UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

UNITED STATES SECURITIES AND EXCHANGE COMMISSION, Plaintiff, v. EQUITYBUILD, INC., EQUITYBUILD FINANCE, LLC, JEROME H. COHEN, and SHAUN D. COHEN Defendants.	Case No. 1:18-cv-5587 Hon. John Z. Lee Magistrate Judge Young B. Kim

OBJECTION TO ORDER DATED JULY 9, 2019

The following mortgagees (collectively, "Movants", and each individually a "Mortgagee") respectfully file this Objection ("Objection") to the Order dated July 9, 2019 [Dkt 447] ("July 9 Order") pursuant to Fed. R. Civ. P. 72(a): (1) Citibank N.A., as Trustee for the Registered Holders of Wells Fargo Commercial Mortgage Securities, Inc., Multifamily Mortgage Pass-Through Certificates, Series 2018-SB48; (2) U.S. Bank National Association, as Trustee for the Registered Holders of J.P. Morgan Chase Commercial Mortgage Securities Corp., Multifamily Mortgage Pass-Through Certificates, Series 2017-SB30; (3) U.S. Bank National Association, as Trustee for the Registered Holders of J.P. Morgan Chase Commercial Mortgage Securities Corp., Multifamily Mortgage Pass-Through Certificates, Series 2017-SB41; (4) U.S. Bank National Association, as Trustee for the Registered Holders of J.P. Morgan Chase Commercial Mortgage Securities Corp., Multifamily Mortgage Pass-Through Certificates, Series 2018-SB50; (5) Wilmington Trust, National Association, as Trustee for the Registered Holders of Wells Fargo Commercial Mortgage Trust 2014-LC16, Commercial Mortgage Pass-Through Certificates, Series 2014-LC16; (6) Federal National Mortgage Association ("Fannie Mae"); (7) Federal Home Loan Mortgage

Corporation ("Freddie Mac"); (8) UBS AG; (9) BMO Harris Bank N.A.; (10) Midland Loan Services, a Division of PNC Bank, National Association; and (11) BC57, LLC. In support of the Objection, the Movants state as follows:

FACTUAL BACKGROUND

On May 2, 2019, Magistrate Judge Young B. Kim entered a Memorandum Opinion and Order [Dkt 352] ("May 2 Order") granting the Receiver's Second Motion for Court Approval of the Process for Public Sale of Real Property by Seal Bid [Dkt 228] ("Second Sale Motion") and sustaining certain of the Movants' objections to the Second Sale Motion [Dkt 232, 235, 240]. Specifically, the May 2 Order provided Movants with the right to credit bid on the properties at issue in the Second Sale Motion (the "Sale Properties").

On May 22, 2019, Magistrate Judge Kim entered an Order [Dkt 382] ("May 22 Order") granting the Receiver's Fifth Motion for Court Approval of the Process of Public Sale of Real Property by Sealed Bid [Dkt 329] ("Fifth Sale Motion"), over objections of certain Movants [Dkt 364, 370]. In regards to the Fifth Sale Motion, Movants objected on the basis that the Receiver had not proposed an acceptable protocol under which Movants could execute on the credit bid rights the Court granted in the May 2 Order. Accordingly, the May 22 Order instructed the lenders to file a "a joint motion to amend [the May 2 Order] to ***establish procedures for submitting credit bids***" if the lenders were unable to reach an agreement with the Receiver on the manner, timing, and methodology for placing credit bids. May 22 Order, p. 5 (emphasis added).

The Movants filed their Consolidated Motion to Amend May 2, 2019 Memorandum Opinion and Order [Dkt 418] ("Motion to Amend") to establish the procedures for submitting credit bids. The Motion to Amend requested: (1) a determination of the amount due each Mortgagee and all other lien holders for each property; (2) a priority determination as to each lien

recorded against each property listed for sale; (3) waiver of "traditional" closing costs; and (4) the setting of the sale price in excess of the debt.

On July 9, 2019, Magistrate Judge Kim entered the July 9 Order denying the Motion to Amend.

ARGUMENTS

Pursuant to Federal Rule 72, Movants respectfully object to the July 9 Order. Consistent with the May 22 Order, the Motion to Amend set forth a protocol that would permit Movants to execute on the credit bid rights the Court granted in its May 2 Order. Movants have attempted to work with the Receiver throughout the duration of the receivership in connection with the scheduling of the claims process, the sale of the various properties, and discovery regarding the same (Movants produced thousands of pages in discovery in connection with their claims). Moreover, at the plain urging of the July 9 Order, Movants continue to engage in meet and confers with the Receiver's counsel to iron out a credit bid protocol that is fair and mechanically feasible. However, the credit bid protocol currently proposed by the Receiver and now required under the July 9 Order is inconsistent with Illinois law and effectively eliminates the credit bid rights the Court intended to grant in its May 2 Order. Accordingly, the Court should overrule the July 9 Order and grant the Motion to Amend.

I. THE CURRENT "CREDIT BID PROTOCOL" UNDERCUTS THE STATED PURPOSE OF CREDIT BIDDING.

As the United States Supreme Court explained, "[t]he ability to credit-bid helps to protect a creditor against the risk that its collateral will be sold at a depressed price. It enables the creditor to purchase the collateral for what it considers the fair market price (up to the amount of its security interest) without committing additional cash to protect the loan." *RadLAX Gateway Hotel, LLC v. Amalgamated Bank*, 566 U.S. 639, 644 n.2 (2012). In contradiction of the stated purpose of

granting parties like Movants the right to credit bid, the current credit bid structure disincentivizes Movants from credit bidding and, moreover, requires Movants to bear a substantial risk of taking a discounted payoff.

A. The amount due each Mortgagee must be determined before a Mortgagee can credit bid.

The July 9 Order suggests that the Motion to Amend was, in effect, Movants' attempt to make an "end-run" around the Court's prior decisions with respect to the timing of certain priority disputes and whether the Receiver should be required to abandon failing properties. (*See* July 9 Order at n 1.) Movants have no desire to relitigate issues the Court has already decided upon. Rather, the Motion to Amend and this Objection is designed to effectuate the rights the Court granted to Movants in the May 2 Order, consistent with Illinois law.

Under the Receiver's proposed credit bid structure, Movants are required to choose between not taking advantage of their right to credit bid (as confirmed under the May 2 Order) *or* credit bidding on the Sale Properties without knowing precisely how much "credit" they are entitled to bid. If Movants decline the right to credit bid, they undertake the risk the Supreme Court described—that the Sale Properties will be sold at a price well below the amount of debt owed, requiring Movants to take a substantial discount in their payoffs. If Movants move forward on the credit bid, however, without any certainty regarding the amount of their "credit," they are still bound by their bids and may be required to pay cash to make up any shortfall. The protocol outlined in Movants' Motion to Amend addresses these issues so that Movants can make an informed decision on their rights to credit bid, consistent with Illinois law.

Under Illinois law, credit bidding allows a mortgagee to bid the amount of its debt to purchase foreclosed property. *FDIC v. Chicago Title Ins. Co.*, No. 12-CV-05198, 2015 WL 5276346, at *4 (N.D. Ill. Sept. 9, 2015). Significantly, unlike a third party bidder, a lender is not

required to pay cash. *Id.* Indeed, the whole purpose of credit bidding is to avoid the inefficiencies of requiring a lender to tender cash that would immediately be returned back to the lender. *Id.*; *FDIC v. Meyer*, 781 F.2d 1260, 1265 (7th Cir. 1986). Notwithstanding the underlying purpose of a lender's right to credit bid (as restated by Illinois courts), the July 9 Order requires Movants to do just that: tender a letter of credit in the amount of their "credit bid" (which is equivalent to tendering cash) in order to execute on their right to credit bid. Conditioning Movants' rights to credit bid upon the procurement of a letter of credit while requiring them to credit bid without knowing the amount of their "credit" defeats the purpose of a credit bid.

Indeed, as set forth in the Motion to Amend, Movants requested the Court to set a floor on the sale prices for the Sale Properties to mitigate against this risk. If the sale prices *start* at the full amounts of Movants' claims, Movants may then elect *not* to credit bid (since they do not have sufficient information to do so), knowing that the Sale Properties are unlikely to be sold at an amount far below their claims. The July 9 Order refers back to the reasoning provided in the May 2 Order for denying this reasonable modification to the May 2 Order. According to the May 2 Order, the reason the Court denied Movants request to set the floor sale prices of the Sale Properties, was that "lenders now have the ability to exercise their right to submit a credit bid." (May 2 Order at 10.) As detailed above, the July 9 Order curtails that right to such a degree that it threatens to be eliminated.

B. Lien priority must be determined to effectively conduct the credit bid process.

Similarly, lien priority for each property that is listed for sale must be determined to effectively conduct the credit bid process. Adjudication of priority status, similar to determination of the debt amount, is necessary because it identifies the priority structure, sets the limits of the senior lienholders credit bid amount, determines how much cash a junior lienholder must pay to

eliminate a senior lienholder, and determines the amount a foreclosing lienholder must pay in cash if it bids more than its mortgage debt. *Meyer*, 781 F.2d at 1264-65.

For example, in *Partel*, three separate mortgagees each held a mortgage on the same piece of real estate. Their respective priorities and the amounts due each were determined in a consolidated foreclosure action. *Id*. at 963. A public foreclosure sale was held and the second secured lienholder was the highest bidder. The second lienholder's bid consisted of the full amount of the senior lienholder's debt plus the second lienholder's adjudicated debt.[1] *Id*. at 964. The second lienholder obtained title to the property by buying out the senior lienholder and outbidding any other competing parties. *Id*.

The exact same principle applies here. The Receiver has taken the position that EquityBuild investors have prior secured positions on certain of the Movants' properties. While Movants are mindful that the Court has already ruled that the Receiver is not required to make a priority determination prior to moving forward with the proposed sales, this was *before* the Court granted Movants the right to credit bid. Now that the Court has provided for such a right, Movants should be furnished with the information necessary to effectuate those rights. Movants cannot make an informed decision as to whether they must buy out a senior lienholder, the amount of their credit bid, and whether crediting bidding is in their best interest until a determination is made as to the priority of their claims. *See Meyer*, 781 F. 2d at 1264-65.

II. THERE IS NO "CAUSE" TO DENY THE MOVANTS' REQUEST TO MODIFY THE CREDIT BID PROCEDURES.

No cause has been shown to warrant denial of the Motion to Amend. As Magistrate Judge Kim correctly points out, 11 U.S.C. 363(k) grants a secured lien claimant the right to credit bid at the sale of the property on which the lien claimant has a lien "unless the court ***for cause*** orders

[1] The second lienholder was not required to bid the full amount of its debt but did so for unknown reasons.

otherwise." 11 U.S.C. 363(k) (emphasis added). There is no indication there is "cause" here to limit the Movants' statutory right.

The July 9 Order relies on *In re Fisker Automotive Holdings, Inc.*, 510 B.R. 55 (D. Del. 2014) in support of the decision to deny the Motion to Amend. In *Fisker*, a party purchased a creditor's $168 million secured bankruptcy claim for $25 million. In connection with the future sale of the property, a third party expressly represented that it would not participate in the auction if the lender's credit bid was not capped. Accordingly, the court granted the purchaser the right to credit bid only $25 million and not the full amount of the secured claim ($168 million) because bidding at the sale would "not only be chilled without the cap; bidding will be frozen." *Id*. at 60. Here, there is no indication that determining a Movant's debt amount and, in turn, its credit bid amount, would create a chilling effect on bidding. In the present case, adjudicating the amount of each Movants' debt and lien priority prior to the sale will provide clarity as to the terms of the sale and inform all bidders (including third parties) how much a Mortgagee can credit bid. Any interested bidder can use this information to formulate its own bidding strategy.

Moreover, the July 9 order relies on *In re Philadelphia Newspapers, LLC*, 599 F.3d 298 (3d Cir. 2010) to support denial of the Motion to Amend. There, the court analyzed the very narrow issue of whether a certain provision of the bankruptcy code allowed a debtor to confirm a Chapter 11 plan of reorganization without the approval the creditors (i.e., a cramdown) and which denied the creditor's the right to credit bid. The court held that a certain portion of the Bankruptcy Code did allow for this type of cramdown, so long as the plan provides the creditors the "indubitable equivalent" of their secured interest. *Id*. at 313. Here, there is no plan of reorganization and there is no "indubitable equivalent" given to the Movants. Rather, the Receiver proposes to sell certain properties free and clear of the Movants' liens without providing any

"indubitable equivalent" or protection of the Movants' claims, which is a violation of bankruptcy principles and wholly inconsistent with Illinois law. Indeed, *Philadelphia Newspapers* illustrates that if a secured creditor is denied the right to credit bid, it must be given other protections, i.e., indubitable equivalent. Here, no such protections are given to the Movants.

III. MOVANTS' PROPOSED CREDIT BID PROTOCOL CAN RUN IN TANDEM WITH THE RECEIVER'S CLAIMS PROCESS.

In sum, the Court's orders, to date, have authorized the Receiver with selling the Sale Properties *and* provided Movants with the right to credit bid on those sales. In order to effectively hold a sale of a property and to allow credit bidding, Movants and all other interested parties must know what liens are validly recorded against the properties, the priority of those liens, and the amount of each lien. As illustrated in *Fisker*, it is important for third party bidders to know (1) whether a creditor can credit bid; and (2) how much that creditor can credit bid.

The Movants are not attempting to upend the claims process. Rather, the issue presented by Motion to Amend and the Court's request in the May 22 Order relate solely to establishing procedures for submitting credit bids. These procedures can run in tandem with the claims process. The claims bar date was July 1, 2019. The Receiver knows exactly what claims have been asserted against which properties, the amount of the claims, and the claimant for each claim. The Receiver can share this information with Movants and a determination be made as to the priority and amounts owed for each claimant on each property that is subject to a pending sale motion or future sale motions. Currently, there are only eleven Sale Properties on which the Receiver has indicated there are both a "conventional" lender's lien *and* an EquityBuild affiliate lien. *See* Dkt 228, pp. 4-5; Dkt 329 pp. 1-2. The Receiver has admitted that all other Sale Properties are encumbered by "conventional" lenders' liens *only*. *Id*.

Therefore, even before the July 1 claims bar date, the Receiver had in his possession sufficient information to allow him to make such representations to the Court. Now, after the July 1 claims bar date, the Receiver has even more information to determine the priority of liens and amount of each lien for each property he proposes to sell. The Movants simply request lien priority and debt amount be decided before any property that is subject to a pending sale motion (or future sale motion) is sold. At a minimum, the Sale Properties on which Movants have a lien should be listed at a price that ensure they are protected against the risk described by the Supreme Court in *RadLax* (i.e., discounted payoff due to a depressed sale price). As illustrated above, these requests do not implicate every single property the Receiver intends to sell. Rather, the request is limited to only certain properties on which the "conventional" lenders have a lien.

IV. THE MOVANTS REQUEST CLARITY ON WHAT CREDIT BID PROCEDURES CURRENTLY APPLY.

Pursuant to Magistrate Judge Kim's June 20, 2019 Minute Order [Dkt 423], the Movants submitted a redlined version of the Sealed Bid Public Sale of Real Estate Terms and Conditions [Dkt 430] identifying the Movants' requested changed to the terms and conditions, including the waiver of traditional closing costs, which should not be placed upon the Movants. The typical costs associated with a commercial foreclosure include publication costs and the selling agent's commission. Any other costs in a commercial foreclosure beyond publication and the selling agent's nominal commission is generally at the election of the lender. The July 9 Order rejected these changes. It is unclear what terms and conditions currently control credit bidding. Therefore, the Movants respectfully request that the court clarify the exact procedures from credit bidding, including the manner, timing, and methodology of placing credit bids.

CONCLUSIONS

For the foregoing reasons, the Movants object to the July 9 Order and request that this Court grant the relief requested in the Motion to Amend or such other relief as the court deems equitable and just.

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Dated: July 22, 2019

Respectfully submitted,

/s/ Mark Landman
Mark Landman (mlandman@lcbf.com)
Landman Corsi Ballaine & Ford P.C.
120 Broadway, 27th Floor
New York, NY 10271
Ph: (212) 238-4800
Fax: (212) 238-4848
Counsel for Freddie Mac

/s/ James P. Sullivan
James P. Sullivan (jsulliva@chapman.com)
Chapman and Cutler LLP
111 West Monroe Street
Chicago, IL 60603
Ph: (312)845-3445
Fax: (312)516-1445
Counsel for BMO Harris Bank N.A.

/s/ James M. Crowley
James M. Crowley
(jcrowley@plunkettcooney.com)
Plunkett Cooney, PC
221 N. LaSalle Street, Ste. 1550
Chicago, IL 60601
Ph: (312) 970-3410
Fax: (248) 901-4040
Counsel for UBS AG

/s/ Joseph R. Sgroi
Joseph R. Sgroi (jsgroi@honigman.com)
Scott B. Kitei (skitei@honigman.com)
Honigman LLP
2290 First National Building
660 Woodward Avenue
Detroit, MI 48226-3506
Ph: (313) 465-7570
Fax: (313) 465-7571
Counsel for BC57, LLC

/s/ Thomas B. Fullerton
Thomas B. Fullerton
(thomas.fullerton@akerman.com)
Akerman LLP
71 S. Wacker Drive, 47th Floor
Chicago, IL 60606

/s/ Jill L. Nicholson
Jill Nicholson (jnicholson@foley.com)
Andrew T. McClain (amcclain@foley.com)
Foley & Lardner LLP
321 N. Clark St., Ste. 2800
Chicago, IL 60654
Ph: (312) 832-4500
Fax: (312) 644-7528
Counsel for Citibank N.A., as Trustee for the Registered Holders of Wells Fargo Commercial Mortgage Securities, Inc., Multifamily Mortgage Pass-Through Certificates, Series 2018-SB48; U.S. Bank National Association, as Trustee for the Registered Holders of J.P. Morgan Chase Commercial Mortgage Securities Corp., Multifamily Mortgage Pass-Through Certificates, Series 2017-SB30; U.S. Bank National Association, as Trustee for the Registered Holders of J.P. Morgan Chase Commercial Mortgage Securities Corp., Multifamily Mortgage Pass-Through Certificates, Series 2017-SB41; U.S. Bank National Association, as Trustee for the Registered Holders of J.P. Morgan Chase Commercial Mortgage Securities Corp., Multifamily Mortgage Pass-Through Certificates, Series 2018-SB50; Wilmington Trust, National Association, as Trustee for the Registered Holders of Wells Fargo Commercial Mortgage Trust 2014-LC16, Commercial Mortgage Pass-Through Certificates, Series 2014-LC16; and Fannie Mae

Ph: (312) 634-5700
Fax: (312) 424-1900
Counsel for Midland Loan Services,
a Division of PNC Bank, National Association

CERTIFICATE OF SERVICE

I hereby certify that on July 22, 2019, I provided service of the foregoing **Objection to Order Dated July 9, 2019**, via ECF filing to all counsel of record, and via U.S. mail to the following individuals and entities:

Jerome and Patricia Cohen
1050 8th Avenue N.
Naples, FL 34102
Defendant

First Bank
Client Contact Center
600 James S. McDonnell Blvd.
St. Louis, MO 63042

/s/ Jill L. Nicholson
Jill Nicholson (jnicholson@foley.com)
Andrew T. McClain (amcclain@foley.com)
Foley & Lardner LLP
321 N. Clark St., Ste. 2800
Chicago, IL 60654
Ph: (312) 832-4500
Fax: (312) 644-7528
Counsel for Citibank N.A., as Trustee for the Registered Holders of Wells Fargo Commercial Mortgage Securities, Inc., Multifamily Mortgage Pass-Through Certificates, Series 2018-SB48; U.S. Bank National Association, as Trustee for the Registered Holders of J.P. Morgan Chase Commercial Mortgage Securities Corp., Multifamily Mortgage Pass-Through Certificates, Series 2017-SB30; U.S. Bank National Association, as Trustee for the Registered Holders of J.P. Morgan Chase Commercial Mortgage Securities Corp., Multifamily Mortgage Pass-Through Certificates, Series 2017-SB41; U.S. Bank National Association, as Trustee for the Registered Holders of J.P. Morgan Chase Commercial Mortgage Securities Corp., Multifamily Mortgage Pass-Through Certificates, Series 2018-SB50; Wilmington Trust, National Association, as Trustee for the Registered Holders of Wells Fargo

Commercial Mortgage Trust 2014-LC16, Commercial Mortgage Pass-Through Certificates, Series 2014-LC16; and Fannie Mae