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7 **UNITED STATES DISTRICT COURT**
8 **SOUTHERN DISTRICT OF CALIFORNIA**

9
10 SECURITIES AND EXCHANGE
COMMISSION,

11 Plaintiff,

12 v.

13 EMVEST MORTGAGE FUND, LLC,
14 EMVEST, INC., and MILON LYLE BROCK,

15 Defendants.

Case No. 04 CV 2295 DMS (POR)

**SECURITIES AND EXCHANGE
COMMISSION'S RESPONSE TO
SEVENTH VERIFIED REPORT OF
RECEIVER**

Special Briefing Schedule Ordered

Date: November 17, 2006

Time: 1:30 p.m.

Courtroom: 10 (Hon. Dana M. Sabraw)

1 **I. INTRODUCTION**

2 The Court should authorize the permanent receiver (the “Receiver”) to conduct an orderly
3 liquidation of Emvest Mortgage Fund (the “Fund”) and distribute the Fund’s assets to the Fund’s
4 defrauded investors. Almost a year ago, after a bench trial, the Court found that the Defendants
5 in this action defrauded investors by, among other things, telling investors that if they invested in
6 the Fund they would receive a 12% per year return on their money with no erosion of capital.
7 But this was a lie. The investors did not get what the Defendants promised. Under the
8 Defendants’ management, the Fund paid investors returns of 12% per year, but the Defendants
9 whittled away the investors’ capital in order to pay those returns. As a result, by the time the
10 Court appointed the Receiver, the investors’ capital had been eroded by about 15%. (*See*
11 *Receiver’s Seventh Report*, p. 3, Docket No. 339.) Even under the Receiver’s management, the
12 Fund’s investors have not received what the Defendants had promised. In order to restore the
13 value of the investors’ capital, the Receiver has had to reduce the monthly returns to investors to
14 half of what they were promised – 6% per year. Because the investors’ investment in the Fund
15 has never been what was promised, it is time that the Court authorize the Receiver to return the
16 investors’ capital to the Fund’s investors.

17 The majority of the Fund’s investors have indicated that they would like the Receiver to
18 wind down the Fund and return their investments to them. In connection with the Receiver’s
19 Comments and Opposition to the Defendants’ Motion to Terminate the Receivership, the
20 Receiver reported the results of a petition that he circulated to all investors. (*See Receiver’s*
21 *Comments and Opposition to Motion to Terminate*, pp. 4-6, Docket No. 310.) A majority of the
22 Fund’s investors – 62% of them – indicated that they wanted the Fund to be liquidated. (*Id.* p. 5.)
23 The Court should carry out the wishes of the majority of investors.

24 **II. ARGUMENT**

25 **A. The Court Should Authorize the Orderly Dissolution of the Fund**

26 The Commission supports the orderly liquidation of the Fund’s portfolio over time and
27 the return of the Fund’s assets to investors as soon as possible, pursuant to Section 3.3 of the
28 Receiver’s Seventh Report. (*See Receiver’s Seventh Report*, pp. 5-7, Docket No. 339.) Given

1 the length of time that the investors' monies have been tied up in the Fund, it is the
 2 Commission's position that the orderly liquidation of the Fund should take place as soon as
 3 possible, preferably before December of 2008. The Receiver, however, should maximize the
 4 overall return to investors. The Commission believes the estimated 20% to 30% discount that
 5 would result from an immediate sale of the Fund is unacceptable.

6 The Receiver has indicated that the orderly liquidation of the Fund will take longer than it
 7 would take to sell the Fund's portfolio at a discount, and that the Receiver might not be able to
 8 liquidate the Fund until December of 2008. (*See* Receiver's Seventh Report, p. 7, Docket No.
 9 339.) In light of this, the Commission strongly encourages the Court to authorize the Receiver to
 10 make interim disbursements to the Fund's investors, in order to expedite the return of the
 11 investors' money. The Receiver proposes making monthly disbursements to the Fund's
 12 investors, on a pro-rata basis, as the Fund's loans are paid off. (*See* Receiver's Seventh Report,
 13 p. 6:1-3, Docket No. 339.) The Commission supports this approach. The Commission also
 14 believes that it would be appropriate for the Receiver to make less-frequent interim distributions
 15 – perhaps on a quarterly basis – if doing so would reduce the costs to investors.

16 **B. The Court Should Authorize the Receiver's Recommendation for a Summary**
 17 **Claims Proceeding**

18 The Commission believes the Receiver has proposed a reasonable summary claims
 19 procedure. Because the Receiver has already identified all the Fund's investors and has been
 20 making monthly interest payments to them, the Commission believes that there will be few
 21 disputes with investors and that the investors' claims will not resort in adjudication by the Court.
 22 (*See* Receiver's Seventh Report, p. 9, Docket No. 339.)

23 Moreover, contrary to the Response by Unified Mortgage Service, Inc. to Receiver's
 24 Seventh Report and Petition for Instructions ("UMS's Response"),¹ the Receiver would not be

25
 26 ¹ UMS is not a party to this litigation. Nor has UMS properly moved to intervene in this
 27 litigation pursuant to Rule 20 of the Federal Rules of Civil Procedure. In addition to these
 28 procedural failings, the Court should not consider UMS's submission for two additional reasons.

First UMS does not have the investors' interests at heart. Indeed, as UMS admits (*see*
 UMS's Response, p.3, n.1), its only interest in this litigation is its interest in earning fees from
 the Fund and its investors – fees that the Receiver has found to be excessive.

1 the final arbiter of claims. (*See* UMS’s Response, pp. 3-4.) The Receiver’s Seventh Report
 2 clearly indicates that the Receiver would make an initial determination regarding claims and that
 3 “those claimants who disagree with the Receiver’s decision” can file a request asking the Court
 4 to adjudicate a rejected claim. (Receiver’s Seventh Report, p. 9, Docket No. 339.) Courts
 5 commonly adopt this procedure for resolving claims against a receivership.

6 The Commission is concerned that the Fund’s former affiliates – such as Emerald Bay
 7 Financial and UMS – will submit frivolous claims, in an effort to try to regain control of the Fund’s
 8 assets. The adjudication of frivolous claims could deplete the Fund’s assets and reduce the returns
 9 to investors.² The Commission is confident that the Court, acting in equity, will take necessary
 10 steps to protect the Fund’s assets from depletion by the Fund’s former affiliates and insiders – by,
 11 for example, imposing sanctions on third-party claimants who may file baseless claims.

12 **C. The Commission Does Not Favor Appointing New Managers**

13 The Commission has learned that one of the Defendants’ prior employees – Jack Mollin –
 14 has circulated a letter and a petition to investors. (*See* Declaration of Molly M. White (“White
 15 Dec.”) Ex. 1.) Mr. Mollin’s October 13, 2006 letter asks investors to sign a petition that Mr.
 16 Mollin apparently intends to submit to the Court. (*See* White Dec. Ex. 1.) The petition asks the
 17 Court to remove the Receiver from the Fund’s management and replace the Receiver with a new
 18 management board to be elected by the Fund’s shareholders. (*See* White Dec. Ex. 1.)

19 Jack Mollin was a salesperson employed by the Fund and Emerald Bay Financial, who
 20 sold shares of the Fund to investors. (*See* Tr. Trans. (1/9/2006), pp. 344:12-13, 345:6-351:1 &
 21

22 Second, UMS has not submitted competent evidence supporting its arguments. UMS
 23 claims that it has paid more than \$20 million to the Fund from the time the Receiver was
 24 appointed through October 13, 2006. (*See* Declaration of Michele Canty ¶ 4.) But Mrs. Canty,
 25 who is Defendant Brock’s daughter, does not submit any of UMS’s “books and records” that
 26 purportedly support her statement. This is particularly frustrating in light of the Receiver’s
 27 continued, unsuccessful efforts to obtain documentation from UMS. Without the supporting
 28 documentation, Mrs. Canty’s statement lacks foundation and should not be considered competent
 evidence. *See* Fed. R. Evid. 602 & 1006.

² Although the Receiver has offered to engage in the orderly liquidation of the Fund for a
 flat fee of \$12,500 per month, non-operational activities – such as court appearances and claims
 litigation – would be excluded from this management fee. (*See* Receiver’s Seventh Report, p. 6.)
 Thus, the Commission is concerned the Fund’s investors could be unduly harmed if third parties
 were to engage in protracted litigation or meritless claims.

1 362:22-364:1, White Dec. Ex. 2.) Mr. Mollin was a witness at trial. (*See* Tr. Trans. (1/9/2006),
2 pp. 344-397, White Dec. Ex. 2.) He testified that at the time of trial, he had about \$235,000 of
3 his own money invested in the Fund. (Tr. Trans. (1/9/2006), pp. 369:22-370:1, White Dec. Ex.
4 2.) Mr. Mollin also admitted that he filed a bankruptcy petition in December of 2004, in order to
5 gain control of the Fund. (*See* Tr. Trans. (1/9/2006), pp. 372:15-20, White Dec. Ex. 2.) And he
6 acknowledged that he was the person who coordinated the effort to petition the Court in
7 February of 2005. (Tr. Trans. (1/9/2006), pp. 375:24-377:12 & 383:14-385: 20, White Dec. Ex.
8 2.) Mr. Mollin disclosed none of these facts in his letter to shareholders.³ (White Dec. Ex. 1.)

9 The Commission opposes the appointment of a new management board for several
10 reasons. First, as previously indicated, the investors were fraudulently induced to purchase
11 shares of the Fund. They have never received what the Defendants promised. The Fund's
12 investors should not be forced to keep their money in this investment.

13 Second, most of the Fund's investors wish to terminate the Fund. A majority of the
14 Fund's investors has indicated that it would like the Fund to be liquidated and the Fund's assets
15 distributed to investors.

16 Third, although Mr. Mollin suggests that the Receiver is charging exaggerated costs to
17 run the Fund, there is nothing to indicate how much a new management board would cost. Mr.
18 Mollin simply claims that the new management board "would greatly reduce the expenses of the
19 fund" without backing it up with facts to support that statement. (White Dec. Ex. 1.) Even
20 worse, it appears that the management board would not report to the Court, and that the Court
21 would have absolutely no control over the new management board. Thus, there would be
22 absolutely no mechanism for controlling costs – as opposed to the Court-monitored Receiver,
23 whose fees the Court must approve. Indeed, the Fund's investors would pay any new managers a
24 premium to get up to speed on the Fund's operations. Thus, a new management board will likely
25 cost investors far more than they are paying the Receiver to manage the Fund.

26
27
28 ³ The Commission is informed that Mr. Mollin has called investors to urge them to sign the
petition to elect new managers because according to Mr. Mollin, the Receiver wants to liquidate
the Fund at a 20% to 30% loss to investors. (White Dec. ¶ 2.)

1 Finally, Mr. Mollin’s letter does not indicate how the new managers would be elected.
2 He suggests that the “new managers would have large financial investments in the fund,” but he
3 proposes no mechanism for electing new managers. Thus, it is unclear who the new managers
4 would be – whether they would be employees who ultimately answer to the Defendants and
5 former Fund management – or whether they would be independent of the Fund’s prior managers.

6 In any event, electing a new board of managers would be costly, would not carry out the
7 will of the investors, and would not be in the interests of the Fund’s investors. For these reasons,
8 the Commission opposes the imposition of a new board of managers.

9
10 DATED: November 3, 2006

/s/ Molly M. White
Molly M. White
John B. Bulgozdy
Attorneys for Plaintiff
Securities and Exchange Commission

PROOF OF SERVICE

I am over the age of 18 years and not a party to this action. My business address is:

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On November 3, 2006, I served the document entitled **SECURITIES AND EXCHANGE COMMISSION'S RESPONSE TO SEVENTH VERIFIED REPORT OF RECEIVER** on all the parties to this action addressed as stated on the attached service list:

OFFICE MAIL: By placing in sealed envelope(s), which I placed for collection and mailing today following ordinary business practices. I am readily familiar with this agency's practice for collection and processing of correspondence for mailing; such correspondence would be deposited with the U.S. Postal Service on the same day in the ordinary course of business.

PERSONAL DEPOSIT IN MAIL: By placing in sealed envelope(s), which I personally deposited with the U.S. Postal Service. Each such envelope was deposited with the U.S. Postal Service at Los Angeles, California, with first class postage thereon fully prepaid.

EXPRESS U.S. MAIL: Each such envelope was deposited in a facility regularly maintained at the U.S. Postal Service for receipt of Express Mail at Los Angeles, California, with Express Mail postage paid.

HAND DELIVERY: I caused to be hand delivered each such envelope to the office of the addressee as stated on the attached service list.

FEDERAL EXPRESS: By placing in sealed envelope(s) designated by Federal Express with delivery fees paid or provided for, which I deposited in a facility regularly maintained by Federal Express or delivered to a Federal Express courier, at Los Angeles, California.

ELECTRONIC MAIL: By transmitting the document by electronic mail to the electronic mail address as stated on the attached service list.

FAX: By transmitting the document by facsimile transmission. The transmission was reported as complete and without error.

(Federal) I declare that I am employed in the office of a member of the bar of this Court, at whose direction the service was made. I declare under penalty of perjury that the foregoing is true and correct.

Date: November 3, 2006

/s/ Magnolia M. Marcelo
MAGNOLIA M. MARCELO

1 **SEC v. EMVEST MORTGAGE FUND, LLC, et al.**
2 **United States District Court – Southern District of California**
3 **Case No. 04 CV 2295 DMS (POR)**
4 **LA-2864**

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