

ORIGINAL

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

JAMES R. FELTON, ESQ. (CA State Bar No. 138767)  
jfelton@greenbass.com  
GREENBERG & BASS LLP  
16000 Ventura Boulevard, Suite 1000  
Encino, California 91436  
Tel: (818) 382-6200 • Fax: (818) 986-6534

Attorneys for Plaintiff  
Dennis Murphy

**FILED**  
NOV 21 2005  
CLERK, U.S. DISTRICT COURT  
SOUTHERN DISTRICT OF CALIFORNIA  
BY *[Signature]* DEPUTY

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

UNITED STATES SECURITIES AND  
EXCHANGE COMMISSION,

Plaintiff,

v.

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

Defendants.

**CASE NO.: 04CV2295-DMS (LSP)**

**JUDGE:** Hon. Dana M. Sabraw

**FOURTH VERIFIED REPORT OF  
RECEIVER**

**CTRM:** 10  
**DATE:** Not Applicable  
**TIME:** Not Applicable

**Disc. Cut-off:** November 10, 2005  
**Motion Cut-off:** November 10, 2005  
**Trial Date:** January 3, 2006

**Emvest Mortgage Fund, LLC  
Receiver's Fourth Verified Report and Petition for Instructions;  
Prepared by Dennis Murphy, Permanent Receiver,  
For the Period From 8/16/05 to 11/15/05**

This "Receiver's Fourth Verified Report and Petition for Instructions" is filed on behalf of Emvest Mortgage Fund, LLC ("the Fund") in compliance with reporting requirements for Receivers under Civil Rule 66.1 (Receivers). The Receiver's preliminary report covered the period from 11/16/04 to 12/2/04, his first report covered the period from 12/3/04 to 12/30/04, his second report covered the period

**G&B**  
GREENBERG & BASS LLP

185

of

1 from 1/1/05 to 4/15/05, the third report covered the period from 4/16/05 to 8/15/05,  
2 and this fourth report covers the period from 8/16/05 to 11/15/05.

3 **1. Summary of Operations of Receiver:**

4 Stabilized operations of the business continue, with accurate and timely  
5 financial reports now being routinely prepared, with new financial controls in place,  
6 with information routinely being posted on the Fund's web site for all to see, and with  
7 the Receiver continuing to run the business on a daily basis.

8 The Receiver still continues to focus on preserving Members' capital,  
9 reconstructing records of historical loan transactions, and managing the Fund's day-  
10 to-day operations. This continues to include reducing operating costs, funding high  
11 yielding loans while maintaining underwriting standards, identifying and recovering  
12 Fund assets (such as fees which may have been diverted), and bounding various  
13 business risks faced by the Fund.

14 Here is a summary of operations related matters:

15 1.1 Continued Monthly Distributions to Members: The Court Order filed on  
16 3/2/05 allows the Receiver, at his discretion, to "resume making monthly distributions  
17 to the investors of up to 6% annually, as long as justified by the Fund's revenue". The  
18 Receiver resumed making regular monthly distributions in March 2005 at an annual  
19 rate of 6%. As shown in the 9/30/05 Financial Statements (attached as Exhibit #1),  
20 net income for the first nine months of 2005 has exceeded monthly distributions by  
21 about \$120,000; the Receiver therefore anticipates continuing these monthly  
22 distributions.

23 1.2 Emergency Partial Refunds to Members: The Receiver received permission  
24 under the Court Order filed on 3/2/05 to "make distributions to investors based on a  
25 showing of extreme hardship or emergency, not to exceed 20% of those investors'  
26 original capital". The Receiver continues, as appropriate, to make made hardship  
27 disbursements to Members, and the process is working as intended.

1           1.3 Financial Statements for Emvest, Inc.: Financial Statements for Emvest,  
2 Inc. were prepared and the 2004 tax return has been filed. Only within the past few  
3 days, and only in response to the Receiver's direct questions, has it been identified  
4 that Emvest, Inc. actually invested \$45,000 for 45 shares in Emvest Mortgage Fund II.  
5 It is still being determined why the Receiver never received any distributions or any  
6 financial reports from Fund II. Hence, the Receiver hereby requests the following on  
7 Emvest mortgage Fund II: a copy of the Subscription Agreement, the K-1 for 2004,  
8 financial statements for 12/31/04 and 6/30/05, monthly distributions, and a copy of the  
9 offering prospectus.

10           1.4 Compliance with Lending Laws: An independent analysis was done to  
11 determine whether any loans made by the Fund during the Receiver's tenure were not  
12 in compliance with applicable laws. It was determined that four loans may be out of  
13 compliance, and that a total exposure of about \$14,000 was possible. The Receiver  
14 has engaged an outside party (Skyline Funding) to prepare corrected paperwork to  
15 bring all of the loans into compliance. Since the Receiver relied on the compliance  
16 representations of the mortgage brokers who originated these loans, he shall seek any  
17 refunds of fees from those loan brokers.

18           1.5. Change in Loan Servicing Agent from UMS to FCI: As per the  
19 methodology specified by the Court, bids for loan servicing were elicited from other  
20 qualified providers. Unified Mortgage Service, Inc. ("UMS") was then given to the  
21 right of first refusal to match the terms of the service provider that was to be awarded  
22 the contracts. Unified declined to reduce their fee structure to match the winning bid.  
23 Hence, all 17 of the Fund's existing loans for which UMS provided a Loan Servicing  
24 Agreement have been kept at UMS; except for 6 loans in foreclosure, all 30 of the  
25 Fund's other existing loans have been awarded to FCI National Lender Services  
26 ("FCI") for loan servicing. Based on the analysis done as part of the bidding process,  
27 this change could result in a savings to the Fund of approximately \$70,000 per year  
28 for loan servicing.

1           1.6 Posting of Items on Fund's Web Site: The Fund's web site  
2 (<http://emvest.info>) continues to serve as a vehicle for timely dissemination of  
3 information to all of the Fund's stakeholders. During the nine months that the web  
4 site has been in operation, there have been 1,402 unique (i.e. different) visitors to the  
5 site resulting in 6,367 hits. Thus, the site is fulfilling its intended purpose.

6 **2. Financial Statements:**

7           Regular financial statements which conform to Generally Accepted Account  
8 Principles ("GAAP") continue to be prepared on a timely basis, and continue to be  
9 posted regularly on the Fund's web site (<http://emvest.info>) by about the 20<sup>th</sup> of the  
10 following month. Attached, as Exhibit #1 are Financial Statements as of 9/30/05 for  
11 the Fund, including a Balance Sheet, Income Statement, and Statement of Investors'  
12 Equity.

13           2.1 Income Statement: For the first nine months of 2005, the Fund had Net  
14 Income of \$722,746 (which includes a Foreclosed Asset Expense of \$244,125).  
15 Since the Net Income for the Fund for all of 2004 was \$721,953, the Net Income for  
16 the first nine months of 2005 exceeds the Net Income for all of 2004, even with the  
17 expenses in 2005 due to foreclosures and all of the Receiver's accrued fees included.  
18 Since the Income Statement is accrual based (rather than cash based), the 2005 net  
19 income also includes expenses for 100% of the fees billed by the Receiver and his  
20 attorney (although they were not actually paid). The accrued unpaid fees are shown as  
21 Current Liabilities on the Balance Sheet. Thus, even with 100% of the fees for the  
22 Receiver and his attorney deducted from net income, the Fund is still outperforming  
23 2004. Hence, there is reason for continued optimism on net income.

24           2.2 Statement of Members Equity: The equity for current Members has actually  
25 continued to improve since the start of 2005, although it takes an explanation to show  
26 that. Since "hardship withdrawals" of \$602,658 have been paid so far in 2005 to  
27 Members, and since Net Income for 2005 has exceeded Distributions to Members, the  
28 equity for current Fund Members has actually increased by \$120,088 during 2005.

1 **3. Reconstruction of Historical Loan Transaction Records:**

2 As has been previously acknowledged, the records of the Fund's historical loan  
3 transactions were incomplete and disorganized. The Receiver has worked  
4 systematically to reconstruct historical loan transaction records for all parties to use.  
5 The Receiver's goal has been to identify and document as many as possible of the  
6 Fund's historical loan transactions and to aggregate that information into one common  
7 database; sources of information have included the Fund's books and records,  
8 documents provided by Emerald Bay, and documents obtained through discovery by  
9 the SEC. Previous Receiver's Reports have included detailed partial listings of loans  
10 and interim analysis.

11 The structure of the database was established, and data has been entered into it  
12 as source documents have been obtained through the SEC's formal discovery process.  
13 As of 11/15/05, 898 total loans have been identified from various sources as having  
14 been funded by the Fund. The Receiver currently has loan closing statements for 574  
15 loan transactions; certain of the 324 currently undocumented loans may be duplicates  
16 of other loans or could be the result of incorrect financial records.

17 Although the Receiver has been unable to obtain all of the historical data that he  
18 wanted, enough data is available to provide an overall picture of historical operations.  
19 This data shall be made available both to the Defendants and to the SEC.

20 **4. Unresolved Variances from Analysis of Financial Records:**

21 Based on analysis of the data in the Fund's reconstructed books and records, the  
22 Receiver is unable to reconcile certain financial variances. The Receiver requests  
23 refunds with accrued interest and/or the Defendants' assistance in showing why these  
24 amounts were not in fact funds diverted from the Fund by the Defendants.

25 **4.1. Overpayment to Former Members Who Withdrew from the Fund:**

26 From the inception of the Fund in 2002 until the Receiver was appointed at the end of  
27 2004, a total of 25 Members withdrew completely from the Fund; when they left, they  
28 received payoffs calculated by the Defendants. In Exhibit #2, an analysis is provided

G&B  
GREENBERG & BASS LLP

1 which shows that these Members were overpaid by \$120,334 when they left. It is  
2 seen that only one (or at most two) of the 25 departing Members received the correct  
3 payoff amounts. Hence, the Receiver hereby makes a demand of the officers and  
4 directors of the Fund and its Managing Member (Emvest, Inc.) to repay to the Fund  
5 the amount of \$120,334 plus accrued interest until repaid.

6 4.2 Excess Commissions on Purchase of Florida Loan Portfolio: The Receiver  
7 (and the SEC separately) have both previously identified that the Defendants received  
8 a commission of \$186,520 on the purchase for the Fund of a loan portfolio from First  
9 NLC Financial Services, LLC. This amount represents a 43% commission, which the  
10 Receiver believes to be far beyond the normal commission for a transaction of this  
11 type.

12 After being questioned about his views on the appropriateness of this  
13 commission percentage in his deposition, the Receiver conducted a survey of  
14 experienced industry practitioners to determine what percentage commission would be  
15 reasonable and customary for this type of transaction. Attached as Exhibit #3 are  
16 copies of the letter from the Receiver requesting guidance and all five responses. The  
17 consensus of the five responses is that 5% commission would be reasonable and  
18 customary. Hence, based on the portfolio purchase price of \$435,216, a 5%  
19 commission would be \$21,721. Thus, the Receiver hereby makes demand of the  
20 Defendants for a refund of excess commissions taken of \$164,759 (i.e. \$186,520  
21 actually paid, less \$21,761 for a reasonable commission) plus accrued interest.

22 4.3 Points Due to Fund but Diverted to Related Entities: In order to try to  
23 identify if and/or how money may have moved (or been diverted) from the Fund to  
24 related entities such as Emvest, Inc, Emerald Bay Financial and Emerald Bay  
25 Funding, available bank records from those entities were compared with loan closing  
26 statements and the Fund's books and records. An analysis was done by the Receiver  
27 for the five non-Fund bank accounts for which bank statements and records were  
28 available. (The analysis did not include two other non-Fund bank accounts and about

1 300 closing statements which were not available.) As shown in Exhibit #4, the five  
2 bank accounts analyzed were for Emvest, Inc., Emerald Bay Funding, and Emerald  
3 Bay Financial (three accounts).

4 The analysis started with loan closing statements which showed points/fees due  
5 to the Fund, and tracked deposits into these five accounts from the Fund or from loans  
6 originated by the Fund. The analysis also tracked the situation where a check was  
7 deposited into the Fund and then a check for the exact amount was immediately  
8 written to a related non-Fund account. Of the \$378,995 of relevant deposits, all but  
9 \$93,249 was accounted for in the audit trail.

10 The analysis shows in detail how the amount of \$378,995 was diverted from the  
11 Fund into the bank accounts of the other related entities. Hence, demand is hereby  
12 made to the Defendants to reimburse those amounts plus accrued interest.

13 4.4. Syndication Fees in Excess of 4%: On page 9 of the Fund's Prospectus  
14 dated 6/2/04, the Defendants state that the syndication costs shall be 4% for  
15 commissions plus about \$7,500 for other offering costs. As shown in Exhibit #5,  
16 based on the total amount of \$20,310,710 collected from investors, the syndication  
17 costs should have been \$819,928. The actual syndication costs of \$1,028,444 were  
18 25.4% greater than what was stated in the Prospectus. Hence, the Receiver demands  
19 from the Defendants a refund of the excess syndication costs of \$208,516 plus accrued  
20 interest.

21 4.5 Lack of Effort by Defendants to Collect on Receivable from Heritage and  
22 Tristar: The Fund's 12/31/03 Balance Sheet showed an Other Receivable in the  
23 amount of \$117,824.95 due from Heritage Mortgage Fund and Tristar. None of this  
24 amount was ever collected, leaving the amount of \$117,824.95 to be written off as of  
25 12/31/04.

26 As described in the SEC's Opposition to Defendants' Motion for Summary  
27 Judgment (2: 20-21), Heritage and Tristar were investment funds managed by the  
28 Defendant that were rolled over into the Fund. As memorialized in an internal memo

1 from William Kennedy to the Receiver dated 11/14/05 (attached as Exhibit #6), it  
2 appears that Defendant Lyle Brock made no effort to collect this receivable.  
3 Because of this breach of fiduciary responsibility resulting in a loss of \$117,824.95 to  
4 the Fund, demand is hereby made to the Defendants for reimbursement of  
5 \$117,824.95 plus accrued interest until repaid.

6 4.6 Reconciliation of UMS and Form 1098's for Interest Earned by Fund in  
7 2004: A reconciliation was done for selected loans for interest income earned by the  
8 Fund in 2004; the monthly Lender's Statement data from Unified Mortgage Services,  
9 Inc. (UMS) which shows amounts paid to the Fund were compared with the Form  
10 1098's issued by UMS to borrowers on interest paid. These two amounts should  
11 match; that is, the interest shown as paid by the borrowers should equal the interest  
12 income reported by UMS to the Fund. (Since UMS only provided certain Form  
13 1098's, this analysis doesn't track all loans; only loans for which the Form 1098's  
14 were provided are used in the analysis.)

15 As shown in Page 1 of Exhibit #7, the amount reported to borrowers for interest  
16 paid in 2004 is \$32,166 greater than the amount reported to the Fund for 2004. Some  
17 of this variance may be explained by observing that there is up to a 30 day lag from  
18 when UMS receives funds until they send them to the Fund. Hence, a mortgage  
19 payment received by UMS in December (and thus reported to the borrower on their  
20 Form 1098) might not be reflected until the January Lender's Statement.

21 To test this thesis of lagged reporting of payments, the January 2005 Lender's  
22 Statement was examined for the three loans with the largest variances. It is seen from  
23 Page 3 of Exhibit #7 that \$11,868 of variance for these three loans is still not  
24 explained. Hence, the Receiver requests an explanation from UMS of the variance.  
25 Without an explanation from UMS, one theory is that certain funds due to the Fund  
26 may have been diverted from the Fund.

27 ///  
28 ///

G&B  
GREENBERG & BASS LLP

1           4.7 Possible Missing Interest Income from Funded Loans for 2004: As a test to  
2 try to determine whether all interest income was reaching the Fund, an analysis was  
3 done to compare loans funded in 2004 with the amount of interest received on those  
4 loans. (This analysis was only done for 2004, since data for 2003 was incomplete.)  
5 As shown in Exhibit #8, this analysis yielded a list of the 28 loans on the Fund's  
6 books in 2004 where there is either a loan closing statement or an entry on Silvia De  
7 Anda's listing of loans (known as "Exhibit 22") and where no interest income was  
8 received by the Fund for that loan number. Using the Fund's books and records to  
9 identify the number of days from when each loan appeared to when each loan  
10 disappeared from the books, and assuming an interest rate of 12.5%, the amount of  
11 "missing" interest was calculated to be \$37,266 for 2004. The Fund's books show  
12 that these loans were funded; hence, either no interest was paid or some other entity  
13 received the interest. An explanation of this variance is requested.

14           4.8 Variance Overview of Other Loans for 2004: For the loans not already  
15 analyzed elsewhere in this report (because requested data has not been received from  
16 UMS), a macro level analysis was done. Just as would be done in an audit to test and  
17 verify gross income, a comparison was done.

18           As was done above, this analysis compares 2004 interest actually received by  
19 the Fund with an estimate of what interest should have been received by the Fund. As  
20 shown in Exhibit #9, it is seen that \$1,106,430 was the estimate of what should have  
21 been received, as compared with \$820,106 that was actually received. This variance  
22 of \$286,324 is 34.9% of the actual interest received. While there certainly must be  
23 logical explanations for some of this variance, the difference is far too great to ignore.  
24 Since complete loan servicing data has already been requested but not provided by  
25 UMS, complete loan servicing data must now be made available so that it may be  
26 determined whether any these variances were actually diverted from the Fund.

27           4.9 Altered Checks from Southland Title Co. Received on 11/16/05: As has  
28 been explained in previous Receiver's Reports, loan closing statements were

1 compared to the Fund's books and records. When a loan closing statement shows that  
2 points and/or fees were due to the Fund, but when the Fund's books don't reflect  
3 receipt of that payment, the Receiver requested copies of both sides of the cancelled  
4 check from the title company involved. This permitted the Receiver to determine who  
5 received the diverted funds. To date, three of the six title companies involved have  
6 provided copies of checks.

7 On 11/16/05, Southland Title provided copies of 58 such checks totaling  
8 \$63,328. Although these checks were received too late to be included in the  
9 Receiver's analysis for this report, the checks are attached as Exhibit #10 to  
10 demonstrate a distinct pattern of alteration of checks and/or diversion of money due  
11 to the Fund. It even raises the question of liability on the part of the banks that cashed  
12 these obviously altered checks.

### 13 **5. Petition for Instructions:**

14 The Receiver respectfully petitions the Court for instructions in the following  
15 matters:

16 5.1 Actions to Take Against the Defendants, their Officers and Directors: A  
17 variance of more than \$1 million has been identified, and a broad pattern of  
18 questionable actions has been documented which have resulted in significant  
19 monetary damage to the Fund and its Members. To remedy this situation, the  
20 Receiver requests direction from the Court on how to proceed, when to proceed, and  
21 who to pursue. For example, demands for reimbursement may be made from a myriad  
22 of involved entities and their officers and directors (even including the banks that  
23 cashed obviously altered checks), regulatory agencies (e.g. Attorney General,  
24 Department of Real Estate) may be called in, and even the District Attorney may be  
25 contacted to investigate possible criminal activity.

26 For example, in addition to the officers of Emvest, Inc. who have responsibility,  
27 there are directors who received compensation in 2004; therefore, these directors  
28 should also accept responsibility (and liability) for the actions of Emvest, Inc. These

1 paid directors are: Milon L. Brock, Gregg A. Johnson, Timothy J. Canty, III, Steven  
2 C. Bradley, William Thrailkill, and Sylvia De Anda.

3  
4 Dated: November 18, 2005

GREENBERG & BASS  
A Registered Limited  
Liability Partnership

6  
7 By: 

8 JAMES R. FELTON

9 Attorneys for Receiver,  
10 Dennis Murphy

11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28  
  
GREENBERG & BASS LLP

VERIFICATION OF DENNIS M. MURPHY

I, Dennis M. Murphy, declare as follows:

I am the Court appointed Permanent Receiver in this matter. I have read the Fourth Report of Receiver to be filed 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 10<sup>th</sup> day of November, 2005 at Pasadena, CA.



---

DENNIS M. MURPHY