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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

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COMMISSIONERS

- GARY PIERCE, Chairman
- BOB STUMP
- SANDRA D. KENNEDY
- PAUL NEWMAN
- BRENDA BURNS

ARIZONA CORPORATION COMMISSION
DOCKET CONTROL

JAN 13 2011

DOCKETED BY: *[Signature]*

In the matter of:)	DOCKET NO. S-20719A-09-0583
MORGAN FINANCIAL, LLC, an Arizona limited liability company,)	FIRST AMENDED NOTICE OF OPPORTUNITY FOR HEARING REGARDING PROPOSED ORDER TO CEASE AND DESIST, FOR ADMINISTRATIVE PENALTIES AND FOR OTHER AFFIRMATIVE ACTION
MORGAN FINANCIAL LENDERS, LLC, an Arizona limited liability company,)	
JIMMY HARTGRAVES, JR. and LAURIE HARTGRAVES, husband and wife,)	
Respondents.)	
)	

NOTICE: EACH RESPONDENT HAS 10 DAYS TO REQUEST A HEARING
EACH RESPONDENT HAS 30 DAYS TO FILE AN ANSWER

The Securities Division ("Division") of the Arizona Corporation Commission ("Commission") alleges that respondents MORGAN FINANCIAL, LLC, MORGAN FINANCIAL LENDERS, LLC, and JIMMY HARTGRAVES, JR. have engaged in acts, practices, and transactions that constitute violations of the Securities Act of Arizona, A.R.S. § 44-1801 *et seq.* ("Securities Act").

I.

JURISDICTION

1. The Commission has jurisdiction over this matter pursuant to Article XV of the Arizona Constitution and the Securities Act.

II.

RESPONDENTS

2. MORGAN FINANCIAL, LLC ("MF") is a limited liability company organized in the state of Arizona on July 15, 1996.

1 indirectly make, negotiate, or offer to make or negotiate a mortgage banking loan or a mortgage
2 loan.

3 13. MF's primary business was to originate residential mortgage loans and hard money
4 loans, which are asset-based loan financings through which a borrower receives funds and the
5 repayment obligations are secured by the specifically referenced collateral, generally real estate, of
6 the borrower.

7 14. MF obtained money from individuals ("Investors") to use as working capital in
8 connection with MF's origination of residential mortgage loans and hard money loans.

9 15. In exchange for money received from Investors, MF would execute documents titled
10 promissory notes ("Notes"). MF is identified as the Borrower on each of the Notes issued to
11 Investors, who are identified as the Holder.

12 16. The Notes set forth annual rates of interest from twelve percent (12%) to twenty
13 percent (20%).

14 17. In general, the terms of the Notes required that only interest payments were payable
15 until maturity.

16 18. From approximately February 2006 to October 2010, MF has made a total of
17 approximately \$1,599,380 in interest payments to Investors.

18 19. Concurrent with or shortly after the execution of the Notes, each investor executed a
19 subordination agreement in which they agreed that their payment rights would be subordinated to
20 the rights of MF's creditors.

21 20. For each residential and/or hard money loan originated by MF, a deed of trust was
22 executed and recorded to secure the loan. The deed of trust identified MF as the beneficiary.
23 Investors were not named as beneficiaries on the deed of trust nor secured in any other manner.

24 21. From February 2006 through June 2008, MF executed Notes with approximately 35
25 Arizona residents. HARTGRAVES signed the Notes on behalf of MF as its member.

26

1 22. MF raised approximately \$5,461,700 from the issuance of the Notes. The Notes are
2 not registered with the Commission.

3 **B. MERRILL LYNCH LOAN PORTFOLIO**

4 23. In May 2008, MF through its wholly-owned subsidiary, Morgan AZ Financial,
5 LLC, for approximately \$33,000,000 purchased a portfolio of loans (the "Loan Portfolio"), that had
6 been originated by a bankrupt lender. The Loan Portfolio was purchased from Merrill Lynch Bank
7 USA ("Merrill Lynch").

8 24. At the time of purchase by MF, the Loan Portfolio consisted of construction loans to
9 individuals and builders for custom homes that had principal balances totaling \$50,200,000 and an
10 appraised value of approximately \$70,000,000.

11 25. The real estate properties underlying the Loan Portfolio were located in Arizona,
12 California, Washington, and Nevada. The Loan Portfolio included real estate properties consisting
13 of subdivided lots, partially completed homes, and completed homes.

14 26. MF paid \$2,000,000 at closing to Merrill Lynch who financed the balance of the
15 purchase price (\$33,000,000) of approximately \$31,000,000.

16 27. The terms of purchase of the Loan Portfolio were memorialized through a purchase
17 agreement.

18 28. In addition, an agreement titled Master Repurchase Agreement ("MPA") was also
19 executed and includes, but is not limited to, the following provisions:

20 a) Merrill Lynch has a secured first position on all interest and assets of the
21 Loan Portfolio;

22 b) Profits made from servicing, foreclosure and/or resale of the underlying
23 properties or real estate shall first be paid to Merrill Lynch until the outstanding balance owed
24 (\$31,000,000) has been fully repaid;

25 c) MF would be in default if a judgment in excess of \$100,000 was rendered
26 against MF or one of its affiliates and the judgment was not satisfied, discharged, or bonded within

1 the later of 30 days from the date of entry or the period in which the judgment was stayed, bonded
2 or appealed; and

3 d) Upon default, Merrill Lynch may exercise its default rights, which includes
4 but is not limited to, declaring all outstanding amounts immediately due and to immediately sell all
5 relevant Loan Portfolio assets to be applied to the outstanding amount due to Merrill Lynch.

6 29. From May 2008, to the present, MF has been servicing the Loan Portfolio by
7 collecting payments, foreclosing on certain underlying properties, rehabilitating certain underlying
8 properties, and reselling the note or property.

9 30. The properties foreclosed on are titled in the name of MF or its wholly-owned
10 subsidiary, Morgan AZ Financial, LLC.

11 31. Pursuant to the MPA, Merrill Lynch maintains a secured interest in the Loan
12 Portfolio and all homes foreclosed therein, and the rents, profits, and monies generated there from
13 until the amount outstanding has been satisfied in full.

14 32. Pursuant to an independent auditors report dated as of December 31, 2009, MF had
15 approximately \$19,700,000 in real estate assets acquired through foreclosure of the Loan Portfolio
16 properties and approximately \$13,900,000 in notes receivable net of allowance for doubtful
17 accounts.

18 33. There is approximately \$ 21,973,414 owed by MF on the loan payable to Merrill
19 Lynch.

20 **C. LIMITED LIABILITY COMPANY MEMBERSHIP INTERESTS**

21 34. In or around February 2010, MF presented to Investors an opportunity to exchange
22 their unsecured and subordinated Notes for limited liability company membership interests in MF
23 LENDERS.

24 35. Pursuant to an "Exchange Memorandum Dated May 7, 2010," ("Exchange
25 Memorandum"), MF LENDERS was formed for the sole purpose of consolidating the existing
26

1 unsecured, subordinated Notes issued by MF to Investors into one subordinated, secured loan with
2 a principal amount up to \$6,234,559¹, to be issued by MF LENDERS to MF.

3 36. According to the Exchange Memorandum, Investors holding the Notes issued by
4 MF could exchange their Notes for membership interests in MF LENDERS with initial capital
5 contributions equal to the principal amount of their Notes; however, no new monies would be
6 exchanged between the Investors and MF as a result of the exchange.

7 37. The Exchange Memorandum further sets forth that the loan made by MF LENDERS
8 to MF would be secured by a collateral assignment by MF to MF LENDERS of MF's second lien
9 on the Loan Portfolio. Further, a UCC financing statement would be filed listing MF Lenders as the
10 beneficiary.

11 38. The Exchange Memo includes the following additional information:

12 a) MF intends to repay the loan to MF LENDERS in approximately 30 months;

13 b) MF would service the notes underlying the Loan Portfolio, foreclose,
14 rehabilitate, and/or re-sell the properties underlying the Loan Portfolio. MF would have broad
15 discretion in the management and operation of MF Lenders. In addition, MF would conduct the
16 day to day operations of MF Lenders;

17 c) After the amount owed to Merrill Lynch is repaid, then the proceeds from
18 management of the loan portfolio will be applied first to repay the principal of the loan made by
19 MF LENDERS to MF, second, to pay the stated interest (8%), and third, to pay the additional
20 interest equal to one-half of the net profits derived from MF's management of the loan portfolio;
21 and

22 d) Upon repayment of the amount owed to Merrill Lynch, MF and MF Lenders
23 would share equally the net profits derived from MF's management of the loan portfolio.

24 39. The Exchange Memo also included a copy of the MF LENDERS operating
25 agreement.

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¹ Includes the amount (\$897,000) of the promissory note issued to Hartgraves by MF in exchange for his investment.

1 **VII.**

2 **HEARING OPPORTUNITY**

3 Each respondent, including Respondent Spouse, may request a hearing pursuant to A.R.S.
4 § 44-1972 and A.A.C. R14-4-306. **If a Respondent or a Respondent Spouse requests a hearing,**
5 **the requesting respondent must also answer this Notice.** A request for hearing must be in writing
6 and received by the Commission within 10 business days after service of this Notice of Opportunity
7 for Hearing. The requesting respondent must deliver or mail the request to Docket Control, Arizona
8 Corporation Commission, 1200 W. Washington, Phoenix, Arizona 85007. Filing instructions may be
9 obtained from Docket Control by calling (602) 542-3477 or on the Commission's Internet web site at
10 <http://www.azcc.gov/divisions/hearings/docket.asp>. Additional information about the administrative
11 action procedure may be found at
12 <http://www.azcc.gov/divisions/securities/enforcement/AdministrativeProcedure.asp>.

13 If a request for a hearing is timely made, the Commission shall schedule the hearing to begin
14 20 to 60 days from the receipt of the request unless otherwise provided by law, stipulated by the
15 parties, or ordered by the Commission. If a request for a hearing is not timely made the Commission
16 may, without a hearing, enter an order granting the relief requested by the Division in this Notice of
17 Opportunity for Hearing.

18 Persons with a disability may request a reasonable accommodation such as a sign language
19 interpreter, as well as request this document in an alternative format, by contacting Shaylin A.
20 Bernal, ADA Coordinator, voice phone number 602/542-3931, e-mail sabernal@azcc.gov.
21 Requests should be made as early as possible to allow time to arrange the accommodation.

22 **VIII.**

23 **ANSWER REQUIREMENT**

24 Pursuant to A.A.C. R14-4-305, if a Respondent or a Respondent Spouse requests a hearing,
25 the requesting respondent must deliver or mail an Answer to this Notice of Opportunity for
26 Hearing to Docket Control, Arizona Corporation Commission, 1200 W. Washington, Phoenix,

1 Arizona 85007, within 30 calendar days after the date of service of this Notice. Filing instructions
2 may be obtained from Docket Control by calling (602) 542-3477 or on the Commission's Internet
3 web site at <http://www.azcc.gov/divisions/hearings/docket.asp>.

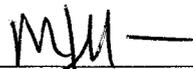
4 Additionally, the answering respondent must serve the Answer upon the Division. Pursuant
5 to A.A.C. R14-4-303, service upon the Division may be made by mailing or by hand-delivering a
6 copy of the Answer to the Division at 1300 West Washington, 3rd Floor, Phoenix, Arizona, 85007,
7 addressed to Phong (Paul) Huynh.

8 The Answer shall contain an admission or denial of each allegation in this Notice and the
9 original signature of the answering respondent or respondent's attorney. A statement of a lack of
10 sufficient knowledge or information shall be considered a denial of an allegation. An allegation
11 not denied shall be considered admitted.

12 When the answering respondent intends in good faith to deny only a part or a qualification
13 of an allegation, the respondent shall specify that part or qualification of the allegation and shall
14 admit the remainder. Respondent waives any affirmative defense not raised in the Answer.

15 The officer presiding over the hearing may grant relief from the requirement to file an
16 Answer for good cause shown.

17
18 Dated this 13 day of January, 2011.

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21 _____
22 Matthew J. Neubert
23 Director of Securities
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25
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