Senate Testimony of Henry Camferdam

1. Good Morning. My name is Henry Camferdam. I live in Carmel, Indiana. I appreciate the opportunity to talk to you today. I have been looking forward to this opportunity for quite awhile.

2. I want to talk to you about two areas:

    a. My involvement in what I was told was a legal tax savings strategy known as "COBRA"; and

    b. what action I would like to see taken against the people who designed, promoted and sold me this tax strategy.

3. In the early 1990s, I started a company called Support Net, Inc. (" Support Net"). Over time, this company became a tremendous success. In 1995, Support Net hired Ernst & Young ("E&Y") to work on various state sales tax issues.

4. In early 1996, Jeff Adams and I, on behalf of Support Net, hired E&Y to do Support Net's audit & tax work. E & Y designated Jay Heck as the lead audit partner and Wayne Hoeing as the senior tax manager.

5. On or about February 26, 1996, Carol Bockelman Trigilio was hired as Support Net's CFO on the suggestion and /or reference of Jay Heck at E&Y, where she formerly worked in their Entrepreneurial Audit Services Group.

6. In the summer of 1996, Support Net, because of its capital needs due to its rapid growth, began discussions with E&Y about E&Y assisting Support Net with

finding potential investors or a buyer.

7. This culminated on or about August 26, 1996, with Support Net signing an engagement letter agreement for E&Y to prepare a Senior Offering Memorandum.

8. In October 1996, E&Y began soliciting potential buyers/investors with the Senior Offering Memorandum it had prepared. Support Net initially went to market to raise capital to grow the business, because it was, at that time, one of Indiana's fastest growing companies. Support Net went from $50 million to $500 million in sales in 3 years.

9. The process, however, culminated not just in raising capital but rather in a sale of the business to Gates/Arrow Distributing, Inc., a division of Arrow Electronics, Inc ("Arrow"). On or about June 9, 1997, Support Net received a Letter of Intent from Arrow.

10. On or about October 16, 1997, a definitive Agreement between Arrow and Support Net was announced on Wall Street, followed by a sale in December of that year of 50.12% of Support Net to Arrow. E&Y received a commission for this sale of approximately $900,000.00.

11. E&Y was also the audit/tax professionals for Arrow. The local E&Y office in Indianapolis (Jay Heck and Wayne Hoeing) continued to perform the audit and tax work for Support Net, in conjunction with their peers in New York assigned to Arrow.

12. All amounts from the sale of Support Net received by Jay Michener, Jeff Adams, Carol Trigilio and me (collectively, the " Partners") in 1997 and 1998 (and these

amounts were in the millions) were duly reported on both federal and state tax returns, and tax was paid. E&Y prepared the tax returns for me, Jeff Adams, Support Net, and BAMC, LLC (which held the Partners' interests in Support Net). Prior to the COBRA tax strategy sold to us by E&Y, none of us had ever been involved in a tax shelter of any sort, and we had always reported and paid the taxes we owed.

13. Unfortunately, a business dispute arose between Arrow and BAMC, LLC . In March 1999, BAMC, LLC and the Partners filed a lawsuit in federal Court in New York against Arrow and others for, among other things, breach of contract and fraud.

14. In the late summer of 1999, we at Support Net worked with Wayne Hoeing of E&Y and tax professionals at Arthur Anderson to evaluate the tax and business impact of settlement offers we received from Arrow.

15. In August 1999, we received and accepted a settlement offer from Arrow for in excess of $70 million cash, in exchange for a sale to Arrow of the remainder of Support Net not previously sold. E&Y was aware of this settlement, as we had been staying in touch with them frequently to consider the tax impact of any settlement offer.

16. In addition, all four of the Partners had consulted with Wayne Hoeing of E&Y during this same time frame as to what tax payments should be made (and when). Wayne advised us that Federal estimated taxes were to be paid by January 15, 2000, and state estimated taxes were to be paid prior to December 31, 1999, so they could be itemized on our 1999 Federal returns. Also, in September 1999, we

consulted with Wayne and worked through Third Quarter estimated taxes and again confirmed tax payments for the Support Net sale. The four of us fully intended to report and pay the taxes owed, as we had always done in the past. We had actually set aside the money we needed to pay the taxes and the rest was invested.

17. In late October 1999, Wayne contacted Carol about a potential tax saving strategy to benefit me due to my large capital gain on the sale of Support Net. Carol informed me that Wayne briefly presented the idea to her: for gains over $50 million in 1999, worked whether the gains were ordinary or capital, involved foreign currency options, and took advantage of a "tax loophole" that he did not specifically describe. According to Wayne, the strategy would eliminate all capital gains taxes, thus saving me millions. Carol suggested that he call me directly. After I spoke with Carol about her conversation with Wayne, I told Jay Michener and Jeff Adams generally about my conversation with Carol.

18. As suggested by Carol, Wayne called me about the potential tax saving strategy. During our discussion, I suggested to Wayne that all four of the Partners meet with E&Y to see their presentation of the idea, since all of us had gains on the sale. Wayne told me then of the urgency: that we needed to start the transaction within the next week to ten days because the transaction took about 6-8 weeks to complete and that it needed to be completed prior to the end of 1999. As a result, we agreed to meet with E&Y on or about November 5, 1999, to hear the details of the strategy.

19. On or about November 5, 1999, the Partners met with Wayne Hoeing, Brian

Upchurch, and Carl Rhodes of E&Y at E&Y's Indianapolis office. There was no one else present (*i.e.*, no one from Jenkens & Gilchrist or Brown & Wood). With the exception of having to sign a short confidentiality agreement as soon as we arrived (before anything else took place), it was a typical casual meeting for us with Wayne, with whom we had a long-standing relationship. Carl was there at the suggestion of our broker, Dave Knall. Dave had known Carl for years and felt his judgment was conservative and could be trusted. Wayne and Carl brought Brian to the meeting: Brian actually conducted the meeting and seemed to be the most knowledgeable about what was being discussed; it appeared that Wayne and Carl were really present more for client relations, than for any substantive knowledge they might have.

20. The meeting on or about November 5,1999, lasted one to two hours. Primarily, it was a PowerPoint presentation presented by Brian Upchurch. Brian appeared to be the lead contact in Indianapolis for the COBRA transaction; according to the Power Point, COBRA stood for "Currency Options Bring Reward Alternatives." Wayne and Carl, to a lesser extent, assisted with answering our questions and in giving their take on the strategy. We asked many types of questions, because none of us understood the deal. In response, Wayne and Brian stated, "That's why you have us." I depended on Wayne to tell us if this transaction was valid and appropriate for us. Wayne advised us that they could make this transaction work for us. Wayne told us this was a valid tax shelter; that the tax shelter would be upheld if we were audited; and that Ernst & Young would defend us up to Court. They also showed us an opinion letter from Jenkens & Gilchrist during the

presentation, which we were told was "insurance" in the event of an audit. They also suggested we obtain a second legal opinion just to make sure. They informed us they had another law firm, Brown & Wood, which could provide us with a second legal opinion. We weren't allowed to keep any of the materials discussed in this meeting.

21. During the November 5, 1999, meeting, we contacted Steve Humke, our attorney at the Ice Miller firm in Indianapolis and requested he join us in the meeting. He could not join us at that time. Carl and Brian later visited Steve's office. I spoke with Steve after their meeting. Steve told me that the meeting lasted almost one hour. Steve also told me that Carl and Brian would not permit him to bring in an Ice Miller tax expert or any other attorney. Steve had to sign the same confidentiality agreement we did. They let him briefly look at the Jenkens opinion. According to Steve, the meeting was "rushed". Steve told me that he could not render an opinion on the transaction, as Carl and Brian wouldn't even let him keep the opinion to review. Steve advised me that Jenkens & Gilchrist was a large, reputable firm and that we would have to rely on our relationship with E&Y for direction.

22. Following the meeting on or about November 5, 1999, Wayne picked the "loss" I needed to generate. The loss was almost in alignment with the prior ownership of BAMC, LLC (which had held the shares of Support Net and was owned by the Individual Plaintiffs).

23. Wayne told me they were in a hurry to get the deal done. As a result, a few days later, I believe on or about November 9, 1999, the four of us met Wayne Hoeing

and several other individuals at Twin Lakes Golf Course before Jeff, Jay, and I were to play golf. Because of the urgency, Wayne wanted to squeeze the meeting in before our tee time. The purpose of the meeting was to sign all the paperwork to start the implementation of the tax strategy, including transactional documents and a two page engagement agreement (the "Engagement Agreement") between each of us and E&Y. The meeting only lasted 30 minutes or so. No copies of the documents were given to us at that time – Wayne said they would be mailed to us later. Although the transactional documents were later sent to us in a binder, the Engagement Agreement and the promotional materials used during the meeting were never sent to us. I did not understand the transaction. During this meeting, Jay asked Wayne, "What is this strategy?" Wayne responded by saying, "It is already done, don't worry about it."

24. No time was spent at this meeting on or about November 9, 1999, discussing the documents, as Wayne continued to tell us that we needed to go forward with the strategy immediately to have it completed by the end of the year. He appeared to be in a hurry to get the deal done, and, in fact, acted as though the deal was done. Trusting Wayne, I quickly signed the voluminous documents, which included documents for the formation of limited liability companies for each of the four of us, a partnership known as Carmel Partners, and an S-corp called BAMC, Inc. I viewed it as like closing a mortgage loan, where it was sign the documents or go to another lender, except that in this case E&Y was the only party we knew of who could eliminate our taxes, in their words, "legally and conservatively." I also knew that I didn't have the time to show the Engagement Agreement to Steve

Humke or another lawyer, and was led to believe that because of all the confidentiality surrounding the strategy that wasn't really an option anyway.

25. Through the rest of November and December of 1999, we did as instructed by E&Y to implement the tax strategy known as "COBRA." I also had a brief conversation with David Parse at Deutsche Bank at which time David Parse picked the options for us (the "Euro" for me, the "Yen" for the others) because I had no idea what to do. We also signed and sent Deutsche Bank accounts forms on which they had already filled in information about our supposed investment experience before sending them to us.

26. In early December 1999, the four of us received engagement letters from Jenkens and Gilchrist. I signed and returned mine. I **never** talked to anyone at Jenkens and Gilchrist, and this is the only agreement we had with them about the work they were doing for us.

27. On or about December 22, 1999, we sent, as directed, a wire to E&Y from Carmel Partners' account for $1,056,000. On December 29, 1999, we sent, as directed, a wire to Jenkens & Gilchrist from BAMC, Inc.'s account at Duetsche Bank for $2,012,000.

28. On or about June 20, 2000, we received a letter from Brian Upchurch of E&Y transmitting to us a package containing the Brown & Wood opinion (dated March 9, 2000), a request for each of us to sign an engagement letter with Brown & Wood, other materials, and a request for us to send payment to Brown & Wood. I never talked to anyone at Brown & Wood. In fact, all of their documents were sent to us via E&Y – not directly to us. I never intended, expected, or contracted

to arbitrate with Brown and Wood regarding the COBRA transaction. We initially didn't want to pay Brown & Wood because their opinion letter was received so late; however, Brian Upchurch with E&Y told us if we didn't pay Brown & Wood they would probably "turn us in" to the IRS. On October 2, 2000, we mailed a payment of $75,000 to Brown & Wood.

29. In March 2002, E&Y sent me a letter informing me about a "Tax Amnesty Program" offered by the IRS. This letter was followed-up by a telephone call with E&Y wherein E&Y advised me not to participate in the "Tax Amnesty Program". During the discussions where E&Y told me not to participate in the Tax Amnesty Program, E&Y did not inform me about the existence and implications of IRS Notice 2000-44, which I later came to understand was directed at COBRA and similar transactions that indicated the IRS did not believe those transactions were lawful. Following the advice of my accountants, I did not enter the Tax Amnesty Program.

30. On approximately June 6, 2002, Wayne Hoeing of E&Y informed me by letter that the IRS was investigating E&Y and was demanding the production of broad categories of documents and other information with regard to the COBRA transaction I did.

31. E&Y informed me that E&Y had received administrative summons from the IRS and that in the opinion of E&Y, documents and information in their files pertaining to the professional services they had rendered to me in connection with the COBRA transaction were responsive to the summons.

32. In a letter dated June 6, 2002, signed by Wayne Hoeing of E&Y, I was informed

that E&Y would produce documents and information regarding the transaction I had done if no objection was received. I informed E&Y the same day that I objected to the disclosure of any information about me, including my name and any documents related to the transaction I had done.

33. In September 2002, E&Y informed me that, on the advice of their outside counsel, they planned on disclosing my name to the IRS but promised that no documents would be produced and that E&Y would notify me if the IRS required production of my documents.

34. On approximately September 5, 2002, a suit was filed in the Northern District of Illinois seeking to prevent E&Y from disclosing to the IRS the identify of individuals that had completed the COBRA transaction. There were several hearings in connection with this lawsuit. E&Y at no time informed me that they believed the Court had permitted them to disclose my name to the IRS or that they intended to do so immediately. Unfortunately, on approximately September 24, 2002, E&Y voluntarily disclosed my name to the IRS. E&Y's disclosure of my name to the IRS was done in express violation of the instructions I had given to E&Y not to disclose my identity, documents, information, or any communications to the IRS without my consent, which was never given. No Court ever ordered E&Y to disclose my identity to the IRS. The bottom line is that E&Y was more worried about protecting themselves and currying favor with the IRS than protecting the rights of their clients.

35. I want to emphasize the following points to the Committee:

a. E&Y and Jenkens & Gilchrist took advantage of a long-term relationship I

had with E&Y. E&Y and Jenkens & Gilchrist took advantage of the trust and confidence I had for E&Y. E&Y and Jenkens & Gilchrist took advantage of E&Y's knowledge of my financial condition. I did not approach E&Y for this tax strategy; rather, they approached me. I fully intended to pay the taxes I owed on the gain from the sale of my company.

b. I was never made aware of the actual relationships and roles of E&Y, Jenkens & Gilchrist, and Deutsche Bank with respect to COBRA. For instance, E&Y informed me that COBRA was an E&Y tax strategy. I now know that COBRA was a Jenkens & Gilchrist tax strategy. E&Y informed me that Jenkens & Gilchrist was an "independent" law firm that would review the tax strategy and write an opinion letter supporting the strategy, which would protect me from penalties in the event of an audit. This was untrue. I now know that Jenkens & Gilchrist was not an "independent" law firm since Jenkens & Gilchrist designed, created and promoted this tax strategy. Finally, I was not aware that E&Y, Jenkens & Gilchrist, and Deutsche Bank met before marketing COBRA to determine how to split the fees up among them.

c. E&Y told me not to enter the IRS Amnesty Program. However, a short time later E&Y turned my name over to the IRS without my permission.

d. Neither E&Y nor Jenkens & Gilchrist explained to me that existence and significance of various IRS Notices, which indicated that the IRS would disallow COBRA. If I had been informed of the existence and significance of this information, I would not have done the tax strategy to

begin with and certainly would have entered the Amnesty Program when it was offered by the IRS.

e. E&Y and Jenkens & Gilchrist used high pressure sales tactics to sell me the COBRA. E&Y also emphasized the need for me to "trust them". My trust in E&Y resulted in this ordeal I am now in.

f. I have always paid my taxes. In fact, I paid the taxes I owed from the initial sale of part of Support Net. I would have paid the taxes I owed on the gain from the sale of the rest of Support Net; however, my trusted legal and tax advisors placed me in a tax savings strategy that they represented was completely legal. Since I had never entered into a tax shelter and had never been audited, I relied on the advice and recommendations of E&Y and Jenkens & Gilchrist.

36. In closing, I have several questions for the Committee:

a. While I and other taxpayers in this situation have been subjected to tough talk about penalties and interest, E&Y, Jenkens & Gilchrist, and Deutsche Bank have not come under scrutiny for their conduct. Why have you not brought action against E&Y, Jenkens & Gilchrist, Deutsche Bank, and others that marketed these tax shelter products to trusting individuals like myself?

b. Why are E&Y, Jenkens & Gilchrist, and Deutsche Bank allowed to keep hundreds of millions of dollars in fees that were paid for these transactions, while the participating tax payers are currently undergoing extensive and expensive audits?

c. What is being done to make E&Y, Jenkens & Gilchrist, and Deutsche Bank accept responsibility for their conduct?

d. What can be done to protect future taxpayers from being in the position I and many others are in: having to pay one group of lawyers to defend me from the IRS, and another group of lawyers to assert my civil claims against the promoters who talked me into this strategy?