

Court documents show depth of financial loss for those invested in Humboldt Creamery

Public records show major cash flow problems with CEO and CFO depositing personal funds

(Originally published in the 6-11-09 edition of The Ferndale Enterprise. Copyright.)

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Outside investors were writing checks to Humboldt Creamery just two days before former CEO Rich Ghilarducci resigned and his lawyer warned of possible financial irregularities, warning the company it should perhaps suspend its offering of \$5 million in preferred securities.

Meanwhile, the CEO and CFO were depositing personal checks to cover cash flow three weeks before Ghilarducci departed.

Details made public by the federal bankruptcy court and available on the Internet show that \$370,000 in Preferred Series B notes were sold in February, 2009. All eight notes sold were deposited between February 3 and February 18. Ghilarducci resigned on February 20 and left for Arizona.

On February 18 \$30,000 was received by the creamery and deposited from Richard

and Betty Littlefield. On February 17, \$20,000 was received from Pam Ford Cavanaugh and \$50,000 from Jim West. On February 10, \$10,000 was received from David Lem and Evelyn Giddings and \$40,000 from John Petrusha. On February 6 \$20,000 was received from Jerry Carlson and on February 5, a check for \$100,000 was received from Jerome Davis and on February 3, a check for \$100,000 from the Becker Insurance Agency.

The notes were unsecured and are now part of perhaps as much as \$30 million owed unsecured creditors who are lining up behind the \$54 million in debt owed to secured bank loans.

Meanwhile, another \$3.6 million in unsecured notes dating back to 2003, many with maturity dates of this year, are listed in the court as unsecured non-priority claims. The names listed on the notes range from producers, including current board members and their children to other relatives. Several employees, including former CEO Ghilarducci, along with his

wife, hold more than \$283,000 in notes.

The creamery's interim CEO Len Mayer said the notes to Ghilarducci were in exchange for \$200,000 received from the former CEO to "cover payables" in February 2008. The money was turned into a three-year member note, paying 7.5 percent interest.

Meanwhile, in the month prior to his resignation, listed in court records under an exhibit of "payments to insiders within the last year," Ghilarducci received two checks on January 8 and January 15 for a total of \$125,125. Mayer again confirmed they were reimbursements for personal checks Ghilarducci wrote to cover shortfalls.

In an exhibit of payments in the last 90 days submitted to the court, three reimbursement checks of \$47,000, \$69,000 and \$34,000, totaling \$150,000 were written to Ghilarducci from the creamery on January 28. The checks were voided on January 31. On January 29, one check in the amount of \$150,000 was again writ-

ten to Ghilarducci from the creamery. It was voided on January 30.

Mayer said the creamery checks — reimbursements for Ghilarducci's checks to cover cash flow — were voided because his personal checks did not clear.

On January 29 a creamery check reimbursing CFO Tony Titus for a personal check of \$100,000, was written. Mayer said the check to the creamery from Titus was written on the CFO's home equity line of credit to cover cash shortfalls. The checks from Titus and to Titus were written all in one day, "which was the plan," said Mayer.

Titus confirmed Mayer's explanation.

Mayer called the use of personal funds to cover cash flow "unusual.

"You don't want to get to that point, ideally," he said. "We had a \$31 million line of credit and usually, you'd want some of that in reserve."

That line of credit, however, was tapped out in December, said Mayer, unbeknownst to any other executives and the board,

he said, adding that he had "heard that cash has been tight at the creamery for years, but not that critical.

"I have been told that is because we ran more or less on a shoestring because the mission of the creamery was simply to return money to the farmers/owners, not to make a huge profit itself," he said. "Obviously there was much more going on than this."

Mayer added that "sure" the CFO believed the audited financial statements.

"Those statements showed a company with a lot of debt that does lead to cash pinches from time to time, but it's something you believe you'll be able to work your way out of."

Creamery board member Dennis Leonardi said he was astonished to hear of executives using personal checks to cover cash flow.

"Everyone could sit there and not raise a question to the board?" he asked, adding that the board only knew about checks bouncing after Ghilarducci resigned and they looked at bank statements.

"If you're making a profit and have huge depreciation, why don't you have the cash?"

Fellow board member Blake Alexandre said he, like others, was unaware of the serious nature of the cash flow problem, although he does understand big businesses having shortages.

"I run a big business," he noted. "I understand how cash flow works and doesn't work. If Tony was doing it on our behalf and had good intentions," said Alexandre. "Did we as board members have a clue? Absolutely not. We were absolutely in the dark about this."

Alexandre said knowing that the "guy in control and the guy that kept it a secret," referring to Ghilarducci, was using personal checks and getting reimbursed "would have triggered red flags with me.

"We would have looked into this whole thing with a whole lot more detail," he said.