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1 Sternberg Enterprises Profit Sharing Plan
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U.S. BANKRUPTCY
DISTRICT OF ARIZONA

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF ARIZONA**

<p>8 In Re:</p> <p>9</p> <p>10 MORTGAGES, LTD., an Arizona corporation</p> <p>11 Debtor(s).</p>	<p>)</p> <p>)</p> <p>)</p> <p>)</p> <p>)</p> <p>)</p> <p>)</p>	<p>In Proceedings Under Chapter 11</p> <p>Case No. 2-08-bk-07465 RJH</p> <p>MOTION TO RECONSIDER THE COURTS OCTOBER 21, 2009 MEMORANDUM DECISION AS AMENDED</p>
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14 Sternberg Enterprises Profit Sharing Plan, ("Sternberg") requests that this Court reconsider its
15 Memorandum Decision Dated October 21, 2009 and its Order dated October 27, 2009 amending such
16 decision. Because of the conflict of interest, breach of fiduciary duty, and Agency Agreement
17 interpretation issues described below ML Manager should not be granted authority to sell Sternberg or
18 any non transferring Pass-Through Investor's interest in any loan without their consent. Paragraph U of
19 the confirmation order limits the costs and expenses to the serving and collecting of ML Loans. Allowing
20 ML Manager to exercise its business judgment whether to obtain financing to cover exit costs and
21 operational expenses, and when to make charge backs allows, without specific authorization language in
22 the Reorganization Plan, ML Manger to breach the many fiduciary duties is has to such investors.

23 1 ML Manager Acknowledges that Non Transferring Pass Through Investors (NTI) Fractional
24 Share Interest are not encumbered by the loan financing. Nevertheless they are attempting to accomplish
25 the same result by (1) failing to assess portions of the Bankruptcy Costs attributable to each loan ,
26 proportionately among the fractional share holders (2) charging exit financing costs to NTI for loan
27 amounts that did not have to be borrowed in the first place or could to have been repaid quickly had
28 prompt assessments been made, (3) as described below, subjecting the NTI to the onerous provisions of

1 the exit financing loan agreement, such as requiring the sale of the fractional interest collateral or
2 providing the exit lender with priority rights to purchase the fractional interest collateral, by requiring
3 NTI interests to be sold together with the sale of the exit financing collateral. ML Manager claims to have
4 the authority do so under the “authority to sell” provisions of the Agency Agreements.(4)Contrary to the
5 express provisions of the Agency Agreement, threatening to withhold from NTI 70 % of the proceeds of a
6 sale of their fractional interest.

7 2 ML Manager concedes that no provision in the Reorganization Plan allows it to sell NTI
8 fractional interests. It therefore is relying on language of in the Agency Agreements allowing it to sell.

9 3 The language of the Agency Agreements does not and can not exempt ML Managers from
10 fulfilling its’ fiduciary duties to each of its Principals, assumed by accepting the assignment of the
11 Agency Contracts. Nothing in the Plan authorizes ML Manager to breach such fiduciary duties. The
12 agency relationship imposes on the agent the duty of utmost good faith, integrity, honesty, and loyalty in
13 agent’s transactions. *Mussleman v Southwest Realty, Inc.* 794 P2nd 814, 146 Ariz. 414. When his loyalty
14 is questioned Agent has the burden of proof to show that he did exercise the utmost good faith to his
15 principal. *Mallamo V Hartman* 219 P 2nd 1039, 70 Ariz. 294.

16 4 ML Manger has voluntarily assumed a fiduciary duty that severely conflicts with ML Manger’s
17 duty to NTI. It obligated Loan LLC’s and itself under an exit financing loan. Transferring Pass through
18 investors (TI) having exchanged their fractional interests in each loan now own interests in Loan LLC’s.
19 Each Loan LLC is obligated to repay the amount borrowed for its’ benefit. Cathy Reece has represented
20 to the court that the Loan LLC members do not have the money to pay proportionate amount of the exit
21 financing obligation. Consequently, each Loan LLC will therefore be required to sell their interest in the
22 loans in the worst of market conditions to fund the repayment of the exit financing.

23 5 Sternberg and other NTI have funds and have requested and are requesting ML Manager to
24 promptly assess them for their share of the exit costs so that they either not pay or minimize exit financing
25 expenses and costs. The assessments collected could be used at ML Manager’s discretion to repay he exit
26 financing or to pay amounts that would other wise have to be borrowed in the future. From the time of the
27 payment of the assessment by each NTI (and so longs as there is not another unpaid assessment) such
28 investor’s portion will have been paid and basic interest should stop. It is understood that there are other

1 exit financing costs that are incurred, based on the requirements of the exit loan documents. Those to the
2 extent applicable said amounts, if any, should be calculated equitably allocated and promptly assessed
3 before being borrowed. Prompt payment by NTI should result in no additional borrowing of those funds
4 for the benefit of NTI. It is recognized that calculations leading to the assessments are based on estimates
5 and estimates may be wrong. Subsequent corrective assessments could be made and paid without the
6 necessity to borrow additional funds for NTI's benefit. That initial calculations will have to be changed is
7 not a justification for the failure to make such initial calculations prompt initial assessments based on such
8 calculations. In meetings soliciting signatures on ballots approving the Plan, Plan Proponents financial
9 adviser explained to those present how payment decisions could be made by initial calculations and
10 changes by subsequent calculations. Likewise Sternberg and NTI have the ability to pay continuing
11 assessments of loan collection and loan administration costs and are hereby requesting that funds not be
12 borrowed on their behalf. ML Manager has a fiduciary duty to Sternberg and NTI to minimize the amount
13 borrowed on its behalf and the time period such borrowed amounts remain unpaid. There can be good
14 faith reason for doing otherwise. ML Manager has the fiduciary obligation to promptly make such
15 assessments. Part of the Court's Decision regarding issues 4 and 5 presents difficulties. The wording"
16 This Plan does impose that such charge back be fair, equitable and proportional, but within those
17 limitations the ML Manager can exercise his business judgment whether to obtain financing to cover said
18 exit costs and operation expenses and when to make the charge backs." It will be argued that this
19 language exempts ML Manager from the fiduciary duties described above. Moreover it ignores the
20 representations made by the Plan Proponents within the disclosure statement that NTI will not get the
21 benefit from the exit financing. Are NTI not entitled to an evidentiary hearing concerning these issues?

22 6 If all assessments are made and paid, and NTI is not legally or equitably obligated on the exit
23 financing loan why should their fractional interests be subject to an involuntary of forced sale? They
24 have no need or desire to have their factional loan interests and the fractional real estate interests they
25 acquire upon foreclosure sold for unacceptable amounts under present market conditions. ML Manger has
26 the fiduciary duty to preserve NTI collateral and not to sell NTI collateral prematurely.

27 7 To maximize Loan LLC recovery on the sale of its collateral during this forced sale period ML
28 Manger declared that it will sell each loan in its entirety including the NTI owned fractional interests.

1 This effectually subjects the NTI to the forced sale and lender's negotiation rights to purchase the
2 collateral provided for in the exit financing loan documents. ML Manager ignores its fiduciary duty and
3 requests the court sanction such activity. This sharp conflict of interest and proposed behavior by ML
4 Manger is so egregious that ML Manger should not be allowed to function as NTI agent.

5 8 This conflict of interest violates the requirement that a person will not be permitted to take on to
6 himself the character of Agent where on account of his relationship to others he would be compelled to
7 assume incompatible and inconsistent duties and obligations. *Modern Pioneers Ins. Co. V Nandin* 437
8 P2nd 658, 103 Ariz. 125. An agreement to act on behalf of a Principal causes Agent to be a fiduciary, and
9 among Agents fiduciary duties, is the duty not to act as, or on account of an adverse party without the
10 Principal's consent. *Valley National Bank of Phoenix v Milmore* 248 P 2nd 74074 Ariz. 290, *Halderman v*
11 *Gosnell Development Crop.* 748 P 2nd 1209, 155 Ariz. 585.

12 9 ML Manager and its advisors may have violated the antifraud provisions of the Federal and
13 State Securities Laws and breached their fiduciary duties by soliciting conveyances of ML Loan fractional
14 interests and issuing of membership interests in the Loan LLC's without the required full and adequate
15 disclosure. Included in what should be required for such disclosure is (a) a valuation range of each
16 applicable ML Loan (b) the collection status of each applicable ML Loan (c) a detailed analysis and
17 description of the exits costs and the exit financing and the allocation of such costs to each applicable loan
18 (d) the method and formulas of allocation of such costs to the Loan LLC's and NTI (e) the provisions of
19 the exit financing documents and how transferring and non-transferring fractional interest holders are
20 affected by such agreement(f) the provisions of the inter borrower agreement and how transferring
21 and non-transferring fractional share holders are effected by such agreement(g) the risks to and the
22 comparative risks of the transferring and non-transferring fractional interest holders and (h) ML
23 Manager's conflict of interest.

24 10 In an attempt to circumvent its fiduciary duties ML Manager refers to "authorization to sell
25 participants interest" language in the some of the agency agreements. However the conditions
26 incorporated within the provisions of a contract must be interpreted in the light of the intentions of the
27 parties at the time of the execution of the contract. Furthermore when intentions can be determined from
28 the entire instrument, the intentions shall be determined by construing the contract as a whole.

1 Cavanaugh v Schaefer 545 P2nd 102, 112 Ariz. 600. Each part of the contract must be read in the light of
2 the other parts of the contract. C & T Land & Development Co. v Bushnell 470 P 2nd 102, 106 Ariz.21.
3 Therefore the “authorization to sell” language in the agreement must be interpreted taking into
4 consideration the scope of the Agents authority under the Agency Agreement, the fiduciary obligations of
5 the agent, the disclosures made and the facts and circumstances existing at the time of the execution of the
6 agency and other agreements.

7 11 The Agency Agreements did not specifically provide Mortgages Ltd. (referred to as “ML”)
8 authority to borrow on its Principal’s behalf or to encumber its Principal’s fractional share interest in the
9 ML Loans. It was not the intention of any of the parties any such loan transaction would occur. It was
10 therefore not the intention the parties that the any fractional interest holder provide the Agent with the
11 authority to sell the holders interest against its will to repay such unauthorized loan or to accommodate
12 the repayment of such loan to the fractional shareholder’s detriment. Moreover the intention of the parties
13 must be ascertained with the assumption that the Agent must act in a manner that is not in violation of its
14 fiduciary duties described above. ML’s business practices and ML’s Private Offering Memorandum
15 disclosures are relevant. The only two circumstances are when fraction interest were sold by ML to others
16 are described in paragraphs 16 and 17 below. Such circumstances do not exist as of the effective date of
17 the Plan.

18 12 ML’s March 10, 2004 Private Offering Memorandum, (referred to as “POM”) relevant portions
19 of which are attached hereto as exhibit “A”, describes ML’s functions. (a) It originates loans and sells
20 interests in the loans to the fractional interest holders. (b) It enters into Agency Agreements with
21 investor’s, including the collection and disbursement of loan payments.

22 13 On page 8 of the POM, ML acknowledged that “MLS has a fiduciary duty to its clients and all
23 sales must be in accordance with the applicable securities laws.”

24 14 The provisions of the Agency Agreement are summarized on pages 12 and 13 of the POM.
25 Eight functions are described. The authority to borrow on principal’s behalf or to encumber principal’s
26 collateral is not included.

27 15 The last authorized function on page 13 of the POM is “Request any additional payments from
28 the holder of the Direct Deed of Trust investment for any fees, costs or expense not covered by payments

1 by the Borrower on the loan (including enforcing the loan in an event of default). In such explanation the
2 reimbursement costs are limited to those that could have been collected from the borrower.

3 16 The next paragraph on page 13 of the POM describes a circumstance when ML is permitted to
4 sell a participant's interest in the loan. "If a Borrower is being loaned funds in stages (commonly referred
5 to as "draws"), you will be required to fund such amounts subsequent to your initial purchase of the
6 Direct Deed of Trust Investment. The aggregate principal amount of the Loan will consist of both the
7 initial loan amount and the subsequent funding of "draws". Such advances are additional principal on the
8 underlying Loan. In either event the Agency Agreement permits the Company to sell all or such portion
9 of your Direct Deed of Trust Investment if you fail to make any such requested payments within three
10 business days." In practice conveyance procedures have been used to readjust the per cent of participation
11 as more funds are advanced. There were no unfunded construction draw requirements in any of the loans
12 Sternberg had an interest in. Because funds are not being solicited to fund any "draw", readjustment of
13 participation interests is not within the scope of ML Manager's function.

14 17 A second circumstance when fractional interest could be sold by ML relates to ML Loans that are
15 in default because borrowers are not current in their payments or otherwise failed to perform under the
16 loan documents. ML created a program called the "Performance Plus Program" where one group of
17 investors is formed to purchase a loan that is in default from the initial group of investors. This program is
18 referred to on Page 35 of the of Private Offering Memorandum Dated July 10, 2006 (referred to as POM
19 II") portions of which are attached hereto as "Exhibit B". The Company typically sells for its unpaid
20 principal amount any Loan that is in default in the payment of principal and interest. The program was
21 administered as an accommodation to those investors who preferred to sell their interests in defaulted
22 loans and to those investors who would take the risk for a higher interest return. These transactions
23 transpired under circumstances that ML repeatedly represented that non of its clients suffered a loss of
24 principal during the long history of the company. Authorization of the sale of Participant Fractional
25 Interest in a ML Loan at a discount was never intended.

26 18 Twenty eight pages of the POM (pages 22-45) included a detailed discussion of 45 risk factors.
27 Eighteen pages of the private offering memorandum dated July 10, 2006 (pages 9-23) included a detailed
28 discussion more than 27 risks. It is clear that ML attempted to include every known risk. Nowhere do

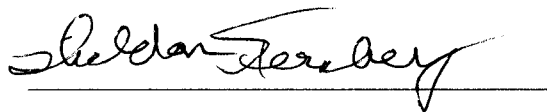
1 these documents disclose that ML had an absolute right to sell a participant's fractional interest in a loan
2 at a price that will provide a sharp discount from the amount paid for participant's investment and with
3 out the receipt of interest. No where did it disclose that Participant's fractional Interests in could be
4 encumbered with a loan that ML would be a participant in and ML could use its authority to sell the loan
5 in its entirety for the benefit of those participants encumbering their interests and to the detriment of those
6 who did not. Nor has ML disclosed in such documents the conflict of interest inherent in the claimed
7 power of sale when the agent and a number of fractional interest holders become indebted and fractional
8 interests in the loans serve as collateral. Such failure to disclose is not because of a fraudulent non-
9 disclosure in violation of the Securities laws but because it was never intended ML would have the
10 authority to sell fractional interests for purposes other than described above.

11 19 For the reasons and under the circumstances set forth above ML Manger should not be permitted
12 to sell NTI fractional loan interest without NTI consent. However ML Manager claims such right without
13 limitation. No evidentiary hearing was held. The documents executed by Sternberg and other NTI are not
14 before this court. Amendments to the Agency agreements impacting the "authority to sell" are not before
15 this court. The court has not heard the evidence impacting the interpretation of the Agency Agreements as
16 to the issues presented herein.

17 20 Because Sternberg has not participated in previous hearings concerning the agency, clarification
18 is requested as to whether any of the issues raised herein is precluded because of because it was
19 previously decided by the Court.

20 21 Paragraph U 4 of confirming order provides "Before such distributions are made, Pass-Through
21 Investors shall be assessed the proportionate share of costs and expenses of serving and collecting the ML
22 Loans in a fair, equitable and nondiscriminatory manner and shall be reimburse in the same manner as the
23 other Investors" The language of the order is clear and unambiguous. The assessment has to be related to
24 the serving and collection of the loan and not exit financing costs. As pointed out by the court no
25 evidentiary hearing was held.

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27 DATED this 29th day of October, 2009

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Sheldon Sternberg, Trustee
Sternberg Enterprises Profit Sharing Plan

Copies of the foregoing via e-mail
this 29th day of October, 2009 upon

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