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UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF ARIZONA

In re:
MORTGAGES, LTD.,
Debtor.

CASE NO. 2:08-bk-07465-RJH

CHAPTER 11

**RESPONSE TO MOTION FOR ORDER
OF DISCHARGE OF ORIGINAL
TRUSTEE AND FOR RELEASE OF
TRUSTEE'S BOND**

The ML Liquidating Trust, (hereafter the "Trust"), by and through undersigned counsel, hereby responds to the Motion For Order Of Discharge Of Original Trustee And for Release of Trustee's Bond, filed by the Original Liquidating Trustee, Kevin O'Halloran, (hereafter "O'Halloran"), and asks that the Motion be denied in its entirety for the reasons set forth in the Memorandum of Points and Authorities supporting this Response.

Memorandum of Points and Authorities

I. Procedural Facts:

O'Halloran served as Trustee of the ML Liquidating Trust established by the confirmed Plan in the Mortgages Limited bankruptcy. He resigned as Trustee and Matthew Hartley has been appointed as his successor as of December 3, 2010.

O'Halloran has requested an order relating to his resignation and replacement that has three elements.

(1.) Discharge of any and all claims that might be asserted by any party against him arising out of his service as Liquidating Trustee and Chief Executive Officer and President of ML Servicing Co., Inc., the Reorganized Debtor, or

1 (2.) Alternatively, requiring the ML Trust Board to escrow the sum of One Hundred
2 Sixty Thousand Dollars (\$160,000.00) to be used solely for paying the renewal premium on
3 Director and Officer insurance policies now in force.

4 The foregoing is stated as an alternative seeking that one of the two be granted.

5 (3.) A release of the bond procured by O'Halloran at the expense of the Trust as required
6 by the ML Liquidating Trust Agreement.

7 In support of his Motion O'Halloran provided confidential information about the
8 financial status of the Trust that the Trust disputes.

9 **II. Disputed Facts;**

10 The Liquidating Trust Has Adequate Cash Flow and is not illiquid as O'Halloran asserts.
11 While the liquidity of the Trust is not relevant to the Motion in any respect, the filing of a Motion
12 containing false information requires a firm rebuttal because of the potentially adverse impact of
13 the dissemination of such false information. Already, within ten days of the filing of
14 O'Halloran's Motion it has been cited by an opponent to the Trust in pending legal proceedings
15 and, at a minimum, creates additional attorney's fees for the Trust in rebutting the
16 misinformation.¹¹

17 Specifically, O'Halloran falsely alleges that *"Based on the financial condition of the*
18 *Trust, ...the Trust will not have sufficient resources to pay renewal premiums for the Insurance*
19 *Policies in June 2011 when they come due."* He then analyzes, supposedly, the cash flow
20 situation concluding that the "illiquidity" of the trust renders it incapable of meeting its
21 obligations.

22 The Declaration of Matthew Hartley, successor Trustee to O'Halloran, attached as
23 Exhibit A hereto, disputes O'Halloran's statements and affirms that Hartley has concluded that
24 the assets and borrowing sources appear more than adequate to cover the cash flow expenses of
25 the Trust. The Trust is not "illiquid" as alleged in O'Halloran's Motion.

26 Moreover, the Declaration states that O'Halloran, himself, explained the entire financial
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1 circumstances of the Trust to Hartley when Hartley inquired before Hartley agreed to serve as
2 Trustee. Hartley sought to assure himself that there were sufficient assets and sufficient cash
3 flow resources to properly carry out his responsibilities over the term of the Trust. O'Halloran
4 assured Hartley that the Trust had adequate cash flow to cover its expenses over its anticipated
5 term and that it was not illiquid. These assurances were made only a little more than a month
6 before O'Halloran's Motion was filed.

7 **III. Request (1): O'Halloran Is Not Entitled To A Release Greater Than Provided In The**
8 **Plan And Liquidating Trust Agreement:**

9 O'Halloran's Motion asks that the court order him to be released from "any and all
10 claims that might be asserted by any party against Mr. O'Halloran". As authority for this request
11 he relies upon Paragraphs 16 and 17 of the Liquidating Trust Agreement and Section 10.1 of the
12 Plan. However, granting such a broad discharge to Mr. O'Halloran that discharges his liability to
13 "any party" seems inappropriate and of doubtful legal effect without such persons being before
14 the court. Moreover, O'Halloran misinterprets what the Liquidating Trust Agreement says he is
15 entitled to have.

16 First, O'Halloran quotes from Paragraph 16 even though it appears that Paragraph 15,
17 **Liability of the Liquidating Trustee**, is the Paragraph of the Liquidating Trust Agreement that
18 was obviously intended to define the Trustee's liability. It makes no difference, however, since
19 Paragraph 15 and 16 use the same key language quoted in his Motion. However, it should be
20 recognized that the quoted language relied upon by O'Halloran says that the Trustee shall have
21 no liability "*...to any holder of a claim...*".

22 The meaning of the phrase "*any holder of a claim*" can be found in the definitions set
23 forth in Liquidating Trust Agreement. Two kinds of claims are defined in Paragraph 1,
24 **Definitions**; one is an "Allowed Claim" in the bankruptcy case and another is a "Disputed
25 Claim" in the bankruptcy case.

26 This key language quoted and acknowledged by O'Halloran in his Motion limits his
27 protection to liability asserted by holders of a claim in the bankruptcy proceeding upon becoming
28 Trustee; it does not immunize O'Halloran by granting some sort of license to commit future

1 tortious acts against third parties with whom he may later deal with as Trustee. Likewise, it does
2 not say that the Trustee shall have no liability **to the Trust** for breach of his duties as Trustee;
3 moreover, it clearly contemplates that he not be discharged from liability to the Trust because
4 Paragraph 24 requires him to post a bond assuring payment of such liabilities. Yet, O'Halloran
5 requests the court to release him from "any and all claims that might be asserted by any party
6 against...Mr. O'Halloran." The plain language as defined in the Liquidating Trust Agreement
7 only protects O'Halloran from claims made by claimants in the bankruptcy proceeding, a
8 reasonable precaution upon creation of the Liquidating Trust.

9 Since the Liquidating Trust Agreement is the instrument O'Halloran relies upon, the
10 making of the requested Order requires other authority not cited by O'Halloran. No such
11 authority exists. While an Order using the language of the Liquidating Trust Agreement would
12 be redundant, Respondent has no objection to an Order acknowledging that O'Halloran has been
13 discharged of further duties as Trustee and that he continues to enjoy the protections and
14 immunities set forth in the Liquidating Trust and Plan.

15 **IV. Request (2): O'Halloran Is Entitled To Indemnification By the Estate, Not To**
16 **Insurance:**

17 O'Halloran asserts that Paragraph 17 of the Liquidating Trust Agreement provides that he
18 is entitled to be indemnified for matters incurred by reason of being employed by the Trust. This
19 is a "red herring" that has nothing to do with whether or not the Trust must buy insurance. There
20 is no dispute about the Liquidating Trust Agreement providing for indemnification for certain
21 acts. The question is whether the Liquidating Trust Agreement requires third party insurance
22 instead of recourse to the Trust assets at such later time as something might arise.

23 Of course, O'Halloran acknowledges that the Trust has such insurance that is now in
24 effect. He also asserts that he knows of no potential claims. Under such circumstances a
25 demand to escrow funds for such a future event is overreaching.

26 Moreover, the successor Trustee and Board presently intend to continue some sort of
27 adequate Directors and Officers insurance after the current expiration date and such a policy will
28 surely protect O'Halloran, too. However, whether to do so, the amount of the policy and its

1 terms are matters properly within the authority of the successor Trustee and the Board. This is a
2 business issue to be determined at a point in time closer to the expiration of the current policy.
3 Importantly, Paragraph 17 says nothing about having to purchase insurance relating to the
4 obligation of the Trust to Indemnify.

5 It is interesting that O'Halloran asserts that he knows of no claims against him but wants
6 insurance to be purchased in case any arise that he does not know about. Yet, he wants the Trust
7 to be ordered to release its now unknown claims against him when it is only O'Halloran who
8 might know of circumstances that may create such claims.

9 **IV Request (3): Release Of The Performance Bond Is Premature**

10 In a Chapter 7 bankruptcy, a trustee has the general duties of gathering the estate assets,
11 liquidating them, distributing the proceeds to creditors, and closing the estate. *See* 11 U.S.C. §
12 704(a). Trustees are required to use reasonable diligence in exercising these duties. *See* United
13 States v. Shaddock, 112 F.3d 523, 531 (1st Cir.1997). Thus, a trustee can face personal liability
14 for failing to reasonably carry out their duties. *See* In re Gorski, 766 F.2d 723, 727 (2d Cir.1985).
15 Indeed, a trustee can be held personally liable based on negligence alone. *See* Id.; *see also* In re
16 Cochise College Park, 703 F.2d 1339, 1357 (9th Cir.1983).

17 11 U.S.C. § 322(d) provides for a two year statute of limitations for causes of action
18 brought against a bankruptcy trustee's bond, commencing upon the date the trustee is discharged.
19 Thus it appears that O'Halloran is not entitled to the discharge of his bond but merely to an order
20 confirming that he has been discharged from his duties as of the date the Successor Trustee was
21 appointed. His bond would then be discharged by operation of law after two years.

22 This also makes sense because any liability under the bond that O'Halloran was to post
23 assuring performance of his duties would not ordinarily be expected to appear until much later in
24 the life of the Trust, not within a month or two of a successor Trustee being put in place.
25 O'Halloran asserts in a footnote that the Board has had the opportunity to investigate his
26 performance. In fact, this is the sort of inquiry that the Successor Trustee would conduct in the
27 performance of his duties over a period of time. No document explaining and listing his
28 decisions and actions to pursue or forego legal proceedings on causes of action has been filed.

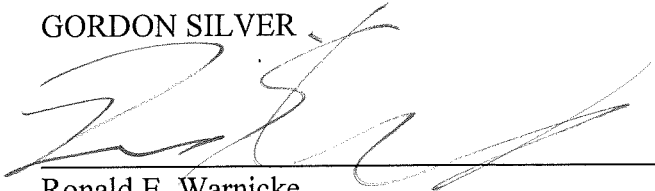
1 Likewise, no outside audit of Trust finances has been conducted. There is no basis for
2 O'Halloran stating that he should be discharged of liability, (as opposed to discharged from his
3 duties,) merely because the Trust does not yet know of any delinquencies in performance.
4 Although there is currently no indication that there are any claims, the court would be acting
5 prudently to allow adequate time to pass to survey the situation instead of granting a Motion with
6 so little legal authority.

7 **VI. Conclusion**

- 8 1. O'Halloran is only entitled to a Release confirming the liabilities from which he is
9 insulated by the Liquidating Trust Agreement and the Plan so O'Halloran should
10 not be granted the fulsome release requested.
- 11 2. O'Halloran is not entitled to have the Trust ordered to purchase insurance and
12 certainly not to have funds escrowed.
- 13 3. The Bond should not be released or discharged.
- 14 4. The Trust is not "illiquid" and no action should be predicated upon such a
15 misstatement

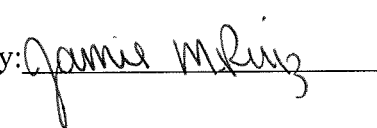
16 Dated this 28th day of January, 2011.

17 GORDON SILVER

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24 COPIES sent via the U.S Bankruptcy
25 Court's ECF noticing system this
26 28th day of January, 2011.

27 COPIES served by email on the
28 Individuals listed below this
28th day of January, 2011.

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The undersigned certifies that a copy
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11 **UNITED STATES BANKRUPTCY COURT**
12
13 **FOR THE DISTRICT OF ARIZONA**

14 In re:

15 MORTGAGES, LTD.,

16 Debtor.

Chapter 11

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

Declaration

17 STATE OF ARIZONA)
18) ss.
19 County of Maricopa)

20 I, MATTHEW HARTLEY, based upon my personal knowledge, declare:

21 1. On December 3, 2010, I replaced Kevin O'Halloran as the duly appointed
22 Liquidating Trustee for the ML Liquidating Trust (the "Trust").

23 2. In or about November, 2010, I discussed with Mr. O'Halloran more than once
24 the finances of the Trust including whether the Trust had adequate funds to pay the costs of
25 administering the estate. During each discussion Mr. O'Halloran assured me that the Trust
26 had more than enough resources to pay its obligations.

27 3. After becoming Liquidating Trustee, I investigated the financial situation of
28 the Trust and confirmed that the Trust has adequate finances to pay its obligations, including
the payment of general liability insurance, director and officer liability insurance, and the
cost to pursue the various lawsuits against parties to which the Trust holds claims against.

Exhibit A