

LAWRENCE G. WASDEN
Attorney General

ALAN CONILOGUE
Deputy Attorney General
State of Idaho
P. O. Box 83720
Boise, ID 83720-0031
Telephone: 208.332.8093
Fax: 208.332.8016
ISBN 3196
alan.conilogue@finance.idaho.gov

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**IN THE DISTRICT COURT OF THE FIRST JUDICIAL DISTRICT
OF THE STATE OF IDAHO, IN AND FOR BENEWAH COUNTY**

STATE OF IDAHO, DEPARTMENT OF
FINANCE, SECURITIES BUREAU,

Plaintiff,

vs.

STEPHEN L. HOWELL, SECURITY
FINANCIAL SERVICES, INC.,
SECURITY FINANCIAL FUND, LLC,
and SECURITY INVESTORS FUND,
LLC,

Defendants.

Case No. CV 2012-403

COMPLAINT

Fee category: Exempt

COMES NOW the State of Idaho, Department of Finance, Gavin M. Gee, Director, (the Department), by and through its counsel, Alan Conilogue, Deputy Attorney General, and upon information and belief, complains and alleges as follows:

1. This action is brought pursuant to Idaho's Uniform Securities Act (2004), Idaho Code § 30-14-101 *et seq.* (the Act), and in particular Idaho Code § 30-14-603, wherein the Department is authorized to bring actions seeking injunctive and other relief against persons who

have either violated or are about to violate provisions of the Act or any rule promulgated thereunder.

VENUE

2. The acts and practices alleged herein comprising violations of law by the above-named Defendants occurred in Ada County, Bingham County, Benewah County, and elsewhere in Idaho. Defendants resided or were located in Idaho when the alleged acts constituting violations of the Act were committed.

JURISDICTION

3. Defendants, in connection with the offer and sale of securities, made material misrepresentations and omitted material information in connection with the offer or sale of such securities, and engaged in a course of business that operated as a fraud or deceit on other persons, in violation of Idaho's Uniform Securities Act (2004), Idaho Code § 30-14-101 *et seq.* Jurisdiction is conferred under the provisions of that Act.

DEFENDANT

4. **Stephen L. Howell** (Howell) is an individual residing near Plummer, Benewah County, Idaho, who conducted business as himself and under several other names. Howell has conducted business in Ada, Bingham, Canyon, and Benewah Counties, and elsewhere in the state of Idaho. His current address is 181 Misty Mountain Trail, Plummer, Idaho.

5. **Security Financial Services, Inc.**, (SFServices) was initially incorporated in Idaho as TSI Group, Inc. on February 28, 1989. On September 27, 1991, TSI Group, Inc. changed its name to Security Financial Services, Inc. SFServices has conducted business in Ada, Bingham, Canyon and Benewah Counties, and elsewhere in the state of Idaho. SFServices' business was finding investors and borrowers, and originating and servicing loans. It was and is

a management business that manages money invested in related funds, below. It offered and sold variable interest five-year debentures to fund Security Financial Fund, LLC and Security Investors Fund, LLC. These debentures are securities pursuant to Idaho Code § 30-14-102(28).

6. **Security Financial Fund, LLC** (SFFund), is a limited liability company formed in Idaho on March 22, 2004, with an initial address of 4950 Debonair Lane, Meridian, Idaho. Its current mailing address is PO Box A, Plummer, Idaho, with a physical location of either 181 or 190 Misty Mountain Trail, Plummer, Idaho. SFFund issued securities in the form of debentures and conducted business in Ada, Bingham, Canyon, and Benewah Counties, and elsewhere in the state of Idaho.

7. **Security Investors Fund, LLC** (SIF) is a limited liability company formed in Idaho on July 19, 2007, with an initial address of 4950 Debonair Lane, Meridian, Idaho. Its current mailing address is PO Box A, Plummer, Idaho, with a physical location of either 181 or 190 Misty Mountain Trail, Plummer, Idaho. SIF issued securities in the form of debentures and conducted business in various counties in the state of Idaho.

8. These three companies are all mere alter egos for Howell, and were used to effectuate the fraudulent and **deceitful** course of business related to the offer or sale of securities as described in this Complaint. The companies have such a unity of interest with Howell that the separate personalities of the companies and Howell no longer exist. Further, if Howell is allowed to hide behind the corporate facades it will sanction the fraud, promote injustice, and shield Howell from accountability for the fraud he perpetrated on investors. Their corporate existence should be ignored.

CASE SUMMARY

9. The statements in this Summary of the Case are not part of the allegations

supporting the Department's causes of action, but are simply intended to provide a framework for understanding this regulatory enforcement lawsuit.

10. Howell initially formed SFServices for the purpose of brokering loans by finding investors and pairing them with persons needing real estate loans. He eventually established two funds, SFFund and SIF, into which he pooled investor money, and used those monies to make real estate related loans. Howell solicited investors and accepted investor money and placed it into the two funds.

11. Howell defrauded investors by making representations about his funds' investments, by omitting from their solicitations certain material information, and by engaging in a course of business that operated as a fraud or deceit upon other persons. Howell essentially treated the funds as a personal asset and used the monies and opportunities related to the business transactions of the funds, as a means to enrich himself, often contrary to the best interests of the funds and their investors.

FACTS

12. In the early days of its existence, SFServices made money by brokering loans. It would find lenders and borrowers and put them together for the purpose of making real estate related loans. In 2004, Howell started up SFFund and began to pool investor money, which he would then lend to borrowers.

13. Howell raised around \$20,000,000 in SFFund, which was its maximum subscription amount. In order to raise more, Howell started up SIF in 2007.

14. Howell also leveraged SFFund by obtaining a line of credit through Zions Bank. This was intended to allow the SFFund access to funds needed on a short-term basis. For example, Howell could access the Zions line of credit to to enable SFFund to fund a loan or

make a payout to a withdrawing investor when he otherwise did not have sufficient cash on hand.

15. Over time, Howell allowed the Zions line of credit to grow so large that it became entrenched in his business, and he did not pay it down to zero on a regular basis. It took on the nature of a permanent loan to SFFund, and eventually grew to over \$4.6 million.

16. In 2008, the real estate market took a turn for the worse, and Howell could no longer sustain his previous business practices. He described the change in a document entitled “History of Liberty Resource” that he prepared and distributed to investors: “As we got into 2008 and it took awhile to see that the economy had changed so much. One thing was that we before had averaged over a million dollars in payoffs each month and that all the sudden (sic) came to a screeching halt.”

17. In addition to losing cash flow from loans being paid off by borrowers, SFFund began to experience rising delinquencies. Howell wrote: “By mid summer it was obvious that the economy had changed significantly and that many customers were not paying properly and that nearly everything had significantly changed.”

18. In 2008, Howell was well into developing a resort property in Wyoming. (See, Liberty Resources, below.) The 2008 reversal of fortune meant that Howell could no longer fund the development, and it meant that investors were at risk of losing money.

19. About the same time, a small group of investors began pressuring Howell for information. Howell had an investor, G.B., contribute over \$2,000,000 to SFFund in 2006, and G.B. slowly increased that investment through 2007. Howell solicited more money from G.B., and between August, 2007, and February, 2008, G.B. increased his investment to over \$10,000,000. As his investment increased, G.B. asked for reports and information about his

investment.

20. G.B. was joined in his requests by a few other investors who were pushing for information. One wrote: “As an investor with over \$800,000 invested in SF Fund I kept in close contact with Howell and Jarvis Jr. about the affairs of the Fund. As the economy started to slow down in 2007 I stepped up my scrutiny. I was given very optimistic reports (a good con job in hindsight). Finally in 2008, I and others were given more and more bad news.”

21. On September 17, 2008, in response to this pressure, Howell disclosed the Liberty resort development loans and some of the other problems with SFFund. A bit later, Howell disclosed the information to all investors. This was the first any of the investors knew about Howell’s involvement with Liberty 2 (see paragraph 44, specifically, and surrounding paragraphs for a discussion of Liberty 2).

22. An investor group was set up to review the financial problems of the fund and to determine a course of action, and over the next few months they grappled with the problems created by the money-losing resort development.

23. In January, 2009, Zions declared a default on the terms of its agreement with SFFund, and directed that SFFund stop paying interest payments to investors and to instead devote all net income to paying down the line of credit.

24. G.B. eventually took control of Liberty, divested SFFund’s interest in its assets, and sold the resort at a loss.

25. Howell and his funds have not accepted new investor money, or made a new loan, since 2008.

26. Howell is care-taking the funds, receiving payments from performing loans, making payments to Zions, and selling off fund-owned properties after foreclosing on some of

them.

Self Dealing

27. Howell made several loans to himself, often on favorable terms, using investor money. He also made loans to borrowers who were clearly bad credit risks, but did so because it promoted his personal interest. In one case, for example, he found a borrower whose loan was in foreclosure and arranged for SFFund to loan the borrower money to rebuy the property after the foreclosure. However, Howell bought the property at the foreclosure, using SFFund money, and put it in his name, rather than the fund's. After marking up the price \$30,000, Howell then sold it back to the foreclosed buyer in a pre-arranged deal, who bought it from Howell at the inflated price using an SFFund loan.

28. Howell made several other loans to himself from SFFund, and treated them more favorably than loans to arm's length borrowers. His first loan to himself, HOWST, was begun in 2002, or before, and carried through at least September, 2008. HOWST's current status is unknown.

29. Another loan to himself, HOWST2, began in December, 2005 as a \$350,000 loan (see The Hawk Haven Loan, below). The balance went as low as \$150,728, but by May 18, 2009, had climbed to \$385,181.13. The last payment made on this loan was in January, 2009. It is being carried by SFFund as a delinquent loan, but interest has ceased to accrue, and no effort is being made to collect or foreclose. The balance remains at \$385,181.13.

30. Another loan to himself, MISMO, began in November, 2007 as a \$200,000 loan. The balance climbed to \$400,240.54 by February, 2008, then declined to \$252,392.68 by July, 2009. The last payment made on this loan was in July, 2009. It is being carried by SFFund as a delinquent loan, but interest has ceased to accrue, and no effort is being made to collect or

foreclose. The balance remains at \$252,392.68.

31. Another loan to himself, MISMO2, began in September, 2007 as a \$150,000 loan. This loan was made with SIF funds. The current status is unknown.

32. Howell's naming convention for loans typically used the first three letters of the borrower's last name, and the first two of the first name. Thus, a loan to Stephen Howell became HOWST. It was also his convention to add a number to successive loans. Thus, the second loan to Howell was HOWST2. SFFund had loans named WESDO13 (13 loans), AVEJE11 (11 loans) and several others. These loans reveal Howell's naming convention of sticking with the original loan identifier, but adding a number to reflect a new loan to an existing borrower.

33. After HOWST and HOWST2, Howell named his next loans MISMO and MISMO2. This had the effect of concealing the number of loans he was making to himself.

34. Howell made two more loans to himself, RESLI and PASRE, which were both related to the Liberty property and development. These two loans reached \$6,261,802.70 and \$4,510,771.24, respectively, for a total of \$10,772,573.94, in September, 2008.

35. In September, 2009, Howell owed his funds \$11,410,147.75.

36. The RESLI and PASRE loans have been written off, and no effort is being made to enforce the loan guarantees given by Howell and his Liberty 2 partners for these loans. HOWST2 and MISMO2 are still listed on the books, but are not being paid down or foreclosed. Howell extracted over \$11 million in investor money from the funds to his personal benefit with these four loans.

37. As alleged in Paragraph 59 below, as well as elsewhere, Howell would belatedly execute documents to cover previously completed transactions. This obscured his failure to document the loans properly in the first place. This is part of a pattern of deception by Howell.

Another example of deception occurred in March, 2009, described next.

38. In March, 2009, Liberty 2 had been sued by a trucking company for past due amounts. Howell, anticipating losing the lawsuit, scrambled to hide assets of Liberty from the plaintiff. On March 18, 2009, Howell wrote to members of his oversight committee and disclosed this plan: “I want to get approval to transfer assets such as snowmobil’s (sic), 4-wheelers, backhoe and other titles and equipment to [G.B.] now for protection purposes. We are defending a lawsuit ... I am not sure we can win this law suit and there could be other pending suits that could cause us to loose (sic) equipment and other assetts (sic) that could be attached shortly. ... I feel that we need to trust [G.B.] at this point and transfer any of the titled snow mobils (sic), backhoe and such ... for the continued protection of the assetts. (sic)” He wrote to G.B. on the same day: I am talking about any equipment, snow mobils (sic), 4 wheeler, backhoe and anything else that could be attached. I am not confident that we can win this law suit from [plaintiff], and if they attach land it will not be a problem, but if they attach other equipment it could.”

39. The next day, Howell again wrote to G.B. about the pending lawsuit: “For sure any equipment that is owned in Liberty Resource we would need to move to some other entity.”

Liberty Resources (RESLI & PASRE loans)

40. In February, 2006, Howell approved a loan to Liberty Resources, LLC, (Liberty 1)¹ for \$2.2 million. The members of Liberty 1, Stephen L. (Stephen) and Brett W. (Brett), had a deal worked out whereby they would buy a resort property in Wyoming, develop it with condominiums, sell the condos, and then run a lodge and recreation business from the property.

¹ As explained below, Howell and others took over Liberty Resources, LLC from its initial members. To distinguish acts of the different owners, this Complaint refers to the first group as Liberty 1, and to the second group as Liberty 2.

41. An appraisal of the property dated October, 2005 pegged the value of ten individual condos on the property at \$260,000, 21 “pad sites” where additional condos could be built at \$120,000 each, and a lodge with a value greater than \$1,000,000, for a total of \$6,120,000. The lodge contained a functioning restaurant and bar.

42. As part of the loan, Liberty 1 and SFFund agreed to an escrow withholding. They agreed to withhold \$75,144 of the loan to be used by SFServices to make the first few payments on the loan. That is, SFFund booked a loan in the amount of \$2,200,000, but only gave \$2,000,000 to the borrowers. Some of the remaining \$200,000 paid various fees, but the last \$75,144 was held by either SFFund, SFServices or a title company as an escrow agent. As a payment came due, it was made using the withheld amount. This caused the loan to appear current, even though the borrowers were making no payments. Instead, they were incurring more debt.

43. SFFund funded the loan, but it immediately went sour. Stephen and Brett had believed they had purchasers lined up to buy the initial group of condos, and believed they had a lender willing to finance these purchases. However, right after SFFund funded the loan to Liberty 1, the condo lender backed out and Stephen and Brett were suddenly unable to sell the condos. Without the profit from the sale of the condos, Stephen and Brett were unable to repay the loan.

44. At this point, Howell hatched a plan to step in and take over the Liberty enterprise, along with his friend, Rich Jarvis I, and his employee, Rich Jarvis II (aka, Rich Jarvis Jr.). The three of them replaced Stephen as members of Liberty Resources, LLC, with each (Howell, Jarvis I, Jarvis II, and Brett) having a 25% share (Liberty 2). None of these men had experience in developing or running a resort, hotel, restaurant, or bar.

45. Howell chose not to foreclose the Liberty 1 loan, thereby giving SFFund ownership of the property, and he chose not to have SFFund make the condominium loans to the prospective purchasers. Instead, Howell, the Jarvises and Brett assumed the Liberty 1 loan, effective August 10, 2006, which by then had grown to \$2,249,354.12.

46. On August 11, 2006, Stephen signed a settlement agreement wherein he gave up his interest in Liberty 1 in exchange for \$40,000. Brett received \$25,000 as part of the transition. There was no reason to buy out Stephen and Brett, since they were already being relieved of liability for the \$2,200,000 loan. These payments show that Howell was profligate with SFFund's, and its investors', money.

47. The transfer of ownership occurred primarily by virtue of a Loan Assumption Agreement, dated August 10, 2006, wherein the four members of Liberty 2 assumed the promissory note that SFFund had signed with Liberty 1, Stephen and Brett. None of the members of Liberty 2 personally guaranteed the loan until about two years later.

48. By assuming Liberty 1's SFFund loan, which transferred Liberty 1's interest in the property to Liberty 2, Liberty 2 gained ownership of a property appraised for \$6,120,000, a difference of \$3,870,646, thereby securing any profit that might be made for themselves.

49. Howell did not initially disclose his interest in Liberty 2 to SFFund investors, nor would it be obvious to any investor looking over the books. The loan was listed on SFFund accounting documents as RESLI.²

50. Once in control of Liberty 2, as its managing member, Howell began pouring SFFund money into developing the property and running the recreation business. He remodeled

² In accord with Howell's loan naming convention of using the first three letters from a borrower's last name and two or three letters from the borrower's first name. See Paragraph 32. Thus, Liberty Resources became RESLI.

the lodge and cabins. He built a hotel on the property, hoping that busses going to and from Yellowstone Park would stop. He bought snowmobiles, anticipating a winter recreation business. He paid payroll and other expenses of running the lodge, bar, restaurant, and recreational business property. By September 10, 2008, the RESLI loan balance had increased to \$6,261,802.

51. In addition to making the RESLI loan look as if it were a performing loan, another effect of the escrowed payments was to contribute to SFFund's overall 12% interest payments to investors. A loan as large as RESLI, if not paying interest, could cause the return to investors to dip, which in turn could cause investors to ask questions.

52. Another possible effect is that Howell could skim money from the fund. SFServices takes two percent of the interest paid by a borrower as a loan servicing fee. If a given loan interest rate is 14%, SFServices gets two percent and SFFund investors get 12%. If Howell continued this practice with the RESLI loan, another effect of the ostensible payments was to transfer money from SFFund to Howell on an ongoing basis. For example, on February 15, 2007, Howell caused Liberty 2 to make a \$32,510 payment to SFServices as payment on the SFFund loan, using money loaned to Liberty 2 from SFFund. Of that \$32,510, \$21,235.60 was applied to interest. The RESLI loan interest rate was 10.25%, and thus the investors would get 8.25% and Howell 2%. Of the \$21,235.60 in interest, the investors would get \$16,987, and Howell would get \$4,247.

53. In addition to the ongoing payments, SFServices charged a \$77,700 loan origination fee to make this loan, and a \$295 document preparation fee. Since Stephen and Brett paid no money out of pocket to purchase the property, this fee was a transfer of money from SFFund to Howell.

54. Soon after taking over Liberty 1, the Liberty 2 Group renamed the business as “The Passage Resort,” and conducted the public face of business under that name. On October 31, 2007, Howell opened up a new loan, PASRE (Passage Resort), and used the funds to develop the property, run the business and make payments on the loan. At the time PASRE opened, the RESLI loan balance was \$5,222,176.

55. The two loans, RESLI and PASRE, both related to the same property, were to the same borrower, and paid similar bills. The Department believes and alleges that Howell opened up the second loan, PASRE, in order to keep RESLI from growing too large and attracting attention from investors, and served as a means of deceiving investors about the Liberty 2 loans and Howell’s involvement with Liberty 2.

56. Howell continued to add to the RESLI and PASRE loan balances so that by July 31, 2008, the balances were \$5,976,510 and \$4,510,771, respectively, for a total of \$10,487,281. The two Liberty 2 loans eventually reached a total of \$10,772,574. The bills paid in the names Liberty 2 and Passage Resort were paid on checks written by SFServices.

57. Although the Passage Resort business had income, it had no profits and no way to repay the \$10,000,000 loan. This Liberty 2 loan initially carried monthly payments of \$21,760. Although the actual interest rate is unclear, a 10% rate on a \$10,000,000 loan would require interest payments of over \$80,000 a month. A very profitable business generating a 10% profit would need to gross \$800,000 a month, year round, to service just the interest on the loan.

58. When the economic downturn occurred in 2008, payments to the SFFund declined and Howell could no longer dump money into the Liberty 2 project. Howell explained: “By mid-summer it was obvious that the economy had changed significantly and that many customers were not paying properly...”, “that all the (sic) sudden came to a screeching halt

which left us short on being able to get the work finished and paid for...” and “[i]t was obvious that we had a serious problem because of the lack of funding necessary to have everything completed and the funds necessary to continue operation.”

59. Knowing he would have to disclose to investors his involvement in Liberty 2, the loans to it, and its problems, Howell began to execute documents that made it look like SFFund and Liberty 2 had been dealing at arm’s length. On August 1, 2008, Howell signed a security agreement as the managing member of Liberty 2, giving SIF a security interest goods and equipment owned by Liberty 2 and used at the resort property, to secure a debt of an unstated amount. On August 1, 2008, Howell signed a promissory note as the managing member of Liberty, committing Liberty 2 to pay \$8,572,574 to SFFund, at a 13% interest rate. Howell also signed a Mortgage Deed giving SFFund a security interest in the Liberty 2 land in Wyoming, in the amount of \$8,572,574.

60. Investors eventually learned of the Liberty 2 loans and made efforts to salvage the situation. Those efforts were only partially successful, and after sustaining large losses, the loans were written down to \$5,442,007.21.

61. The last \$5,442,007.21 was “charged off” and removed from SFFunds’s and SIF’s books as an asset.

62. Under pressure from investors, the Jarvises and Howell, but not Brett, signed a guaranty of the Liberty 2 loans, RESLI and PASRE, in October, 2008. Howell dba SFServices is taking no action to enforce this guaranty, other than filing a claim in Jarvis II’s bankruptcy action.

The Childs Loan

63. On April 25, 2002, George E. Childs (Childs), obtained a loan from the Bank of

Idaho (BoIdaho) for purchase of a property consisting of his residence and residential lot. BoIdaho secured the \$131,950 loan with a Deed of Trust giving it an interest in the residence property. The loan was to mature in 2032, and his monthly payment was \$1,348. The residence was and is located in Bingham County, near the town of Shelley.

64. In June, 2002, Childs, obtained a loan from the Bank of Commerce (Commerce) for purchase of a piece of property adjoining his residential lot near Shelley. This property contained some structures and fixtures related to the boarding and showing of horses. Commerce secured the \$130,235.90 loan by taking an interest in the horse property. The loan was to mature about eight years later, in 2010. Childs' monthly payment was \$1,900.

65. By February, 2005, Childs was in breach of his agreement with Commerce, and Commerce issued a notice of default. After some back and forth, a trustee's sale was eventually set for January 31, 2006.

66. At some point, Howell entered this picture, because his son Chad Howell (Chad) commissioned an appraisal of the residence property, through Chad's company, Strong Paw Financial, of Meridian, Idaho. This December 26, 2005 appraisal valued the residence property at \$211,000.

67. The horse property was not appraised, but Paul Fife, an Associate Broker with High Desert Realtors, issued a one-page "Market Analysis" dated January 6, 2006, in which he estimated the value to be \$575,000 to \$585,000. A "Price Opinion" given by Douglas Page of High Desert Realtors suggested a range of \$575,000 to \$600,000. High Desert was later paid \$500 in closing funds for these opinions.

68. On January 9, 2006, Childs completed and faxed to Chad a loan application, loan origination agreement, Good Faith Estimate (GFE), and related documents. In these documents,

Childs listed income of \$5,000 from trucking sales, and \$578 in child support.

69. The payoff on the horse property was estimated at \$141,534 on January 10, 2006, and the payoff on the residence was estimated at \$138,725 on January 12. Childs' total debt on both properties in January 2006 was approximately \$280,259. That number increased daily due to ongoing interest accumulation.

70. Howell and Childs were making arrangements to buy the horse property at the trustee's sale and to pay off the loan on the residence property, which was not going through foreclosure, funding both by a loan from SFFund. Childs would then have both his properties consolidated on a single loan.

71. Several events occurred on January 31, 2006. The trustee's sale of the horse property was held. Chad appeared and bid on the property for Howell. Commerce made a credit bid and opened bidding at \$142,416.30. Chad and another bidder competed for the property, with Chad eventually placing the winning bid of \$226,000. Because the property sold for more than was owed to Commerce, Childs was entitled to the extra, \$83,583.70. Childs directed that these excess sales proceeds be paid to SFServices.

72. That same day, Howell instructed SFService's bank, Zions Bank, to advance \$100,000 from a line of credit for the Childs property, and also instructed Zions to wire \$226,000 to Commerce.

73. Also on the 31st, Childs and Howell executed a Real Estate Purchase Agreement, for Childs to buy the property from Howell for \$256,000. The extra \$83,583.70 from the Trustee's sale was applied as earnest money and as a down payment for the purchase. The trustee issued a Trustee's Deed vesting title to the property in Howell and his wife.

74. At the close of the day on January 31, 2006, Howell had directed his company to

borrow \$100,000 on its line of credit and then pay \$226,000 for the horse property, but vested title in his and his wife's names. He simultaneously sold the property back to the foreclosed debtor, Childs, for \$256,000, making a one-day personal profit of \$30,000³.

75. Between January 31 and March 17, 2006, Childs worked with Chad and Howell to complete the loan and to refinance the residence property, so that Childs ended up with one loan, owed to SFFund, in the amount of \$347,000.

76. The cost of consolidating the two properties into the SFFund loan was \$430,156.94. Applying the \$83,583.70 down payment and various closing costs brought the total owed by Childs down to \$347,000. Childs, who had been in foreclosure due to lack of payment, had just increased his debt from around \$280,000 to \$347,000, or by about \$67,000.

77. This loan bore an interest rate of 14%, and required Childs to make monthly payments of \$4,177.05. It also required a final lump sum payment of \$340,082.32, due on March 17, 2011. It is unclear how Childs, with only \$5,578 in monthly income, and after making these payments, only \$1,402 in net income, was going to obtain the \$340,082.32 payoff in five years.

78. At the closing of the loan on March 16, 2006, SFServices was paid \$9,350 as a loan fee, and Chad's company, Strong Paw Financial, was paid \$25,350 as a "Mortgage Brokers Fee." Also, Howell and his wife deeded the horse property back to Childs.

79. The Howells did not sign a promissory note or loan documents with SFFund when it purchased the horse property in their names. He simply had SFFund buy it for him, no doubt contemplating the pending transfer back to Childs. Putting the property in his name was not necessary to the transaction, other than it allowed him to skim \$30,000 from the deal.

³ Later documents indicate that the contract sales price was \$245,000, which would reduce Howell's profit to \$20,000.

80. Within months, Childs had fallen behind on his payments to SFFund. The fund and Childs went back and forth with a series of Notices of Default and a subsequent cure of the default.

81. SFServices eventually foreclosed its interest in the two properties a year later, on November 27, 2007, by which time Childs owed \$416,412.65, due to unpaid accruing interest.

82. After evicting Childs, SFServices spent over \$25,000 to refurbish and maintain the properties.⁴ The two properties were sold to separate purchasers, with title transferring in November, 2010. The horse property was sold for \$150,000, and the Department believes that the residence property fetched in the vicinity of \$183,000, for a total of \$333,000.

The Hawk Haven Loan (HOWST2 loan)

83. Marvin M. Gibbons (Gibbons) commissioned an appraisal of about 15 acres of farm ground east of Kuna, Idaho, near Hawk Haven Road, dated December 4, 2000. That appraisal set the value of the parcel at \$226,000.

84. On February 14, 2002, Gibbons gave SFServices a security interest in the Hawk Haven property (Hawk Haven), to secure payment of a \$135,000 loan.

85. On July 28, 2004, Gibbons conveyed Hawk Haven to SFServices. The following January, SFServices deeded the property to Gibbons' company, Quintessence Consulting, Inc. (Quintessence). At the same time, Quintessence gave SFFund a security interest in the property, to secure a \$270,000 loan.⁵

86. Four months later, in April, 2005, SFFund assigned its interest in the property to

⁴ The source of these funds is unclear. Howell may have required SFFund as the property owner to spend the money, or he could have used SFServices funds.

⁵ Multiple related transactions occurred at the same time involving Gibbons residence property, the effect of which was to give SFFund a security interest in both Gibbon's residence property, and Hawk Haven.

the Farmers and Merchants State Bank Trust Department, Custodian for the Roy Barrett IRA (Farmers). In June, Farmers reconveyed the property back to Quintessence. Howell asserts that this reconveyance was in error. At this point, Quintessence owed SFFund whatever the balance of the loan was, but SFFund had nothing to secure payment.

87. On November 10, 2005, Howell and his wife borrowed \$350,000 from SFFund and executed a promissory note in that amount, in order to buy Hawk Haven. Quintessence passed title in Hawk Haven to Stephen and Darri Howell, husband and wife. The Howells gave SFFund a security interest in a property identified as “550 Turkey Troot (sic) Trail, Plummer Idaho⁶” to secure the loan. 550 Turkey Trot Trail has been renamed and is now 181 Misty Mountain Trail, which is Howell’s residence.

88. No appraisal was done prior to this new loan. The last appraisal had been done in 2000, almost five years earlier.

89. The Deed of Trust securing the property for SFFund was never recorded.

90. Howell bought a title insurance policy for Hawk Haven in the amount of \$288,020, indicating that the property was valued at that amount. Since Gibbons owed only around \$270,000 on the property, Howell essentially made himself a “home equity loan” for about \$80,000.

91. The \$350,000 loan was carried on SFFund’s books under the name HOWST2. The interest rate was 6.75%.

92. About a year later, in September, 2006, the Howells gave a security interest in Hawk Haven to Farmers to secure a revolving line of credit that had a maximum of \$350,000. Farmers’ security interest was modified in May, 2007 to reduce the \$350,000 to a maximum of

⁶ See paragraphs 102 - 108, below.

\$174,345.48. The Department believes and alleges that Howell did not disclose the existence of SFFund's unperfected security interest in the property to Farmers. Because Howell failed to record the SFFund Deed of Trust, and therefore failed to perfect its security interest, Howell was able to use that same property to secure a second \$350,000 loan.

93. At the time of the Farmers' line of credit loan, the Howells still owed SFFund around \$350,000 in the HOWST2 loan.

94. In September, 2008, the Howells signed a promissory note for \$380,000, payable to SFFund, and pledged Hawk Haven as collateral. The interest rate on this loan was 10%. That same month, the trustee for Farmers reconveyed Farmers' interest in Hawk Haven back to the Howells.

95. The \$380,000 promissory note replaced the previous SFFund \$350,000 loan, which at the time of the replacement had a balance of \$329,581.64. The effect was that Howell advanced himself \$50,000 from SFFund, and increased his debt to the fund. Although the note and security interest were dated in September, 2008, the \$50,000 was actually advanced to Howell on July 2, 2008. As with the Liberty 2 loan, Howell belatedly executed loan documents to cover previously completed transactions. This again obscured his failure to document the loans properly in the first place.

96. Another effect of the replacement was that SFFund now had a security interest in Hawk Haven, but still had the unperfected security interest in the Turkey Trot Trail property.

97. Howell was frequently late with the SFFund payments, sometimes by months. By the time Howell advanced himself the additional \$50,000 in July, 2008, he had made only 18 payments of the 31 payments due on the original loan.

98. Howell's last payment on the Hawk Haven loan was made on January 29, 2009.

SFServices has not initiated foreclosure of its security interest on this property.

99. Gibbons offered to buy the property back from Howell, about a year ago, at current market value. Howell refused the offer.

100. Although the loan documents establish an interest rate of 10%, it is set in SFFund's accounting software at 8%.

101. Howell's accounting software adds unpaid interest to the principal owed, and updates the balance, only when a payment is made. Because Howell has not made a payment for over three years, the delinquency reports that SFFund prepares, and that are provided to investors, substantially underreport the actual amount Howell owes on this loan. The reports reflect a balance of \$385,181.13, but the last time that was accurate was January 29, 2009. Depending on how it is calculated, the balance is closer to a range of \$500,000 - \$550,000.

The Benewah County Loans (MISMO, MISMO2 and WYADO2 loans)

102. Howell has caused SFFund and SIF to make at least three loans related to his personal residence in Plummer, Idaho, which he calls Misty Mountain.

PDR10 aka 550 Turkey Trot Trail aka 181 Misty Mountain Trail

103. Howell's residence sits on a 20 acre lot east of Plummer, Idaho, and is listed in Benewah County Assessor records as PDR10. SFServices, in its pre-SFFund days, loaned Donald and Betty Wyatt \$260,000 on December 16, 2002 to purchase PDR10, and took a security interest in the property in that amount. This loan was carried on SFServices books as WYADO.

104. The Wyatts defaulted on this loan and a trustee's sale was held on January 20, 2005. In addition to the SFServices loan, the Wyatts owed unpaid taxes for 2002 and 2003.

105. The sale was held, and SFServices was the highest bidder. Although its credit bid

was the largest part of the highest bid, SFServices had to pay an additional amount to cover the back taxes. The trustee gave SFServices a Trustee's Deed for PRD10 on January 20, 2005.

106. On October 26, 2005, SFServices transferred title to the property to Stephen and Darri Howell. There is no evidence known to the Department of any compensation for this transaction, and therefore the Department believes and alleges that Howell just simply transferred ownership to himself, for free.

107. The Department believes and alleges that Howell transferred the property into his name so that he would own his residence property, rather than SFServices, and in preparation to use the property to secure a November 10, 2005 loan in the amount of \$350,000, which was used to purchase Hawk Haven. See Paragraph 87 above.

108. On March 3, 2008, the Howells borrowed \$500,000 from Charter One, a division of RBS Citizens, N.A., of Providence, Rhode Island. The Howells gave Charter One a Deed of Trust on PDR10 to secure this loan, thereby "pulling out" the equity and encumbering the property.

PDR8

109. On October 25, 2005, the Howells bought and took title to a 20 acre property listed with the Benewah County Assessor as PDR8. This property shares about 660 feet of its western border with Howell's residence property, PDR10, making the two properties essentially one.

110. No appraisal was done on either property.

111. On August 11, 2008, the Howells gave SIF a Deed of Trust on PDR8 and on another nearby piece of property they owned outright, to secure a debt in the amount of \$215,000.

112. There is no corresponding loan in that amount, but in September, 2008, Howell initiated a loan from SIF in the amount of \$150,000. This loan is carried on SFServices books as MISMO2 (Misty Mountain # 2). The Department believes and alleges that Howell is not making payments on this loan.

PDR27

113. PDR27 is a property located just downhill from the Howell residence outside Plummer, Idaho, approximately 1,000 feet. The road to the Howell property follows the southern border of PDR27 for about 700 feet.

114. Donald and Betty Wyatt bought this property on November 26, 2005, for \$119,000. The sellers credited the Wyatts with “the non refundable down payment from previous tenant in exchange for work and expense on the damage and state of the property, of \$21,000.” Thus, the Wyatts were able to purchase PDR27 for an outlay of \$98,000.

115. The Wyatts borrowed \$104,000 from SFFund on the same day, in order to purchase the property, even though just 11 months earlier they had defaulted on their first loan with SFFund. The loan was and is carried on SFServices books as WYADO2.

116. SFServices charged no loan origination fee to make this loan.

117. The stated interest rate was 11%. The loan was set up with a \$990.42 monthly payment, which was essentially an interest only payment, for five years. The Wyatts were to make a lump sum payment of \$102,041.32 on November 29, 2010, to pay off the loan.

118. The Wyatts executed a Deed of Trust giving SFFund a security interest in the property.

119. SFFund used its Zions line of credit to fund this loan, thereby increasing its debt to Zions by \$104,000. In exchange, SFFund assigned its security interest in PDR27 to Zions, as

security.

120. Three days later, on November 29, 2005, the Wyatts signed an “Option to Purchase” giving the Howells the ability to buy the property for \$115,000.

121. In February, 2006, the Wyatts made the February payment with an insufficient funds check.

122. Over the next three years, SFServices issued several “Final Foreclosure” letters, on March 20, 2006 (three months delinquency, \$3,170.30), on October 23, 2006 (three months delinquency, \$3,170.30), on April 19, 2007 (three months delinquency plus late fees, \$3,768.10), on May 29, 2008 (two months delinquency plus late fees, \$2,149.40), on January 6, 2009 (four months delinquency plus late fees, \$4,199.76), and on April 2, 2009 (four months delinquency plus late fees, \$4,249.28).

123. The WYADO2 loan began to appear on SFFund Loan Delinquency reports in September, 2008. Although the Department does not have a delinquency report for every month since then, the WYADO2 loan appears on all ten of the delinquency reports that the Department does have⁷, dated after September, 2008.

124. For the period May 18, 2009 through October 4, 2010, the delinquency report shows the interest always being paid up through the month preceding the report. For example, the May 18, 2009 report shows interest as being paid through April 30, 2009, and the October 4, 2010 reports shows interest as being paid through September 30, 2010. It is unclear why the interest is always shown as current even though the loan is carried as delinquent and foreclosure notices show months of late payments.

⁷ Beginning with September, 2008, the Department has delinquency reports for: November, 2008; January, 2009; May, 2009; October, 2009; January, 2010; April, 2010; October, 2010; April, 2011; and April, 2012.

125. Although being carried on the delinquency reports, the balance due on the loan stayed at exactly \$105,588.62 from May, 2009 through October, 2010.

126. In January, 2010, the interest rate on WYADO2 dropped to 7%, and by April, 2010, it had dropped by 6%, where it remains.

127. The WYADO2 loan was to be paid off by November, 2010, but it was not. By not collecting or foreclosing, and by dropping the interest rate, Howell was enabling the Wyatts to stay on the property. Had he foreclosed, Howell would have lost his personal option to buy the property.

128. Howell allowed the Wyatts to remain on the property in order to preserve his option to buy it, to the detriment of SFFund investors.

129. SFServices paid property taxes on the property on July 21, 2009, August 13, 2010, and September 30, 2011.

Shay Hill

130. On June 22, 2006, the Howells bought another nearby property known as Shay Hill, for \$112,500. The sellers "carried the paper" on the purchase, and took a security interest in the property as security. By October 24, 2006, the Howells had paid off the sellers, and they conveyed clear title to Howells.

131. On September 1, 2008, the Howells executed a Promissory Note and a Deed of Trust for a \$250,000 loan from SFFund, thereby giving the fund a security interest in the property. This was shortly after Howell met with a few concerned investors and disclosed the problems with the Liberty 2 loans and the other delinquencies.

132. The \$250,000 loan had been advanced to Howell nearly a year earlier. He received \$200,000 on November 20, 2007 and \$50,000 on December 13, 2007. These

transactions are reflected on the Borrower Statement of Account for the loan known as MISMO.

133. Howell executed the 2008 loan documents anticipating scrutiny from investors.

134. According to the April 10, 2010 Delinquency Report, the last payment on this loan was made October, 2008. SFServices is making no effort to foreclose this loan and sell the property.

Misrepresentations

135. To induce investors to invest, Howell made certain representations. These representations were false.

136. Howell represented to investor L.C., and others, that he did not make loans to himself, other than the Hawk Haven loan.

137. Howell represented in Paragraph 11 of the Security Financial Prospectus that “The Operating Agreement of the Issuer provides that the management of the Issuer is under the direct control of a Board of Managers consisting of three Managers,” and that “The Board of Managers appoints the officers of the Issuer.”

138. Lise Lotte-Stoffel was listed in the prospectus as one of the Managers of SFFund. In a corporate filing with the Idaho Secretary of State dated January, 2012, she is still listed as a member of SFFund.

139. Lotte-Stoffel states that she has attended no corporate organizational meetings and has appointed no officers.

140. Investors L.C. and S.M. understood that the Board of Managers would be actively involved in supervising the SFFund, and would review the large or unusual loans. This did not occur.

141. Howell stated in Paragraph 4.1 of the prospectus that “In each instance Security

Financial will obtain at least one third party appraisal of the subject property to determine the loan to value ratio.” Howell failed to obtain third party appraisals for at least these properties/loans: WYADO2; MISMO; Hawk Haven (an appraisal was done, but five years before the loan, and therefore it was not valid at the time of the loan); Abbey & Crumb Development, LLC, \$253,000 loan, Lot 10 Block B, Fritz Heath Forest Tract; Avery, \$164,725 loan, 320 S 3rd West, Rigby, Idaho; Brantner, \$150,000 loan, 88840 Highway 3 North, St. Maries, Idaho; Christensen, \$72,000 loan, 4001 Elmore, Parma, Idaho; and Cysewski #2, \$142,000 loan. Some loans relied exclusively on the county assessor’s assessment.

142. In the Debentures issued to investors, Howell stated: “Essentially, the investments made with proceeds from the issuance of these Debentures will be held by the Company [SFFund] for the benefit of and for payment so the Debentures...” This statement is false because as identified above regarding the Hawk Haven, Childs, HOWST, HOWST2, MISMO and MISMO2 loans, the investments were not made for the benefits of the debentures, but rather for the benefit of Howell.

Material Omissions

143. Howell did not tell potential investors certain information that would be necessary to make other statements not misleading, and that an investor would likely consider as material to a decision to invest with Howell. Howell failed to disclose the following material information:

- a. His involvement in Liberty Resources, LLC;
- b. That he would loan money for the purchase of personal property, such as snowmobiles;
- c. That he would exceed the loan to value ratios stated in the Prospectus;

- d. That he would make loans without obtaining third party appraisals;
- e. That he would make numerous loans to himself and his family;
- f. That he would be the largest single borrower from SFFund;
- g. That the family loans would often be on more favorable terms than arms-length loans;
- h. That he would not repay the loans made to him;
- i. That he would sit on properties he owned, in which SFFund has a security interest, and make no effort to foreclose and sell the properties to repay the fund;
- j. That he would make questionable loans to unqualified borrowers in order to promote his personal interests.

COUNT ONE

(Fraud - False and Misleading Statements)

144. The allegations of paragraphs 1 through 8 and 12 through 143 above are realleged and incorporated herein as if set forth verbatim.

145. Idaho Code § 30-14-501(2) provides that it is unlawful for any person, directly or indirectly, in connection with the offer, sale or purchase of a security, to make an untrue statement of material fact or omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading.

146. Howell's misrepresentations to prospective investors as set forth in paragraphs 135 through 142 were made in connection with the offer, sale or purchase of securities. Howell's misrepresentations were false and misleading, constituting violations of Idaho Code § 30-14-501(2) as to each misrepresentation to each investor.

147. Howell's omissions of material facts and failures to disclose to prospective

investors as set forth in paragraph 143 were made in connection with the offer, sale or purchase of securities. Howell's omissions of material facts and failures to disclose constitute violations of Idaho Code § 30-14-501(2) as to each omission and failure to disclose to each investor.

COUNT TWO
(Fraudulent Conduct)

148. The allegations of paragraphs 1 through 8 and 12 through 143 above are realleged and incorporated herein as if set forth verbatim.

149. Idaho Code § 30-14-501(3) provides that it is unlawful for any person, directly or indirectly, in connection with the offer, sale or purchase of a security, to engage in an act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.

150. Howell's acts as set forth in paragraphs 1 through 8 and 12 through 143 above were made in connection with the offer, sale or purchase of securities. His conduct as described those paragraphs constitutes engaging in transactions, acts, practices, or courses of business which operate or would operate as a fraud or deceit upon investors or prospective investors, in violation of Idaho Code § 30-14-501(3) as to each victim. The fraud was accomplished by a lengthy pattern of self dealing, often to the detriment of the fund, and by a pattern of actions designed to conceal or perpetuate the fraud.

PRAYER FOR RELIEF

WHEREFORE, the Department prays for judgment in favor of the Department and against Howell as follows:

1. That Howell be adjudged to have violated Idaho's Uniform Securities Act (2004), Idaho Code § 30-14-101 *et seq.*, rules promulgated thereunder, and other applicable

federal laws and regulations as proven at trial, as to Counts One and Two alleged above, as well as any additional counts proven at trial.

2. That Howell be permanently enjoined from engaging in any act or practice violating any provision of the Act or any rule promulgated thereunder, pursuant to Idaho Code § 30-14-603(b)(1), and that he be permanently enjoined from selling or offering for sale securities in any form in the state of Idaho.

3. That Howell be ordered to pay a civil penalty of up to ten thousand dollars (\$10,000) for each violation of the Act as the Court deems appropriate, pursuant to Idaho Code § 30-14-603(b)(2)(C), for total penalties of at least twenty thousand dollars (\$20,000), and that the Court award a money judgment in favor of the Department in such amount.

4. That Howell's personal assets be frozen and that a receiver be appointed to take charge of such assets to liquidate them and apply them to the proper administration of the funds.

5. That the receiver take charge and control of the funds and manage them for the benefit of the investors.

6. That the Department be awarded attorney fees and costs incurred in the preparation and prosecution of this action, pursuant to Idaho Code § 12-121, and that the Court award a money judgment in favor of the Department in such amount. Should judgment be taken by default herein, the Department asserts that \$5,000 is a reasonable sum for the same.

7. For such further relief as this Court may deem just and equitable under the circumstances.

DATED this 4th day of OCTOBER, 2012.



ALAN CONILOGUE
Deputy Attorney General