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JS-6

UNITED STATES DISTRICT COURT  
CENTRAL DISTRICT OF CALIFORNIA

|                            |                                    |
|----------------------------|------------------------------------|
| SECURITIES & EXCHANGE )    | Case No. CV 08-1323-VAP (OPx)      |
| COMMISSION, )              |                                    |
| Plaintiff, )               | [Motion filed on June 11,          |
| v. )                       | 2009]                              |
| JAMES B. DUNCAN; et al., ) | <b>ORDER GRANTING PLAINTIFF'S</b>  |
| Defendants.)               | <b>MOTION FOR SUMMARY JUDGMENT</b> |

**I. BACKGROUND**

Plaintiff the Securities and Exchange Commission ("Commission") filed its Complaint in this action on February 27, 2008, alleging that defendants engaged in two offering frauds orchestrated by defendant James B. Duncan ("Duncan"): (1) an offering by defendant Total Return Fund, LLC ("TRF"), and (2) an offering by defendants Stonewood Consulting, Inc. ("Stonewood") and Pacific Wealth Management, LLC ("PWM"), or the "Stonewood/PWM offering." Defendants Hendrix Montecastro ("Montecastro") and Maurice McLeod ("McLeod")

1 participated with Duncan in the Stonewood/PWN offering.  
2 The gravamen of the Commission's action is that the  
3 defendants were running a Ponzi-like scheme in which they  
4 fraudulently obtained investments, and used investor  
5 funds to pay personal expenses and to pay earlier  
6 investors.

7  
8 Based upon these allegations, the Commission asserts  
9 three claims for relief against Defendants: first, for  
10 the unregistered offer and sale of securities in  
11 violation of sections 5(a) and 5(c) of the Securities  
12 Act, 15 U.S.C. §§ 77e(a) and 77e(c); second, for fraud in  
13 the offer or sale of securities in violation of section  
14 17(a) of the Securities Act; and third, for fraud in  
15 connection with the purchase or sale of securities in  
16 violation of section 10(b) of the Exchange Act and Rule  
17 10b-5 thereunder, 17 C.F.R. § 240.10b-5.

18  
19 On June 11, 2009, the Commission filed the instant  
20 Motion for Summary Judgment. As to defendants Duncan and  
21 Montecastro, the Commission is seeking disgorgement,  
22 civil penalties, and an order permanently enjoining them  
23 from further violations of the registration and anti-  
24 fraud provisions of the federal securities laws. As to  
25 defendant McLeod, the Commission seeks disgorgement and a  
26 civil penalty pursuant to the Judgment of Permanent  
27 Injunction against McLeod entered August 28, 2008. See

28

1 August 28, 2008 Judgment of Permanent Injunction Against  
2 Maurice E. McLeod at ¶ IV (Docket No. 82). Finally, the  
3 Commission seeks a default judgment against defendants  
4 TRF, Stonewood, and PWM, and a permanent injunction  
5 against each entity enjoining them from further  
6 violations of the federal securities laws.

7  
8 The Commission's Motion includes the following  
9 supporting materials: Statement of Uncontroverted Facts  
10 and Conclusions of Law ("SUF"), Declaration of Sara D.  
11 Kalin ("Kalin Decl."), Declaration of Pamela Chattoo  
12 ("Chattoo Decl."), Declaration of William J. Michiels  
13 ("Michiels Decl."), Declaration of Kent C. Bailey  
14 ("Bailey Decl."), Declaration of Phillip H. Henry ("Henry  
15 Decl."), Declaration of Maurice M. McLeod ("McLeod  
16 Decl."), Declaration of Christopher Oetting ("Oetting  
17 Decl."), Declaration of Vicky R. Reiss ("Reiss Decl."),  
18 Declaration of Anna Richter ("Richter Decl."), and  
19 Declaration of Deborah L. Weber ("Weber Decl.").

20  
21 The Commission noticed the Motion for a hearing date  
22 of July 6, 2009, at 10:00 a.m. Under Local Rule 7-9, a  
23 party must file Opposition papers no later than 14 days  
24 before the date designated for the hearing of the Motion.  
25 Defendants' Opposition was therefore due on June 22,  
26 2009, but no Defendant has filed timely Opposition.

27  
28

1 **II. LEGAL STANDARD**

2 A motion for summary judgment shall be granted when  
3 there is no genuine issue as to any material fact and the  
4 moving party is entitled to judgment as a matter of law.  
5 Fed. R. Civ. P. 56(c); Anderson v. Liberty Lobby, Inc.,  
6 477 U.S. 242, 247-48 (1986). The moving party must show  
7 that "under the governing law, there can be but one  
8 reasonable conclusion as to the verdict." Anderson, 477  
9 U.S. at 250.

10  
11 Generally, the burden is on the moving party to  
12 demonstrate that it is entitled to summary judgment.  
13 Margolis v. Ryan, 140 F.3d 850, 852 (9th Cir. 1998);  
14 Retail Clerks Union Local 648 v. Hub Pharmacy, Inc., 707  
15 F.2d 1030, 1033 (9th Cir. 1983). The moving party bears  
16 the initial burden of identifying the elements of the  
17 claim or defense and evidence that it believes  
18 demonstrates the absence of an issue of material fact.  
19 Celotex Corp. v. Catrett, 477 U.S. 317, 323 (1986).

20  
21 If the moving party has the burden of proof at trial  
22 (the plaintiff on a claim for relief, or the defendant on  
23 an affirmative defense), the moving party must make a  
24 showing sufficient for the court to hold that no  
25 reasonable trier of fact could find other than for the  
26 moving party. See Calderone v. United States, 799 F.2d  
27 254, 259 (6th Cir.1986) (quoting W. Schwarzer, Summary  
28

1 Judgment Under the Federal Rules: Defining Genuine Issues  
2 of Material Fact, 99 F.R.D. 465, 487-88 (1984)). This  
3 means that, if, as here, the moving party has the burden  
4 of proof at trial, that party "must establish beyond  
5 peradventure all of the essential elements of the claim  
6 or defense to warrant judgment in [that party's] favor."  
7 Fontenot v. Upjohn Co., 780 F.2d 1190, 1194 (5th  
8 Cir.1986).

9  
10 The burden then shifts to the non-moving party to  
11 show that there is a genuine issue of material fact that  
12 must be resolved at trial. Fed. R. Civ. P. 56(e);  
13 Celotex, 477 U.S. at 324; Anderson, 477 U.S. at 256. The  
14 non-moving party must make an affirmative showing on all  
15 matters placed in issue by the motion as to which it has  
16 the burden of proof at trial. Celotex, 477 U.S. at 322;  
17 Anderson, 477 U.S. at 252; see also William W. Schwarzer,  
18 A. Wallace Tashima & James M. Wagstaffe, Federal Civil  
19 Procedure Before Trial, 14:144.

20  
21 A genuine issue of material fact will exist "if the  
22 evidence is such that a reasonable jury could return a  
23 verdict for the non-moving party." Anderson, 477 U.S. at  
24 248. In ruling on a motion for summary judgment, the  
25 Court construes the evidence in the light most favorable  
26 to the non-moving party. Barlow v. Ground, 943 F.2d  
27 1132, 1135 (9th Cir. 1991); T.W. Electrical Serv. Inc. v.

28

1 Pacific Elec. Contractors Ass'n, 809 F.2d 626, 630-31  
2 (9th Cir. 1987).

3

4 **III. UNCONTROVERTED FACTS<sup>1</sup>**

5 **A. Undisputed Facts Related to the TRF Offering**

6 TRF was a Nevada limited liability company that  
7 Duncan had formed in 2003, with offices located in  
8 Orange, California. (SUF 27.) Duncan owned and  
9 controlled TRF, and controlled all of the financial  
10 transactions involving TRF's bank account, which were  
11 done either at Duncan's express direction or with his  
12 express approval. (Id. ¶ 28.)

13

14 TRF filed no registration statement with the  
15 Commission before July 2007 with respect to any  
16 securities offered and/or sold pursuant to the provisions  
17 of the Securities Act of 1933 (the "Securities Act") or  
18 the Securities Exchange Act of 1934 (the "Securities  
19 Exchange Act"). (Id. ¶ 28)

20

21 Between March 2004 and September 2006, Duncan sold  
22 approximately \$1.9 million of TRF securities to  
23 approximately 24 investors in four states. (Id. ¶ 39.)

24

25

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26 <sup>1</sup> The Court adopts as uncontroverted those material  
27 facts that are supported by evidence proffered by the  
28 Commission. The Commission proffered many background  
facts that are not material to its claims; the Court  
finds it unnecessary to refer to those facts in this  
Order.

1 Duncan directed and supervised the preparation of various  
2 offering documents that were provided to potential TRF  
3 investors, including a "Private Placement Memorandum"  
4 ("PPM"), a "trifold offering brochure," and "Instructions  
5 for Subscription." (Id. ¶ 40.) Duncan also caused an  
6 Internet site to be created for the offering,  
7 www.trfillc.com. (Id. ¶ 41.) Duncan personally solicited  
8 investors for the TRF offering, and caused subscription  
9 information to be sent to potential investors. (Id. ¶  
10 42.) TRF's offering documents stated that TRF was  
11 offering securities for sale and that the offering was  
12 not registered with the Commission; in fact, TRF did not  
13 have an offering registered with the Commission. (Id. ¶  
14 43.)

15  
16 Duncan and TRF represented that 95% of investor funds  
17 would be used for investments and fees were limited to  
18 5%. (Id. ¶ 45.) Defendants represented that investments  
19 made by TRF were "secured and collateralized using real  
20 estate, acquisition of business with positive cash flow  
21 and accounts receivable backed by government funding."  
22 (Id. ¶ 44.) Defendants further represented that "over 80%  
23 of all accounts receivable in this program are government  
24 backed and funded." (Id.) Duncan and TRF also  
25 represented that TRF was providing factoring services to  
26 "businesses in the Western United States, primarily in  
27 California, Nevada, and Arizona" and that the "majority  
28

1 of these contractors work on Federal, State and Municipal  
2 funded projects. The most common projects are water  
3 treatment plants." (Id. ¶ 45.)

4  
5 No such investments were made. (Id. ¶ 46.) Instead,  
6 some of the TRF investor funds were disbursed from the  
7 account in cash to Duncan, to Duncan's wife, or to pay  
8 Duncan's personal expenses. (Id. ¶ 50.) The majority of  
9 TRF investor funds that were deposited into TRF's bank  
10 account were disbursed shortly thereafter to a company  
11 named Pilo USA, Inc. ("Pilo"), which apparently was  
12 controlled by an associate of Duncan. (Id. ¶ 48.) A few  
13 days after the disbursement from TRF to Pilo, Pilo sent  
14 the funds to defendant Oetting Industries, Inc. ("Oetting  
15 Industries"). (Id. ¶ 49.) Duncan then directed the  
16 disbursement of the TRF investor funds from the Oetting  
17 Industries bank account. (Id. ¶¶ 48-49.) From the  
18 Oetting Industries account, Duncan directed TRF investor  
19 funds to (i) be disbursed to Duncan in cash, (ii) pay  
20 personal expenses of Duncan and his friends, (iii)  
21 provide funds for his wife, and (iv) be disbursed for  
22 Duncan's benefit. (Id. ¶¶ 48.)

23  
24 Duncan also used new TRF investor funds to pay  
25 earlier TRF investors. (Id. ¶ 52.) TRF records, produced  
26 by Duncan, record a transaction in October 2004, where  
27 \$208,000 received from a TRF investor was disbursed the

28

1 next day to make a "complete payoff" to one TRF investor  
2 and a "partial payoff" to a second TRF investor. (Id.)

3

4 TRF failed to file an answer to the complaint filed  
5 in this action, and on May 28, 2008, the Clerk of the  
6 Court entered a default against TRF pursuant to  
7 Fed. R. Civ. P. 55(a). (Id. ¶ 29.)

8

9 **B. Undisputed Facts Relating to the Stonewood/PWM**  
10 **Offering**

11 Beginning in June 2004 through July 2007, Montecastro  
12 operated a business under the name Stonewood. (Id. ¶  
13 16.) Stonewood was (i) a real estate broker that  
14 arranged the purchase of houses for investors; and (ii) a  
15 mortgage loan broker that processed loan applications  
16 (including verification of information) and brokered  
17 loans to various lenders. (Id.) Montecastro was Chief  
18 Executive Officer, Secretary, and Chief Financial Officer  
19 of Stonewood. (Id. ¶ 17.) Duncan and Defendant  
20 Montecastro were partners in defendant Stonewood. (Id. ¶  
21 8.)

22

23 Stonewood filed no registration statement with the  
24 Commission prior to July 2007 with respect to any  
25 securities offered or sold pursuant to the provisions of  
26 the Securities Act or the Exchange Act. (Id. ¶ 33.)

27

28

1 Duncan owned and controlled the limited liability  
2 company that became defendant PWM and caused the name to  
3 be changed to PWM. Duncan effectively controlled PWM.  
4 (Id. ¶ 9.) Duncan installed McLeod as the President of  
5 PWM. (Id. ¶ 36.) McLeod took instructions from Duncan  
6 and Montecastro, however. (Id. ¶ 36.)

7  
8 PWM filed no registration statement with the  
9 Commission prior to July 2007 with respect to any  
10 securities offered or sold pursuant to the  
11 provisions of the Securities Act or the Exchange Act.  
12 (Id. ¶ 37.)

13  
14 From 2004 through 2007, defendants Duncan,  
15 Montecastro, and McLeod, through Stonewood and PWM,  
16 engaged in a complex offering fraud that raised over \$27  
17 million from investors. (Id. ¶ 54.) In contrast to the  
18 TRF offering, defendants did not provide investors with  
19 any documents in the Stonewood/PWM offering; they wanted  
20 to avoid creating a "paper trail." (Id. ¶ 59.) Instead,  
21 defendants used three techniques to recruit investors who  
22 they called "Core Clients" for the Stonewood/PWM  
23 offering: (1) telephone banks staffed by salespersons who  
24 used scripted sales pitches; (2) word of mouth from  
25 existing Core Clients to friends, relatives, and members  
26 of organizations to which Core Clients belonged, such as  
27 religious or military groups; and (3) so-called

28

1 "Investment Seminars" for Core Clients and potential  
2 clients staged in hotel conference centers. (Id. ¶¶ 57,  
3 65-67.)

4  
5 Defendants sometimes held themselves out as a  
6 "Christian organization," used a church pastor to recruit  
7 investors, and referred to "God's will" during  
8 presentations at investment seminars. (Id. ¶ 96.)  
9 Defendants repeatedly touted Duncan's financial  
10 expertise, and told investors that Duncan and Montecastro  
11 were millionaires. (Id.) Using these techniques,  
12 Defendants found numerous Core Clients in California and  
13 Arizona. (Id. 62.)

14  
15 Defendants offered to help Core Clients achieve  
16 "financial freedom" or become "millionaires." (Id. ¶ 55.)  
17 As Montecastro admitted, he sold investors "a  
18 dream." (Id.) Investors were informed that they must  
19 follow "three rules" to invest with defendants: (1) give  
20 complete control of their financial affairs to  
21 Stonewood/PWM; (2) trust the decisions made for them  
22 without asking questions; and (3) commit to invest for a  
23 period of three years. (Id. ¶ 56.) Defendants then  
24 made all investment decisions for Core Clients. (Id. ¶¶  
25 60-61.) Defendants represented to investors that they  
26 would purchase investment homes that would be sold at a  
27 profit at the end of three years. Defendants also

28

1 represented that they could provide some or all of the  
2 funds needed to help Core Clients purchase real estate  
3 because defendants had "hard money" investors who were  
4 willing to provide funds. (Id. ¶ 58.) Defendants also  
5 told investors that they invested funds in precious  
6 metals, foreign currency, and stocks. (Id. ¶ 65.)

7  
8 Defendants did not conduct an investment business.  
9 (Id. ¶ 68.) The Stonewood/PWM offering was in fact a  
10 complex and evolving Ponzi-like scheme. (Id. ¶ 68.)  
11 Defendants used the funds generated through Stonewood/PWM  
12 to pay personal expenses of Duncan and others, provide  
13 funds to Montecastro, pay old investors with new money,  
14 make down-payments on investment homes, and to make  
15 mortgage payments for Core Clients through so-called  
16 "concession fees." (Id. ¶ 58, 68.) Concession fees were  
17 generated when defendants arranged for the purchase of  
18 "investment homes" for Core Clients and obtained  
19 financing based on an inflated purchase price, which was  
20 higher than the sales price received by the seller. (Id.  
21 ¶ 58.)

22  
23 Defendants were able to obtain loans that generated  
24 concession fees because they processed the loan  
25 applications, obtained the appraisals, verified the loan  
26 documentation, and then brokered the loan to a lender who  
27 provided funding. (Id. ¶ 89.) Defendants maintained a  
28

1 "stable" of appraisers who provided appraisals that  
2 supported the inflated loan amounts. (Id. ¶ 87.)  
3 Defendants also included fraudulent "verification of  
4 deposit" information to support the mortgage loan  
5 applications. (Id. ¶ 90.) The false verification of  
6 deposit information and forms were provided by Duncan and  
7 misrepresented the Core Clients' assets to the lenders.  
8 (Id. ¶¶ 90-91.)

9

10 Defendants failed to disclose the concession fees to  
11 many investors, or misrepresented to investors that the  
12 concession fees would be invested for them in other  
13 assets. (Id. ¶¶ 85-86.) Defendants also failed to  
14 disclose that concession fees were being used to leverage  
15 the scheme, that is, to provide funds to purchase more  
16 investment houses and generate more fees. (Id. ¶¶ 94-95.)  
17 Defendants failed to disclose that concession fees  
18 generated by new Core Clients were used to pay mortgages  
19 of earlier clients. (Id. ¶ 85-86.)

20

21 Defendants also obtained funds directly from  
22 investors through 401(k) rollovers, credit card advances,  
23 refinancing investors' personal residences, or deposits  
24 of investor funds. (Id. ¶ 64.) In connection with  
25 refinancing investors' personal residences, defendants  
26 took care of all aspects of arranging the refinancing,  
27 disbursing funds to investors, and instructing investors

28

1 to send those funds to one of defendants' companies as an  
2 investment. (Id. ¶ 64.) Defendants' then used these  
3 funds to perpetrate the Ponzi-like scheme, rather than  
4 for legitimate investments as Defendants promised. (Id.  
5 ¶¶ 73-75.

6  
7 While touting Duncan's financial expertise and his  
8 status as a millionaire, Defendants failed to disclose  
9 that Duncan had a history of state securities law  
10 violations, which includes orders issued against him in  
11 2002, 2004, and 2005. (Id. ¶¶ 4-6, 96-98.) In addition,  
12 McLeod regularly touted that PWM was a "Christian  
13 organization" but failed to disclose his criminal record.  
14 (Id.) Duncan installed McLeod as President of PWM, but  
15 told McLeod not to disclose his criminal history to  
16 investors. (Id. ¶ 2425.)

17  
18 As he had during the TRF offering, Duncan used  
19 investors funds from Stonewood/PWM to pay his exorbitant  
20 living expenses, which he hid by using nominees and third  
21 parties. (Id. ¶¶ 76-77, 82.) Duncan spent lavishly on  
22 frequent trips to Las Vegas. (Id. ¶¶ 78, 81.) Duncan's  
23 credit card charges and luxury car expenses paid through  
24 just one of his nominees exceeded \$271,000 for only seven  
25 months of 2006. (Id. ¶ 78.)

26 ///

27

28

1 Defendants took several steps to evade detection.  
2 First, when the real estate community became suspicious  
3 of Stonewood because of the unusually high fees it  
4 generated, Duncan created PWM as the front for the fraud,  
5 while real estate transactions continued to be arranged  
6 through Stonewood. (Id. ¶ 104.) Second, defendants  
7 laundered the concession fees through Oetting Industries,  
8 which then doled out the money to Duncan and Montecastro.  
9 (Id. ¶¶ 103, 105.) Third, as the scheme was collapsing,  
10 Defendants destroyed documents at Duncan's direction.  
11 (Id. ¶¶ 114-115.) Fourth, after this action was filed,  
12 defendants apparently abandoned the corporate entities of  
13 Stonewood and PWM, leaving no registered agent to serve;  
14 all three entity defendants defaulted and to the extent  
15 they had representation by counsel, such representation  
16 ceased. (Kalin Dec. ¶¶ 51-54.)

17  
18 Stonewood and PWM each failed to file an answer to  
19 the Complaint filed in this action, and on April 3, 2008,  
20 the Clerk of the Court entered a default against  
21 Stonewood and PWM pursuant to Fed. R. Civ. P. 55(a). (Id.  
22 ¶¶ 34, 38.)

23

24 **C. Duncan's and Montecastro's Fraudulent Conduct May be**  
25 **Continuing.**

26 In or around October 2007, Duncan represented to a  
27 potential investor that he had bought a surgical center

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1 for \$1.2 million, planned to buy 10 more surgical  
2 centers, and had 47 investors in the project. Duncan took  
3 this investor in his luxury automobile to tour a surgical  
4 center in California, after paying for him to  
5 fly from Las Vegas to Orange County. This investor  
6 provided Duncan with a total of \$225,000 in early  
7 November 2007. (Id. ¶ 116.) In

8  
9 November 2007, Duncan flew to Las Vegas to make a  
10 presentation to potential investors for the surgical  
11 center investment opportunity, and provided investors  
12 with documents purporting to explain the investment. (Id.  
13 ¶ 117.) Montecastro met with an investor and Duncan in  
14 late 2007, and represented that he and Duncan had moved  
15 from investing in real estate to surgical centers. (Id. ¶  
16 118.)

#### 17 18 **D. Other Material Facts**

19 During the Commission's investigation into this  
20 matter, Duncan asserted his Fifth Amendment right against  
21 self-incrimination and refused to answer questions. (SUF  
22 ¶ 11.) In this litigation, Duncan asserted his Fifth  
23 Amendment privilege in responses to interrogatories and  
24 requests for admission served by the Commission. Duncan's  
25 counsel informed the Commission that Duncan would  
26 continue to assert his Fifth Amendment privilege at  
27 deposition. (Id. ¶ 12.)

28

1 During the Commission's investigation, Montecastro  
2 provided responses to some of the staff's questions, and  
3 then asserted his Fifth Amendment privilege against  
4 self-incrimination. (Id. ¶ 18.) At his deposition in  
5 this action, Montecastro asserted his Fifth Amendment  
6 privilege in response to all questions. (Id. ¶ 19.)

7

8

#### IV. DISCUSSION

9

##### **A. The Interests In Issue Are "Securities"**

10 Each of the Commission's claims requires it to prove  
11 that the interest defendants were selling or offering  
12 were "securities." The Commission has presented  
13 undisputed facts establishing that the investment  
14 interests offered by defendants were securities.

15

16 The investment interests offered by defendants were  
17 investment contracts, and investment contracts are  
18 securities. See Section 2(a)(1) of the Securities  
19 Act, 15 U.S.C. § 77b(a)(1), and Section 3(a)(10) of the  
20 Exchange Act, 15 U.S.C. § 78c(a)(10). An investment  
21 contract is (1) an investment of money; (2) in a  
22 common enterprise; (3) with the expectation of profits to  
23 come solely from the efforts of others. SEC v. W. J.  
24 Howey Co., 328 U.S. 293, 298-99 (1946). See also SEC v.  
25 Edwards, 540 U.S. 389 (2004); SEC v. Rubera, 350 F.3d  
26 1084, 1090 (9th Cir. 2003). In the Ninth Circuit, either

27

28

1 horizontal commonality (a pooling of investor funds and  
2 interests) or vertical commonality (the fortunes of the  
3 investor are linked with those of the promoters) will  
4 satisfy the common enterprise element. See SEC v. R.G.  
5 Reynolds Enters., Inc., 952 F.2d 1125, 1130-31 (9th Cir.  
6 1991); Hocking v. Dubois, 885 F.2d 1449, 1455 (9th Cir.  
7 1989).

8  
9 The Commission has demonstrated that the products  
10 defendants were offering and selling satisfy all three  
11 elements of the Howey test. First, the Commission has  
12 shown that the money provided to Defendants were  
13 investment. The Core Clients provided cash, money from  
14 IRA accounts, and proceeds from the refinancing of  
15 personal residences. The concession fees were also  
16 investments of money by the Core Clients. In this case,  
17 Core Clients allowed their credit to be used by  
18 defendants to purchase investment homes, and the Core  
19 Clients then became personally liable for the mortgage  
20 loans. Thus, the first Howey element is satisfied  
21 because the Core Clients gave up "tangible and definable  
22 consideration" or committed their assets such that they  
23 were subject to financial loss. See International  
24 Brotherhood of Teamsters v. Daniel, 439 U.S. 551, 560  
25 (1979); Hector v. Wiens, 533 F.2d 429, 432 (9th Cir.  
26 1976) (investment funded by bank notes secured by  
27  
28

1 livestock was investment of money under Howey because  
2 investor was subject to financial loss).

3

4 The Commission has demonstrated the second element of  
5 the Howey test by showing that Defendants pooled and  
6 commingled investors' funds, thus establishing horizontal  
7 commonality. Investors' returns were linked to those of  
8 defendants, with whom they would split the profits on the  
9 investment homes, thus establishing vertical commonality.

10

11 The Commission has shown the third element of the  
12 Howey test because the investors' expected profits were  
13 to be derived from the efforts of the defendants.  
14 Indeed, defendants' "three rules" explicitly demonstrate  
15 this element because they vested defendants with  
16 exclusive management and control of investor funds. In  
17 addition, investors had no role in the purchase or sale  
18 of investment houses.

19

20 Based on the foregoing undisputed facts, the  
21 Commission has demonstrated with the products defendants  
22 were offering and selling were "securities" within the  
23 meaning of the Securities Act. Defendants have presented  
24 no evidence or argument to dispute these facts. The  
25 Commission has therefore met its burden on this element  
26 of its claims.

27 ///

28

1 **B. Claim One - Violation of the Registration Provisions**  
2 **of the Securities Act**

3  
4 Sections 5(a) and 5(c) of the Securities Act, 15  
5 U.S.C. §§ 77e(a) and 77e(c), prohibit the offer or sale  
6 of securities in interstate commerce, unless the  
7 securities have been registered with the Commission or  
8 are exempt from registration. SEC v. Phan, 500 F.3d 895,  
9 901-02 (9th Cir. 2007); SEC v. Eurobond Exch., Ltd., 13  
10 F.3d 1334, 1338 (9th Cir. 1994); SEC v. Murphy, 626 F.2d  
11 633, 640 (9th Cir. 1980).

12  
13 A prima facie Section 5 violation is established by  
14 showing: "(1) no registration statement was in effect or  
15 filed with the Commission as to such securities; (2) the  
16 defendant sold or offered to sell these securities; and  
17 (3) interstate transportation or communication or the  
18 mails were used in connection with the sale or offer of  
19 sale." SEC v. Continental Tobacco Co., 463 F.2d 137, 155  
20 (5th Cir. 1972); see SEC v. Phan, 500 F.3d at 902; SEC v.  
21 Calvo, 378 F.3d 1211, 1214 (11th Cir. 2004).<sup>2</sup> Once a  
22 prima facie case has been established, a party claiming  
23 an exemption from registration must meet the burden of

24  
25 <sup>2</sup> Unlike a violation of the antifraud provisions,  
26 "[n]either negligence nor scienter is an element of a  
27 prima facie case under Section 5." SEC v. Friendly  
28 Power Company, LLC, 49 F. Supp. 2d 1363, 1367 (S.D. Fla.  
1999); SEC v. Calvo, 378 F.3d 1211, 1215 (11th Cir. 2004)  
("Scienter is not a consideration" to demonstrate a  
Section 5 violation.).

1 proving the claimed exemption. SEC v. Ralston Purina  
2 Co., 346 U.S. 119, 126 (1953); SEC v. Murphy, 626 F.2d at  
3 641. Exemptions to registration are construed narrowly.  
4 SEC v. Murphy, 626 F.2d at 641.

5  
6 Section 5 imposes liability on persons who directly  
7 or indirectly offer or sell securities in unregistered,  
8 nonexempt transactions in interstate commerce. SEC  
9 v. Alpha Telecom, Inc., 187 F. Supp. 2d 1250, 1258 (D.  
10 Or. 2002), *aff'd sub nom.*, SEC v. Rubera, 350 F.3d 1084  
11 (9th Cir. 2003). Here, the Commission contends that  
12 Duncan and Montecastro are liable for the registration  
13 violations directly, for personally participating in the  
14 offering; that Montecastro is liable indirectly as the  
15 CEO of Stonewood; and that TRF, Stonewood, and PWM are  
16 liable directly for the registration violations.

17  
18 The Commission has established each element of its  
19 claims against Defendants for the offering and sale of  
20 unregistered securities. First, the Commission has shown  
21 that no registration statements were filed or in effect  
22 for any of the offerings. Indeed, the TRF offering  
23 materials explicitly state that no registration statement  
24 had been filed.

25  
26 Second, the Commission has shown that the defendants  
27 offered or sold securities. As discussed above, the  
28 Commission has shown that the investments in issue were

1 "securities." Section 2(a)(3) of the Securities Act, 15  
2 U.S.C. § 77b(a)(3), defines "offer to sell" to include  
3 "every attempt or offer to dispose of, or solicitation of  
4 an offer to buy, a security or interest in a security,  
5 for value." Section 2(a)(3) of the Securities Act, 15  
6 U.S.C. § 77b(a)(3), defines "sale" to include "every  
7 contract of sale or disposition of a security or interest  
8 in a security for value." The TRF offering materials,  
9 the telemarketing scripts, and the PWM "Investment  
10 Seminars" constitute ample evidence that defendants were  
11 offering to sell securities. The millions of dollars  
12 that defendants obtained from investors through TRF and  
13 Stonewood/PWM offerings establish that defendants did, in  
14 fact, sell securities.

15  
16 Third, the Commission has shown that defendants used  
17 means of interstate transportation and communication, and  
18 the mails. In the TRF offering, defendants sent  
19 subscription materials by mail, and received signed  
20 subscription agreements in the mail. Defendants also  
21 instructed investors to wire funds to the TRF bank  
22 account. TRF had an Internet site that was generally  
23 available, and defendants used electronic mail ("email")  
24 to communicate in connection with the fraudulent  
25 offering. In the Stonewood/PWM offering, defendants held  
26 "Investment Seminars" in Arizona and California,  
27 communicated among themselves by email to facilitate the  
28

1 scheme, and used telephones to communicate with  
2 investors, as shown by the telemarketing scripts.

3  
4 By presenting evidence establishing each of the above  
5 facts, the Commission has established a prima facie  
6 violation of Section 5. Defendants bear the burden of  
7 proving that an exemption from registration applies. SEC  
8 v. Ralston Purina Co., 346 U.S. 119, 126, (1953); Murphy,  
9 626 F.2d at 641. In view of Duncan's and Montecastro's  
10 assertion of their Fifth Amendment privilege, and the  
11 default of defendants Stonewood, PWM, and TRF, defendants  
12 have not made such a showing. See SEC v. Colello, 139  
13 F.3d 674, 677 (9th Cir. 1998) (permitting adverse  
14 inference against defendants who invoke their Fifth  
15 Amendment right in civil litigation).

16  
17 For the foregoing reasons, the Commission has met its  
18 initial burden on summary judgment to show facts and  
19 evidence establishing each element of its Section 5  
20 claim. The burden now shifts to Defendants to  
21 demonstrate a genuine issue of material fact that must be  
22 resolved at trial. Celotex, 477 U.S. at 324; Anderson,  
23 477 U.S. at 256. Defendants have not opposed the  
24 Commission's Motion on its merits and present no evidence  
25 to rebut the Commissions' arguments. Accordingly, the  
26 Commission is entitled to summary judgment on its claim  
27 for the unregistered offer and sale of securities in  
28 violation of sections 5(a) and 5(c) of the Securities

1 Act, 15 U.S.C. §§ 77e(a) and 77e(c), its first claim for  
2 relief.

3  
4 **C. Claims Two and Three - Violation of the Anti-fraud**  
5 **Provisions of the Securities Act**

6 The Commission's second and third claims allege  
7 Defendants violated the anti-fraud provisions of the  
8 Securities Act. Section 17(a) of the Securities Act, 15  
9 U.S.C. § 77q(a), prohibits fraud in the offer or sale of  
10 securities, and Section 10(b) of the Exchange Act, 15  
11 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. §  
12 240.10b-5, prohibit fraud in connection with the purchase  
13 or sale of any security.

14 Rule 10b-5 provides that:

15 It shall be unlawful for any person, directly or  
16 indirectly, by the use of any means or  
17 instrumentality of interstate commerce, or of the  
18 mails, or of any facility of any national securities  
19 exchange,

20 (a) to employ any device, scheme, or artifice to  
21 defraud,

22 (b) to make any untrue statement of a material  
23 fact or to omit to state a material fact  
24 necessary in order to make the statements made,  
25 in the light of the circumstances under which  
26 they were made, not misleading, or

27 (c) to engage in any act, practice, or course of  
28 business which operates or would operate as a  
fraud or deceit upon any person, in connection  
with the purchase or sale of any security.

To establish a prima facie case under Section 17(a)  
of the Securities Act and Section 10(b) of the Exchange  
Act, and Rule 10b-5, the Commission must prove by a  
preponderance of the evidence three basic elements: (1) a  
material misrepresentation, omission of material fact, or

1 other fraudulent device; (2) in connection with the  
2 purchase, offer, or sale of a security; (3) with the  
3 requisite mental state; and (4) by means of interstate  
4 commerce. SEC v. Phan, 500 F.3d at 907-08; SEC v. Rana  
5 Research, Inc., 8 F.3d 1358, 1364 (9th Cir. 1993); SEC v.  
6 First Jersey Securities, Inc., 101 F.3d 1450 (2d Cir.  
7 1996). Violations of Section 17(a)(1), Section 10(b),  
8 and Rule 10b-5 require scienter, while violations of  
9 Sections 17(a)(2) and 17(a)(3) require a showing of  
10 negligence. SEC v. Phan, 500 F.3d at 907-08; SEC v. Dain  
11 Rauscher, Inc., 254 F.3d 852, 856 (9th Cir. 2001). The  
12 Commission has presented evidence sufficient to establish  
13 each element of both of its fraud claims against all  
14 Defendants.

15  
16 **1. The Commission has Shown that Defendants Made**  
17 **Material Misrepresentations and Omissions in**  
18 **Connection with the Offer or Sale of Securities.**  
19

20 Violations of the antifraud provisions require that  
21 the misstatements and omissions made by the defendants  
22 concern material facts. Basic Inc. v. Levinson, 485 U.S.  
23 224, 231-32 (1988); TSC Indus., Inc. v. Northway, Inc.,  
24 426 U.S. 438, 449 (1976). A fact is material if there is  
25 a substantial likelihood that a reasonable investor would  
26 consider it important in making an investment decision.  
27 See TSC Indus., Inc., 426 U.S. at 449. Liability arises  
28 not only from affirmative representations but also from

1 failures to disclose material information. SEC v. Dain  
2 Rauscher, 254 F.3d 852, 855-56 (9th Cir. 2001). The  
3 antifraud provisions impose "'a duty to disclose material  
4 facts that are necessary to make disclosed statements,  
5 whether mandatory or volunteered, not misleading.'" SEC  
6 v. Fehn, 97 F.3d 1276, 1290 n.12 (9th Cir. 1996) (quoting  
7 Hanon v. Dataproducts Corp., 976 F.2d 497, 504 (9th Cir.  
8 1992)).

9  
10 In the TRF offering, defendants Duncan and TRF made  
11 material misrepresentations and omissions about how  
12 investor funds would be used. Defendants represented  
13 that 95% of investor funds would be used for the purchase  
14 of real estate, business assets, or accounts receivable.  
15 Defendants represented that they provided factoring  
16 services to contractors working on federal, state, and  
17 municipally funded water treatment plants. In fact,  
18 defendants made no such investments. Instead, TRF  
19 investor funds were diverted to pay Duncan's personal  
20 expenses and pay off earlier investors. That defendants  
21 were not making any investments as represented is  
22 information that a reasonable investor would consider  
23 important and was therefore material. Similarly, that  
24 95% of the investor funds were not being used to make  
25 investments, but instead Duncan was simply converting the  
26 funds to his own use through nominees, is material  
27 information that a reasonable investor would find  
28 important.

1 In the Stonewood/PWM offering, the Defendants  
2 misrepresented to Core Clients that they would become  
3 "millionaires" or "financially secure" in three years.  
4 Similarly, defendants' misrepresentations that Duncan and  
5 Montecastro were millionaires, and their failure to  
6 disclose Duncan's regulatory history and McLeod's  
7 criminal record, were material. Misrepresentations and  
8 omissions concerning the background and success of  
9 persons soliciting funds are material, because these are  
10 the types of facts that investors consider important.

11  
12 Defendants' failure to disclose to Core Clients the  
13 manner in which concession fees were generated and how  
14 they were used were material omissions. Defendants  
15 failed to disclose that concession fees were generated by  
16 paying more than the asking price for investment homes,  
17 thus potentially saddling investors with over-leveraged  
18 property that had no equity. That defendants were paying  
19 inflated prices for investment homes was important  
20 information that clearly is relevant to any investment  
21 decision. Defendants failed to disclose that the  
22 concession fees were being used to pay earlier investors,  
23 and to leverage the scheme, which was material  
24 information. A reasonable investor would consider it  
25 important that assets were being bought at inflated  
26 prices or were over-leveraged.

27  
28

1 Defendants' failure to disclose to Core Clients that  
2 defendants were submitting false loan applications to  
3 mortgage lenders was a material omission. Defendants  
4 failed to disclose that investors were able to purchase  
5 multiple investment houses only because false asset  
6 information was being provided to mortgage lenders in the  
7 names of investors. This omission rendered materially  
8 misleading the statements to investors regarding assets  
9 provided on their behalf by "hard money" investors.  
10 Additionally, investors would have considered this  
11 information important because it would have shown that  
12 PWM and Stonewood were not conducting legitimate business  
13 operations, and because the fraudulent loan applications  
14 could have subjected the investors to potential civil or  
15 criminal liability.

16  
17 Defendants failed to disclose that substantial  
18 amounts of investor funds were being diverted to Duncan,  
19 Montecastro, and their family members. Defendants also  
20 represented that they were a "Christian organization."  
21 In fact, Duncan and Montecastro were using investor funds  
22 for regular sprees in Las Vegas. An investor would  
23 consider it important to know that the principals were  
24 misrepresenting their beliefs and not using investor  
25 funds as represented, but rather to fund a lavish  
26 lifestyle which meant there was little likelihood that  
27 investors would receive a reasonable return, or any  
28 return, on their investments.

1 Defendants' material misrepresentations and omissions  
2 were made in connection with the sale of securities, in  
3 the form of investment contracts, thus satisfying the  
4 second element of a prima facie violation of the  
5 antifraud provisions.

6  
7 **2. The Commission has Shown that Defendants Acted**  
8 **With Scienter.**

9 Section 17(a)(1) of the Securities Act, 15 U.S.C. §  
10 77q(a)(1), and Section 10(b) of the Exchange Act, 15  
11 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. §  
12 240.10b-5, also require a showing of scienter. Aaron v.  
13 SEC, 446 U.S. 680, 701-02 (1980). Scienter is defined as  
14 a "mental state embracing intent to deceive, manipulate,  
15 or defraud." Ernst & Ernst v. Hochfelder, 425 U.S. 185,  
16 193 n.12 (1976). In the Ninth Circuit, scienter may be  
17 established by a showing of recklessness. Hollinger v.  
18 Titan Capital Corp., 914 F.2d 1564, 1568-69 (9th Cir.  
19 1990); Vernazza v. SEC, 327 F.3d 851, 860 (9th Cir.  
20 2003). Further, recklessness may be inferred from  
21 circumstantial evidence. Herman & MacLean v. Huddleston,  
22 459 U.S. 375, 390-91, n.30 (1983); SEC v. Burns, 816  
23 F.2d 471, 474 (9th Cir. 1987).

24  
25 The Commission has presented facts and evidence  
26 showing that Defendant Duncan acted with a high level of  
27 scienter. Duncan orchestrated the TRF offering and then  
28 laundered investor funds before diverting them to his own

1 use. The uncontroverted facts showing Duncan used stepped  
2 transactions, moving TRF funds first to Pilo, then to  
3 Oetting Industries, before diverting them to his own use,  
4 is strong evidence of his intent to deceive and defraud.  
5 Similarly, Duncan's use of a front-man as the President  
6 of TRF, and his failure to identify his role in TRF in  
7 the offering materials, is strong evidence of his intent  
8 to deceive and defraud. There is no evidence that Duncan  
9 ever intended to, or had the capacity to, make  
10 investments of the type represented in the TRF offering  
11 literature.

12  
13 Similarly, in the Stonewood/PWM offering, Duncan's  
14 efforts to conceal his involvement and his control are  
15 strong evidence of his scienter. Duncan concealed his  
16 partnership in Stonewood, which was officially registered  
17 as Montecastro's company even though Duncan was  
18 Montecastro's partner. Similarly, when Duncan decided to  
19 change from Stonewood to PWM, he installed McLeod as the  
20 front-man, even though Duncan owned that corporate entity  
21 and Duncan and Montecastro directed and controlled it.

22  
23 Duncan's effort to conceal any connection between  
24 himself and the investment companies, and the concession  
25 fees and other investor funds, is also evidence of a high  
26 level of scienter. Duncan arranged to have the  
27 concession fees paid to Stonewood, then transferred to  
28 Oetting Industries, where Duncan then disbursed them,

1 sometimes only after sending them to other companies,  
2 with the apparent intent to hide the origin of the funds  
3 and his connection to it. The complex web of  
4 transactions served to obscure Duncan's involvement,  
5 which is clear evidence of his intent to deceive.  
6 Duncan's use of numerous nominees such as Oetting,  
7 Bailey, and Contreras, to pay his personal expenses from  
8 the proceeds of the fraud, is additional evidence of his  
9 high level of scienter. Duncan's efforts to destroy  
10 documents as the scheme was falling apart are strong  
11 evidence of his high level of scienter.

12  
13 The Commission has also shown that Montecastro acted  
14 with a high level of scienter. Montecastro was the  
15 mortgage loan broker whose company maintained a "stable"  
16 of appraisers to help facilitate the purchase of  
17 investment houses at purchase prices higher than the  
18 selling prices, thus generating cash out from the  
19 transactions in the form of "concession fees."  
20 Montecastro also had a "unique" asset verification  
21 process for loan applications, which relied on Duncan to  
22 provide false documentation regarding the assets of Core  
23 Clients who were being used to purchase investment  
24 houses. Once the transactions were complete, Montecastro  
25 transferred the concession fees from Stonewood to Oetting  
26 Industries, thus participating in the effort to disguise  
27 the origin and destination of the funds. This is  
28 evidence of Montecastro's intent to defraud and deceive.

1 Montecastro's participation as the owner of Stonewood, as  
2 a mortgage broker, and as a licensed realtor were  
3 integral to the fraud, and is evidence of a high level of  
4 scienter. Moreover, Montecastro's actions in collecting  
5 and destroying documents from the PWM office in early  
6 2007 is evidence of his high level of scienter.

7  
8 The Commission has also shown that Duncan's scienter  
9 is imputed by law to the corporate entities he controls,  
10 and therefore should be imputed to TRF, Stonewood, and  
11 PWM. Similarly, Montecastro's scienter is properly  
12 imputed to Stonewood. See SEC v. Manor Nursing Ctrs.,  
13 Inc., 458 F.2d 1082, 1096 (2d Cir. 1972).

14  
15 Because defendants acted with scienter, or at least  
16 recklessly, they each violated Section 17(a)(1) of the  
17 Securities Act and Section 10(b) of the Exchange Act and  
18 Rule 10b-5 thereunder. In addition, because defendants  
19 acted at least recklessly, their conduct is more than  
20 sufficient to satisfy the negligence standard required to  
21 violate Section 17(a)(2) and (3) of the Securities Act.  
22 See SEC v. Dain Rauscher, Inc., 254 F.3d at 856.

23  
24 In addition to the uncontroverted evidence presented  
25 that Duncan and Montecastro violated the antifraud  
26 provisions, the Court has the discretion to draw an  
27 adverse inference against those defendants based on their  
28 invocation of their Fifth Amendment right against self-

1 incrimination. SEC v. Colello, 139 F.3d 674, 677 (9th  
2 Cir. 1998). This is an appropriate case to draw such an  
3 inference.

4  
5 Based on the foregoing, the Commission has met its  
6 initial burden to present facts and evidence showing that  
7 defendants Duncan, Montecastro, TRF, Stonewood and PWM  
8 violated the anti-fraud provisions of Section 17(a) of  
9 the Securities Act, 15 U.S.C. § 77q(a), and Section 10(b)  
10 of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5  
11 thereunder, 17 C.F.R. 240.10b-5. The burden now shifts to  
12 Defendants to demonstrate a genuine issue of material  
13 fact that must be resolved at trial. Celotex, 477 U.S.  
14 at 324; Anderson, 477 U.S. at 256. Defendants have not  
15 opposed the Commission's Motion and present no evidence  
16 to rebut the Commission's arguments. Accordingly, the  
17 Commission is entitled to summary judgment on these  
18 claims.

19  
20 **D. The Commission's Request for Default Judgment to be**  
21 **Entered Against TRF, Stonewood, and PWM.**

22  
23 Federal Rule of Civil Procedure 55(b)(2) permits the  
24 Court, upon application of a party, to enter default  
25 judgment against a party who has failed to plead or  
26 otherwise defend an action. See Kloepping v. Fireman's  
27 Fund, No. 1996 U.S. Dist. Lexis 1786, at \*3-4 (N.D. Cal.  
28 Feb. 14, 1996). A judgment by default under Federal Rule

1 55(b)(2) is left to the Court's sound discretion. Aldabe  
2 v. Aldabe, 616 F.2d 1089, 1092 (9th Cir. 1980); see  
3 PepsiCo, Inc. v. Triunfo-Mex. Inc.,  
4 189 F.R.D. 431, 432 (C.D. Cal. 1999) ("In applying this  
5 discretionary standard, default judgments are more often  
6 granted than denied").

7  
8 Under Ninth Circuit law, a district court should  
9 consider the following factors in exercising its  
10 discretion: (1) the possibility of prejudice to the  
11 plaintiff, (2) the merits of plaintiff's substantive  
12 claim, (3) the sufficiency of the complaint, (4) the sum  
13 of money at stake in the action, (5) the possibility of a  
14 dispute concerning material facts, (6) whether the  
15 default was due to excusable neglect, and (7) the strong  
16 policy underlying the Federal Rules of Civil Procedure  
17 favoring decisions on the merits. Eitel v. McCool, 782  
18 F.2d 1470, 1471-72 (9th Cir. 1986). The well-pleaded  
19 allegations contained in a complaint are taken as  
20 admitted on a default judgment. Benny v. Pipes, 799 F.2d  
21 489, 495 (9th Cir. 1986), opin. amended, 807 F.2d 1514,  
22 cert. denied, 484 U.S. 870(1987).

23  
24 The Commission has established the merits of its  
25 claims against TRF, Stonewood, and PWM, and, as discussed  
26 above, there is no dispute as to the facts. There is no  
27 evidence that the default of these entity defendants was  
28 the result of excusable neglect. The Commission would be

1 prejudiced if a default judgment was not entered, because  
2 it would effectively allow entities controlled by Duncan  
3 and Montecastro to evade judgment by simply disappearing  
4 after this enforcement action was filed. Such a result  
5 would prejudice the Commission and be detrimental to  
6 enforcement of the federal securities laws. Furthermore,  
7 default judgment may be necessary to prevent defendants  
8 from resurrecting the entities or their names.  
9 Accordingly, the Court will enter a default judgment  
10 against TRF, Stonewood, and PWM.

11  
12 **E. Remedies**

13 As remedies, the Commission is seeking permanent  
14 injunctions against defendants Duncan, Montecastro, TRF,  
15 Stonewood, and PWM, enjoining them from further  
16 violations of the registration and anti-fraud provisions  
17 of the federal securities laws. The Commission is also  
18 seeking disgorgement and prejudgment interest from  
19 Duncan, Montecastro, and McLeod. Finally, the Commission  
20 moves for imposition of a third tier penalty in the  
21 amount of \$130,000 each on defendants Duncan,  
22 Montecastro, and McLeod.

23  
24  
25 **1. Permanent Injunctions Are Appropriate Against**  
26 **Defendants TRF, Stonewood, PWM, Duncan, and**  
27 **Montecastro.**  
28

1 Section 20(b) of the Securities Act, 15 U.S.C. §  
2 77t(b), Section 21(d) of the Exchange Act, 15 U.S.C. §  
3 78u(d)(1), and Section 209(d) of the Advisers Act, 15  
4 U.S.C. § 80b-9(d), provide that upon proper showing, a  
5 permanent injunction shall be granted in enforcement  
6 actions brought by the Commission. That burden is met  
7 when the evidence establishes a reasonable likelihood of  
8 a future violation of the securities laws. SEC v.  
9 Murphy, 626 F.2d 633, 655 (9th Cir. 1980); SEC v.  
10 Koracorp Indus., Inc., 575 F.2d 692 (9th Cir. 1978). A  
11 defendant's past illegal conduct raises a presumption  
12 that he will commit future violations. Koracorp, 575  
13 F.2d at 698. When predicting the likelihood of future  
14 violations, the Court should evaluate the totality of the  
15 circumstances. SEC v. Fehn, 97 F.3d 1276, 1295-96 (9th  
16 Cir. 1996) citing Murphy, 626 F.2d at 655. The factors to  
17 be considered include the degree of scienter involved;  
18 the isolated or recurrent nature of the infractions; the  
19 defendant's recognition of the wrongful nature of his  
20 conduct; the likelihood that, based on the defendant's  
21 occupation, future violations might occur; and the  
22 sincerity of the defendant's assurances against future  
23 violations. Id. That the illegal conduct has ceased  
24 does not foreclose injunctive relief. Id. A permanent  
25 injunction may be particularly appropriate where a  
26 violation was "founded on systemic wrongdoing, rather  
27 than an isolated occurrence," or involved a "high degree  
28

1 of scienter." SEC v. Berger, 244 F. Supp. 2d, 180, 193  
2 (S.D.N.Y. 2001).

3  
4 Defendants here evidenced a high level of scienter,  
5 the wrongful conduct continued over the course of at  
6 least three years and defendants evolved their conduct  
7 to evade detection as well as to continue to separate  
8 investors from their money. Defendants have not  
9 recognized the wrongful nature of their conduct and have  
10 not given any indication that they will not engage in  
11 such conduct in the future. Indeed, there is evidence  
12 here that defendants Duncan and Montecastro may have  
13 participated in another offering in late 2007. Under the  
14 totality of the circumstances, and in view of the  
15 egregious nature of defendants' past conduct, permanent  
16 injunctions against Duncan, Montecastro, TRF, Stonewood,  
17 and PWM are appropriate.

18  
19 **2. Defendants Duncan, Montecastro, and McLeod**  
20 **Should Disgorge Ill-Gotten Gains and Pay**  
21 **Prejudgment Interest.**

22  
23 Disgorgement is an available and appropriate  
24 equitable remedy for securities fraud, and for violations  
25 of Section 5 registration violations. See SEC v. J.T.  
26 Wallenbrock, 440 F.3d 1109, 1113 (9th Cir. 2006); SEC v.  
27 First Pacific Bancorp, 142 F.3d 1186, 1191 (9th Cir.  
28 1998); SEC v. Rind, 991 F.2d 1486, 1493 (9th Cir. 1993).

1 In contrast to damages, which are designed to compensate  
2 fraud victims, disgorgement forces a defendant to  
3 surrender his unjust enrichment and eliminates any  
4 incentive for violating the law. Rind, 991 F.2d at 1491,  
5 1493; First Pacific Bancorp, 142 F.3d at 1191. The  
6 amount of disgorgement should include all gains flowing  
7 from illegal activities. See SEC v. Cross Fin. Servs.,  
8 908 F. Supp. 718, 734 (C.D. Cal. 1995); SEC v. Lund, 570  
9 F. Supp. 1397, 1404 (C.D. Cal. 1983).

10  
11 In calculating disgorgement, the Commission need only  
12 show a reasonable approximation of profits causally  
13 connected to the violation. First Pacific Bancorp, 142  
14 F.3d at 1192 n.6. The Commission is not required to  
15 trace every dollar of the proceeds or to identify moneys  
16 which have been commingled. SEC v. Great Lakes Equities,  
17 Co., 775 F. Supp. 211, 214 at n.21 (E.D. Mich. 1991).  
18 Any uncertainty in the calculation of disgorgement  
19 "should fall on the wrongdoer whose illegal conduct  
20 created that uncertainty." SEC v. Patel, 61 F.3d 137,  
21 140 (2d Cir. 1995) (citation omitted); SEC v. First  
22 Jersey Secs., Inc., 101 F.3d 1450, 1475 (2d Cir. 1996),  
23 cert. denied 522 U.S. 812 (1997); SEC v. Interlink Data  
24 Network of L.A., Inc., Civ. No. 93 3073, 1993 U.S. Dist.  
25 LEXIS 20163, at \*26-28, 52-54 (C.D. Cal. 1993). Once the  
26 Commission has shown a reasonable approximation of  
27 profits, the burden shifts to the defendant to show that  
28 the Commission's proposed disgorgement is not a

1 reasonable approximation. SEC v. First City Fin. Corp.,  
2 Ltd., 890 F.2d 1215, 1232 (D.C. Cir. 1989).

3  
4 An order of disgorgement should include prejudgment  
5 interest to ensure that the wrongdoer does not profit  
6 from the illegal activity. See SEC v. Manor Nursing  
7 Ctrs., Inc., 458 F.2d at 1105; SEC v. Cross Financial  
8 Services, Inc., 908 F. Supp. 718, 734 (C.D. Cal. 1995).  
9 The interest rate prescribed by 28 U.S.C. § 1961, used  
10 for calculation of post-judgment interest, is generally  
11 the appropriate rate to calculate prejudgment interest  
12 unless the trial judge finds, on substantial evidence,  
13 that the equities of a particular case require a  
14 different rate. See Western Pacific Fisheries, Inc. v.  
15 S.S. President Grant, 730 F.2d 1280, 1289 (9th Cir.  
16 1984); SEC v. Cross Financial Services, 908 F. Supp. at  
17 734.

18  
19 The Commission has introduced evidence that Duncan  
20 orchestrated the TRF and Stonewood/PWM unregistered  
21 offerings. Moreover, the Commission has offered ample  
22 evidence that Duncan controlled the proceeds of the TRF  
23 offering, received the bulk of the concession fees from  
24 Stonewood and controlled their disposition, and  
25 Duncan-controlled companies received funds directly from  
26 investors. Thus, Duncan effectively controlled all the  
27 proceeds of the fraud, and as such, the total amount  
28 raised of \$29,498,679 represents a reasonable

1 approximation of his ill-gotten gains. Accordingly, it  
2 is appropriate to order Duncan to disgorge the total  
3 amount raised in the offerings of \$29,498,679, plus  
4 prejudgment interest of \$843,006.70, for a total judgment  
5 of \$30,341,685.70.

6  
7 Defendant Montecastro was Duncan's partner in the  
8 Stonewood/PWM offering. Montecastro and his relatives  
9 directly pocketed millions of dollars from the fraud,  
10 while investors lost their homes. The total amount  
11 raised in the Stonewood/PWM offering, from concession  
12 fees and directly from investors, was \$27,515,421. This  
13 therefore represents a reasonable approximation of  
14 Montecastro's ill-gotten gains, and it is appropriate to  
15 order Montecastro to disgorge \$27,515,421, plus  
16 prejudgment interest of \$786,329.60, for a total judgment  
17 of \$28,301,750.60.5

18  
19 Defendant McLeod consented to entry of a Permanent  
20 Injunction. Although he played an important role as  
21 Duncan's front man for PWM, McLeod was not involved in a  
22 significant way until 2006 - near the collapse of the  
23 scheme. McLeod's role was clearly subordinate to Duncan  
24 and Montecastro. The Commission's expert accounting  
25 witness found that McLeod directly received approximately  
26 \$469,223 in proceeds from the fraud, which is a  
27 reasonable approximation of his ill-gotten gains.  
28 Prejudgment interest on that amount is \$13,409.35. The

1 Court therefore finds that it is appropriate to order  
2 McLeod to disgorge \$482,632.35.

3  
4 **3. Civil Penalties Against Defendants Duncan,**  
5 **Montecastro, and McLeod**

6  
7 Congress enacted civil penalty provisions to achieve  
8 the dual goals of punishment of the individual violator  
9 and deterrence of future violations. SEC v. Marker, 427  
10 F. Supp. 2d 583, 592 (M.D. Fla. 2006), citing SEC v.  
11 Coates, 137 F. Supp. 2d 413, 428 (S.D.N.Y. 2001). The  
12 deterrence of securities fraud through the imposition of  
13 monetary sanctions serves such important goals as  
14 encouraging investor confidence, increasing the  
15 efficiency of financial markets, and promoting the  
16 stability of the securities industry. SEC v. Palmisano,  
17 135 F.2d 860, 866 (2d Cir. 1998).

18  
19 Sections 20(d)(1) of the Securities Act, 15 U.S.C. §  
20 77t(d)(1), and 21(d)(3)(A) of the Exchange Act, 15 U.S.C.  
21 § 78u(d)(3)(A), provide that the Commission may seek, and  
22 the Court may impose, civil monetary penalties for  
23 securities violations. Three "tiers" of penalties may be  
24 imposed in an amount "determined by the court in light of  
25 the facts and circumstances." See Section 20(d)(2) of  
26 the Securities Act, 15 U.S.C. § 77t(d)(2)(A), and Section  
27 21(d)(3)(B) of the Exchange Act, 15 U.S.C. §  
28 78u(d)(3)(B). If the violation "involved fraud, deceit,

1 manipulation, or deliberate or reckless disregard of a  
2 regulatory requirement" and "such violation directly or  
3 indirectly resulted in substantial losses or created a  
4 significant risk of substantial losses to other persons"  
5 a third tier penalty may be imposed. See Section  
6 20(d)(2)(C) of the Securities Act, 15 U.S.C. §  
7 77t(d)(2)(C), and Section 21(d)(3)(B)(iii) of the  
8 Exchange Act, 15 U.S.C. § 78u(d)(3)(B)(iii).

9  
10 The Court finds that it is appropriate to assess the  
11 maximum third tier civil money penalty in the amount of  
12 \$130,000 against each of the individual defendants  
13 Duncan, Montecastro, and McLeod. The assessment of a  
14 penalty in this amount is appropriate because defendants  
15 defrauded numerous investors, and their conduct resulted  
16 in substantial losses to investors - in some cases,  
17 investors lost their homes.

18  
19 In addition, the factors used to determine the  
20 appropriateness of an injunction are helpful to consider  
21 when assessing penalties. SEC v. Abacus International  
22  Holding Corp., 2001 U.S. Dist. LEXIS 12635, 2001 WL  
23 940913, \*5 (N.D. Cal. August 16, 2001). These factors  
24 include: the degree of scienter involved; whether the  
25 violations are recurrent; and the likelihood that  
26 defendant's occupation will present opportunities for  
27 future violations. See SEC v. Murphy, 626 F.2d at 655  
28 (9th Cir. 1980). For the reasons stated above with

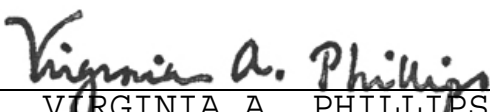
1 regard to evaluation of these factors in determining  
2 whether injunctive relief is appropriate, imposition of  
3 the maximum third tier penalty of \$130,000 against each  
4 of the individual defendants is appropriate.

5  
6 **V. CONCLUSION**

7 For the foregoing reasons, the Court GRANTS the  
8 Commission's Motion for Summary Judgment as to all of  
9 Plaintiff's claims against each Defendant.

10  
11 **IT IS SO ORDERED.**

12  
13  
14 Dated: July 6, 2009

  
\_\_\_\_\_  
VIRGINIA A. PHILLIPS  
United States District Judge