

UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF ILLINOIS  
EASTERN DIVISION

UNITED STATES SECURITIES AND  
EXCHANGE COMMISSION,

Civil Action No. 18-cv-5587

Plaintiff,

Hon. John Z. Lee

v.

Magistrate Judge Young B. Kim

EQUITYBUILD, INC.,  
EQUITYBUILD FINANCE, LLC,  
JEROME H. COHEN, and  
SHAUN D. COHEN, Defendants.

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**OBJECTION OF LIBERTY EBCP, LLC TO  
ORDER DATED MAY 22, 2019 REGARDING FIFTH MOTION**

Liberty EBCP, LLC ("Liberty"), by its counsel, Jaffe, Raitt, Heuer & Weiss, P.C. files this *Objection to Order Dated May 22, 2019 Regarding Fifth Motion* ("Objection"), and in support thereof, states as follows:

**INTRODUCTION**

Liberty is seeking limited review of portions of the *Order* dated May 22, 2019 issued by Magistrate Judge Young B. Kim (the "May 22 Order") (R 382). The *May 22 Order* addresses the *Receiver's Fifth Motion for Court Approval of the Process for Public Sale of Real Property by Sealed Bid* (the "Fifth Procedures Motion") (R 329). Three of Liberty's properties, upon which Liberty holds a mortgage, are subject to the Fifth Procedures Motion: 7656 S. Kingston, 7546-48 S. Saginaw and 8201 S. Kingston (the "Properties").

## ARGUMENT

### **1. The May 22 Order Fails to Acknowledge Liberty’s Objection to the Fifth Procedures Motion.**

The second sentence of the *May 22 Order* references objections to the *Fifth Procedures Motion* having been filed by U.S. Bank and UBS AG, but not Liberty. Liberty had also filed a timely objection to the *Fifth Procedures Motion*, styled as *Objection of Liberty EBCP, LLC to Receiver’s Fifth Motion for Court Approval of the Process for Public Sale of Real Property by Sealed Bid* on April 22, 2019 (R 333) (the “*Liberty Fifth Procedures Motion Objection*”). Therefore, the *May 22, 2019 Order* should be reviewed, in light of its failure to reference the *Liberty Fifth Procedures Motion Objection*.

### **2. Liberty Objects to the Determination that the Sealed Bid Process Does Not Have to Incorporate the Provisions of 28 U.S.C. §2001(a).**

The Receiver, in the *Fifth Procedures Motion*, proposes to sell the Properties pursuant to the public sale provisions of 28 U.S.C. § 2001(a)<sup>1</sup>. Section 2001(a) requires a sale “at the courthouse, parish or city in which the greater part of the property is located, or upon the premises or some parcel thereof located therein, as the court directs.” The Receiver proposes to sell pursuant to a sealed bid process, which in no way includes the requirements of Section 2001(a). Liberty took exception with this process in the *Liberty Fifth Procedures Motion Objection* because it was outside of the statutory requirements of Section 2001(a). Judge Kim, after citing to certain case law, determined in the *Memorandum Opinion and Order Dated May 2, 2019* (the “*May 2 Order*”) that:

In the exercise of its discretion here, the court finds that the Receiver’s proposed sale procedures comply with Section 2001(a) for several reasons. As an initial matter, Liberty has not shown that a public sale on the courthouse steps or

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<sup>1</sup> Per footnote 2 to the *May 2 Order*, the Receiver is not relying on the provisions of 28 U.S.C. §2001(b) in support of the Properties’ sale.

Properties would result in a better outcome for any party, creditor or investor than the public auction proposed here. Nor has Liberty demonstrated that any of the identified properties can actually be “sold” on the courthouse steps. The Receiver is not authorized to sell anything without the court’s approval, which cannot take place until after the auction period expires. The Receiver has the authority to “take all necessary and reasonable actions” to sell or lease “all real property in the Receivership Estate.” (R. 16, Receivership Order, ¶ 38). While the Receiver must act “with due regard to the realization of the true and proper value of such real property,” (id.), neither Liberty nor any other Lender or Party has shown that the Receiver has not acted in the best interest of the Receivership Estate. And the Receiver describes measures—including publishing notice of the sale in a number of prominent publications and marketing the public sale on publicly available websites and through social media—that seek to “maximize awareness and interest” in the Properties. The court therefore overrules Liberty’s objection and approves the sale procedures proposed by the Receiver, except as otherwise provided below.

*May 2 Order*, pages 5-6.

Liberty assumes that the same justification would support a denial of Liberty’s request for a public sale of the Properties, set forth by Liberty in the *Liberty Fifth Procedures Motion Objection*. Liberty objects for the following reasons.<sup>2</sup>

First, the statute is explicit. It mandates where the sale is to take place. When a statute is explicit on its face, a court should not ignore its plain meaning.

Second, the statute does not require that Liberty show that a public sale on the courthouse steps or the Properties would result in a better outcome for any party, creditor or investor than the procedure proposed by the Receiver. This is not a standard under Section 2001(a). Compliance with Section 2001(a) is not discretionary.

Third, certain of the cases cited in the *May 2 Order* relied on, in support of other courts’ deviation for the explicit requirements of Section 2001(a), are distinguishable. In both *SEC v. Billion Coupons*, Nos. 09-00068, 09-00069, 2009 WL 2143531 (D. Haw. July 13, 2009) and in

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<sup>2</sup> The hearing on the *Objection to Memorandum Opinion and Order Dated May 2, 2019* (R 359) of Liberty has not yet been heard by the Court.

*Pennant Mgmt., Inc. v. First Farmers Fin., LLC*, No. 14 CV 7581, 2015 WL 5180678 (N.D. Ill. Sept. 4, 2015), the opinions specifically noted that no objection to deviation from the requirements of Section 2001(a) were posed by any party. And in *United States v. Hunwardsen*, 39 F. Supp. 2d 1157 (N.D. Iowa 1999) the issue was not whether the parties could deviate from the requirements of Section 2001, but, rather, whether the proposed sale should be carried out under the strictures of Section 2001(a) versus Section 2001(b).

Fourth, there is a distinction between the method of sale versus confirmation of the sale. The drafters set forth in Section 2001(a) how the sale is to be *conducted*, not how it is to be *approved*. Once *conducted*, the parties then seek *approval* by reporting to the court, as occurs in bankruptcy sales, the results of the sale, and the court then confirms the sale, based on offers of proof, transcripts of the auction sale or other evidence of the bids submitted and sale process generally. This two-step process is borne out of the pleadings in this case. Pursuant to the *Receiver's Motion for Court Approval of the Process For Public Sale of Real Property by Sealed Bid* (R130) (the "*First Procedures Motion*") the Receiver sought approval of sale procedures for the first set of properties. Thereafter, after choosing the highest bidders based on the sealed bids received, the Receiver filed the *Receiver's First Motion for Court Approval of the Sale of Certain Real Estate and for the Avoidance of Certain Mortgages, Liens, Claims and Encumbrances* (R 230) (the "*First Approval Motion*"), under which the Receiver sought approval of the sale resulting from an initial sale effort. Under the *May 2 Order's* rationale, no receivership sale could ever occur in accordance with Section 2001. That is simply not the law.

Fifth, the *May 2 Order* incorrectly relies on the marketing process proposed, as justification for deviation from the sale process set forth under Section 2001(a). 11 U.S.C. §

2002 sets forth the minimum publication requirements related to a public sale (i.e., the minimum marketing process):

A public sale of realty or interest therein under any order, judgment or decree of any court of the United States shall not be made without notice published once a week for at least four weeks prior to the sale in at least one newspaper regularly issued and of general circulation in the county, state or judicial district of the United States wherein the realty is situated.

The marketing process proposed by the Receiver complies with Section 2002 and even provides for greater exposure than required by Section 2002. But compliance with Section 2002 does not write the public sale process requirements of Section 2001(a) out of the statute. The provisions are meant to be read together, not to supplant one another.

Sixth, the Receiver's desire to seek sealed bids is not mutually exclusive to the requirements of Section 2001(a). After receipt of sealed bids, the Receiver has the ability, per approved procedures, to announce that the highest sealed bidder will be the opening bidder at the public sale at the property or on the courthouse steps, with a last opportunity for higher and better offers. Providing this last chance can only enhance the amount potentially received for the Properties. As noted in the *Objection of Liberty EBCP, LLC to Receiver's Second Motion for Court Approval of the Process for Public Sale of Real Property by Sealed Bid* (R 232) ("*Liberty's Second Procedures Motion Objection*"), with respect to the First Approval Motion, the proposed sale prices ranged from 45% to 88% of original purchase price for the properties purchased by EquityBuild less than two years earlier (R 232, page 5). Allowing a last opportunity for bidding can only enhance the potential outcome to creditors. Accordingly, the sale procedures should include compliance with Section 2001(a).

**3. While the May 2 Order Granted Liberty the Right to Credit Bid, the Manner, Timing and Methodology for Placing the Credit Bid Has Not Been Spelled Out.**

After issuance of the *May 2 Order*, Liberty has engaged in negotiations with the Receiver, seeking clarification of the manner, timing and methodology proposed to be employed to receive credit bids, as part of the sale process. The Receiver's counsel acknowledged that the *May 2 Order* does not address these issues and advised that the Receiver was determining how it was going to proceed. Unfortunately, prior to the deadline for filing the *Liberty Fifth Procedures Motion Objection* and the deadline for filing this *Objection*, the Receiver and Liberty have not reached agreement on how the credit bid procedures should be modified (nor have any of the other lenders). Therefore, Liberty is seeking clarification of the manner, timing and methodology for placing a credit bid.

As set forth in *Liberty's Second Procedures Motion Objection*, Liberty's right to credit bid, assuming compliance with Section 2001(a), could be exercised at the time of the sale on the courthouse steps or at the Properties. However, without clarification, Liberty is fearful that it will not have the "last look" opportunity to bid, which Liberty would otherwise have under state law (as a foreclosing lender) or as a secured creditor under a Bankruptcy Code Section 363 sale, under 11 U.S.C. §363k.

As matter of law, Liberty has not been, and cannot be, divested of its right to credit bid, as a result of the receivership proceeding. Judge Kim held the same, in the *May 2 Order*. Further, as Judge Kim noted in his *Memorandum Opinion and Order* in this case (R 223) "The court is mindful that it has 'minimal authority' to extinguish 'preexisting state law security interest[s],' should such interests exist." Judge Kim supported this proposition by citing to *SEC v. Wells Fargo Bank, N.A.*, 848 F. 3d. 1339, 1344 (11<sup>th</sup> Cir. 2017). Judge Kim also noted that "the rights of the receivers can be no greater than those of their predecessors in title", citing to *Guaranty Trust Co.*

of *N.Y. v. Fentress*, 61 F. 2d. 329, 333 (7<sup>th</sup> Cir. 1932) and *SEC v. Madison Real Estate Grp., LLC*, 647 F. Supp. 2d 1271, 1277 (D. Utah 2009). In *SEC v. Madison Real Estate Grp., LLC*, the court stated “[i]t is well-established that a receiver appointed by a federal court takes property subject to all liens priorities **or privileges** existing or accruing under the laws of the State.” (emphasis added). The right to credit bid is a privilege. *See also, U.S. Commodity Futures Trading Comm’n v. AlphaMetrix, LLC*, No. 13 C 7896, 2017 WL 5904660, at \*2, n.3 (N.D. Ill. Mar. 9, 2017) (“[a] pre-existing contractual remedy between creditor and debtor would bind the receiver . . .”); *United States v. Security Indus. Bank*, 459 U.S. 70, 76-78 (1982) (creditor’s state law security interests were “property” entitled to Fifth Amendment protection). Therefore, absent a receivership, Liberty would be free to foreclose on its collateral and credit bid at such a sale. Those rights are not extinguished by virtue of a receivership action.

Moreover, Local Rule 66.1 for the Northern District of Illinois provides that the receivership estates should be administered similar to bankruptcy cases. The United States Supreme Court has held that secured creditors have the right to credit bid when their collateral is being sold pursuant to a plan or a sale under Bankruptcy Code Section 363 (a sale free and clear of liens, as is proposed herein). *Radlax Gateway Hotel LLC v. Amalgamated Bank*, 566 U.S. 639, 644 (2012). *See also*, 11 U.S.C. §363(k) (“at a sale under subsection (b) of this section of property that is subject to a lien . . . the holder of such claim may bid at such sale and . . . may offset such claim against the purchase price of such property”). The reason for the right to credit bid is to protect “against the risk that [a lender’s] collateral will be sold at a depressed price.” *Morgan v. Blieden*, 107 F. 2d 133 (8<sup>th</sup> Cir. 1939).

Accordingly, Liberty objects to the *May 22 Order*, as it fails to specify the manner in which Liberty will be permitted to place any credit bid. Any credit bid should be a “last look” bid at a

public sale, with the right of other bidders to place an even higher bid, at the time of the sale under Section 2001(a). Such a public sale could occur after the sealed bids are received and the Receiver determines which of the sealed bids should be the opening bid at the public sale at the property or on the courthouse steps. This assures that the Properties are sold at their highest possible value.

**4. Liberty Objects to the Finding That Liberty's Objection to the Property Manager's Ability to Bid is Moot.**

Liberty and its Properties were not subject to the *First Approval Motion*, pursuant to which one of the two property managers to the Receiver, WPD Management, LLC ("WPD") proposed to purchase two of the properties subject to the *First Approval Motion*. Therefore, Liberty's rights were not impacted by the *First Approval Motion*. And in connection with the hearing on approval of the *First Procedures Motion*, the Court explicitly stated, on the record, that its ruling on those procedures would have no impact on procedures later proposed in the *Second Procedures Motion*. The same should hold true with respect to the *Fifth Procedures Motion*. Notwithstanding Liberty's reservation of rights, Judge Kim, in the *May 2 Order*, held that any objection by Liberty to the property managers, as bidders was moot. Liberty objected to this ruling with respect to the *May 2 Order* and objects to the extent it is binding with respect to the *May 22 Order*.

The property managers have, among other duties, the obligation to provide overall property management and leasing services, to prepare financial reports and to assist in due diligence visits by interested purchasers. It is no secret that Liberty and the other lenders have been at odds with the Receiver over access to the property managers to have questions answered, based on substantial changes in occupancy, turnover costs, leasing commissions and property expenditures, between the pre and post-receivership periods; information that materially affects a given property's net operating income and therefore, market value. To this date, the Receiver has refused to permit Liberty to engage directly with the property managers to explain these material discrepancies and



after the Receiver directed that such questions be put in writing to the Receiver, none have been answered. *See, Motion to Determine the Rights of Liberty EBCP, LLC with Respect to the Receivership Estate and Other Relief* (R101).

Based on WPD's dual role as the Receiver's agent and as a proposed purchaser and the possible dual role of the other property manager as purchaser, a higher system of checks and balances than is set forth in the Second Procedures Motion is required. The law in the bankruptcy area is quite clear that heightened scrutiny of a fiduciary or its agents involvement in a bankruptcy sale is to be given. 18 USC §154, part of the bankruptcy crimes statute, states that a "custodian, trustee, marshal or other officer of the court" who "knowingly purchases, directly or indirectly any property of the estate" or "knowingly refuses to permit a reasonable opportunity for inspection by parties in interest of the documents and accounts relating to the affairs of the estate" can be subject to a fine and removed from office. In *Donovan & Schuenke v. Sampsell*, 226 F. 2d 804 (9<sup>th</sup> Cir. 1955), a sale of real property of the debtor was made to an individual who had served as an officer of debtor during bankruptcy, and then resigned before the sale. The Ninth Circuit set aside the sale, stating:

It is elementary that a fiduciary cannot deal or receive a transfer of the property which is the subject of the trust. It makes no difference whether the fiduciary be called an agent, custodian, trustee or officer. It makes no difference whether it can be proved that the fiduciary profited by the transaction. The principle is established by general law and does not depend upon the existence of a statute for enforcement. To affirm [such a] sale would seem to place a premium on shady dealings in a court of bankruptcy.

*Id.* at 812.

While Liberty has absolutely no notice of any impropriety in the actions of WPD as property manager or as purchaser, the opportunity exists for a conflict of interest. WPD, on the one hand, is trying to maximize value, as agent of the Receiver, but is also, on the other hand, a prospective purchaser, seeking to purchase at the lowest possible cost. What is disseminated

affects price. Therefore, Liberty believes that the property managers should not be deemed to be eligible bidders related to Liberty's Properties.

**5. If the Property Managers are Permitted to Bid, There Must Be Much Greater Transparency in the Sale Process.**

The *May 2 Order* overruled Liberty's request that it be provided the opportunity to "provide input into and be involved with the sale process and have direct access to the property managers for the Properties". *See, May 2 Order*, pages 8. Similarly, the *May 2 Order* overruled Liberty's request that lenders "be permitted to preview and approve due diligence materials before being provided to prospective bidders," and that "the Receiver should be compelled to share all offer information with the mortgage holders." *See, May 2 Order*, Page 9. The *May 22 Order* does not address this objection of Liberty.

Liberty submits that the Receiver cannot have it both ways. If the foxes watching the hen house (the property managers) are eligible to bid, then someone needs to watch the foxes. Without a check and balance on the system, there is no assurance that the foxes will not be shading the process for their benefit as potential bidders. The property managers, as agents of the Receiver, are likewise officers of this Court.

The property managers control the accounting. How much is spent on a given property, the turnover rate of units, when and if improvements are made fall partially or fully within the property managers' discretion. Income producing real estate prices are based, in large part, on the net operating income of a given property. Therefore, the financial information being shared with prospective bidders (rent rolls, occupancy rates, historic financial statements, rent receivable agings, projections, capital expenditure reports and budgets, etc.) is critical in determining the price a bidder may be willing to pay. Based on the lack of access to the property managers, to date, to clarify questionable issues, Liberty should be provided with the opportunity to preview the

due diligence materials proposed to be disseminated to bidders on its Properties, in order to comment on the same and clarify, *with the Receiver*, any material issues prior to their dissemination. Without this check and balance on the system, information provided to bidders may unnecessarily depress the valuation of a given Property, to the detriment of both Liberty and the receivership estate. The Receiver should welcome a vetting of these due diligence materials with Liberty, to ensure their accuracy and to avoid any objections posed at a sale approval hearing that the diligence materials unfairly depressed the offers received by the Receiver.

The property managers also control potential bidders' access to the properties. Which apartments are shown (renovated versus those in disrepair), mechanical systems, etc. can impact a bidder's view of a given property. It is commonplace in bankruptcy sales that the fiduciary (debtor or trustee), in conjunction with an asset sale, meet and confer with the parties who have an interest in the property being sold, to provide input on what may bring the estate and all creditors the highest value. This also provides a safety valve, to permit purchasers to vet any frustration or stonewalling which they perceive, as part of their due diligence process. Such third parties (lender, creditors' committees or others) do not supplant the business judgment of the fiduciary, but instead are a resource to assist the fiduciary in fulfilling its duty. This open process also avoids surprises, such as is evolving in this case, where the parties learned, for the first time, through the *First Sale Motion*, of the involvement of an insider, the property manager WPD, as purchaser. Such events, as well as others, arise in any sale process, and the ability to address these issues openly before approaching a courtroom helps facilitate a more orderly and unquestioned sale process.

**CONCLUSION**

For the foregoing reasons, Liberty objects to the *May 22 Order* and requests that this Court grant to it the relief requested herein or such other relief as the Court deems equitable and just.

Respectfully Submitted,

/s/ Jay L. Welford

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Date: June 4, 2019

**CERTIFICATE OF SERVICE**

I hereby certify that on June 4, 2019, I provided service of the foregoing *Objection to Order Dated May 22, 2019 Regarding Fifth Motion*, via ECF filing to all counsel of record, and via electronic mail or U.S. mail to the following individuals and entities:

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