UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

U.S. SECURITIES AND EXCHANGE COMMISSION,	)	
Plaintiff,	)	**Civil Action No. 18-CV-5587**
v.	)	**Judge John Z. Lee**
EQUITYBUILD, INC., *et al.*,	)	**Magistrate Judge Young B. Kim**
Defendants.	)	

SEC'S RESPONSE IN OPPOSITION TO LENDERS' MOTION TO FORCE RECEIVERSHIP ENTITIES INTO BANKRUPTCY

Having failed to derail the Receiver's liquidation of real estate, initiation of an orderly claims process, and receipt of compensation for his work, the institutional lenders now seek to force the Receiver into bankruptcy and divest this Court of jurisdiction. While the lenders claim that bankruptcy would be more "efficient" and "economical," the opposite is true. Adding a bankruptcy trustee, who would need to start over at square-one, would impose another layer of administrative expenses that would cut into the recovery of the victimized investors, institutional lenders, and other creditors. And, despite the lenders' claims that bankruptcy provides a more specialized court to administer the receivership estate, it is apparent the lenders are merely forum shopping for a new tribunal that may offer them, but not the victimized investors, better outcomes. For these reasons and those discussed below, the Court should deny the lenders' motion.

1. Background

It bears emphasizing that the lenders, who seek to dictate the Receiver's liquidation and distribution efforts, comprise a minority of the receivership's creditors. As reflected by the Receiver's claims analysis submitted to the Court (ECF 548-1), out of the approximately 1,780 claims submitted to the Receiver, less than 100 were submitted by the institutional lenders compared to more than 1,640 submitted by investors.[1] Moreover, the $121.6 million in collective claims made by the victimized investors nearly double the $67.9 million in claims made by the institutional lenders.

While the lenders' collective claims are much smaller than those of the investors, the lenders have played an outsized role in shaping the Receiver's work to sell properties and administer an orderly claims process. Specifically, through their repeated objections, the lenders have had a real voice in influencing the Receiver's efforts. A prime example is being granted the right to credit bid and set certain terms of the bidding. Other examples include requiring the Receiver to segregate rents, modify his deadlines, and provide the lenders with various categories of information to inform their credit bidding decisions.

With the Court having resolved the lenders' objections, the Receiver is finally able to complete his mandates of liquidating real estate and administering the claims process. This month, the Receiver obtained Court approval to consummate the sale of the second tranche of real estate in his liquidation plan (ECF No. 545) and to begin the public sales process for the fifth tranche (ECF No. 540).[2]

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[1] The approximately 40 remaining claims, totaling around $1.6 million, were submitted by other creditors including trade creditors and the City of Chicago.

[2] The sales of the first, third, and fourth tranches were approved by May 21, 2019. (ECF 346, 378)

Regarding the claims process, the Receiver recently reported that: (a) the vast majority of potential claims have already been submitted, (b) the limited number of outstanding claims will be received by November 20, and (c) the Receiver is beginning to evaluate the validity and priority of the submitted claims. (ECF No. 548).

Given all that the Receiver has accomplished, even the lenders acknowledge that "[m]uch of the work is…already done." (Oct. 8, 2019 Hearing Tr. at 13:14-15).

2. Transferring Receivership Entities to a Bankruptcy Trustee is Neither Efficient nor Economical

Despite conceding that the Receiver has already undertaken so much work, the lenders want the Receiver to go pencils-down, and transfer all of his liquidation and distribution responsibilities to a bankruptcy trustee. The lenders claim that forcing receivership entities into bankruptcy is "efficient," "economical," and would "reduce expenses." (ECF 538, pp. 2, 8). This claim is belied, in the first instance, by the fact that bankruptcy would require the appointment of a trustee, adding a second layer of administrative expenses that would significantly deplete the funds available to creditors.[3]

Not only would a bankruptcy trustee (and presumably the law firm of its choosing) require the expenditure of significant assets, much of the trustee's work would be duplicative, unnecessary, and delay recovery for the creditors. At the very least, a trustee would devote substantial time and resources on basic introductory work that the Receiver has already performed. Examples include: gaining an understanding of Equitybuild's business, becoming familiar with this litigation and its voluminous docket, reviewing large amounts of relevant

[3] The lenders propose that the Receivership would continue while certain receivership entities go into bankruptcy. (ECF 538, p. 3 ("Nor are the Lenders requesting that the Receiver relinquish his role.")). This proposal thus requires two sets of administrative expenses, one for the Receiver and one for a bankruptcy trustee.

documents, and selecting professionals to assist in the liquidation of properties and administer the claims process. Presumably, any trustee and multiple attorneys the trustee retains would bill for this time-consuming work. There is no valid reason to saddle investors and other creditors with the heavy costs required to get a trustee up to speed and able to pick up where the Receiver is now.

Putting aside the heavy transaction costs required to transfer receivership entities into bankruptcy, the lenders fail to articulate why a bankruptcy trustee would be more capable than the Receiver in completing the Receiver's work of liquidating properties and administering the claims process. These are bread-and-butter tasks for any receiver, and the Receiver here has made significant headway on both fronts. Indeed, the Court has already approved the Receiver's liquidation and claims-process proposals, and the Receiver should be allowed to complete his work per the processes approved by the Court.

3. The Lenders' Reasons for Preferring Bankruptcy are Unavailing

While the lenders advance a variety of reasons why they prefer bankruptcy, none are persuasive. For instance, the lenders tout the protections of the bankruptcy code's automatic stay provisions, which preclude litigation against the debtor outside of bankruptcy court. (ECF 358, p. 5 ¶ 13). But the lenders ignore that the Court has already ordered a stay of litigation in its Order Appointing Receiver, rendering a bankruptcy stay redundant. (ECF 16, ¶¶ 32-34). The lenders also point to bankruptcy-specific asset sale guidelines which will "eliminate much of the issues" surrounding the Receiver's efforts to liquidate real estate. (ECF 538, p. 4 ¶ 9). However, the lenders' objections to the sales process have since been resolved by the Court (ECF 540, 545), and there are no outstanding liquidation issues the lenders identify as being more

appropriately resolved in bankruptcy.[4]

Next, the lenders claim that bankruptcy is better because, unlike a magistrate judge, a bankruptcy court can issue final orders. (ECF 538, p. 6 ¶ 18). However, the lenders acknowledge that a bankruptcy court's orders are entitled to review by a district court. (*Id.*). The lenders have repeatedly shown the willingness to appeal Magistrate Judge Kim's rulings that do not go their way. There is scant reason to suggest they would not appeal bankruptcy rulings adverse to their interests. Because a district court would ultimately be the arbiter of any bankruptcy ruling, there is no efficiency gained by having a bankruptcy court, as opposed to Magistrate Judge Kim, be the initial tribunal to hear the parties' disputes.[5]

Finally, the lenders claim bankruptcy is preferable because of the presence of a "neutral" U.S. Trustee. (ECF 537, pp. 5-6, ¶¶15-16). Yet the lenders overlook that the Receiver himself is a neutral third party, who is an agent of the Court tasked with maximizing the pool of assets available to *all* of the estate's creditors. Indeed, in approving the Receiver's fee applications, the Court recognized the importance of allowing the Receiver to complete his work:

> there is a significant need for the receiver assets to be managed by a *neutral party* until an orderly claims process is concluded. Thus, the Court finds that the receiver's efforts have benefitted, and will continue to benefit, the receivership estate…

(October 8, 2019 Hearing Tr. at 7:2-7) (emphasis added).

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[4] The lenders complain this case has been "bogged down" by "inefficiencies and uncertainties" the lenders claim would be avoided in bankruptcy. (ECF 538, p. 7 ¶ 20). But responsibility for the delays in this case rest squarely with the lenders, who have objected to virtually all of the Receiver's actions. Now that the Court has resolved the lenders' objections, there is no reason – absent more obstruction from the lenders – that the liquidation and claims processes cannot proceed in a more expeditious manner.

[5] Any suggestion that a bankruptcy court, as opposed to Magistrate Judge Kim, is more likely to reach the "correct" decision on any given issue is belied by the fact that this Court has repeatedly affirmed Magistrate Judge Kim's rulings. Even the lenders acknowledge that the current forum is "capable" of handling the liquidation and claims processes. (October 8, 2019 Hearing Tr. at 12:5).

While the lenders lament that many of the Receiver's actions are not in *their* best interest, they cannot establish that the Receiver is acting adverse to the creditor pool as a whole. Because the lenders make up only a minority of the receivership's creditors, the lenders' preferences as to forum should not be given greater weight than the vast majority of the creditors who have not objected to the Receiver's conduct. This notion is particularly apt given the equitable nature of the receivership, which flows from a massive Ponzi scheme that victimized hundreds of investors. The lenders overlook that equitable remedies that are available in this forum, but not bankruptcy, may be the preferable vehicle for resolving the competing claims of the receivership's various classes of creditors.

4. The Decision Whether to Enter Bankruptcy Should Rest with the Receiver

The Court's Order Appointing Receiver is explicit that the decision whether to enter bankruptcy rests with the Receiver, as opposed to any third party. (ECF 16, p. 22, ¶ 51). The Order is equally clear that it "bar[s] any person or entity, other than the Receiver, from placing any of the Receivership Defendants in bankruptcy proceedings." (*Id.*, ¶ 52). By imposing these restrictions, the Court entrusted the decision to enter bankruptcy to the Receiver's sound business judgment. The Court should not allow minority creditors such as the lenders to usurp that discretion, especially when the Receiver adamantly opposes the bankruptcy forum.

5. Conclusion

Transferring this case to bankruptcy would be highly inefficient, impose another level of administrative expense (a trustee), cause delay, and require the duplicative and unnecessary expenditure of resources. Moreover, the lenders have not made a showing that the liquidation and claims procedures approved by this Court, and tailored to the specific nature of this case, are in any way inferior to those available in bankruptcy. Rather, the lenders' motion is a rank

attempt at forum shopping that should not be countenanced.

Dated: October 29, 2019

Respectfully submitted,

/s/ Benjamin Hanauer

Benjamin J. Hanauer (hanauerb@sec.gov)
Timothy J. Stockwell (stockwellt@sec.gov)
U.S. Securities and Exchange Commission
175 West Jackson Blvd., Suite 1450
Chicago, IL 60604
Phone: (312) 353-7390
Facsimile: (312) 353-7398

CERTIFICATE OF SERVICE

I hereby certify that I provided service of the foregoing Response, via ECF filing, to all counsel of record and Defendant Shaun Cohen, on October 29, 2019. I further certify that I caused the foregoing Response to be served on Defendant Jerome Cohen, via email at jerryc@reagan.com.

/s/ Benjamin Hanauer

Benjamin J. Hanauer
175 West Jackson Blvd., Suite 1450
Chicago, IL 60604
Phone: (312) 353-7390
Facsimile: (312) 353-7398

One of the Attorneys for Plaintiff