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8 THOMAS A. SEAMAN

9 UNITED STATES DISTRICT COURT
10 NORTHERN DISTRICT OF CALIFORNIA

12 SECURITIES AND EXCHANGE
COMMISSION,

13 Plaintiff,

14 vs.

15 SMALL BUSINESS CAPITAL CORP.;
16 MARK FEATHERS; INVESTORS PRIME
FUND, LLC; and SBC PORTFOLIO
17 FUND, LLC,

18 Defendants.

Case No. CV12-03237

**MOTION FOR ADMINISTRATIVE
RELIEF UNDER LOCAL RULE 7-11;
REQUEST FOR AUTHORITY TO PURSUE
CLAIMS AGAINST CALIFORNIA
BUSINESS BANK AND ITS DIRECTORS
AND OFFICERS**

Ctrm: 4 - 5th Floor
Judge: Hon. Edward J. Davila

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1 Thomas A. Seaman ("Receiver"), the Court-appointed permanent receiver for Small
2 Business Capital Corp. ("SB Capital"), Investors Prime Fund, LLC ("IPF"), SBC Portfolio
3 Fund, LLC ("SPF"), and their subsidiaries and affiliates (collectively, "Receivership Entities"),
4 hereby moves for administrative relief in the form of an order authorizing the Receiver to pursue
5 claims against California Business Bank ("CBB") and its directors and officers (collectively,
6 "Proposed Defendants"). If such authority is granted, the Receiver will file a separate but related
7 action in this Court against Proposed Defendants.¹

8 I. BACKGROUND

9 Between September 28, 2010 and June 28, 2011, CBB offered for sale its common stock,
10 no par value, at a price of \$3.00 per share ("Private Placement Offering"). On or about June 28
11 2011, IPF purchased 330,000 shares of CBB stock at \$3.00 per share for a total purchase price of
12 \$990,000. Proposed Defendants issued false and misleading statements in CBB's Private
13 Placement Memorandum ("PPM") in connection with the Private Placement Offering. The PPM
14 misrepresented and inflated CBB's loan portfolio and thus overstated CBB's capital and book
15 value by failing to disclose problems with numerous loans, including loans CBB made to its
16 directors.

17 More specifically, during the first and second calendar year quarters of 2011, while the
18 Private Placement Offering was pending and CBB was trying to raise capital, Proposed
19 Defendants falsely represented in the PPM that CBB had \$8.3 million in Tier-1 capital. In making
20 this representation, Proposed Defendants failed, among other things, to properly reserve for
21 approximately \$5 million in loans that had been made primarily to three borrowers – the Maturin
22 Group, Tom Dean, and CBB Director, N. Aaron Yashouafar. The collectability of these loans was
23 highly questionable during the pendency of the Private Placement Offering and while the PPM
24 was available to potential investors. Yet CBB did not disclose this risk in the PPM. IPF learned,
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27 ¹ The Preliminary Injunction Order authorizes the Receiver to investigate and prosecute claims
28 and causes of action on behalf of the Receivership Entities and to engage counsel to assist in
such efforts. Docket No. 34, Part XII.G. The Receiver seeks authority to pursue claims
against CBB in an abundance of caution and to make the Court aware of the potential recovery
and estimated attorney fees and costs of such action.

1 after the fact, that in many instances, CBB had not updated the loan files, the asset appraisals,
2 and/or the financial statements for some or all of these borrowers for several years. Had Proposed
3 Defendants properly recognized and adequately disclosed the problems with these loans, the PPM
4 would have stated a loan portfolio that was at least \$5 million less than what was actually stated,
5 and CBB would not have represented that it had \$8.3 million in Tier-I capital.

6 CBB also made loans to two other Directors, Gary Cross and Michael Maluccio. The PPM
7 made no reference to these loans or the fact that they were made to insiders.

8 CBB also held a loan issued to D'Carillo's Ornamental in the amount of \$330,000. CBB
9 filed a notice of default against this borrower in December 2010. The PPM made no reference to
10 this loan or the default, and no loan loss reserve for the loan was included in the financial
11 statements attached to the PPM.

12 CBB also held a loan issued to David Shalom in the amount of \$830,000. The loan
13 matured in 2009. In September 2010, CBB obtained an appraisal of the collateral (a second
14 position deed of trust on two multi-unit industrial buildings). The appraisal showed a loan-to-
15 value ratio of over 95%. Accordingly, the Financial Accounting Standards Board standards
16 (FAS 114) required CBB to implement a loan loss reserve of \$236,141. CBB did not implement
17 the reserve until June 30, 2011, *after* IPF's stock purchase. The PPM made no reference to this
18 loan or the default, and no loan loss reserve for the loan was included in the financial statements
19 attached to the PPM.

20 Although the events described above relating to the Maturin and Dean loans took place
21 before IPF's purchase of its stock, CCB, operating through the individual Proposed Defendants,
22 delayed in recognizing the charge-offs related to these loans until after IPF purchased its shares.
23 CBB and the individual Proposed Defendants did so in order to induce IPF to complete its
24 purchase. In July 2011, retroactive to June 30, 2011, CBB implemented a charge-off of
25 \$1,000,000 directly against CBB's capital accounts for the Maturin Group and Tom Dean loans.
26 The facts that lead to this charge-off were known by the individual Proposed Defendants prior to
27 June 28, 2011, and before IPF made its stock purchase. This \$1,000,000 charge-off resulted in a
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1 direct reduction in CBB's tangible book value of approximately \$0.75 per share, less than a month
2 after the close of the Private Placement Offering.

3 Proposed Defendants failed to disclose that it had made insider loans to Directors
4 Yashouafar, Cross and Maluccio, and in particular that Yashouafar had defaulted on a \$1,900,000
5 loan and resigned from the Board of Directors. Proposed Defendants also failed to disclose the
6 problems associated with the D'Carillo's Ornamental and Shalom loans or to include a loan loss
7 reserve for these loans. Had these loans and the problems associated with them been disclosed
8 and an appropriate reserve for them included in the financial statements attached to the PPM, the
9 value of CBB's assets would have been materially reduced and CBB's Tier-1 capital would have
10 been recognized at substantially and materially below the \$8,300,000 million represented in the
11 PPM, and CBB's book value would have been reduced to an amount substantially and materially
12 below the \$3.00 per share that IPF paid.

13 As a result of the examination of CBB's financial records conducted by CBB's regulators
14 after June 2011, CBB was forced by its regulators to recognize approximately \$3 million in losses
15 on its loan portfolio; losses that Proposed Defendants should have recognized and disclosed to IPF
16 prior to its stock purchase, pursuant to banking and accounting regulations applicable to CBB.
17 These loan losses were the result of facts known by CBB and the individual Proposed Defendants,
18 but not disclosed by them prior to June 28, 2011.

19 II. CLAIMS AGAINST PROPOSED DEFENDANTS

20 The Receiver believes IPF has strong claims against Proposed Defendants based on the
21 facts described above. An initial draft complaint is attached as Exhibit A to the Declaration of
22 Thomas Seaman filed herewith ("Seaman Declaration"). In light of the material
23 misrepresentations and omissions by Proposed Defendants, IPF has lost most, if not all, of its
24 investment. In fact, within a month of IPF's purchase, the value of CBB's stock dropped
25 dramatically and currently is listed with a bid price of \$0.28 per share. Seaman Declaration, ¶ 2.

26 The Receiver has discussed the projected attorney fees for the case with Allen Matkins.
27 Allen Matkins will bill its time at the same discounted hourly rates at which it represents the
28 Receiver in this case. Depending if and when the case settles or is otherwise resolved, Allen

1 Matkins estimates that the attorney fees for the case could be as little as \$35,000 and as much as
2 \$125,000. Seaman Declaration, ¶ 3.

3 III. ARGUMENT

4 "The power of a district court to impose a receivership or grant other forms of ancillary
5 relief does not in the first instance depend on a statutory grant of power from the securities laws.
6 Rather, the authority derives from the inherent power of a court of equity to fashion effective
7 relief." *SEC v. Wencke*, 622 F.2d 1363, 1369 (9th Cir. 1980). The "primary purpose of equity
8 receiverships is to promote orderly and efficient administration of the estate by the district court
9 for the benefit of creditors." *SEC v. Hardy*, 803 F.2d 1034, 1038 (9th Cir. 1986). As the
10 appointment of a receiver is authorized by the broad equitable powers of the court, any distribution
11 of assets must also be done equitably and fairly. See *SEC v. Elliot*, 953 F.2d 1560, 1569 (11th Cir.
12 1992).

13 District courts have the broad power of a court of equity to determine the appropriate
14 action in the administration and supervision of an equity receivership. See *SEC v. Capital*
15 *Consultants, LLC*, 397 F.3d 733, 738 (9th Cir. 2005). The Ninth Circuit explained:

16 A district court's power to supervise an equity receivership and to
17 determine the appropriate action to be taken in the administration of
18 the receivership is extremely broad. The district court has broad
19 powers and wide discretion to determine the appropriate relief in an
20 equity receivership. The basis for this broad deference to the district
21 court's supervisory role in equity receiverships arises out of the fact
22 that most receiverships involve multiple parties and complex
23 transactions. A district court's decision concerning the supervision
24 of an equitable receivership is reviewed for abuse of discretion.

25 *Id.* (citations omitted); see also *Commodities Futures Trading Comm'n. v. Topworth Int'l, Ltd.*,
26 205 F.3d 1107, 1115 (9th Cir. 1999) ("This court affords 'broad deference' to the court's
27 supervisory role, and 'we generally uphold reasonable procedures instituted by the district court
28 that serve th[e] purpose' of orderly and efficient administration of the receivership for the benefit
of creditors."). Accordingly, the Court has broad equitable powers and discretion in the
administration of the receivership estate.

Here, with the assistance of counsel, the Receiver has analyzed the facts and the law and
believes that IPF has strong claims against Proposed Defendants arising from the material

1 misrepresentations and omissions. IPF purchased the stock for \$990,000 so the restitution
2 damages are approximately that amount. The Receiver does not anticipate that discovery will be
3 particularly complex or voluminous. CBB is currently under scrutiny from the FDIC and other
4 regulators, so the collectability of a judgment is a concern, but the Receiver believes CBB has
5 insurance coverage for some or all of IPF's claims.

6 Allen Matkins will represent the Receiver as efficiently as possible and will bill its time at
7 the same discounted hourly rates at which it represents the Receiver in this case. As noted above,
8 depending if and when the matter settles, Allen Matkins estimates that the attorney fees for the
9 case could be as little as \$35,000 and as much as \$125,000. Approval of all fees and costs will be
10 sought via fee applications filed in this case.

11 **IV. CONCLUSION**

12 Based on the foregoing, the Receiver requests authority to pursue claims against Proposed
13 Defendants.

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15 Dated: March 29, 2013

ALLEN MATKINS LECK GAMBLE
MALLORY & NATSIS LLP

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17 By: _____ /s/ Ted Fates

TED FATES
Attorneys for Receiver
THOMAS A. SEAMAN

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