

# **USA CAPITAL DIVERSIFIED TRUST DEED FUND, LLC**

Robert G. Worthen, Chairman of the Board

December 1, 2009

Dear USA Capital Diversified Trust Deed Fund, LLC Investor:

I again write on behalf of the Board of Directors of USA Capital Diversified Trust Deed Fund, LLC (“DTDF”) to update you regarding DTDF’s efforts to collect assets and to make distributions to investors. I am pleased to report DTDF is distributing \$7.0 million to DTDF investors, which represents 4.7% of the total investment in DTDF of just under \$149.6 million. This is the third distribution to investors (the first was in December 2007 and the second was in February 2009), bringing the total return of investment to 13.4% (first distribution of 2% plus second distribution of 6.7% plus third distribution of 4.7%).

For those investors who do not have a custodial account, your portion of the \$7.0 million distribution is enclosed. For investors with custodial accounts, your portion of the \$7.0 million distribution was mailed to the custodian of your DTDF investment.

We continue to focus on recovering assets and on the investigation and prosecution of causes of action against potential recovery targets. This letter builds off of the information provided in the previous letters and covers the following topics:

1. Communications with DTDF Investors
2. Accessing the DTDF Website
3. Settlement with USA Commercial Mortgage Trust (“USACM”)
4. Investigating and Prosecuting Causes of Action against Potential Target Defendants
5. Advocating DTDF Interests in Other Bankruptcy Cases
6. Preserving Assets of Insiders (Thomas Hantges and Joseph Milanowski)
7. Status of Other Recovery Sources
8. Tax Research

## **Communications with DTDF Investors**

We will send you another letter within the next three to four months. As it is very expensive to communicate with our professionals, who bill hourly fees, I am pleased to receive your phone calls and to answer questions about our status to the best of my ability. My personal cell phone number is (702) 239-4222 or you may send us inquiries at [diversifiedfund@orrick.com](mailto:diversifiedfund@orrick.com).

For address changes, please print and complete the Change of Address form posted on the DTDF website (form can be found under 1. Updates/Questions). If you don’t have access to a computer to visit the website, please send a written request with your legal vesting name and account number to DTDF at the following address:

USA Capital Diversified Trust Deed Fund  
C/O FTI Consulting, Inc.  
Two North Central Avenue, Suite 1200  
Phoenix, Arizona 85004

**Accessing the DTDF Website**

The website provides updates on recent developments and is a convenient way to track the progress of DTDF collection efforts. Every letter to DTDF investors, including this one, is posted there. Here are two ways to access the DTDF Website:

- TYPING: Type <http://usacapdtfd.bmcgroup.com/default.aspx> into the browser screen at the top of your monitor.
- GOOGLE: If you type “USA Capital Diversified Information” in Google, the first resulting link should be the DTDF Website. Simply click on the link and you will be at the DTDF Website.

To stay informed of new postings to the website, you can request automatic notifications of website updates. This can also be done by signing up on the website in Section 1. Updates/Questions. By signing up and providing a valid email address, you will receive alerts via email when new content is uploaded to the website.

**Settlement with USA Commercial Mortgage Trust (“USACM”)**

As mentioned in prior letters to DTDF investors, DTDF reached a settlement with USACM in early 2008. As part of the settlement, DTDF received a \$128 million unsecured claim in the USACM Estate and agreed to share DTDF and USACM net litigation recoveries. Litigation recoveries will be split 50% to DTDF and 50% to USACM up to \$20 million and 35% to DTDF and 65% to USACM thereafter.

On October 19, 2009, the Court heard the motion filed by the USACM Trust for an order authorizing the Trust’s initial interim distribution to beneficiaries holding allowed claims. Silar Advisors LP and Asset Resolution LLC filed an objection to that motion, and Silar Advisors, LP and Asset Resolution LLC also filed a complaint against USACM Trust in an effort to block the release of the proceeds of the recovery efforts by the Trust. The Court overruled the Silar and Asset Resolution’s objection and authorized the USACM distribution to the allowed beneficiaries.

As a result, DTDF received funds of approximately \$6.6 million from USACM based on DTDF’s allowed claim. DTDF will receive future disbursements from USACM, however, the amount and timing of future distributions to DTDF as an unsecured creditor of USACM has not been determined.

**Investigating and Prosecuting Causes of Action against Potential Target Defendants**

DTDF and USACM are working together to pursue various lawsuits. The table below shows the active cases where DTDF is a plaintiff. The timing and outcome of each of the cases is unknown at this time, except as otherwise noted below.

<b>Case No.</b>	<b>Defendant</b>
08-01132	Stanley E. Fulton <sup>1</sup>

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<sup>1</sup> Plaintiff is DTDF. The parties participated in mediation in early May 2009, and they remain engaged in ongoing settlement discussions. The Court granted the defendant’s summary judgment motion as to one of DTDF’s claims and as to one aspect of an affirmative defense asserted by Fulton to the remaining claim. The Court vacated the trial date because DTDF intends to challenge this ruling in the district court.

<b>Case No.</b>	<b>Defendant</b>
08-01133	Kathryn L. Petersen; Kathryn L. Petersen Living Trust; KLP Trust dated 7/15/99; Specialized Development Tahoe, LLC <sup>2</sup>
08-01134	Mary Petersen; Mary Petersen Family Trust dated 8/12/98; Michael D. Petersen; Michael D. Petersen Family Trust dated 8/12/98; Kathryn L. Petersen; Kathryn L. Petersen Living Trust; KLP Trust dated 7/15/99 <sup>3</sup>
08-01135	Wells Fargo Bank, N.A. <sup>4</sup>
08-0112-0	David A. Fogg <sup>5</sup>
2:08-CV-461	Deloitte & Touche, LLP; Victoria Loob <sup>6</sup>

### **Advocating DTDF Interests in Other Bankruptcy Cases**

#### USAIP Chapter 11 Case

DTDF and USACM, joined by other creditors of USAIP, filed an involuntary chapter 11 petition against USAIP in early April 2007. As a result, USAIP is a debtor in a bankruptcy case pending in Las Vegas (case #07-11821-LBR). USAIP is the maker of a \$58,374,918.81 promissory note (the “\$58 Million Note”) to USACM for the benefit of creditors (including DTDF). Repayment of the \$58 Million Note and other obligations of USAIP are secured by liens on USAIP’s interest in entities owned 100% or in part by USAIP. DTDF and USACM will share collections on the \$58 Million Note on an equal basis. Lisa M. Poulin was appointed as trustee for USAIP.

DTDF filed a timely proof of claim seeking \$176,380,998 from the USAIP estate. Resolution of claims against the USAIP estate and the possibility of payment are months or years away. DTDF continues to monitor the USAIP case, including reviewing its monthly operating reports.

Per the Monthly Operating Report ending September 2009, USAIP reported that is has approximately \$1.5 million in cash on hand with approximately \$1.1 million in unpaid professional fees. USAIP has also scheduled a hearing to approve the sale of certain of the

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<sup>2</sup> Plaintiff is DTDF. The parties have reached a confidential settlement, subject to the Court’s approval at a hearing to be held on December 2, 2009.

<sup>3</sup> Plaintiffs are USACM and DTDF. The parties have reached a confidential settlement, subject to the Court’s approval at a hearing to be held on December 2, 2009.

<sup>4</sup> Plaintiffs originally were USACM, DTDF and FTDF. FTDF and USACM have dismissed their claims as plaintiffs. The defendant filed a motion to stay this litigation and to compel arbitration. On June 19, 2009, the bankruptcy court denied that motion, meaning that the case will proceed to trial in the bankruptcy court. Trial is anticipated in first or second quarter of 2010.

<sup>5</sup> Plaintiffs are USACM and DTDF. The Bankruptcy Court scheduled a hearing on February 20, 2009 in order to schedule a settlement conference. A settlement conference was scheduled for April 29, 2009, but it was not successful. The district court will set a trial date at a scheduling conference on December 18, 2009. Trial is anticipated in January or February 2010.

<sup>6</sup> Plaintiffs were USACM and DTDF. DTDF’s claims against Deloitte were dismissed on August 15, 2008.

remaining assets (USAIP's interest in Twelve Horses and its interest in Colt Gateway LLC). These proposed sales are \$600,000 on a combined basis.

Tree Moss Partners, LLC Chapter 11 Case

Tree Moss Partners, LLC ("Tree Moss") is a debtor in bankruptcy due to an involuntary bankruptcy petition (Case No. 06-13758-LBR) filed by DTDF. Ms. Poulin has been appointed trustee for Tree Moss. Tree Moss owns 63 units of the condominium project adjacent to the Hotel Zoso in Palm Springs. USAIP's equity in this entity is not pledged as collateral for the \$58 Million Note. DTDF filed a proof of unsecured claim for \$23,116,045 in the Tree Moss case.

The sale of the condominium property that was approved in April 2008 by the Bankruptcy Court did not close. As a result, the Trustee is actively marketing the property for sale. The timing of a sale of the property and subsequent timing and amount of distribution to DTDF are unknown.

HMA Sales, LLC Chapter 11 Case

HMA Sales is a debtor in bankruptcy due to a voluntary chapter 11 petition (Case No 07-12694) filed by USAIP under the control of Ms. Poulin. Ms. Poulin is the trustee for HMA Sales. DTDF and HMA Sales reached a settlement agreement in June 2007 that was discussed in prior letters to investors. As a result of the settlement agreement DTDF received \$8.9 million in 2007 and will receive additional monies from HMA. DTDF continues to monitor the HMA case and work with Ms. Poulin and her counsel to collect additional sums relating to the Royal Hotel.

BySynergy, LLC Chapter 11 Case

BySynergy is also a debtor in bankruptcy due to an involuntary bankruptcy petition (Case No. 08-7680-rtb) filed by parties other than DTDF on June 25, 2008. DTDF is monitoring the bankruptcy case to determine what amounts, if any, will become available for distribution to DTDF on account of BySynergy's loan from DTDF.

**Preserving Assets of Insiders (Thomas Hantges and Joseph Milanowski)**

Thomas Hantges ("Hantges")

Due to the filing of an involuntary bankruptcy petition by DTDF, USACM and other creditors, Hantges is a debtor in a chapter 11 bankruptcy case in Las Vegas, Case No. 07-13163-lbr. Michael Carmel was appointed trustee in the Hantges bankruptcy case.

USACM and the Trustee for the Hantges estate entered into an agreement for prosecution of claims by USACM against Lucius Blanchard, the Blanchard Children's Trust, Palomino Partners and Thomas A. Hantges. The lawsuit was filed by USACM on August 25, 2008 (Case No. 08-01268).

In the adversary proceeding brought by Mr. Carmel as trustee for the Hantges estate against Lucius Blanchard, individually and as trustee of the Hantges Children's Education Trust (No. 08-01002), the parties engaged in discovery and negotiated a settlement for all causes of action in July 2009.

The order approving a global settlement for the above two cases (Nos. 08-01268 and 08-01002) was signed on October 14, 2009.

DTDF continues to monitor the bankruptcy case of Thomas Hantges, however with the settlement of the above referenced litigation, Mr. Carmel filed a motion to convert the Hantges

Chapter 11 bankruptcy case to a Chapter 7 on October 27, 2009. The option was granted on November 13, 2009.

DTDF timely filed a proof of claim against the estate of Hantges seeking the amount of \$182,538,254. Resolution of claims against the Hantges estate and the possibility of payment are months or years away. DTDF continues to monitor the Hantges case.

Joseph Milanowski (“Milanowski”)

Similarly, due to the filing of an involuntary bankruptcy petition by DTDF, USACM and other creditors, Milanowski is a debtor in a chapter 11 bankruptcy case in Las Vegas, Case No. 07-13162-lbr. The Bankruptcy Court entered an order for relief over strenuous objection by Milanowski and his counsel, and thereafter the United States Trustee appointed Ford Elsaesser as the trustee. Milanowski appealed the order for relief, but the United States District Court for the District of Nevada dismissed the appeal on May 8, 2008.

The chapter 11 trustee in the Milanowski bankruptcy case reached a settlement agreement with Milanowski, whereby the trustee will settle the bankruptcy estate's claims against Milanowski for roughly \$1,000,000. On January 9, 2009, the trustee filed a motion to approve the settlement agreement with the Court. An order granting this settlement was filed on May 28, 2009.

DTDF filed a complaint in the bankruptcy court, Adv. No. 07-13162-lbr, to determine the non-dischargeability of Milanowski's debts to DTDF. Similar lawsuits were filed against Milanowski by USACM (No. 08-01093), Aurora Investment L.P (No. 07-01212), the Kehl family (No. 08-01052), the PBGC (No. 08-01044), and BySynergy, LLC (No. 07-01209). Milanowski has answered DTDF's complaint. On October 28, 2008, the Court entered an order staying litigation and discovery pending the conversion of the case to a chapter 7, or the filing of a chapter 11 plan providing for discharge. On November 18, 2009, Mr. Elsaesser filed a motion to convert to chapter 7. The motion will be heard on December 18, 2009.

DTDF filed a proof of claim against Milanowski for \$182,538,254. Resolution of claims against the Milanowski estate and the possibility of payment are months or years away.

On April 23, 2008, the SEC brought an action against Milanowski “in connection with a multi-million dollar fraud” seeking an order requiring Milanowski to disgorge sums obtained. DTDF is not prosecuting this action. The complaint was filed with the United States District for the District of Nevada and is Case No. 2:08-CV-00511. The SEC filed a motion for summary judgment against Milanowski on June 23, 2009. Milanowski responded to the motion on August 17, 2009.

A criminal action was brought against Milanowski by the U.S Attorney's office to which Milanowski pleaded guilty to one count of wire fraud. Milanowski is the only defendant named so far in the criminal case, however, the U.S. attorney's office said the investigation is continuing. The Deputy U. S. Attorney recommended that Milanowski be sentenced to 12 years in prison and be required to make restitution. The Chief U.S. District Judge could sentence him to up to 20 years in prison and fine him up to \$250,000. Sentencing was originally set for October 23, 2009, but was postponed to January 15, 2010 to allow time for Milanowski to cooperate with regards to recovery efforts for DTDF and his other victims. The original guilty plea agreement was initially sealed but is now public.

## **Status of Other Recovery Sources**

### **Colt Loans**

DTDF and the two other direct lenders who are DTDF's co-beneficiaries of a promissory note secured by a first trust deed on certain parcels and buildings comprising a portion of the overall Colt project have, through Connecticut counsel hired by the three, initiated a foreclosure action. The case is working its way through the Connecticut courts.

### **Loans Serviced By Compass/Silar**

Compass was the servicer of nine DTDF loans. Silar Advisors, LLC, represents that Silar foreclosed on its loan to Compass on September 26, 2008, and that Asset Resolution, LLC was an entity created to continue the servicing process. Asset Resolution LLC filed bankruptcy on October 14, 2009. DTDF will monitor the Asset Resolution bankruptcy case to determine how the DTDF loans are impacted by the bankruptcy. There has been no recent collection activity on any of these nine loans.

### **Tax Research**

In light of the recent IRS Ruling and Procedure that deals with theft losses, many of you have asked about the deductibility of such losses. DTDF has listened to such questions and concerns, taking them very seriously, and has discussed the tax issues with a number of tax professionals. Following such discussions, DTDF hired an accounting firm that specializes in tax matters to research and advise DTDF on potential theft loss tax adjustments for DTDF as a fund. We have chosen to seek a pre-filing agreement with the IRS to get IRS approval as to how the losses should be treated. We are working towards, and hope for conclusions by March 2010 when the next K-1s will be mailed out to you.

Although you may not be prohibited from taking any individual tax position as you and your tax professional feel is accurate, you may rest assured that DTDF will claim losses on DTDF's tax return and pass those losses through to investors on Schedules K-1. DTDF will post an update on the website when the research has been concluded and any meetings with the IRS have resulted in either agreement or disagreement.

### **Conclusion**

DTDF has every intention of making one or more distributions in the future, but at this time, we cannot estimate the timing or the amount of the next one. Please know DTDF continues to focus on the recovery of assets and the prosecution of causes of action against potential recovery targets. We continue to ask for your patience, and want to assure you that the Board and the DTDF professionals are giving our best efforts to obtain the best possible recovery for you.

Best Regards,  
Robert G. Worthen  
Chairman of the Board