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 REPLY SUPPORTING RECEIVER'S NINTH MOTION TO CONFIRM SALES

The SEC supports the Receiver's Ninth Motion to Confirm the Sale of Real Estate (ECF No. 749). Of the fourteen properties the Receiver's Motion seeks to sell, objections have been lodged for only two. (ECF No. 769). These objecting institutional lenders, Citibank and Fannie Mae, are among the approximately 30 claimants on each of the two properties, with the other claimants being defrauded investors. (ECF No. 693, pp. 17-20). In their objections, Citibank and Fannie Mae ask the Court to ignore the competing claims of the investors and forego the claims resolution process the Court has spent months working to implement. Instead, Citibank and Fannie Mae seek to bypass the claims process altogether. They demand the two properties be either abandoned to them or have their sales proceeds simply turned over, without any due process afforded to the victimized investors.

Beyond being inconsistent with this case's equitable nature and contrary to the priority determination processes Citibank and Fannie Mae have themselves proposed to the Court, most of their objections have already been overruled. For these reasons, and those discussed below, the Court should similarly overrule their objections and allow the Receiver's sales to proceed.

A. Citibank's and Fannie Mae's Objections Relate to Two Properties that are Subject to Competing Claims of Victimized Investors

The Receiver's Ninth Sales Motion seeks to confirm the sales of fourteen residential apartment buildings. (ECF No. 749, p. 15). The only objections to that Motion are Citibank's objection to the sale of 6250 South Mozart and Fannie Mae's objection to the sale of 1113-41 East 79th Place (ECF No. 769).[1] The Receiver's index of claims shows that for the two properties, Citibank and Fannie Mae each compete with the claims of approximately 30 defrauded investors. (ECF No. 693, pp. 17-20). For the Mozart property, the Receiver observes that investors recorded mortgages on the property more than fifteen months before Citibank recorded its mortgage, a fact that Citibank does not dispute. (ECF No. 749, pp. 21-22). While the Receiver does not identify any investor mortgages on the 79th Place property, approximately 30 investors have filed claims, presumably with the expectation of being heard in an orderly claims process. (ECF No. 693, pp. 17-20).

While the SEC acknowledges that certain of the investor claims on the two properties exceed $100,000, many of the claims are much smaller. For instance, the Receiver notes that lower-dollar investor claims exist on the Mozart property in amounts such as $3,500, $7,009, $7,330, $10,000, and $14,200. (ECF No. 693, pp. 19-20). Similarly, for the 79th Place property, investors asserted claims of $8,450, $11,000, $15,000, and $17,251. (*Id.* at 17-18). These lower value claims are consistent with other small investor claims asserted on properties throughout the

[1] For the component of the Receiver's motion that seeks the restoration of certain rent proceeds, the only substantive objection was lodged by a small group of investors. (ECF No. 764). Those investors ignore that the Court has already granted a functionally identical motion by the Receiver to restore rent proceeds for another property. (*See* ECF Nos. 460, 493 & 494). Because the Receiver's grounds for restoring rent proceeds in his current Motion are the same as for the motion the Court previously granted, and for the reasons stated in the Receiver's Motion, the Court should overrule these investors' objections.

Receiver's portfolio.[2]

As the Receiver notes in his Motion, the Mozart and 79th Place properties were marketed pursuant to procedures approved by the Court. (ECF No. 749, p. 15 (citing ECF Nos. 618, 681)). Both Citibank and Fannie Mae have objected throughout the sales process, raising many of the same objections they now repeat. But the Court overruled those objections and allowed the marketing and bidding process to proceed. (*See* ECF Nos. 628, 676, 681).

After the Court approved the marketing procedures for the Mozart and 79th Place properties, the Receiver opened a competitive bidding process that resulted in eleven offers for the Mozart properties and five offers for the 79th Place property. (ECF No. 749, pp. 20-21). For the Mozart property the Receiver accepted a $925,000 offer that exceeded his $850,000 asking price. (*Id.*, p. 21). The $1,150,000 winning bid for the 79th Place property was narrowly below the Receiver's $1,250,000 asking price. (*Id.*, p. 20).

The Receiver has represented that the proceeds from the sale of both properties, as well as the other properties at issue in his Motion, "will be held in separate subaccounts established by the Receiver…and will not be available to pay operating expenses of the Receivership." (ECF No. 749, pp. 41-42). The Receiver further proposes that the Court determine how to distribute those sales proceeds through the claims and priority-determination process. (*Id.*)

[2] For other Receivership properties on which claims have been asserted, investors have filed dozens of lower value claims such as those in the amounts of $714, $786, $817, $971, $979, $1,000, $1,374, $1,600, $2,000, $2,022, $2,228, $2,303, $2,608, $2,618, $2,627, $2,875, $3,000, $3,188, $3,200, $3,451, $3,715, $3,900, $3,965, $4,000, $4,747, $4,858, $5,000, $5,500, $6,000, $6,056, $6,500, $6,634, $6,708, $7,000, $7,152, $7,200, $7,300, $7,500, $7,728, $7,800, $7,910, $8,426, $8,523 $8,700, $8,730, $8,932, $9,000, $9,274, and $9,500. (*See* ECF No. 693, pp. 5-39).

B. Citibank and Freddie Mae's Objections, Many of Which Have Already Been Overruled, Are Unavailing.

As discussed below, most of Citibank and Fannie Mae's objections have already been rejected by the Court. And the remaining ones run contrary to positions the lenders have recently taken or otherwise lack merit.

First, Citibank and Fannie Mae argue that the Court cannot approve a sale price that is lower than the security interest on that property, such that no equity will be left for the Receivership estate. (ECF No. 769, p. 14). But Citibank and Fannie Mae ignore that the Court has repeatedly approved the sales of properties for prices less than the mortgages securing them, including properties sold below the Receiver's asking price. (*See*, *e.g.*, ECF No. 676, p. 7). The Court has similarly rejected previous arguments that the Receiver cannot sell the properties "free and clear" of any liens or encumbrances, provided that those liens attach to the ultimate sales proceeds of the properties. (ECF No. 601 ("While LMJ suggests that the judicial sale for which approval is now being sought will forever extinguish its mortgage and release its claim with respect to 7448−52 South Essex, all competing mortgages…will continue to attach to the sales proceeds with equal force and effect as they did to the property.")). It is telling that Citibank and Fannie Mae fail to acknowledge the Court's previous rulings, let alone provide a valid reason for the Court to deviate from the established law of the case.

Trying to escape the Court's prior rulings, Citibank and Fannie Mae cite to *Pennant Mgmt. v. First Farmers Fin., LLC*, 2015 U.S. Dist. LEXIS 96642 (N.D. Ill. July 24, 2015). But *Pennant* is inapposite given that, unlike this case, there was no dispute as to the seniority of the liens at issue.[3] The same is true of the other cases Citibank and Fannie Mae prominently cite in

[3] Despite being distinguished by its lack of competing secured lienholders, *Pennant* actually supports the Receiver's Motion and the Court's prior rulings. There, Judge St. Eve approved an

their objections: *SEC v. Madison Real Estate Group, LLC*, 647 F. Supp. 2d 1271 (D. Utah 2009), *SEC v. Bravata* (E.D. Mich.), and *SEC v. Northridge Holdings, Ltd.* (N.D. Ill.).[4] Unlike those cases, this Receivership involves competing claims of priority by secured mortgage holders (including victimized investors). For this reason, the Court's decision to proceed with property sales followed by a priority-determination process that will ultimately distribute the sales proceeds is a sound exercise of the Court's equitable discretion. *See, e.g., SEC v. Wealth Mgmt. LLC*, 628 F.3d 323, 333 (7th Cir. 2010) (to allow a receiver to "classify claims sensibly," a receiver's distribution plan may appropriately "subordinate the claims of certain investors to ensure equal treatment.") (citations omitted).

Second, Citibank and Fannie Mae argue that selling the properties violates the Fifth Amendment's "takings" clause. As an initial matter, to the extent these lenders failed to raise this objection in earlier motions to confirm sales of properties on which they assert liens, the Court should find this argument to be waived. (*See*, *e.g.*, ECF No. 540, p. 5 ("as the magistrate judge pointed out, the Lenders have waived this objection by failing to raise it in their previous objections to the Receiver's second motion for court approval ... The Lenders could have raised this issue when they sought the right to credit bid, but they did not.")).

Citibank and Fannie Mae's Fifth Amendment argument fails on substantive grounds as well. It is notable that in advancing this argument, they do not cite to a single decision holding

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approach where the Receiver could sell the subject properties "free and clear of liens" with the liens later attaching to the proceeds of the sales. *Pennant*, 2015 U.S. Dist. LEXIS 96642, *17.

[4] The undersigned attorney was the SEC's lead litigation counsel on *Bravata*, and can represent that the defrauded investors in that case did not have security interests on the subject properties and there was no dispute as to the priority of the institutional mortgage holders. Because the *Bravata* properties were significantly underwater, the receiver in that case chose the cost-efficient measure of abandoning the properties and allowing the undisputed mortgage holder to foreclose. Similarly, in *Northridge*, there are not competing claims of mortgage priority.

that a judicial resolution of a legal dispute triggers the Takings Clause. Indeed, the Supreme Court has declined to recognize the concept of "judicial takings." *See, e.g., Sifuentes v. Am. Cyanamid Co.*, 787 F. Supp. 2d. 843, 849 (E.D. Wisc. 2011) ("Defendants cite no authority for the proposition that there can be a judicial taking. In [*Stop the Beach Renourishment, Inc. v. Fla. Dep't of Envtl. Prot*.], 130 S. Ct. 2592, 177 L. Ed. 2d 184 (2010), four justices supported this idea, not enough to establish a binding precedent."); *Gibson v. Am. Cyanamid Co.*, 760 F.3d 600, 626 & n.10 (7th Cir. 2014) (noting lack of authority for judicial decisions constituting takings); *City of Shelby v. Galvin*, 2020 IL App (5th) 190271-U, at 22-23 (Ill. App. Ct. Feb. 28, 2020) (trial court order amending property rights did not constitute a taking), *In re Lazy Days' RV Ctr., Inc.* 724 F.3d 418, 425 (3d Cir. 2013) (bankruptcy court's "adjudication of disputed and competing claims cannot be a taking").

Third, Citibank and Fannie Mae argue that selling the properties in advance of the priority determination process violates their due process rights. But recently, Citibank and Fannie Mae requested a lengthy discovery process in advance of priority determinations, which did not include a pause in property sales. (ECF No. 708, pp. 11-14). Citibank and Fannie Mae also asked the Court to defer the Receiver's request for payment until the Court can "examine the results of the Receiver's work after it occurs." (*Id.*, p. 22). Presumably, the "work" these lenders referenced includes property sales, and the processes Citibank and Fannie Mae promoted could not be employed absent the sale of Receivership property.

As a decision cited by Citibank and Fannie Mae recognizes, a court satisfies due process in a receivership context if "its summary procedures permit parties to present evidence when the facts are in dispute and to make arguments regarding those facts." *SEC v. Elliott*, 953 F.2d 1560, 1567 (11th Cir. 1992). Here, Citibank and Fannie Mae have been afforded ample process by: (1)

filing their present response to the Receiver's motion, and (2) being able to participate in a claims process where they can present evidence and be heard by the Court. *Id.*; *see also Simer v. Rios*, 661 F. 2d 655, 667 (7th Cir. 1981) ("Notice and an opportunity to be heard are the touchstones of procedural due process.").

Moreover, while complaining that selling the properties deprives them of due process, Citibank and Fannie Mae fail to address the severe due process implications their proposal would impose on the approximately 60 investors who have competing claims on the two properties. Should the Court sustain Citibank and Fannie Mae's objections, and immediately award the sales proceeds to them, there will be no opportunity for the investors to be heard or advocate arguments for lien priority.

In order to provide due process and fairness to all claimants, the Court has repeatedly rejected similar lender arguments and ruled that an orderly claims process is the best method to resolve the competing claims of the investors and institutional lenders. (*See, e.g.*, ECF No. 676, p. 6 ("The Lenders argue that the sales proceeds should not be held in escrow pending a claims process, and rather should be immediately disbursed to various Lenders that purportedly have first-priority liens…As the Court has repeatedly stated—including *supra* in discussing the sixth motion for approval of the process for sale of certain real estate—an orderly claims process is the proper way of adjudicating competing claims that exist as to the properties."); *see also* ECF No. 540, p. 5 ("Previously, when the Lenders requested an expedited priority determination, this Court denied the request, stating that priority determinations must take place in the course of an "orderly claims process.")).

The Court has likewise held that an orderly claims process should occur even for properties where a lender has a recorded mortgage but the investors do not. (ECF No. 676, p. 6

n.2 ("Though there are no competing mortgages for four of the properties at issue…the Court is persuaded that, with respect to these properties, 'other issues remain to be resolved during the initiated claims resolution process, including without limitation the alleged balance due in connection with the corresponding loan, the propriety of all of the component amounts of the claims asserted, and the entitlement of the Receiver to an administrative lien on a portion of the proceeds, if warranted.'") (citations omitted)). Indeed, in such circumstances, the investors should be given the opportunity, if they choose, to assert legal or equitable arguments regarding the validity of any mortgages. Because the Court has already held that no distributions or priority determinations should occur outside of the claims resolution process, Fannie Mae's request for an immediate payout should be denied.

Fourth, Citibank and Fannie Mae object that allowing the sales process to proceed impermissibly creates "federal common law" at the expense of their state law rights. Even crediting this argument, because this is an equitable proceeding, the Receiver and SEC are not asking the Court to apply or alter federal common law. Moreover, the Seventh Circuit allows courts to deviate from state law in the context of equitable receiverships. *See, e.g., Wealth Mgmt. LLC.*, 628 F.3d at 333-34; *Duff v. Central Sleep Diagnostics, LLC*, 801 F.3d 833, 842 (7th Cir. 2015). Because the Court may appropriately tailor equitable considerations to the unique features of this Receivership, continuing with the sale of receivership property will not impermissibly lead to the creation of federal common law.

Fifth, Citibank and Fannie Mae object that the Receiver's sales have not "generated the true and proper value of the properties." In doing so, Citibank and Fannie Mae provide no evidence that the competitive bid process the Receiver employed resulted in properties being sold for less than their true market price. Instead, Citibank and Fannie Mae merely renew

objections that have previously been rejected by the Court. (*See, e.g.*, ECF No. 676, p. 7 ("the Court is not persuaded that [the sales] amount is "grossly inadequate,"… nor is it persuaded by UBS's vague contentions that a better marketing and sales process would have fetched a higher price…Relatedly, the Court finds compelling the Receiver's explanation for why the market of potentially interested investors for 7450 South Luella was thin."); ECF No. 704 ("consistent with the Court's earlier determination [677], the Receiver's decision to continue marketing and selling the properties at issue is sensible even in light of the ongoing COVID−19 crisis.")).

Given that the Receiver's procedures for selling the Mozart and 79th Place properties were consistent with those for prior sales that the Court approved, objections to the present sales process should likewise be overruled. (*See, e.g.* ECF No. 676, p. 4 (the Court "does not intend to dictate the Receiver's every move, absent a showing that he is exceeding his [broad grant of] authority or otherwise violating the Receivership Order." (citations omitted)).

Sixth, Citibank and Fannie Mae ***again*** object to the credit bid procedures previously approved by the Court. But the Court has already ruled, in detail, on those objections in authorizing the Receiver's credit bidding procedures. (*See* ECF No. 540, pp. 4-6). There is no valid reason to revisit that ruling.

Seventh, Citibank and Fannie Mae renew their objections that the Receiver's property managers should not have been allowed to bid for the Mozart and 79th Place properties. Again, the Court has previously overruled an identical objection. (ECF 540, pp. 4-5 ("the Court overrules the Lenders' objections concerning…whether managers of the properties should be deemed eligible bidders")). The Court's prior ruling aside, Citibank and Fannie Mae offer no evidence why the Receiver should decline the *highest* bids for the properties, simply because the bids were made by an affiliate of the Receiver's property manager. On the other hand, one could

only imagine Citibank and Fannie Mae's complaints if the Receiver had accepted lower offers from different potential purchasers.

Finally, Citibank and Fannie Mae's objections should generally be overruled because they will lead to further delay and increased costs. Such costs include those associated with the Receiver maintaining negative-cash flowing properties that he seeks to liquidate in order to eliminate ongoing expenditures by the Receivership. Despite their objections, Citibank and Fannie Mae recognize, and even complain of, the ongoing costs associated with properties that the Receiver has yet to sell. (ECF No. 628, p. 19 (discussing "costs to the estate, including tax liabilities, insurance premiums, property management fees, and maintenance and repairs costs, which continue to accrue for each day a property is held in the estate")). Sustaining their objections would only bring increased delays and costs that all parties believe should be avoided.

C. Conclusion

The Court has repeatedly voiced approval for the sales processes the Receiver has chosen to employ and has authorized the property sales that have resulted. The objections Citibank and Fannie Mae lodge are mostly recitations of previous objections that the Court has already overruled. And to the extent Citibank and Fannie Mae make new objections, those objections do not provide valid reasons to deviate from the sales procedures that have been successfully implemented for multiple tranches of properties. Accordingly, the Court should overrule the objections, grant the Receiver's motion, and allow the Receiver's liquidation efforts to proceed.

Dated: September 14, 2020

Respectfully submitted,

/s/ Benjamin Hanauer

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CERTIFICATE OF SERVICE

I hereby certify that I provided service of the foregoing Reply, via ECF filing, to all counsel of record and Defendant Shaun Cohen, on September 14, 2020. I further certify that I caused the foregoing Response to be served on Defendant Jerome Cohen, via email at jerryc@reagan.com.

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