United States Bankruptcy Court, Northern District of Illinois

JUDGE	Deborah L. Thorne	**Case No.**	22-00504
DATE	10/11/2022	**Adversary No.**	22-00096
CASE TITLE	Heiligman, Ch. 7 Trustee v. Knight		
TITLE OF ORDER	Order Denying Defendant's Motion to Dismiss		

STATEMENT

This matter comes before the court on Defendant Jennifer Knight's motion to dismiss the complaint filed against Defendant by the chapter 7 trustee ("Plaintiff" or "Trustee"). Trustee's complaint alleges that Debtor made constructive fraudulent transfers to Defendant in the amount of $375,000 for less than reasonably equivalent value while Debtor was insolvent. For the reasons explained below, Defendant's motion is denied.

I. BACKGROUND

On January 16, 2022, Carlton Wayne Knight ("Debtor") filed a voluntary petition under chapter 7 of the Bankruptcy Code. (*See* Dkt. No. 1.) In his Statement of Financial Affairs, Debtor listed that he made a transfer of $375,000 to Defendant, his spouse, on September 29, 2020 (the "Transfer"). (*See* Statement of Financial Affairs ("SOFA"), Dkt. No. 48, at 5.) The Trustee sent a demand letter to Defendant on April 12, 2022, requesting repayment of the Transfer. (*See* Compl. ¶ 14, Adv. Dkt. No. 1.)

On June 10, 2022—after not receiving a payment or substantive response from Defendant—the Trustee brought this action to avoid and recover the Transfer. In his complaint, the Trustee alleges that Debtor did not receive reasonably equivalent value in exchange for the Transfer and that, at the time of the Transfer, Debtor was insolvent. (*Id.* ¶¶ 11–12.) The complaint contains three counts. The first is to avoid the Transfer under 11 U.S.C. § 548(a)(1)(B), the second

is to recover the Transfer under 11 U.S.C. § 550, and the third is to disallow Defendant's claims under 11. U.S.C. § 502(d) until she repays the Transfer amount plus interest. Defendant filed a motion to dismiss the Trustee's complaint, alleging that the Trustee failed to state a cause of action because Debtor was not the transferor and Defendant was not the transferee.[1] (*See* Def.'s Mot. to Dismiss, Adv. Dkt. No. 8.)

II. DISCUSSION

A. Defendant's Motion to Dismiss Is Denied

To survive a Rule 12(b)(6) motion to dismiss, "a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (quoting *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007)). This standard does not require a complaint to contain detailed factual allegations. *Twombly*, 550 U.S. at 555. A claim is plausible "when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Adams v. City of Indianapolis*, 742 F.3d 720, 728 (7th Cir. 2014) (quoting *Iqbal*, 556 U.S. at 678). In construing a complaint, a court must "accept all well-pleaded facts as true and draw reasonable inferences in the plaintiffs' favor." *Roberts v. City of Chicago*, 817 F.3d 561, 564 (7th Cir. 2016).

1. Count I: 11 U.S.C. § 548(a)(1)(B)

Plaintiff seeks to avoid the Transfer to Defendant under § 548(a)(1)(B), which allows the Trustee to avoid any transfer that was made within two years before the date of filing for which

[1] Defendant also contends that the complaint must be dismissed because paragraphs 16 and 17—in which the Trustee states that he may learn of and try to avoid other transfers and that he reserves the right to amend the complaint—fail to appraise Defendant of any cause of action and "circumvent[ ] a host of due process rights." (Compl. ¶¶ 15–16.) The Court disagrees. This is not a cause of action but mere surplusage. "[T]he proposition that a particular complaint includes surplusage is not a basis to dismiss the complaint; at most, it serves as a basis to strike the surplusage." *Adams v. BRG Sports, Inc.*, No. 17 C 8544, 2018 WL 4853130, at *3 (N.D. Ill. Oct. 5, 2018); *see also U.S. ex rel. Garst v. Lockheed-Martin Corp.*, 328 F.3d 374, 378 (7th Cir. 2003) (stating that surplusage "can and should be ignored" but is not grounds to dismiss a complaint). Defendant's reply asks the Court to strike these paragraphs; this request is denied.

the Debtor "received less than a reasonably equivalent value in exchange for such transfer" and "was insolvent on the date that such transfer was made . . . or became insolvent as a result of such transfer." 11 U.S.C. § 548(a)(1)(B). "Under federal and state fraudulent-transfer law, a debtor is insolvent if it has 'a balance sheet on which liabilities exceed assets.'" *In re Chi. Mgmt. Consulting Grp.*, 929 F.3d 803, 809 (7th Cir. 2019) (quoting *Baldi v. Samuel Son & Co., Ltd.*, 548 F.3d 579, 581 (7th Cir. 2008)). With respect to reasonably equivalent value, the Seventh Circuit has said that there is no "fixed mathematical formula"—reasonable equivalence "should depend on all the facts of the case." *Barber v. Golden Seed Co.*, 129 F.3d 382, 387 (7th Cir. 1997) (internal quotation marks and citation omitted). Courts may consider "the fair market value of what was transferred and received, whether the transaction took place at arm's length, and the good faith of the transferee." *In re Smith*, 811 F.3d 228, 240 (7th Cir. 2016) (citing *Barber*, 129 F.3d at 387).

Construing all well-pleaded facts in favor of Plaintiff, the complaint states a plausible claim to avoid the alleged constructive fraudulent transfer to Defendant. The Transfer took place on September 29, 2020, which was fewer than two years before Debtor filed his petition on January 16, 2022. The complaint plausibly alleges that Debtor was insolvent at the time of the Transfer or made insolvent as a result of the Transfer; the Transfer was for $375,000, and Debtor's liabilities exceeded his assets by approximately $345,000 at the time he filed his petition. (*See* Compl. ¶¶ 13, 22.) Moreover, the complaint alleges that Debtor did not receive anything in exchange for the Transfer, meaning that he did not receive reasonably equivalent value. (*Id.* ¶ 21.)

Defendant's motion to dismiss does not contest that the complaint is sufficient with respect to insolvency and reasonably equivalent value. Instead, Defendant argues that Plaintiff failed to state a cause of action because Debtor was not the transferor and Defendant was not the transferee; the Transfer was made from an account owned by Real Dealz Properties ("RDP") and Housing

Services Initiatives ("HSI") and paid to Knight Real Estate Group, Inc. (Mot. to Dismiss at ¶ 12.) In support of this claim, Defendant appended a bank statement and a number of receipts ("Group Exhibit B") that were also filed alongside Defendant's Motion to Quash a Rule 2004 Subpoena in the underlying bankruptcy case. (*See* Dkt. No. 142.) Defendant contends that the Court should consider Group Exhibit B because the documents are subject to judicial notice and because Fed. R. Civ. P. 10(c) allows documents appended to a motion to dismiss to become part of the complaint if the complaint refers to them and they are central to the plaintiff's claim. (*Id.* ¶¶ 12–13.)

The Court is not inclined to consider Defendant's Group Exhibit B in ruling on the motion to dismiss. *See Rosenblum v. Travelbyus.com Ltd.*, 299 F.3d 657, 661 (7th Cir. 2002) ("As a general rule, on a Rule 12(b)(6) motion, the court may consider only the plaintiff's complaint."). While Rule 10(c) allows some exhibits to become part of the complaint, it is a "narrow exception aimed at cases interpreting, for example, a contract. It is not intended to grant litigants license to ignore the distinction between motions to dismiss and motions for summary judgment." *Levenstein v. Salafsky*, 164 F.3d 345, 347 (7th Cir. 1998). Group Exhibit B does not fall under Rule 10(c). It is not referenced in the complaint—in fact, the Trustee had not seen these documents before filing the complaint (*see* Pl.'s Resp. to Def.'s Mot. to Dismiss at 4, Adv. Dkt. No. 11)—and it is not central to the Plaintiff's claim. *Cf. Franklin v. DePaul Univ.*, No. 16 C 8612, 2017 WL 3219253, at *4 (N.D. Ill. July 28, 2017) (declining to consider evidence attached to a motion to dismiss where the complaint did not reference the exhibit and plaintiff had not seen it).

Nor should the Court take judicial notice of the contents of the documents in Group Exhibit B. To be subject to judicial notice, a fact must be "not subject to reasonable dispute" because it (1) "is generally known within the trial court's territorial jurisdiction" or (2) "can be accurately and readily determined from sources whose accuracy cannot reasonably be questioned." Fed. R.

Evid. 201(b). While the fact that the documents were filed is subject to judicial notice, the truth of their contents is subject to reasonable dispute. *Cf. Liberty Mut. Ins. Co. v. Rotches Pork Packers, Inc.*, 969 F.2d 1384, 1388 (2d Cir. 1992) ("A court may take judicial notice of a document filed in another court not for the truth of the matters asserted in the other litigation, but rather to establish the fact of such litigation and related filings." (internal quotation mark omitted)). Because Defendant's motion asks the Court to consider the substance of the Group Exhibit B documents—not merely the existence of the filing—judicial notice is improper. Plaintiff has stated a plausible claim for constructive fraudulent transfer, and Defendant's motion is denied with respect to Count I.

2. Count II: 11 U.S.C. § 550

Once a transfer is avoided as fraudulent, § 550 allows the Trustee to recover property transferred or the value of such property. *See* 11 U.S.C. § 550. This provision "divides transferees into two categories: the 'initial transferee' under § 550(a)(1) and 'any immediate or mediate transferee' under § 550(a)(2)." *Smith*, 811 F.3d at 244. An initial transferee is "simply the first transferee in the chain of title" and "has no defense against liability under § 550." *Id.*

The complaint alleges that Defendant received the Transfer from Debtor, which would make her an initial transferee. As discussed above, Defendant's motion to dismiss disputes these facts. But the Trustee is correct in noting that Defendant's arguments go to the merits of the claim rather than the sufficiency of the complaint. *See Gibson v. City of Chicago*, 910 F.2d 1510, 1520 (7th Cir. 1990) ("The purpose of a motion to dismiss is to test the sufficiency of the complaint, not to decide the merits."). While discovery might reveal that the Transfer was from RDP and HSI to Knight Real Estate (and perhaps, then, to Defendant), this possibility does not undermine the sufficiency of the Trustee's complaint. Drawing all reasonable inferences in the Trustee's favor

yields the conclusion that the Transfer was from Debtor to Defendant. The Trustee has adequately pled a claim under § 550, and Defendant's motion is denied as to Count II.

3. Count III: 11 U.S.C. § 502(d)

Section 502(d) explains that courts "should disallow any claim of any entity" who was a transferee of a voidable transfer under § 548 or from whom property is recoverable under § 550. *See* 11 U.S.C. § 502(d). Because the Trustee has sufficiently pled causes of action against Defendant under §§ 548 and 550, the Court finds that the complaint also states a plausible claim under § 502(d). Defendant's motion to dismiss is denied as to Count III.

B. Summary Judgment Is Not Appropriate at this Stage

Defendant urges that, in the alternative, her motion to dismiss be treated as a motion for summary judgment under Rule 12(d). This rule provides that "[i]f, on a motion under Rule 12(b)(6) or 12(c), matters outside the pleadings are presented to and not excluded by the court, the motion must be treated as one for summary judgment under Rule 56." Fed. R. Civ. P. 12(d). Summary judgment is appropriate when the movant shows that there is "no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(a).

The Court declines to treat the instant motion as a motion for summary judgment. As discussed above, the Court did not consider Group Exhibit B when ruling on the motion to dismiss. Even if it were prudent to consider Group Exhibit B, there are genuine disputes of material fact that would prevent the entry of summary judgment. For example, the parties disagree as to how many transfers took place, the identities of the transferor and transferee, and whether Defendant was an initial transferee. Defendant's answer—which has not yet been filed—may reveal additional disputes of material fact as well. *See In re KJK Const. Co., Inc.*, 414 B.R. 416, 426 (Bankr. N.D. Ill. 2009) ("In consideration of the general caution that summary judgment should

not be granted if there is an issue presented as to any material fact, if the motion is made before an answer is filed, courts are reluctant to grant summary judgment unless it is very clear that an answer will not raise any significant issues of fact." (internal quotation mark omitted) (collecting cases)). Summary judgment is not appropriate at this time.

III. CONCLUSION

Defendant's motion to dismiss is denied as to all counts, and Defendant must file an answer to the complaint within twenty-one days.

Date: October 11, 2022

Honorable Deborah L. Thorne
United States Bankruptcy Judge