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3:04-CV-02295 SEC V. EMVEST MORTGAGE FUND

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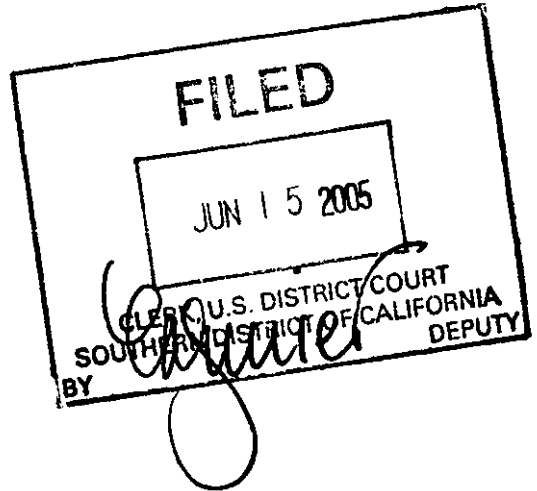
David R. Clark
Partner

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May 26, 2005

VIA HAND DELIVERY TO CHAMBERS

United States Magistrate Judge Louisa S. Porter
Courtroom No. H
United States District Court
880 Front Street
San Diego, CA 92101



RE: Securities and Exchange Commission v. Emvest Mortgage Fund, LLC, et. al.
Southern California District Court Case No. 04cv2295 DMS (POR)

Dear Judge Porter:

As you know by now, we represent a third-party witness, Unified Mortgage Service, Inc. ("UMS"). Pursuant to your order allowing one, please consider this letter to constitute our surebuttal brief to the reply letter brief dated April 22, 2005, which was directed to Magistrate Judge Papas by the Securities and Exchange Commission ("SEC").

I. Background to this Motion

On our about December 29, 2004, the SEC served a document subpoena on non-party witness, UMS. UMS timely responded to that subpoena on January 12, 2005. A copy of that response, which also contained the actual document requests, was attached as Exhibit 3 to the letter brief submitted to Magistrate Judge Papas by UMS on April 15, 2005, opposing the SEC's motion to compel. Since that time, UMS has either produced all documents it indicated would be produced, or provided the SEC (and/or the Receiver) with access and opportunity to copy those documents.

UMS is the loan servicing agent for lenders making loans through the Emvest Fund. Accordingly, the documents produced consist essentially of all of the borrower files maintained by UMS and lender statements of account.

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After counsel had engaged in good faith meet and confer sessions, without reaching agreement on whether or not the SEC was entitled to have any more documents from UMS, the SEC made a motion to compel pursuant to its letter directed to Magistrate Judge Papas on March 9, 2005. On behalf of UMS, we responded by our letter brief to Magistrate Judge Papas dated April 15, 2005.

The primary grounds for our opposition are set forth in that April 15th letter brief, to which we respectfully refer this Court. The SEC replied to our opposition by its letter brief dated April 22, 2005, to which this surrebuttal is directed.

II. UMS Is Not A "Related Entity" to Any of the Named Defendants

It is important again to emphasize that UMS is not a party to this action. Moreover, this action has now been pending for more than six months, and the SEC has made no motion, nor evidenced any intention, to name UMS as an additional defendant. UMS remains merely a third-party witness, having custody of some documents potentially relevant to the SEC's securities fraud allegations against the defendants, solely by virtue of UMS being the loan servicing agent for lenders funding loans through the Emvest Fund portfolio.

Contrary to the SEC's first contention, UMS has provided undisputed and indisputable evidence that it is not related to any of the named defendants. We attach as Exhibit "1" hereto, an updated declaration of Michele A. Canty which was filed on May 13, 2005. It is similar, but more extensive than the one submitted by Ms. Canty on December 3, 2004, which was attached as Exhibit "5" to our April 15th submission.

The named defendants in this action are the Emvest Mortgage Fund, LLC; Emvest, Inc.; and Milton Lyle Brock. Ms. Canty is (and always has been) the one hundred percent shareholder of UMS since she purchased the company in 1995. She is also the president and sole director of UMS. None of the three named defendants have any ownership interest in UMS. None of the named defendants are officers or directors of UMS.

There is no evidence currently, and there never will be any, contrary to Ms. Canty's declaration. If it hasn't done so already, the SEC could subpoena the California Secretary of State or the Department of Corporations and confirm the stock ownership of UMS, as well as its officers and directors. Thus, it is indeed true that UMS is an unrelated, innocent entity in this matter.

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III. UMS Is Not An Affiliate of Any of the Defendants

Contrary to the SEC's second contention, UMS is *not* "affiliated" with any of the named defendants. In terms of technical securities law definition of affiliation, UMS obviously has none, because none of the three defendants are owners, officers, or operators of UMS. Applying even a more liberal definition of affiliation still would not help the SEC at all here. UMS, as an entity, has no affiliation/relationship with either Emvest, Inc. or Mr. Brock at all. UMS' only affiliation/relationship with the Emvest Mortgage Fund is its vendor relationship as the loan servicing agent for lenders funding loans through the fund. However, for securities law purposes and/or discovery purposes, an entity does not become "affiliated" with one of the named defendants merely by doing business with one of the named defendants. The SEC has cited no case, and no case goes that far.

The SEC next argues that "the defendants" have consistently represented that UMS is affiliated with the Fund. It is ironic, to say the least, that the SEC now purports to rely on the truth of the defendants' supposed representations in that regard, while at the same time prosecuting the same defendants for misrepresentations so serious as to amount to securities fraud. In any event, no such representations were ever authored or approved by UMS, and Ms. Canty has already testified in her declarations that to the extent advertisements supposedly tied UMS somehow to the fund, they were mistaken. Once again, there is absolutely no evidence to the contrary.

IV. There Is No Common Ownership Between UMS and Defendant Emvest, Inc.

There is absolutely no common ownership between UMS and Defendant Emvest, Inc. In a somewhat misleading assertion, the SEC nevertheless argues that because Ms. Canty has a community property interest, by virtue of her marriage to Tim Canty, to shares of stock of Emvest, Inc., that happenstance somehow constitutes "common ownership between UMS and Emvest, Inc." Not only does such a contention ignore reality, UMS itself is owned by Ms. Canty outright as her separate property, having been acquired before her marriage. Thus, there is no common ownership between UMS and Emvest, Inc., and there is no evidence to the contrary.

In the interest of full disclosure, it is true that Mr. Brock is Ms. Canty's father and Tim Canty, an executive of Emvest, is her husband, but neither of them have any role or involvement with UMS. The happenstance of having a father and a husband does not *ipso facto* make the daughter/wife an alleged co-conspirator, or an aider or abettor of alleged securities law violations. Nor does it make her separate company, UMS, a party to any alleged fraud or an affiliate of one or more of the named defendants.

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V. Defendants (Supposedly) Account for a Large Portion of UMS' Business

The SEC next contends that defendants supposedly account for a large portion of UMS' business. How the SEC can make such a statement is unknown, and the SEC cites to no evidence to support such a proposition.

The only evidence (again from Ms. Canty's declaration) is that less than twenty percent of the total loans which UMS currently services are loans in the Emvest Fund portfolio. Logically, that might mean that less than twenty percent of UMS' gross revenues are attributable to loans in the Emvest portfolio. The amount of net income or profit from those loans is unknown, but it would certainly not constitute "a large portion of UMS' business." But even if it did, the volume of business is irrelevant to the legitimacy of the discovery request.

The SEC's discovery request in this regard is completely irrelevant and clearly contemplates an unwarranted fishing expedition into the financial affairs of UMS. The amount of money UMS makes is none of the SEC's business. Moreover, and quite understandably, UMS is extremely reluctant to identify its other customers to the SEC. UMS' outside certified public accountants already quit when they learned of the SEC's allegations. The Better Business Bureau has sought to revoke UMS' membership, once again on the basis of the unsubstantiated allegations made by the SEC. In this day and age of heightened governmental investigation and the risk of exposure, clients get nervous for no legitimate reason. UMS does not want to risk losing any more of its valued relationships, and there is no compelling reason for this Court to require such disclosures.

VI. Judge Sabraw Held that UMS Was Not So Affiliated with the Named Defendants to be Subjected to the Receivership, and Judge Sabraw also Declined to Include Emvest Fund II Within the Receivership

The SEC either misinterprets or misunderstands the argument previously made by UMS in its April 15th brief. Judge Sabraw specifically declined to find that either UMS was somehow so affiliated with the named defendants to be subject to the Receivership, and also declined to expand or include Emvest Fund II within the Receivership. The SEC and the Receiver had made those requests, and they were both refused. Clearly, that indicates that Judge Sabraw did *not* find UMS and the Emvest Fund II so affiliated or intertwined with the named defendants to legitimately include them in the Receivership, and that was the extent of UMS' argument in that regard.

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VII. Documents Concerning UMS Are Not Relevant to this Litigation

The SEC finally argues, without any proof whatsoever, that UMS illegally siphoned money from the Fund. First, as stated, there is absolutely no evidence to support that assertion. Second, the SEC should probably attempt to obtain any such evidence from one of the named defendants, who would have responsibility to respond to such discovery requests as parties to the action. Third, if the SEC (or the Receiver, for that matter) had evidence related to any specific transaction involving UMS, than a proper discovery request to UMS could be specifically tailored. However, the SEC's overbroad and shotgun requests to fish through UMS' financial records are not warranted at this time based on this record.

Finally, the SEC's "disgorgement" theory is fatally flawed. In the first place, UMS is entitled by its contract to the loan servicing fees which it has earned. Secondly, those loan servicing fees are at market rates. Thirdly, as a non-party to this action, the SEC would never be able to compel UMS to disgorge anything. Thus, this argument is a red herring.¹

VIII. Conclusion

For the reasons set forth here and in the letter brief submitted on April 15, 2005, to Magistrate Judge Papas, the SEC's motion to compel should be denied in its entirety. If appropriate in the discretion of this Court, counsel for UMS respectfully requests a hearing if the Court is so inclined.

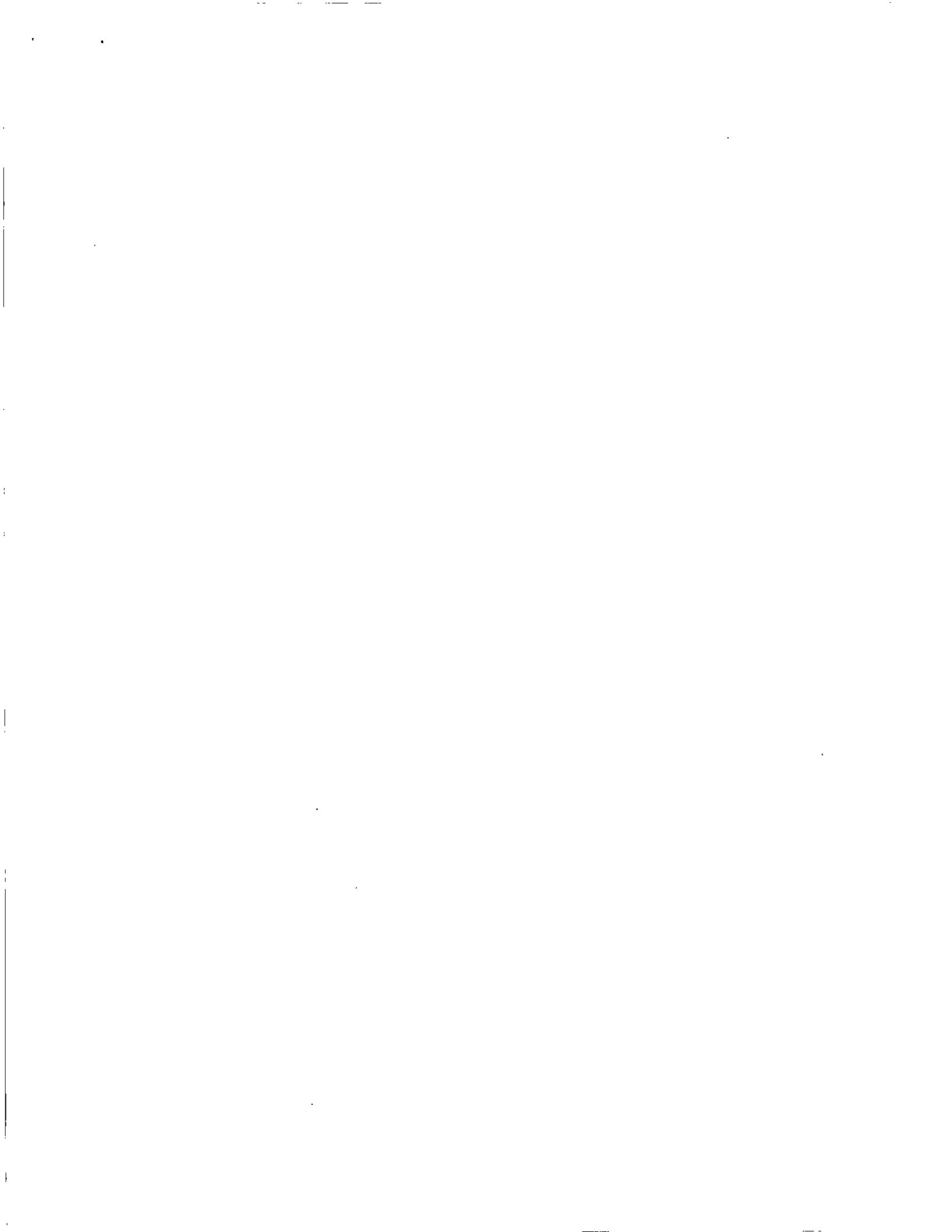
Very truly yours,



DAVID R. CLARK
of
HIGGS, FLETCHER & MACK LLP

cc: Susan F. Hannan, Esq.
(Counsel for the SEC)

¹ The SEC's argument that Emvest Fund II documents are discoverable from UMS is likewise without merit. Judge Sabraw has ruled repeatedly that the Emvest Fund II is not a party to this action and its documents are therefore irrelevant. Accordingly, UMS has no obligation to produce them, if it has any of them. Finally, UMS' tax returns are privileged and not discoverable under applicable California law, even if they were relevant (which they are not). 684629.1



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7 Attorneys for Third-Party Witness,
8 Unified Mortgage Service, Inc.

05 MAY 13 PM 1:36

U.S. DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA

DEPUTY

9 UNITED STATES DISTRICT COURT
10 SOUTHERN DISTRICT OF CALIFORNIA

11 UNITED STATES SECURITIES AND
12 EXCHANGE COMMISSION,,
13

14 Plaintiff,

15 v.

16 EMVEST MORTGAGE FUND, LLC,
17 EMVEST, INC., and MILON LYLE
18 BROCK,,
19

20 Defendants.

CASE NO. 04cv2295-DMS (POR)

DECLARATION OF MICHELE A. CANTY
OF UNIFIED MORTGAGE SERVICE IN
RESPONSE TO SECOND VERIFIED
REPORT OF RECEIVER AND SEC'S
SUBMISSION REGARDING SAME

Date: May 27, 2005
Time: 10:30 a.m.
Courtroom No.: 10

Before the Honorable:
United States District Judge Dana M. Sabraw

21 I, Michele A. Canty, state and declare as follows:

22 1. I am over the age of 18 years old and competent to make this Declaration.

23 2. I am presently the 100% shareholder of Unified Mortgage Service, Inc., and I have
24 been the sole shareholder since approximately 1995 when I purchased Unified Mortgage Service.

25 3. I am also the President and the sole Director of Unified Mortgage Service and
26 have remained in those capacities at all times since I purchased it.

27 4. None of the named defendants, nor any of the non-defendant entities accused by
28 the S.E.C. in this case are a part of Unified Mortgage Service, Inc. We are not "affiliated" with,
nor are we subsidiaries of any of the named defendants.

1 5. Before this case was filed, I was not even aware that there allegedly was language
2 in the Prospectus or other advertisements concerning the Emvest Fund which erroneously
3 characterized Unified Mortgage Service as being a purported affiliated company, or having
4 common ownership and management with the Emvest Fund. To the extent that such statements
5 were made by individuals marketing the Emvest Fund, they were inaccurate because Unified
6 Mortgage Service has never been affiliated or shared in ownership or control with any of the
7 named defendants in this case.

8 6. In the interests of fairness and full disclosure, Milon Lyle Brock is my father and
9 Tim Canty is my husband, but neither of them have any role or involvement with Unified
10 Mortgage Service, Inc., an entity which I bought before my marriage and have maintained it at all
11 times thereafter as my separate property.

12 7. Unified Mortgage Service is in the business of servicing loans, and that is our only
13 business. Essentially, what we do is to monitor mortgage loans, collect installment payments
14 from the borrowers and account for them.

15 8. Unified Mortgage Service is currently servicing in excess of five hundred
16 mortgage loans, of which less than twenty percent (approximately ninety-one) are mortgage loans
17 in the Emvest Fund portfolio.

18 9. Unified Mortgage Service has never researched, bought or sold any mortgage
19 loans for the Emvest Fund. Unified Mortgage Service has never raised, nor sought to raise, any
20 money for the Emvest Fund. Unified Mortgage Service has never had any contacts with any
21 investors regarding the Emvest Fund.

22 10. The Emvest Fund is simply one of many clients for whom we service mortgage
23 loans.

24 11. Contrary to the Receiver's statement at section 4.2 of his Second Verified Report,
25 Unified Mortgage Service has a written loan servicing agreement with each lender who made
26 loans through the Emvest Fund. Indeed, I specifically recall handing a sample one to Mr. Murphy
27 at a prior meeting he had with me and my legal counsel. In any event, an exemplar copy of one
28 of my loan servicing agreements with a lender in the Emvest Fund is attached hereto as Exhibit

1 "1," and incorporated herein by this reference as though fully set forth.

2 12. Unified Mortgage Service does charge a loan servicing fee of approximately one
3 percent of the current principal balance of each loan in the portfolio. In my professional opinion,
4 and I have been in the loan servicing business for more than ten years, this rate is exactly the
5 typical market rate, contrary to the speculation of the Receiver that it is above market.

6 13. This loan servicing fee is paid by the individual lenders to compensate Unified
7 Mortgage Service for servicing their loans and collecting their payments.

8 14. In addition, Unified Mortgage Service is entitled pursuant to its contract to retain
9 all late fees and other related charges collected from the borrowers. In my professional
10 assessment, it is also customary for a loan servicing company to keep such charges. Moreover,
11 these charges are collected from the borrowers and not the lenders, so this money would never be
12 property of Emvest Fund, in any event.

13 15. It is occasionally the case that a loan servicing company would agree to reduce its
14 normal fees to take over an existing loan portfolio or to get its foot in the door with a new client.
15 However, any such cost saving is temporary and illusory, and would be recouped later.

16 16. I take exception to the Receiver's statement that Unified Mortgage Service
17 collected approximately \$250,000 in fees for calendar year 2004. According to my personal
18 analysis of Unified Mortgage Services' business records, the actual loan servicing fee collected
19 by Unified Mortgage Service for calendar year 2004 from the lenders in the Emvest Fund was the
20 sum of \$103,415.34. Any money collected by Unified Mortgage Service over that amount during
21 calendar year 2004 was attributable to late fees or other related charges paid by the borrowers,
22 which the Emvest Fund was never entitled to in the first place.

23 17. I also know from my review of our records that Unified Mortgage Service
24 collected and paid to the Emvest Fund during calendar year 2004 the sum of \$9,318,398.43 in
25 loan payment collections attributable to approximately \$13,000,000 in loan principal outstanding
26 for 2004, so my servicing fee was actually substantially less than one percent of principal and
27 slightly more than one percent of actual collections.

28 18. Neither I nor anyone else employed by Unified Mortgage Service has received any

1 complaints or criticisms about our work and the performance of our contracts, either from any
 2 lender or the Receiver, and our loan files are complete and currently maintained, so there is no
 3 cause to attempt to prematurely terminate our loan servicing arrangements or to "rebid" our
 4 contracts prior to their stipulated termination.

5 19. Moreover, Unified Mortgage Service has worked at least twice before with Court-
 6 appointed receivers, and never have our loan servicing agreements been renegotiated.

7 20. I categorically object and deny that any defendant (including my father and my
 8 husband) has used Unified Mortgage Service to purportedly "skim" money from the Emvest
 9 Fund, nor has Unified Mortgage Service taken one penny more than it was entitled to receive.
 10 Neither Unified Mortgage Service nor I have siphoned any of that money to any defendant or any
 11 person affiliated with any defendant.

12 21. Obviously, as a vendor to the Emvest Fund, and not a party to this action, Unified
 13 Mortgage Service had absolutely nothing to do with any alleged securities fraud or any supposed
 14 Ponzi scheme.

15 22. There is no reason, let alone a compelling reason, to accept the Receiver's
 16 unfounded recommendation to relet Unified Mortgage Service's contracts in violation of their
 17 terms.

18 I have personal knowledge of the facts referred to above, and would and do so hereby
 19 testify as though called and sworn as a witness.

20 In accordance with the laws of the State of California, I declare under penalty of perjury
 21 that the foregoing is true and correct and that this declaration is executed on May 12, 2005, in
 22 San Diego, California.

23
 24 
 25 MICHELE A. CANTY
 26
 27
 28

EXHIBIT 1

LOAN SERVICING AGREEMENT

Loan Account: E31222

**GARY GRAMLING
CONSTRUCTION GRAMLING**

EMVEST MORTGAGE FUND LLC

This Loan Servicing Agreement (the "Agreement") is dated Jan 9, 2004 and is between Unified Mortgage Service, Inc., a real estate broker licensed by the State of California ("Broker") and the lender or lenders whose signatures appear below and in counterparts to this Agreement (together, the "Lender"). If the Loan is owned by multiple Lenders, the "Majority" in this Agreement are the Lenders who own more than 50% of the record beneficial interest in the Note evidencing the Loan (more than 50% of the undivided interests in the Note), exclusive of any interest of a licensed real estate broker that is the issuer or servicer of the Loan, or any affiliate of that licensed real estate broker.

The parties agree as follows:

1.0 Scope. Lender retains Broker as Lender's agent to employ commercially reasonable and prudent practices to collect all scheduled payments on the Loan identified above (the "Loan"), including the protection of the security for the Loan. Broker shall consult with and follow instructions from Lender on non-routine collection matters. If the Loan is owned by multiple Lenders (a "Multi-Lender Loan"), Broker shall consult with all Lenders but shall only follow instructions from the Majority. A default upon any interest in the Note shall constitute a default upon all interests. The Majority may determine and direct the actions to be taken on behalf of all lenders in the event of default or with respect to other matters requiring the direction or approval of lenders, including but not limited to, designation of brokers, servicing agents or others acting on their behalf and the sale, encumbrance or lease of any real properties which may be owned by lenders as the result of foreclosure or receipt of a deed in lieu of foreclosure.

2.0 Term and Termination. This Agreement shall begin when the escrow for the Loan closes or the date set forth above, whichever is later. It shall terminate when any of these events occur: (a) payment in full of the Loan and reconveyance of the deed(s) of trust securing the Loan; (b) 30 days' written notice by Broker to Lender and, unless Lender is in breach of this Agreement, the notice shall be accompanied by a written offer from another licensed and qualified real estate broker, or from another qualified loan servicer exempt from licensure as a real estate broker, to service the Loan for Lender under the terms of this Agreement; (c) 30 days' written notice by Lender to Broker, in which case Lender shall immediately pay Broker the present value, assuming a rate of return of 100.0%, of the sum of Broker's servicing fee for the remaining term of the loan; or (d) unless paragraph 7.0 is checked, recordation of a trustee's deed following a foreclosure of the Loan. Prior to the effectiveness of any termination, Broker shall deliver to Lender all of Lender's funds, an appropriate accounting and all necessary documentation. At termination, Lender shall immediately reimburse Broker for any outstanding advances made pursuant to paragraph 4.0.

3.0 Specific Loan Servicing Functions. Broker shall: (a) issue payment coupons or monthly statements to the borrower directing Loan repayment to Broker; (b) issue payoff demands, beneficiary statements and mortgage ratings; (c) demand, receive and collect all Loan payments, deposit them by the next business day into Broker's trust account and pay them to Lender within 30 days of receipt (within 25 days if the Loan is a Multi-Lender Loan); (d) issue annual income tax statements to the borrower and Lender; (e) answer borrower inquiries, demands and requests; (f) grant appropriate payment deferrals, but not of the maturity of the Loan unless approved by Lender or the Majority in the case of a Multi-Lender Loan; (g) monitor the continued effectiveness and claims on any property insurance listed in the Loan escrow instructions; (h) request and receive notices of default on senior liens; (i) receive notices of property tax delinquencies; and, (j) with the consent of Lender or the Majority, as the case may be, substitute trustees pursuant to Civil Code Section 2934a, initiate and direct judicial or non-judicial foreclosure of the Loan, as Lender or the Majority deem appropriate, and with such consent, communicate to the trustee or sheriff the amount of any credit bid. Broker shall promptly communicate to Lender any material information about collection of the Loan and the source of non-borrower Loan payments. Broker shall furnish to Lender a list of names and addresses of all lenders holding an interest in the Note upon five (5) days written notice. Broker may produce a copy of this Agreement as evidence of its authority.

4.0 Protective Advances. Lender shall make such advances as approved by the Majority or, if Lender is the only owner of the Loan, such advances that are necessary and prudent to protect and to collect Lender's interest in the Loan. If the Loan is a Multi-Lender Loan, and Lender fails to make advances approved by the Majority, other owners of the Loan are authorized to advance the amount Lender failed to advance and to receive payment in full with interest at 10% per annum before any further payments to Lender and, if this box is checked the non-defaulting Loan owners shall also have the option, exercisable within 30 days after Lender's default, to purchase Lender's interest in the Loan at N/A of what is owed to Lender, payable within 15 days after the election to purchase is made. Broker, in its absolute discretion, may advance its own funds to protect the security of Lender's Loan, including advances to cure senior liens, property insurance,

Loan Account: E31222
Loan Servicing Agreement Page 1 of 3

LENDER:

Address: 591 CAMINO DE LA REINA #103
SAN DIEGO, CA 92108

Percentage Ownership: 100.000%

Send Payments to: 591 CAMINO DE LA REINA #103
SAN DIEGO, CA 92108

Account Number: E591

Lender's Signature:


EMVEST MORTGAGE FUND LLC

Date

BROKER: Unified Mortgage Service, Inc.

BY: 
Name, Title

Date