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10 UNITED STATES DISTRICT COURT  
11 CENTRAL DISTRICT OF CALIFORNIA

13 SECURITIES AND EXCHANGE  
14 COMMISSION,

15 Plaintiff,

16 vs.

17 LARRY R. POLHILL,

18 Defendant.

EDCV13-1729 MRP/SPX  
COMPLAINT

21 COMPLAINT

22 Plaintiff Securities and Exchange Commission ("SEC") alleges as follows:

23 JURISDICTION AND VENUE

24 1. This Court has jurisdiction over this action pursuant to Sections 20(b),  
25 20(d)(1) and 22(a) of the Securities Act of 1933 (the "Securities Act"), 15 U.S.C. §§  
26 77t(b), 77t(d)(1) & 77v(a), and Sections 21(d)(1), 21(d)(3)(A), 21(e) and 27 of the  
27 Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. §§ 78u(d)(1),  
28 78u(d)(3)(A), 78u(e) & 78aa. Defendant Larry R. Pohill has, directly or indirectly,

1 made use of the means or instrumentalities of interstate commerce, of the mails, or of  
2 the facilities of a national securities exchange, in connection with the transactions,  
3 acts, practices, and courses of business alleged in this Complaint.

4 2. Venue is proper in this district pursuant to Section 22(a) of the Securities  
5 Act, 15 U.S.C. § 77v(a), and Section 27 of the Exchange Act, 15 U.S.C. § 78aa,  
6 because certain of the transactions, acts, practices, and courses of conduct  
7 constituting violations of the federal securities laws occurred within this district, and  
8 Polhill resides in this district.

9 SUMMARY

10 3. This case concerns a decades-long investment fraud perpetrated on over  
11 485 investors who are now owed almost \$160 million by American Pacific Financial  
12 Corporation (“APFC”), which was controlled at all relevant times by Defendant Larry  
13 R. Polhill.

14 4. Polhill used APFC to buy and sell real estate and distressed assets,  
15 offering investors the opportunity to invest in the company, mainly through the  
16 unregistered issuance of promissory notes that were allegedly secured by collateral,  
17 such as specific pieces of property.

18 5. Polhill made a number of material misrepresentations and omissions to  
19 investors during the course of APFC’s note offering. Specifically, Polhill (i)  
20 misrepresented to investors that the notes were secured by specific collateral when, in  
21 fact, no such security interest existed; (ii) failed to disclose that what collateral did  
22 exist was often already pledged to other lenders or impaired in some other way; and  
23 (iii) misrepresented that he would notify investors if their collateral went into default.  
24 As a result, when APFC declared bankruptcy in 2010, investors who had been  
25 promised that their loans were secured by specific assets were named in the  
26 bankruptcy as unsecured creditors and left with nothing to show for their investment.

27 6. In addition to the promissory note offering, Polhill also offered investors  
28 the opportunity to invest in several APFC-sponsored limited partnerships, known as

1 “Funds.” The Funds pooled investor money and used it to make loans to APFC.  
2 APFC paid interest on the loans to the Funds, and the interest was distributed out to  
3 Fund investors. Interests in the Funds were securities in the form of investment  
4 contracts, but were never registered with the SEC as they should have been.

5 7. As a result, Polhill has violated Sections 5(a), 5(c), and 17(a)(2) of the  
6 Securities Act, 15 U.S.C. §§ 77e(a), 77e(c), and 77q(a)(2); Section 10(b) of the  
7 Exchange Act, 15 U.S.C. § 78j(b); and Exchange Act Rule 10b-5(b), 17 C.F.R. §  
8 240.10b-5(b). Unless restrained and enjoined, Polhill is reasonably likely to continue  
9 to violate the federal securities laws.

#### 10 THE DEFENDANT

11 8. **Larry R. Polhill**, age 61, resides in Grand Terrace, California. At all  
12 relevant times, he was the president of APFC and controlled its operations.

#### 13 AFFILIATED ENTITY

14 9. **American Pacific Financial Corporation** is a California corporation  
15 formed on June 5, 1978, and based in San Bernardino, California. APFC purported to  
16 be a “private equity real estate and equity venture capital firm.” On September 21,  
17 2010, APFC filed for Chapter 11 protection in the United States Bankruptcy Court for  
18 the District of Nevada. In May 2011, the bankruptcy court appointed a Chapter 11  
19 Trustee to take over APFC’s operations, and in February 2012, the matter was  
20 converted to a Chapter 7 bankruptcy. APFC’s investors are named as unsecured  
21 creditors in the bankruptcy proceeding.

#### 22 STATEMENT OF FACTS

##### 23 A. Background

24 10. APFC was incorporated in 1978, and was originally in the real estate  
25 brokerage business. Polhill took control of the company shortly after 1978, and used  
26 it to invest primarily in real estate. Although during most of APFC’s existence, the  
27 company was co-owned by Polhill and another individual, Polhill had complete  
28 control over the company at all relevant times.

1           11. Over the years, the company became more involved in the business of  
2 buying distressed assets, including buying companies out of bankruptcy.

3           12. Polhill offered investors the opportunity to invest in APFC through  
4 promissory notes issued by APFC. Under the terms of these notes, APFC was  
5 supposed to make regular interest payments at rates ranging from 5%-17% per year.  
6 Also, by their terms and based on representations from Polhill, the notes were  
7 purportedly secured by specific assets owned by APFC.

8           13. Investors could also invest in APFC-sponsored limited partnerships,  
9 known as "Funds." The Funds pooled investor money to make loans to APFC, and  
10 APFC's interest payments on those loans were supposed to be distributed to investors  
11 in quarterly distributions.

12           14. Between the mid-1980s and 2007, APFC made regularly scheduled  
13 interest payments to its investors. As a result, its investor base continually grew, and  
14 the company began making larger and larger investments in distressed assets by  
15 buying numerous companies out of bankruptcy. The company's investments  
16 included companies involved in the food and beverage services, plastic lumber,  
17 semiconductors, entertainment, trucking, education and aerospace.

18           15. While a few of APFC's investments were successful, unbeknownst to  
19 investors, the vast majority failed. As a result, the assets held by APFC—which were  
20 securing the loans held by investors—decreased in value. A 2011 forensic  
21 examination performed on behalf of APFC's committee of unsecured creditors found  
22 that more than 83% of the company's 2005 assets were eventually written off as bad  
23 debts, and that the company was insolvent at least as early as 2005, and probably for  
24 years prior to that.

25           16. In early 2008, APFC ceased making its scheduled payments to most  
26 investors but continued to issue newsletters, make payments to preferred investors,  
27 and engage in other activities designed to lull investors into a false sense of security  
28 regarding their investments with the company. In its bankruptcy filing, APFC listed

1 its last promissory note as having been issued in April 2008.

2 17. In September 2010, APFC filed for Chapter 11 bankruptcy, disclosing a  
3 total of approximately \$103 million owed to more than 485 “unsecured” promissory  
4 note holders, and \$55 million owed to the Funds. In May 2011, the bankruptcy court  
5 appointed a Chapter 11 Trustee to investigate and oversee APFC’s operations, based  
6 on allegations of fraud. In February 2012, a Chapter 7 Trustee was appointed, and  
7 the Chapter 7 Trustee has filed an adversary proceeding against Polhill alleging fraud.

8 **B. Polhill’s Fraudulent Promissory Note Offerings**

9 18. The majority of Polhill’s securities offerings were in the form of APFC  
10 promissory notes. Polhill told investors that their investments would be for a  
11 specified term, would generate interest payments on a monthly or quarterly basis, and  
12 that their investments were safe because they were secured by a specific piece of  
13 collateral owned by APFC.

14 19. The APFC notes were entitled “Contractual Loan Agreement/  
15 Promissory Note Secured by Pledge of Collateral.” They were made between the  
16 individual investors and APFC, and were all in the same general one-page form,  
17 which outlined the investment amount, the term of the note (usually one to four  
18 years), and the agreed-upon interest rate, which ranged between 5-17%. A sample  
19 APFC promissory note is attached hereto as Exhibit A.

20 20. The notes also included an extension/renewal provision that allowed  
21 APFC to automatically extend the terms of the notes if an investor did not specifically  
22 request payment at the end of the initial term. As a matter of course, the notes were  
23 routinely extended for multiple terms.

24 21. In addition, the notes stated that they were secured by collateral in the  
25 form of a specific asset, such as a piece of property.

26 22. The notes also stated that if the pledged collateral went into default, the  
27 investor would have the opportunity to choose among several different options,  
28 including receiving substitute collateral or a “principal reduction” of their loan (i.e., a

1 refund of some portion of their investment).

2 23. Polhill signed all of the notes on behalf of APFC, and was personally  
3 responsible for choosing the collateral that would be used as security for each note.  
4 Polhill did not specifically check on the adequacy of the collateral pledged for each  
5 note, but rather claimed he relied on “his gut” to inform his decisions.

6 24. APFC and Polhill had no procedure in place to prevent the same piece of  
7 collateral from being pledged to multiple note-holders, or issuing notes secured by  
8 collateral that had, for example, already been pledged to a bank. Additionally, APFC  
9 had no procedures in place to monitor the safety of a note’s collateral during its initial  
10 and extended terms.

11 25. Polhill also never took any steps to perfect the notes’ security interests.  
12 As a result, it was only when APFC filed for bankruptcy and named all of the note  
13 holders as “unsecured creditors,” that the investors were informed that their notes  
14 were not truly “secured,” and that the collateral underlying their notes often either no  
15 longer existed or was insufficient to cover all of the loans for which it had been  
16 pledged.

17 **1. Misrepresentations regarding the Security of the Notes**

18 26. Polhill misrepresented the security of APFC’s notes to investors.

19 27. The notes expressly stated that they were secured by specific collateral.  
20 In addition to the terms of the notes themselves, Polhill told investors that  
21 investments in the notes were safe because they were secured by specific assets.

22 28. The APFC notes also included the following statement regarding the  
23 steps APFC would take to secure the notes:

24 AMERICAN PACIFIC FINANCIAL CORPORATION is hereby  
25 authorized *and instructed* to service all pledged collateral *including*  
26 *the filing of all required notices* and taking any prudent action  
necessary to preserve the equity of said collateral.

27 (Emphasis added.)

28 29. These representations regarding the notes’ security were false. The

1 notes were never truly “secured” by any collateral because Polhill failed to file the  
2 paperwork necessary to perfect a legal security interest in the collateral on behalf of  
3 investors. As a result, when APFC declared bankruptcy, over 485 investors who held  
4 allegedly “secured” notes, were listed as unsecured creditors, and had nothing to  
5 show for their investment.

6 30. Polhill, whose business involved buying assets out of bankruptcy, was  
7 fully aware of the importance of legal security interests, and how to perfect them.  
8 For example, in contrast to how he failed to ensure that the notes held by the  
9 investors were secured, Polhill made sure that APFC’s own security interests in third  
10 party assets were legally secured through the filing of UCC paperwork.

11 **2. Misrepresentations regarding the Status of the Notes’ Collateral**

12 31. Polhill also failed to disclose to investors that the collateral supposedly  
13 securing their notes was often impaired at the time he issued the notes.

14 32. Sometimes when the notes were issued to investors, the collateral  
15 identified as security for the notes had already been pledged to a senior lender, such  
16 as a bank. On other occasions, the identified collateral had been pledged to too many  
17 other investors.

18 33. As an example, one investor held an APFC note with a term of January  
19 2008 to January 2011. The note stated that it was secured by real estate located in  
20 Glen Cove, New York, which the note claimed had been pledged as collateral for the  
21 note. However, Polhill and APFC had failed to disclose that this property was  
22 already encumbered by a senior mortgage. Moreover, neither Polhill nor APFC  
23 disclosed that APFC had defaulted on the mortgage payments it owed on that  
24 collateral back in 2007—well before it issued the note to the investor.

25 34. As another example, over 80 investors held notes from APFC note  
26 offerings from 2004 to 2008. These notes specifically stated that the notes were  
27 secured by accounts receivable owed by Café Valley, a privately-held bakery, and the  
28 notes claimed this account receivable had been pledged as collateral for the notes.

1 However, Polhill and APFC never disclosed that this collateral was already subject to  
2 a senior bank lien.

3 **3. Misrepresentations regarding Events of Default**

4 35. Pohill misrepresented and failed to disclose events of default regarding  
5 the collateral supposedly securing the APFC notes.

6 36. The terms of the notes issued by Polhill represented that investors would  
7 be notified of problems with their collateral by claiming that the investors would be  
8 given the option of receiving new collateral or a reduction in the principal balance of  
9 their loan in the event such problems occurred. The notes included language stating  
10 that the defined collateral would secure the note "at all times during the course of this  
11 Agreement."

12 37. The notes also included the following language:

13 Whenever pledged collateral becomes in default, or whenever  
14 requested by AMERICAN PACIFIC FINANCIAL CORPORATION,  
15 Beneficiary agrees to release said pledged collateral to AMERICAN  
16 PACIFIC FINANCIAL CORPORATION and upon such release,  
17 Beneficiary shall select any one of these three options:

- 18 (1) Receiving a principal reduction in this loan (in an amount equal to  
19 that pledged as security by the released collateral), or  
20 (2) Accepting substitute security, or  
21 (3) Directing that funds be held in trust, pending approval of  
22 replacement security by Beneficiary.

23 38. In addition, the last paragraph of the note stated that pledged collateral  
24 "is to be held in safekeeping by AMERICAN PACIFIC FINANCIAL  
25 CORPORATION and available for inspection to Beneficiary upon request."

26 39. These representations were false. Polhill and APFC did not maintain  
27 the collateral pledged as security for the notes throughout their terms, and often sold  
28 or lost the original pledged collateral without notifying investors.

39. APFC and Polhill also did not notify investors when collateral went into  
default and did not offer investors the options of (i) reducing their loans; (ii)



1 accepting substitute security; or (iii) placing their funds in trust pending their  
2 approval of a replacement security as required under the terms of the promissory  
3 note. Finally, APFC and Polhill did not hold the pledged collateral in safekeeping  
4 and available for inspection by the investors upon request.

5 41. In fact, APFC and Polhill had no procedures or safeguards in place to  
6 track the status of investor collateral and ensure that appropriate notice was being  
7 provided in the event of default.

8 42. Furthermore, even when Polhill was fully aware that collateral securing  
9 investor notes was impaired, he did not tell investors. For example, in one instance,  
10 Polhill's cousin held one of the APFC notes. When his cousin learned that the  
11 collateral securing that note was no longer valuable, the cousin asked Polhill for  
12 substitute collateral. Polhill agreed, and substituted new collateral to secure that note.  
13 However, Polhill did not inform any of the other investors holding that note that the  
14 collateral was impaired.

15 43. Moreover, Polhill and APFC represented that, throughout the course of  
16 the investors' investment, their notes were secured by a specific piece of collateral  
17 that the investors would be able to rely on if APFC ever failed to repay their loans or  
18 otherwise default on the notes. In reality, Polhill had often sold or disposed of the  
19 collateral with no notice to investors.

20 44. For example, one investor held an APFC note with an initial term of  
21 May 2003 to March 2005, which was later extended through 2008. His note  
22 specifically stated that the note was secured by accounts receivable owed by GB&L  
23 Trucking, a trucking business, and the note claimed this account receivable had been  
24 pledged as collateral for the note. However, GB&L went out of business in or about  
25 2005. Polhill did not inform the investor until mid-2008 that GB&L had gone out of  
26 business.

27 45. As another example, an investor held an APFC note with an initial term  
28 of June 1997 to June 2001, which was later extended through 2008. His note

1 specifically stated that the note was secured by property located in Hesperia,  
2 California, and the note claimed this property had been pledged as collateral for the  
3 note. However, APFC sold the collateral in 2004. Neither Polhill nor APFC ever  
4 informed the investor that his collateral had been sold or that there was no longer any  
5 asset securing his note.

6 46. Each of the misrepresentations and omissions alleged above involved  
7 material information. Investors would have considered it important to their  
8 investment decision to know (i) that their purportedly “secured” promissory notes  
9 were not actually secured; (ii) that their pledged collateral was often inadequate; and  
10 (iii) that Polhill did not abide by the terms of the notes and notify investors when their  
11 pledged collateral was in default.

12 47. Moreover, Polhill knew, or was reckless or negligent in not knowing,  
13 that each of the misrepresentations and omissions alleged above was false and  
14 misleading.

15 **C. Polhill’s Unregistered Offering of Securities**

16 48. In addition to committing fraud, Polhill violated the securities  
17 registration laws. As alleged above, Polhill offered investors the opportunity to  
18 invest in both promissory notes and APFC Funds.

19 49. Three separate Funds existed at the time APFC filed for bankruptcy.  
20 The table below shows the name of each Fund and the terms of the offerings.  
21 American Pacific Advisors, a wholly-owned subsidiary of APFC, acted as the general  
22 partner for each Fund.

23

Name of Fund	Offering Period	Funds Raised Since 2005
American Pacific Financial Group, LP	1989-2007	about \$6 million
American Pacific Financial Group II, LP	1993-2007	about \$5 million

24  
25  
26  
27  
28

Name of Fund	Offering Period	Funds Raised Since 2005
American Pacific Venture Fund, LP	1989-2007	about \$3 million

50. APFC and Polhill controlled the Funds by using the same wholly-owned subsidiary of APFC as a general partner for each Fund. In addition, APFC and Polhill disregarded entity form by, for example, making payments to Fund investors out of APFC's common checking account. Further, the Funds were all engaged in the same type of business—loaning money to APFC. Investor money was also comingled in APFC's corporate account.

51. In addition, the offer and sale of Fund units were part of a single plan of financing—to make loans to APFC or its affiliates. The Funds also involved the same class of security (limited partnership units), they were made at or about the same time (from the late 1980s/early 1990s through the late 2000s), the same type of consideration (cash, generally in the form of IRA funds) was used in all Fund investments, and the sales of all Fund units were made for the same general purpose (to make loans to APFC). Finally, there were no periods of six months or more during which no offers or sales of Fund units were made.

52. The Funds, like the promissory notes, provided investor capital to APFC. Investors invested in a Fund, which loaned money to APFC. In exchange, APFC made interest payments to the Funds, which distributed them out to investors.

53. Polhill pooled investor funds in APFC's main checking account, and used the money at his discretion to, for example, pay APFC expenses, or make interest payments to investors.

54. Investors purchased the promissory notes in order to earn profits in the form of interest. The notes bore significant risk because while APFC marketed the notes as having the risk-reducing feature of being secured by a specific piece of collateral, in fact, the notes were not secured and were often under-collateralized.

55. In selling the promissory notes and the Fund investments, Polhill and



1 light of the circumstances under which they were made, not misleading.

2 60. By engaging in the conduct described above, Polhill violated, and unless  
3 restrained and enjoined will continue to violate, Section 17(a) of the Securities Act,  
4 15 U.S.C. § 77q(a).

5 **SECOND CLAIM FOR RELIEF**

6 **Fraud in Connection with the Purchase or Sale of Securities**

7 (Violations of Section 10(b) of the Exchange Act and Rule 10b-5 Thereunder)

8 61. The SEC realleges and incorporates by reference paragraphs 1 through  
9 56 above.

10 62. Polhill made material misrepresentations and omissions to investors  
11 regarding the security of their promissory notes, the status of the collateral allegedly  
12 securing their promissory notes, and APFC's investor notification procedures in the  
13 event an investor's collateral went into default.

14 63. By engaging in the conduct described above, Polhill, directly or  
15 indirectly, in connection with the purchase or sale of a security, by the use of means  
16 or instrumentalities of interstate commerce, of the mails, or of the facilities of a  
17 national securities exchange, with scienter, made untrue statements of a material fact  
18 or omitted to state a material fact necessary in order to make the statements made, in  
19 light of the circumstances under which they were made, not misleading.

20 64. By engaging in the conduct described above, Polhill violated, and unless  
21 restrained and enjoined will continue to violate, Section 10(b) of the Exchange Act,  
22 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5.

23 **THIRD CLAIM FOR RELIEF**

24 **Unregistered Offer and Sale of Securities**

25 (Violations of Sections 5(a) and 5(c) of the Securities Act)

26 65. The SEC realleges and incorporates by reference paragraphs 1 through  
27 56 above.

28 66. By engaging in the conduct described above, Polhill, directly or

1 indirectly, made use of means or instruments of transportation or communication in  
2 interstate commerce or of the mails, to offer to sell or to sell securities, or to carry or  
3 cause such securities to be carried through the mails or in interstate commerce for the  
4 purpose of sale or for delivery after sale.

5 67. No registration statement has been filed with the SEC or has been in  
6 effect with respect to any of the offerings alleged herein.

7 68. By engaging in the conduct described above, Polhill violated, and unless  
8 restrained and enjoined will continue to violate, Sections 5(a) and 5(c) of the  
9 Securities Act, 15 U.S.C. §§ 77e(a) and 77e(c).

10 **PRAYER FOR RELIEF**

11 WHEREFORE, the SEC respectfully requests that the Court:

12 **I.**

13 Issue findings of fact and conclusions of law that Polhill committed the alleged  
14 violations.

15 **II.**

16 Issue a permanent injunction restraining and enjoining Polhill and his  
17 officers, agents, servants, employees, attorneys, and all persons in active concert of  
18 participation with them, and each of them, from violating Sections 5(a), 5(c), and  
19 17(a) of the Securities Act, 15 U.S.C. §§ 77e(a), 77e(c), and 77q(a), and Section  
20 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R.  
21 § 240.10b-5.

22 **III.**

23 Issue an Order directing Polhill to disgorge all ill-gotten gains from his illegal  
24 conduct, together with prejudgment interest thereon.

25 **IV.**

26 Issue an Order directing Polhill to pay a civil penalty under Section 20(d) of  
27 the Securities Act, 15 U.S.C. § 77t(d), and Section 21(d)(3) of the Exchange Act, 15  
28 U.S.C. § 78u(d)(3).

V.

Issue an Order pursuant to Section 20(e) of the Securities Act and Section 21(d)(2) of the Exchange Act, 15 U.S.C. § 77t(e) and 15 U.S.C. § 78u(d)(2), barring Polhill from acting as an officer or director of any issuer that has a class of securities registered pursuant to Section 12 of the Exchange Act or that is required to file reports pursuant to Section 15(d) of the Exchange Act.

VI.

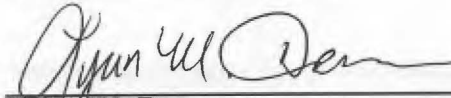
Retain jurisdiction of this action in accordance with the principles of equity and the Federal Rules of Civil Procedure in order to implement and carry out the terms of all orders and decrees that may be entered, or to entertain any suitable application or motion for additional relief within the jurisdiction of this Court.

VII.

Grant such other and further relief as this Court may determine to be just and necessary.

Dated: September 24, 2013

Respectfully submitted,



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John W. Berry  
Lynn M. Dean  
Sara D. Kalin  
Attorney for Plaintiff  
Securities and Exchange Commission

CONTRACTUAL LOAN AGREEMENT/PROMISSORY NOTE

Secured by Pledge of Collateral

May 18, 2006
San Bernardino, California

In consideration of \$ 60,000.00, received this date, AMERICAN PACIFIC FINANCIAL CORPORATION ("Obligor"), a California corporation, promises to pay to: Veronica I. Ibarra a single woman ("Beneficiary"), resident(s) of the state of California, the principal sum of Sixty Thousand and 00/100 Dollars, for the contract period beginning May 18, 2006 with interest from May 18, 2006 at eight per cent (8%) per annum, interest (chosed a or b), x (a) shall accrue and be payable with principal upon maturity as defined in the following paragraph, or (b) be payable in the amount of \$N/A on the N/A day of each (month/quarter) during the contract. Said payments shall be payable to Lender or Designee at the following address:

Veronica I. Ibarra (SSN [redacted] 3391)
[redacted]
Rialto, CA [redacted]

COPY

The initial expiration of this Agreement shall be on May 18, 2007 at which time the entire unpaid balance of principal plus all accrued interest shall either, at Beneficiary's option, be due and payable in full in legal tender of the United States of America, or extended according to the provisions of the following paragraph.

EXTENSION/RENEWAL PROVISION: Beneficiary or Designee shall be notified in writing of the pending expiration date and of the interest rate AMERICAN PACIFIC FINANCIAL CORPORATION will pay upon extension of this agreement. Beneficiary or Designee shall within ten (10) days of the expiration date of this agreement or any previous extension thereof, notify AMERICAN PACIFIC FINANCIAL CORPORATION in writing of Beneficiary's intention to receive payment in accordance with its provisions. It is agreed, that if AMERICAN PACIFIC FINANCIAL CORPORATION does not receive said notice, it shall then automatically extend this agreement for a period of time equal to the last term. Said extended term shall bear interest on all unpaid principal and interest as per the provisions, terms and conditions of said notice.

It is agreed that AMERICAN PACIFIC FINANCIAL CORPORATION reserves the privilege to make principal payments in any amount, at any time without penalty with a pro-rata reduction of monthly payments.

At all times during the course of this Agreement, the security will be maintained by one or more of the following:

- TYPE OF SECURITY:
(1) United States Currency
(2) Funds held in trust in Banks, Thrift and Loan Associations or Savings and Loan Associations
(3) Raw or product inventory
(4) Accounts receivable
(5) Equipment
(6) Pledged notes and Deeds of Trust as defined in item #8
(7) Pledged Real Property equity as defined in item #8
(8) Pledged collateral is defined as: Accounts Receivable, Cafe Valley Inc.

Whenever pledged collateral becomes in default, or whenever requested by AMERICAN PACIFIC FINANCIAL CORPORATION, Beneficiary agrees to release said pledged collateral to AMERICAN PACIFIC FINANCIAL CORPORATION and upon such release, Beneficiary shall select any one of these three options:

- (1) Receiving a principal reduction in this loan (in an amount equal to that pledged as security by the released collateral), or
(2) Accepting substitute security, or
(3) Directing that funds be held in trust, pending approval of replacement security by beneficiary.

AMERICAN PACIFIC FINANCIAL CORPORATION is hereby authorized and instructed to service all pledged collateral including the filing of all required notices and taking any prudent action necessary to preserve the equity of said collateral.

Unless otherwise agreed by the parties, all notes, Deeds of Trust and any pledged collateral, as referred to under item #8 above, is to be held in safekeeping by AMERICAN PACIFIC FINANCIAL CORPORATION and available for inspection to Beneficiary upon request.

The undersigned Beneficiary acknowledges receipt of this Promissory Note.

ACCEPTED AND APPROVED BY:

BENEFICIARY: [Signature]
Veronica I. Ibarra

AMERICAN PACIFIC FINANCIAL CORPORATION
BY: [Signature]
Larry R. Pechill, President



DO NOT DESTROY THIS NOTE
When paid, this note must be surrendered



## SECURITIES INFORMATION

THE INTERESTS OFFERED HEREBY HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR THE SECURITIES LAWS OF CERTAIN STATES AND ARE BEING OFFERED AND SOLD IN RELIANCE UPON EXEMPTIONS FROM THE REGISTRATION REQUIREMENTS OF SAID ACT AND SUCH LAWS. THE INTERESTS HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION, ANY STATE SECURITIES COMMISSION OR OTHER REGULATORY AUTHORITY, NOR HAVE ANY OF THE FOREGOING AUTHORITIES PASSED UPON OR ENDORSED THE MERITS OF THIS OFFERING OR THE ACCURACY OR ADEQUACY OF THE OFFERING MEMORANDUM. ANY REPRESENTATION TO THE CONTRARY IS UNLAWFUL.

THE OFFERING OF THESE SECURITIES HAS NOT BEEN REGISTERED WITH THE SECURITIES AND EXCHANGE COMMISSION ("SEC") UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "ACT"), AND IS MADE PURSUANT TO CERTAIN EXEMPTIONS THEREUNDER AS A TRANSACTION BY AN ISSUER NOT INVOLVING ANY PUBLIC OFFERING. FURTHER THIS PRIVATE PLACEMENT MEMORANDUM, EXCEPT AS MAY BE INDICATED IN A SUPPLEMENT HERETO, HAS NOT BEEN SUBMITTED TO OR REVIEWED BY ANY STATE SECURITIES COMMISSION. AS A CONSEQUENCE, SUCH SECURITIES WILL BE REQUIRED TO BE HELD INDEFINITELY UNLESS THEY ARE SUBSEQUENTLY REGISTERED UNDER THE ACT OR AN EXEMPTION FROM SUCH REGISTRATION IS AVAILABLE. THERE IS NO PUBLIC MARKET FOR THE SECURITIES AND NONE IS LIKELY TO DEVELOP. THE PARTNERSHIP IS UNDER NO OBLIGATION TO REGISTER THE SECURITIES UNDER THE ACT OR TO COMPLY WITH REGULATION A OR ANY OTHER EXEMPTION UNDER THE ACT.

THE COMMISSIONER OF CORPORATIONS OF THE STATE OF NEVEDA, or ANY OTHER STATE OR JURISDICTION DOES NOT RECOMMEND OR ENDORSE THE PURCHASE OF THE SECURITIES.

THE Limited Liability Company or COMPANY UNDERTAKES (1) TO MAKE AVAILABLE TO EVERY INVESTOR AND HIS/HER REPRESENTATIVES, DURING THE COURSE OF THIS TRANSACTION AND PRIOR TO SALE, ANY INFORMATION REQUESTED BY HIM/HER REGARDING THE CORPORATION, AND (2) THE OPPORTUNITY TO ASK QUESTIONS AND RECEIVE ANSWERS FROM THE CORPORATION OR ANY PERSON ACTING ON ITS BEHALF CONCERNING ALL TERMS AND CONDITIONS OF THIS OFFERING, AND TO OBTAIN ANY ADDITIONAL INFORMATION NECESSARY TO VERIFY THE ACCURACY OF INFORMATION MADE AVAILABLE TO SUCH OFFEREE.

THIS SECURITY IS TRANSFERRABLE ONLY UNDER LIMITED CIRCUMSTANCES. THE TRANSFERRABILITY WILL BE PROHIBITED FOR ALL PRACTICAL PURPOSES. IT IS NOT ANTICIPATED THAT THERE WILL BE ANY FUTURE REGISTRATION OF THESE INTERESTS. INVESTORS MUST, THEREFORE BE AWARE THAT THERE IS NOT A PUBLIC MARKET FOR THE RESALE OF INTERESTS. INVESTORS BY SIGNING ON THE OPPOSITE PAGE OF THIS DOCUMENT HEREBY REPRESENT THAT THEY ARE SOPHISTICATED AND ARE DEEMED TO BE ACCREDITED INVESTORS AS DEFINED IN THE APPLICABLE CODE.