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Pro Per

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IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

CLERK
BANKRUPTCY
DISTRICT OF ARIZONA

In re:

MORTGAGES LTD.,

an Arizona corporation,

Debtor.

) In Proceedings Under Chapter 11
) Case No. 2:08-bk-07465-RJH
) **ROBERT FURST'S OBJECTIONS TO**
) **MORTGAGES LTD.'S DISCLOSURE**
) **STATEMENT IN SUPPORT OF ITS**
) **CHAPTER 11 PLAN OF**
) **REORGANIZATION**

Robert G. Furst hereby submits his Objections to Mortgages Ltd.'s Disclosure Statement in Support of its Chapter 11 Plan of Reorganization (the "Debtor's Disclosure Statement"). Mr. Furst is an Investor of the Debtor.

The fundamental underpinning of the Debtor's Plan of Reorganization is that the Debtor, as servicing agent, is somehow entitled to **\$213 million in Interest Rate Spread, Default Interest Spread and Late Charges** from its Investors for services rendered (and not rendered) since the inception of these Chapter 11 bankruptcy proceedings. Debtor's assertion, at the eleventh hour¹, that its Investors owe \$213 million to the Debtor is not only a complete fabrication, but more importantly, it also reveals the Debtor's blatant fiduciary disloyalty to its Investors and the total breakdown of its

¹ Notably, none of the Debtor's prior filings with the Bankruptcy Court listed or mentioned a receivable from the Investors for Interest Rate Spread, Default Interest Spread or Late Charges.

1 legal, ethical and moral "compass" (thereby necessarily disqualifying the Debtor from any further
2 service as a fiduciary to the Investors). Entangled in a clear conflict of interest between the Investors
3 economic survival and its own, the Debtor unforgivably and impermissibly chooses the latter.
4

5 The Debtor's position is fatally flawed because (1) the operative documents irrefutably
6 establish, as a matter of law, that the Debtor is only entitled to receive Interest Rate Spread, Default
7 Interest Spread and Late Charges out of the Borrowers' payments to the Investors, if and when they
8 are received, and (2) the Debtor's 45-year operating history clearly reveals, as a matter of fact, that
9 the Investors never made, and were never asked to make, any payments to the Debtor for Interest
10 Rate Spread, Default Interest Spread and Late Charges which were not paid by defaulting Borrowers.
11 Most importantly, Debtor's position defies common sense because it is based upon the ridiculous
12 notion that the Investors are the "personal guarantors" of the Borrowers' loan payments for the
13 benefit of the Debtor.
14

15 In summary, the Debtor, armed with nothing more than a bogus fee claim against the
16 Investors, does not have the requisite assets necessary to finance its emergence from bankruptcy, and,
17 as a consequence, the Debtor's Plan of Reorganization must necessarily fail. At this late stage of
18 these Chapter 11 bankruptcy proceedings (and after months of unnecessary delay and expense
19 fighting over plan exclusivity issues), it is outrageous and disgraceful that the Debtor has nothing
20 more to offer, as a Plan of Reorganization, than a "Hail Mary" attempt to finance its business future
21 at the Investors' expense.
22

23
24 **I. Overview: The Agreement of the Parties**

25 The business model of the Debtor was simply to obtain funds from Investors and lend those
26 funds to Borrowers. The Debtor made its profit by collecting Origination Points directly from the
27 Borrowers, and by collecting an Interest Rate Spread, Default Interest Spread (if applicable) and Late
28

1 Charges (if applicable) out of the Borrowers' payments to the Investors. The Debtor, in its
2 Disclosure Statement, admits this much, by stating that "[t]he Debtor made its profit mainly from
3 loan origination fees and by retaining the difference between the interest received from the borrowers
4 and the interest paid to the Investors, the "interest rate spread."² (Emphasis added.)
5

6 Most importantly, the express agreement between the Debtor and the Investors, as evidenced
7 by the operative documents and the Debtor's 45-year business practice, has always been the
8 following:

- 9 1. If a Borrower performed its payment obligations, the Debtor, as servicing agent,
10 would (a) collect the payments received from the Borrower, (b) pay the Investors
11 their appropriate interest rate, and (c) retain the balance of the Borrower's payment
12 as the Interest Rate Spread.
13
- 14 2. If a Borrower defaulted on its payment obligations but later cured its default, the
15 Debtor would (a) collect the payments received from the Borrower, (b) pay the
16 Investors their appropriate interest rate, and (c) retain the balance of the
17 Borrower's payment as Interest Rate Spread, Default Interest Spread and Late
18 Charges, as the case may be.
19
- 20 3. If a Borrower defaulted on its payment obligations and never cured its default, the
21 Debtor would do one of the following:
 - 22 a. The Debtor might elect to foreclose the Loan and schedule a foreclosure sale of
23 the underlying property.
 - 24 i. If, at the foreclosure sale, the property sold for more than the principal
25 balance of the Loan, plus the accrued interest owed to the Investors, the
26 Debtor would retain the excess sales proceeds as Interest Rate Spread,
27
28

² Debtor's Disclosure Statement, Section 5.4 (page 14).

1 Default Interest Spread and Late Charges. However, if the property
2 sold for a purchase price equal to or less than the principal balance of
3 the Loan, plus accrued interest owed to the Investors, the Investors
4 would receive 100% of the sale proceeds, and the Debtor would not
5 receive any Interest Rate Spread, Default Interest Spread and Late
6 Charges.
7

8 ii. If, on the other hand, the Investors acquired the property through the
9 foreclosure sale, they would continue to hold the property for ultimate
10 sale at a later date. In this case, the Debtor would not receive any
11 Interest Rate Spread, Default Interest Spread and Late Charges, either
12 at the time of the foreclosure sale or at the later sale of the property.
13

14 b. Alternatively, the Debtor might elect to sell the defaulted Loan to a
15 Performance Plus Investor, who acquired the Loan with full knowledge that it
16 was non-performing. In this case, the Performance Plus Investor would pay
17 the original Investors 100% of the unpaid principal balance, plus all accrued
18 interest owing to them. The Debtor would not receive any Interest Rate
19 Spread, Default Interest Spread and Late Charges from the original Investors.
20

21 In sum, in accordance with the operative agreements and the Debtor's 45-year operating
22 history, the Debtor is not, and has never been, entitled to receive any Interest Rate Spread, Default
23 Interest Spread and/or Late Charges from the Investors.
24

25 **II. Debtor's Plan of Reorganization**

26 The Debtor's Plan of Reorganization is predicated upon the false premise that, in the event
27 that a Borrower defaults on its payment obligations to the Investors, the Debtor is entitled to collect
28

1 from the Investors the unpaid Interest Rate Spread, Default Interest Spread and Late Fees owed by
2 the defaulted Borrower. The Debtor, in its Disclosure Statement, falsely claims that it has always had
3 this right to collect these amounts from the Investors and that it has, in fact, actually collected them
4 from the Investors in the past. Not surprisingly, the Debtor does not cite even a single instance in
5 which the Investors paid these amounts to the Debtor, because the Investors never did so.
6

7 The Debtor shamelessly claims that, by May 31, 2009, the Interest Rate Spread, Default
8 Interest Spread and Late Charges "will have accrued to over \$213 million which would normally be
9 assessed to the Loans and paid to the Company."³ The Debtor offers mock comfort to the Investors
10 by stating that, "[t]o ameliorate this rather unanticipated result," the Debtor is willing to "relinquish"
11 75% of these fabricated amounts.
12

13 The Debtor's Plan of Reorganization disregards the glaring truth that the Debtor has
14 accomplished virtually nothing for the Investors during the nine-month period for which it claims
15 entitlement to \$213 million in compensation. During this period, the Debtor laid off approximately
16 80% of its employee staff; it completed virtually no loan foreclosures; it initiated virtually no lawsuits
17 seeking to enforce personal guarantees; and it modified only a single loan which is generating any
18 monthly interest income for the Investors.⁴
19

20 Tellingly, George Everette and Christopher Olson, the two members of the Debtor's Board of
21 Directors at the time that the Debtor's Plan of Reorganization was drafted, refused to "sign off" on
22

23 ³ Debtor's Disclosure Statement, Section 8.1.5 (pages 44-45).

24 ⁴ It should be noted that the Debtor has recently commenced a last-minute attempt to clean up its
25 tarnished image. The Debtor has engaged in a flurry of recent activity which should have begun nine
26 months ago, so that it can now claim that it has at least "initiated" some enforcement action in
27 relation to some of the defaulted loans. Unfortunately, for the Investors, the only relevant
28 "scorecard" for the Debtor's performance is their monthly interest check from the Debtor, and for the
current month, Investors with \$500,000 investments mortgage pools received checks for less than one
dollar!

1 the Debtor's Plan of Reorganization and were asked to resign the day before the Plan was submitted
2 to the Court. Even Peter Dunn, one of the new Board members, also claims he did not "sign off" on
3 the Plan. The unanswered question remains: Who, if anyone, will admit that they "signed off" on the
4 Debtor's Plan?
5

6 **III. Evidence Contradicting the Debtor's Claim**

7 There is a mountain of evidence clearly contradicting the Debtor's claim that it is entitled to
8 collect from the Investors all unpaid Interest Rate Spread, Default Interest Spread and Late Charges
9 owed by the defaulting Borrowers. Moreover, there is absolutely no evidence supporting the
10 Debtor's position.
11

12 **A. The Debtor's Promotional Materials and Representations to Its Investors**

13 For more than 45 years, the Debtor repeatedly promised its Investors that (1) they would not
14 be charged any fees (other than out-of-pocket expenses) in relation to their mortgage investments,
15 and (2) all of the Debtor's compensation would be paid only from the payments received by the
16 Borrowers.
17

18 To illustrate this point, in the Debtor's Quarterly Newsletter for the Winter of 2006, Scott
19 Coles, the Chief Executive Officer, expressly stated that "[l]iquidity, diversification and double digit
20 returns in conjunction with no fees is our benchmark commitment to our investors." (Emphasis
21 added.) This statement obviously "flies in the face" of the Debtor's claims that it is entitled to \$213
22 million in compensation from its Investors for services rendered during these nine months of Chapter
23 11 bankruptcy proceedings.
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1 **B. The Private Offering Memorandum**

2 In addition, the Private Offering Memorandum for Pass-Through Loan Participations, dated
3 February 11, 2008, consistently states that all compensation received by the Debtor, as servicing
4 agent, would be paid out of, and deducted from, the Borrowers' payments to the Investors.
5

6 **1. "Compensation to the Company and its Affiliates" Section**

7 In the section entitled "Compensation to the Company and its Affiliates," there is not a
8 single reference that "the Investors will pay to the Debtor" any type of compensation.
9 Instead, the POM repeatedly states that the Debtor "will receive" or "will entitled to"
10 various types of compensation, with the understanding that the amounts will be paid,
11 in all cases, from the payments received from the Borrowers. To illustrate:
12

13 **a. Interest Rate Spread:** On page 24, the POM states that the Debtor "will
14 receive" the Interest Rate Spread from the "interest payments on each Loan."

15 Implicit in this statement is that, if the Borrower does not make its payment to
16 the Investors, then the Debtor will not receive the Interest Rate Spread.
17

18 **b. Default Interest Spread:** On page 25 (second paragraph), the POM states that
19 the Debtor "will receive" the Default Interest Spread from "any additional
20 interest payments . . . provided for in a Loan." Once again, it is implicit that, if
21 the Borrower does not make the "additional interest payments," then the
22 Debtor will not receive the Default Interest Spread.
23

24 **c. Late Charges:** On page 25 (third paragraph), the POM states that the Debtor
25 "will be entitled to retain all late charges in the event of a default by the
26 Borrower." The POM further states that the late charges "are paid by the
27 Borrower, although such amounts will be deducted from the payments received
28

1 from the Borrower on a Loan. (Emphasis added.) In this case, the POM
2 expressly provides that the Late Charges are "paid by the Borrower," not the
3 Investors.
4

5 **2. "Summary" Section**

6 There are no statements contained in the "Summary" section of the POM which
7 support Debtor's unsupportable position. Notably, the subsection entitled "Resale of
8 Defaulted Loans" clearly contradicts Debtor's position.
9

10 **a. "Resale of Defaulted Loans":** In the subsection entitled "Resale of
11 Defaulted Loans," the POM states in relevant part:

12 "The Company typically sells for its unpaid principal amount any Loan
13 that is in default in the payment of principal or interest. . . While such
14 sales are intended to protect the Participation holders' capital, there is
15 no assurance that any sale of a defaulted Loan can be made at a price
16 equal to the unpaid principal amount." (Emphasis added.)
17

18 This language makes sense only if the Investors are not obligated to pay the
19 Debtor for all unpaid Interest Rate Spread, Default Interest Spread and Late
20 Charges owed by the defaulted Borrowers, for the following reason: If
21 the Investors are, in fact, obligated to pay these unpaid fees (which will
22 usually exceed 30% of the principal balance of an unpaid loan) to the
23 Debtor, then the Debtor would have to sell the defaulted Loans for
24 substantially more than the "unpaid principal amount" (i.e., 130% of the
25 unpaid principal amount or more) in order to protect the Investors' capital
26 investment.
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b. **“Compensation to the Company”**: The subsection entitled “Compensation of the Company” also provides no support for the Debtor’s assertion that it is entitled to receive the Interest Rate Spread, Default Interest Spread and Late Charges from the Investors in the event that the Borrowers default on the Loans. Instead, the POM merely states that the Debtor “will receive certain compensation.” When read in conjunction with pages 24-25 of the POM (see Section A above), it is clear that the Debtor is only entitled to compensation from the payments made by the Borrowers, and not from the Investors.

3. **“Risk Factors” Section**

The “Risk Factors” section of the Private Offering Memorandum also confirms that the Debtor is not entitled to receive the unpaid Interest Rate Spread, Default Interest Rate and Late Charges from the Investors. For example, the subsection entitled “There will be limited remedies upon default of a Borrower” states in relevant part on page 21:

“The lender will have the right to bid on and purchase the property underlying a Loan at a foreclosure or trustee’s sale following a default by the Borrower. If the lender is the successful bidder and purchases the property underlying a Loan, the lender’s return on such Loan will depend upon the amount of cash or other funds that can be realized by refinancing, selling or otherwise disposing of the property. . . . Conditions in real estate loan markets may affect the availability and cost of real estate loans Such conditions may adversely affect the ability to sell the property securing a Loan in the event that it is in the best interests to foreclose upon and purchase the property. To the extent

1 that the funds generated by such actions are less than the amounts advanced by
2 the lender for such Loan, the lender may realize a loss of all or part of the
3 principal and interest on the loan. There can be no assurance that the
4 Participation holders will not experience financial loss upon a default by a
5 Borrower. (Emphasis added.)
6

7 With regard to the underlined language, if the Investors were indeed obligated to pay any
8 fees to the Debtor, then the Investors would have to sell the foreclosed property for
9 substantially more than “the amounts advanced by the lender” in order to avoid realizing a
10 “loss of all or part of the principal and interest on the loan.” The clear implication is that
11 the Investors are not obligated to pay any fees to the Debtor.
12

13 **C. The Agency Agreement**

14 The Agency Agreement also clearly establishes that all compensation received by the Debtor
15 is paid out of the payments made by the Borrowers to the Investors. Paragraph 1(c) of the Agency
16 Agreement, entitled “Compensation,” provides that the Debtor may receive the Interest Rate Spread,
17 Default Interest Spread and Late Charges from the Borrowers’ payments, as follows:
18

- 19 (1) Retain fees and charges assessed under the Loan Documents and collected by
20 Agent, including . . . late charges.
- 21 (2) Deduct from payments received by Participant a portion of the interest payments
22 on any Loan in which Participant acquires an interest.
- 23 (3) Collect and retain any interest on the principal balance of any Loan which is over
24 and above the normal rate set forth in the applicable promissory note, including the
25 default interest rate. (Emphasis added.)
26
27
28

1 In each case, in order for the Debtor to receive any compensation, the Borrower must make its
2 payments to the Investors, at which time the Debtor, as servicing agent, may "collect" and "retain"
3 (or "deduct") the Interest Rate Spread, Default Interest Spread and Late Charges.
4

5 **D. Audited 2005 Financial Statements of the Debtor**

6 Footnote 1 to the Debtor's audited financial statements for the fiscal year ending October 31,
7 2005, also contradicts the Debtor's position by revealing that all servicing fees collected by Debtor
8 during that year were received from the Borrowers' payments to the Investors. Specifically, footnote
9 1 states that the "[s]ervicing fees are recognized at the time remittances are received for principal and
10 interest on mortgage loans owned by others."
11

12 Not surprisingly, there is no mention in footnote 1 that any servicing fees were paid by the
13 Investors out of their own pockets.

14 **E. Audited 2006 Financial Statements of the Debtor**

15 Footnote 4 to the Debtor's audited financial statements for the fiscal year ending December
16 31, 2006, also contradicts the Debtor's position, as follows:
17

- 18 1. Footnote 5 references an asset of the Debtor known as the River Run Golf Course. At
19 one time, the River Run Golf Course was the collateral for a defaulted Loan owned by
20 certain Investors.
- 21 2. Footnote 4 reveals that the Debtor acquired a portion of the River Run Golf Course
22 from its Investors (out of a mortgage pool) at a purchase price equal to the Investors'
23 "cost basis" (i.e., the unpaid principal balance of the Loan).
24
- 25 3. The fact that the Debtor bought the Investors' interest in the property for its cost basis
26 contradicts Debtor's position that the Investors were obligated to pay to the Debtor the
27 unpaid Interest Rate Spread, Default Interest and Late Charges owed by the Borrower.
28

1 That is, if the Investors truly owed these amounts to the Debtor, then the Debtor would
2 have deducted these amounts from the "cost basis" payment it made to the Investors.
3

4 **F. Audited 2007 Financial Statements of the Debtor**

5 Footnote 2 to the Debtor's 2007 audited financial statements also indicates that the Debtor
6 looked solely to the Borrowers as the source of its servicing income. Footnote 2 states that the value
7 of the Debtor's 2007 servicing rights was reduced by an allowance for uncollectible servicing
8 income. Logically, the Debtor's servicing income could only be considered to be uncollectible if the
9 source of the payment is the defaulting Borrowers; if, on the other hand, the Debtor truly believed
10 that it had the right to collect the servicing income directly from the Investors, none of the servicing
11 income would ever be considered to be uncollectible because the Debtor has ongoing custody of the
12 Investors' mortgages assets as an ultimate source of payment.
13

14 **IV. Objections to the Debtor's Plan of Reorganization**

15 Based upon the uncontroverted facts set forth in Section III above, Robert Furst has the
16 following objections to the Debtor's Disclosure Statement:
17

18 **A. Section 5.4 should be modified in the following respects:**

- 19 1. The second sentence of the first paragraph states that "[t]he Debtor made its
20 profit mainly from loan origination fees and by retaining the difference
21 between the interest received from the borrowers and the interest paid to the
22 Investors, the "interest rate spread" or ML Spread." (Emphasis added.) This
23 sentence is a surprising admission by the Debtor and confirms the 45-year
24 mutual understanding of the Debtor and its Investors that the Interest Rate
25 Spread was paid to the Debtor only if and when it was received from the
26 Borrowers.
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2. However, the third sentence of the first paragraph is ambiguous and should be clarified to avoid any future misunderstandings and to consistently reflect this 45-year mutual understanding of the Debtor and its Investors. The clarification should be made by adding the underlined language below (which was taken from the POM, page 25, third paragraph):

“The Debtor was also entitled to various fees and charges in conjunction with the loans made to Borrowers; these fees have always been paid by the Borrowers by deducting the amounts from the payments received from the Borrowers on the Loans.”

B. Section 5.4(1), entitled “The Private Offering Memorandum,” should be modified in the following respects:

1. The Debtor should be required to expressly disclose that, in the entire POM, there is not a single supporting statement for its position that the Investors are obligated to pay the Debtor, as servicing agent, for all unpaid Interest Rate Spread, Default Interest Spread and Late Charges. This disclosure should be in bold type with all capitalized letters.

2. The Debtor cites two sentences in the POM which state that Debtor will receive certain compensation “regardless of the returns to the Participation holders” (POM, page 8) and “regardless of the profitability of or cash distributions to Participation holders.” (POM, page 28)

a. These two citations provide no legal support for Debtor’s current position that the Investors are now somehow responsible for unpaid and unearned Interest Rate Spread, Default Interest Spread and Late

1 Charges owed by the Borrowers. Rather, these citations merely state
2 that Debtor may receive compensation (e.g., loan origination fees) from
3 a Borrower in relation to a Loan which subsequently proves to be
4 unprofitable for the Investors.
5

6 b. Because the two citations do not provide any legal (or logical) authority
7 for Debtor's position, they should be deleted as potentially misleading
8 to the Investors. (Alternatively, if the Debtor is permitted to reference
9 these two citations, then the Debtor should be required to add clarifying
10 language (which is consistent with the POM, page 25, third paragraph)
11 that all of the Debtor's compensation has always been, and will always
12 be, paid out of the Borrowers' payments to the Investors.
13

14 3. The Debtor cites the POM, page 40, which states that, if the Debtor resigns
15 as the servicing agent, "the Company is entitled to receive the collection
16 fee pursuant to the terms of the Loan and/or the Interest Rate Spread based
17 on the remaining term of the loan over the life of the Loan."
18

19 a. This statement does not support the Debtor's position at all. It
20 merely means that, if the Debtor resigns as servicing agent, the
21 Debtor is entitled to receive the collection fees and the Interest Rate
22 Spread over the life of the loan, if and when the Borrower makes
23 the payments.
24

25 b. It does not mean, as the Debtor seems to imply, that the Investors
26 are now responsible for paying the Interest Rate Spread.
27
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1 c. Because the Debtor is mischaracterizing this citation, the citation
2 should be deleted. The citation is an obvious effort by the Debtor
3 to trick the Investors who are reading the Disclosure Statement into
4 believing that they previously assumed the obligation to pay all
5 unpaid Interest Rate Spread, when, in fact, they did not do so.
6

7 C. Section 5.4(2), entitled "The Agency Agreement," should be modified in the following
8 respects:
9

10 1. The Debtor correctly cites Section 1(c) of the Agency Agreement as stating
11 that the Debtor may (1) retain late charges collected by the Debtor (Section
12 1(c)(1)), (2) deduct the interest rate spread from payments received by the
13 Investor (Section 1(c)(2)), and (3) collect and retain the default interest rate
14 (Section 1(c)(3)).

15 2. However, the Debtor misleadingly states that its entitlement to the Interest
16 Rate Spread, Default Interest Spread and Late Charges is "clearly
17 manifested in the operative documents."
18

19 a. This statement is misleading because it incorrectly suggests that the
20 Debtor is entitled to receive these fees from the Investors, not the
21 Borrowers.
22

23 b. Clarifying language must be inserted expressly disclosing to the
24 Investors that the Debtor is entitled to these fees only out of the
25 payments received from the Borrowers.
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3. The Debtor states that “in the interest of providing a greater return to the Investors, the Debtor has agreed to relinquish a significant portion of the Spread and Fee Income.”

a. This statement is totally untrue and is intended to deceive the Investors into believing that (i) the Investors legitimately owe the Debtor \$213 million, and (ii) the Investors should be grateful that the Debtor only intends to collect approximately \$50+ million from them.

b. The Debtor should be required to delete this false and misleading statement.

4. The Debtor should be required to disclose that Christopher Olson and George Everette resigned as members of the Debtor’s Board of Directors because they were unwilling to “sign off” on Debtor’s Plan of Reorganization because they did not believe that the Debtor was entitled to collect the unpaid Interest Rate Spread, Default Interest Spread and Late Charges from the Investors.

D. Section 8.1.4, entitled “Preservation and Enhancement of Investors’ Interests” should be modified in the following respects:

1. The Debtor should be required to restate the title because it suggests that the Debtor is acting in good faith to preserve and enhance their economic interests. In fact, in dereliction of its fiduciary duties to its Investors, the Debtor has created a fictional \$213 million fee obligation for the Investors in order to improperly resolve its own desperate financial situation. .

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2. The Debtor states the Debtor “will relinquish to Investors a substantial portion of the ML Fees to be charged to the Investors.” This statement should be deleted because (i) the Investors are not responsible for the unpaid Interest Rate Spread, Default Interest Spread and Late Charges, and therefore (ii) the Debtor is not relinquishing anything to which it is entitled.

3. The Debtor should be required to disclose in precise terms the nature of the Debtor’s compensation agreement for the past 45 years. Specifically, the Debtor should be required to insert the detailed summary of this compensation agreement, as set forth in Section I above.

4. The Debtor has an agreement with its 401(k) Plan that, with regard to the Loans owned partially by the Plan, the Debtor will pass on all of the servicing fees to the Plan. Therefore, if the Debtor is truly entitled to Interest Rate Spread, Default Interest Spread and Late Charges from the Investors, as it claims, then the Debtor must collect those fees and pay all of them to the Debtor’s 401(k) Plan, without any 75% relinquishment (because the Plan certainly would not waive fees to which it was entitled). The Disclosure Statement incorrectly states that the Investors will not be required to pay any fees for defaulted Loans owned partially by the 401(k) Plan.

E. Section 8.1.5, entitled “Relinquishment and Sharing of Spread and Fee Income” should be modified in the following respects:

1. The Debtor should be required to restate the title because it suggests that the Debtor is acting in good faith to preserve and enhance the Investors’

1 economic interests. In reality, the Debtor is shamelessly attempting to take
2 the Investors' assets for itself.

3
4 2. This entire section should be deleted as a total fabrication, for the
5 following reasons:

6 a. The Debtor incorrectly states that “[a]s per the Agency and
7 Operating Agreements, the Company has the right to and in the past
8 has collected from each Loan, a “spread” which was the difference
9 between the interest rates the Company charged its Borrowers and
10 the interest rate the company agreed to pay its Investors.”
11 (Emphasis added.)
12

13 1. This statement gives the false impression that the Investors
14 are responsible for, and have paid in the past, the Interest
15 Rate Spread, which they have not.
16

17 2. To accurately reflect the Debtor's rights and historical
18 practices, this sentence should read as follows (which is
19 consistent with Debtor's statement in Section 5.4):
20

21 “As per the Agency and Operating Agreements, the
22 Company has the right to and in the past has collected
23 from each interest payment, a “spread” which was the
24 difference between the interest rates the Company
25 received from its Borrowers and the interest rate the
26 company agreed to pay its Investors.”
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b. The Debtor incorrectly states that “the Company has the right to and in the past has retained various fees and charges due under the Borrower loan documents, i.e., origination fees, default interest, late fees, extension fees, etc.” (Emphasis added.)

1. This statement gives the false impression that the Investors are responsible for, and have paid in the past, these fees, which they have not.

2. To accurately reflect the Debtor’s rights and historical practices, this sentence should be clarified to read as follows (which is consistent with Debtor’s statement in Section 5.4):
“The Company has the right to and in the past has retained various fees and charges out of the payments made by the Borrowers under the Borrower loan documents, i.e., origination fees, default interest, late fees, extension fees, etc.”

c. The Debtor should be required to cite specific defaulted loans in which the Investors were required to pay to the Debtor the Interest Rate Spread, Default Interest Spread and Late Fees owed by the defaulting Borrowers. If the Debtor cannot cite specific examples, the Disclosure Statement should specifically say so in bold type and with all capitalized letters).

d. The Debtor states that, by May 31, 2009, “these so-called ML Spread and ML Fees will have accrued to over \$213 million which

1 would normally be assessed to the Loans and paid to the
2 Company.” This statement should be deleted because is totally
3 untrue, contrary to the POM and the Agency Agreement, and defies
4 common sense.
5

6 e. The Debtor states that “[t]he Company is relinquishing over \$166
7 million which would normally go to the Company and will now go
8 to the Investors.” This statement should be deleted because (i) the
9 Investors are not responsible for the unpaid Interest Rate Spread,
10 Default Interest Spread and Late Charges, and therefore (ii) the
11 Debtor is not relinquishing anything to which it is entitled.
12

13 E. With respect to certain investors, the Debtor does not have the right to modify
14 and/or extend the terms of Loans in which they are participating. Consequently,
15 the Debtor should be required to disclose how it will “cash out” those Investors
16 who did not authorize the Debtor to modify or extend Loans on their behalf.
17

18 F. The Debtor should be required to disclose which individuals approved the
19 Debtor’s Plan of Reorganization. Did Peter Dunn approve the Plan? Did Steve
20 Chanen? Did Richard Feldheim?
21

22 G. The Debtor should be required to disclose that Richard Feldheim, who was
23 previously removed as Chief Executive Officer at the request of the Debtor’s
24 previous Board of Directors and also the Official Investor Committee, has secretly
25 resumed involvement in the business affairs of the Debtor. There is a great deal of
26 animosity between the Investors and Richard Feldheim, and the Investors have the
27 right to know that Mr. Feldheim is still lurking in the background.
28

1 H. The Debtor should be required to disclose that Laura Martini has continued to
2 work for the Debtor as a consultant after she was removed from the Debtor's
3 Board of Directors.
4

5 I. The Debtor should be required to disclose that Christopher Olson, the Chief
6 Financial Officer of the Debtor for more than seven years, testified under oath on
7 March 25, 2009, that the hiring of Richard Feldheim, as President, and Carolyn
8 Johnsen, Esq., as legal counsel, were huge mistakes.
9

10 J. The Debtor should be required to disclose that, with respect to those Investors
11 which are qualified plans under ERISA, the alleged \$50+ million in compensation
12 "owed" by the Investors to the Debtor is "unreasonable compensation," thereby
13 constituting a "prohibited transaction" under ERISA. The Debtor should be
14 required to explain how it will pay the excise taxes resulting from these prohibited
15 transactions.
16

17 K. Section 8.1.5, entitled "Amendments to the Agency Agreements" should be
18 modified in the following respects to preserve the original intent of the parties:

19 a. Section 1(c) should be modified to state that the Debtor, as servicing agent,
20 is entitled to compensation only out of payments received from the
21 Borrowers.
22

23 b. Section 2 should be clarified to state that the Debtor, as servicing agent, is
24 a "fiduciary" of the Investors, and as such, must indemnify the Investors
25 from any loss or liability resulting from the Debtor's wrongful actions.
26

27 c. Consistent with the Debtor's 45-year operating history, a provision should
28 be added requiring the Debtor to consult with the Investors before

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modifying any loan. If the interests of the Investors are materially impacted (e.g., subordination, reduction of principal or interest payments, etc.), then a majority-in-interest of the Investors must concur before the modification can be consummated. (Alternatively, an investor board consisting of Elliott Pollack, Bruce Buckley and Scott Summers could act on behalf of the Investors.)

d. Section 3 should be modified to permit the Investors to remove the Debtor, as servicing agent, for "cause," by a vote of 75% of the Investors (determined by their participating interests). This power is already contained in the Operating Agreements for the mortgage pools, and a similar provision is needed in the Agency Agreement (especially if the Debtor is given expanded powers not previously contemplated by the Investors).

e. To avoid further disputes, clarifying language should be inserted that, with respect to those Investors who did not give the Debtor discretion to modify and/or extend Loans, they will be "cashed out" in the event the Debtor does, in fact, enter into modification and/or extension agreements.

L. Section 8.9, entitled "Administration of the ML Loans/Pre-Emergence and Post-Emergence Fees and Charges" should be modified in the following respects:

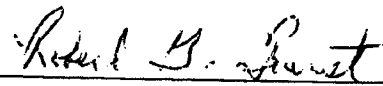
a. PLS and the ML Trust should not have a priority right to be paid the Pre-Emergence and Post-Emergence Fees and Service Charges from the proceeds from each ML Loan. The Debtor's well-established business practice was to make all payments to the Investors on a priority basis.

1 b. With regard to Investors in the Revolving Opportunity Loan Program and
2 Capital Opportunity Loan Program, PLS and the ML Trust are certainly not
3 entitled to a priority payment from the loan proceeds because the Debtor
4 expressly guaranteed all principal and interest payments to the Investors
5 under these two programs. Notably, the Revolving Opportunity Loan
6 Program Agreement expressly states that the Investors receive all of their
7 interest before any interest is paid to the Debtor at all.
8

9 **V. Conclusion**

10 Prior to addressing the contents of the Debtor's Disclosure Statement, the Court should first
11 rule on the predicate issue of whether the Debtor is entitled to receive the Interest Rate Spread,
12 Default Interest Spread and Late Charges from the Investors in the event that the Defaulting
13 Borrowers do not pay them. The operative documents and the 45-year history of the Debtor, together
14 with common sense and logic, clearly establish that Debtor is not entitled to recover these fees from
15 the Investors. Once the Court so concludes, the Debtor's Plan of Reorganization must necessarily fail
16 because the Debtor will have no assets with which to reorganize.
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19 DATED: March 30, 2009

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21 _____
22 Robert G. Furst
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