UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

UNITED STATES SECURITIES AND EXCHANGE COMMISSION, Plaintiff,	No. 18-CV-5587
vs.	Hon. John Z Lee
EQUITYBUILD, INC., EQUITYBUILD FINANCE, LLC, JEROME H. COHEN, and SHAUN D COHEN, Defendants.	Magistrate Judge Young B Kim

CREDITOR 1839 FUND I, LLC'S BRIEF IN OPPOSITION TO LENDERS' MOTION FOR LEAVE TO PERMIT BANKRUPTCY CASES FOR RECEIVERSHIP ENTITIES

NOW COMES 1839 Fund I, LLC, a creditor of the receivership entities, by and through its attorney, Kurtz & Augenlicht LLP, and in response to certain creditor's Motion for Leave to Permit Bankruptcy Cases for Receivership Entites states as follows:

I. INTRODUCTION

While the Movants' Motion serves as a glowing advertisement for the admittedly exceptional judges of the Bankruptcy Court for the Northern District of Illinois, it fails to engage with the substance of their own request in any meaningful way. Bankruptcy proceedings are more than a set of rules and a watchful U.S. Trustee; they are a machine designed to take the entirety of an insolvent debtor's assets, fit claims into the debtor's means, and pay to those creditors whatever the bankruptcy trustee can. The bankruptcy trustee, not the U.S. Trustee, is vested with a great deal of discretionary power over sales and to avoid transactions based on fraud. The latter is particularly concerning in a case where the overwhelming majority of claims are based on transactions made as part of a Ponzi scheme, perhaps the most famous type of fraud. Further, granting individual creditors the ability to file involuntary bankruptcy proceedings against receivership entities in a targeted and piecemeal fashion would have profound, negative repercussions on the Receiver's ability to manage the receivership estate and this

Court's ability to manage the litigation, sale of property, and restitution for all creditors who were caught up in the Cohens' scheme.

II. BANKRUPTCY WOULD ALLOW THE INSTITUTIONAL LENDERS TO PREFERENTIALLY CARVE UP THE RECEIVERSHIP ESTATE

While the Motion states that the receivership estate is insolvent, it provides no document nor references any which would demonstrate the estate's insolvency. [Doc. 538 ¶ 2]. The Receiver has stated that the estate is solvent, however it is difficult to discern how either party can definitively make these statements when the claims process has not yet closed. On a fundamental level, bankruptcy is only available to bankrupt debtors, individuals and organizations whose debts outsize their assets. It is impossible to even determine whether the estate as a whole owes more than it has when the Receiver, with the approval of this Court, has determined how much it owes, and to whom. Leaving aside the procedural hurdles and conflicts of moving a receivership estate into bankruptcy, this request with regard to the estate writ large is unsupported and at best premature, considering the Receiver himself has stated in his most recent report that "no conclusions have been made by the Receiver nor is the Receiver making any recommendation to the Court in this report as to the certainty, eligibility, or priority of any claim at this time." [Doc. 548 p. 2].

Movants later hone on the idea of bankruptcy for individual receivership defendants. While suffering from the same incomplete information as a bankruptcy of the entirety of the estate, the problem on an individual receivership defendant level is less pronounced. However, this case presents more than a simple "liquidation of assets," "distribution of those concomitant proceeds," and "adjudicating of competing claims" which Movants tout as superior to the process established by this Court. [Doc. 538 ¶ 5, 15, 20]. The receivership defendants are all parts of a larger puzzle crafted by the Cohens to hide, exaggerate, and transfer assets in a longstanding scheme to defraud their creditors. The SEC and Receiver have alleged, and this Court acknowledged the possibility of, manipulation of secured interests as part of this scheme leading to confused and potentially duplicative interests due to those transfers. [Doc. 223 pp. 8-9].

Bankruptcy proceedings are completely unprepared to take this holistic approach to the assets put in receivership because the entire system is designed for one debtor and one set of property held by that debtor placed in a bankruptcy estate. *See* 11 U.S.C. § 541. By taking specific, individual debtors out of the Cohens' constellation of interchangeable fraud vehicles, Movants would be able to identify the most valuable targets for which they have claims and isolate those assets from the claims of other creditors holding fraudulently manipulated or unsecured claims that would, when taken as whole, be attributable to those defendants. The end result of this would be the dilution of the receivership estate for the benefit of these Movants and the detriment of other creditors. It would further fracture the uniform treatment of creditors, as different receivership entities' cases would be assigned to different bankruptcy judges and bankruptcy trustees, leading to multiple and feasibly inconsistent trustee actions and court orders as each entity is treated separately rather than as part of a whole. This is a particular danger due to the broad avoidance powers enjoyed by each individual bankruptcy trustee, exercised largely at their discretion.

III. THE BANKRUPTCY TRUSTEE'S AVOIDANCE POWER WOULD PRECLUDE UNIFORM AND EQUITABLE HANDLING OF CLAIMS

Of special concern in this context is the Trustee's broad authority to avoid fraudulent and preferential transfers. As the SEC noted in its Complaint, Defendants operated their business, recruiting new lenders, operating real estate, and paying funds, up until the date of this Court's injunction. [Doc. 1 pp. 12-13]. Every one of those payments was a preferential transfer under the Bankruptcy Code, and potentially could be avoided if the trustee exercises their discretion to do so and the bankruptcy judge finds that this Court's stay tolled the pre-petition look-back period for preferential transfers. *See* 11 U.S.C. § 547 (b). This would serve to further muddy the waters as defrauded creditors would be dragged into various bankruptcy proceedings to fight over the origin of funds and the rights of distribution for a specific receivership entity. Worse, since the entire business arrangement was fraudulent, none of the "good faith and honest dealing" affirmative defenses to avoidance – new value, ordinary course of business, or purchase money security interests – would be available. The bankruptcy trustee could, in sound judgment and proper use of their discretion, use this small snapshot of the larger Ponzi scheme and turn it into a weapon against those creditors not involved in that receivership entity's bankruptcy.

This risk is particularly grave regarding the trustee's ability to avoid fraudulent transfers. The trustee generally may, at their discretion, avoid a transaction which was made "with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date such transfer was made or such obligation was incurred." 11 U.S.C. § 548 (a) (1) (A). The object of every Ponzi scheme is to hinder creditors by robbing Peter to pay Paul, and the SEC's allegations show this scheme was no different. [Doc. 1 ¶ 45]. A creditor whose transfer with respect to the assets of one receivership entity is targeted by the trustee would have no defense whatsoever since the entire object of all transactions were fraudulent. In that way, an unwary trustee could, in an honest attempt to clear title and deliver value to the "legitimate" creditors of the bankruptcy estate, irrevocably destroy the rights, even secured rights, of non-bankruptcy creditors of the Cohens' scheme.

This specific power has a look-back period of 2 years from the petition date, although it is again unclear how a bankruptcy judge would handle the potential tolling by this Court's stay. *See* 11 U.S.C. § 548 (a) (1). This date can be extended if the trustee has similar remedies under applicable state law. 11 U.S.C. § 544 (b); *In re Kaiser,* 525 B.R. 697 (Bankr. N.D.Ill. 2014). The Seventh Circuit has recognized that a state's codification of the Uniform Fraudulent Transfer Act ("UFTA") is the relevant statute for avoidance of fraudulent transfers and provides the trustee with the power to avoid transfers on behalf of unsecured creditors of the estate. *In re Equip. Acquisition Res., Inc.*, 742 F.3d 743, 746

(C.A. 7, 2014). This time period puts creditors who bought in or had their interests modified by the defendants from 2014 to the present at risk. This is notable and concerning because according to the SEC, 2017 was the year the Cohens' converted their operation into real estate funds, which as interests in personal property rather than real property are much more malleable and vulnerable to manipulation. [Doc. 1 ¶¶ 53-56]. This period would also cover a number of investors who were forced to convert secured notes to unsecured notes by the defendants, such as this creditor. [Doc. 1 ¶ 49]. While potentially helpful to particular creditors, the discretionary nature of this relief, the fragmented proceedings before the various courts, and the profound effect on the nature of the receivership estate as a whole exposes every creditor to an extreme amount of risk for loss and inequitable treatment by a trustee unable to see the forest for the trees.

IV. THE BANKRUPTCY PROCESS IS POORLY EQUIPPED TO HANDLE THIS CASE

These two major concerns demonstrate the significant and unacceptable risk to creditors, particularly smaller creditors which comprise the majority of claims, of allowing the moving creditors to seek bankruptcy relief against individual receivership entities. At best, the proceedings would create another layer of bureaucracy with the only benefit being duplicative rules and a specialized but extremely crowded venue. At worst, it would allow creditors to slice up the receivership estate, push for individual trustees to exercise their avoidance powers to gain inequitable advantage over other creditors, and potentially bleed the whole estate dry. Considering this Court has already enacted a stay, a claims process, and a plan for orderly liquidation of the receivership assets, there is nothing to be gained by going into bankruptcy and for many creditors a significant risk of loss. The court should deny this motion.

Dated: October 29, 2019

Respectfully submitted,

/s/ Michael O'Malley Kurtz

Michael Kurtz(mkurtz@kalawchicago.com)
Kurtz & Augenlicht LLP
123 W Madison St, Ste. 700
Chicago, IL 60602
P: (312) 265-0106
F: (312) 265-0254
Counsel for 1839 Fund I, LLC

CERTIFICATE OF SERVICE

I hereby certify that I provided service of this Response to all counsel of record via the Court's ECF system on October 29, 2019.

/s/ Michael O'Malley Kurtz

Michael Kurtz(mkurtz@kalawchicago.com)
Kurtz & Augenlicht LLP
123 W Madison St, Ste. 700
Chicago, IL 60602
P: (312) 265-0106
F: (312) 265-0254
Counsel for 1839 Fund I, LLC