

USDC SCAN INDEX SHEET



CAG 1/27/05 10:06

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

59

SUPPL.

ORIGINAL

FILED

05 JAN 27 AM 9:20

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

BY *Casimier*
NUNC PRO TUNC

JAN 25 2005

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA

UNITED STATES SECURITIES AND
EXCHANGE COMMISSION,

Plaintiff,

vs.

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

Defendants.

CASE NO. 04CV2295-DMS(LSP)

**VERIFIED SUPPLEMENTAL
INFORMATION RE: FIRST
VERIFIED REPORT OF
RECEIVER; DECLARATION OF
JAMES R. FELTON IN
SUPPORT THEREOF**

Date: January 28, 2005
Time: 10:30 a.m.
Ctrm: 10
(Hon. Dana M. Sabraw)

LAW OFFICES
GREENBERG & BASS
A REGISTERED LIMITED LIABILITY PARTNERSHIP
16000 VENTURA BOULEVARD
SUITE 1000
ENCINO, CALIFORNIA 91436-2730
(818) 986-6300 (818) 986-5687
(213) 872-2655 FAX (818) 986-6534

The Receiver, Dennis Murphy, hereby submits the following supplemental information for purposes of this Court's review of his report set for January 28, 2005.

First, the Court should be aware that on January 20, 2005, the Honorable James Meyers, United States Bankruptcy Court Judge, granted the Receiver's Motion to Dismiss the involuntary bankruptcy filed against Emvest Mortgage Fund, LLC, USBC Case No. 04-10567-JM.

Second, the Plaintiff in this action has raised a conflict issue with reference to the Receiver's counsel in this matter. The basis of the alleged conflict is described in the declaration of James R. Felton attached hereto. The Receiver has reviewed this matter thoroughly with Mr. Felton and does not believe that a


LAW OFFICES
GREENBERG & BASS
A REGISTERED LIMITED LIABILITY PARTNERSHIP
16000 VENTURA BOULEVARD
SUITE 1000
ENCINO, CALIFORNIA 91436-2730
(818) 382-5200 (818) 996-5687
(213) 472-2653 FAX (818) 986-6334

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

conflict of interest exists that would require the disqualification of Greenberg & Bass. As always, to the extent that this Court disagrees, the Receiver would abide by this Court's determination in this regard.¹

Dated: January 21, 2005

GREENBERG & BASS
A Registered Limited
Liability Partnership

By: 
JAMES R. FELTON
Attorneys for the Receiver

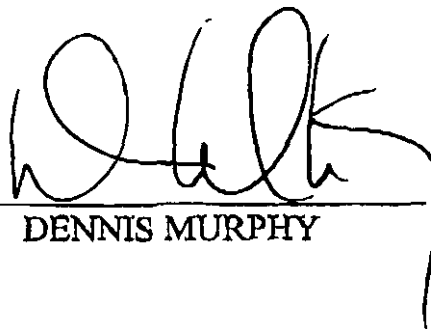
¹ Given the nature of this supplemental report, it has only been served upon the parties to this action, as opposed to the approximate 300 other creditors that were given notice of the First Report. To the extent that this Court wants the Receiver to serve all 300 creditors with this Supplement, the Receiver will do it.

VERIFICATION OF DENNIS MURPHY

I, Dennis Murphy, declare as follows:

1. I am the Court appointed Receiver in this matter. I have read the Supplemental Information Re: First Report of Receiver to be filed with this Court concurrently with this Verification and know the contents thereof. The information contained therein is true and correct of my own personal knowledge.

I declare under penalty of perjury pursuant to the laws of the State of California that the foregoing is true and correct. Executed this 21st day of January, 2005 at Pasadena, CA.


DENNIS MURPHY

Editor's Note:

State Bar Ethics Opinions cite the applicable California Rules of Professional Conduct in effect at the time of the writing of the opinion. Please refer to the California Rules of Professional Conduct Cross Reference Chart for a table indicating the corresponding current operative rule. There, you can also link to the text of the current rule.

<p>THE STATE BAR OF CALIFORNIA STANDING COMMITTEE ON PROFESSIONAL RESPONSIBILITY AND CONDUCT</p> <p>FORMAL OPINION NO. 1989-108</p>

ISSUE:

Is it unethical for an attorney to represent two clients who are not directly adverse to one another where the attorney will be arguing opposite sides of the same legal question before the same judge?

DIGEST:

Even where there is a substantial likelihood that one or both clients will be prejudiced by the representation, the attorney is not acting unethically by continuing the representation. The prudent attorney, however, will advise both clients of the other representation (if to do so will not violate the attorney/client relationship) and allow both an opportunity to seek new counsel.

AUTHORITIES**INTERPRETED:**

Rules 5-102(B) and 6-101 of the Rules of Professional Conduct of the State Bar of California (operative through May 26, 1989); Rules 3-110 and 3-310 of the Rules of Professional Conduct of the State Bar of California (operative May 27, 1989). Business & Professions Code section 6068, subdivision (e).

STATEMENT OF FACTS

An attorney represents a major manufacturer in mass tort litigation arising out of past and prospective injuries allegedly resulting from the client's products. The matter is in litigation, and after two years of discovery, the attorney has filed a motion for summary judgment which will turn on how the trial judge determines an issue of law. While the above matter is pending, in an unrelated case being handled by the same attorney for a different client, the very same legal issue is involved. However, the attorney finds that they will have to argue the opposite position with respect to the legal issue than that being taken on behalf of the product manufacturer. The manufacturer is not a party to this other litigation, and the other client is not involved in the manufacturer's litigation. Both cases are pending in federal court, and have been assigned to the same judge.

The attorney realizes that it would be in the best interests of the second client to file a motion based upon this legal issue.

DISCUSSION

The above facts represent the "worst case" scenario presented by the so-called "issues conflict" conundrum. These and other similar fact situations result in a collision of countervailing ethical and jurisprudential principles. Not surprisingly, there exists little precedent to assist the practitioner in resolving this dilemma.

Conflict of Interest

The most obvious issue presented is whether a conflict of interest can occur where two clients who have adverse interests are not directly adverse to each other in the same legal matter. Most authorities speak of conflicts of interests only where the

representation involves the same case or transaction. Normally the scope of the "adversity" which gives rise to a conflict has been limited to party identification. If the conflict of interest rules apply in these circumstances, the rule which is most applicable is 5-102(B), which prohibits the following:

A member of the State Bar shall not represent conflicting interests, except with the written consent of all parties concerned.

New Rule of Professional Conduct 3-310(B), operative May 27, 1989, provides:

A member shall not concurrently represent clients whose interests conflict, except with their informed written consent.

Despite the broad language used in the text of these rules, the "interests" usually arise within the context of the same legal matter. For example, in *Pepper v. Superior Court* (1972) 76 Cal. App.3d 252 [142 Cal.Rptr. 759], the relevant question presented was whether an attorney-member of a country club could sue the club on behalf of several unhappy members. The attorney had never represented the club, and the court held that a social relationship with the club did not per se disqualify the attorney-member from representing dissident club members.

However, in opinion 1987-93, this Committee opined that a conflict exists where a criminal defense counsel has a close personal relationship with court personnel. In broadening the reach of the conflict of interest rules, at least one court in another context has held that a member may not assume a "position" adverse or antagonistic to a client without that client's consent. In *People v. Davis* (1957) 48 Cal.2d 241, a criminal defense lawyer, without client consent, argued in closing argument that his client was at the murder scene when the client had testified that he was not. The court found this conduct unethical because the attorney was himself assuming an adverse position to the client.

The facts presented by the above hypothetical muse the possibility that the representation of one party may materially impact adversely the interests of the other. By continued representation the member will be doing his or her best to establish precedent which may be used against the other client.

Furthermore, as to both clients, the credibility of the attorney before this tribunal may be seriously at risk, as the member attempts to persuade the judge to rule first one way than the other way on the same issue. Clearly the interests of each client would be better served without the existence of the other representation.

On the other hand, there are other jurisprudential and practical reasons which argue against finding a disciplinable conflict under even these most egregious facts. Stepping back from the hypothetical which burdens our present consideration of this issue, "issues conflicts" are common and prolific in our adversarial system of justice. Almost daily the litigator or transactional attorney finds himself or herself taking positions on behalf of clients which are antithetical to another client. For example, if one finds the attorney in our hypothetical to have committed a disciplinable offense, by what reasoning would a conflict not similarly exist if an attorney arguing in favor of the discovery of medical records of an adverse party did not disclose to the client that a contrary position had been taken in another court? Or would business counsel be remiss in not advising a real estate client that he or she had argued against the inclusion of the same lease provision in another negotiation with the same adverse party?

While the facts here are extreme, to find a conflict employing a test which could be imposed uniformly to "issues conflicts" of all stripes threatens the ability of attorneys to carry out their roles in the legal system. In practice areas like family law and in small communities, the practical problems stemming from such an expansive rule would be insurmountable. Indeed, every time an attorney argues a point of law it is probable that other clients will then or later be adversely affected. In accepting an engagement, would the attorney be required to advise the client and seek consent every time an issue arises where the attorney has taken the other side?

Such a finding will also interfere with the strong social policy favoring one's right to counsel of choice. The pool of available attorneys will of necessity be diminished if withdrawal results from "issues conflicts" situations. The right to counsel of choice has been referred to by courts on several cases to support decisions finding the absence of a conflict of interest. (See *Maxwell v. Superior Court* (1982) 30 Cal.3d 606 [180 Cal.Rptr. 177]; *Pepper v. Superior Court, supra*, 76 Cal.3d 252.) Conflict of issue detection within a firm of even several attorneys using even the most sophisticated automated conflict of interest check system would be virtually impossible. There is simply no practical way that attorneys can track the legal issues that evolve during the

course of an engagement in a system which will enable the attorney to later retrieve the information before a contrary position is taken for another client.

There are a host of circumstances in the legal profession where conflicts of interest would otherwise arise but, because of strong public policy considerations, or practical concerns, the conduct does not subject the member to discipline. To mention a few of such circumstances, consider the well-recognized exceptions from the conflict rules pertaining to contingent fee agreements, in-house insurance defense counsel, and the negotiation of literary rights contracts as a means of attorney compensation. Bucking the trend are decisions such as *Wheat v. United States* (1988) U.S. [108 S.Ct. 1619], in which the United States Supreme Court denied a criminal defendant the right to waive a conflict of interest in favor of the defendant's counsel of choice. Self-limiting to the facts of that case, the court refused to allow criminal defendants to "whipsaw" trial courts by waiving conflicts to first obtain counsel of choice, and later to attack the court's accommodation on the grounds that ineffective counsel resulted.

The Committee believes that, on balance, these considerations prevent application of 5-102(B) and 3-310(B) to "issues conflicts". While we recognize the potential for harm arising from such matters, we feel that countervailing policy considerations, plus the impossible practical limitations of conflict detection, justify limiting the conflict of interest rules to traditional concepts. If it were possible to proscribe the nondisclosure and non-consensual representation defined by our hypothetical without improperly infringing on the types of inherent "issues conflicts" which occur commonly and which cannot even be fairly detected by even the most dedicated practitioner, we would not hesitate to do so. We must conclude that these most rare and extreme scenarios where potential harm is high nevertheless must yield, as they have in other instances, to higher priorities.

In so concluding, the Committee is mindful of the Discussion to new Rule of Professional Conduct 3-310 which states: "Rule 3-310 is not intended to prohibit a member from representing parties having antagonistic positions on the same legal question that has arisen in different cases, unless representation of either client would be adversely affected." The Commission which drafted this rule determined only that issues conflicts were not within the scope of rule 3-310. Stated conversely, the Commission did not intend the rule to proscribe advancing antagonistic legal positions. It has been left to determine if, under any circumstances, such dual representation is prohibited even where the representation might adversely affect the clients involved.

Despite our opinion, the prudent attorney would be well-advised to disclose "issues conflicts" where the attorney has reason to believe clients might be harmed by the continued undisclosed dual representation, thereby providing the clients an opportunity to retain other counsel. This Committee is unable to provide a definitive test as to when disclosure should be made.

There are a wide array of circumstances under which the issues conflict is likely to occur, and the risk of harm to the client will differ accordingly. Client sensitivities to this dilemma will also vary significantly by individual and the client's level of sophistication. Thus, the member necessarily must make the determination on a case by case basis. Beyond client relations considerations, the attorney must keep in mind the potential for civil liability if harm to the clients does occur which might have been avoided by timely disclosure.

Attorney Competence

A second argument in favor of proscribing the undisclosed representation of two unrelated clients where there is an "issues conflict" is that to do so violates rule 6-101 of the Rules Professional Conduct pertaining to attorney competence. The portion of that rule which might have application here is as follows:

....

(B) Unless the member associates or, where appropriate, professionally consults another lawyer who the member reasonably believes is competent, a member of the State Bar shall not

(1) Accept employment or continue representation in a legal matter when the member knows that the member does not have, or will not acquire before performance is required, sufficient time, resources and ability to, perform the matter with competence, or

8

(C) As used in this rule, the term "ability" means a quality or state of having sufficient learning and skill and being mentally, emotionally and physically able to perform legal services. (Amended by order of Supreme Court, effective October 21, 1983.)

New Rule of Professional Conduct 3-110, Failing to Act Competently, operative May 27, 1989, is in accord with rule 6-101.

The argument is that if the credibility of the member is indeed compromised by the dual representation, it is no less a disability than any other type which falls within this rule. Therefore, the attorney lacks the skill and "ability" (at least in a transactional sense) to competently represent the client. (See *People v. Saldana* (1984) 157 Cal.App.3d 443, 461.) The court in *People v. Davis, supra*, 48 Cal.2d 241, ruled that it was a violation of legal ethics for defense counsel to "impair, compromise, or destroy" his client's cause of action or defense.

However, the rule specifically defines "ability" as possessing the necessary physical, emotional, and mental faculties to perform the task competently. Thus, this Committee believes it would go beyond the scope of this rule to argue in favor of disciplining an attorney as being incompetent by virtue of the "disability" caused by taking inconsistent legal positions before the same trial judge.

Client Loyalty

The last question which must be addressed is whether the conduct violates the duty of loyalty traditionally owed to clients. There are numerous authorities which speak convincingly of the high level of fidelity, and trust that necessarily makes up part of this professional relationship. (See *People v. Davis, supra*, 48 Cal.2d 241.) Our Supreme Court has referred to this obligation as being of "the highest character." (See *Lee v. State Bar* (1970) 2 Cal.3d 927, 939.) Elsewhere, the obligation has been described to include a duty to make "a full disclosure of all facts and circumstances which are necessary to enable the parties to make a fully informed decision ... including the area of potential conflict and the possibility and desirability of seeking independent legal advice." (*Betts v. Allstate Ins. Co.* (1984) 154 Cal.App.3d 688, 716.)

However, as it relates to the function of attorneys in the legal system, even the most unsophisticated client would not assume that the attorney represents no other clients who may have divergent interests in their particular legal matters. While certainly a close question, we do not believe that there can be any reasonable expectation on the part of the client that the duty of undivided loyalty prohibits the attorney from taking an inconsistent legal position on behalf of another client. It is our opinion that if the attorney chooses not to disclose the two representations the attorney does not violate his or her duty of loyalty to the client.

This opinion is issued by the Standing Committee on Professional Responsibility and Conduct of the State Bar of California. It is advisory only. It is not binding upon the courts, the State Bar of California, its Board of Governors, any persons or tribunals charged with regulatory responsibilities, or any member of the State Bar.

ETHICS OPINIONS

9

LAW OFFICES
GREENBERG & BASS
A REGISTERED LIMITED LIABILITY PARTNERSHIP
16000 VENTURA BOULEVARD
SUITE 1000
ENCINO, CALIFORNIA 91436-2730
(818) 342-6200 (818) 986-5687
(213) 872-2653 FAX (818) 986-6534

1 PROOF OF SERVICE

2 1013A (3) CCP Revised 1/1/88

3 STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

4 I am employed in the County of Los Angeles, State of
5 California in the office of a member of the bar of this Court at
6 whose direction the service was made. I am over the age of 18 and
7 not a party to the within action. My business address is: 16000
8 Ventura Boulevard, Suite 1000, Encino, California 91436.

9 On January 21, 2005, I served the foregoing documents
10 described as:

11 VERIFIED SUPPLEMENTAL INFORMATION RE: FIRST VERIFIED REPORT OF
12 RECEIVER; DECLARATION OF JAMES R. FELTON IN SUPPORT THEREOF

13 on the interested parties in this action.

14 by placing the true copies thereof enclosed in sealed
15 envelopes addressed as stated on the attached mailing list.

16 [BY MAIL] I caused such envelope to be deposited in the mail
17 at Encino, California. The envelope was mailed with postage
18 thereon fully prepaid.

19 I am "readily familiar" with the firm's practice of collection and
20 processing correspondence for mailing. It is deposited with the
21 U.S. postal service on that same day in the ordinary course of
22 business. I am aware that on motion of party served, service is
23 presumed invalid if postal cancellation date or postage meter date
24 is more than 1 day after date of deposit for mailing in affidavit.

25 [BY FACSIMILE] I transmitted a true copy of said document by
26 facsimile machine, pursuant to Rule 2005. The facsimile machine
27 I used complied with Rule 2003(3) and no error was reported by the
28 machine. Said fax transmission(s) were directed as indicated on
the attached service list.

[BY PERSONAL SERVICE] I caused such envelope to be delivered
by hand to the offices of the addressee.

Executed on January 21, 2005, at Encino, California.

(State) I declare under penalty of perjury under the laws of
the State of California that the above is true and correct.

(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.

27 MARGARET TYNDALL
28 (Type or Print Name)

Margaret Tyndall

LAW OFFICES
GREENBERG & BASS
A REGISTERED LIMITED LIABILITY PARTNERSHIP
16000 VENTURA BOULEVARD
SUITE 1000
ENCINO, CALIFORNIA 91436-2730
(818) 392-6900 (818) 996-5487
(213) 872-2655 FAX (818) 966-6534

SERVICE LIST

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
v. EMVEST MORTGAGE FUND, et al.
CASE NO. 04CV23295-DMS (LSP)

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

Molly M. White, Esq.
Kelly Bowers, Esq.
Securities and Exchange Commission
5670 Wilshire Blvd., 11th Floor
Los Angeles, CA 90036
Fax: (323) 965-3908

Robert A. Cocchia, Esq.
B. Luke Pistorius, Esq.
McKenna, Long & Aldridge, LLP
Symphony Towers
750 B Street, Suite 3300
San Diego, CA 92101
Fax: (619) 595-5450

Dennis M. Murphy, CPA, CIRA
630 N. Rosemead Blvd., Suite 100
Pasadena, CA 91107
Fax: (626) 794-7298

David R. Clark, Esq.
Higgs, Fletcher & Mack LLP
401 West A Street, Suite 2600
San Diego, CA 92101-7913
Fax: (619) 696-1410