

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MINNESOTA
Civil No. 08-5348 (ADM/JSM)

UNITED STATES OF AMERICA,)
)
Plaintiff,)
)
v.)
)
THOMAS JOSEPH PETTERS, et. al.,)
)
)
Defendants.)

**MEMORANDUM OF LAW IN SUPPORT OF MOTION OF RECEIVER FOR
ORDER AUTHORIZING AND CONFIRMING PURCHASE AND OPTION
AGREEMENT RELATING TO STOCK OF REDSTONE AMERICAN GRILL,
INC.**

Douglas A. Kelley, by and through his counsel, respectfully submits this memorandum of law, in support of his motion for an order authorizing and confirming the purchase and option agreement relating to the stock of Redstone American Grill, Inc..

BACKGROUND AND ARGUMENT

1. Defendant Thomas Joseph Petters owns (subject to existing liens): (i) 1,325,000 common shares (the “Common Shares”) of Redstone American Grill, Inc. (“Redstone Grill”); and (ii) a 33.33% membership interest in Midtown Partners, LLC, a Minnesota limited liability company (“Midtown Partners”) that owns 2,500,000 preferred shares (the “Preferred Shares”) of Redstone Grill; (the foregoing Common Shares and

33.33% membership interest being collectively referred to as the “Property”). (Aff. Receiver at ¶ 2.)

2. Redstone Grill and its subsidiaries operate five restaurants, located in Minnetonka and Eden Prairie, Minnesota; Oakbrook Park, Illinois; Marlton, New Jersey and Plymouth Meeting, Pennsylvania. (*Id.* at 3.) As of May 30, 2009, these five restaurants employed approximately 700 full-time and part-time employees. Redstone Grill incurred a substantial financial loss in 2008, primarily due to slower sales in the third and fourth quarter and costs relating to abandoned expansion plans. (Aff. C. Oberlander.)

3. During 2008, approximately 34% of Redstone Grill’s total revenue was from the sale of alcoholic beverages. Each of the five Redstone Grill restaurants has a license to sell alcoholic beverages. The continued operation of all of the restaurants is dependent upon maintenance of a liquor license for each of the restaurants. (*Id.* at ¶ 4.)

4. The Common Shares constitute approximately 16.3% of Redstone Grill’s outstanding common stock. The Preferred Shares owned by Midtown Partners (in which Mr. Petters has a one-third ownership interest) are convertible into additional shares of Redstone Grill common stock on a one-for-one basis. (*Id.* at ¶ 5.)

5. A subsidiary of Redstone Grill is a party to a Consent Order issued by the New Jersey Department of Law and Public Safety, Division of Alcoholic Beverage Control, which requires that Redstone Grill must cease to have Mr. Petters as a stockholder no later than July 15, 2009. Failure to comply with the Consent Order will result in loss of the New Jersey restaurant’s liquor license. Redstone Grill faces similar

loss of its other liquor licenses if Mr. Peters remains a stockholder of Redstone Grill. (*Id.* at ¶ 6); (Aff. Receiver at ¶ 4.)

6. Redstone Grill reasonably believes that loss of its New Jersey liquor license will lead to the closure of its New Jersey restaurant, the closure of its other restaurants, and the loss of employment for substantially all of Redstone Grill's employees. (Aff. Receiver at ¶ 5.)

7. Redstone Grill is in default under its principal credit agreement with its principal lender and is in negotiations with the lender to attempt to obtain a waiver of those defaults. Redstone Grill has advised that the loss of the New Jersey liquor license would likely result in the immediate acceleration of all outstanding indebtedness to this lender and the probably liquidation of Redstone Grill. (*Id.* at ¶ 6); (Aff. C. Oberlander at ¶ 7.)

8. The Common Shares and the Preferred Shares have been pledged to Home Federal Savings Bank ("Home Federal") to secure a loan of \$5 million that Home Federal made to Midtown Partners in July 2007. A second lien security interest in the Common Shares and in Mr. Petters' membership interest in Midtown Partners is claimed by Edgebrook, Inc. ("Edgebrook") to secure a \$4 million promissory note issued to it by Mr. Petters in August 2008. (Aff. Receiver at ¶ 7); (Aff. C. Oberlander at ¶ 8.)

9. Because of the recent losses sustained by Redstone Grill, the security interest of Home Federal and the possible security interest of Edgebrook, the default under the credit agreement, and current conditions in the restaurant industry and the national economy, the Receiver believes that the market value of Mr. Petters' equity

interest in the Property, taking into account the related debt, is currently zero, or at best a nominal amount. (Aff. Receiver at ¶ 8); (Aff. C. Oberlander at ¶ 9.)

10. Counsel for the Receiver and the Receiver for Redstone Grill, have negotiated with Redstone Grill, Home Federal and Edgebrook the terms of a Purchase and Option Agreement (with consents by Home Federal and Edgebrook) under which (i) the Receiver would sell to a subsidiary of Redstone Grill all of Mr. Petters' equity interest in the Property (subject to existing security interests) for \$75,000 in cash, and (ii) the Receiver would obtain a three year option to repurchase the Property for \$75,000 if the Receiver elected to do so. The option affords the Receiver or his assignee the possibility of re-acquiring the Property for possible re-sale at a higher price if during the next three years the value of the Property recovers in value. (Aff. Receiver at ¶ 9, Ex. A Option Agreement); (Aff. C. Oberlander at ¶ 10.)

11. The Receiver recognizes that because of the purported security interests in the Property, if in the future there is a foreclosure of one or more of those security interests, the option under the Purchase and Option Agreement to purchase the equity of the Property would likely become worthless. However, if nothing is done now to remove Mr. Petters' ownership of the Property, then there is a great risk that Redstone Grill will go out of business in the near future, due to loss of its liquor licenses. Thus a sale now of Mr. Petters' interest in the Property for \$75,000, which the Receiver believes is more than its current market value, (i) realizes \$75,000 in cash now, (ii) avoids a significant risk in the near future that the Property will never have the opportunity to recover in

value, and (iii) preserves some possibility of realizing more value for the Property in the future. (Aff. Receiver at ¶ 10.)

12. In order to avoid loss of Redstone Grill's liquor licenses and loss of employee jobs, and to create the possibility of realizing a greater value for Property at some point in the future, it is in the best interests of the receivership for the Receiver to enter into the Purchase and Option Agreement and close the sale of the Property as provided therein. (Aff. Receiver at ¶ 11); (Aff. C. Oberlander at ¶ 11.)

13. On June 16, 2009, Plaintiff United States of America and Douglas A. Kelley, as Receiver for said Defendant Thomas Petters stipulated as to the matters set forth in the of Affidavit of the Receiver regarding the Purchase and Option Agreement relating to the stock of Redstone American Grill, Inc. and Affidavit of Craig Oberlander Regarding Purchase and Option Agreement relating to the stock of Redstone American Grill, Inc., (collectively, the "Affidavits") and agreed that an Order may be issued by the Court authorizing the Receiver to enter into the Purchase and Option Agreement and close the sale provided for therein. Defendant Thomas Petters refused to enter into the stipulation. (Stipulation.)

CONCLUSION

For the foregoing reasons, we respectfully request the Court issue an Order authorizing Douglas A. Kelley, as Receiver for Thomas Joseph Petters, to enter into and carry out the terms of the Purchase and Option Agreement relating to the stock of Redstone American Grill, Inc. in accordance with the terms and conditions thereof.

DATED: June 23, 2009

LINDQUIST & VENNUM P.L.L.P.

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