



Hon. Linda B. Riegle  
United States Bankruptcy Judge

**UNITED STATES BANKRUPTCY COURT  
DISTRICT OF NEVADA**

\*\*\*\*\*

In re: )  
          ) Case No. BK-S-06-10725-LBR  
USA COMMERCIAL MORTGAGE )  
COMPANY, ) Case No. BK-S-06-10726-LBR  
                                  ) Case No. BK-S-06-10727-LBR  
                                  ) Case No. BK-S-06-10728-LBR  
                                  ) Case No. BK-S-06-10729-LBR  
                                  ) Debtor. )

In re: )  
          ) USA CAPITAL REALTY ADVISORS, LLC )  
                                  ) Debtor ) Chapter 11

In re: )  
          ) USA CAPITAL DIVERSIFIED TRUST )  
DEED FUND, LLC )  
                                  ) Debtor ) Jointly Administered Under  
                                  ) Case No. BK-S-06-10725

In re: )  
          ) USA CAPITAL FIRST TRUST DEED )  
FUND, LLC )  
                                  ) Debtor ) Date: June 20, 2007  
                                  ) Time: 10:30 a.m.

In re: )  
          ) USA SECURITIES, LLC )  
                                  ) Debtor )

Affects: All Debtors

1                   **ORDER ON EMERGENCY MOTION TO ENFORCE CONFIRMATION**  
2                   **AND FOR SANCTIONS AND ORDER ON**  
3                   **SUBJECT MATTER JURISDICTION**

4                   Compass Partners (and its affiliates and designees) was the purchaser of loan servicing  
5 rights from the debtor under an asset purchase agreement pursuant to a confirmed plan of  
6 reorganization. On May 25, 2007, Compass USA SPE LLC, and Compass Financial Partners  
7 LLC (together “Compass”) filed an emergency motion for this court to enforce its confirmation  
8 order and for contempt (“Motion to Enforce Confirmation,” Docket # 3773). In its Motion,  
9 Compass states that Ms. Donna Cangelosi and others (collectively referred to as the “Lenders  
10 Protection Group”)<sup>1</sup> seek to wrongfully terminate Compass as the loan servicer and take for  
11 themselves the servicing rights and fees. The Motion to Enforce Confirmation alleges that the  
12 Lenders Protection Group mailed at least fifty letters to borrowers of loans stating that Compass  
13 was not authorized to act on behalf of the lenders and that “all payments made to Compass  
14 would be made at your own peril.” The letters directed borrowers to make all payments to  
15 “Lender 2 Lender, LLC,” a Nevada limited liability company established by Ms. Cangelosi.  
16 Compass argued in its Motion to Enforce Confirmation that these acts were a direct violation of  
17 the asset purchase agreement with the debtor and the confirmed plan, as well as a collateral  
18 attack on the provisions of this court’s orders. The “debtor” filed a joinder to the motion.  
19 (Docket 3999.)

20                   The motion was opposed (Docket 3853) on the stated grounds that the members of the  
21 Lenders Protection Group had terminated Compass as the servicer on each of the loans in  
22 accordance with the loan servicing agreements and that it had the right to do so without notice  
23 and without cause. Alternatively, the Lenders Protection Group contended that if the loan  
24 servicing agreements required cause to terminate Compass as servicer, then they had the cause to

---

25  
26                   <sup>1</sup>Ms. Cangelosi established what she called the “Lender Protection Group.” This group was  
27 never recognized as a formal committee, and is apparently a collection of individuals represented  
28 by Mr. Smith.

1 do so. The Lenders Protection Group also argued that this court did not have subject matter  
2 jurisdiction.

3 This court entered an order preserving the status quo as of the day before the  
4 termination letters were sent. The court further ordered supplemental briefing on the issue of  
5 subject matter jurisdiction, and it continued the matter to June 20, 2007.

6 For the reasons set out herein, this court finds that it has subject matter jurisdiction  
7 pursuant to 28 U.S.C. § 1334 as to a number of the issues raised, and supplemental jurisdiction  
8 with respect to the remaining issues. However, because the resolution of these issues will involve  
9 the determination both core and non-core matters under 28 U.S.C. § 157, this court recommends  
10 that the reference be withdrawn.<sup>2</sup>

## 11 **FACTS**

### 12 ***A. The Business of USACM and the Loan Servicing Agreements.***

13 One of the debtors, USACM Capital Mortgage (“USACM”) was in the business  
14 of underwriting, originating, brokering, funding, and servicing mortgage loans. It solicited  
15 individuals and entities to invest in fractional interests in loans, and also originated and serviced  
16 those loans. As of the date of the filing of the bankruptcy petition, USACM was servicing 115  
17 loans involving 3,600 investors. (“Debtors’ First Amended Disclosure Statement,” Docket  
18 # 1798, pp. 22-24.) Two separate debtors, USACM Capital Diversified Trust Deed Fund, LLC,  
19 (“DTDF”) and USACM First Trust Deed Fund (“FTDF”) were also investors in the  
20 fractionalized loans brokered by USACM. These funds were comprised of a number of  
21 members who invested in the funds, with the funds then investing in loans. As of the date of the  
22 petition, DTDF had approximately 1,350 members and FTDF had 950 members. (“Debtors’ First  
23 Amended Disclosure Statement, Docket # 1798, pp. 25-26.)

24 As noted, USACM entered into loan servicing agreements with those entities for whom it  
25

---

26 <sup>2</sup>At the request of the court, counsel for Ms. Cangelosi has prepared a recommendation for  
27 withdrawal of the reference. It will be separately entered.

1 had brokered loans. Under paragraph 2(e) of the loan servicing agreements, the lender authorized  
2 and empowered USACM on it's behalf to, among other things, execute and deliver payoff  
3 demands and beneficiary statements, consent to modifications of the loans if the effect would not  
4 materially or adversely affect the security provided by the real or personal property, institute  
5 foreclosure proceedings, engage in settlement discussions, and enter into forbearance and other  
6 settlement-related agreements. USACM, however, could not permit any modification to any loan  
7 that would change the interest rate, forgive the payment of any principal or interest (expressly  
8 excluding late charges or the difference between default and non-default interest), change the  
9 outstanding principal amount, or extend the maturity date, without the lender's prior consent. If  
10 the lender failed to grant or deny consent within 3 business days after notice, consent was  
11 deemed to have been conclusively been given. ("Motion to Enforce Confirmation, Docket #  
12 3773, "Exhibit A.")<sup>3</sup>

13 Under paragraph 5 of the loan servicing agreements, USACM was entitled to retain  
14 monthly, in connection with those services, a service fee, any late charges collected from the  
15 borrower, and default interest collected from the borrower pursuant to the terms of the note.  
16 (Motion to Enforce Confirmation, Docket # 3773, "Exhibit A.")

17 The loan servicing agreements contained two provisions relating to termination.  
18 Paragraph 9 provided that the lender:

19 [M]ay, by 30 days written notice to USACM, terminate this  
20 agreement, and the power of attorney granted, if one is granted,  
21 under Section 9 of this Agreement, if USACM fails to perform its  
22 obligations hereunder.<sup>4</sup>

---

23 <sup>3</sup>A sample loan service agreement was attached as "Exhibit A" to the declaration of David  
24 Blatt, which was filed as "Exhibit A" in support of the Motion to Enforce Confirmation. (Docket  
# 3773.)

25 <sup>4</sup>Section 9 of the Agreement supplied to the court has nothing to do with a power of attorney.  
26 Rather, Section 9 merely provides that the lender's name is the exact form for registration.  
27 Paragraph 11 deals with a "Limited Power of Attorney." A different version on file with this  
Court in connection with a separate matter refers to Paragraph 11. (Docket 847, p.19.)

1 (Motion to Enforce Confirmation, Docket # 3773, “Exhibit A.”)

2 Paragraph 3 provided that:

3 Pursuant to NAC 645B.073, in the event of default, foreclosure, or  
4 other matters that require action, if for any reason USA fails to act  
5 on Lender’s behalf . . . then Lender may, with approval of fifty-one  
6 percent (51%) or more of all the holders of the beneficial interest  
7 of record in the Loan, act on behalf of all such holders of  
8 beneficial interest of record.

9 The actions included the designation of the servicing agent or other person to act on  
10 behalf of the holders of the beneficial interests in the loan. (Motion to Enforce Confirmation,  
11 Docket # 3773, “Exhibit A.”)

12 ***B. Bankruptcy and the Situation Prior to Filing.***

13 USACM and its related affiliates filed a chapter 11 petition on April 13, 2006.  
14 USACM’s management was replaced with a chief restructuring officer and crisis manager,  
15 Thomas Allison and Mesirow Financial Interim Management, LLC. (Docket # 26.)<sup>5</sup> Hence none  
16 of the former insiders had a role in administering the case or in the plan negotiations. Indeed,  
17 former management appealed the order confirmation the plan. (Docket # 2481.)

18 The United States Trustee appointed committees for the direct lenders,<sup>6</sup> for creditors of  
19 the two separate debtors USACM Capital Diversified Trust Deed Fund, LLC<sup>7</sup> and USACM First

---

20 <sup>5</sup>While this order was designated as an interim order, the court extended those orders  
21 throughout the case.

22 <sup>6</sup>The United States Trustee denominated this committee the “Official Committee of Holders  
23 of Executory Contract Rights” of USACM. (Docket # 202.) The court, believing that this  
24 designation created a legal distinction without a finding that the contracts were executory  
25 contracts, denominated these individuals and entities who held fractionalized interest in unpaid  
26 loans as “direct lenders.” Under the plan, “direct lenders” are defined as each entity, except  
USCAM and the Funds, who is a beneficiary under a loan originated and serviced by USACM  
on behalf of lenders. (Docket # 1799, (1)(A)(42).

27 <sup>7</sup>Docket #203.

1 Trust Deed Fund,<sup>8</sup> and for the unsecured creditors.<sup>9</sup> Each of those committees retained counsel  
2 and were actively involved in the case.

3 During the case, it became apparent (and the court ultimately found) that the borrowers  
4 on many of the underlying loans were in default and had either not made any payments, or had  
5 not made payments in accordance with their notes and deeds of trust. Despite the fact that  
6 lenders were only to receive payments in accordance with their contracts and the underlying  
7 notes and deeds of trust, the lenders continued to receive payments on their notes as if payments  
8 were being made. Obviously, these funds came from sources other than the borrowers and were  
9 made from monies that were due to USACM as servicing or other fees, loans which had been  
10 paid (but the principal not repaid to the lenders), and money borrowed from third parties.  
11 (“Debtors’ First Amended Disclosure Statement, Docket # 1798, pp. 28-29; Declaration of  
12 Thomas Allison in Support of Confirmation, Docket # 2147, p. 31.”)<sup>10</sup> These payments were  
13 described in the plan as “pre-paid interest.” However, that was only a term of convenience, as  
14 the lenders had no right to receive funds that were not paid by the borrower.<sup>11</sup>

15 As noted above, FTDF owned interests in a number of loans. Some of these loans were  
16 performing and many others were in default. These loans were also serviced by USACM.  
17 DTDF had also invested in loans brokered and serviced by USACM.

18 During negotiations with the debtor (through Mesirow Financial) and the four  
19 committees, it was determined that in light of the costs of attempting to service the loans,  
20 including commencing foreclosure or otherwise realizing on the collateral of loans in default,  
21

---

22 <sup>8</sup>Docket #204.

23 <sup>9</sup>Docket #201.

24 <sup>10</sup>This court made certain oral findings of fact on the record in accordance with FED. R.  
25 BANKR P. 7052, which included the adoption of the facts set forth by Mr. Allison.

26 <sup>11</sup>See N.R.S. § 645B.250, which provides that a mortgage broker is prohibited from advancing  
27 payments to an investor on behalf of a person who has obtained a loan and is in default.

1 and given that there was no ability to continue as a mortgage broker, the only way in which  
2 creditors could receive payment was through an asset purchase agreement and plan. (*See*  
3 *generally*, “Debtors’ First Amended Disclosure Statement, Docket # 1798, pp. 79-80.)

4 ***C. The Asset Purchase Agreement, the Plan, and the Confirmation Order .***

5 ***1. Asset Purchase Agreement.***

6 The debtors, with the concurrence of the committees, filed a motion to sell  
7 the servicing rights, including the fees to which USACM was entitled as servicer, and the loan  
8 portfolio of FTDF at auction with SPCP Group, LLC (“Silver Point”) as the stalking horse  
9 bidder. (Docket # 1352.) Other bidders qualified, but ultimately Compass was the successful  
10 bidder.<sup>12</sup>

11 The closing of the sale to Compass was conditioned upon confirmation of a plan with  
12 provisions consistent with the terms of the asset purchase agreement. (“Asset Purchase  
13 Agreement,” § 5.3, filed as “Exhibit A” to Docket # 2164.)

14 Under the Asset Purchase Agreement, Compass purchased the First Trust Deed Fund  
15 Assets and the Commercial Mortgage Assets. The “Commercial Mortgage Assets” were defined  
16 as:

17 [A]ll Servicing Agreements . . . for all of the Serviced Loans . . .  
18 including, without limitation, Default Rate Interest, Accrued  
19 Servicing Fees, Late Charges, Success Fees, other fees and sums  
20 due the loan servicer under any of the Servicing Agreements” [and  
21 USCAM’s rights in the loans].<sup>13</sup>

22 “Default Rate Interest” was defined as the “amount of interest payable upon default under  
23 each Serviced Loan at any time.” “Accrued Servicing Fees” was defined, with certain  
24 exceptions as “all servicing fees and servicer advances accrued, but unpaid, as of the of the  
25 Closing

---

26 <sup>12</sup>See Docket # 2147, Allison Declaration in Support Confirmation, pp. 25-28, for a  
27 description of the sale process.

28 <sup>13</sup>USACM held a fractionalized interest in some loans.

1 Date. . . .” “Late Charges” was defined as the amount of late charges payable upon default  
2 under each Serviced Loan at any time.” (“Asset Purchase Agreement,” § 1.1, filed as “Exhibit  
3 A” to Docket # 2164.) The asset purchase agreement, at Section 5.2, also required the Sale  
4 Approval Order to contain certain provisions. In further provided the following:

5  
6 Sec. 7.3. Servicing Agreements. Nothing contained in the  
7 Agreement shall modify the obligations owed to the Lenders by  
8 the loan servicer or rights of the Lenders against the loan servicer  
9 (or the rights of the loan servicer against the Lenders) under the  
10 applicable Servicing Agreements and otherwise applicable  
11 law . . . . [U]nder no circumstance shall any pre-Closing Date  
12 liability assertable by any party attach to Purchase, or to any Asset  
13 acquired by purchaser . . . . [N]otwithstanding any other provision  
14 herein, or any order which may in the future be entered by the  
15 Bankruptcy Court, all servicing fees due pursuant to the terms  
16 stated in the Servicing Agreements, and all interest due on the First  
17 Trust Deed Fund Assets, shall continue to be due and payable, and  
18 Purchaser shall collect such servicing fees and interest for its sole  
19 benefit on and after the Closing Date.

## 20 **2. The Plan.**

21 The plan provided for the compromise of Direct Lender claims in that claims for  
22 the recharacterization<sup>14</sup> of loans as property of the estate were released. While rights  
23 to recover principal or interest paid in advance were preserved, lenders would continue to  
24 receive monies paid on the loan after the pre-paid amounts were netted. (Debtor’s Third  
25 Amended Plan, Docket # 1799, Section II (C)(1)(e).) In connection with this provision, the  
26 liquidating trust would receive the amounts netted on account of the pre-paid interest, and the  
27 asset purchaser and any subsequent purchaser were required to continue to net these sums.  
28 (Section IV(E)(1).)

Because the plan affected the direct lenders by virtue of the compromise discussed above,

---

<sup>14</sup>While under 11 U.S.C. § 541(d), property in which the debtor holds only equitable title is not property of the estate, the commingling of funds received from all sources and payments on loans in default may result in the characterization of such loans as property of the estate. *See, e.g; In re Lemons & Assoc.*, 67 B.R. 198 (Bankr. D. Nev. 1986).

1 the direct lenders voted on the plan. The direct lenders, along with all other classes entitled to  
2 vote, voted by majority and amount to accept the plan. An order confirming the plan was entered  
3 on January 8, 2007. (Docket #2376.) Findings of fact and conclusions of law were also entered  
4 on January 8, 2007, as modified herein. (Docket # 2377.)<sup>15</sup>

5 At the time of confirmation, the issue arose as to the meaning of the acquisition of the  
6 loan serving agreements free and clear of claims and the rights of a lender to terminate on  
7 account of pre-petition defaults by USACM. Compass agreed that a lender had the right to effect  
8 a substitution of USACM as a loan servicer under Section 3 of any loan servicing agreement  
9 (and Compass had the right to any defenses) to the extent that such right was matured and  
10 exercisable as of the petition date. Such rights were denominated as “Surviving Section 3 Right.”  
11 Such rights were, however, only exercisable in accordance with certain procedures which  
12 included a 30 day notice of an intent to exercise such right, the right of Compass to challenge the  
13 exercise by filing a motion within thirty days, and that this court should retain jurisdiction to  
14 adjudicate any such disputes. (Findings of Fact, Docket # 2377 at ¶ KK,; Confirmation Order,  
15 Docket # 2376, at ¶ 14.)<sup>16</sup>

16 Other relevant provisions of the Findings of Fact include the following, at ¶ KK:  
17

18 The transfer of the Acquired Assets . . . will be a legal, valid, and  
19 effective transfer of the Acquired Assets, and will vest the Asset  
20 Purchaser with all right, title, and interest of the Sellers to the  
21 Acquired Assets free and clear of all liens, claims, interest,  
22 obligations and encumbrances whatsoever, including, but not  
23 limited to, (A) all monetary and non-monetary defaults and rights  
24 that purport to give to any party a right or option to effect any  
25 forfeiture, modification, right of first refusal, or termination of the  
26 Sellers’ or the Asset Purchasers’s interest in, or rights in or under,

---

24 <sup>15</sup>Despite the failure to cross out the parenthetical “proposed” designation, the court adopted  
25 the findings and conclusions (Docket # 2377) and the confirmation order (Docket #2376) and  
26 entered them as the court’s orders.

26 <sup>16</sup>The Lenders Protection Group asserts that it is not claiming any rights to terminate based  
27 upon defaults by USACM.

1 the Acquired Assets, or any similar rights, based in any way on  
2 any action taken (or failed to be taken) by any of the Debtors or  
3 any other matter or occurrence relating to the period prior to the  
4 Closing [other than the surviving section 3 rights] . . . © . . . (ii) all  
5 debts arising in any way in connection with any agreements, acts,  
6 or failures to act, of any of the Sellers or any of the Sellers'  
7 predecessors or affiliates; all claims (as that term is defined in the  
8 Bankruptcy Code), obligations, liabilities, rights of recoupment or  
9 setoff, demands, guaranties, options, rights, restrictions, interest  
10 and matters of any kind and nature in any way relating to the  
11 existence, ownership, management or servicing of the Acquired  
12 Assets prior to Closing, whether known or unknown, contingent or  
13 otherwise, whether arising prior to or subsequent to the  
14 commencement of these cases . . . and whether imposed by  
15 agreement, understanding, law, equity, or otherwise . . . .

16 Paragraph KK also provided that:

17  
18 In the event of a proper exercise of remedies under Section 3 of the  
19 Loan Servicing Agreement, (I) neither the Direct Lenders nor any  
20 replacement servicer selected by such Direct Lender shall have the  
21 right or ability to compromise, subordinate, or impair, in any  
22 respect, any claims purchased by Compass from the Estates for  
23 default interest, accrued servicing fees, late charges, success fees,  
24 or other amounts under the Loan Servicing Agreement, and (ii) the  
25 Confirmation Order shall be binding upon such replacement  
26 servicer. . . <sup>17</sup>

27 **3. Confirmation Order.**

28 The confirmation order contained the following additional potentially  
relevant provisions:<sup>18</sup>

The provisions of the Plan and this Confirmation Order shall  
bind . . . (f) all Direct Lenders. (¶ 8.)

— — — —

---

<sup>17</sup>These provisions were also contained in paragraph 14 of the Confirmation Order except that the last sentence includes the phrase “rights, claims or interests purchased by Compass.”

<sup>18</sup>The court makes no determination as to the interpretation of any of these provisions as it relates to the issue presently before the court.

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28

1 The transfer . . . constitutes a legal, valid and effective transfer of  
2 the Acquired Assets, and shall vest the Asset Purchaser with all  
3 right, title, and interest of the Sellers . . . free and clear of all  
Claims and Interests of any kind or nature whatsoever. (¶ 17.)

- - - -

4 This court retains jurisdiction as set forth in Section VIII. D of the  
5 Plan, including the jurisdiction to enforce and implement the terms  
6 and provisions of this Confirmation Order and the Asset Purchase  
7 Agreement . . . including, but not limited to, retaining  
jurisdiction . . . (b) to protect the Asset Purchaser against any  
Interests against the Sellers or the Acquired Assets. (¶ 23.)

- - - -

8 All Persons holding Interests against or in the Sellers or the  
9 Acquired Assets of any kind or nature whatsoever (including but  
10 not limited to . . . Direct Lenders . . . shall be, and are, forever  
11 barred, estopped, and permanently enjoined from asserting,  
12 prosecuting, or otherwise pursuing such Interests of any kind or  
13 nature whatsoever against the Asset Purchaser . . . or the Acquired  
14 Assets . . . with respect to any Interest of any kind or nature  
15 whatsoever such Person or entity had, has, or may have against or  
16 in the . . . Acquired Assets. Following the Closing, no holder of an  
17 Interest in the Sellers shall interfere with the Asset Purchaser's  
18 title to or use and enjoyment of the Acquired Assets based on or  
19 related to such Interest, or any actions that the Sellers may take in  
20 their Chapter 11 Cases. (¶ 25.)

- - - -

17 After the effective date . . . the Direct Lenders . . . shall be entitled  
18 to distributions from the Direct Lender Loans in accordance with  
19 the related Loan Servicing Agreements, the applicable loan and  
20 security documents, and applicable Nevada law, by the Asset  
21 Purchaser, as the third party servicer. . . . [T]he Asset Purchaser  
22 is authorized and directed to net Prepaid Interest sums due from  
23 the Direct Lenders and Collect Prepaid Interest from Borrowers,  
24 and remit those amounts to . . . the USACM Trust. . . After the  
25 Closing, the Direct Lenders are obligated to comply with the terms  
26 of the applicable Loan Servicing Agreements including the  
27 obligation to pay the fees at the rate expressed as a percentage  
28 specified in Section 5 thereof[.] (¶ 47.)

- - - -

24 Nothing in the Plan or this Confirmation Order shall be deemed to  
25 modify, in any respect, the Direct Lenders' notes or the deeds of  
26 trust securing such notes. (¶ 48.)

- - - -

1 Nothing contained in the Asset Purchase Agreement shall modify  
2 the obligations owed to the Lenders by Compass as the loan  
3 servicer or rights of the Lenders against Compass as the loan  
4 servicer (or the rights of Compass as the loan servicer against the  
5 Lenders) under the applicable Loan Servicing Agreements and  
6 otherwise applicable law. Compass shall distribute any sums due  
7 to Lenders under any of the Loan Servicing Agreements in  
8 accordance with the Loan Servicing Agreements, as the same may  
9 be modified with consent of the applicable Lenders, and with  
10 otherwise applicable law. Compass shall apply all payments and  
11 proceeds from Serviced Loans . . . however collected . . . in  
12 accordance with the provisions of the notes and/or loan  
13 agreements. Further, notwithstanding the foregoing, to the extent  
14 the Bankruptcy Court has entered an order, including, but not  
15 limited to, this Confirmation Order, which interprets or enforces  
16 provisions of the Loan Servicing Agreements or directs the  
17 distribution of payments under the Loan Servicing Agreements or  
18 payments collected from Borrowers, Compass, the Lenders, and all  
19 other affected parties shall abide by the terms of such order(s). If,  
20 as between the provisions of the Loan Servicing Agreements and  
21 the order(s) of the Bankruptcy Court, it is not clear to Compass  
22 how the sums collected shall be distributed, then Compass shall  
23 hold the sums payable to the Lender until Compass either receives  
24 direction from the Lender . . . regarding disbursement of interest,  
25 or is directed by an order from a court of competent jurisdiction.  
26 Nothing contained here is intended to waive any defenses of the  
27 Lenders . . . under the Loan Servicing Agreements. For the  
28 avoidance of doubt, under no circumstance shall any pre-Closing  
Date liability assertable by any party attach to Compass, or to any  
asset acquired by Compass, pursuant to the Asset Purchase  
Agreement. Furthermore, for the avoidance of doubt,  
notwithstanding any other provision in the Asset Purchase  
Agreement, this Confirmation Order, or any order which may be in  
the future be entered by the Bankruptcy Court, all servicing fees  
due pursuant to the terms stated in the Loan Servicing Agreements,  
and all interest due on the First Trust Deed Fund Assets . . . shall  
continue to be due and payable, and Compass shall collect such  
servicing fees and interest for its sole benefit on and after the  
Closing Date. (¶ 82.)

21 ***D. Post-Confirmation Events.***

22 Donna Cangelosi and the Lenders Protection Group opposed the confirmation of  
23 the plan.<sup>19</sup> Their objections were overruled. The Lenders Protection Group appealed and, rather  
24 than seeking a stay on appeal pursuant to the Federal Rules of Bankruptcy Procedure, sought and  
25

---

26 <sup>19</sup>As noted, this Group was an ad hoc group and although the Court required the filing of  
27 statements under Rule 2019, these statements were not always kept up-to-date.

1 received an ex-parte stay on appeal from the Bankruptcy Appellate Panel. That stay was quashed  
2 by the District Court after the case was returned to the District Court when the debtors failed to  
3 consent to jurisdiction before the BAP. Rather than seeking a stay in this court, the Lenders  
4 Protection Group abandoned that effort prior to the closing.

5         The closing occurred and Compass paid approximately \$67 million for the assets. In its  
6 Motion to Enforce Confirmation, Compass contends that Ms. Cangelosi and the Lenders  
7 Protection Group have been engaged in a concerted effort, both before and after confirmation of  
8 the plan, to derail the reorganization and to deter Compass, and that the letters to borrowers and  
9 the termination letters were a part of this scheme as opposed to the exercise of any legitimate  
10 rights of the direct lenders to terminate Compass as a servicing agent. (See Docket # 3773,  
11 “Exhibit B,” Declaration of Boris Piskun.)

12         Apparently, Ms. Cangelosi and others have caused the formation of limited liability  
13 companies, which are described as being comprised of direct lenders who have allegedly  
14 assigned their rights to the LLC in exchange for membership interests. A different LLC was  
15 formed for each loan. It also appears that the LLC’s contemplate that default interest will be paid  
16 to them (and shared by the manager and the members) and not to Compass. (“Exhibit F” to  
17 Docket # 3830; Docket #3873, “Exhibit “A.”)

18         One of the “members” of the LPG, Todd Hansen, has allegedly contacted a borrower and  
19 represented that only he has the right to speak on behalf of lenders in that loan. (Docket 3773,  
20 Blatt Declaration.)

21         On May 18, 2007, Compass filed an action in state court against Ms. Cangelosi and  
22 others for intentional interference with contractual relations and prospective economic  
23 advantage, defamation, and breach of the covenant of good faith and fair dealing. (“Exhibit F” to  
24 Docket # 3854.) On May 23, 2007, Compass dismissed the lawsuit without prejudice.  
25 (“Declaration of Donna Cangelosi, “Docket # 3854.)

1 On or about May 18, 2007, Ms. Cangelosi caused to be sent to each borrower a letter  
2 stating that Compass had been terminated and that payments should be made to the “Lender 2  
3 Lender, LLC,” an entity apparently managed by Ms. Cangelosi. (Docket 3854, ¶ 13; Docket  
4 #3773, “Exhibit B” to Blatt Declaration.) Simultaneously, Ms. Cangelosi, on behalf of the  
5 particular LLC, sent a letter terminating Compass’s servicing rights. The letters stated that the  
6 agreements were terminated based upon Nevada Adm Code 645B.073 as well as various actions  
7 and inactions of Compass Partners. (See “Exhibit C “to Docket # 3830.)

8 The Lenders Protection Group filed an action based upon diversity jurisdiction in Federal  
9 District Court (#07-CV-000241-ECR-VPC) for declaratory relief as well as for damages on or  
10 about May 21, 2007.<sup>20</sup> (Docket # 3854, “Exhibit H”.) The plaintiffs request judgment for  
11 declarations that:

- 12 1. Under the Nevada Administrative Code plaintiffs, together with other direct  
13 lenders making up 51% of the beneficial interests of any loan, have the absolute  
right to terminate Compass as loan servicer and designate a new loan servicer.
- 14 2. Payments made by borrowers are first to be applied to accrued non-  
15 default rate interest and then to principal, and then to default interest and  
late fees, which priority may only be altered by the direct lenders in each  
16 loan.
- 17 3. That the plaintiffs and other direct lenders have the absolute right to  
18 modify the terms of their promissory note and deed of trust with the third-  
party borrower to maximize their recovery.
- 19 4. That as a result of the maturity of various loans in the USACM  
20 portfolio, Compass has never had a valid power of attorney to act on  
behalf of plaintiffs on the loans.
- 21 5. Plaintiffs and other direct lenders have the right to determine the  
22 priority of allocating payments made by any third-party borrower, and  
Compass has no such right.
- 23 6. Plaintiffs are entitled to terminate Compass as servicer on any loan  
based upon Compass’s breaches of the loan servicing agreements.
- 24 7. Compass is not entitled to any compensation provided for in  
25 Section 5 of the loan servicing agreements.

---

26  
27 <sup>20</sup>The named plaintiffs are each of the newly formed LLC’s.

1                    ***E. Proceedings in this Court.***

2                    Compass removed the action to this court. While a motion to strike fugitive  
3 pleading and remand has been filed, it has not yet been set for hearing. Compass brought this  
4 Motion to Enforce Confirmation to enforce the terms of the confirmation order and for contempt.  
5 In its Motion, Compass seeks the following orders against Cangelosi, Hansen, LPG, L2L and  
6 parties acting in court:

- 7                    1. An order directing them to comply with the terms of the  
8 Confirmation Order and the loan servicing agreement.
- 9                    2. An order directing them and others to issue letters to the  
10 borrowers that the prior letters shall have no force and effect and  
11 that Compass will continue to service until further order of the  
12 court.
- 13                    3. An order enjoining them from communicating with borrowers  
14 under the loans, and sanctioning them.
- 15                    4. Sanctioning them for civil contempt.

16                    The court, as well as the Lenders Protection Group, raised the issue of subject matter  
17 jurisdiction and asked for additional briefing. Pending this hearing, the court ordered that the  
18 status quo be maintained as of the day prior to the purported termination letters. However, the  
19 Lenders Protection Group could take steps to terminate in accordance with the contracts and if  
20 valid, would be recognized.

21                    **LEGAL DISCUSSION**

22                    The court finds that it has subject matter jurisdiction to adjudicate Compass’s motion and  
23 has supplemental jurisdiction to adjudicate those issues for which it may not directly have  
24 subject matter jurisdiction. For those issues for which the court has only supplemental  
25 jurisdiction, such issues are, however, “non-core” and subject to either withdrawal to the District  
26 Court (absent consent) or this court’s making of findings and recommendations to the District  
27 Court. Because of the need for expeditious and unified hearings, the court recommends that the  
28 reference be withdrawn.

1 As the court noted at the prior hearing, the mere fact that a court reserves jurisdiction in  
2 it's orders to adjudicate further disputes does not end the question of whether or not the court has  
3 subject matter jurisdiction. Rather, subject matter jurisdiction is not given by consent but by  
4 statute. A court retains jurisdiction to determine if it has jurisdiction. *In re Harleston*, 275 B.R.  
5 546, 549 (B.A.P. 9<sup>th</sup> Cir. 2002), *aff'd*, 331 F.3d 699 )(9<sup>h</sup> Cir. 2003).

6 Pursuant to 28 U.S.C. § 1334(b), the district courts (and by referral, the bankruptcy  
7 courts) have original but not exclusive jurisdiction of all civil proceedings arising under title 11,  
8 or arising in or related to cases under title 11. Bankruptcy Courts may hear and determine all  
9 cases under title 11 and all core proceedings arising under title 11, or arising in a case under title  
10 11. 11 U.S.C. § 157(b)(1). Core proceedings include matters concerning the administration of  
11 the estate, allowance or disallowance of claims against the estate, confirmations of plans, orders  
12 approving the sale of property and other proceedings affecting the liquidation of the assets of the  
13 estate. 11 U.S.C. § 157(b)(2). The bankruptcy judge may hear a proceeding that is not a core  
14 proceeding but that is otherwise related to a case under title 11. In such case, the court may not,  
15 without consent, enter a final order, but must submit proposed findings of fact and conclusions of  
16 law to the district court that enters the final order. 11 U.S.C. § 157©. Finally, a district court may  
17 withdraw, in whole or in part, any case or proceeding referred to the bankruptcy court. 11 U.S.C.  
18 § 157(d).

19 Clearly, a court retains jurisdiction to interpret and enforce its own orders. *In re*  
20 *Franklin*, 802 F.2d 324, 326 (9<sup>th</sup> Cir. 1986). “Related to” jurisdiction is a grant of some breadth  
21 and includes suits between third parties which have an effect on the bankruptcy estate. *Celotex*  
22 *Corp. v. Edwards*, 514 U.S. 300, 308 n. 5 (1995). *Stratosphere Litigation L.L.C. v. Grand*  
23 *Casinos*, 298 F.3d 1137, 1142 (9<sup>th</sup> Cir. 2002). The test for pre-confirmation jurisdiction has been  
24 broadly formulated such that if the outcome of the proceeding could conceivably have any effect  
25 on the estate being administered in bankruptcy, whether or not it be against the debtor or against  
26 the debtor's property, then the court has jurisdiction. *In re Fietz*, 852 F.2d 455, 457(9<sup>th</sup> Cir.1988).

1 In the Ninth Circuit, while post-confirmation jurisdiction is more limited than pre-  
2 confirmation jurisdiction, the bankruptcy court still retains jurisdiction for matters which have a  
3 “close nexus” to the bankruptcy plan or proceeding sufficient to uphold bankruptcy court  
4 jurisdiction over the matter. *In re Pegasus Gold Corp.*, 394 F.3d 1189 (9<sup>th</sup> Cir. 2005). As the  
5 Ninth Circuit held, adopting the Third Circuit’s test in *In re Resorts Int’l, Inc.*, 372 F.3d 154 (3d  
6 Cir. 2004):<sup>21</sup> Matters affecting “the interpretation, implementation, consummation, execution, or  
7 administration of the confirmed plan will typically have the requisite close nexus.” *In re Pegasus*  
8 *Gold Corp.*, 394 F.3d 1189, 1194 (9<sup>th</sup> Cir. 2005)(quoting *In re Resorts Int’l, Inc.*, 372 F.3d 154,  
9 166-67 (3d Cir. 2004).

10 The Ninth Circuit in *Pegasus* also recognized that bankruptcy courts may properly  
11 exercise supplemental jurisdiction over claims which have a more tangential relationship to the  
12 underlying bankruptcy court. Hence if the remaining claims involve a “common nucleus of  
13 operative fact” and would ordinarily be expected to be resolved in one judicial proceeding, the  
14 bankruptcy court has supplemental jurisdiction over the remaining claims. *Pegasus*, 394 F.3d  
15 1189, 1195 (9<sup>th</sup> Cir. 2005).

16 Before addressing the application of the law governing subject matter jurisdiction for  
17 post-confirmation issues, it is important to note what this motion is not about. It is, despite the  
18 protestations of the Lenders Protection Group, not merely about the determination of whether or  
19 not Compass has committed breaches of the Loan Servicing Agreement. Nor is it merely about  
20 the interpretation of the contract or the order of the application of the proceeds received from a  
21 particular borrower. This Court agrees that if the Lenders Protection Group had sent letters of  
22 termination which specified the manner in which Compass had failed to perform in accordance  
23

---

24  
25 <sup>21</sup>The Lender Protection Group states in its opposition that the Ninth Circuit test is the same  
26 as the Seventh. (Docket #3853.) This is incorrect. The Seventh Circuit test is more limited.  
27 *See, e.g., Celotex Corp. v. Edwards*, 514 U.S. 300 (1995); *In re Fietz*, 852 F.2d. 455, 457 (9<sup>th</sup> Cir.  
1988)(pre-confirmation jurisdiction); *In re Fedpak Sys, Inc.*, 80 F.3d 207, 213-14 (7<sup>th</sup> Cir. 1996),  
*In re Commercial Loan Corp.*, 363 B.R. 559 (Bankr. N.D. Ill. 2007).



1 sale order.

2 The most dramatic impact on the sale order was the letter sent to borrowers advising  
3 them not to pay Compass. The Lenders Protection Group also seeks to modify the underlying  
4 loans to apparently direct that interest to be allocated in a certain manner and to declare that  
5 Compass has no rights to the fees it purchased. This directly impacts the sale order and asset  
6 purchase agreement because Compass purchased the rights to the loan servicing agreements as  
7 well as the fees due to USACM. Even if validly replaced as a servicer, it had the rights to the  
8 accrued fees. Finally, Compass argues that these issues could lead to an action for rescission.

9 Furthermore, Compass and any replacement servicer were required to net pre-paid  
10 interest and pay it over to the Liquidating Trust. The termination letter sent to borrowers directly  
11 impacts the estate, because if the borrowers fail to pay, there is no pre-paid interest to be  
12 remitted. While counsel for the Lenders Protection Group indicated they would abide by such  
13 provision if they were allowed to proceed, the estates' rights to receive these fees is implicated  
14 by a change in servicer. In particular, would the Lenders Protection Group take the position that  
15 it was not required to remit pre-paid interest pending a resolution of it's appeal notwithstanding  
16 that it failed to seek a stay?

17 The Lenders Protection Group also argues that it has the right to terminate for cause and  
18 the court has no jurisdiction to so determine. It is clear from the various hearings and orders that  
19 Compass acquired the loan servicing agreements as written. It gained no greater rights than held  
20 by USACM nor any lesser rights. Conversely, the direct lenders each retain their rights,  
21 including the right to terminate the contracts in accordance with the terms of the agreement. As  
22 noted, if this case were simply about that, the court would decline jurisdiction. However, there is  
23 a non-frivolous claim that the alleged terminations were subterfuge for an attempt to interfere  
24 with Compass's rights. For example, rather than individual lenders determining whether or not  
25 Compass had failed to act, the Lenders Protection Group provided form letters which did not  
26 specify any cause, has engaged in a series of communications seeking to stop Compass, and has

27

28

1 formed LLC's to acquire all servicing rights. ("Motion to Enforce Confirmation, Docket # 3773,  
2 "Exhibit A.") This court believes that where such subterfuge is alleged, it has jurisdiction to  
3 determine whether or not the lenders are in good faith exercising their rights under the contract  
4 or are attempting to avoid the effect of this court's orders. *See In re Petrie Retail Inc*, 304 F.3d  
5 223 (2d Cir. 2002)(court has post-confirmation jurisdiction.) However, even if the court does not  
6 have core or related to jurisdiction with respect to this particular dispute, the court has  
7 supplemental jurisdiction over this common nucleus of facts.

#### 8 **WITHDRAWAL OF THE REFERENCE**

9 While this court has found that it has subject matter jurisdiction to determine the issues  
10 raised by Compass's motion, that does not end the question of the nature and extent of this  
11 court's jurisdiction.

12 As stated above, unless the parties consent, this court cannot enter final orders with  
13 respect to non-core matters. The issues implicated in this include matters over which this court  
14 has only supplemental jurisdiction as well as matters which are within the court's jurisdiction  
15 under § 1334, but are non-core under § 157. Hence, the court would be in the position of making  
16 only findings and recommendations as to some matters. The issues here are inextricably  
17 intertwined, and to attempt to delineate the matters and/or bifurcate hearings would constitute a  
18 waste of judicial resources.

19 The court cannot enforce the provisions of the plan without determining whether or not  
20 the contracts were validly terminated. Furthermore, this court cannot enforce the provisions of  
21 the plan without determining whether Compass is applying the monies received in accordance  
22 with the provisions of the notes and deeds of trust and loan servicing agreements.

23 Accordingly, this court believes that the most expeditious way of proceeding is for the  
24 District Court to withdraw the reference.

1 **INTERIM RELIEF**

2 Until the reference is withdrawn, this court retains jurisdiction to enter all orders.  
3 FED. R. BANK. P. 5011. It is apparent that interim relief is required so that borrowers will not use  
4 this dispute as an excuse not to remit payments and so that funds collected can be distributed to  
5 the direct lenders and especially those direct lenders who are not involved in this dispute.  
6 However, the rights of the Lenders Protection Group must be preserved such that if it some or all  
7 of its members have validly terminated the loan servicing agreements, they can proceed in the  
8 manner they wish to proceed.<sup>23</sup> At the prior hearing on June 22, 2007 the parties and the court  
9 determined how this should be accomplished. Compass is directed to prepare the order, with the  
10 Lender Protection Group to approve or disapprove such order pursuant to the provisions of Local  
11 Bankruptcy Rule 9021.

12 **IT IS SO ORDERED.**

13  
14 Copies noticed through ECF to:  
15 LENARD E. SCHWARTZER [bkfilings@s-mlaw.com](mailto:bkfilings@s-mlaw.com)  
16 RICHARD MCKNIGHT [mcknightlaw@cox.net](mailto:mcknightlaw@cox.net), [gkopang@lawlasvegas.com](mailto:gkopang@lawlasvegas.com)  
17 ALAN R SMITH [mail@asmithlaw.com](mailto:mail@asmithlaw.com),  
[turk@asmithlaw.com](mailto:turk@asmithlaw.com); [marsh@asmithlaw.com](mailto:marsh@asmithlaw.com); [darby@asmithlaw.com](mailto:darby@asmithlaw.com)  
18 ROB CHARLES [rcharles@lrlaw.com](mailto:rcharles@lrlaw.com), [cjordan@lrlaw.com](mailto:cjordan@lrlaw.com)

19 Copies noticed through BNC to:  
20 ORRICK HERRINGTON & SUTCLIFFE LLP  
21 400 CAPITOL MALL #3000  
22 SACRAMENTO, CA 95814-4497  
23  
24

25 \_\_\_\_\_  
26 <sup>23</sup>Despite the fact the loan servicer has the right to foreclose on loans in default (and perhaps  
27 the duty to do so), the Lenders Protection Group apparently does not want Compass to cause  
28 foreclosure of some or all of the defaulted loans.