment Acquisition Resources, Inc. ("EAR") was solvent or insolvent as of the dates of certain transfers that span the four years prior to its bankruptcy filing on October 23, 2009.

EXPERIENCE AND QUALIFICATIONS

I am a senior consultant and the Chief Financial Officer of Development Specialists, Inc. ("DSI"), a consulting firm that has provided management, turnaround and workout consulting, crisis management, financial advisory services and litigation support services including expert witness testimony for over three decades. DSI has offices throughout the United States including Los Angeles and San Francisco, California; Miami, Florida; Chicago, Illinois; New York, New, York; and Columbus, Ohio. I have been employed by DSI for over twenty (20) years.

My primary responsibilities at DSI involve advising clients and other constituents within a bankruptcy or troubled-company situation. I have acted as a Chief Financial Officer, Financial Advisor, Chapter 11 Trustee, Responsible Party and Examiner in bankruptcy proceedings. I have also acted as financial advisor to troubled businesses both within and outside of a bankruptcy proceeding. I have significant experience in circumstances of fraud and forensics accounting and have testified on solvency on three occasions: Avidus Trading LLC, Computer World Solution, Inc., and Commercial Loan Corporation.

I received my Bachelor of Business Administration with a concentration in Public Accounting from Loyola University of Chicago I am a licensed Certified Public Accountant (CPA) in the State of Illinois. My Curriculum Vitae is included as Exhibit 4 to this report.

EXPERT OPINION

In my opinion, Equipment Acquisition Resources, Inc. was insolvent beginning at least as early as December 31, 2005 and at all times thereafter. The definition of "insolvent" above is based upon:

Section 101(32)(A) of Title 11 of the Bankruptcy Code which states:

> "...with reference to an entity other than a partnership and a municipality, financial condition such that the sum of such entity's debts is greater than all of such entity's property, at a fair valuation, exclusive of – (i) property transferred, concealed or removed with intent to hinder, delay or defraud such entity's creditors; and (ii) property that may be exempted from property of the estate under section 522 of this title; ..."

The Illinois Fraudulent Transfer Act, 740 ILCS 160/3 which states:

> "(a) A debtor is insolvent if the sum of the debtor's debts is greater than all of the debtor's assets at a fair valuation."
>
> "(b) A debtor who is generally not paying his debts as they become due is presumed to be insolvent."

I formed my opinion based on my review of the documents included in Exhibit 3.

EQUIPMENT ACQUISITION RESOURCES, INC.

EAR is an Illinois Corporation, organized and existing under the laws of the state of Illinois and operated in several buildings near its headquarters at 555 S. Vermont Street, Palatine, Illinois. EAR purported to be a market maker in the semiconductor manufacturing equipment sales and servicing industry, and marketed and sold technologically advanced equipment to customers throughout the world. EAR also purportedly performed processing services for companies in the semiconductor industry.

NATURE OF THE FRAUD

EARs's fraudulent scheme generally involved it purchasing high-tech equipment near the end of its life-cycle at extremely low prices relative to the cost of a new unit. EAR then sold that same piece of equipment to a shill company, Machine Tools Direct, Inc. ("MTD") at dramatically more than the price EAR had paid for the piece of equipment.

EAR concurrently entered into purchase and lease transactions with financial institutions. MTD would sell the piece of equipment to the financial institution purchaser and then EAR would enter into a lease whereby EAR would make lease payments to the financial institution purchaser. The purchase price was dictated by the artificial, high invoice issued by MTD.

Further, EAR commonly sold the same piece of equipment to multiple financial institution purchasers, and thus pledged a piece of equipment to multiple financial institution purchasers or created fictitious pieces of equipment.

EAR received the proceeds from the lenders' purchase of the equipment - less a cut for MTD and used the proceeds to pay EAR's lease obligations, purchase non-business related assets, fund distributions to shareholders, and, inter alia, make direct payments to casinos for gaming activities by the principals of the company and others.

Evidence of the fraud goes back at least to 2003. For the period from 2005 through the date of the bankruptcy filing in late 2009, there appears to be a limited amount of legitimate business activity. Documents of representative fraudulent transactions are included as Exhibit 1.

MAGNITUDE OF TRANSACTIONS WITH MACHINE TOOLS DIRECT, INC.

As discussed above, the shill company in the fraud scheme was Machine Tools Direct, Inc. The method by which EAR recorded financial transactions with MTD was modified over the years, presumably in an attempt to conceal the fraudulent activity. Further, not all of the historical financial information was able to be located. Nevertheless, I was able to determine that the level of transactions with MTD were substantial throughout the periods in question as follows:

> 2005 – Approximately 86% of EAR's cash receipts in 2005 totaling approximately $30.2 million were received from MTD, corresponding to cash receipts from non-MTD customers of approximately $4.9 million. (Note that no sales registers were available for 2005).
>
> 2006 –Approximately 78% of EAR's sales in 2006 totaling approximately $43.4 million were to MTD / fraudulent customers corresponding to sales to ligitimate customers of no more than $6.6 million. It is likely that an additional portion of the $6.6 million figure represents additional fraudulent sales, however, that was not readily discernable from the information available.
>
> 2007 - Approximately 92% of EAR's sales in 2007 totaling approximately $50.5 million were to MTD corresponding to sales to non-MTD customers of approximately $4.4 million.
>
> 2008 - Approximately 97% of EAR's sales in 2008 totaling approximately $82.9 million were to MTD corresponding to sales to non-MTD customers of approximately $2.8 million.

Based upon analyzes performed, sales to legitimate customers were less than $7 million per year for calendar years 2005 through 2008.

HISTORICAL FINANCIAL STATEMENTS

The company issued for the years ended December 31, 2005 through 2008 financial statements that were prepared by an independent accounting firm, Von Lehman & Company ("Von Lehman"). These financial statements were audited by Von Lehman for the years ended December 31, 2008 and 2007 and were reviewed by Von Lehman for the years ended December 31, 2006 and 2005. These financial statements were not properly prepared in accordance with Generally Accepted Accounting Principles ("GAAP"), however, the balance sheet misstatements were generally limited to the valuation of i) amounts due from MTD, ii) inventory, iii) equipment under capital lease, iv) income taxes and v) transactions with insiders.

METHODOLOGY FOR VALUING ASSETS OTHER THAN INVENTORY AND EQUIPMENT UNDER CAPITAL LEASE

Assets (excluding Inventory and Equipment Under Capital Lease) per the historical financial statements were adjusted as follows as summarized in Exhibit 2:

Cash - No adjustments were made to the presented balances.

Accounts Receivable – No adjustments were made to the presented balances except for accounts receivable due from MTD. Transactions with MTD were generally fraudulent and any cash received from MTD was the direct result of EAR entering into an additional fraudulently induced lease with a financial institution. All accounts receivable due from MTD were valued at zero as accounts receivable from MTD would not have any value absent EAR entering into another fraudulent transaction.

Prepaid Expenses - No adjustments were made to the presented balances.

Property and Equipment (excluding Equipment Under Capital Lease) - No adjustments were made to the presented balances which were at cost less accumulated depreciation (net book value).

Deposits On Leased Equipment - No adjustments were made to the presented balances. This balance generally represents advance lease payments made to financial institutions pursuant to lease agreements.

Other Deposits - No adjustments were made to the presented balances.

Engineering Technology – EAR recorded an asset at December 31, 2006 in the amount of $908,267. This balance was written off by the auditors in 2007 "because there was no verifiable documentation to support their existence." The Engineering Technology balance was valued at zero as there was no support that it represented an asset.

Notes Receivable - No adjustments were made to the presented balances for amounts due from non-insiders. EAR recorded $10,350,000 note receivable from officers of the Company in 2008 that was valued at zero due to lack of ability to repay this note.

METHODOLOGY OF COMPUTING DEBTS

Liabilities per the historical financial statements were adjusted as follows as summarized in Exhibit 2:

Line of Credit - No adjustments were made to the presented balances.

Installment Notes Payable - No adjustments were made to the presented balances.

Accounts Payable - No adjustments were made to the presented balances.

Customer Deposits - No adjustments were made to the presented balances.

Accrued Expenses - No adjustments were made to the presented balances.

Capital Lease Obligations - The capital lease obligations represent the recognition of the liability EAR has for remaining payments due under leases recorded on a present value basis. The recognition of this obligation as a liability along with a corresponding asset on the balance sheet is required under GAAP if the lease meets certain criteria which indicate that lease is more of a financing transaction rather than a lease transaction. Most of EAR lease transactions include a buyout at the end of the lease term at the bargain purchase price of $1, which is an indication of a financing transaction.

There has been no indication that the capital lease obligations were not properly recorded in the financial statements. Accordingly, no adjustments were made to the capital lease obligations.

Operating Lease Obligations - EAR also entered into operating type leases in increasing values during the periods in question. The values of these leases were not reflected in the balance sheets rather lease payments would be recorded as expense over the term of the lease. Rent expense recorded on equipment operating leases in the historic financial statements were as follows:

2005 -	$295,496
2006 -	$1,500,000
2007 -	$7,958,294
2008 -	$15,900,485

These leases represent additional debts of EAR with no corresponding consideration to EAR since the underlying asset, if it existed, was not worth the value represented in the leasing transaction. For purpose of determining EAR's debts, the remaining lease payments have been discounted at a 6.3% to 8.0%, based upon an average of financing leases incurred each year, to determine the present value of the obligations. The amount of the debt assigned to the operating leases is as follows (December 31,):

2005	$0
2006	$12,060,639
2007	$34,276,469
2008	$52,066,378

Notes Payable – Stockholder - No adjustments were made to the presented balances. EAR recorded a $2,526,925 note payable to Stockholder as of December 31, 2005. This liability was satisfied in 2006 by transferring assets to the Stockholder.

Income Taxes Payable - If the historical financial statements of EAR are restated to exclude the fraudulent sales transactions, there is no taxable income and no taxes payable. Accordingly, all of the income tax liability accounts have been reduced to zero. The computation reflects an asset for the amount of taxes that had been previously paid EAR as those amounts would generally be refundable if the taxable income had been reported properly as a loss.

Fair Market Value of Interest Rate Swap - No adjustments were made to the presented balances.

Deferred Income Tax Liability - If the historical financial statements of EAR are restated to exclude the fraudulent sales transactions, there is no taxable income and no taxes payable. Accordingly, all of the income tax liability accounts have been reduced to zero.

FAIR VALUE OF ASSETS VERSUS DEBT BEFORE CONSIDERING INVENTORY AND EQUIPMENT UNDER CAPITAL LEASES

Based upon the above computations summarized in Exhibit 2, debts exceed the fair value of assets before considering Inventory and Equipment Under Capital Lease as follows:

December 31, 2005	$31,057,109	Exhibit 2- A
December 31, 2006	$46,939,303	Exhibit 2 - B
December 31, 2007	$65,073,625	Exhibit 2 - C
December 31, 2008	$116,090,271	Exhibit 2 - D

VALUE OF INVENTORY AND EQUIPMENT UNDER CAPITAL LEASE

Nature of Inventory - EAR's inventory balance was comprised of parts and equipment. The inventory parts allegedly supported both the processing and the refurbishing businesses. Each year EAR would transfer the net book value of equipment from the category of *Equipment Under Capital Lease* to the *Inventory* category, according to the audited financial statements, "...when it is no longer being used by the Company for research and development processes, and the related capital lease has been paid in full." This indicates that the equipment had minimal value at the time of the transfers.

Transfers from *Equipment Under Capital Lease* to *Inventory* made during the periods in question are as follows (for the year ended):

	For the year	Cumulative from 2005
2005	$8,640,051	$8,640,051
2006	$7,862,043	$16,502,094
2007	$7,431,500	$23,933,594
2008	$6,686,566	$30,620,160

Primarily as a result of the previously discussed transfers, EAR's inventory balance increased significantly during the periods in question as follows per the historical financial statements (December 31,):

2005	$21,637,561
2006	$27,645,015
2007	$31,922,906
2008	$43,425,524

Nature of Equipment Under Capital Lease - The equipment acquired by EAR pursuant to capital leases was allegedly used in the operation of its purported processing business. EAR's processing business was very limited, if it existed at all. The leased equipment was the exact same equipment that the company supposedly refurbished as part of its equipment resale business.

As the fraud continued, the balance recorded in the historical financial statements for *Equipment Under Capital Lease*, net of accumulated depreciation, increased significantly during the periods in question as follows (December 31,):

2005	$37,964,209
2006	$42,171,696
2007	$56,563,700
2008	$88,941,274

The *Equipment Under Capital Lease* account represents the fraudulent lease transactions that were active leases. The value of the fake equipment and the inflated value of equipment reflected in the fraudulent lease transactions for leases that had been paid off were transferred to the *Inventory* account.

Value of Inventory and Equipment Under Capital Lease

A physical count of equipment performed in late 2009 demonstrated that EAR possessed less than half of the pieces of equipment reflected in the financial statements. This is consistent with EAR's practice of changing serial numbers of pieces of equipment to facilitate leasing one piece of equipment from multiple financial institutions.

EAR abandoned its inventory and equipment to is lenders in late 2009. At the time of the abandonment, the inventory and equipment had a net book value of over $130 million. In February 2011, an auction of EAR's inventory and equipment was conducted and the sales reconciliation report shows that the gross proceeds were approximately $6.9 million, or a little more than 5% of the net book value. The auction proceeds received (representing just a small fraction of the net book value) is consistent with the nature of the fraud whereby a shill was used to fraudulently induce financial institutions to enter into equipment leases at huge multiples to actual value or where the underlying equipment did not even exist.

Based upon the above discussions, the fair value of the combined inventory and equipment of EAR would be far less than the amount that would be required to make EAR solvent based on assets versus debts tests as of the following dates.

December 31, 2005	$31,057,109	Exhibit 2- A
December 31, 2006	$46,939,303	Exhibit 2 - B
December 31, 2007	$65,073,625	Exhibit 2 - C
December 31, 2008	$116,090,271	Exhibit 2 - D

CONCLUSION

Based upon my analysis as described above, my opinion is that the sum of EAR's debt exceeded its assets at a fair valuation at December 31, 2005; December 31, 2006; December 31, 2007; and December 31, 2008.

I did not attempt to analyze assets and debts for interim periods between the calendar year ends described above, however, I noted no transactions that would suggest that the financial condition of EAR changed in the interim periods between the ends of the calendar years referred to in the preceding paragraph.

My opinion is that EAR would not have been able to continue in business in 2005 through 2009 without new funds generated from additional fraudulent lease transactions. Accordingly EAR was not able to pay its debts as they become due in the normal course of business in 2005 through 2009.

Therefore, my opinion is that EAR was insolvent beginning at least at December 31, 2005 and for all periods thereafter under the definitions of the Bankruptcy Code and the Illinois Fraudulent Transfer Act.