

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

UNITED STATES SECURITIES AND
EXCHANGE COMMISSION,

Plaintiff,

v.

EQUITYBUILD, INC., et al.,

Defendants.

Case No. 1:18-cv-5587

Hon. Manish S. Shah

**OBJECTIONS TO MAGISTRATE JUDGE KIM’S RECOMMENDATION ON
RECEIVER’S SECOND MOTION FOR APPROVAL OF FEE ALLOCATIONS
FOR INTERIM PAYMENT PURSUANT TO RECEIVER’S LIEN**

The Institutional Lenders identified on Exhibit 1 (the “Objecting Institutional Lenders”) respectfully object to Magistrate Judge Kim’s June 21, 2023 Order (Dkt. 1491) concerning the Receiver’s Second Motion for Approval of Fee Allocations for Interim Payment Pursuant to Receiver’s Lien (“RF2A”) (Dkt. 1321) (the “Recommendation”). As explained below, the Objecting Institutional Lenders continue to assert and thus preserve their objections and the arguments made in their Objection to Magistrate Judge Kim’s Oral Ruling and Minute Order on First Fee Allocation Motion (Dkt. 1389), which objections this Court overruled in their entirety except for a limited number of fee line items which the Receiver agreed required correction (Dkt. 1450).

These objections are made pursuant to the Court’s August 17, 2021 Order, which states:

Going forward, the Lenders are admonished that, to the extent they seek to preserve arguments the Court has already rejected, they should do so in a summary fashion that incorporates citations (with pinpoint cites) to previous filings that have thoroughly laid out the objection. And pursuant to their attorneys’ duty of candor to the tribunal, *see* Am. Bar. Assoc. Model. R. 3.3(a)(2), the Lenders must simultaneously set forth citations to the Court’s prior rulings on each

argument. If the Lenders believe that an objection should be revisited in light of new facts or changed circumstances, then the Lenders must clearly set forth the reasons the Court should depart from its prior rulings. This practice will serve to redirect the resources of Receiver, the Court, and the other stakeholders in this case to the Lenders' new and potentially meritorious arguments, instead of forcing everyone to retread the same ground every few months.

Dkt. 1031 at pp. 11-12, n.32.

In accordance with the Court's instructions, the Objecting Institutional Lenders do not repeat arguments previously overruled except as necessary for the Court to understand the context, but incorporate those arguments by reference as stated herein to preserve their objections.

The Recommendation is clearly erroneous regarding the matters referred to the Magistrate Judge by the District Court, and contrary to law, because it fails to draw an appropriate distinction, on the one hand, between fees attributable to work of benefit to the victorious secured creditors – whoever they might be – and the secured properties (potentially justifying a surcharge on the segregated sales proceeds), and, on the other hand, fees associated with work of general benefit to all creditors in the Estate (fees that should be borne by the Estate generally and not surcharged against the segregated sales proceeds). *See* Dkt. 1030. The District Court has overruled substantially all of the Objecting Institutional Lenders' objections and arguments in this regard except as noted in Sections A and F below (and except where the Receiver has agreed a correction was required in light of the objections). *See, e.g.*, Dkts. 1366, 1450, 1452, 1468).

STANDARD OF REVIEW

The Objecting Institutional Lenders incorporate the same standard of review stated at Dkt. 1389, pp. 3-4. These objections are timely filed on July 5, 2023 under Fed. R. Civ. P. 72(a) because Magistrate Judge Kim entered the order and Recommendation to which the Objecting Institutional Lenders herein object on June 21, 2023. Dkt. 1491.

ARGUMENT

Magistrate Judge Kim recommended that all of the Objecting Institutional Lenders' objections be overruled. Dkt. 1490. Each category of objections is addressed separately below.

A. Claims-Adjudication (Other Than Group 1)

This category, while bearing some superficial similarity to other objections the Court has ruled on in other contexts, is a new objection category that the District Court has never squarely addressed before. The Objecting Institutional Lenders object to the timing of payment of Receiver's fees which were associated with work in the nature of claims adjudication reflected as "Premature Adjudication" in the rightmost column of Dkt. 1443-3, and "Claims Adjudication (other than Group 1)" in the rightmost column of Dkt. 1443-4.

While the Objecting Institutional Lenders acknowledge that, based on the Court's prior rulings, such fees arguably fall under the "implementation and management of an orderly summary claim-priority adjudication process" (Dkt. 1030 at p.2) priming lien category, whether they are properly surcharged or not depends on the result of the adjudication process as discussed below. This objection category (see Objecting Institutional Lender arguments at Dkt. 1443 at pp. 5-7, incorporated herein by reference) concerns only adjudication-related fees associated with properties other than those in Group 1 because the objected-to fees were incurred for adjudication-related fees after the Group 1 briefing concluded and/or because the Receiver associates the adjudication-related fees with properties other than those in Group 1.

As to the Group 1 litigation, the Court and Receiver both acknowledged, before Group 1 adjudication began in earnest, that it would be premature to award adjudication-related Receiver fees immediately - early in the adjudication process - because it would not be clear "until the conclusion of the claims process" whether the Receiver's adjudication activities benefitted the secured properties and ultimately victorious secured creditor. Dkt. 1030 at p.14, n.7. The Court

indeed delayed awarding a priming lien against segregated sales proceeds for the Receiver's fees with respect to Group 1 adjudication fees until December 30, 2022, as part of the Receiver's 17th Fee Petition, in light of "[t]he court's forthcoming ruling on the priority dispute in the Group 1 bucket..." Dkt. 1366 at p.2.

The Receiver incorrectly asserts that the District Court has already overruled this objection category, citing the Court's overruling of the Institutional Lender's Objections to the 18th Fee Petition. *See* Receiver's discussion at Dkt. 1481 at p.2. In fact, the Institutional Lenders had no objections in this category in the 18th Fee Petition (Dkt. 1394, Objecting Institutional Lenders' objections to 18th Fee Petition, with no argument concerning Groups 2-3 adjudication) because the Receiver had not yet begun the Group 2 adjudication process in earnest as to the fees there at issue. *See* Dkt. 1394.

The Objecting Institutional Lenders' argument here to delay Group 2 adjudication fees, as the Court delayed Group 1 adjudication fees, made its first appearance in the Institutional Lenders' Objections to the RF2A (Dkt. 1443, pp. 5-7) and the 19th Fee Petition (Dkt. 1486, p.7). Magistrate Judge Kim recommended that the Objecting Institutional Lender's Objections in this regard be overruled, Dkt. 1491, but the District Court has yet to opine. And the District Court has not yet ruled on the 19th Fee Petition (Dkt. 1478).

The Objecting Institutional Lenders respectfully argue that the Court's awarding of the Group 1 fees just six weeks prior to the Court's Group 1 priority ruling (Dkt. 1386) was based on the near-conclusion of the Group 1 adjudication process, and not on a wholesale rethinking of the Court's earlier logic in delaying the awarding of such fees until the adjudication process for Group 1 substantially played out. *See* Dkt. 1366 at p.2 (Court's reasoning in granting the 17th Fee Petition including as to Group 1 adjudication fees).

Accordingly, the Objecting Institutional Lenders respectfully request that the Court delay awarding the Receiver's fees for adjudication-related work for the reasons stated at Dkt. 1443 pp. 5-7, and for the same reasons the Court delayed awarding such fees as to the Group 1 litigation (Dkt. 1030 at p.14, n.7). At a minimum, such fees should not be awarded until the Court adjudicates lien priority in the Group to which the fees relate and determine whether the requested fees benefit the prevailing party in that priority dispute. The Objecting Institutional Lenders reserve their right to argue for a longer delay at the conclusion of the adjudication process depending on the result of the adjudication.

B. Claims-Adjudication – Group 1 Litigation

As BC57, LLC (“BC57”) previously argued, and incorporates such arguments by reference in accordance with the Court's instructions (Dkt. 1443, pp. 7-10; Dkt. 1346 at p.5; Dkt. 1394, pp. 7-8), payment of the Receiver's fees associated with Group 1 adjudication and litigation should be delayed pending appeal of the Group 1 priority ruling. This category of objection is denoted by a “Group 1 Adjudication” label in the rightmost column of Dkt. 1443-4. The purpose of delaying payment of such fees is that if BC57 prevails on its appeal of the Group 1 priority ruling (Dkt. 1386), the Receiver's litigation efforts against BC57 will not have benefitted BC57 or the secured properties, and thus no surcharge on the segregated sales proceeds would be justified under *SEC v. Elliott*, 953 F.2d 1560 (11th Cir. 1992). BC57 reiterates those objections (Dkt. 1443, pp. 7-10; Dkt. 1346 at p.5; Dkt. 1394 at pp. 7-8) which the Court has overruled at Dkt. 1366 at pp. 1-2; Dkt. 1450.

C. Non-Adjudicatory Claims-Related Fees

The Objecting Institutional Lenders continue to object to fees associated with the Receiver's work to the extent they relate to claims generally but are not adjudicatory in nature, such as searching for potential claims, coordination with potential claimants who have not become

claimants, and intake and organization of existing claims. These objections are denoted by the label “Claims-related tasks not associated with adjudication” in the rightmost column of Dkt. 1443-3, and “Claims Administration” in the rightmost column of Dkt. 1443-4.

The Objecting Institutional Lenders incorporate by reference their detailed descriptions of this objection category at Dkt. 1443 pp. 10-11; Dkt. 1389 (legal argument at pp. 1-8, specifics on this category at pp. 10-11); and Dkt. 1210 at p.14. The Court overruled these objections and broadened the “implementation and management of an orderly summary claim-priority adjudication process” priming lien category (Dkt. 1030 at p.2) to include “giving notice to interested parties, locating and preserving records, and handling creditor inquiries” (Dkt. 1366 at 2) in granting the Receiver’s 17th Fee Petition. The Court also overruled this objection category when granting the First Fee Allocation Motion (Dkt. 1450) and has overruled all similar objections the Institutional Lenders have made since.

D. General Receivership Operations

The Institutional Lenders continue to object to fees related to general receivership work that the Receiver would have needed to do even if no secured creditors were claimants in the Receivership and even if there were no secured claim adjudication process, such as for maintaining a service list and making EquityBuild’s electronic records available to all claimants. These objections are denoted by the “General Receivership Activities” label in the rightmost column of Dkt. 1443-3 and Dkt. 1443-4. The Objecting Institutional Lenders raised these arguments as to prior fee petitions and as to the First Fee Allocation Motion and incorporate them by reference here in accordance with the Court’s instructions. *See* Dkt. 1443 at pp. 11-13; Dkt. 1210 at pp. 12-13. The District Court has overruled these objections previously. Dkt. 1443 at 13 (citing Dkt. 1381 & 2/10/2021 Hearing Transcript at 137-47); *see also* Dkt. 1371 (“The point of allocating was to attempt to preserve the distinction between claimants with property-specific interests from other

unsecured claimants, but not to create an opportunity for secured claimants to shift Receiver's fees onto the unsecured.").

E. Ambiguous Entries

The Objecting Institutional Lenders object to certain line items that were ambiguous as to what work the Receiver was doing to incur the associated fees. This category is reflected by the "Ambiguous" label in the rightmost column of Dkt. 1443-4 and the objections are described at Dkt. 1443 pp. 13-14, incorporated herein by reference per the Court's instructions. While the District Court has not yet had occasion to review these particular entries in an allocation context, the District Court has overruled similar objections previously. *See, e.g.*, Dkt. 1353 at pp.8-9 (and citations therein); Dkt. 1181 at pp. 9-14.

F. General Allocations Pro Rata

The Objecting Institutional Lenders continue to object to certain of the Receiver's pro rata general allocations. *See* Dkt. 1443 at pp. 14-15, explaining the objection category, incorporated herein by reference per the Court's instruction. The Receiver's fee entries in this regard are reflected at Dkt. 1321, Exh. B. This set of fees relates to work that the Receiver does not attribute to any one specific property or subset of properties, so the fees for such work are divided across *all* properties in the Receivership pro rata based on their sales proceeds. Dkt. 1443-3 reflects the Objecting Institutional Lenders' objections as to the categories described in Sections A-E above (Dkt. 1443-4 reflects the Section A-E categories of objections as to fees the Receiver attributes to specific properties). In addition to those categories, some entries are labeled "Fees charged to all the properties pro-rata even though they appear to relate to only one specific claimant or property or a subset of either definitely smaller than all the claimants\properties" in the rightmost column of Dkt. 1443-3 denoting the Objecting Institutional Lenders objections in this Section F category.

The Objecting Institutional Lenders respectfully request that the District Court review Dkt. 1443-3 (14 pages) and the line items labeled with the above description because several clearly reflect, on their face, that something less than *all* properties in the Receivership were at issue in the fee description. While the District Court has never reviewed or considered objections about these particular fee entries in an allocation context, it overruled similar objections raised in the First Fee Allocation Motion. *See, e.g.*, Dkt. 1481, Exh. A (Transcript of 4/26/2023 hearing at pp. 22-23); Dkt. 1481 at pp. 12-13 (Receiver summary of Court's prior ruling on similar issues but involving different fee entries). The Court also overruled similar objections made in the 17th and 18th Fee Petitions (Dkts. 1366, 1452).

G. A Holdback Percentage of 20% of All Fees Plus 20% of All Fees to be Drawn From Segregated Sales Proceeds Remains Appropriate.

The Objecting Institutional Lenders continue to object to any holdback less than 20% of all fees *plus* 20% of all fees to be drawn from segregated sales proceeds. This Court has imposed such holdbacks on numerous occasions before, including since Judge Shah was assigned to the matter. *See, e.g.*, Dkt. 1312 at 4 (“The court also imposes a holdback of 20% of the fees (but not expenses) requested in the applications, and an additional 20% holdback on any fees to be paid from the sales proceeds of encumbered real estate.”).

The Objecting Institutional Lender's arguments on this point are expressed in their Motion to Reconsider Order Granting Receiver's First Allocation Motion, Dkt. 1471 (in its entirety), incorporated herein by reference and which objection the Objecting Institutional Lenders continue to assert. The Court denied the Motion to Reconsider and overruled these objections retroactively even as to fee petitions that, when approved and ruled on, included both holdbacks. Dkt. 1483. The Court also denied the Objecting Institutional Lenders' objections requesting both holdbacks as to the fees at issue in the 17th Fee Petition (Dkt. 1366) and 18th Fee Petition (Dkt. 1452). In these

rulings, however, the District Court has preserved a 20% holdback on all fees without the additional 20% holdback on fees to be paid out of segregated sales proceeds. *See id.*

H The Receiver’s Operating Account (General Estate Funds), Rather Than the Segregated Sales Proceeds, Should be the Source of Funds to Pay the Receiver for Fees to Which the Objecting Institutional Lenders Object.

The Objecting Institutional Lenders continue to object to the Receiver being paid out of segregated sales proceeds pursuant to a priming lien for all of the fees to which they have asserted objections, and argue the Receiver should instead be paid such objected-to fees out of the general Estate funds in the Receiver’s Operating Account. This argument is more fully expressed at Dkt. 1210, p.17; Dkt. 1389, pp. 4-9 (legal arguments); and Brett Natarelli’s email to Judge Shah’s chambers (copying counsel of record) dated January 4, 2023.

The District Court has overruled this objection. Dkts. 1371, 1366, 1452. In the interest of clarity, however, the Objecting Institutional Lenders reiterate that the District Court has not disapproved in concept paying some of the Receiver’s fees out of the general Estate funds in the Operating Account so long as the Receiver has agreed to that source of payment. The Court has, on numerous recent occasions, ordered that some of the Receiver’s fees be paid out of the general Estate funds in the Operating Account. *See, e.g.*, Dkt. 1449 at 3(a)(iii) (authorizing “\$17,197.26 to pay Rachlis Duff & Peel, LLC for approved fees set forth on its invoices submitted with the Receiver’s Eighteenth Interim Application that have not been allocated to specific properties”); Dkt. 1372 (authorizing “\$12,455.50 to pay Rachlis Duff & Peel, LLC for approved fees set forth on its invoices submitted with the Receiver’s Seventeenth Interim Application that have not been allocated to specific properties”). Earlier in the Receivership, the Receiver regularly sought and was paid out of general Estate funds in the Operating Account. *See, e.g.*, Dkt. 1031 at pp. 13-14 (discussing historic source of payment).

CONCLUSION

For each of the foregoing reasons, the Objecting Institutional Lenders respectfully request that the Court reject the Recommendation and sustain all of the Objections, order that the Receiver’s fees herein objected to be paid out of the Estate’s funds in the Operating Account, and that the Receiver’s fees not objected to herein be paid only subject to an additional 20% holdback on top of the 20% holdback the Court has already ordered.

Respectfully submitted,

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