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Jan. 23, 2007

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USA Capital dissidents follow wrong protocol, judge decides

By [JOHN G. EDWARDS](#)
[REVIEW-JOURNAL](#)

A federal judge on Monday voided a decision by an appellate bankruptcy court panel and told a dissident investor group to first ask the bankruptcy judge to freeze the \$962 million USA Capital bankruptcy case while it is being appealed.

U.S. District Judge Robert C. Jones overturned the action of a bankruptcy appeals panel that last week stayed the bankruptcy case until Feb. 20.

Jones said the panel "improvidently granted" the stay. The federal judge also directed attorneys for the dissident investors to ask Bankruptcy Judge Linda Riegler to rule on whether to grant a stay and whether to require the appealing parties to post a bond.

Riegler, who presides over the USA Capital case, will hold a hearing on the stay at 3:30 p.m. Wednesday. Jones said he could hear a possible appeal of Riegler's decision the following day.

During Monday's hearing, attorneys for the bankrupt estate of USA Capital said they feared the stay could derail the planned \$67 million sale of some USA Capital assets and the right to provide loan servicing on USA Capital brokered loans to Compass Partners of New York.

The "drop dead" date is Feb. 16, meaning that Compass could walk away from its agreement if the sale were delayed four days, they said.

Attorney Alan Smith, who represents 400 investors in USA Capital, said he

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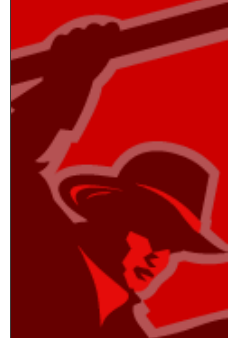
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and attorney Janet Chubb, who represents other dissident investors, intend to appeal to Jones if they are not satisfied with Riegle's decision on Thursday.

Riegle previously said she would deny the dissident investors' request for a stay. But then she decided the dissidents should first present their arguments to her before she decided on the stay.

Instead of presenting the arguments to Riegle, Smith and Chubb obtained a temporary stay from the bankruptcy appeals panel, which attorneys for USA Capital argued was the wrong place to file the initial request for a stay.

Smith told the federal judge that he was not trying to stop work on the USA Capital bankruptcy case while the stay was in effect.

Smith said the stay only applied to \$40 million in investor money that Compass does not want to buy.

The Jan. 17 decision by the appeals panel does not specifically limit its stay to that money, ordering that USA Capital maintain the "status quo" while the stay was in place.

USA Capital, a private money lender, solicited investments from individuals for fractional interests in short-term mortgage loans that were secured by real estate. Investors were attracted by high interest rates, typically around 12 percent, that they could earn on the so-called trust deed loans.

When borrowers stopped paying on mortgage loans, however, USA Capital continued paying interest and principal on loans as if the past-due borrowers were current. Then, it became insolvent and filed for bankruptcy court protection in April. It was controlling investments made by about 6,000 investors around the country.

Riegle required the interim managers of USA Capital to withhold payments to investors whose loans were past due until enough money had been retained to offset the money they were paid on loans that were not being repaid.

Smith said Riegle should have required USA Capital to file a lawsuit in bankruptcy court to keep that money, but he said no lawsuit was filed. Riegle approved a plan with provisions calling for USA Capital to keep the overpayment amounts for nonperforming loans.

"If that money is spent, I can't see any mechanism for (the dissident investors) to recover that money," Smith said.

Donna Cangelosi, one of the investors making the appeal, said the opposing attorneys were using "strong-arm tactics," threatening to punish those who did not agree with the compromise reorganization plan for USA Capital.

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