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CLERK, U.S. DISTRICT COURT  
SOUTHERN DISTRICT OF CALIFORNIA

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10 UNITED STATES DISTRICT COURT  
11 SOUTHERN DISTRICT OF CALIFORNIA

BY FAX

12 SECURITIES AND EXCHANGE  
13 COMMISSION,

14 Plaintiff,

15 v.

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

18 Defendants.

Case No. 04 CV 2295 DMS (LSP)

REPLY BRIEF SUPPORTING ENTRY OF  
PRELIMINARY INJUNCTION AND  
PERMANENT RECEIVER

Date: December 3, 2004

Time: 10:30 a.m.

Courtroom: 10 (Hon. Dana M. Sabraw)

1 **I. INTRODUCTION**

2 On August 16, 2003 the Fund's former accountants warned Mr. Brock that since "the  
3 inception [of the Fund] you have been paying a 12.5% distribution based on [the investors']  
4 original capital contributed," which has been "in excess of the actual earnings of the fund." (See  
5 Declaration of Susan F. Hannan in Support of Plaintiff's Ex Parte Application ("Hannan Dec. I")  
6 Ex. 15.) Nowhere does Defendants' Opposition to Plaintiff's Application for Preliminary  
7 Injunction and Appointment of a Receiver ("Opposition") address this. The defendants' failure  
8 to address this important piece of evidence, and the testimony supporting it, undermines the  
9 defendants' claim that the Commission has not provided reliable evidence that the defendants  
10 used investor capital to pay returns.

11 The defendants instead try to refute the evidence presented in the Declaration of Kelly  
12 Bowers in Support of the Plaintiff's Ex Parte Application ("Bowers Dec. I."), with the  
13 Declaration of J. Stephen Hawkins ("Hawkins Dec."). But Mr. Hawkins's preliminary review is  
14 based on unreliable data and presents a distorted view of the Fund. Mr. Hawkins also fails to  
15 provide adequate proof that items Mr. Bowers categorized as expenses should be reclassified.

16 Defendants also claim the Commission has not met its burden of providing substantial  
17 evidence that there is a prima facie case of securities fraud and that defendants will likely  
18 continue their fraudulent conduct unless enjoined. Relying on a few ambiguous excerpts from  
19 the Fund's Prospectus, and ignoring the numerous other representations that the defendants made  
20 to investors, the defendants claim they told investors that they would use investor capital to pay  
21 investor returns. When the excerpts from the Prospectus are put in context with the defendants'  
22 other representations, this argument fails. In sum, the Commission has provided substantial  
23 evidence that the defendants engaged in securities fraud, and that unless they are further  
24 enjoined, they will likely resume their fraudulent conduct.

25 **II. ARGUMENT**

26 **A. The Hawkins Review is Unreliable and Presents a Distorted Picture**

27 The defendants offer the unreliable Declaration of J. Stephen Hawkins to rebut the  
28 Commission's analysis of the Fund. In conducting his "preliminary review," Mr. Hawkins relied

1 solely on the Fund's QuickBooks computer program, an accounting program the Fund uses to  
2 classify receipts and disbursements.<sup>1</sup> (Declaration of Alka N. Patel ("Patel Dec.") Ex. 1  
3 (Hawkins dep.), pp.25:16-26:24.) The QuickBooks program relies on information that people  
4 input into the program. (Patel Dec. Ex. 1 (Hawkins dep.), pp. 26:25-28:19.) Because the  
5 program relies on human input, errors are possible. In fact, Mr. Hawkins acknowledged that the  
6 Fund's controller had misclassified certain payments, which errors he corrected.<sup>2</sup> (Patel Dec. Ex.  
7 1 (Hawkins dep.), pp. 86:9-87:3.) Despite the possible existence of other errors, Mr. Hawkins  
8 did not compare (or test) the information in QuickBooks with actual source documentation, such  
9 as the Fund's checks, receipts, or loan documents, to determine the accuracy of information in  
10 QuickBooks. (Patel Dec. Ex. 1 (Hawkins dep.), pp. 29:16-31:5 & 33:14-34:4.) As a result, Mr.  
11 Hawkins's QuickBooks-based "preliminary review" may be based on erroneous information.

12 Defendants claim that the accrual method of accounting is a "preferred" method to  
13 determine the Fund's profitability, because it allows the Fund to record as current earnings  
14 money that the Fund expects to collect in the future, regardless of whether the Fund actually  
15 collects it. (Oppo. pp. 6-7; *see also* Patel Dec. Ex. 1 (Hawkins dep.), pp. 37:25-40:7.) Relying  
16 on a Balance Sheet and Profit and Loss Statement that Mr. Hawkins prepared, the defendants  
17 claim the accrual method shows that the Fund generated a net profit in 2004. (Oppo. p. 7.)

18 But the Hawkins Balance Sheet and P&L present a distorted view of the Fund. First,  
19 although Mr. Hawkins accrued revenue, he did not accrue expenses (Patel Dec. ¶ 4(a) & Ex. 1  
20 (Hawkins dep.), pp. 91:15-92:24), even though he testified that he would expect that the Fund  
21 would have incurred expenses in a current period that it paid later. (Patel Dec. Ex. 1 (Hawkins  
22 dep.), pp. 42:18-43:11.) In other words, he took into account all the benefits of an accrual

23  
24 <sup>1</sup> Significantly, Mr. Hawkins took no steps to determine if the Fund was using investor capital to  
25 pay distributions to investors. (Patel Dec. ¶ Ex. 1 (Hawkins dep.), pp. 93:15-94:18.) He does  
26 not refute, and in fact never saw, the August 16, 2003 memo that Kornfeld & Levy sent Brock,  
27 warning him that the Fund was using investor capital to pay distributions. (Patel Dec. ¶ Ex. 1  
28 (Hawkins dep.), pp. 93:23-94:7.)

<sup>2</sup> On November 19, 2004, Sylvia DeAnda sent Mr. Hawkins a memo telling him that she had  
improperly classified four checks as payments of interest, when some or all that money should  
have been classified as payments of principal. (Patel Dec. Ex. 1 (Hawkins dep.), pp. 56:25-  
57:21.) Relying solely on Ms. DeAnda's memo, and without reviewing any source documents,  
Mr. Hawkins reclassified those four checks as payments of principal. (Patel Dec. Ex. 1  
(Hawkins dep.), pp. 84:8-85:24.)

1 method, by including in the current period revenue that the Fund expects to collect in the future,  
2 but he did not include any of the corresponding expenses that it incurred. Second, Mr. Hawkins  
3 was unable to identify the specific items that were adjusted when he converted the Fund's  
4 financial statements from a cash basis to an accrual basis. (Patel Dec. ¶ 4(b) & Ex. 1 (Hawkins  
5 dep.), pp. 87:21-88:3.) Third, without looking at any source documentation and in sole reliance  
6 on Mr. Brock's representations, Mr. Hawkins assumed that the Fund would be able to recover  
7 attorney's fees and other costs the Fund has spent to collect on troubled loans. (Patel Dec. ¶ 4(c)  
8 & Ex. 1 (Hawkins dep.), pp. 79:7-82:8.) Despite this evidence of troubled loans, Mr. Hawkins  
9 did not book reserves to cover any troubled loans. (Patel Dec. ¶ 4(c) & Ex. 1 (Hawkins dep.),  
10 pp. 78:12-79:5.) In fact, Mr. Hawkins testified that he has done no work related to the Fund's  
11 trust deeds, and consequently does not know their market value, or whether the Fund's loans are  
12 non-performing. (Patel Dec. Ex. 1 (Hawkins dep.), pp. 32:22-33:7 & 50:18-51:12.) Finally,  
13 although Mr. Hawkins capitalized certain costs – classifying them as an asset instead of a  
14 liability – Mr. Hawkins did not know what those costs were, only that they were paid to the  
15 Fund's affiliate, Emerald Bay Financial. (Patel Dec. ¶ 4(d) & Ex. 1 (Hawkins dep.), pp. 73:6-  
16 76:15.) In fact, Mr. Hawkins was unable to explain many items on the Balance Sheet he  
17 prepared. (Patel Dec. ¶ 4(e) & Ex. 1 (Hawkins dep.), pp. 52:13-55:10.)

18 **B. The Defendants' Criticisms of the Bowers Declaration Are Unsubstantiated**

19 Defendants take issue the fact that Mr. Bowers did not attempt to reconcile his findings  
20 with the information in QuickBooks. (See Oppo. p. 8.) Contrary to what defendants claim,  
21 however, the defendants never gave the Commission an electronic copy of their QuickBooks  
22 computer files. (Declaration of Susan F. Hannan in Support of Reply ("Hannan Dec. III") ¶ 6.)  
23 During its investigation, the Commission repeatedly asked for the files, but defendants were  
24 either unable or unwilling to produce them. (Hannan Dec. III ¶¶ 2-6.) Although the  
25 Commission would have preferred to have access to Fund's QuickBooks program, because it  
26 would have sped the Commission's work, the documents the Fund produced are sufficient to  
27 show, and do show, that defendants used investor capital to pay disbursements to investors.

28 The defendants claim that Mr. Bowers has made "gross errors," which account for a

1 \$571,411.27 reduction in revenue. (Oppo. p. 8; *see also* Patel Dec. Ex. 1 (Hawkins dep.), pp.  
2 62:22-63:6.) Mr. Hawkins's critique of Mr. Bowers's work is based on two categories of  
3 expenditures that Mr. Hawkins claims should have been treated as assets, instead of  
4 expenditures: (1) "capital advances" and (2) "cost of assets or investments." (*See* Hawkins Dec.  
5 Ex. C.) There is no reliable basis on which to reclassify either of these groups of expenditures.  
6 First, Mr. Hawkins claims that certain expenditures should have been classified as "capital  
7 advances" instead of expenses, because those expenditures are recoverable. (*See* Hawkins Dec.  
8 Ex. C; *see also* Patel Dec. Ex. 1 (Hawkins dep.), pp. 66:7-23.) But Mr. Hawkins reviewed no  
9 source documentation to verify whether these expenditures were in fact recoverable, and simply  
10 relied on Mr. Brock's assertions that they were. (Patel Dec. ¶ 4(c) & Ex. 1 (Hawkins dep.), p.  
11 17:25-20:3; 66:7-68:12.) Second, Mr. Hawkins claims that two other expenditures, a check for  
12 \$186,520 and a check for \$42,500, should have been categorized as "assets" instead of expenses.  
13 (*See* Hawkins Dec. ¶ 9 & Ex. C.) Again, his sole basis for reclassifying these expenditures is  
14 Mr. Brock's claim that they should be reclassified. (Patel Dec. Ex. 1 (Hawkins dep.), pp. 68:13-  
15 69:3.) But when Mr. Hawkins was asked what those costs were, he testified that he had no idea;  
16 he only knew they were paid to Emerald Bay Financial in connection with some loans. (Patel  
17 Dec. ¶ 4(d) & Ex. 1 (Hawkins dep.), p. 73:6-76:15.)

18 **C. The Commission Has Shown a Prima Facie Case of Securities Fraud**

19 The defendants claim that because the Commission seeks "complete control over the  
20 assets and the operation of [defendants'] business," the Commission must meet a higher  
21 evidentiary burden.<sup>3</sup> (*See* Oppo. p.5.) First, the Commission does not seek control over the  
22 defendants' business.<sup>4</sup> Instead, the Commission seeks to (1) obtain a preliminary injunction  
23 preventing defendants from further violating the securities laws; and (2) extend the appointment  
24 of the receiver.

25  
26 <sup>3</sup> In making this argument, defendants cite *Weinberger v. Romer-Barcelo*, 455 U.S. 305, 313  
27 (1982). But that case is inapposite because it involved entry of a preliminary injunction under  
the Federal Water Pollution Control Act, which applies a traditional four-prong test to decide if  
an injunction is proper.

28 <sup>4</sup> The receiver is not a branch of the Commission but acts as an arm of the Court. *Ledbetter v.*  
*Farmers Bank & Trust Co.*, 142 F.2d 147, 150 (4th Cir. 1944), *cert. Denied*, 323 U.S. 719.

1 Moreover, granting a preliminary injunction and extending the receivership will not  
2 necessarily shut down the defendants' business.<sup>5</sup> For the past two weeks, the temporary receiver  
3 has been controlling the Fund. Business is still taking place, albeit without Mr. Brock at the  
4 helm, in order to ensure that Fund assets do not continue to be dissipated. If the receiver deems  
5 it appropriate to take steps to modify, shut down, or sell the business, the receiver will make a  
6 recommendation to the Court, the defendants will have an opportunity to be heard, and the Court  
7 will decide whether to accept the receiver's recommendation. *See, e.g., SEC v. Basic Energy &*  
8 *Affiliated Res.*, 273 F.3d 657, 661-671 (6th Cir. 2001). Thus, receivership is hardly the  
9 "draconian" remedy that defendants claim.

10 In any event, the Commission has provided substantial evidence, showing: (1) a prima  
11 facie case that a violation of the securities laws has occurred; and (2) that there is a reasonable  
12 likelihood that the violation will be repeated. *See, e.g., SEC v. Unique Fin. Concepts, Inc.*, 196  
13 F.3d 1195, 1199 n.2 (11th Cir. 1999); *SEC v. Unifund SAL*, 910 F.2d 1028, 1037 (2d Cir. 1990);  
14 *SEC v. United Fin. Group*, 474 F.2d 354, 358-59 (9th Cir. 1973).

15 **1. The Defendants Violated the Securities Laws**

16 Without citing any evidence, the defendants claim the Fund pays investors a 12% per year  
17 return on their unreturned invested capital, and provides an example of how the Fund  
18 purportedly works. (*See* *Oppo.* pp. 3-4.) According to the defendants, in 2008, the Fund will  
19 pay investors their initial investment "less any payments [the investor] received in excess of  
20 available earnings." (*Oppo.* p. 4.) In other words, defendants claim that it was *not* their plan to  
21 return the investors' initial investment. The only problem is that the defendants did not tell this  
22 to investors.<sup>6</sup> Instead, the defendants sent newsletters claiming that investors experienced no  
23 loss of capital. (*See* *Hannan Dec. I*, Ex. 11, p. 192; Ex. 13, p. 214). They told investors that the  
24

25 <sup>5</sup> The Commission is confident that the receiver's report will establish that the defendants'  
26 business is not as healthy as they claim. Defendants claim they have \$23 million in assets,  
27 including \$17 million in trust deeds. (*Oppo.* p. 2.) But the trust deeds are valued at "face value"  
28 and do not take into account whether the loans are actually performing. (*Patel Dec. Ex. 1*  
(*Hawkins dep.*), pp. 32:22-33:7 & 50:18-51:12.)

<sup>6</sup> Nor is that what the Fund did. The accountants' August 16, 2003 memorandum to Lyle Brock  
indicates that when investors left the Fund, the defendants were "distribut[ing] their original  
investments in full." (*Hannan Dec. I*, Ex. 15, p. 229.)

1 Fund "maintain[s] a portfolio yield of 12.5+% annually." (Sable Dec. Ex. 4, p. 16.) And that  
2 "[t]he Fund is continuing to generate returns above 12%." (Hannan Dec. I Ex. 19, p. 288.)

3 The defendants claim the Fund's Prospectus made no omissions or misrepresentations.  
4 Not only do the defendants fail to address the misrepresentations and omissions that the  
5 defendants made in their advertisements, newsletters, and elsewhere, but their reliance on the  
6 purported disclosures in the Prospectus is disingenuous.

7 a. **The Prospectus Does Not Tell Investors the Fund Used Investor**  
8 **Capital to Pay Investor Returns**

9 The defendants do not address the obvious in their Opposition. If the defendants did not  
10 intend to mislead investors, why doesn't the Fund Prospectus state in plain words that "in the  
11 event the Fund's real estate investments do not yield 12% returns, the difference will be paid out  
12 of investor principal"? In fact, when Mr. Brock was asked to identify where the Prospectus  
13 revealed to investors that they would get back their principal, Mr. Brock was unable to locate  
14 anything. (Hannan Dec. III Ex. 6 (Brock test.), pp. 160:21-162:2.) Instead, the defendants rely  
15 on ambiguous phrases in their forty-plus page prospectuses to cobble together an argument that  
16 they told investors they were investing in a Ponzi scheme.<sup>7</sup> Reason dictates, however, that if  
17 investors knew their 12% "return" would be paid with investor capital, no rational investor  
18 would have invested in the Fund.

19 The defendants first quote language from the Prospectus stating that "[s]hareholders are  
20 entitled on a cumulative but non-compounding basis to a 12% per annum priority return on their  
21 unreturned original invested capital (the "Priority Operating Return Distribution"), which  
22 distributions are to be made on a monthly basis, in arrears." (See Hannan Dec. I, Ex. 6, pp. 50-  
23 51; Ex. 7, pp. 90-91; Ex. 8, p. 138.) Defendants now claim that the reference to "unreturned  
24 original invested capital" told investors that portions of the investors' capital might be returned.  
25 That is a strained interpretation of this passage, because investors were allowed to withdraw  
26

27 <sup>7</sup> Contrary to defendants' assertions, the Fund is a Ponzi scheme. A Ponzi scheme is "a  
28 fraudulent investment scheme in which funds paid in by later investors are used to pay  
artificially high returns to the original investors, thus attracting more funds." (Webster's New  
World Dictionary: Third College Edition (1988).) That is exactly what happened here.

1 portions of their original invested capital. (See Hannan Dec. III Ex. 6 (Brock test.), pp. 140:16-  
2 144:25 & Ex. 7, pp. 50-52.) For example, an investor who originally invested \$10,000 could  
3 withdraw \$5,000 of their original investment, and the remaining \$5,000 would be the investors'  
4 "unreturned original invested capital." (See, e.g., Hannan Dec. III Ex. 6 (Brock test.), pp.  
5 140:16-141:19 & Ex. 7, pp.50-52.) Thus, the quoted language simply told investors that they  
6 would be paid 12% per year on the original invested capital that the investor did not ask the Fund  
7 to return. Moreover, although defendants now claim that the Prospectus requires a reduction in  
8 the investors' accounts as distributions are made, that is not how the Fund operated. Investors  
9 were paid 12 to 12.5% of their total invested Funds, not of their reduced capital accounts. (See  
10 Hannan Dec. I ¶ 9; Ex. 1 (Brock test.), pp. 93:24-96:14; & Ex. 3 (DeAnda test.), pp.112:2-22;  
11 Hannad Dec. III Ex. 8, pp. 76-81.)

12 Second, the defendants cite to two vague passages in the Fund's Operating Agreement:  
13 (1) "Shareholders are entitled on a cumulative but non-compounding basis, payable monthly in  
14 arrears, to a 12% per annum priority return on their original invested capital, as reduced by  
15 cumulative Priority Operating Return Distributions to Shareholders" and (2) "The 'Priority  
16 Operating Return Distribution' is twelve percent (12%) per annum on the amount of capital  
17 contributed to the Company in consideration for Shares reduced by the cumulative amount of  
18 distribution to shareholders in respect of such Shares on a cumulative but non-compounding  
19 basis."<sup>8</sup> Not only is this legalese buried in the Operating Agreement, but when asked about this  
20 passage, Mr. Brock indicated that the Fund was not, in fact, making distributions in this fashion.  
21 (Hannan Dec. III, Ex. 6 (Brock test.), pp. 204:3-207:9.)

22 Finally, the defendants suggest that the risk factors in the Prospectus somehow disclose  
23 that investor returns would be paid with investor capital. But the defendants cite only a portion  
24 of the passage. The full passage states:

25 **Sufficiency of Loan Portfolio.** There can be no assurance of return of  
26 invested capital *inasmuch as* the ability of the Company to generate  
27 income will depend upon a wide variety of factors, including the default  
28 rate of the Loans and the recovery rate of the Company in connection

<sup>8</sup> Defendants do not cite the pages on which this language is found and Commission counsel was unable to locate it. The Commission will assume, however, that the language is found in the Operating Agreement and that the quotes are accurate.

1           therewith, the adequacy of the capital reserves maintained by the  
2           Company, which reserves may be deemed to be inadequate given the level  
3           or risk of the Company's investments and the fact that the Company has  
4           the right to make distributions subject only to certain limitations set forth  
5           in the Operating Agreement, the Company's ability to identify Loans for  
6           the Loan Portfolio of appropriate levels of risk and return, the servicing of  
7           the Loans by the servicing Agent, the Financial strength of the Company,  
8           which may determine the Company's ability to make optional advances in  
9           connection with a default upon a senior lien, and certain conditions over  
10          which the Company will have little or no control such as regional and  
11          local economic conditions, competition among lenders, note purchasers on  
12          the secondary market, investors in tax liens, real estate purchasers and  
13          developers, new government regulation, and certain acts of nature or of  
14          government seizure.

15          (See Hannan Dec. I, Ex. 6, p. 62 (emphasis added).) The phrase "inasmuch as" qualifies the  
16          circumstances under which the Fund might not return invested capital. Nowhere in what follows  
17          does the Prospectus explain that if the Fund does not generate adequate income from its  
18          investments, it will pay distributions with investor capital.

19                                   **b. The Fees Paid to the Fund's Affiliates Violate the Prospectus**

20          Defendants claim they did not make any misrepresentations to investors about the fees  
21          that they paid their affiliate, Emerald Bay Financial ("EB Financial"). In order to make this  
22          argument, they simply re-characterize the type of fees that the Fund paid EB Financial. The  
23          Prospectus states that "affiliates of [Emvest] may receive loan origination, broker's, finder's  
24          and/or other fees from third-parties (but not the Company) in connection with the acquisition  
25          and/or disposition of assets comprising the [Fund's] Loan Portfolio, and may also receive  
26          directly from the [Fund] Servicing Fees for servicing the [Fund's] Loans." (Hannan Dec. I Ex. 8,  
27          p. 151 (emphasis added).) Defendants admit that the \$243,719.48 that the Fund paid EB  
28          Financial represented the "discount fee" due to EB Financial. Clearly a "discount fee" would  
29          qualify as an "other fee."

30                                   **c. The Investors' 12% Return is Funded With Other Investors' Capital**

31          The defendants claim that there is no evidence that the Fund used investor capital to pay  
32          investor returns. But defendants completely ignore the August 16, 2003 memorandum from the  
33          Fund's accountants warning Mr. Brock that the Fund was paying investors' distributions with  
34          other investors' capital. (Hannan Dec. I, Ex. 15, pp. 229-230.) Moreover, Mr. Brock has  
35          admitted that the Fund was using investor principal to pay the 12% distributions. (Hannan Dec.

1 III, Ex. 6 (Brock test.), pp. 160:7-162:2 & 204:3-207:9.)

2 **d. The Fund Misrepresented That it Would Preserve Investors'**  
3 **Capital**

4 At least by August of 2003, when the Fund's accountants warned Mr. Brock that the Fund  
5 was using investor capital to pay returns, the defendants knew, or should have known, that they  
6 were not complying with the Fund's stated objective. (See Hannan Dec. I Ex. 15.) Despite Mr.  
7 Brock's knowledge that the Fund was not meeting this objective, the Prospectus summary, which  
8 was prominently displayed on the Emvest website, continued to list as one of the Fund's top four  
9 objectives the preservation of investor capital. (Hannan Dec. I Ex. 12, p. 197.) The defendants  
10 also continued to tell investors that the Fund was earning at least 12%, when it was not. (See  
11 e.g., Sable Dec. Ex. 4, p. 16; Hannan Dec. I Ex. 19, p.288.)

12 **2. There is Substantial Evidence Showing a Reasonable Likelihood of**  
13 **Future Violations**

14 If the Court does not grant a preliminary injunction and extend the appointment of the  
15 receiver, it is highly likely that the defendants would commit future violations of the securities  
16 laws. Although the key factor to be considered is the past illegal conduct of the defendant, see  
17 *United States v. Odessa Union Warehouse Co-op*, 833 F.2d at 176 (citing *SEC v. Koracorp.*  
18 *Indus., Inc.*, 575 F.2d 692, 298 (9th Cir. 1978), courts also consider the degree of scienter  
19 involved; the isolated or recurrent nature of the violative conduct; the defendant's recognition of  
20 the wrongful nature of the conduct; the likelihood that, because of the defendant's occupation,  
21 future violations may occur; and the sincerity of the defendant's assurances (if any) against  
22 future violations. See, e.g., *SEC v. Murphy*, 626 F.2d 633, 655 (9th Cir. 1980).

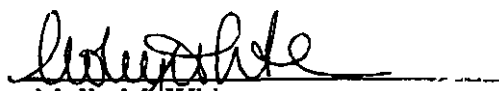
23 The defendants claim they would not be able to commit future securities violations  
24 because the Fund "is now closed to new money, whether from new investors or current  
25 investors." (Oppo. p. 13.) But as shown in the Commission's Supplemental Brief, even after the  
26 Fund was purportedly closed to new investors, the defendants continued to accept investments  
27 into the Fund. (See Supplemental Brief, p. 7 & evidence cited therein.) Because the defendants  
28 continued to accept investments into the Fund after the Fund was closed, it is likely they would

1 continue to accept investments if again given control of the Fund.<sup>9</sup> Furthermore, defendants  
2 would continue to dissipate the assets of existing investors.

3 Defendants claim that "after more than 28 years of being self-employed in the trust deed  
4 business, the Complaint in this case is the first [securities fraud] allegation made against Mr.  
5 Brock." (Oppo. p. 13.) While it may be the first time that the Commission has accused Mr.  
6 Brock of securities fraud, it is not the first time he has been accused of wrongdoing related to his  
7 businesses. As set forth in the Commission's Ex Parte Application, in 1984, Brock's real estate  
8 broker's license was suspended for 30 days, as a result of a trust account violation. (See also  
9 White Declaration Supporting Reply ("White Dec. II") ¶ 2 & Exs. 1-4.) Then, on March 14,  
10 1994, the California Department of Corporations ordered Brock to desist and refrain from further  
11 offering or selling securities. (White Dec. II. ¶ 5, Ex. 4.) And, in 2000, Brock civilly settled an  
12 action filed by the San Diego District Attorney's Office relating to Brock's activities as a  
13 mortgage broker. (See Hannan Dec. I Exs. 21 & 1 (Brock test.), pp. 56:13-58:7.) Clearly, Mr.  
14 Brock has had a difficult time operating his business within the confines of the law.

15 Significantly, the Commission need not rely on Mr. Brock's past encounters with the  
16 authorities to establish the likelihood of future violations. Mr. Brock's egregious conduct as it  
17 relates to the Fund, and its continuation for more than a year, suffices. Moreover, the  
18 Commission has presented evidence of the other factors, which evidence the defendants do not  
19 refute, establishing that if the Court does not continue to enjoin defendants, they will continue to  
20 commit securities fraud. (See Memo. of Ps & As Supporting Ex Parte Application, pp. 13-14.) \

21  
22 DATED: November 30, 2004

  
Molly M. White  
Susan R. Hannan  
Attorneys for Plaintiff Securities and Exchange  
Commission

26 <sup>9</sup> The defendants claim the Commission's decision not to name Fund II in the Complaint  
27 undermines the Commission's argument. But the Commission did not name Fund II because the  
28 defendants did not start running Fund II until late June 2004. As one would expect, in the first  
few months of Fund II's existence there was not a lot of activity. Instead of waiting to obtain  
more evidence regarding Fund II, and giving defendants more time to continue to defraud  
investors, the Commission decided the prudent course was to take immediate action.