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UNITED STATES DISTRICT COURT

DISTRICT OF OREGON

PORTLAND DIVISION

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

AEQUITAS MANAGEMENT, LLC; AEQUITAS HOLDINGS, LLC; AEQUITAS COMMERCIAL FINANCE, INC.; AEQUITAS CAPITAL MANAGEMENT, INC.; AEQUITAS INVESTMENT MANAGEMENT, LLC; ROBERT J. JESENIK; BRIAN A. OLIVER; and N. SCOTT GILLIS,

Defendants.

Case No. 3:16-CV-00438-PK

**SECURED CREDITORS WEIDER HEALTH & FITNESS'S AND BRUCE FORMAN'S STATEMENT ON PROPOSED PROCEDURE FOR ADEQUATE PROTECTION HEARING**

**REQUEST FOR ORAL ARGUMENT**


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During the recent hearing on this matter, the Court and the parties discussed holding a hearing to determine the amount of proceeds generated by the sale of receivership assets that should be segregated and reserved for secured creditors Weider Health & Fitness (Weider) and Bruce Forman (Forman). After approving the Receiver's proposed sale of assets "free and clear" of Weider's and Forman's interests (see Order, ECF No. 362), the Court instructed the parties to confer on procedural and discovery issues concerning the adequate hearing and report back to the Court.

Weider and Forman propose a straightforward procedure for determining the amount to be reserved that is rooted in binding authority and squarely addresses the segregation-amount question the Court seeks to answer. Weider and Forman propose that the parties present argument and evidence concerning whether Weider and Forman: (i) have an interest in the proceeds of the sale of CarePayment® healthcare receivables; (ii) validly perfected their security interests; and (iii) loaned money to the Receivership Entities that the borrower (CarePayment Holdings, LLC) has not repaid. If Weider and Forman establish these three facts, the Court should order that the Receiver segregate the full amount of Weider's and Forman's interest pending resolution of the extent, validity, and priority of the interests in a subsequent adversary proceeding, if any.[1]

The Receiver, on the other hand, seeks to conduct an amorphous hearing that is unmoored from case authority and sidesteps well-established procedural protections for secured creditors like Weider and Forman. The Receiver would prefer to hold an interim hearing, on unspecified allegations, under unspecified and unsupported legal standards, and fish for unspecified evidence, all to convince the Court to reserve some unspecified amount less than the amount in dispute, pending later resolution of Weider's and Forman's interests, at which point the Receiver may well have spent the money in which the Court later determines that Weider and Forman have perfected priority interests. Setting aside that this procedure contravenes well-established authority, it makes no sense: there is no point in conducting an ad-hoc and ill-defined proceeding now, in order to

[1] The adversary proceeding would require that the Receiver file a complaint notifying Weider and Forman of the basis for the Receiver's allegations. That proceeding would provide the parties a full opportunity to investigate and litigate those allegations.

segregate and preserve less than the full value of Weider's and Forman's interests, when—as the Receiver itself admits—the extent, validity, and priority of those interests must be fully litigated in the future, at which point the Court will then determine whether Weider and Forman should receive the full value of their interests or something less.

Because the law neither supports nor contemplates the Receiver's unsupported approach to adequate protection, it should be rejected in favor of Weider's and Forman's reasoned proposal.

## BACKGROUND

Between 2011 and 2015, Weider and Forman loaned millions of dollars to Receivership Entities, including $10.5 million to CarePayment Holdings, LLC. Weider & Forman Limited Obj. 5-8, ECF No. 344. The CarePayment Holdings loans are secured by many things, including: (i) equity interests in CarePayment Holdings' subsidiaries, CarePayment, LLC and CP Funding I Holdings, LLC; and (ii) CarePayment® receivables portfolios owned by these subsidiaries. Id. In December 2016, the Receiver moved for an order approving the sale of certain Receivership assets "free and clear" of interests. Receiver's Mot. 4 & ¶¶ 28, 30, ECF No. 323. The sale included an exclusive right to purchase CarePayment® healthcare receivables owned by the subsidiary companies (Receiver's Resp. 8-9, ECF No. 353), which means that the Receiver's sale disposed of some of the collateral securing the Weider and Forman loans.

Weider and Forman filed a limited objection to the sale, demonstrating their interest in the receivables, but agreeing to consent to the sale as long as they received adequate protection for their first-priority, secured interests as required by 11 U.S.C. § 363(e) and the Court's order appointing the Receiver. Weider & Forman Limited Obj. 2-3, 25-26, 29-30, ECF No. 344. Consistent with legislative history and Ninth Circuit precedent (see Bankruptcy Reform Act, S. Rep. No. 95-989, at 56 (1978), as reprinted in 1978 U.S.C.C.A.N. 5787, 5842, and In re Clark, 266 B.R. 163, 171 (Bankr. 9th Cir. 2001)), Weider and Forman requested that the adequate protection take one of two forms, either: (i) attach Weider's and Forman's interests to the proceeds of the sale and segregate the amount owed to them for later distribution; or (ii) pay Weider and Forman from the proceeds of the sale to extinguish their interests. Weider/Forman Limited Obj. 2-3, 25-26, 29-30, ECF No. 344.

This was not an unusual request: the Receiver provided this protection to Terrell Group Management, LLC (TGM) after it filed a limited objection. Jan. 20, 2017 Hr'g Tr. 15:20-16:7.

Weider and Forman stressed in their pleadings and during the hearing that, although they had the contractual right to prevent the sale of their collateral, their intent was not to prevent the sale, but rather to ensure that when the Receiver disposes of the collateral, it protects their interests (i.e., does not spend the sale proceeds up to their interests)—an assurance that the Receiver was unwilling to provide, despite it being the very protection required by section 363(e). Weider & Forman Limited Obj. 2, ECF No. 344 ("Weider and Forman do not wish to impede a sale that may ultimately benefit all parties impacted by the allegations here…. They simply wish to avoid a scenario in which their contractual rights are derogated and their interests in millions of dollars of first-priority, secured debt are unprotected…. The solution to the problem … is a Court order providing Weider and Forman adequate protection…. [T]hey will give their consent to the proposed sale on the condition that the Court order adequate protection[.]"); Jan. 20, 2017 Hr'g Tr. 18:14-16 ("Your Honor, if we – if the receiver was amendable to what Terrell got, which is segregation, we're done here.").

The Receiver responded by arguing that Weider's and Forman's interests are subject to a "bona fide dispute," and the sale could therefore proceed under 11 U.S.C. § 363(f)(4) without their consent; the Court could set aside some amount of sale proceeds as adequate protection; and entitlement would be litigated during the subsequent claims process. Receiver's Resp. 2, 22-26, ECF No. 353. Indeed, the Receiver acknowledged that, "because the receiver needs to sell the assets, Weider/Forman is entitled to some protection." Jan. 20, 2017 Hr'g Tr. 25:24-26:1. The Receiver then requested a hearing to determine the sum to be segregated, asserting the novel proposition that the Court should segregate some amount less than the disputed interest as "adequate" protection. Receiver's Resp. 2, 26, ECF No. 353. The Receiver also repeatedly

asserted in its response brief[2] and during oral argument[3] that the requested hearing would be limited to determining the sum to be segregated, and that parties would need to litigate the extent, validity, and priority of Weider's and Forman's interests during the claims process.

Based on the Receiver's representations that a hearing is needed to determine the amount of reserve, the Court ordered that there would be a hearing on what, if any, reserve should be segregated from the sale's proceeds as adequate protection pending subsequent resolution of Weider's and Forman's claims. Id. at 27:11-12, 29:7-30:3, 30:9-11. The Court asked the parties to confer over the scope and timing of the hearing. Id. at 23:18-24:3, 24:21-25:4, 29:9-16.

The Court also granted interim protection pending the hearing, ordering that "if there's an exercise of the option and … we have not resolved the question of the right to those funds or the amount of those funds … before anything is dissipated, I wanted to come back to court and give

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[2] Receiver's Resp. 2, ECF No. 353 ("The Receiver requests that this Court set a preliminary hearing … to require Weider/Forman to provide evidence of the funds it advanced to CP Holdings … and thereafter decide the amount … the Receiver should segregate."); id. at 10 n.3 ("The preliminary hearing is not intended to resolve the extent, validity, and priority of the alleged claim."); id. at 12 ("The Receiver requests that this Court set a preliminary hearing … to determine the amount of funds … the Receiver should segregate … because the existence of that obligation is disputed."); id. ("The preliminary hearing is limited in scope—it will not address the allowance or treatment of Weider/Forman's claim, that needs to wait until for the claim process and distribution plan[.]"); id. at 14 ("The preliminary hearing would establish whether there is sufficient evidence to warrant the segregation of funds[.]"); id. ("The Receiver requests a hearing …, and discovery before then, that would allow the Court to assess the amount of funds the Receiver should segregate[.]"); id. at 26 ("This Court should deny Weider/Forman's objections, approve the sale of … Receivables Assets free and clear of liens …, with … a further hearing …, to determine the amount …, if any, which the Receiver will hold pending the future adjudication … of the Weider/Forman claim at the appropriate time….").

[3] Jan. 20, 2017 Hr'g Tr. 19:24-20:3 ("[T]here was a discussion internally about providing some protection to Weider/Forman for their loan. The receiver is not willing to do that without Your Honor holding a further hearing so that we can determine the extent to which funds should be held."); id. at 21:1-7 ("[W]e think that the amount that should be held is substantially less than that…. I want to be careful to be clear with you that this isn't a complete resolution of the Weider/Forman claim. This would be limited in scope for the purpose of having you determine what the correct amount of funds that should be held is."); id. at 25:11-25:13 ("The claims process, Your Honor, requires a full investigation, a plan and distribution, which is many months out."); id. at 26:14-16 ("Your Honor should have a further hearing where we decide the amount of the reserve, not where we litigate the entire claim.").

you a chance to express your client's concern…. So you are … in effect, protected[.]" Id. at 33:1-7. With these interim protections in place, the Court approved the sale "free and clear" of Weider's and Forman's interests. Order, ECF No. 362.

**WEIDER'S AND FORMAN'S PROPOSAL**

Weider and Forman propose that the hearing, if any, should track the well-established legal requirements for assessing the amount to be reserved when there is a bona fide dispute over proceeds from a sale under 11 U.S.C. § 363(f). Those legal requirements, as applied here, require a determination of only three issues:

1. Whether Weider and Forman have an interest in proceeds from the sale of CarePayment® healthcare receivables that are part of the sale option;
2. Whether Weider and Forman perfected their security interests; and
3. The amount of Weider's and Forman's security interests.

The Court can resolve these issues by examining law and documents, without testimony or a hearing (except, if requested, oral argument on these issues). As discussed below, authority makes clear that the Receiver's contention that the Court should reserve some amount less than the full amount of Weider's and Forman's security interest based on allegations of fraudulent conveyance does not reduce the amount that must be set aside as adequate protection. Instead, these allegations established the existence of a "bona fide dispute" as to Weider's and Forman's interests, which allowed the sale to proceed, but requires segregation of the full disputed amount until the Court can resolve the extent, validity, and priority of the interests in a later adversary proceeding.

**THE RECEIVER'S PROPOSAL**

During a meet-and-confer discussion on January 27, 2017, counsel for the Receiver was unable to identify the grounds on which he would seek to decrease the amount held in reserve for Weider and Forman, and indicated he would not know what those grounds might be until after he conducts discovery.[4] Indeed, he stated that he cannot even have a position on the amount of

[4] This would be an impermissible use of discovery, because discovery is a tool to assist in proving or disproving clearly-defined allegations, not an excuse to engage in a fishing

reserve without a hearing. The Receiver did not identify the underlying issues that would require resolution during a hearing, the goal or topics of discovery, or any authority that would allow the Court to reserve less than the amount of Weider's and Forman's interests pending later adjudication. At the end of the call, the parties agreed to touch base the following week.

On February 2, 2017, Weider's and Forman's counsel emailed the Receiver's counsel, outlining the issues to be addressed at the hearing, proposed scope of discovery, and a schedule to accomplish discovery and briefing. See Decl. of Matthew Donald Umhofer, Ex. 1. Weider's and Forman's counsel cited In re Clark, 266 B.R. 163, 171 (Bankr. 9th Cir. 2001), which answers the segregation issue presented here. Umhofer Decl., Ex. 1.

On February 3, 2017, the Receiver's counsel explained it was busy and would be in touch by the following Wednesday. See Umhofer Decl., Ex. 2.

The following Wednesday, February 8, 2017, the Receiver's counsel explained it was still busy and would be unable to call before Friday. See Umhofer Decl., Ex. 3.

On Friday, February 10, 2017, without further communication with Weider's and Forman's counsel, the Receiver filed its quarterly report. See Jan. 31, 2017 Report, ECF No. 365. As to the hearing, the Receiver stated that: (i) it would segregate all sale proceeds in a non-interest bearing account "until the Court rules how much, if any, should so be retained;" (ii) the hearing should be limited to determining only what "set aside" should be required; it should not address the amount and priority of Weider's and Forman's claims, which are issues to be litigated during a later "claims administration process;" and (iii) its apparent basis for disputing the reserve amount is a belief that Weider and Forman may not have loaned CarePayment Holdings $6 million of the $10.5 million principal loan amount. Id. at 40. The Receiver alluded

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expedition. See McHenry v. Renne, 84 F.3d 1172, 1178 (9th Cir. 1996) (complaint must set forth "who is being sued, for what relief, and on what theory, with enough detail to guide discovery") (emphasis added); Barker v. JP Morgan Chase Bank, 2016 WL 3647329, at *10 (D. Or. July 7, 2016) ("Mr. Barker acknowledges in his complaint that his claims are part of a 'fishing expedition' to find through discovery what he does not yet know. This is not a permissible use of a complaint.").

to "[o]ther defenses" it "might" have, but—again—stated those defenses would be addressed during the claims process. Id.

The report also contained alarming statements that cause Weider and Forman to question whether the Receiver is acting in the interests of all creditors (including them):[5]

- The Receiver represented that Weider's and Forman's "new counsel" stated it no longer intended to participate in a proposed $8.5 million settlement (Jan. 31, 2017 Report at 38, ECF No. 365) when, in fact:
    - on October 14, 2016, the Receiver offered to pay Weider and Forman $8.5 million "due at or near the time of closing of the receiver's sale of CarePayment Technologies, Inc., which will provide the liquidity to fund the payment" (see Decl. of Bruce Forman, Ex. A);
    - but, on December 16, 2016, the Receiver moved to approve the sale of CarePayment Technologies, Inc. without even mentioning Weider and Forman (see Mot., ECF Nos. 323-325); and
    - on January 12, 2017, Weider's and Forman's counsel sent the Receiver's counsel a letter stating "we'd prefer to resolve the matter with no further delay and avoid objections … my clients are prepared to accept the reduced amount of $8.5 million, on the condition that the receiver seeks immediate court approval of this $8.5 million settlement" (see Umhofer Decl., Ex. 4);
    - but, the Receiver was unwilling to seek Court approval for the settlement and threatened to rescind the settlement if Weider and Forman filed their objection (which, of course, they were required to do to avoid waiver objections) (cf. Jan. 31, 2017 Receiver's Report 39-40 (representing that Weider and Forman rejected the $8.5 million settlement offer, which "frees the Receiver to assert the Receivership Entity's full legal rights")).
- The Receiver represented that Weider and Forman demanded preferential treatment in the form of immediate repayment (Jan. 31, 2017 Report at 38, ECF No. 365) when, in fact, Weider and Forman asked for either segregation or repayment (Weider & Forman Limited Obj. 2-3, 25-26, 29-30, ECF No. 344)—protection expressly set forth in the Bankruptcy Code. See 11 U.S.C. § 361

[5] See Booth v. Clark, 58 U.S. 322, 331 (1854) ("A receiver is an indifferent person between parties, appointed by the court … in behalf of all parties, and not of the complainant or of the defendant only."); S.E.C. v. Hardy, 803 F.2d 1034, 1038 (9th Cir. 1986) ("[A] primary purpose of equity receiverships is to promote orderly and efficient administration of the estate by the district court for the benefit of creditors.").

(stating adequate protection may be provided by requiring "a cash payment or periodic cash payments" or "a replacement lien").

- And, the Receiver represented that Weider and Forman attempted to "hold this Receivership and its assets hostage so they can step ahead of all other investors" (Jan. 31, 2017 Report at 39, ECF No. 365) when, in fact, Weider and Forman went out of their way to explain that, despite their rights, they would not object to the proposed sale as long as they received adequate protection in the form of segregation or repayment (Weider & Forman Limited Obj. 2-3, ECF No. 344).

In light of these (and similar) exchanges, Weider and Forman cannot rely on the Receiver alone to protect their interests and respectfully have requested, and continue to request, protection from the Court. Nothing underscores Weider's and Forman's need for the Court's protection more than the Receiver's position that the collateral for the loans includes only the companies that own the receivables, not the receivables themselves, which—according to the Receiver—should allow it to sell the receivables with impunity. Jan. 31, 2017 Report at 37-40, ECF No. 365. By the time of any later distribution, this would mean there is no money left to satisfy Weider's and Forman's first-priority, secured interests. Cf. Jan. 20, 2017 Hr'g Tr. 21:9-14 ("[W]hat protection are you willing to put in place until that hearing is resolved? Because I'm not going to tell Weider/Forman that we'll have a hearing, and when we get to the end of it, there [are] no assets because … whatever has happened, they're gone…. [I]n the interim … what protections are put in place to preserve Weider's rights, if in fact they are correct that they are … entitled to some priority on a larger share of the assets[.]").

On February 10, 2017, the Receiver's counsel responded to Weider's and Forman's counsel regarding the proposal for the adequate protection hearing. Umhofer Decl., Ex. 5. He took the position that this Court had already ruled that it would "hear evidence relating to failure of consideration and other factors affecting his ultimate determination of whether your clients are entitled to a reserve and, if so, in what amount." Id. The Receiver characterized Weider's and Forman's proposal as a request for reconsideration of issues that had been determined at the January 20, 2017 hearing. Id.

Weider and Forman disagree with the Receiver's characterization of the Court's statements regarding the adequate protection hearing. The Court held that there would be a hearing limited to what, if any, funds should be held in reserve to protect Weider's and Forman's interests:

- "This is ultimately about what reserve … or if there's any reserve, I think is the real question." Jan. 20, 2017 Hr'g Tr. 27:11-12.
- "[L]et's have the hearing on your entitlement [to a reserve]." Id. at 29:10.
- "We're talking about a later hearing as to whether you're entitled to have a reserve at all and what the amount should be." Id. at 30:9-11.

Beyond this, the Court did not rule on the issues to be addressed in the hearing, the evidence to be exchanged and submitted, or even the form of the hearing; instead, it asked the parties to confer and, if they could not come to an agreement, seek further clarification from the Court:

- "I would like to … hear from both of you what form the hearing would take. Are we going to have evidence or would it be in the form of summary judgment with declarations, or how we will present information?" Jan. 20, 2017 Hr'g Tr. 21:15-19.
- "I'm happy to have you address first the scope of the hearing, and perhaps in a telephone conference resolve whether it should be a more complete hearing…. If you can't do that amongst yourselves, … set the hearing date. I'd like to get you to consult and confer about how to present evidence, whether we're going to have a formal taking of testimony or you can submit declarations and other exhibits for me to review and then just orally argue it…. I need to have you consult and confer about the scope. I need you to tell me whether I need to be informed to weigh in on whether we're going to take up all the issues you're suggesting or what you call the subpart that Mr. Ream is suggesting, and then I'd like to hear from you both about how that hearing should best take place, whether we do it in a written record or we do it in person with oral argument, with live testimony." Id. at 23:18-25:4 (emphasis added).
- "I suggest a [proposal] from you both so I understood it better and then taking it up by telephone conference[.]" Id. at 26:17-20.
- "[I]f you would discuss the form of that hearing, and if you need prehearing discovery, call Mr. Magnuson and give me a hearing date or dates that you're interested in, tell me how much time you think you need in terms of live testimony or what's to be submitted in advance, and we'll get it on the record and on the calendar and do it." Id. at 29:10-16.

- "Could you consult? I don't know what discovery you're going to be taking and … how your schedules work and who is flying in from where for this…. So you work it out and let me know. Okay?" Id. at 29:22-30:3.

Because discussions with the Receiver's counsel appear to have come to an impasse, Weider and Forman respectfully file this proposal in anticipation of a telephonic (or other) conference to discuss the scope of the adequate protection hearing.

## SCOPE OF PROPOSED HEARING

### I. Having Obtained A Sale "Free And Clear" Of Weider's And Forman's Interests On The Basis Of An Alleged "Bona Fide Dispute," The Receiver Must Now Reserve The Entire Disputed Amount Pending Resolution Of Weider's And Forman's Claims

The Court need not conduct a hearing to determine the sum to be segregated as adequate protection because the Receiver must segregate the entire disputed amount pending adjudication of Weider's and Forman's interests. SEC receivers may sell assets "free and clear" of interests under the parameters set forth in 11 U.S.C. § 363(f). See, e.g., S.E.C. v. Capital Cove Bancorp LLC, 2015 WL 9701154, at *4-8 (C.D. Cal. Oct. 13, 2015). Section 363(f) allows a receiver to sell property free and clear of any interest only in one of five circumstances:

> (1) applicable nonbankruptcy law permits sale of such property free and clear of such interest;
>
> (2) such entity consents;
>
> (3) such interest is a lien and the price at which such property is to be sold is greater than the aggregate value of all liens on such property;
>
> (4) such interest is in bona fide dispute; or
>
> (5) such entity could be compelled, in a legal or equitable proceeding, to accept a money satisfaction of such interest.

11 U.S.C. § 363(f).

Here, the Receiver successfully relied on section 363(f)(4) in obtaining approval for a sale "free and clear" of Weider's and Forman's interests on the basis of a "bona fide dispute." Receiver's Resp. 2, 22-26, ECF No. 353 (arguing Weider's and Forman's interests are the subject of a bona fide dispute on the basis of potentially forthcoming allegations of fraudulent

conveyance). "The purpose of § 363(f)(4) is to permit property of the estate to be sold free and clear of interests that are disputed by the representative of the estate so that liquidation of the estate's assets need not be delayed while such disputes are being litigated." In re Clark, 266 B.R. 163, 171 (Bankr. 9th Cir. 2001).

The power to order a sale under section 363(f)(4) is not unlimited; it is cabined by the adequate protection requirement, which provides that, "[n]otwithstanding any other provision of this section, at any time, on request of an entity that has an interest in property used, sold, or leased, or proposed to be used, sold, or leased, by the trustee, the court, with or without a hearing, shall prohibit or condition such use, sale, or lease as is necessary to provide adequate protection of such interest." 11 U.S.C. § 363(e) (emphasis added). In a sale under section 363(f)(4), which by definition proceeds over the interest-holder's objection, the contours of adequate protection are well-established: "the proceeds of sale are held subject to the disputed interest and then distributed as dictated by the resolution of the dispute; such procedure preserves all parties' rights by simply transferring interests from property to dollars that represent its value." In re Clark, 266 B.R. at 171 (emphasis added).

This is consistent with section 363's legislative history, which emphasizes that sales "free and clear" of interests are "subject to the adequate protection requirement," and "[m]ost often, adequate protection in connection with a sale free and clear of other interests will be to have those interests attach to the proceeds of the sale." Bankruptcy Reform Act, S. Rep. No. 95-989, at 56 (1978), as reprinted in 1978 U.S.C.C.A.N. 5787, 5842. Adequate protection can also take the form of cash payments or periodic cash payments. Id. at 5790-91; accord 11 U.S.C. § 361. Either way, "the law is clear, if party has an interest in property that is in bona fide dispute, sale of the property free and clear of the party's interest will not result in irreparable harm because the party has recourse against the proceeds of the sale." In re GGW Brands, LLC, 2013 WL 6906375, at *24 (Bankr. C.D. Cal. Nov. 15, 2013) (emphasis added).

This means that, after receiving approval for a sale under section 363(f)(4), a receiver must hold the proceeds of the sale subject to the disputed interest pending later resolution. See In re Gerwer, 898 F.2d 730, 733 (9th Cir. 1990) (explaining that "[u]nder section 363(e), the

district court had the duty of safeguarding the lienholder's interest" and, after approving a sale under section 363(f)(4), "did so by blocking the account in which the proceeds were to be deposited"); In re NJ Affordable Homes Corp., 2006 WL 2128624, at *15 (Bankr. D.N.J. June 29, 2006) ("[I]t must not be forgotten that the interests of the Title Holders and Institutional Lenders will attach to the proceeds of sale and will be afforded the rights and priorities as ultimately determined by this Court at a future hearing," and "[a]s the Trustee stated during the … hearing, '[i]f there is a valid mortgage that needs to be paid from the proceeds of sale, that mortgage gets paid."); In re Downour, 2007 WL 963258, at *2 (Bankr. N.D. Ohio Mar. 28, 2007) ("[B]ecause the interest is in bona fide dispute and because the validity of the claimed mortgage will have to be determined through an adversary proceeding, Countrywide is entitled to a replacement lien in the net proceeds of sale under 11 U.S.C. § 363(e).").[6]

Contrary to the Receiver's position in briefing and argument, there is simply no authority that would allow the Court to reserve less than the full amount of the disputed interest precisely because it is disputed—it has yet to be resolved. Reserving anything less is not adequate. Allowing the Receiver to reserve less is a Court order allowing the Receiver to take and spend Weider's and Forman's interests without the due process protections provided by a full adversary hearing to determine the extent, validity, and priority of those interests, which would violate the Fifth Amendment to the United States Constitution. In re Bjornson, 1985 WL 660526, at *3 (Bankr. D.N.D. Dec. 12, 1985) ("Normally, the interests of parties in property sold pursuant to section 363(f) attach to the proceeds until the validity and value of the interests is established," and "[p]roceeds from a sale … must be sufficient to provide adequate protection of those

[6] See also SEC v. Capital Cove Bancorp LLC, 2015 WL 9701154, at *8 (C.D. Cal. Oct. 13, 2015) (approving "free and clear" sale but "liens will attach to the proceeds of the sale 'with those liens, claims, and encumbrances to maintain the same force, effect, and priority against the sales proceeds as existed at the time of the closing of the sale"); In re Kellogg-Taxe, 2014 WL 1016045, at *6 (Bankr. C.D. Cal. Mar. 17, 2014) (approving "free and clear" sale but staying payment from sale proceeds pending quiet title action to resolve validity and priority of liens); In re Wilson, 494 B.R. 502, 506 (Bankr. C.D. Cal. 2013) ("Those interests, as validly claimed by the interest holders, must be paid over to the interest holders upon sale under Section 363.").

interests in the property.") (emphasis added); MacArthur Co. v. Johns-Manville Corp., 837 F.2d 89, 94 (2d Cir. 1988) ("It has long been recognized that when a debtor's assets are disposed of free and clear of third-party interests, the third party is adequately protected if his interest is assertable against the proceeds of the disposition.") (emphasis added); In re Gulf States Steel, Inc. of Ala., 285 B.R. 497, 513 (Bankr. N.D. Ala. 2002) ("the process embodied in § 363 of removing liens from one form of collateral and granting replacement liens in another form of economically equivalent collateral is much closer to the universally accepted practice of providing secured creditors with adequate protection for the use, sale or lease of collateral by the trustee on the condition that the trustee provide the affected secured creditor with adequate protection of its interest in the collateral") (emphasis added); cf. Bankruptcy Reform Act, S. Rep. No. 95-989, at 49 (1978), as reprinted in 1978 U.S.C.C.A.N. 5787, 5835 ("The concept of adequate protection is derived from the Fifth Amendment protection of property interests as enunciated by the Supreme Court.") (citing Wright v. Union Central Life Inc. Co., 311 U.S. 273 (1940), and Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555 (1935)).

## II. Allegations Of Fraudulent Conveyance Do Not Diminish The Amount Of Reserve; They Merely May Establish The Existence Of A "Bona Fide Dispute" As To The Security Interest, Which Is Resolved During A Separate Adversary Proceeding

The Receiver argues that it should be allowed to reserve an amount less than the amounts outstanding under the Weider and Forman loans as "adequate" protection because Weider and Forman "may" ultimately be owed less under a theory of fraudulent conveyance, although "further investigation" into the matter is required, and any final determination must occur during a much-later claims process. Receiver's Resp. 2, 4-6, 13, 23-26, ECF No. 353; Jan. 20, 2017 Hr'g Tr. 20:17-21:7; 25:7-13, 26:12-16. The danger, as this Court has already recognized, is that "[m]oney goes away." Jan. 20, 2017 Hr'g Tr. 31:13. Setting aside that any allegations of fraudulent conveyance are baseless and the Receiver's position eviscerates the constitutionally-based

requirement of adequate protection, the Receiver is simply incorrect that allegations of fraudulent conveyance somehow allow it to reserve less than the disputed amount pending final adjudication.

As noted above, section 363(f)(4) allows a court to approve a sale "free and clear" of any interest when "such interest is in bona fide dispute," so that liquidation of assets are not delayed while disputes are litigated, but it requires that the proceeds of the sale be held subject to the disputed interest pending resolution of the dispute. In re Clark, 266 B.R. at 171. Before obtaining approval for the "free and clear" sale, of course, it was the Receiver's burden to "'provide some factual grounds to show some objective basis for the dispute.'" SEC v. Capital Cove Bancorp LLC, 2015 WL 9701154, at *5 (C.D. Cal. Oct. 13, 2015) (citations omitted).[7]

Receivers sometimes do, and here did, allege that a lien is voidable on the basis of fraudulent conveyance, but this merely goes to the existence of a bona fide dispute, which allows the sale to proceed without consent. Id. at *5-8 (finding fraudulent conveyance allegations sufficient to establish a "bona fide dispute" as to the voidability, and allowing sale to proceed, but noting claimant is protected by "adequate assurance requirement"). The finding of a "bona fide dispute" does not—and constitutionally cannot—allow a receiver to segregate less than the disputed amount (let alone spend the disputed amount) before a court's final resolution of the dispute. Id. at *8 (explaining adequate protection is based in the Fifth Amendment, which generally requires sales proceeds be held subject to resolution of dispute).

A federal bankruptcy court explained the issue in In re Laines, 352 B.R. 410 (Bankr. E.D. Va. 2005). A receiver might have many theories for disputing the validity of a lien, including fraudulent conveyance, but "§ 363(f) merely permits the sale to go forward," and "does not

[7] The Court appears to have concluded that the Receiver satisfied its burden by alleging that a bona fide dispute exists, which is generally insufficient to justify a section 363(f)(4) sale. See In re Octagon Roofing, 123 B.R. 583, 590 (Bankr. N.D. Ill. 1991) ("merely alleging a dispute" is insufficient to justify a sale under section 363(f)(4); receiver must show "some factual grounds" to show an "objective basis" for the dispute); In re Robotics Vision Sys., Inc., 322 B.R. 502, 506 (Bankr. D.N.H. 2005) (discussing "wide range of evidentiary requirements that must be met before a court may make a determination that a bona fide dispute exists"). Regardless, Weider and Forman do not object to the sale provided that the Court orders adequate protection as discussed in this filing and required by 11 U.S.C. § 363(e).

invalidate a lien or adjudicate that a lien does not attach to the property." Id. at 415. "[T]he lien, if any, transfers to the proceeds of sale." Id. "If it is not clear that there will be sufficient proceeds to pay all asserted liens in full, administrative expenses will not normally be paid at [the] time [of the sale]." Id. In other words, a receiver must protect the entire disputed amount until a court can rule on the merits of the dispute in the course of a full adversary proceeding. Id. ("[A]ny action that seeks to affect a party's lien … is either a contested matter (such as a motion to sell free and clear under § 363(f)) or an adversary proceeding (such as a complaint to determine the extent, validity, or priority of a lien).").

This is why, after finding a "bona fide dispute," courts order that the sale proceeds be held subject to resolution of the dispute. See, e.g., In re Clark, 266 B.R. at 171; In re Gerwer, 898 F.2d at 733; In re Kellogg-Taxe, 2014 WL 1016045, at *6. A full adversary proceeding on the issue of fraudulent conveyance is then constitutionally and statutorily required before depriving a party of its secured interests (i.e., before spending their collateral). Fed. R. Bankr. P. 7001(1)-(2) & advisory committee notes (requiring adversary proceeding to avoid transfer under 11 U.S.C. § 548, governing fraudulent conveyance); In re Paolini, 11 B.R. 317, 318–19 (Bankr. W.D.N.Y. 1981) (even when it was undisputed that conveyance was fraudulent, the fraudulent conveyance statute is not "self-operating"; allowing a court to invalidate a lien without the required adversary proceeding would "fly in the face of the most fundamental concept of 'due process," and "deny an alleged fraudulent transferee the opportunity to defend his title"); In re Character Corner, Inc., 2007 WL 4707459, at *3 (Bankr. M.D. Fla. July 30, 2007) (explaining "Trustee may not seek avoidance and recovery of any transfers made to" entities who had not been named in, or served with process in, fraudulent transfer adversary proceedings because these companies "were not afforded due process of law guaranteed by the Fifth and Fourteenth Amendments to the Constitution of the United States").

The Receiver itself acknowledges—as it must—that a full investigation and separate proceeding is required before determining the extent, validity, and priority of Weider's and Forman's interests. Jan. 31, 2017 Receiver's Report 40, ECF No. 365; Receiver's Resp. 26, ECF

No. 353; Jan. 20, 2017 Hr'g Tr. 25:7-13, 26:12-16. Yet the Receiver's proposal to segregate less than the disputed amount prior to a full determination on Weider's and Forman's claims eviscerates these very protections.

## III. Similarly, Allegations Of Insufficient Consideration Do Not Diminish The Amount Of Reserve; They Merely May Establish A "Bona Fide Dispute" As To The Security Interest, Which Is Resolved During A Separate Adversary Proceeding

In its recent report, the Receiver stated that it had "compelling evidence" that Weider and Forman did not loan $6 million of the $10.5 million principal to CarePayment Holdings, which appears to be its basis for asking this Court to reserve less than the amount in dispute. Jan. 31, 2017 Receiver's Report 40, ECF No. 365. The Receiver has not disclosed this "compelling evidence," but presumably it includes the Supplemental Declaration of Bruce Forman filed on January 20, 2017 (re-filed February 15, 2017). See id. (stating that, since its last report, the Receiver "now has compelling evidence, including a declaration filed by Mr. Forman, that Weider/Forman did not in fact loan to CP Holdings LLC $6 million of the $10.5 million"). The Receiver's position that this justifies reserving less than the disputed amount is wrong for at least three reasons.

First, as the Receiver acknowledges, the validity of Weider's and Forman's interests must be litigated later. See supra at 3-5 & nn. 2-3. The adequacy of consideration goes to an agreement's validity. See Cir. City Stores, Inc. v. Najd, 294 F.3d 1104, 1108 (9th Cir. 2002) ("contract defenses, such as lack of consideration …, may invalidate an arbitration agreement").

Second, the Receiver's position is factually incorrect; evidence already on file shows Weider and Forman did loan the "disputed" $6 million (and entire $10.5 million) to CarePayment Holdings. The transactions can be summarized in four steps:

1. Between May 2011 and May 2013, Weider loaned and invested $12 million in Aequitas-related companies. (Specifically: (i) on May 3, 2011, Weider loaned $2 million to Aequitas Commercial Finance, LLC; (ii) on May 25, 2012, Weider invested $2 million in Aequitas CarePayment Fund, LLC; (iii) on January 29, 2013, Weider loaned $5 million to ASFG Leverage 1, LLC (later renamed CSF Leverage I, LLC); and (iv) on May 17, 2013, Weider loaned $3 million in ASFG Leverage 1, LLC (aka CSF Leverage I).)

- The receipts for the $12 million wire transfers are on file. See Supp. Forman Decl. Ex. A, ECF No. 368.

2. Between May 2013 and December 2013, the Aequitas-related companies were in a position to repay the May 3, 2011 loan and the May 25, 2012 investment (total $4 million), but the parties negotiated a new agreement whereby Weider loaned the $4 million to CSF Leverage I on new terms. So, by the end of 2013, CSF Leverage I had a total outstanding loan debt to Weider of $12 million, set to mature by the end of 2014.

   - CSF Leverage I acknowledged this $12 million loan debt in an agreement already on file. See Supp. Forman Decl. Ex. B at 1, ECF No. 368.

3. In 2014, as the $12 million loan debt was coming due, CSF Leverage I re-paid Weider $6 million and the parties negotiated a new agreement whereby Weider agreed to forego repayment of the remaining $6 million in exchange for a new $6 million loan to CarePayment Holdings on new terms.[8]

   - A letter agreement discussing the new $6 million loan to CarePayment Holdings is on file. See Supp. Forman Decl. Ex. B at 3, ECF No. 368.

   - The Weider-CarePayment Holdings loan documents are also on file. See Forman Decl. Exs. E-H, ECF No. 345.

4. In 2015, Weider and Forman loaned CarePayment holdings an additional $4.5 million, for a total, outstanding, principal debt of $10.5 million.

   - The receipt for the $4 million wire transfer is on file. See Supp. Forman Decl. Ex. A, ECF No. 368.

   - The receipt for the $500,000 wire transfer is being filed concurrently with this statement. See Decl. of Bruce Forman, Ex. B.

   - The Weider- and Forman-CarePayment Holdings loan documents are also on file. See Forman Decl. Exs. A-D & I-L, ECF No. 345.

Third, to the extent the Receiver's position is that the $6 million loan was "to" CSF Leverage I and not "to" CarePayment Holdings, this is legally incorrect. The Weider-CarePayment Holdings agreement provides that the $6 million is to be funded from CSF Leverage I's outstanding debt to Weider. See Forman Decl. Ex. E ¶ 3, ECF No. 345 ("The parties

[8] CarePayment Holdings, like CSF Leverage I, was a wholly owned subsidiary of Aequitas Commercial Finance, LLC. This new $6 million loan to CarePayment Holdings was designed to fund purchases of CarePayment® healthcare receivables by CarePayment Holdings and its subsidiaries, and involved new terms with new security and collateral.

acknowledge … that the Advance is to be made through conversion of a portion of the outstanding principal amount of the CSF Leverage I Loan pursuant to a letter agreement dated as of September 30, 2014[.]"). Weider's discharge of CSF Leverage I's debt in exchange for the new CarePayment Holdings note is consideration. See Barclays Bank PLC v. Skulsky Trust, 287 A.D.2d 365, 366 (N.Y. App. Div. 2001) ("Discharge of a pre-existing debt owed by a third party is legal consideration."); Davidson v. Madden, 89 Or. 209, 215–16 (1918) ("The rule is established in Oregon that, where a person, as a full or part consideration for an executed contract, promises another to … discharge some legal debt … due from such other to a third person, the latter, though a stranger to the consideration and not an immediate party to the contract, may maintain an action thereon if the agreement was made directly or primarily for his benefit.").

## IV. The Issues To Be Resolved Can Be Resolved With Limited Discovery And Briefing

The adequate protection hearing envisioned by section 363(f)(4) can be resolved with limited document discovery, briefing, and oral argument. In the context of a "free and clear" sale, the party asserting an interest must prove two things: (1) "that it holds a perfected security interest in post-petition revenues to which its liens still rightly attach;" and (2) "the amount of money to which its liens attach." In re Nov. 2005 Land Inv'rs, LLC, 636 Fed. Appx. 723, 725 (9th Cir. 2016). As detailed above, under section 363(f)(4), the burden then shifts to the receiver to prove that there is a "bona fide dispute" that justifies a "free and clear" sale, subject to adequate protection, pending ultimate resolution of the dispute. In re NJ Affordable Homes Corp., 2006 WL 2128624, at *10 (Bankr. D.N.J. June 29, 2006); In re Terrace Chalet Apartments, Ltd., 159 B.R. 821, 828 (N.D. Ill. 1993); In re Genesys Research Inst., Inc., 2016 WL 3583229, at *13 (Bankr. D. Mass. June 24, 2016); In re Gulf States Steel, Inc. of Ala., 285 B.R. 497, 507 (Bankr. N.D. Ala. 2002); In re Daufuskie Island Props., LLC, 431 B.R. 626, 646

(Bankr. D.S.C. 2010); In re Scimeca Found., Inc., 497 B.R. 753, 773 (Bankr. E.D. Pa. 2013); accord In re Duncan, 406 B.R. 904, 910 (Bankr. D. Mont. 2009).

Here, Weider and Forman already satisfied their burden in their limited objection by demonstrating that: (i) they have an interest in the post-petition revenues—i.e., the sale includes an exclusive option that disposes of some of the collateral for their first-priority, secured loans (Weider & Forman Limited Obj. 5-8, ECF No. 344); (ii) they perfected their security interests (liens) by filing the appropriate UCC-1 financial statements (id. at 8, 19-20); and (iii) the amount of money to which their liens attach was $13,211,460 as of January 18, 2017, but post-petition interest continues to accrue on a monthly basis as part of their priority claim (id. at 26-29).[9]

This did not appear to be controversial, as the Receiver had previously:

- acknowledged that CarePayment Holdings, which owns the collateral companies, is "encumbered by … approximately $10.5 million of secured debt from Weider and Forman," Sept. 14, 2016 Receiver's Report 52, ECF No. 246;
- "[i]n anticipation of" this very sale, "engaged in negotiations with Weider and Forman for a reduced payoff of their secured loans … [and] received strong support" for a proposed settlement, id. at 54; and
- concluded, "[b]ased on the facts [then] known to the Receiver, [that] the Weider/Forman Loans appear to be substantially over-collateralized and validly perfected," id.

It was only in the Receiver's reply brief supporting its motion for sale approval that, for the first time, it raised allegations of a potential fraudulent conveyance to cast doubt on the extent, validity, and priority of Weider's and Forman's interests. Receiver's Resp. 2, 4-6, 13, 23-26, ECF No. 353. The Receiver argued that: (i)Weider's and Forman's collateral does not include the receivables, but instead, is limited to equity interests in the companies that own the receivables (id. at 7-8, 12-13); (ii) Weider and Forman did not actually transmit $6 million of the loan amount (id. at 2, 5-6,

[9] The Receiver acknowledges that post-petition interest continues to accrue. Jan. 20, 2017 Hr'g Tr. 26:4-9 ("Now, the risk for the receiver to take on … is there will be a continued accrual of interest if the Court ultimately determines that [Weider and Forman] have a secured claim, a certain amount of interest, whether that's their 17 percent or 25 percent compounded monthly. The receiver understands that risk[.]").

12-14); and (iii) Weider's and Forman's claim is subject to a bona fide dispute in that a portion of it may be voidable under a theory of fraudulent conveyance (id. at 2, 5-6, 23-26).

While Weider and Forman are surprised by these assertions and unequivocally deny them, they agree that, to the extent the Court is not satisfied by prior briefing and the documents on file, there are three issues that this Court must resolve before ordering adequate protection:

1. Whether Weider and Forman have an interest in proceeds from the sale of CarePayment® healthcare receivables that are part of the sale option;
2. Whether Weider and Forman perfected their security interests; and
3. The amount of Weider's and Forman's security interests.

These questions require only limited document discovery and no depositions or live testimony. The first issue turns on the definition of "collateral" in the loan documents and whether Weider and Forman have an interest in the sale of CarePayment® healthcare receivables; the only discovery required is the parties' exchange of loan documents and correspondence regarding collateral. The second issue turns on the requirements for perfecting a security interest, and whether Weider and Forman satisfied them; the only discovery required is Weider's and Forman's production of documents evidencing as much. The third issue turns on the exchange of monies between the parties and a straightforward calculation of interest; the only discovery required is Weider's and Forman's production of documents evidencing disbursement of loan principal, and the parties' exchange of documents showing CarePayment Holdings' repayment (if any) of principal and interest to date.

These issues have nothing whatsoever to do with the amount of money that must be held in reserve, as—again—courts have explained that the entire disputed amount is reserved until final adjudication. See e.g., In re Clark, 266 B.R. at 171. Any discovery and briefing regarding fraudulent conveyance must await a full adversary proceeding, including a complaint notifying Weider and Forman of the basis for the fraudulent conveyance allegations; a full period for discovery; and possibly a jury trial (see Eberhard v. Marcu, 530 F.3d 122, 136 (2d Cir. 2008)

("'[A] party claiming the right to the possession of the property as against the receiver or any one else is entitled to a jury trial.'")).

**PROPOSED SCHEDULE**

Weider and Forman respectfully propose the following schedule:

| EVENT | DEADLINE/DATE |
|---|---|
| Parties' production of documents identified in Section IV above | 30 days after the date of the Court's order setting a hearing date |
| Weider's and Forman's brief addressing the issues identified in Section IV above | 14 days after the production deadline |
| Receiver's response brief | 14 days after Weider's and Forman's brief |
| Weider's and Forman's reply brief | 7 days after the Receiver's brief |
| Oral argument | 14 days after Weider's and Forman's reply brief, or any time thereafter convenient for the Court |

Once these issues are resolved, Weider and Forman respectfully submit that no hearing is necessary to determine the amount of adequate protection—segregating the full amount of Weider's and Forman's interests is required. As Weider and Forman previously explained, that amount was $13,211,460 as of January 18, 2017, and should include interest at the post-default rate as it accrues. See Weider & Forman Limited Obj. 26-29, ECF No. 344.

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