

1 Fennemore Craig, P.C.
Cathy L. Reece (No. 005932)
2 Keith L. Hendricks (No. 012750)
3003 North Central Avenue, Suite 2600
3 Phoenix, AZ 85012-2913
Telephone: (602) 916-5000
4 Email: creece@fclaw.com
Email: khendric@fclaw.com
5

6 Attorneys for Official Committee of Investors

7 IN THE UNITED STATES BANKRUPTCY COURT
8 FOR THE DISTRICT OF ARIZONA

9 In re
10 MORTGAGES LTD.,
11 Debtor.

Chapter 11
Case No. 2:08-bk-07465-RJH
OBJECTION TO UNIVERSITY & ASH
SETTLEMENTS BY INVESTORS
COMMITTEE
Date: November 10, 2008
Time: 1:00 p.m.

13 The Official Committee of Investors (“Investors Committee”) hereby files its
14 Objection to the University & Ash Settlements which is currently scheduled to be heard
15 November 10, 2008. On November 5, 2008 after 5 p.m., the Debtor filed a “Supplement”
16 to the Motion, but attached a brand new settlement agreement (“New Settlement
17 Agreement”) with a completely different structure and significantly different terms (“New
18 Settlement Motion”). The proposed amended notes and deeds of trust were not attached
19 and have not been provided. The New Settlement Motion was filed and served two
20 business days before the hearing. Upon information and belief, some of the investors may
21 have received an email on November 6, 2008 with the brand new settlement attached and
22 others have not seen it yet.

23 The Investors Committee objects to the New Settlement Motion for several
24 reasons. First, the New Settlement Motion has been significantly changed from the one
25 noticed to the investors. The investors must be given a reasonable time and opportunity to
26 understand and evaluate the New Settlement Motion. To further aggravate the situation,
27 the Investors Committee has received no documents from University & Ash despite its
28 repeated requests and its subpoena and was not allowed to depose their witness until

1 5 p.m. the business day before the hearing. As a result, the hearing must be continued.
2 Second, the New Settlement Motion has significant provisions that can only be instituted
3 under a plan of reorganization and will substantively predetermine the terms of the
4 treatment of the Borrowers and the investors in these loans. As such it is a *sub rosa* plan
5 and cannot be approved under a 9019 Motion. Its approval must await the plan
6 confirmation. Third, the business terms of the New Settlement Motion are not reasonable.
7 The terms swing too far in favor of the Borrowers, create unreasonable risk for the
8 investors, are illusory and minimize the chance of recovery. Fourth, the Debtor has no
9 authority to agree to such extreme modifications to the lender-borrower transactions.
10 Fifth, the Debtor has no interest in the two Roosevelt Gateway loans and only a negligible
11 interest in the University & Ash loan. (The Debtor may only have \$168,180 in the \$30
12 million University & Ash loan.) It appears that the primary reason the Debtor is entering
13 into this settlement is because of the alleged lender liability exposure which exists solely
14 because of its alleged failure to fund the University & Ash loan. This settlement was
15 being made “to buy peace” with an aggressive borrower in the face of a motion to appoint
16 a trustee. The Debtor is trying to use the assets of the investors as a way to satisfy its own
17 exposure. This conflict of interest violates the Debtor’s fiduciary duty to the principals it
18 serves and irreparably damages the investors. This kind of action can not be a reasonable
19 exercise of the Debtor’s business judgment.

19 **I. INADEQUATE NOTICE OF THE NEW SETTLEMENT MOTION**

20 The New Settlement Motion significantly changed the terms of the settlement. It
21 was filed two business days before the hearing after 5 p.m. Some of the investors may
22 have received it by email one business day before the hearing and others have not seen it.
23 This can hardly be determined to be adequate and meaningful notice. The investors must
24 be given a reasonable time and opportunity to understand and evaluate the New
25 Settlement Motion. To further aggravate the situation, the Investors Committee has
26 received no documents from University & Ash despite its repeated requests and its
27 subpoena. Plus, in order to provide documents for the deposition and presumably the
28

1 hearing on this \$43 million settlement, University & Ash's counsel was requiring the
2 Investors Committee to execute a confidentiality agreement. Of course, they did not bring
3 this up until the day before the deposition. Also, the Investors Committee was not
4 allowed to depose the University & Ash witness until 5 p.m. the business day before the
5 hearing. The Investors Committee also brings to the Court's attention that the draft
6 amended note and loan documents were not attached to the Supplement and were not
7 served on investors or the Investors Committee. Given the nature of the New Settlement
8 Agreement and the lack of the amended loan documents, there is a serious question about
9 the adequacy of the notice given to the investors. As a result, the hearing must be
10 continued.

11 **II. THE NEW SETTLEMENT MOTION IS REALLY A SUB ROSA PLAN**
12 **AND CANNOT BE APPROVED AS A 9019 MOTION**

13 The new settlement has significant provisions that can only be instituted under a
14 plan of reorganization and will substantively predetermine the terms of the treatment of
15 the Borrowers and the investors in these loans. As such, it is a *sub rosa* plan and cannot
16 be approved under a 9019 Motion. Its approval must await the plan confirmation.

17 It is well established that a settlement which has the effect of dictating the terms of
18 the debtor's plan of reorganization prior to the confirmation process cannot not be
19 approved. See *In re Braniff*, 700 F.2d 935, 940 (5th Cir.1983) ("The debtor and the
20 bankruptcy court should not be able to short circuit the requirements of Chapter 11 for
21 confirmation of a reorganization plan by establishing the terms of the plan sub rosa ...");
22 *In re Iridium*, 2005 WL 756900 at *7 ("the trustee *169 is not authorized to enter into a
23 settlement if it results in a de facto or sub rosa plan of reorganization"); *In re Crowthers*
24 *McCall Pattern, Inc.*, 114 B.R. 877, 887 (Bankr.S.D.N.Y.1990) ("A transaction which
25 would effect a lock-up of the terms of a plan will not be permitted").

26 The *Braniff* Court, for instance, refused to approve two settlements by the debtor
27 that purported to resolve disputes with certain of its secured and unsecured creditors.
28 Those settlements involved a complex transfer of cash, aircraft, equipment, leases and

1 landing slots in exchange for travel scrip, notes and a profit participation in the purchaser.
2 *Braniff*, 700 F.2d at 938. The proposed agreements would have required the debtor to
3 distribute travel scrip in any plan of reorganization, a requirement the Fifth Circuit
4 declared impermissibly “had the practical effect of dictating some of the terms of any
5 future reorganization plan.” *Id.* at 939-40. As that court recognized, “[t]he debtor and the
6 Bankruptcy Court should not be able to short circuit the requirements of chapter 11 for
7 confirmation of a reorganization plan” by establishing the essential terms of a plan in
8 connection with a separate agreement. *Id.* at 940.

9 Following *Braniff*, courts have refused to condone settlement agreements that do
10 far less than Debtor’s sweeping proposals to modify the protections otherwise afforded its
11 investors. In the *Continental Air Lines* case, for instance, the bankruptcy court approved
12 two of the debtor’s post-petition aircraft leases. Creditors appealed, contending that the
13 proposed leases “represent pieces of a creeping plan of reorganization” and that they
14 “could have defeated a plan of reorganization containing the leases.” 780 F.2d at 1227,
15 1228. The Fifth Circuit vacated the bankruptcy court’s decision, noting that the
16 protections afforded by the confirmation process “might become meaningless” if they
17 could be avoided piecemeal through agreements reached prior to confirmation. *Id.* at
18 1227-28 (“[u]ndertaking reorganization piecemeal pursuant to § 363(b) should not deny
19 creditors the protection they would receive if the proposals were first raised in the
20 reorganization plan”).

21 Here, Debtor’s attempt to summarily modify the lender-borrower relationships in
22 three loans in the aggregate of over \$43 million is beyond the pale. And while the
23 investors may eventually vote on a plan, that right will be meaningless if Debtor
24 effectuates these pre-plan settlements that irrevocably limit the options available at the
25 time of confirmation for these three loans. In the Bankruptcy Case, the Agency
26 Agreements and the Operating Agreements have not been assumed by the Debtor yet the
27 terms of the settlement contemplate many actions by the Debtor which will require
28 performance by the Debtor for the next 15 years. The New Settlement Agreement is

1 being entered into by “Mortgages Ltd. in its capacity as debtor and debtor in possession”
2 according to the opening paragraph and is signing “for itself and on behalf of the Loan
3 Beneficiaries.” In addition, the New Settlement Agreement at Section 2(g) (which is
4 attached to the New Settlement Motion) indicates that under a plan of reorganization the
5 three loans may be transferred into a new ML Holding Company (or a separate entity for
6 each loan) which will be created to hold the ownership interests in the three notes and
7 deeds of trust. This provision is clearly beyond the scope of a 9019 Motion and can not
8 be implemented by a 9019 Motion. Finally, the New Settlement Motion purports to
9 reduce the amount of the University & Ash claim against the estate by almost \$15.4
10 million which represents an almost 50% payout on their alleged unsecured claim on the
11 University & Ash claim which has been filed against the estate. Other unsecured creditors
12 have not been paid and may not receive the same percentage distribution. This reduction
13 of almost \$15.4 million also guarantees that the investors in the University & Ash Note
14 will receive at best only 50% of their proceeds from their interest in the note and deed of
15 Trust. This is all being done on less than 2 business days notice, without the protections
16 or right to vote on this significant change and without the benefit of an adequate
17 disclosure statement. Pre-petition claims of the Borrowers should not be paid absent a
18 confirmed plan of reorganization. *In re Airbeds, Inc.* 92 B.R. 419, 424 (9th Cir. BAP
19 1988). Thus the New Settlement Motion is an attempted “end run” around the protections
20 afforded to the investors under the Bankruptcy Code, and as they are *sub rosa*, they
21 cannot be approved.

22 **III. THE TERMS OF THE NEW SETTLEMENT MOTION ARE NOT**
23 **REASONABLE**

24 The terms of the New Settlement Agreement are not within the zone or range of a
25 reasonable settlement. Both the business and legal terms swing too far in favor of the
26 Borrowers, create unreasonable risk for the investors, are illusory and minimize any
27 chance of recovery. The facts are as follow:

- 28 1. The Debtor has agreed to restructure three separate loans with three separate

1 Borrowers in one New Settlement Agreement. The Borrowers are University & Ash,
2 LLC (“UA”), Roosevelt Gateway LLC (“RG”) and Roosevelt Gateway II LLC (“RGII”).
3 Each Borrower has given a separate note, separate deed of trust on its property and other
4 security interest in its collateral to the Debtor. Each note has a separate set of investors
5 with undivided fractional interests and each deed of trust has separate beneficiaries from
6 the other deeds of trust. All three properties are presently raw land. The three loans are
7 cross defaulted but not cross collateralized except that each of the RG Loan and the RGII
8 Loan are subject to a second deed of trust in favor of the other’s lender. Only the UA loan
9 was to be a construction loan.

10 2. The restructure proposed as set forth in Section 2 of the New Settlement
11 Agreement is as follows:

12 (a) The University & Ash Loan (“UA Loan”) principal is reduced from
13 \$30,300,000 to \$14,900,000, a reduction of \$15,400,000;

14 (b) The interest rate on the UA Loan, the Roosevelt Gateway LLC loan
15 (“RG Loan”) and the Roosevelt Gateway II LLC loan (“RGII Loan”) are decreased from
16 the current rates of 14.5%, 14.75% and 13.25%, respectively, to an interest rate of 6.68%
17 for a period of 10 years and then the interest rate is increased to 15.2% thereafter, which
18 interest is accrued but not compounded and is paid only out of “Net Cash Available for
19 Distribution”. This results in a significant decrease in the rates the Borrowers agreed to
20 pay at the expense of the investors in the notes.

21 (c) Payments under any proposed amended notes will be paid out of Net
22 Cash Available for Distribution. Because the properties are not projected to produce any
23 cash flow for 5 years, there will not be any payments to investors for at least 5 years.

24 (d) Under Section 2(e), the final maturity date of the loans is extended
25 out for 15 years unless the Net Cash Available for Distribution repays the loans prior to
26 that time. If any aspect of the bankruptcy proceeding causes a delay in the development
27 of any of the projects, in the Borrowers’ judgment, then the 15-year final maturity date
28 and interest accrual is tolled for the duration of the delay. Debtor concedes that the loans

1 can only be repaid based upon a sale of the UA property and the RG properties and
2 Debtor projects a holding period of 10 to 14 years before the investors would receive any
3 significant payments on the loans. Thus what was intended to be a short term construction
4 loan has been changed to a long term hold to the detriment of the investors.

5 (e) The Borrowers on UA and RG propose to find a joint venture partner
6 (“JV Partner”) to put up equity (which the Borrowers apparently are not capable of doing)
7 and to obtain a new construction loan to build student friendly apartments on each
8 property where the total cost is approximately \$139 million including land cost on each
9 site. The Debtor and Borrowers envision for each site a construction loan of
10 approximately \$105 million, a Mezzanine Loan of \$14 million and new equity from the
11 JV Partner of \$8 million. The Borrowers intend to give a preference to the new JV
12 Partner on the contributed capital plus 50% of all cash received from the operation and
13 sale of the projects. The whole purpose is to turn two pieces of raw land into two finished
14 apartment projects by holding the investors funds hostage for 15 years.

15 (f) To obtain a pre-development loan, a construction loan or a permanent
16 loan, the Borrowers intend to give the new lender a first priority lien on the property of the
17 Borrower. While Section 2(h) is not drafted very clearly and we have no loan documents
18 to review, it may be that the Debtor intends that all three properties may be given as
19 security for a construction loan on the first property. Clearly, where the RGII investors
20 have a second deed of trust on the RGI property, they would be forced to subordinate or
21 effectively give up their collateral to secure a loan on the RGI property and in essence will
22 be in third position. Thus the Debtor wants to allow the Borrowers to use each investor’s
23 individual collateral to secure a loan for another Borrower. The concept that the Debtor,
24 which is a fiduciary for each of the investors, could suggest that it is acceptable for it, as
25 agent, to use (by subordination) the collateral of one investor group to secure a loan for
26 another Borrower on a separate property in which the one investor group has only a
27 collateral interest is truly amazing. In order to secure such new loans, under Section 2(h)
28 the investors are required to subordinate their deeds of trust to the new loan.

1 (g) Further, after funding of the new loan or any Additional Funding, the
2 investors are required under the last half of Section 2(f) to release any right to ever
3 foreclose under their deeds of trust. The sole remedy from that point forward will be to
4 receive a distribution of Net Available Cash Flow when and it is available. In this event,
5 the normal short term mortgages will be turned into long term cash flow mortgages on
6 projects in which they virtually have no say. The investors are suddenly in the
7 development business against their will.

8 (h) In Section 3 of the New Settlement Agreement, the Debtor also
9 proposes to allow the Borrowers to obtain "Additional Funding" in the form of loans or
10 equity from third parties or from principals or affiliates of the Borrowers. The only time
11 consent is required is if there would be a Material Deviation from Economic Results and
12 then the consent would be given by Debtor as manager of the new proposed ML Holding
13 Company or as agent for each of the new limited liability companies which may be form.
14 Thus, the investors really will not have a say in any such funding. The Borrowers can
15 give away additional portions of the cash flow to pay for the Additional Funding and thus
16 effect the Net Cash Available for Distribution available to pay the loans.

17 (i) Also, under the last sentence of Section 2(f), the Borrowers could
18 take away the investors' ability to foreclose their loans by simply having an affiliate make
19 a minor Additional Funding while trying to find a construction loan and JV Partner. Since
20 the investors have no approval rights on Additional Funding except as described above,
21 the Borrowers could turn the investors' rights into a cash flow mortgage without ever
22 getting a construction loan.

23 (j) Upon Court approval, the settlement becomes effective under Section
24 5 and then under Section 4 the guarantees of the loans are extinguished and the
25 Guarantors walk without any further liability. Further, the release language of Section 5 is
26 overly broad, can be read to release other claims of the Loan Beneficiaries in unrelated
27 loans, and should be limited to only these loans.

28 (k) Under Section 2(l) of the New Settlement Agreement, the definition

1 of "Net Cash Flow from Operations" allows the Borrowers to deduct in subsection (i)
2 repayment of all new loans to the Borrowers and in subsection (ii) the repayment of all
3 Additional Funding (which could include the equity of the Borrowers). As a result, the
4 purported split of such net cash flow with 75% to go to the investors is illusory. It is
5 speculative as to whether the investors will receive anything since they will be
6 subordinate and junior to all Additional Funding and basically all indebtedness on the
7 properties.

8 3. The New Settlement Agreement does not provide for adequate investor
9 protection and in fact gives way too much power to each Borrower. For instance, there is
10 no requirement that the amount of the construction loan, the Mezzanine loan and equity
11 provided must be equal to the estimated costs of the project. There are no standards for
12 how much equity interest can be given to a JV Partner. Under Section 2(f), the investors
13 are required to subordinate their deeds of trust with only a vague standard of any
14 subordination agreement commercially reasonably required by the lender. Since the
15 investors have a total of \$43 million invested in notes given by the Borrowers and the
16 Borrowers only have maybe \$5 million to \$8 million in the projects, it seems strange that
17 the investors have virtually no approval rights when they have far more at risk than the
18 Borrowers.

19 4. Under Section 2(g), the Debtor proposes to create a new holding company
20 to hold all three of the loans. The new ML Holding Company will have a board which
21 may provide "input" to the Borrower under Section 2(k) but has virtually no approval
22 rights. If approvals are required, the Debtor asserts that it can give the approval on behalf
23 of the investors as their agent. Any time that the approval of the investors is required, if
24 the Borrower alleges that the approval was unreasonably withheld, the Borrower can toll
25 interest accrual under the last sentence of Section 2(h) until a court of competent
26 jurisdiction determines whether the consent or approval was unreasonably withheld.

27 5. Under Section 2(l), the Net Cash Available from Operations is to be paid
28 75% to the investors and 25% to the Borrower and Net Cash Available from Capital

1 Transactions is paid 50% to the investors and 50% to the Borrowers. A review of the
2 projection attached to the New Settlement Agreement reveals that in 10 years the
3 investors could theoretically recover (if everything turns out to be true) \$47,040,000 and
4 the Borrowers could recover \$38,451,398. In 14 years, the investors could theoretically
5 recover \$64,064,000 and the Borrowers could recover \$63,997,443. The investors, who
6 have four times as much money involved in the projects, recover a little more than the
7 Borrowers since the transaction is slanted to favor the Borrowers at the expense of the
8 investors.

9 6. Under Section 2(m) of the New Settlement Agreement, if the Borrowers
10 allege that the ML Holding Company has unreasonably withheld a consent as required in
11 that paragraph, the Borrowers for a period of 2 years can purchase the property at the
12 appraised value which in today's market may be less than the amount of the loans. This is
13 just another strong-arm tactic in favor of the Borrowers to prevent the investors or the
14 Debtor from withholding an approval on a close question of reasonableness.

15 7. Under Section 5(a) of the New Settlement Agreement, the settlement is
16 implemented and becomes effective prior to a plan being confirmed so that the investors
17 never really have a chance to vote on the proposal if the Court approves the settlement.

18 8. The New Settlement Agreement in Section 6 and 7 provides for mutual
19 release of the Borrowers of all claims against the Debtor and vice versa and a release of
20 the Guarantors in Section 4. These releases clearly are to the benefit of the Debtor against
21 whom the Borrowers have alleged claims and filed a \$155 million lender liability claim in
22 this proceeding. The Borrowers do not have any claims against the investors that are
23 credible, so that this New Settlement Agreement's main purpose is to protect the Debtor at
24 the expense of the investors. The Debtor has a clear conflict of interest in this matter.

25 9. The Debtor and Borrowers have not filed or provided the amended and
26 restated loan documents which should be reviewed for their provisions. The New
27 Settlement Motion should not be approved without any opportunity for the Investors
28 Committee and investors to review the loan documents.

1 **IV. THE DEBTOR DOES NOT HAVE AUTHORITY TO BIND INVESTORS**
2 **OR THE MP FUNDS TO THE TERMS OF THE SETTLEMENT**

3 As more fully explained in the Investors Committee’s “Statement of Position” and
4 “Supplement to Statement of Position” filed in this matter, the Debtor as Agent or
5 Manager has limited authority and such authority does not include the extreme actions
6 required for the New Settlement Motion. The Debtor has no authority to agree to such
7 extreme modifications to the lender-borrower transaction. Among other things, the
8 principal is significantly reduced; the interest rates are reduced; the guarantees are
9 released; the maturity is extended 15 years; the short term loans are turned into permanent
10 15-year financing; there is no cash payment to the investors for at least 5 years while the
11 Borrowers are allowed to pull out significant development fees; the subordination terms
12 do not protect the investors and could result in the liens being extinguished without any
13 payment to investors; the remedy of foreclosure is extremely compromised; and the
14 buyout provision for fair market value wipes out the ability of the investors to recover the
15 property itself. The Debtor has no authority to agree on behalf of the investors to any of
16 these items, let alone all of them.

17 As stated in the Supplement, these issues of authority are intended to be used to
18 protect the Investors and the Collateral. The Debtor, as the servicing agent or collection
19 agent or as the Manager with regards to the collection of the Loans, must also exercise its
20 responsibilities in a manner to protect the Loans and Collateral. The specific issues raised
21 herein demonstrate how the terms of the New Settlement Agreement do not protect the
22 Investors and are thus outside the scope of authority for the Debtor.

23 In analyzing the New Settlement Motion, one over-riding fact must be kept in
24 mind: The Debtor is acting as a fiduciary for other people’s money. It came from
25 investors or other entities, including hundreds of individuals, including many elderly
26 investors who depend on this money. This is not a business deal to many of these
27 investors; it is their life savings – life savings that some of these elderly investors cannot
28 access and are relying on for their continued support in a troubled market. In other words,

1 the Debtor is playing with other people's money. The Debtor itself has only \$168,180 in
2 the \$30 million UA Loan and nothing in the RG Loan or the RGII Loan. The Investors
3 Committee's goal in this matter is not to be obstructionist or unreasonable, but it is simply
4 to protect the investors' rights and to get as much of the investors' money back to them as
5 soon as possible.

6 **V. DEBTOR HAS NOT SATISFIED ITS REASONABLE BUSINESS**
7 **JUDGMENT WHILE STILL MEETING ITS DUTIES OF CARE,**
8 **COMPETENCE OR DILIGENCE TO THE INVESTORS**

9 This New Settlement Motion does not satisfy Debtor's obligation as agent or under
10 the business judgment rule to act with the care, competence and the diligence required of
11 agents in similar circumstances, for a variety of reasons.

12 The Debtor has no interest in the two Roosevelt Gateway loans and only a
13 negligible interest in the University & Ash loan. (The Debtor may only have \$168,180 in
14 the \$30 million UA Loan.) Yet the primary reason the Debtor is entering into this
15 settlement is because of its lender liability exposure due to its alleged failure to fund. This
16 settlement is being made "to buy peace" with the aggressive Borrowers in the face of a
17 motion to appoint a trustee. The Debtor is trying to use the assets of the investors as a
18 way to satisfy its own exposure. The investors did not cause this problem. They are
19 innocent victims of alleged misconduct by their agent, the Debtor. To the extent that the
20 Borrowers are able to argue that there might be lender liability claims against the
21 investors, it is only because of the Debtor's actions, not the investors. Any remedy which
22 the investors might have against the Debtor to make up for this alleged problem will be
23 inadequate and the investors may never be made whole. This conflict of interest violates
24 the Debtor's fiduciary duty to the principals it serves and irreparably damages the
25 investors.

26 The investors unfairly bear the risk of this settlement. Significantly, there is no
27 analysis by the Debtor in either its original Motion or the New Settlement Motion. There
28 are no third party market studies showing the feasibility of these student apartment
projects. No analysis showing the impact of the current economic market on the viability

1 of obtaining new financing or on the projects. There is no valuation analysis showing the
2 “as complete” values which would justify this risk and the release of guarantees.

3 This New Settlement Agreement violates the Debtor’s obligation to act with the
4 care, competence and diligence exercised by agents in similar circumstances.
5 Specifically, Section 8.08 of the *Restatement (Third) Agency* provides:

6 Subject to any agreement with the principal, an agent has a
7 duty to the principal to act with the care, competence, and
8 diligence normally exercised by agents in similar
9 circumstances. Special skills or knowledge possessed by an
10 agent are circumstances to be taken into account in
11 determining whether the agent acted with due care and
12 diligence. If an agent claims to possess special skills or
13 knowledge, the agent has a duty to the principal to act with the
14 care, competence, and diligence normally exercised by agents
15 with such skills or knowledge.

16 The Debtor serves as an agent, or otherwise manages, a loan portfolio of nearly \$1 billion,
17 substantially all of the portfolio being comprised of other people’s money (the investors,
18 etc.). The Debtor should accordingly be held to a high standard of care. Although the
19 Debtor’s breach of its duty of loyalty is addressed below, it’s duties of care, competence
20 and diligence are expressly implicated here. It has not met those duties.

21 Moreover, due to the power of attorney and agency relationships, the scope of the
22 agent’s authority must be strictly constructed. It is well established that courts must
23 strictly construct the grant of authority in a power of attorney. *Lightning Delivery Co. v.*
24 *Matteson*, 45 Ariz. 92, 97 39 P.2d 938, 941 (1935) (“[i]t must be kept in mind that under
25 all the authorities powers of attorney should be strictly construed and that the courts
26 should never by construction extend the power they confer beyond that given in terms, or
27 is absolutely necessary to carry that conferred into effect”); *Archbold v. Reifenrath*, 744
28 N.W.2d 701, 708 (Neb. 2008) (“[p]owers of attorney are by necessity strictly construed,
and broad encompassing grants of power are to be discounted”).

This New Settlement Motion does not satisfy the business judgment rule. The
business judgment rule presumes that “in making a business decision the directors of a
corporation acted on an [1] informed basis, [2] in good faith and [3] in the honest belief

1 that the action taken was in the best interest of the company.” *United Dairy of Ariz. v.*
2 *Schugg*, 212 Ariz. 133, 140, 128 P.3d 756, 763 (Ariz. Ct. App. 2006). In this case, the
3 Debtor has a duty to be acting on behalf of the investors, with whose money it is making
4 deals.

5 By acting as set forth above, the Debtor has placed its own interests above the
6 interests of the investors. This conflict for the Debtor prevents this decision from being a
7 reasonable exercise of the business judgment rule and constitutes a breach of the Debtor’s
8 duty to its principals.

9 The Debtor also owes a duty of loyalty and a duty to not self deal to the investors
10 and should be required to live up to that standard. In particular, Section 8.02 of the
11 *Restatement (Third) of Agency* provides that “[a]n agent has a duty not to acquire a
12 material benefit from a third party in connection with transactions conducted or other
13 actions taken on behalf of the principal or otherwise through the agent’s use of the agent’s
14 position.” Similarly, Section 8.05(1) of the *Restatement (Third) of Agency* provides that,
15 “[a]n agent has a duty (1) not to use property of the principal for the agent’s own purposes
16 or those of a third party.” As noted above, the Debtor failed to provide the additional
17 construction funds and now is forced to settle the lender liability allegations and the threat
18 of a trustee motion at the expense of the investors. This is the very definition of an agent
19 using its principal’s property for the agent’s own purposes.

20 Therefore, the Investors Committee requests that the New Settlement Motion be
21 denied.

22 DATED this 7th day of November, 2008.

23 FENNEMORE CRAIG, P.C.

24
25 By /s/ Cathy Reece (005932)

26 Cathy L. Reece
27 Keith L. Hendricks
28 Attorneys for the Official Committee of
Investors

1 COPY of the foregoing emailed or mailed
2 this 7th day of November, 2008 to the parties
3 on the attached Service List.

4 /s/ Susan Stanczak-Ingram

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SERVICE LIST
2:08-bk-07465

<p>John R. Clemency, Esq. Todd A. Burgess, Esq. Greenberg Traurig, LLP 2375 E. Camelback Road, #700 Phoenix, AZ 85015 clemencyj@gtlaw.com burgessst@gtlaw.com Atty for: Mortgages Ltd.</p>	<p>Jonathan E. Hess Office of the U.S. Trustee 230 N. 1st Avenue, Suite 204 Phoenix, Arizona 85003-1706 Jon.e.hess@usdoj.gov Atty for: US Trustee</p>	<p>Donald L Gaffney Donald Fredrick Ennis Snell & Wilmer LLP One Arizona Center Phoenix, Arizona 85004-2202 dgaffney@swlaw.com dfennis@swlaw.com Atty for: Central & Monroe; KGM Builders; Osborn III Partners</p>
<p>David Wm. Engelman Steven N. Berger Bradley D. Pack Engelman Berger, P.C. 3636 N. Central Avenue, #700 Phoenix, Arizona 85012 dwe@engelmanberger.com snb@engelmanberger.com bdp@engelmanberger.com Atty for: Tempe Land Company</p>	<p>Robert A. Shull Mariscal, Weeks, Mchityre & Friedlander 2901 N. Central, #200 Phoenix, Arizona 85012-2705 rob.shull@mwmf.com Atty for: Artemus Realty Capital, and Gold Creek, Inc.</p>	<p>Shelton L Freeman Nancy J. March DeConcini McDonald Yetwin & Lacy 7310 North 16th Street Phoenix, Arizona 85020 tfreeman@dmylphx.com nmarch@dmylphx.com Atty for: Radical Bunny, LLC</p>
<p>Sean O'Brien Gust Rosenfeld, PLC 201 E. Washington St., #800 Phoenix, AZ 85004-2327 spobrien@gustlaw.com Atty for: Larry Lattig, Litigation Trustee</p>	<p>Richard R. Thomas T. Whitney Thomas Scjern Richardson 1640 South Stapley Dr., #205 Mesa, Arizona 85204 rthomas@thomas-schern.com twhitney@thomas-schern.com Atty for: Eva Sperber-Porter, Litchfield Road Associates Limited Partnership, and Baseline & Val Vista Associates Limited Partnership</p>	<p>Daniel P. Collins Collins, May Potenza, Baran & Gillespie 201 North Central Ave., #2210 Phoenix, Arizona 85004-0022 dcollins@cmpbglaw.com Atty for: William Hall</p>
<p>Dennis J. Wickham Seltzer Caplan McMahon Vitek 750 B Street, Suite 2100 San Diego, California 92101 wickham@scmv.com Atty for: Southwest Value Partners Fund XIV, LP</p>	<p>Jerry L. Cochran Cochran Law Firm, P.C. 2999 N. 44th Street, #600 Phoenix, Arizona 85018 jcochran@cochranlawfirm.com Atty for: Metropolitan Lofts</p>	<p>Lawrence E. Wilk Jonathan P. Ibsen Jaburg & Wilk, P.C. 3200 North Central Ave, #2000 Phoenix, Arizona 85012-2440 lew@jaburgwilk.com jpi@jaburgwilk.com Atty for: Laura Martini</p>

SERVICE LIST
2:08-bk-07465

<p>Kevin J. Blakley Gammage & Burnham, P.L.C. Two North Central Avenue, 18th Fl Phoenix, Arizona 85004 Kblakley@gbllaw.com Atty for: Ronald L. Kohner</p>	<p>Gerald K. Smith Lewis and Roca LLP 40 N. Central Ave., #1900 Phoenix, Arizona 85004-4429 gsmith@lrlaw.com Atty for: the Estate Scott M. Cole and Trustee of the SMC Revocable Trust U/T/A</p>	<p>Terry A. Dake Terry A. Dake, Ltd. 11811 North Tatum Blvd, #3031 Phoenix, Arizona 85028-1621 Tdake@cox.net Atty for: Penny Hardaway Investments</p>
<p>Rebecca J. Winthrop Ballard Spahr Andrews & Ingersoll, LLP 2029 Century Park East, #800 Los Angeles, CA 90067-2909 winthropr@ballardspahr.com Atty for: University & Ash, Roosevelt Gateway; Roosevelt Gateway II and KML Development</p>	<p>Dean C. Waldt Ballard Spahr Andrews & Ingersoll, LLP Plaza 1000 – Suite 500 Main Street Voorhees, NJ 08043-4636 waldtd@ballardspahr.com Atty for: University & Ash, LLC, Roosevelt Gateway, Roosevelt Gateway II and KML Development</p>	<p>Charles A. Lamar Justin C. Lamar 818 North First Street Phoenix, Arizona 85004 clamar@kmldevelopment.com jlamar@kmldevelopment.com Atty for: University & Ash; Roosevelt Gateway, Roosevelt Gateway II and KML Development</p>
<p>Ryan W. Anderson Guttilla Murphy Anderson, PC 4150 West Northern Avenue Phoenix, AZ 85051 randerson@gamlaw.com Atty for: Department of Financial Institutions</p>	<p>Jerome K. Elwell Warner Angle 3550 N. Central, #1500 Phoenix, AZ 85012 jelwell@warnerangle.com Atty for: Francine Haraway</p>	<p>C. Taylor Ashworth Alissa C. Lacey Stinson Morrison Hecker LLP 1850 N. Central Ave., #2100 Phoenix, AZ 85004 tashworth@stinson.com alacey@stinson.com Atty for: Oxford & Investor Group</p>
<p>Felecia A. Rotellini Robert Charlton Arizona Dept. of Financial Institutions 2910 N. 44th St., Suite 310 Phoenix, AZ 85018 frotellini@azdfi.gov rcharlton@azdfi.gov</p>	<p>William J. Maledon John L. Blanchard Osborn Maledon 2929 N. Central Ave., #2100 Phoenix, AZ 85012 wmaledon@omlaw.com jblanchard@omlaw.com Atty for: Rightpath Limited Development Group, LLC</p>	<p>Christopher S. Reeder Yaw-Jiun Wu Sheppard, Mullin, Richter & Hampton 333 South Hope St., 48th Floor Los Angeles, CA 90071 creeder@sheppardmullin.com gwu@sheppardmullin.com Atty for: Right Path</p>

SERVICE LIST
2:08-bk-07465

<p>C. Bradley Vynalek Quarles & Brady LLP One Renaissance Square 2 North Central Avenue Phoenix, AZ 85004 bvynalek@quarles.com Atty for: Ashley Coles</p>	<p>Craig A. Raby Office of the Attorney General 1275 W. Washington Phoenix, AZ 85007 craig.raby@azag.gov</p>	<p>Scott A. Rose Kerry M. Griggs The Cavanaugh Law Firm 1850 N. Central Ave., #2400 Phoenix, AZ 85004 srose@cavanaghlaw.com kgriggs@cavanaghlaw.com Atty for: Central PHX Partners</p>
<p>Christopher A. LaVoy LaVoy & Chernoff, PC 201 N. Central Avenue, #3300 Phoenix, AZ 85004 cal@lavoychernoff.com Atty for: Sue Ross and Ted Dodenhoff</p>	<p>Robert J. Spurlock Bonnett, Fairbourn, Friedman & Balint 2901 N. Central Avenue, #1000 Phoenix, AZ 85012-3311 bspurlock@bffb.com Atty for: Foothills Plaza IV, LLC</p>	<p>S. Cary Forrester Forrester & Worth, PLLC 3636 N. Central Avenue, #700 Phoenix, AZ 85012 scf@fwlawaz.com Atty for: the Lewis Trust</p>
<p>Sheldon Sternberg 3212 Rainbow Ridge Drive Prescott, AZ 86303 sheldonsternberg@q.com Atty for: Pro Per</p>	<p>Gerald T. Hickman Jardine, Baker, Hickman & Houston 3300 North Central Ave. #2600 Phoenix, AZ 85012 ghickman@jbhhlaw.com Atty for: Mayer Hoffman McCann</p>	<p>Philip R. Rudd Ethan B. Minkin Kutak Rock LLP 8601 N. Scottsdale Rd., #300 Scottsdale, AZ 85253 philip.rudd@kutakrock.com ethan.minkin@kutakrock.com Atty for: Arizona Bank & Trust</p>
<p>Christopher S. Reeder Margaret M. Mann Sheppard, Mullin, Richter & Hampton 333 South Hope St., 48th Floor Los Angeles, CA 90071-1448 CReeder@sheppardmullin.com MMann@sheppardmullin.com Atty for: Rightpath Limited Development Group, Mayland Way Partners; Daniel L. Hendon; Rick L. Burton; Raymond Rodrigues; Robert C. Banovac; Rightpath Limited; and Gledale Jet Center</p>	<p>John J. Dawson John A. Harris Quarles & Brady LLP One Renaissance Square 2 North Central Avenue Phoenix, AZ 85004 jdawson@quarles.com jharris@quarles.com Atty for: Southwest Value Partners Fund XIV and Southwest Value Partners Finance I</p>	<p>Stanford E. Lerch Anthony E. DePrima Lerch and DePrima PLC 4000 N. Scottsdale Road, #107 Scottsdale, AZ 85251 slerch@ldlawaz.com tdeprima@ldlawaz.com Atty for: Howard Farkash (Successor TTEE OFT)</p>

SERVICE LIST
2:08-bk-07465

<p>Richard H. Herold Hinshaw & Culbertson LLP 3200 N. Central Ave., #800 Phoenix, AZ 85012-2428 rherold@hinshawlaw.com Atty for: Irwin Union Bank</p>	<p>Patrick R. Barrowclough Atkinson, Hamill & Barrowclough PC 3550 N. Central Ave., #1150 Phoenix, AZ 85012 Patrick.Barrowclough@azbar.org Atty for: Chuck Niday, Trustee for Ross Verne Family Trust</p>	<p>Brian M. Bergin Catherine A. Sims Rose Law Group PC 6613 N. Scottsdale Road, #200 Scottsdale, AZ 85250 bbergin@roselawgroup.com csims@roselawgroup.com Atty for: Kelly Haddad and Navval Haddad, Creditors</p>
<p>Don C. Fletcher The Cavanagh Law Firm 1850 N. Central Ave., #2400 Phoenix, AZ 85004 dfletcher@cavanaghlaw.com Atty for: Sorenson Companies</p>	<p>Michael W. Carmel Michael W. Carmel, Ltd. 80 East Columbus Avenue Phoenix, AZ 85012-2334 Michael@mcarmellaw.com Atty for: Vanderbilt Farms, Vistoso Partners, Ellsworth 160, Riggs/Queen Creek 480, ABCDW, LLC</p>	<p>Gabriel G. Green Sheppard, Mullin, Richter Hampton, LLP 333 S. Hope St., 48th Floor Los Angeles, CA 90071-1448 GGreen@sheppardmullin.com Atty for: Rightpath Limited Development, Maryland Way Partners, Daniel L. Hendon, Rick L. Burton, Raymond Rodriguez, Robert C. Banovac; Glendale Jet Center</p>
<p>Randy Nussbaum Dean Dinner Nussbaum & Gillis 14500 N. Northsight Blvd. #116 Scottsdale, AZ 85260 rnussbaum@nussbaumgillis.com ddinner@nussbaumgillis.com Attys for: Official Unsecured Creditors Committee of Mortgages Ltd.</p>	<p>Carolyn J. Johnsen Bradley J. Stevens Todd Adkins Todd B. Tuggle Jennings Strouss & Salmon PLC 201 E. Washington Street Phoenix, AZ 85004 cjohnsen@jsslw.com tadkins@jsslw.com bstevens@jsslw.com TTuggle@jsslw.com Attys for Mortgages Ltd.</p>	<p>John M. McCoy III Sandra W. Lavigna David Brown Attn: Ronnie B. Lasky 5670 Wilshire Blvd., 11th Fl. Los Angeles, CA 90036-3648 Attys for U.S. Securities and Exchange Commission mccoyj@sec.gov lavignas@sec.gov browndav@sec.gov</p>
<p>Richard Patrick U.S. Attorneys Office 40 N. Central Ave., Suite 1200 Phoenix, AZ 85004-4408 Richard.Patrick@usdoj.gov</p>	<p>Dale C. Schian Schian Walker PLC 3550 N. Central Ave., Suite 1700 Phoenix, AZ 85012-2115 dschian@swazlaw.com Attys for VTL Investors</p>	<p>Jeffrey S. Kaufman Jeffrey S. Kaufman, Ltd. 5725 N. Scottsdale Rd., #190 Scottsdale, AZ 85250 Jeff@KaufmanEsq.com Atty for Brien H. Butler, as Trustee of the Brien H. Butler Living Trust, Earl Geller, as Trustee of The Martin Hershman Trust dated 10/17/1996, and First Trust Company of Onaga, Custodian FBO Earl Geller IRA</p>



File an Answer/Response/Objection to a Motion:

2:08-bk-07465-RJH Mortgages Ltd. CASE CONVERTED on 06/24/2008

Type: bk	Chapter: 11 i	Office: 2 (Phoenix)
Judge: RJH	Assets: y	Case Flag: Appeal, Exhibits

U.S. Bankruptcy Court

District of Arizona

Notice of Electronic Filing

The following transaction was received from CATHY L. REECE entered on 11/7/2008 at 8:28 PM AZ and filed on 11/7/2008

Case Name: Mortgages Ltd.
Case Number: 2:08-bk-07465-RJH
Document Number: 951

Docket Text:

Objection to Motion/Application to *University & Ash Settlements by Investors Committee* (related to motions(s)[570]) filed by CATHY L. REECE of FENNEMORE CRAIG on behalf of Official Committee of Investors (related document(s)[570] motion Motion to Approve Compromise/Settlement) (Attachments: # (1) Service List). (REECE, CATHY)

The following document(s) are associated with this transaction:

Document description:Main Document

Original filename:C:\Documents and Settings\sstancza\My Documents\Mtg Ltd - Objection to University & Ash Settlement.pdf

Electronic document Stamp:

[STAMP bkecfStamp_ID=875559564 [Date=11/7/2008] [FileNumber=12576002-0] [467d2c07be20aa45e40ded686356da02dc1ef37e0ba69fca1e7f8684dd18f1547c4e54a918df4045d3effe2076962354ecb7ffa0023cf6ddfa4e629e8e020aca]]

Document description: Service List

Original filename:C:\Documents and Settings\sstancza\My Documents\Mtg Ltd - Service List as of 10 27 08.pdf

Electronic document Stamp:

[STAMP bkecfStamp_ID=875559564 [Date=11/7/2008] [FileNumber=12576002-1] [20df7e9efcc6cf3d4146f30b62417a41f7ad5ecf0404c9d83ba4eb80afd9a62a19360ee75dfabd2d558774d630102963b9be20ed81741be395c4a1cda332606d]]

2:08-bk-07465-RJH Notice will be electronically mailed to:

TODD M. ADKINS on behalf of Mortgages Ltd. tadkins@jsslaw.com, bstevens@jsslaw.com;dsharp@jsslaw.com;mgoudreau@jsslaw.com;khodges@jsslaw.com

MICHAEL P ANTHONY on behalf of Harold S. Jalowsky & Thelma D. Jalowsky, Trustees of Jalowsky Trust dated 5/31/89 manthony@carsonlawfirm.com, Ireininger@carsonlawfirm.com

PATRICK R. BARROWCLOUGH on behalf of Chuck Niday, Trustee of Ross Verne Family Trust Patrick.Barrowclough@azbar.org

CHRISTOPHER H. BAYLEY on behalf of Central & Monroe, LLC CBayley@swlaw.com;docket@swlaw.com;mminnick@swlaw.com

ALLEN B BICKART on behalf of Abrahams bickartlaw@aol.com

KEVIN J. BLAKLEY on behalf of KOHNER kblakley@gblaw.com

SHANE D. BUNTROCK on behalf of T & N Living Trust buntrock@azlegal.com, janet@azlegal.com;hawkes@azlegal.com;chryste@azlegal.com

TODD A. BURGESS on behalf of Mortgages Ltd. burgesst@gtlaw.com

MICHAEL W. CARMEL on behalf of VANDERBILT FARMS, LLC. michael@mcarmellaw.com, nancy@mcarmellaw.com

JOHN R. CLEMENCY on behalf of MCA FINANCIAL GROUP, LTD. clemencyj@gtlaw.com

JERRY L. COCHRAN on behalf of 4633 Van Buren, L.L.C. jcochran@cochranlawfirmpc.com, jill@cochranlawfirmpc.com

SCOTT B. COHEN on behalf of Arizona Bank & Trust SBC@ENGELMANBERGER.COM, SKR@ENGELMANBERGER.COM

DANIEL P. COLLINS on behalf of HALL dcollins@cmpbglaw.com, cmpbglaw@gmail.com

JOSEPH E. COTTERMAN on behalf of Hoffland jec@gknet.com, dal@gknet.com;mhe@gknet.com

JAMES E. CROSS on behalf of RIGTHPATH LIMITED DEVELOPMENT GROUP, LLC, et al jcross@omlaw.com, kstewart@omlaw.com

TERRY A. DAKE on behalf of Penny Hardaway Investments, LLC tdake@cox.net

JOHN J. DAWSON on behalf of Southwest Value Partners Finance I, LLC jdawson@quarles.com

ADAM B DECKER on behalf of Farnsworth Wholesale Company, C/O JacksonWhite PC adecker@jacksonwhitelaw.com

JONATHAN A. DESSAULES on behalf of Horizon Consulting, Inc. jdessaules@dessauleslaw.com

DEAN M. DINNER on behalf of Official Committee of Unsecured Creditors ddinner@nussbaumgillis.com, srivera@nussbaumgillis.com

DAVID WM ENGELMAN on behalf of Tempe Land Company, LLC dwe@engelmanberger.com, William.Dorsey@kattenlaw.com;Kenneth.Ottaviano@kattenlaw.com;cao@engelmanberger.com;Jeffrey.

DONALD F. ENNIS on behalf of Central & Monroe, LLC dfennis@swlaw.com,
jgolder@swlaw.com;docket@swlaw.com

DON C. FLETCHER on behalf of The Sorensen Companies dfletcher@cavanaghlaw.com

S. CARY FORRESTER on behalf of The Lewis Trust scf@fwlawaz.com

SHELTON L. FREEMAN on behalf of Mortgages Ltd. tfreeman@dmylphx.com,
kgibson@dmylphx.com;hcooling@dmylphx.com;marchibald@dmylphx.com;jnokes@dmylphx.com

DONALD L. GAFFNEY on behalf of Central & Monroe, LLC dgaffney@swlaw.com,
dgaffney@swlaw.com;docket@swlaw.com;jrogalla@swlaw.com

SCOTT R. GOLDBERG on behalf of AD HOC COMMITTEE OF INVESTORS IN THE VALUE-TO-
LOAN OPPORTUNITY FUND I L.L.C. ecfdoCKET@swazlaw.com,
sgoldberg@swazlaw.com;dstephens@swazlaw.com;jlangstraat@swazlaw.com

GABRIEL G. GREEN on behalf of RIGHTPATH LIMITED DEVELOPMENT GROUP, LLC, et al
ggreen@sheppardmullin.com

ANDREW A. HARNISCH on behalf of SOJAC I, LLC, an Arizona limited liability company
aharnisch@swlaw.com, docket@swlaw.com,jgolder@swlaw.com

RICHARD HENRY HEROLD on behalf of Irwin Union Bank, F.S.B. rherold@hinshawlaw.com,
khaley@hinshawlaw.com

GERALD T. HICKMAN on behalf of Mayer Hoffman McCann P.C. ghickman@jbhhlaw.com

KERRY ALEXANDER HODGES on behalf of Mortgages Ltd. khodges@jsslaw.com,
mouTT@jsslaw.com

WILLIAM S. JENKINS on behalf of Marion wsj@mjlegal.com, bak@mjlegal.com;js@mjlegal.com

CAROLYN J. JOHNSEN on behalf of Mortgages Ltd. cjjohnsen@jsslaw.com

JEFFREY S. KAUFMAN on behalf of CUSTODIAN FBO JEFFREY S KAUFMAN BENEFICIARY
FOR SAMUEAL KAUFMAN IRA Jeff@Kaufmanesq.com, amy@kaufmanesq.com

CHRISTOPHER R. KAUP on behalf of Mountain Funding, L.L.C. crk@tblaw.com,
jas@tblaw.com;lfa@tblaw.com

ALISA C. LACEY on behalf of Oxford and Investor Group rmcgee@stinson.com

SANDRA W. LAVIGNA on behalf of U. S. Securities and Exchange Commission lavignas@sec.gov

RICHARD H. LEE on behalf of Revocable Trust Of Irene Ruth Ahearn lee@azbar.org

STANFORD E. LERCH on behalf of FARKASH slerch@ldlawaz.com, ldlaw@ldlawaz.com

RICHARD M. LORENZEN on behalf of Goldenbridge Acquisition Holdings II, LLC

rlorzen@perkinscoie.com, docketphx@perkinscoie.com

MARGARET M MANN on behalf of Maryland Way Partners mmann@sheppardmullin.com,
michelemccconnell@sheppardmullin.com

NANCY J MARCH on behalf of RADICAL BUNNY, LLC nmarch@dmyl.com

DAVID ANTHONY MCCARVILLE on behalf of Normark Farms david@mccarvillelawoffices.com

HOWARD C. MEYERS on behalf of Steele Foundation, Inc. hmeyers@bcattorneys.com,
bchesley@bcattorneys.com

ROBERT J. MILLER on behalf of Rev Op Group rjmiller@bryancave.com,
sally.erwin@bryancave.com,pxdocket@bryancave.com

ETHAN BENNETT MINKIN on behalf of Arizona Bank & Trust ethan.minkin@kutakrock.com

ADAM B. NACH on behalf of MCA FINANCIAL GROUP, LTD.
adam.nach@azbar.org;lnbkcourt@yahoo.com

RANDY NUSSBAUM on behalf of Official Committee of Unsecured Creditors
rnussbaum@nussbaumgillis.com,
sdousdebis@nussbaumgillis.com;rnussbaum@nussbaumgillis.com;mlindauer@nussbaumgillis.com

SEAN P. O'BRIEN on behalf of Gust Rosenfeld as Ordinary Course Professional for Mortgages Ltd.
spobrien@gustlaw.com, share@gustlaw.com

BRADLEY DAVID PACK on behalf of Tempe Land Company, LLC bdp@engelmanberger.com,
kca@engelmanberger.com;bjc@engelmanberger.com;cks@engelmanberger.com

RICHARD G. PATRICK on behalf of U. S. Securities and Exchange Commission
richard.patrick@usdoj.gov, evelyn.bender@usdoj.gov;USAAZ.ECFPCivil@usdoj.gov

DAVID N RAMRAS on behalf of Silverman david@ramraslaw.com

CATHY L. REECE on behalf of Official Committee of Investors creece@fclaw.com,
clevine@fclaw.com

CHRISTOPHER SCOTT REEDER on behalf of Maryland Way Partners
creeder@sheppardmullin.com

STUART BRADLEY RODGERS on behalf of MCA FINANCIAL GROUP, LTD.
stuart.rodgers@lane-nach.com

PHILIP R. RUDD on behalf of Arizona Bank & Trust philip.rudd@kutakrock.com

DALE C. SCHIAN on behalf of AD HOC COMMITTEE OF INVESTORS IN THE VALUE-TO-
LOAN OPPORTUNITY FUND I L.L.C. ecfdoCKET@swazlaw.com,
dschian@swazlaw.com;dstephens@swazlaw.com;jlangstraat@swazlaw.com;cjess@swazlaw.com;sgoldt

ROBERT A. SHULL on behalf of Artemus Realty Capital, LLC rob.shull@mwmf.com

GERALD K SMITH on behalf of SMITH gsmith@lrlaw.com, mburns@LRLaw.com

WARREN J. STAPLETON on behalf of RIGTHPATH LIMITED DEVELOPMENT GROUP, LLC, et al wstapleton@omlaw.com, pnieto@omlaw.com

JASE STEINBERG on behalf of Marion js@mjlegal.com, wsj@mjlegal.com;bak@mjlegal.com

BRADLEY JAY STEVENS on behalf of Mortgages LTD, an Arizona corporation bstevens@jsslaw.com, dsharp@jsslaw.com;tadkins@jsslaw.com

RICHARD RAY THOMAS on behalf of Baseline & Val Vista Associates Limited Partnership rthomas@thomas-schern.com, twhitney@thomas-schern.com

TODD B. TUGGLE on behalf of Mortgages Ltd. ttuggle@jsslaw.com

DEAN C WALDT on behalf of University & Ash, LLC, Roosevelt Gateway LLC, Roosevelt Gateway II LLC and KML Development waldd@ballardspahr.com

ROBERT C WARNICKE on behalf of Americapital, LLC administrator@warnickelittler.com

LINDSI M. WEBER on behalf of Hoffland lindsay.weber@gknet.com, dal@gknet.com

DENNIS J. WICKHAM on behalf of Southwest Value Partners Fund XIV, LP wickham@scmv.com

LAWRENCE E. WILK on behalf of Martini lew@jaburglaw.com, jpi@jaburgwilc.com;amh@jaburgwilc.com

REBECCA J. WINTHROP on behalf of University & Ash, LLC, Roosevelt Gateway LLC, Roosevelt Gateway II LLC and KML Development winthropr@ballardspahr.com