United States Bankruptcy Court
Northern District of Illinois
Eastern Division

<u>Transmittal Sheet for Opinions</u>

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Bankruptcy Caption: Mack Industries, LTD

Bankruptcy No.: 17 B 09308

Adversary Caption: Ronald R. Peterson, as Chapter 7 Trustee for Mack v. Colony American Finance Lender LLC et al.

Adversary No.: 19 A 00576

Date of Issuance: **March 31, 2021**

Judge: **Carol A. Doyle**

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United States Bankruptcy Court, Northern District of Illinois

Name of Assigned Judge	**Carol A. Doyle**	**Case No.**	17 B 09308
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DOCKET ENTRY TEXT

The Defendants' Motion to Dismiss is granted. All claims are dismissed except the claim in Count 1 to avoid fraudulent transfers based on constructive fraud against Mack LOC I LLC.

[For further details see text below.]

STATEMENT

Ronald Peterson filed this adversary proceeding as the chapter 7 trustee of three debtors: Mack Industries II LLC, Mack Industries V LLC, and Mack Industries VI LLC (collectively "the Debtors"). They are all related to the principal debtor in this group of cases - Mack Industries, LLC ("Mack"). The trustee sues three defendants: Colony American Finance Lender LLC ("Colony"), CAF REO-1 LLC ("CAF"), and Mack LOC I LLC ("LOC I"). He seeks to avoid transfers of real property from the Debtors to LOC I as fraudulent based on constructive fraud and actual fraud. He also seeks to pierce the corporate veils of CAF and LOC I to recover the value of the transfers from Colony.

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The defendants moved to dismiss, arguing that the trustee cannot recover the value of any alleged fraudulent transfer from Colony under § 550(a)(1) of the Bankruptcy Code and that the trustee failed to allege fraud with particularity because the scheme to defraud he alleges is not connected to the transfers. The defendants also contend that the trustee failed to allege facts to support his veil piercing claims against LOC I and CAF. The defendants are correct. The motion to dismiss will be granted.

1. Background

The trustee filed approximately 400 adversary complaints seeking to avoid transfers that were allegedly fraudulent or preferential. In almost all of those cases, he sued as trustee of two chapter 7 debtors: Mack and Oak Park Avenue Realty, Ltd. ("Oak Park"). He alleged that transfers were fraudulent because Mack was trying to deplete its assets to prevent one of its creditors from collecting from it.

According to all of the complaints, Mack had a contract to manage hundreds of properties owned by American Residential Leasing Company LLC. Mack was required to lease the properties, maintain them, pay the property taxes, and pay certain rental and other fees to American Residential. In mid-2014, Mack tried to renegotiate the contract with American Residential. During negotiations, a Mack vice president allegedly threatened that Mack would deplete its assets so American Residential could not collect if it refused to renegotiate. The trustee contends that Mack carried out this plan by using its assets for the benefit of other entities. He seeks to recover from many parties who purchased property from Mack or a related entity and then hired Oak Park to manage the properties, including collecting rent from tenants. Mack often paid those parties even though Oak Park owed them the money. The trustee is also attempting to recover from parties who provided goods and services to Mack that Mack used to improve properties owned by other entities. Thus, in most of his adversary proceedings, the trustee is trying to recover payments made by Mack to parties it did not owe or who improved property owned by others.

This case is different. It does not involve payments or transfers made by Mack. Here, the trustee is suing an entity (Colony) that loaned money to a Mack-related entity - LOC I - secured by mortgages on properties owned by LOC I. The trustee alleges that one way that the McClellands, who owned the various Mack entities, carried out their scheme to defraud American Residential was by organizing LOC I in November 2015. Amended Complaint ¶ 65. LOC I was owned by LOC III, which was owned by James K. McClelland. Am. Compl. ¶ 67. The McClellands caused the transfer of 169 parcels of real property from the Debtors to LOC I to add "a further barrier to prevent American Residential from collecting its debt." Am. Compl. ¶ 68. In December 2015, LOC I entered into a revolving loan agreement with Colony for up to $15 million. The total loan amount was later raised to $30 million. Am. Compl. ¶ 69. The purpose of the loan was to allow LOC I to acquire and renovate real estate. Am. Compl. ¶ 70. Under the terms of the loan, Colony would advance the lesser of 75% of the value of each parcel of real estate LOC I acquired, or 85% of the cost of the property and its expected renovation. Am. Compl. ¶ 70. Colony's loan to LOC I was secured by the real estate that LOC I acquired. Am. Compl. ¶ 71. To further secure Colony's loan to LOC I, LOC III pledged its membership interests in LOC I to Colony. Am. Compl. ¶ 72.

In 2015, the Debtors owned many parcels of real estate in the Chicago area. Am. Compl. ¶ 73. Between April and October 2016, each of the Debtors transferred multiple parcels of property to LOC I (totaling 169 properties).[1] The trustee defines these transfers of real property from the Debtors to LOC I as the "Transfers" he seeks to avoid and recover. Am. Compl. ¶ 74. By transferring the properties, the Debtors transferred the equity in those properties to LOC I. Am. Compl. ¶ 75. There were valid mortgages on various properties but "the Debtors had an average of 30% equity in the properties they transferred to LOC I." Am. Compl. ¶ 76. Some mortgages asserted against properties were not valid because a Mack entity other than the one that owned the property at the time purported to grant the mortgages. Am. Compl. ¶ 77. The properties transferred by the Debtors to LOC I became collateral for the Colony loan. Am. Compl. ¶ 78.

The Transfers were grouped into eight transactions or draws. Each draw had a closing where all the steps of the transaction occurred as simultaneously as possible. Am. Compl. ¶ 79. For each draw, the Debtors would transfer a group of properties to LOC I, Colony would advance a portion of the total available loan amount, prior mortgages on the properties were paid and released, and Colony would obtain mortgages on the properties transferred. Am. Compl. ¶ 79. The Debtors transferred approximately $12.2 million in equity in the properties to LOC I to secure the Colony loan. Am. Compl. ¶ 89. This estimate of equity is based on "the values that Colony assigned to each property at the time of the draw after obtaining a professional valuation," with three exceptions. Am. Compl. ¶ 90. By January 2017, LOC I had defaulted on the loan and Colony declared a default. Am. Compl. ¶ 91.

Colony then "took steps to liquidate its collateral as quickly as possible and to attempt to insulate itself from future potential liability." Am. Compl. ¶ 92. Colony held a UCC sale of LOC III's membership interests in LOC I. At the UCC sale, Colony credit bid a portion of the outstanding balance on its loan and acquired the membership interests in LOC III. Am. Compl. ¶ 93. At the conclusion of the sale, Colony caused the membership interests to be transferred to CAF, "its designee and wholly owned special purpose entity/subsidiary." "Colony (through CAF) became the holder of 100% of the membership interests" of LOC I, "and it assumed control of management of LOC I and its properties." Am. Compl. ¶ 95. Colony then caused LOC I to sell the real estate "quickly and below market value, and to use the proceeds to pay

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[1]Other entities transferred an additional 9 properties to LOC 1. Am. Compl. ¶ 74.

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Colony's debt." Am. Compl. ¶ 96. Colony caused LOC I to sell 136 properties for a total of approximately $12.8 million. Am. Compl. ¶ 98. Just "months earlier," Colony had valued these 136 properties at approximately $24.7 million. Colony then "caused LOC I's status with the Secretary of State to be changed to 'revoked' as of May 11, 2018." Am. Compl. ¶ 99.

Colony was aware of the Debtors' and Mack's bankruptcies and filed a proof of claim in the Mack bankruptcy case seeking $6.9 million for conversion, misappropriation, fraud, aiding and abetting fraud, conspiracy to defraud, tortious interference of contract, fraudulent transfer, and/or unjust enrichment. Am. Compl. ¶ 100. There is "no evidence" that Colony made any attempt to ascertain LOC I's general financial condition "or to pay or even give notice to LOC I's other creditors, including the Debtors." Am. Compl. ¶ 101. In various court filings, "Colony admitted that it was the party in control of LOC I, that it caused LOC I to sell its real estate, and that it applied the net proceeds of the property sales to its debt." Am. Compl. ¶ 102. Creditors existed with standing to bring an action against the Debtors to avoid the transfers described in the complaint under applicable non-bankruptcy law, including American Residential. Am. Compl. ¶ 103.

The trustee asserts claims against Colony and LOC I in Count 1 to avoid the transfers of real property from the Debtors to LOC I as fraudulent based on constructive fraud under 11 U.S.C. §§ 544(b)(1), 548(a)(1)(B), and 550(a) and 740 ILCS 160/5(a)(2), 6(a) and 8(a). In Count 2, he seeks to avoid the transfers as fraudulent based on actual fraud under 11 U.S.C. §§ 544(b)(1), 548(a)(1)(A) and 550(a) and 740 ILCS 160/5(a)(1) and 8(a). In Count 3, the trustee seeks to pierce the corporate veils of LOC I and CAF to hold Colony liable for the allegedly fraudulent transfers made by the Debtors to LOC I.

The defendants move to dismiss on a number of grounds, including: (1) the trustee has failed to state a claim in Counts 1 and 2 that he can recover against Colony under § 550(a)(1) of the Bankruptcy Code because Colony was neither the initial transferee nor a party for whose benefit the transfers were made; (2) the trustee failed to allege an actual fraud claim in Count 2 with particularity, and specifically the trustee failed to connect the fraudulent scheme he alleged to the transfers he seeks to avoid; and (3) the trustee failed to allege facts to support his claims to pierce the corporate veils of LOC I and CAF. The defendants are correct on each of these arguments.

2. <u>Claim under Section 550(a)(1)</u>

The trustee brings the fraudulent transfer claims in Counts 1 and 2 to avoid the transfers from the Debtors to LOC I and recover the value of the transfers from both Colony and LOC I. Colony argues that the trustee fails to state a claim that he can recover against it under § 550(a)(1) of the Bankruptcy Code, 11 U.S.C. § 550(a)(1). Section 550(a)(1) allows the trustee to bring into the bankruptcy estate the value of property transferred when the transfer is avoided under various Code provisions including §§ 548 and 544, the two provisions under which the trustee seeks to avoid the transfers in this case. The trustee must fit his claims within one of the categories in § 550(a) or there is no point in "avoiding" the transfers under §§ 544(b) or 548(a) because they could not be recovered into the bankruptcy estate. *See Lassman v. Patts (In re Patts)*, 470 B.R. 234, 242 (Bankr. D. Mass. 2012) ("A successful avoidance under § 544 will nullify a transfer, but it will not give a trustee control over the asset."); *see also Southmark Corp. v. Schulte, Roth & Zabel, L.L.P.*, 242 B.R. 330, 337 (N.D. Tex. 1999) (§ 550 provides an avenue of recovery for the trustee who prevails under an avoidance section of the Code); *Santee v. Northwest Nat'l Bank (In re Mako, Inc.)*, 127 B.R. 471, 473 (Bankr. E.D. Okl.1991) (same); *Hassett v. Zimmerman* (*In re O.P.M. Leasing Services, Inc.)*, 32 B.R. 199, 202 (Bankr. S.D.N.Y. 1983) (same).

Section 550(a) provides:

> (a) [T]o the extent that a transfer is avoided under section 544, . . . 548, . . . of this title, the trustee may recover, for the benefit of the estate, the property transferred . . . from -
> (1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or
> (2) any immediate or mediate transferee of such initial transferee.

11 U.S.C. § 550(a)(1).

Section 550(b) then provides defenses for transferees as follows:

> (b) The trustee may not recover under section (a)(2) of this section from –
> (1) a transferee that takes for value, including satisfaction or securing of a present or antecedent debt, in good faith, and without knowledge of the voidability of the transfer avoided; or
> (2) any immediate or mediate good faith transferee of such transferee.

11 U.S.C. § 550(b)(2).

Colony argues that it does not fall within either category in § 550(a)(1). It was not the initial transferee of the transfers or an "entity for whose benefit" the transfers were made. Colony is correct.

The trustee seeks to avoid the transfers of the property from the Debtors to LOC I but he seeks to recover the value of the transfers from Colony. Colony contends that the amended complaint alleges that LOC I received title to the properties from the Debtors so LOC I, not

Colony, is the initial transferee for purposes of § 550(a)(1). As the Seventh Circuit explained in *Bonded Fin. Serv., Inc. v. European Am. Bank*, 838 F.2d 890, 893 (7th Cir. 1988), a "transferee" for purposes of § 550(a)(1) is the first entity that has "dominion over the money or other asset, the right to put the money to one's own purposes." *See also CLC Creditors' Grantor Trust v. Howard Savings Bank (In re Commercial Loan Corp.)*, 396 B.R. 730, 742 (Bankr. N.D. Ill. 2008) (the initial transferee is the first entity to have dominion over the asset); *Peterson v. Hofmann (In re Delta Phones, Inc.)*, No. 05-ap-1205, 2005 WL 3542667, at *3 (Bankr. N.D. Ill. Dec. 23, 2005) (same). Here, there is no doubt that the first entity to have dominion over the real property was LOC I. Until it obtained title to the properties, it could not convey any interest in the properties to Colony or anyone else.

The trustee seeks to avoid this obvious conclusion and deem Colony the initial transferee by alleging that the different components of the loan transactions were conducted "as simultaneously as possible." Am. Compl. ¶ 79. He alleges that for each group of properties or "draw," "the Debtors transferred properties to LOC I, Colony would advance a portion of the total available loan amount, prior mortgages on the properties were paid and released, and Colony would obtain mortgages on the properties transferred." Am. Compl. ¶ 79. This argument is unavailing. The transfers the trustee seeks to avoid are of real property from the Debtors to LOC I. As the trustee alleges, the first step of the loan process was to transfer title from the Debtors to LOC I. Only after LOC I held title could it then convey an interest in the properties to Colony by granting a mortgage on each property for which funds were advanced.[2] There is no question that LOC I was the initial transferee of the real property and Colony was an immediate transferee - not of title to the properties but of an interest in the properties in the form of a lien. After LOC I received title and funds from Colony, it granted Colony a lien - an interest in the property - in the amount of the loan funds advanced for each specific property. Under the allegations of the amended complaint, Colony never held title to the properties so it was not a transferee of any sort of title to the properties. Instead, the ownership interests in LOC I were eventually transferred to CAF, which caused the sale of the properties directly from LOC I to various buyers to pay down the secured debt. Colony was not the initial transferee of the transfers under § 550(a)(1); LOC I was.

Colony next argues that it is not an "entity for whose benefit such transfer was made" under § 550(a)(1). Colony is correct on this point as well. As explained in *Bonded Financial*, "a subsequent transferee cannot be the 'entity for whose benefit' the initial transfer was made." 838

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[2]The trustee recognizes this by alleging that some of the original mortgages on properties transferred by the Debtors to LOC I were not valid because they were not granted by the entity that owned the property at the time. Am. Compl. ¶ 77. Thus, LOC I could not grant a valid mortgage to Colony on any property until after it held title to the property.

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F.2d at 895. The statute "separates initial transferees and beneficiaries, on the one hand, from 'immediate or mediate transferee[s]' on the other." *Id*. The court further explained that the "paradigm 'entity for whose benefit such transfer was made' is a guarantor or debtor - someone who receives the benefit but not the money." *Id*. *See also Bodenstein v. Univ. of Northern Iowa (In re Peregrine Fin. Group, Inc.*), 589 B.R. 360, 380-81 (Bankr. N.D. Ill. 2018) (holding that the "entity for whose benefit the transfer was made" refers to "entities that benefit as guarantors of the debtor, or otherwise, without ever holding the funds."). A subsequent transferee can never be that entity.

Here, Colony argues that it was the subsequent transferee of an interest in the properties transferred in the form of a lien. It contends that it therefore cannot be the entity for whose benefit the transfers were made under *Bonded Financial*. The trustee attempts to argue around this binding precedent, citing *Senior Transeastern Lenders v. Official Committee of Unsecured Creditors (In re TOUSA Inc.)*, 680 F.3d 1298 (11th Cir. 2012). *Bonded Financial* is binding no matter what *TOUSA* holds but the decision is easily distinguished in any event. It involved a complex situation in which pre-petition lenders obtained payment in a settlement with a parent that was funded through loans that were secured by liens on the assets of subsidiaries who owed no money to the pre-petition lenders who received the loan proceeds. The court affirmed the bankruptcy court's determination that the liens were granted for the benefit of the pre-petition lenders. Here, there is no similar web of relationships and no liens were given by entities that received nothing in return. Colony entered into the loan agreements with LOC I and exchanged loan funds for the liens conveyed to it by the initial transferee - LOC I - to secure the loans. This is a simple arrangement that fits squarely within the dictates of *Bonded Financial*. Colony is not an entity for whose benefit the transfers of property from the Debtors to LOC I were made. It therefore is not a party from whom the trustee can recover under § 550(a)(1) the value of any transfers avoided in Counts 1 and 2.

The trustee also contends that, even if the court determines that Colony does not fall within § 550(a)(1), his claims to recover the transfers from Colony should not be dismissed. He argues that whether Colony is an initial transferee or other type of transferee does not affect the validity of his claim, it only changes the defenses available to Colony. This is not correct. The trustee seeks to avoid the transfers and make Colony pay for them without ever articulating a basis for recovery beyond § 550(a)(1), which does not apply to Colony. The trustee has not alleged any other basis for holding Colony liable for the transfers he seeks to avoid - the transfer of title from the Debtors to LOC I.

The trustee states in a footnote in his response that Colony is a transferee of an interest in the properties transferred because it received a lien on each property after it loaned funds to LOC I. Trustee Response p. 5, n. 2. He is correct that the transfer of a lien qualifies as a "transfer" for purposes of fraudulent transfers law. 11 U.S.C. § 101(54) (defining "transfer" to include "the creation of a lien"). Colony acknowledges as much. But the trustee failed to allege a claim to avoid the transfers of the liens to Colony. The transfers of the liens from LOC I to Colony were separate from the transfers of title from the Debtors to LOC I. The trustee has alleged no facts that would support avoiding the transfers of the liens from LOC I to Colony as fraudulent based on constructive fraud or actual fraud. The court assumes that the trustee did not seek to avoid the transfers of the liens because his allegations establish that Colony gave dollar-for-dollar value for the liens; it received a lien only in the amount of funds it gave Colony for each property. Thus, it is hard to conceive of a viable basis for avoiding the transfers of the liens as fraudulent based on constructive or actual fraud.[3] In any event, the trustee has not alleged any factual basis for avoiding the transfer of the liens as fraudulent in Count 1 or Count 2.

The amended complaint does not allege any basis for recovering the transfers of property from the Debtors to LOC I from Colony under § 550(a). The trustee has therefore failed to state a claim for recovering against Colony in Counts 1 and 2.

The defendants have not moved to dismiss Counts 1 and 2 against LOC I on the basis that the trustee failed to state a claim for recovery of any transfers avoided under § 550(a)(1). They concede that LOC I was the initial transferee under § 550(a)(1) of the transfers the trustee seeks to avoid - the transfer of title from the Debtors to LOC I.

3. <u>Actual Fraud Claim - Failure to State Claim with Particularity</u>

The defendants also seek to dismiss Count 2 on the basis that the trustee failed to state a claim for actual fraud with the particularity required by Rule 9(b). As with Count 1, the trustee

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[3]The trustee alleges that Colony received a lien on each property for the funds it advanced for the property. This establishes that LOC I received value as a matter of law under the definition of "value" in § 548(d)(2)(A), which provides: "(A) "value" means property, or satisfaction or securing of a present or antecedent debt of the debtor . . . ." 11 U.S.C. § 548(d)(2)(A). Here, under the trustee's allegations, the liens were given to secure the antecedent debt created under the loan agreement after the funds were provided. This exchange of funds for a lien on a dollar-for-dollar basis is "value," and indeed reasonably equivalent value, as a matter of law. *See, e.g., Peterson v. Citibank N.A. (In re Mack Industries, Ltd.)*, No. 19-ap-562, ECF No. 58 (Bankr. N.D. Ill. Dec. 15, 2020); *Peterson v. Capital One N.A. (In re Mack Industries, Ltd.)*, No. 19-ap-372, 2020 WL 6708874, at *3-4 (Bankr. N.D. Ill. Nov. 16, 2020). The trustee therefore has no viable claim based on constructive fraud against Colony for the transfer of liens by LOC I to Colony. A claim to avoid the transfer of the liens based on actual fraud would fail the same reason. A dollar-for-dollar exchange of money loaned for a lien on collateral in an arms-length transaction could not support a claim to avoid the transfer based on actual fraud.

brings this claim against two defendants: LOC I and Colony. The gist of the defendants' argument is that even if the trustee stated a plausible basis for actual fraud regarding Mack's alleged scheme to defraud its creditor, American Residential, he has failed to connect any such scheme to the transfers in this case from the Debtors to LOC I. The defendants are correct.

A. Standards for Actual Fraud Claim

To prevail on a fraudulent transfer claim based on actual fraud, a party must prove that an interest of the debtor in property was transferred by the debtor with actual intent to hinder, delay, or defraud a creditor. 11 U.S.C. § 548(a)(1)(A); *Geltzer v. Barish (In re Starr)*, 502 B.R. 760, 766 (Bankr. S.D.N.Y. 2013); *Brandt v. KLC Financial, Inc. (In re Equipment Acquisition Resources, Inc.)*, 481 B.R. 422, 427 (Bankr. N.D. Ill. 2012).[4] To plead the claim with the particularity required by Rule 9(b) of the Federal Rules of Civil Procedure, a party must specifically identify the transfers, including the property conveyed, the date of the transfers, and any consideration paid for the transfer, and plead facts that show actual intent to defraud. *Starr*, 502 B.R. at 769; 11 U.S.C. § 548(a)(1)(A). The plaintiff must plead the requisite intent with respect to each transfer and must connect the allegations against the defendants to the scheme to defraud creditors. *Equipment Acquisition Resources*, 481 B.R. at 431-32.

Actual intent to defraud can be proved by circumstantial evidence, often referred to as badges of fraud. *See, e.g., Equipment Acquisition Resources*, 481 B.R. at 430-31. As explained in *Frierdich v Mottaz*, "[d]irect proof of actual intent to defraud is not required—indeed, it would be hard to come by—and a trustee can prove actual intent by circumstantial evidence." 294 F.3d 864, 869-70 (7th Cir. 2002). These "badges" include: whether the debtor retained possession or control of the property after the transfer, whether the transferee shared a familial or other close relationship with the debtor, whether the debtor received consideration for the transfer, whether the transfer was disclosed or concealed, whether the debtor made the transfer before or after being threatened with suit by creditors, whether the transfer involved substantially all of the debtor's assets, whether the debtor absconded, and whether the debtor was or became solvent at the time of the transfer. *Id.* A single badge of fraud is insufficient to establish intent but the presence of several may create a presumption that the debtor acted with the requisite intent to defraud. *Id.*

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[4]The elements of an actual fraud claim under the Illinois Uniform Fraudulent Transfer Act are the same as those under § 548(a)(1)(A). 740 ILCS 160/5; *Equipment Acquisition Resources*, 481 B.R. at 427, n.2.

B. No Factual Connection Between Scheme Alleged and Transfers

The trustee has made virtually identical allegations to support his actual fraud claim in all of the amended complaints in the hundreds of adversary proceedings he filed. The short version is that American Residential entered into a contract with Mack in December 2012. The contract required Mack to lease hundreds of properties owned by American Residential, to maintain and pay the taxes on the properties, and to pay American Residential under the formula provided in the contract. The parties amended the contract many times to add new properties for Mack to manage, with the last amendment made in January 2014. In the middle of 2014, Mack tried to renegotiate the terms of the contract. In June 2014, when American Residential was resisting Mack's efforts, a Mack vice president allegedly threatened a vice president of American Residential that if it did not agree to change the contract terms, Mack would deplete its assets so American Residential could not collect on the debt. Mack began to prepare for this before June 2014 by paying contractors for work on properties it did not own, buying supplies to improve properties it did not own, and paying money owed by related Mack entities. "The McClelland family" also began having entities other than Mack acquire properties to renovate and sell. Mack drew down on its own assets to benefit the other related entities. This effort "continued from 2013 to March 2017," when Mack filed for bankruptcy.

This court has held in many other adversary proceedings filed by the trustee that, despite the obvious weaknesses and contradictions in the trustee's allegations, the trustee pleaded just enough to state a claim for actual fraud for at least some of the alleged transfers made by Mack in those cases. Many of the defendants were individuals who purchased properties from Mack or related entities and had Oak Park manage the properties. Oak Park collected the rent but these defendants were paid by Mack. Other defendants provided goods or services that Mack contracted for and paid for but used in properties owned by other entities. In each case, Mack allegedly carried out the scheme by paying the contractual obligations of Oak Park or by contracting for goods and services that allegedly benefitted properties owned by others. Thus, there was some factual link between the alleged scheme to defraud and the payments made by Mack that the trustee sought to avoid.

Here, there is no such link. The trustee does not allege that Mack's assets were used in connection with the properties transferred from the Debtors to LOC I. He never alleges that Mack's funds were used to purchase the properties or any other connection between Mack's assets and the Debtors or the properties transferred. He says nothing about how the properties were acquired. Instead, the amended complaint alleges that the Debtors purchased the properties, many (if not all) with financing provided by other lenders, and then transferred the properties to LOC I. Colony then provided new financing for the properties, the funds it loaned were used to pay off all mortgages granted by the Debtors to previous lenders, and then Colony received a first priority lien on each property in the amount of the funds loaned for the property. There is no factual connection between the fraudulent scheme alleged in the amended complaint, which involved Mack depleting its assets to defraud American Residential, and the transfers the trustee seeks to avoid in this case.

The trustee implicitly acknowledges that he has not alleged facts connecting the properties transferred to assets of Mack. He contends that this does not matter, stating "the provenance of these specific properties, however, does not affect whether American Residential was a creditor or whether the Debtors transferred them to LOC I with actual intent to hinder, delay or defraud American Residential." Trustee Response, p. 9. This is not correct. The scheme to defraud that he alleged was all about Mack depleting *its* assets to prevent American Residential from collecting from them. Without facts connecting Mack's assets to the properties transferred, there is no plausible claim that the alleged scheme to defraud American Residential by depleting Mack's assets had anything to do with the transfers of properties from the Debtors to LOC I.

In fact, contrary to the trustee's assertion, American Residential is not a creditor of the Debtors so Mack's scheme to defraud American Residential cannot provide a viable basis for avoiding the transfers here. As discussed above, to state a claim for fraudulent transfer, the trustee must allege facts showing that the Debtors transferred assets with actual intent to defraud *a creditor of the Debtors*. Under § 544(b), the trustee must demonstrate that there was a "predicate creditor" that (1) existed at the time the transfers were made, (2) still had a viable claim against the debtor when the bankruptcy case was filed, and (3) could have pursued a claim for fraudulent transfer by the debtor at the time the bankruptcy case was filed. As explained in *Kelley v. Opportunity Finance, LLC (In re Petters Co., Inc.),* 550 B.R. 438, 454 (Bankr. D. Minn. 2016), a trustee can only avoid a transfer if there was a predicate creditor with "a claim against the transferor that was enforceable under nonbankruptcy law and that gave the creditor standing to sue the transferee then under the law of fraudulent transfer." *See also Acequia, Inc. v. Clinton (In re Acequia, Inc.)*, 34 F.3d 800, 807 (9th Cir. 1994) (a claim under § 544(b) "depends upon whether . . . a creditor existing at the time the transfers were made . . . still had a viable claim against [the] debtor at the time the bankruptcy was filed."); *Karnes v. McDowell (In re McDowell)*, 87 B.R. 554, 558 (Bankr. S.D. Ill. 1988) (trustee could not establish the required predicate creditor because there were no creditors whose claims were not barred by the statute of limitations before the bankruptcy was filed). Here, the allegations of the amended complaint make it clear that American Residential was not a direct creditor of the Debtors. It had a contract only with Mack. If it obtained a judgment against Mack, it could pursue fraudulent transfers made by Mack to other entities but there are no allegations that Mack transferred assets to the Debtors. Thus, American Residential - the entity against whom the fraudulent scheme was allegedly perpetrated - was not a creditor of any of the Debtors when the transfers occurred or any other time.

The trustee tries to gloss over this issue through a number of allegations, none of which transforms American Residential into a creditor of the Debtors. First, he alleges that the Debtors were the subjects of discovery in American Residential's lawsuit against Mack, suggesting that this makes American Residential a creditor of the Debtors. It does not. Seeking discovery from a non-party does not create a debtor-creditor relationship between the party and the non-party.

Second, the trustee alleges that American Residential "pointed out" in its complaint against Mack and other "filings" that Mack transferred millions of dollars to its affiliates and argued that Mack made these transfers as part of its scheme to stop American Residential from collecting from Mack. Am. Compl. ¶ 64. These alleged "assertions" by American Residential in other litigation do not make it a creditor of the Debtors. The trustee has not alleged that American Residential identified any of the Debtors as a recipient of assets from Mack or that American Residential sued the Debtors for fraudulent transfers. More importantly, the trustee has not alleged any factual basis for American Residential to bring such a claim against the Debtors. The trustee has filed amended complaints in a large number of adversary proceedings in which he provided very detailed information about each transfer made by Mack to the various defendants he sued. Despite having access to Mack's detailed books and records, here he has not alleged that any assets were transferred from Mack to the Debtors. Without a transfer of assets from Mack to the Debtors, American Residential had no basis for pursuing any assets of the Debtors as fraudulent transfers.

Third, the trustee argues that American Residential "made it clear that it intended to pursue the Debtors to recover assets Mack had dissipated." Trustee Response, p. 10. American Residential's alleged "intent" is irrelevant. The trustee must show that there is a factual and legal basis for a claim by American Residential against the Debtors for an alleged fraudulent transfer from Mack to the Debtors, and then from the Debtors to LOC I.[5]

The trustee goes so far as to say the court is *required* to infer that American Residential was a creditor of the Debtors without any facts or a single citation to authority to support this contention. This is not correct. The court need not accept the bald assertion that American Residential was a creditor of the Debtors when it is clear from the trustee's allegations that American Residential had no contractual relationship with the Debtors and the trustee has failed

[5]The trustee also states that "the Debtors also had other mortgage creditors at the time," but he never explains why this matters. Trustee's Response, p 7. This unexplained and unsupported assertion makes no difference here for at least two reasons. First, under the allegations of the complaint, those lenders were paid in full from the funds advanced by Colony so they had no claim against the Debtors or LOC I on the petition date that the trustee could assert. Second, the trustee has not alleged any facts regarding any scheme to defraud the mortgage creditors (presumably for obvious reasons - they were paid in full so could hardly be asserting that anything fraudulent happened) or any other actual unsecured creditor of the Debtors.

to allege any factual basis for American Residential pursuing a fraudulent transfer claim against them.[6]

All of the trustee's allegations regarding his actual fraud claim are based on Mack's alleged scheme to defraud American Residential. Those allegations are not sufficient to allege with particularity a plausible claim based on actual fraud to avoid the transfers in this case.

C. "Diverting" New Real Estate Purchases to Entities Other Than Mack

It is also important to note that one aspect of the trustee's allegations - that part of the scheme to defraud America Residential included the McClellands causing new properties to be purchased by entities other than Mack - does not support his claim based on actual fraud. He alleges that the McClellands created new entities to buy properties, renovate and sell them, businesses that Mack "would have pursued in the past." Am. Compl. ¶ 43. The Debtors were some of those new entities. He alleges that prior to 2013, "[t]he McClellands ran almost the entire real estate business in Mack's name." Am. Compl. ¶ 37. He then alleges that in 2013, Mack began to create new entities "to divert business opportunities and assets from Mack to those entities." Am. Compl. ¶ 38. "By acquiring real estate and other assets in the name of the new entities and transferring real estate from Mack to the new entities, the McClelland family reduced the assets that Mack had that could be collected by American Residential." Am. Compl. ¶ 46.[7]

These allegations about Mack creating new entities, including the Debtors, to undertake new business that it might have undertaken itself prior to 2013 do not show fraudulent intent for a number of reasons. First, as Colony points out, the timing of the creation of the entities is not consistent with the trustee's assertion of fraudulent intent. The amended complaint alleges that the McClellands created at least 15 new entities in 2013 - the first year of the agreement with American Residential and before any fraudulent intent could reasonably be inferred. Am. Compl. ¶ 38. The trustee also specifically alleges that Mack II was created in February 2013, just two months after Mack entered into the first version of the agreement with American Residential.

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[6]The defendants contend that American Residential did not file a claim in the bankruptcy cases of any of the Debtors and the schedules filed by the trustee do not list American Residential as a creditor of the Debtors. The court could probably take judicial notice of these facts but will not do so because the issue was raised for the first time in reply and the analysis above is sufficient to conclude that American Residential was not a creditor of the Debtors at the time of the transfers or when the Debtors' bankruptcy cases were filed.

[7]Significantly, this allegation does *not* state that Mack transferred any real estate *to the Debtors*.

He alleges that Mack V was created in November 2013 and Mack VI was created in April 2014, two months before the alleged threat to American Residential in June 2014. Am. Compl. ¶ 40. The trustee also alleges that "[b]etween December 2012 and January 2014, Mack and American Residential amended their Agreement 20 times to add additional properties." Am. Compl. ¶ 16. It is not reasonable to infer that Mack II or Mack V were created as part of a scheme to defraud American Residential during the first year of the contract when Mack and American Residential were busy adding properties to the contract and there are no allegations of any problems Mack was having with the terms of the contract at that time. It is also a stretch, and therefore not reasonable, to infer that Mack VI, created in April 2014, three months after the last amendment of the contract, was created with intent to defraud anyone, particularly when there are no allegations of any transfers from Mack to Mack VI (or the other two Debtors).

The trustee insists that the court *must* infer that the creation of these entities and their acquisition of properties is fraudulent because he alleged that even before making the threat to American Residential in June 2014, Mack began preparing for a possible breakdown in the business relationship. He alleges: "In the months leading up to and during the negotiations with American Residential, Mack had already began dissipating its assets" and it continued that dissipation when the negotiations failed. Am. Compl. ¶ ¶ 35, 36. Nothing in these general allegations about Mack preparing for difficulties with American Residential compels the inference that the creation of entities at the beginning of the relationship with American Residential and Mack reflected Mack's or the McClellands' fraudulent intent. The trustee does not contest the defendants' assertion that holding different real properties in separate legal entities is "quite customary," nor could he. This practice could more accurately described as commonplace, widespread, or routine.[8] It cannot reasonably be interpreted as suspicious or in any way fraudulent without specific facts justifying such an inference. Merely alleging that the McClellands began preparing for a breakdown in relations with American Residential before the June 2014 threat does not justify the inference of fraudulent intent from such a pervasive and innocuous practice.

Second, and more importantly, there is a fundamental flaw with the premise of the trustee's contention that the alleged "diversion of business opportunities" was part of a scheme to defraud. The trustee's argument assumes that American Residential was entitled to have Mack acquire new properties that it would improve and sell for profits from which American

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[8]The practice of placing different real estate parcels in different corporate entities is so prevalent that the Bankruptcy Code contains various provisions that apply only to cases involving "single asset real estate," which is defined as "property constituting a single property or project, other than residential real property with fewer than four residential units, which generates substantially all of the gross income of a debtor . . . ." 11 U.S.C. § 101(51B). This court has presided over innumerable single asset real estate cases.

Residential could collect for the breach of its contract. The trustee provides no support for his premise that Mack or the McClellands owed American Residential (or any other creditor) a duty to undertake new investment ventures through Mack and that their failure to do so is somehow fraudulent. The court is unaware of any basis for concluding that an entity owes its contracting partner an obligation to invest in new business opportunities so the partner has a better chance of collecting on a debt owed. The McClellands could not deplete Mack's assets to prevent American Residential from collecting but they were under no obligation to purchase new real estate through Mack. No fraudulent intent can reasonably be inferred from their use of separate entities to hold new parcels of real estate (so long as they did not use Mack's assets to purchase the new parcels, which is not alleged here).

Thus, the alleged "diversion" of business accomplished through entities other than Mack purchasing new parcels of property to improve and sell does not support the trustee's claim that the transfers from the Debtors to LOC I were part of a scheme to defraud American Residential or anyone else.

For all of these reasons, the trustee has failed to allege facts with sufficient particularity to state a plausible claim in Count 2 to avoid the transfers from the Debtors to LOC I based on actual fraud.

4. Count 3 - Piercing the Corporate Veil

The defendants argue that Count 3 should be dismissed because it fails to allege facts that would justify piercing *two* corporate veils - of LOC I and CAF - to collect from Colony. The court agrees.

The law of the state of incorporation applies to claims to pierce the corporate veil. *Gierum v. Glick (In re Glick)*, 568 B.R. 634, 660 (Bankr. N.D. Ill. 2017). The defendants are all Delaware limited liability companies. The parties agree that Delaware law applies to this issue.

"Under Delaware law, courts 'will disregard the corporate form only in the exceptional case.'" *Eagle Air Transport, Inc. v. National Aerotech Aviation Delaware, Inc.*, 75 F. Supp. 3d 883, 896 (N.D. Ill. 2014) (quoting *Winner Acceptance Corp. v. Return on Capital Corp.*, Civil No. 3088, 2008 WL 5352063, at *5 (Del. Ch. Dec. 23, 2008) (unpublished)). To state a veil-piercing claim, the plaintiff must plead facts supporting an inference that the corporation, through its alter-ego, is a sham entity and exists for *no purpose other than to defraud* investors and creditors. *Id.* (citing *Crosse v. BCBSD, Inc.*, 836 A.2d 492, 496 (Del. 2003)); *Wallace ex rel. Cencom Cable Income Partners II, Inc., L.P. v. Wood*, 752 A.2d 1175, 1184 (Del. Ch.1999).

"Courts consider the following factors: (1) whether the company was adequately capitalized for the undertaking; (2) whether the company was solvent; (3) whether corporate formalities were observed; (4) whether the controlling shareholder siphoned company funds; or (5) whether, in general, the company simply functioned as a facade for the controlling shareholder." *Eagle Air*, 75 F. Supp. 3d at 896. Delaware courts also require an element of fraud to pierce the corporate veil. *Eagle Air*, 75 F. Supp. 3d at 896*; Mason v. Network of Wilmington, Inc.*, 2005 WL 1653954, at *3 (Del. Ch. 2005); *Wallace*, 752 A.2d at 1184.

"A parent corporation is not liable for the acts of its subsidiary merely because it owns (and votes) a majority of the subsidiary's stock or shares common shareholders, directors or officers with the subsidiary. Nor will conclusory allegations that the parent's management exclusively dominated and controlled the subsidiary's management suffice to state a claim for veil-piercing." *Wenske v. Blue Bell Creameries, Inc.*, C.A. No. 17-0699, 2018 WL 5994971, at *6 (Del. Ch. Nov. 13, 2018). In *Wenske*, the court dismissed a complaint as falling "short of the factual predicate required to justify piercing the veil" with allegations that (1) the parent company was 100% owner of the subsidiary and, in that capacity, appointed all of the subsidiary's directors; (2) the parent and subsidiary have overlapping officers and directors; and (3) the parent manages the subsidiary. Merely sharing corporate officers is not sufficient. *Swiss Reinsurance America Corp. v. Access General Agency, Inc.*, 571 F. Supp. 2d 882, 885 (N.D. Ill. 2008). Insolvency alone is also insufficient. As the *Mason* court noted, if mere insolvency were sufficient to pierce the corporate veil, "the limited liability characteristic of the corporate form would be meaningless." 2005 WL 1653954, at *3.

The *Mason* case is instructive. Mason successfully sued Personnel, a Delaware corporation owned by Schlecker. Mason was unable to collect her judgment because Schlecker caused Personnel to transfer its assets. Mason then sought to hold Schlecker liable by piercing the corporate veil and showing that the transfer was fraudulent. Mason argued that Personnel sold its assets for very little cash but the court found that the majority of the consideration was the assumption of debt. More importantly, the court concluded that there were no facts showing that the transaction was not arms' length, so even if Personnel was rendered insolvent, there was nothing to show that its assets were transferred in an attempt to avoid its creditors.

The trustee must allege facts to support a plausible basis for piercing the veil of each of the two entities he seeks to pierce - LOC I and CAF. Instead of addressing each corporation separately, his allegations treat LOC I and CAF as though they were the same corporation that he can pierce "together" to get to Colony. Not so. He must plead specific facts to support piercing each corporation's veil.[9] He has failed to do so.

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[9]The trustee acknowledges that he is attempting to "double pierce" the veil, which he argues is appropriate in the circumstances. Trustee Response p. 14. He also suggests, however, that Colony first owned the interests in LOC I by credit bidding for them at the UCC sale of LOC III's interests in LOC I. His allegations state, however, that while Colony credit bid for the

The trustee alleges no facts about CAF specifically other than it was created to hold the membership interests of LOC I and was owned and controlled by Colony. He does not allege that CAF was undercapitalized or that it failed to observe corporate formalities. The facts alleged about the unity of ownership and management do not come close to stating a claim to pierce CAF's corporate veil to recover from Colony. As explained above, under Delaware law, mere allegations of unity of ownership, management, and control are insufficient to pierce the corporate veil.

The trustee also fails to allege sufficient facts to support his effort to pierce LOC I's veil. Again, his general allegations that LOC I had no independent existence and that it was controlled by Colony through CAF are insufficient under Delaware law. The trustee also alleges that LOC I became insolvent through the sale of the properties after CAF acquired the interests in LOC I. This does not support piercing the corporate veil in the context of the trustee's other allegations of how and when CAF acquired the interests in LOC I. First, under Delaware law, insolvency alone does not support a claim for piercing. Second, Colony merely foreclosed on the pledge of the ownership interests after LOC I defaulted on the loan, so CAF inherited LOC I in March 2017 as it had been maintained by its previous owner - LOC III, which was owned by James K. McClelland. CAF then caused the sale by LOC I of the properties it owned at that time on which Colony had liens. LOC I's arms-length sale of Colony's collateral to reduce the secured debt owed to Colony would not weigh in favor of piercing the corporate veil merely because the sale proceeds were not sufficient to pay the entire amount owed, thereby creating insolvency. *See, e.g., Mason*, 2005 WL 1653954 (arms-length sale of assets accompanied by assumption of debt was insufficient to justify piercing the corporate veil).

The trustee alleges nothing about undercapitalization or corporate formalities regarding LOC I in his amended complaint. In his response to the motion, however, he states that LOC I was undercapitalized for the undertaking that Colony attempted, without stating what that means. The court assumes that the trustee means that the assets of LOC I were not sufficient to pay the full amount of the secured debt LOC I owed Colony at the time of the sale. As just explained, this would not support the piercing of the veil of LOC I (or CAF) in the circumstances of this case. The trustee also argues in his response that "Colony" did not observe the corporate

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interests - meaning it "paid" for them with the debt owed to it that was secured by the pledge of the interests, "at the end of the sale" Colony caused the interests to be transferred from LOC III not to Colony but to CAF, Colony's "designee." Am. Compl. ¶ 94. Under the trustee's allegations, Colony never actually took title to the ownership interests in LOC I. The court has treated Colony as the parent of CAF, which was the only entity that owned the interests in LOC I after the UCC sale. Thus, the trustee's initial statement - that he must pierce two corporations to get to Colony - is correct. He must therefore allege facts to support piercing each corporation's veil.

formalities. To pierce LOC I's veil, the focus is on corporate formalities observed between LOC I and CAF. The amended complaint is devoid of allegations regarding the observance of corporate formalities by LOC I or CAF (or Colony for that matter).[10]

More importantly, the trustee has failed to allege facts to support the crucial element of his claim without which he cannot pierce either LOC I's or CAF's corporate veil: that LOC I and CAF were shams used solely to commit a fraud or similar injustice on their creditors. Without facts to support this key element, his claims fail under Delaware law. *Eagle Air Transport, Inc.*, 75 F. Supp. 3d at 896, *Winner Acceptance Corp.,* 2008 WL 5352063, at *5; *Crosse*, 836 A.2d at 496; *Wallace*, 752 A.2d at 1184. The only alleged "fraud" or similar injustice alleged by the trustee is that CAF caused LOC I to sell the properties "quickly and below market," without regard to the rights of other creditors, including the Debtors. This is not sufficient to allege the fraud or injustice required to pierce the corporate veil.

The trustee uses pejorative and conclusory terms to try to cast the sale of collateral by a secured lender after a loan default as fraudulent or similarly unjust. He fails, however, to allege any facts that justify such a conclusion. For example, the trustee alleges that Colony did nothing to "protect" other creditors of LOC I. But he fails to identify any creditors except the Debtors, and he fails to state any basis for the Debtors being creditors of LOC I (and no basis is apparent). He does not contend that LOC I had any secured creditor other than Colony who could even

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[10]The trustee argues that he is not required to plead any facts that show that LOC I and CAF did not observe corporate formalities because that information is available only to the defendants. This is not correct. He cites only one case, *Wislow v. Wong*, 713 F. Supp. 1103, 1106 (N.D. Ill. 1989), which was decided long before the Supreme Court changed the standard for pleading to require a plaintiff to plead facts to support each element of his claim. *Ashcroft v. Iqbal*, 556 U.S. 662, 129 S.Ct. 1937 (2009)*; Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 127 S.Ct. 1955 (2007). Also, *Wislow* involved claims under securities laws, not a claim to pierce the corporate veil. It cited only one case (by the same judge), which stated, "*In a securities fraud case*, plaintiffs need only describe the outline of the fraudulent scheme and need not set forth facts which, because discovery has not been completed, are in the exclusive possession of defendants." *Donato v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 663 F. Supp. 669, 673 (N.D. Ill. 1987) (italics added). Thus, this pre-*Twombly* and *Iqbal* "rule" mentioned in *Wislow* applied only in securities cases in any event. The trustee cites no case, decided before or after *Iqbal* and *Twombly*, holding that a plaintiff need not allege facts regarding the observance of corporate formalities for a claim to pierce the corporate veil. If the trustee seeks to pierce the corporate veil based on the failure to observe corporate formalities, he must allege facts supporting that element of the claim.

potentially assert a competing right to the collateral. He also failed to identify any rights that other creditors of LOC I held or state how they were violated by the sales. He alleges that "there is no evidence that Colony, after taking control of LOC I, made any attempt to ascertain LOC I's general financial condition or to pay or even give notice to LOC I's other creditors, including the debtor." Am. Compl. ¶ 101. This allegation fails to state a fact at all. That *the trustee* does not have evidence of the matters asserted is not an allegation that notice required by any applicable law governing the sale of collateral was not given. The trustee fails to identify any UCC provision or other legal requirement that applied to the sales of the collateral or state how LOC I violated them. As a secured creditor with a first position lien on the properties, Colony was entitled to be paid in full from the proceeds of sale of the collateral before any unsecured creditor of LOC I was entitled to payment from the collateral. Colony was not paid in full from the sale of the properties, which is why it filed a proof of claim in Mack's bankruptcy.[11] The trustee's general arguments about other creditors being prejudiced in an unspecified way by the sale does not support the conclusion that LOC I liquidated the collateral in a way that constituted fraud or similar unjust conduct.

The trustee also alleges that the "quick" sales "raised a barrier" to other creditors, such as the Debtors, pursuing their claims against LOC I. Again, he alleges no facts to support these conclusory assertions. As noted above, he gives no description of any claims the Debtors or anyone else held against LOC I or how those claims could have limited Colony's right to liquidate collateral on which it held first priority liens. The trustee also repeatedly describes the sales as "quick." He presents no factual basis for concluding, however, that the sale of the properties over the 9 month period alleged was unreasonable let alone perpetrated a fraud on creditors. Am. Compl. ¶ 97.[12]

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[11]Colony argues that Mack had agreed to renovate the properties and that LOC I caused Colony to advance funds for Mack to do so but Mack never performed most of the work. Colony contends that the failure to improve the many dilapidated properties explains in part the difference between the "as improved" values the trustee references and the prices for which the properties ultimately sold. These arguments based on facts outside the complaint, like many others raised by Colony, cannot be considered on a motion to dismiss.

[12]The defendants contend in their motion that the bulk sales of the properties were the only cost effective way to sell the properties in question, which were "relatively inexpensive and often dilapidated single family homes." They state that a lengthy marketing effort to sell each property individually was not a viable alternative. The trustee did not contest these assertions, though they involve facts not alleged in the complaint that cannot form the basis for dismissal of a complaint. The trustee has not, however, alleged a factual basis for concluding that the time frame of the sales was unreasonable. Merely calling them "quick" does not give rise to an inference of fraudulent or unjust conduct.

Similarly, the trustee's contention that CAF and Colony "unfairly siphoned" off funds from the sale is merely conclusory. Am. Compl. ¶ 142. His allegations show that the collateral was sold and the proceeds were used to pay down the debt secured by the collateral in accordance with Colony's undisputed lien rights. Using the words "unfair" and "siphoned" does not turn this ordinary exercise of a secured creditor's legal rights into fraud or injustice that would justify piercing the corporate veil.

The trustee further alleges that CAF caused the sale of the properties for $12 million less than Colony had "valued" the properties at "just months earlier," apparently based on the valuations given the properties when the loan funds were advanced. Am. Compl. ¶ 98. Yet, again, the trustee does not allege that LOC I violated any provision of the UCC or other applicable law when it sold the properties or even that its actions were unreasonable. The fact that the properties sold for significantly less than the value Colony previously gave them when it loaned the money does not give rise to a reasonable inference of fraud or similar injustice required to pierce the corporate veil. To the contrary, it is reasonable to assume that LOC I, CAF, and Colony had every incentive to get as much as possible for the properties in the circumstances. There is no reasonable basis for inferring that CAF required LOC I to sell the properties for an inappropriately low price to defraud other creditors, particularly since no other creditor could trump Colony's first-lien right to the proceeds. The trustee also alleges that CAF and Colony sold the properties quickly to "insulate themselves from future liability" but, as discussed above, he alleges no facts to show that LOC I was subject to any liability by anyone in the first place or that any party could even potentially have the right to the proceeds of sale of the properties.

Finally, the trustee alleges that Colony "caused LOC I's status with the Illinois Secretary of State to be changed to 'revoked' as of May 11, 2018." Am. Compl. ¶ 99. This fact does not support the inference that anything fraudulent or unjust occurred. Under Illinois law, a foreign LLC's authority to transact business in Illinois may be revoked by the Secretary of State if that company fails to perform ministerial acts like paying a fee and filing an annual report. 805 ILCS 180/45-35. It is unclear to what the trustee refers when he alleges that Colony "caused" LOC I's status to be "revoked" but by May 2018, almost a year after the assets were sold, there would have been no purpose in maintaining good standing for LOC I.

The trustee seeks to pierce the corporate veils of two corporations - an extraordinary remedy - based on an ordinary liquidation of collateral. He must allege facts that support the plausible conclusion that both CAF and LOC I were sham entities that operated for no purpose other than to defraud their creditors. The trustee has failed to meet this burden. He has not shown that the sales did not comply with applicable law for liquidation of collateral, nor has he alleged facts that would raise any lack of compliance with applicable law to the level of fraud or similar injustice. The trustee has also failed to cite any similar case in which the sale of collateral to pay a secured debt was deemed a "fraudulent" or similarly "unjust" action that would justify piercing the veil.[13] He has therefore failed to plead facts sufficient to state a claim to pierce the corporate veils of LOC I and CAF.

5. Conclusion

For all of the reasons stated above, the motion to dismiss is granted as follows:

Count 1: The claim in Count 1 against Colony to avoid and recover fraudulent transfers based on constructive fraud is dismissed. The defendants did not seek dismissal of the claim in Count 1 against LOC I, which is not dismissed.

Count 2: The claim in Count 2 against both Colony and LOC I to avoid and recover fraudulent transfers based on actual fraud is dismissed.

Count 3: The claim in Count 3 to pierce the corporate veils of LOC I and CAF is dismissed.

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[13] The trustee ignores the cases from this district interpreting Delaware law, *Eagle Air Transport*, 75 F. Supp. 3d 883 and *Swiss Reinsurance*, 571 F. Supp. 2d 882, 885, and relies almost exclusively on *NetJets Aviation, Inc.*, 537 F.3d 168 (2nd Cir. 2008). *NetJets*, however, bears no resemblance to this case. In *NetJets*, Zimmerman was the owner of LHC, a Delaware limited liability corporation with which NetJets had entered into two contracts. After LHC terminated the contracts, a large balance remained due to NetJets. LHC then ceased operations. NetJets sued LHC and Zimmerman for breach of contract and equitable remedies. The district court dismissed NetJets' claims against Zimmerman on the ground that there was insufficient evidence to pierce the corporate veil. On appeal, the Second Circuit vacated that portion of the judgment and remanded the case. The court discussed a lot of evidence showing that Zimmerman used LHC as his personal "piggy bank." He put money into LHC when LHC needed it and took money out as he needed it. Zimmerman had LHC making margin calls in his personal investment accounts. LHC made payments to the corporation that owned Zimmerman's home - a $15 million Park Avenue apartment in which Zimmerman and his family lived. Phone bills, cleaning services, health insurance, a $350,000 Bentley for Zimmerman's personal use were personal expenses all paid by LHC. It was a classic case of an individual using a corporate entity in an improper manner that disregarded the rights of LHC's creditors. It does not support the trustee's claims here.

STATEMENT

Dated: March 31, 2021

ENTERED:

Carol A. Doyle
United States Bankruptcy Judge