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7 Counsel for the Rev Op Investors

8 **IN THE UNITED STATES BANKRUPTCY COURT**
9 **FOR THE DISTRICT OF ARIZONA**

10 In re:

11 MORTGAGES LTD.,

12 Debtor.

In Proceedings Under Chapter 11

Case No. 2:08-bk-07465-RJH

13 **MOTION FOR IMMEDIATE PAYMENT**
14 **OF IMPROPERLY WITHHELD**
15 **DISTRIBUTIONS**

Hearing Date: Not Yet Set

Hearing Time: Not Yet Set

16 (Expedited Hearing Requested)

17 AJ Chandler 25 Acres, LLC; Bear Tooth Mountain Holdings, LLP; Cornerstone Realty &
18 Development, Inc.; Cornerstone Realty & Development, Inc. Defined Benefit Plan and Trust;
19 Evertson Oil Company, Inc.; Brett M. McFadden; LLJ Investments, L.L.C.; Michael Johnson
20 Investments II, L.L.C.; Pueblo Sereno Mobile Home Park L.L.C.; Queen Creek XVIII, L.L.C.;
21 Morley Rosenfield, M.D. P.C. Restated Profit Sharing Plan; William L. Hawkins Family L.L.P.;
22 and/or their successors and assigns (collectively, the “Rev Op Investors”) hereby move this
23 Court for an order directing the immediate payment to the Rev Op Investors of funds improperly
24 withheld by ML Manager LLC (“ML Manager”) from the distributions owing to the Rev Op
25 Investors.

26 ML Manager has failed to comply with this Court’s *Minute Entry Order* of March 10,
27 2001 [DE #3110] and, to date, has not distributed the approximately \$240,000 in funds of the
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1 Rev Op Investors allegedly held in escrow.¹ ML Manager also has steadfastly refused to
2 distribute approximately \$7,992 in additional funds that are clearly owing to the Rev Op
3 Investors.

4 While the Rev Op Investors are loathe to file a motion yet again seeking to resolve what
5 should be a cut and dry matter, ML Manager has refused to have the ML Board even consider
6 this matter for several weeks or longer. The Rev Op Investors believe this matter requires
7 prompt resolution and request the entry of an order directing ML Manager to disburse the
8 amounts owing to the Rev Op Investors immediately. The Rev Op Investors also request that the
9 Court award the Rev Op Investors their attorneys' fees and expenses incurred in the preparation
10 and prosecution of this Motion and all related proceedings.

11 In further support of this Motion, the Rev Op Investors respectfully submit as follows:

12 1. On December 17, 2010, ML Manager filed *ML Manager's 1) Notice of Intent to*
13 *Distribute Proceeds in Accordance with Allocation Model, and 2) Motion to Approve Treatment*
14 *of Distribution of Disputed Proceeds* [DE #3017] (the "Distribution Motion"), which sought
15 authority to distribute net proceeds from certain property sales.

16 2. At the time ML Manager filed the Distribution Motion, ML Manager was
17 negotiating a settlement with four members of the "Rev Op Group" represented by Bryan Cave
18 LLP, as discussed in the Distribution Motion.

19 3. On or around January 6, 2011, those four members of the Rev Op Group entered
20 into a settlement with ML Manager, pursuant to that certain *Settlement Agreement*, a true and
21 correct copy of which is attached hereto as Exhibit A.

22 4. As part of the settlement, these "Settling Defendants" (as defined in the
23 Settlement Agreement) agreed to allow ML Manager to deduct approximately \$26,000 from
24 distributions otherwise owing to the Settling Defendants. Paragraph 3 of the Settlement
25 Agreement provides:

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27 ¹ To date, ML Manager has not provided the precise amount held in escrow despite multiple
28 demands.

1 The Settling Defendants agree that ML Manager shall deduct the respective
2 amount listed on Exhibit A hereto as the “Amount Withheld from Loan
3 Distribution” from any distributions on the Loan identified (the “Pro-rated
4 Settlement Amount”). The Settling Defendants and ML Manager agree that the
5 Pro-rated Settlement Amount will be used by ML Manager to cover the Settling
6 Defendants’ pro-rata portion of the Offset Claim.

7 *See* Settlement Agreement, p.3, ¶ 3.

8 5. The term “Offset Claim” is defined in the Settlement Agreement, as follows:

9 ML Manager contends that the actions of the Settling Defendants, among others,
10 have caused ML Manager to incur additional fees, costs and damages in
11 connection with its management of the Loan Portfolio. ML Manager asserts that
12 pursuant to the agency agreements, ML Manager is permitted to recover these
13 fees, costs and damages from the Settling Defendants and others that caused these
14 fees to be incurred. ML Manager contends that as of October 1, 2010, these fees,
15 costs and damages, *including the Fee Judgment* was at least \$300,474.12 (the
16 Offset Claim”).

17 *See* Settlement Agreement, p.3, ¶ K (emphasis added).²

18 6. The term “Fee Judgment” is also defined in the Settlement Agreement:

19 As part of the Bankruptcy Court action against the Settling Defendants, ML
20 Manager requested an award of attorneys’ fees pursuant to Arizona law. The
21 Bankruptcy Court awarded ML Manager its attorneys’ fees and costs in the
22 amount of \$89,364.26 (the “Fee Judgment”).

23 *See* Settlement Agreement, p.2, ¶ H.

24 7. Thus, the Settlement Agreement contemplates that the Settling Defendants would
25 pay their pro-rata portion of the fee award.

26 8. The Distribution Motion similarly contemplated that the amount withheld from
27 the non-settling Rev Op Investors would be *net* of the pro-rata settlement payments made by the
28 Settling Defendants. In the Distribution Motion, ML Manager asserted that, as of the end of
October 2010, “the fees, costs and damages incurred as a result of the litigation with the Rev-Op
Group” totaled “approximately \$336,000.” Because of the pending settlements with the four
Settling Defendants, however, the Distribution Motion requested a provision in the relevant order

² As discussed in Paragraph 8 below, the asserted setoff amount changed as time went on and more fees were allegedly incurred by ML Manager.

1 “authorizing ML Manager to deduct approximately \$310,000 from the distributions of the
2 current [non-settling] Rev-Op Group on a pro-rata basis based on first available cash.”

3 9. Thus, it is clear in both the Settlement Agreement and the Distribution Motion
4 that ML Manager intended for the Settling Defendants to pay their pro-rata portion of the total
5 asserted setoff, which included the \$89,364.26 fee award, and that the non-settling Rev Op
6 Investors would pay the remaining setoff, if any, on a pro-rata basis, *net* of the Settling
7 Defendants’ payments.

8 10. Following a hearing held on January 11, 2011, this Court approved the
9 Distribution Motion in part and authorized the distribution of certain loan proceeds from loans
10 that ML Manager had liquidated through the sale of foreclosed collateral. The Court, however,
11 ordered supplemental briefing on certain indemnification rights alleged by ML Manager.
12 Accordingly, the Court authorized payment of the fee award (net of the Settling Defendants’ pro-
13 rata payment) but ordered the balance of the asserted setoff to be placed into escrow.

14 11. Despite the settlement reached with the Settling Defendants and the relief
15 requested in the Distribution Motion, ML Manager and its counsel apparently held secret
16 intentions of paying its professionals with the distributions owing to the non-settling Rev Op
17 Investors.

18 12. At hearing on January 11, 2011, ML Manager’s counsel spoke in generalities and
19 round-number approximations regarding the amount of the fee award, but no evidence or
20 definitive numbers were provided to the Court or opposing counsel.

21 13. On January 20, 2011, the Court entered its *Order Regarding the Distribution of*
22 *Proceeds* (the “Distribution Order”).³ The Distribution Order again spoke in generalities
23 regarding the amount of disputed funds. With respect to the fee award, the Distribution Order
24 provides:

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27 ³ The Rev Op Investors have appealed the Distribution Order. The Rev Op Investors reserve all
28 applicable rights, and nothing herein shall be construed as an admission or waiver of any kind
with respect to any pending appeals or other matters.

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R. The Offset Claim includes a judgment . . . that ML Manager has obtained against the Rev-Op Group, among others, in the amount of \$89,364.26 (the “Judgment”). The Judgment is on appeal to the United States District Court for the District of Arizona, but has not been stayed.

S. ML Manager is entitled to satisfy the Judgment from distributions that would otherwise be made to the Rev-Op Group, which ML Manager has indicated that it will do on a pro-rata basis. . . .

See Order, p.7.

14. The Distribution Order is consistent with the stated intent of the Distribution Motion and the general concepts of fair, equitable, pro-rata allocation under the Plan and Confirmation Order. The Distribution Order certainly was not intended to resolve exact amounts and allocation percentages. Indeed, counsel for the parties had previously discussed the need for ML Manager to provide the “exact numbers” that would be allocated to the Rev Op Investors and the amount being segregated in escrow.

15. To that end, later on the same day the Order was entered, January 20, 2011, ML Manager’s counsel sent an email to the Rev Op Investors’ counsel regarding the actual amounts asserted by ML Manager to be included in the setoff. ML Manager’s counsel advised: “As we will soon be making the distributions, paying the judgment, and setting aside the Offset Escrow, I just wanted to run by you what we think the pro-rata calculations related to the judgment and the Offset Escrow will be. Let me know if you want to discuss this any further.” A true and correct copy of the email and attachment is attached hereto as Exhibit B.

16. The following day, Friday, January 21, 2011, ML Manager’s counsel sent a follow-up email to counsel for the Rev Op Investors providing further detail and seeking clarification regarding certain allocations. A true and correct copy of the email and attachment is attached hereto as Exhibit C.

17. Counsel for the Rev Op Investors conferred with their client representatives regarding these issues at length over the weekend of January 23, 2011.

18. The following business day, Monday, January 24, 2011, counsel for the Rev Op Investors responded to the emails from ML Manager’s counsel. The response email stated: “Attached is what we believe is the proper spread of the asserted setoff. *In particular, the*

1 *amounts asserted should subtract the pro-rata share of the settling Rev Op Investors.” See*
2 January 24, 2011 email (emphasis added). A true and correct copy of the email and attachment
3 is attached hereto as Exhibit D.

4 19. ML Manager’s counsel never responded to the email or otherwise disputed or
5 addressed the information provided by the Rev Op Investors, and the Rev Op Investors
6 reasonably believed that all of the allocation issues had been resolved.

7 20. Despite actual knowledge of the Rev Op Investors’ position, ML Manager and its
8 counsel ignored the correct allocation of the fee award and moved forward in allocating and
9 potentially even paying the Rev Op Investors’ funds to third parties in an amount greater than
10 that authorized by this Court.

11 21. During this time, the Rev Op Investors were kept in the dark regarding the
12 amounts being withheld and/or distributed to third parties. On January 18, 2011, for example,
13 counsel for the Rev Op Investors inquired regarding the accounting that would be provided with
14 the undisputed distributions due to the Rev Op Investors. ML Manager’s counsel responded in
15 an email, stating that “ML Manager is working on the form of information to provide,” but
16 “[didn’t] yet know what that will be.” A true and correct copy of the email is attached hereto as
17 Exhibit E.

18 22. The Rev Op Investors then waited for more than a month. They did not receive
19 any further information or payment of their “undisputed” funds until February 28, 2011 or later.
20 A scant “accounting” statement came even later. It contained no expense detail and very little
21 useful information.

22 23. In the meantime, the Rev Op Investors filed their *Motion for Distribution of Rev*
23 *Op Investor Funds in Escrow* [DE #3065], which sought payment of the approximately \$240,000
24 in funds that ML Manager was ordered to place in escrow, pending resolution of its asserted
25 indemnification rights.

26 24. At hearing on March 10, 2011, this Court ruled that ML Manager was not entitled
27 to offset the escrowed funds. *See Minute Entry Order* dated March 10, 2011 [DE #3110]. ML
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1 Manager equivocated at hearing regarding the precise amount in escrow, stating without
2 explanation that the amount was likely closer to \$223,000.

3 25. Subsequent to the hearing, on request by the Rev Op Investors, ML Manager
4 finally provided a spreadsheet detailing the allocation of the fee award and the escrowed funds.
5 No information regarding the amount actually placed into escrow was provided, and to date, ML
6 Manager still has not provided such information despite due demand.

7 26. On March 25, 2011, after conferring with the Rev Op Investors regarding the
8 information provided by ML Manager, undersigned counsel informed ML Manager's counsel
9 that ML Manager overcharged the Rev Op Investors for the portion of the judgment to be paid
10 by the settling members of the Rev Op Group. The Rev Op Investors also demanded the
11 immediate disbursement of the escrowed funds that ML Manager had been ordered to distribute
12 more than two weeks previously. A true and correct copy of the email from the Rev Op
13 Investors' counsel is attached hereto as Exhibit F.

14 27. In response, ML Manager's counsel advised the Rev Op Investors *for the first*
15 *time* that ML Manager believed it was not required "to deduct the amount of the settling
16 members of the Rev-Op Group from the judgment."

17 28. ML Manager later advised the Rev Op Investors that it had "been advised" that
18 the escrowed funds had been distributed. To date, however, the Rev Op Investors have not
19 received any distributions. A true and correct copy of the various email exchanges between
20 counsel for the Rev OP Investors and ML Manager's counsel is attached hereto as Exhibit G.

21 29. In sum, ML Manager has failed to comply with this Court's order of March 10,
22 2011, and has taken the position that the non-settling Rev Op Investors are jointly and severally
23 liable for the fee award, despite: (i) the clear language and intent of the Settlement Agreement;
24 (ii) the clear language and intent of the Distribution Motion; (iii) the email of January 24, 2011
25 establishing the Rev Op Investors' understanding of the issue; (iv) ML Manager's failure to
26 respond to that email, indicating its assent to the Rev Op Investors' position; and (v) the Plan and
27 Confirmation Order's requirements for ML Manager to make "holdbacks" in fair, equitable, and
28 proportional fashion.

1 30. Although undersigned counsel has repeatedly requested that ML Manager
2 reconsider its untenable position, ML Manager has refused to have the ML Board even consider
3 this issue for three weeks or longer. Accordingly, the Rev Op Investors are forced to bring this
4 matter before the Court for prompt resolution.

5 31. ML Manager has demonstrated a disconcertingly cavalier attitude with respect to
6 this Court's orders. ML Manager was instructed to distribute the escrowed funds immediately to
7 the Rev Op Investors. Now, almost three weeks after entry of the relevant order, the Rev Op
8 Investors still have not received their distributions. Indeed, the Rev Op Investors do not even
9 know the precise amount that ML Manager placed into escrow, despite repeated demands for
10 such information. The Rev Op Investors now have serious doubts that ML Manager even put
11 their funds into escrow as instructed by the Court.

12 32. Moreover, ML is not entitled to "double dip" for recovery on the fee award. The
13 Settlement Agreement with the Settling Defendants allows ML Manager to charge back
14 approximately \$26,000 of the Settling Defendants' recoveries. This amount expressly includes
15 their pro rata portion of the fee award. It would be highly inequitable for ML Manager to receive
16 a double recovery on the fee award, which is essentially what will happen absent intervention by
17 this Court. Basic notions of fairness and equity preclude this course of action, which ML
18 Manager has taken in bad faith against the Rev Op Investors.

19 33. Nor is ML Manager entitled to pick and choose the provisions of the Plan with
20 which it will comply. The bankruptcy court has broad authority to ensure compliance with the
21 terms of a confirmed reorganization plan. *See* 11 U.S.C. § 1142(b); *In re Emerald Casino, Inc.*,
22 334 B.R. 378 (Bankr. N.D. Ill. 2005); *In re Lacy*, 304 B.R. 439 (Bankr. D. Colo. 2004); *In re*
23 *Goldblatt Bros. Inc.*, 132 B.R. 736 (Bankr. N.D. Ill. 1991).

24 34. In this case, the Rev Op Investors may be charged only their "*proportionate* share
25 of costs and expenses of serving [sic.] and collecting the ML Loans in a *fair, equitable and*
26 *nondiscriminatory manner.*" *See* Plan § 4.13; Confirmation Order ¶ U (emphasis added). The
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1 targeting of a particular investor group and the concept of joint and several liability are
2 incompatible with ML Manager’s obligations under the Plan.⁴

3 35. Moreover, the fee award itself does not provide that the members of the Rev Op
4 Group are jointly and severally liable. Indeed, the members of the Rev Op Group could not be
5 jointly and severally “liable” in a declaratory judgment action, and no provision of the purported
6 contract underlying the fee award gives ML Manager any rights to joint and several liability.

7 36. In addition, Arizona law does not provide for joint and several liability for an
8 award of attorneys’ fees. Arizona has largely abolished joint and several liability altogether. In
9 the tort context—the area of law historically concerned with joint and several liability, Arizona
10 law has abolished joint and several liability by statute. The relevant provision provides that
11 “[e]ach defendant is liable only for the amount of damages allocated to that defendant in direct
12 proportion to that defendant’s percentage of fault, and a separate judgment shall be entered
13 against the defendant for that amount.” *See* A.R.S. § 12-2506. Thus, there is no legal basis for
14 ML Manager to assert joint and several liability for its attorneys’ fees.

15 37. The Rev Op Investors submit that they have been unfairly targeted by ML
16 Manager for discriminatory treatment without legal justification. ML Manager’s conduct is
17 egregious and violates its obligations under the Plan and its fiduciary duties to the Rev Op
18 Investors. In addition, ML Manager’s willful failure to comply with this Court’s orders and the
19 Plan should not be countenanced. Accordingly, the Rev Op Investors seek an award of their
20 attorneys’ fees and expenses incurred in bringing this motion and any proceedings related
21 thereto. *See* 11 U.S.C. § 105(a).

22 WHEREFORE, the Rev Op Investors request that the Court enter an order:

23 A. Directing ML Manager to make the immediate payment of all funds owing to
24 the Rev Op Investors;

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26 ⁴ Although ML Manager’s interpretation of this provision of the Plan and Confirmation Order is
27 currently on appeal, the relief requested herein does not disturb the issues on appeal. The Rev
28 Op Investors reserve all rights with respect to the issues on appeal, and nothing herein shall be
deemed a waiver or admission with respect to the appeal or any other matters.

1 B. Directing any third party, as necessary, to disgorge any funds properly
2 belonging to the Rev Op Investors;

3 C. Awarding the Rev Op Investors their attorneys' fees and expenses incurred in
4 preparing and prosecuting this motion; and

5 D. Granting to the Rev Op Investors such other relief as may be just and proper
6 under the circumstances.

7 DATED this 30th day of March, 2011.

8 BRYAN CAVE LLP

9
10 By /s/ BAS, #022721
11 Robert J. Miller
12 Bryce A. Suzuki
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15 Counsel for the Rev Op Investors

16 COPY of the foregoing served via email
17 this 30th day of March, 2011 upon:

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