

## Lenders' Analysis Of The New Loan Servicing Scheme

After reviewing all of the documents pertaining to the formation of the new loan servicer, L2L, LLC and the individual LLCs, and after very careful and thoughtful consideration and input from many Direct Lenders, we feel compelled to share with each of you the following analysis that we have made of the options which Donna Cangelosi has posed to the Lenders.

We want to begin with a reminder of the simple fact that the two documents you are being asked to sign are *legal contracts with specific consequences for you*. No matter how “well-meaning” they may seem to be, no verbal or written assurances, explanations of intent, “future developments” or the promise of the contracts “evolving” with time have *any bearing on contracts you sign*. Where the contracts you sign are vague or unclear, you are at the mercy of their interpretation by the “other” parties to the contract and/or by a Court at a later point. *Good contracts clearly define terms used*.

While we recognize that Donna and others who have assisted her in creating the new loan servicing model described in the documents have spent considerable time and energy to effectuate the new plan, each of us owes it to ourselves to be vigilant in making certain that the new plan protects our individual and collective interests. Accordingly, we have raised many questions that we encourage each of you to give thought to and require further answers to before making a final decision whether to adopt Donna's loan servicing scheme.

First, please note that we do not intend this discussion to be adversarial or disruptive to the process of substituting a new loan servicer for Compass. We are emphatically opposed to Compass' current practices and do believe Compass has violated and will continue to violate its fiduciary duties towards the Lenders. We believe that Compass, first and foremost, has a fiduciary duty to the Direct Lenders to protect the Lenders' investments and to maximize the return of the investments before taking any other collectible penalties from the Borrowers who have defaulted on the loans. However, there is mounting evidence that Compass has repeatedly thwarted the Borrowers' ability to repay 100% of the principal and interest due the investors by insisting that Compass also recover a 100% of the default and late fees, where it may not have been financially feasible for the Borrower to repay all such charges. Consequently, Compass recently instituted foreclosure proceedings on 21 loans. In many if not all cases, and in further breach of its fiduciary obligations, Compass never advised the Lenders on those loans that such measures would be taken nor if the Borrowers had offered any settlement which may have been preferable to the Lenders than facing the uncertainty of a foreclosure action.

For all these reasons, and in the absence of Compass modifying its negotiation tactics with the Borrowers and continuing to jeopardize the return of the Lenders' investments, we do believe that the Lenders' decision to terminate Compass was meritorious.

However, we think that all Lenders who authorized Donna Cangelosi to terminate Compass had the collective understanding that they were also giving her a mandate to seek out and retain an existing, licensed, experienced, ethical substitute loan servicer. It was the Lenders' expectation that any such loan servicer would conduct its work on behalf of all Lenders under a single loan servicing agreement by which all terms would have equal force and effect on all parties to the contract.

Contrary to such expectations, Donna unilaterally and arbitrarily created a new entity, the so called "L2L, LLC" as the substitute loan servicing organization. The entity was in name only; it was neither staffed, or housed in any location, or operating. More importantly, because it was in name only, it was not licensed to conduct loan servicing. Donna drafted a loan servicing agreement, "Loan Management Agreement", that contained amongst other terms, compensation and costs that would be shared by the Direct Lenders and L2L, LLC.

Concurrent with the creation of L2L, LLC, Donna created and registered LLCs for each group of Lenders on any existing note. Pursuant to the terms of the LLCs, compensation and costs to be shared by future members of the LLCs would be materially different than those compensation/cost obligations set forth in the L2L, LLC. Specifically, any default and late fees collected by L2L, LLC would be paid only to the L2L under the terms of the Loan Management Agreement, and none to the Lenders, but under the LLCs, 100% of the collected default fees and late fees would be disseminated to the LLCs by L2L, LLC and then shared between the managers of the LLCs and the members of the LLCs. Moreover, under the terms of the Loan Management Agreement, the Lenders would be responsible for 100% of all costs associated with collecting on the defaulting loans, as well as 4% service fees on all collected proceeds, paid to L2L, LLC, but under the LLCs, members would only be charged 1% of their capital investment for a purported "legal fund".

Undoubtedly, from the above discussion, a Lenders' class system has been established with inherent inequities between the two classes.

We cannot countenance such an outcome. Intuitively, all Lenders should be alarmed that Donna has not only far exceeded her authority to seek a substitute loan servicer but is now subjecting the Lenders to having to make a choice between joining one of two classes with disparate consequences.

We urge you to read both the Loan Management Agreement and the LLC Operating Agreement and realize for yourselves the distinct differences and question whether Donna's actions should be the basis for rejecting the new loan servicing scheme.

**Notwithstanding the above, we move on to a detailed analysis of the LLC Agreements.**

We have learned through Donna's recent report that many of you in multiple loans have already chosen to transfer the ability to exercise your rights under the loan servicing

agreements to another party, the FDH Management Company – a party that little is known about.

We understand the absolute frustration of all the Direct Lenders, abused and ill-informed by USA, robbed by USA, abused and ill-informed by Mesirow and believing that Compass has been merely a continuation of all that has come before.

But given how willing Lenders have been to jump into another situation without the benefit of more information, we have to ask ourselves--have we learned nothing from the USA debacle? We signed documents relying not on what the documents said, but “assurances” from USA. We had more than ample opportunity to research USA’s principals – we just didn’t do it. This website contains publicly available press coverage on these individuals for several years prior to the bankruptcy. Had we read those articles before investing, we never would have invested with the company. Of course we didn’t read the articles; just like most of the “clients” of USA.

But we fear that with so little information being provided now relative to the new Managers-FDH- and the possible Board Members that will be selected by Donna, that the Lenders may possibly find themselves as frustrated under the new system with how those Managers intend to manage the LLCs. Let’s begin with the very concept of the LLC arrangement as proposed. *When you transfer your interest in a trust deed to ownership in an LLC, you are forever giving up the protections afforded by the Loan Servicing Agreement.* There is no question that the USA supplied Loan Servicing agreements are flawed, but they do provide you with specific rights, including the right to consider and approve changes.

As a minority member of an LLC, it appears that you will have almost no ability to effect the direction of the company, *especially* in the proposed arrangement in which you permanently give a management company authority to make *all* the decisions. Although each LLC is set up with a member board, the board is powerless – all decisions rest with the management company of whom we know nothing

Ask yourself this question: if you become unhappy with the actions of the management company, is there a provision to remove them? Likewise if you become unhappy with the LLC, is there a provision allowing you to convert back? The simple answer to both questions is “no”.

Now ask yourself “Who is FDH Management Company, LLC (the management company)?”, “Who are the principals?”, “What’s their experience?”, “What’s their track record?”, “Are they honest?” Now ask yourself “Who is Lender 2 Lender, LLC (the loan servicing company)?”, “Who are the principals?”, “What’s their experience?”, “What’s their track record?”, “Are they honest?” To the degree either of these companies intends to “outsource” their duties, who makes the decisions on “outsourcing” and what do you know about the “outsource” entities and the acumen of the person selecting the outsourcing entities. Have you been given answers on any of these questions? How do you know what you’re signing up for? History, they say, has a habit of repeating itself.

First off, we know nothing about the individual or individuals pushing this effort – we know nothing about the management and servicing companies – we don't even know if either of these entities is licensed by the State of Nevada. But a little simple research and a thorough examination of the documents accompanying the LLC proposal can tell us a great deal to answer all these questions.

First let's look at the Nevada Secretary of State's website. Although there is no FDH Management, LLC registered, there is a FDH Resolution, LLC. Lender 2 Lender, LLC (L2L) ([click here](#)) and FDH Resolution, LLC (FDH) ([click here](#)) both were registered on May 16, 2007 and have the same registered agent: The Law Offices of Alan R. Smith. The numerous loan LLCs were formed on May 2, 2007 ([click here](#)) and naturally also have the same registered agent. Neither these filings nor the documentation we have been supplied explain the beneficial ownership of either L2L or FDH. While this omission may not seem important on the surface, we'll come back to it. But keep this in the back of your mind: the lack of full and forthright disclosure was part and parcel in USA Capital's dishonesty.

Going back to the question of licensure, it is impossible that either of the entities could be licensed – the companies are only two weeks old.

Let's look at the most meaningful of the documents that have been presented to us – the Management Agreement and LCC Operating Agreement. It's probably best to have copies of both in front of you – we will refer one to the other. We'll start with the LLC Operating Agreement.

Initially we'll start with Section 2.5 Limitations of Liability of Members. The section is superfluous because the very nature of a limited liability company limits your exposure to the amount you invest. Let me re-word this: by committing to convert your loan to equity (ownership) in an LLC you become a member and you are putting your *entire* loan at risk.

Section 3.1 Management of the Company appoints FDH Management, LLC (FDH Resolution, LLC?) as the manager of the company. Section 3.2 creates a Board of Members. Carefully note that they are put in place to *advise* the manager, not *direct* the manager; not control the manager. Effectively the Board of Members has *no power* to exercise *any* control over your investment. Similarly Section 8 of the Loan Management Agreement (Power of Attorney) gives L2L permanent Power of Attorney. There is no provision for canceling or superseding the Power of Attorney.

Next let's look at Section 5.1 Additional Members. The agreement tells you if you don't join by June 10<sup>th</sup>, you will be required to pay an additional \$1,500 processing fee “for the administrative fees, recording fees, legal fees and other costs”. \$1,500 is considerably more than the actual cost of adding a member. Is the Direct Lenders' desire to avoid an additional cost, like the June 10<sup>th</sup> deadline intended to encourage Direct Lenders to jump without thinking (again)?

Article VII – Leveraging the Beneficial Interests permits the manager to borrow money against your investment as may be required by the administrator. *What administrator?* There is no other reference to an administrator in any of the documents. Perhaps a full and complete disclosure is again in order?

The second sentence states, “This credit facility would be used primarily, *but not exclusively* to fund the Company’s...”[emphasis added] It would be more honest to state that the manager could establish a credit facility for whatever reason he/she/they desire.

Although the credit facility is not to exceed 10% of the total beneficial interests (beneficial interests as a term, used throughout these documents that is also never defined) your total investment can be put at risk (“pledged” and subordinated) to underwrite a loan – a loan that the manager can use for any purpose (“other property related expenses”).

The last line second paragraph of this article is also revealing: “without further approval from the members”. Once this agreement is signed, there is *no* approval of *anything* allowed by the members – there is no member input. Why add this phrase to the document but to suggest otherwise and confuse Direct Lenders?

The last sentence of the third paragraph of Article VII should certainly be a warning flag “This credit facility is *intended* to be repaid *primarily* from loan payoffs [emphasis added].” In other words, repayment can also come from your investment or from a cash call.

Finally there is no provision for dissolution (except when the loan is repaid) – you’re stuck without any say, with a powerless Board of Members – your “investment” is controlled by whom?

We will come back to Article 1, Section 2.1 Capital contributions and Article VIII – Distributions of Profits. But first we should look at the Loan Management Agreement.

The Loan Management Agreement should probably more properly be titled Loan Servicing Agreement because that what it does and that’s what it replaces. Taken together however, this document and the LCC Operating Agreement lock you in and put your entire investment at extreme risk. Read on.

Under Section 1 (Duties and Powers of L2L) 51% of the beneficial interests (again not defined) authorize L2L to assist in arranging additional financing, subordinate the loan, reduce or eliminate accrued interest, late fees, default interest, reduce principal balance, etc., etc. **(Under the current USA/Compass LSA each Lender must give its consent to allow the Borrower to pay back less than 100% of the principal and interest).**

Bear in mind that in most of these loans, you have already provided Donna Cangelosi with 51% or more of your Powers of Attorney. So were all the Direct Lenders to

exchange their Trust Deeds for LLCs ownership thereby accepting these terms, and assuming that Ms. Cangelosi controls both FDH and L2L, you have given her absolute control of how many hundred million dollars of your savings? Remember once you're a member you cannot change or have any effect on the direction of the LLCs, FDH or L2L.

Now look at the Termination rights (of just the Loan Management Agreement) in Section 4 of the Loan Management Agreement can only be exercised by Ms. Cangelosi – for only she has 51% of your Powers of Attorney.

It should be further noted that if she terminated L2L, L2L would be entitled “to 1/12 of the asset disposition fee per month, up to a maximum of (12) months, for each month in which it provided services under this Agreement.” Let’s math that out – after a year servicing, L2L stands to collect 3% of your investment during the following year. So hypothetically, was there \$500,000,000 in loans outstanding, after a year L2L would be entitled to \$15,000,000. You dislike USA’s greed or consider Compass’ self serving? Is the new compensation scheme truly a fairer arrangement?

Although Section 2 (a) of the Loan Management Agreement requires L2L to make reports, keep records, and make distributions, Section 9 (Release and Indemnification) and Section 10 (Loan Documentation) pretty much provides an “Get Out of Jail Free” if they don’t. We wonder if Compass has experienced any of these same problems.

Now we have to bring both agreements together to find out how much this proposal will cost you.

Initially, of course the LLC Operating Agreement segments 1% of your investment into a legal fund to be used “...at the discretion of Manager...”

Switching to the Loan Management Agreement Section 3 (Compensation to L2L) there is, of course an “annual fee” (really loan servicing fee) of 1%.

Next this same Section calls for a 3% disposition fee. Note this fee is based on “actual proceeds recovered”, not net proceeds collected. So rather than paying 3% service fees under the USA/Compass LSA calculated from the amount of principal investment you have each made in each of your loans, the new scheme could be interpreted to be based on all proceeds collected including default and late fees. Further, this fee is collected before accounting for legal fees, taxes of foreclosed properties, foreclosure costs, management fee, etc.

Subsection (d) calls for “L2L shall receive all late fees and default interest due and recovered under the terms of the loan.” provided “all Lenders have received all principal and accrued interest due to them”. Going back to the LLC Operating Agreement, under Article VIII Section 8.2, default interest received by the LLC is split 50% to the manager (FDH) and 50% to the Members. Presuming all principal and accrued interest is paid, there would be nothing to split since L2L is to receive the default interest. Is this provision included in the LLC Operating Agreement so the casual reader will *think* they

have an upside? It may come to be that Compass is entitled to default interest (they did purchase it at auction) and late fees. If so assume it is paid first to L2L and then to Compass, has L2L then collected all default interest and is therefore entitled to payment as well?

Article VIII of the LLC Operating Agreement next calls for the Manager (FDH) to receive 30% of “Legal Recovery”. Again, the terms “Legal Recovery” isn’t defined, but assume it means any funds that have to be recovered via legal action. This could mean the proceeds of a foreclosure, proceeds from a personal guarantee or proceeds from actions against the principals of USA Capital. Going back to Section 3 (c) “L2L shall be entitled to recover from any proceeds collected on the Loan, all attorneys’ fees advanced by L2L which are associated with necessary litigation.” In other words, all the attorney fees will come out of your investment AND you will be paying 30% of the “Legal Recovery”. Unbelievable, isn’t it?

Article VIII of the LLC Operating Agreement next calls for a shared distribution of “Other Fee’s Collected” (meaning, we’re sure ‘Other Fees Collected’) between the Manager (FDH) and the Members. Once again “Other Fee’s Collected” is not defined. But *what* other fees? Didn’t Compass purchase the rights to uncollected origination fees, extension fees, exit fees and success fees? There doesn’t appear to be an upside here either.

Section 5 of the Loan Management Agreement allows L2L to delegate (outsource) most of their duties. In Section 12, L2L is to be reimbursed “the out-of-pocket expenses incurred”. Simple question: In the absence of verbiage to the contrary, are outsourced services classified as out-of-pocket expenses? If so, you’re paying almost all the overhead, while the owners of L2L reap huge fees – and you thought Mesirow and the bankruptcy fees were outrageous?

Now let’s return to the LLC Operating Agreement. Article VII (Leveraging the Beneficial Interests). This section, as we’ve said, permits the manager (FDH) to borrow money against your investment. The beauty of this Article, in many Direct Lender’s eyes is that in casual reading, there wouldn’t be cash calls – the loan would cover all the costs. Beautiful, eh? No, not at all. And for a variety of reasons.

First the assumption is that such a loan could be obtained. Pardon the pun, but we wouldn’t bank on it. This is especially true if your loan is a second. If there is no loan, guess what – cash calls! And don’t forget if you can’t pay (or the LLC can’t fully pay), the interest rate assessed the advances after ten days is at the same rate as your loan (Loan Management Agreement, Section 12) whether or not (probably not) the loan is performing.

Assume now that a loan is available. The interest rate the LLC is paying further taps into the value of your membership interest – you are actually paying the interest. Additionally should all the costs exceed the loan maximum of 10% or beneficial interests? You’re right, cash call.

When you consider the probable costs of these agreements, you have to wonder in whose interest it is to have the arrangements in place. Again, who owns L2L and FDH? We understand the need to provide an incentive negotiators and workout experts, but there's a limit to how much cash you can or should spread around.

The actual truth is that most of these loans are not only in default, but severely under water – many they aren't worth what has been loaned against them. It is *easily* conceivable that the fees associated with these agreements could eat up most of our loan value – even on the best of loans.

For now, we think that all of the above issues require careful scrutiny by the Lenders.

We hope that the above has given you reason to pause before executing the documents (contracts). If you agree with our concerns and you believe more information and clarity is absolutely necessary, we encourage you to draft your own questions to Donna, or adopt this discussion as your own, and compel her to give you the answers you deserve so that you can make an informed decision as to what action you will take to protect your own interests.

***Alternatively, if you feel that you have been misled and wrongfully induced to join the LLCs in the absence of sufficient information, and consequently placed in an untenable situation, you have every right to rescind any agreements that you have previously signed by putting Donna on notice of same with instructions that she modify the scheme that addresses the above defects in the existing Agreements.***

Remember, those of us who signed the Election to Terminate Compass and Substitute a New Loan Servicer did so with the understanding that Donna would act as our "fiduciary" and seek out the most qualified and ethical experienced loan servicer who could handle this troubled portfolio. We should expect nothing less at this time.