

Recent Success in Dismissing Fraudulent Conveyance Claims in Deed-in-Lieu Transaction

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In this article, the authors review recent court decisions that are helpful to lenders in highlighting circumstances where courts are amenable to dismissing frivolous challenges to deed-in-lieu agreements in bankruptcy, notwithstanding higher appraised values and allegations of lender misconduct.

On June 17, 2024, in a non-precedential summary opinion in *Wade Park Land Holdings, LLC, et al. v. Kalikow, et al.*, the U.S. Court of Appeals for the Second Circuit (the Second Circuit) affirmed a decision by the U.S. District Court for the Southern District of New York (the District Court or the Southern District), that granted a motion to dismiss fraudulent conveyance claims brought by certain property developers against several of their lenders, who had taken possession of the properties at issue via a deed-in-lieu of foreclosure agreement.¹

The Second Circuit's order and lower court decision are notable in that they permitted dismissal of the action even in the face of allegations that the lenders had transformed "a temporary bridge loan . . . into a fraudulent scheme . . . to take control of two parcels of land," known as "Wade Park," and even though

the plaintiffs cited to two appraisals for values well in excess of the outstanding loan amounts satisfied with the deed-in-lieu agreement.² Although the Second Circuit's summary order is non-precedential, coupled with the underlying District Court decision, these decisions are helpful to lenders in highlighting circumstances where courts are amenable to dismissing frivolous challenges to deed-in-lieu agreements in bankruptcy, notwithstanding higher appraised values and allegations of lender misconduct.

BACKGROUND

From 2012 to 2015, Georgia-based property developer Stanley Thomas acquired 176 acres of land known as Wade Park through various entities and ultimately divided the property into two parcels - a northern parcel, to which Wade Park Land LLC (WP Land) held title, and a

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southern parcel, to which Wade Park Land Holdings, LLC (WPL Holdings) held title.³ Thomas planned to develop both properties into “office towers, retail space, residential housing units, and hotels,”⁴ and financed the acquisition and initial construction on the properties with two loans in principal amount of \$93 million that were set to mature in early 2017.⁵ Around the same time, in November 2016, the Sage Group provided an appraisal that valued the properties, together, at \$466.8 million (the Sage Appraisal).⁶

After several unsuccessful attempts to secure additional financing for Wade Park, Thomas secured a bridge loan in January 2017 from defendants Gamma Real Estate Capital, LLC (Gamma) and Jonathan Kalikow (Kalikow) for approximately \$83 million.⁷ The initial term of the loan was for four months, with a borrower option to extend the term three times, for three months each time, subject to satisfaction of certain conditions.

It further included a term that Kalikow referred to as “The Hammer” - which gave Kalikow, Gamma and the other defendants (WP Development Partners, Gamma Lending Omega, LLC, and GRE WP, LLC) a 75% equity interest in the Wade Park properties through an ownership interest in a bankruptcy-remote entity, and provided that they would retain that interest unless the bridge loan was repaid within sixty days of its maturity date.⁸ Thomas exercised all three extension options, while he also unsuccessfully attempted to secure permanent financing for Wade Park with lenders other than Gamma and Kalikow.⁹

In January 2018, the defendants declared a default on the bridge loan, and subsequently WP Land and WPL Holdings entered into six

consecutive forbearance agreements with the defendants.¹⁰ Plaintiffs WP Land, WPL Holdings and The Thomas Family Trust alleged that during this time Kalikow and Gamma repeatedly frustrated their attempts to obtain additional financing, including buying out unrelated loans that Thomas had attempted to refinance in order to pay back the bridge loan, shouting and yelling at other lenders in meetings to discuss financing, and otherwise refusing to accept financing terms that other lenders proposed.¹¹ Also around that time, in January 2019, an appraisal issued by BBG, Inc. valued Wade Park at \$565 million (the BBG Appraisal).¹²

In February 2019, after the expiration of the forbearance agreements, defendant Gamma Lending Omega, LLC (Gamma Lending Omega) entered into a Deed-in-Lieu Agreement (the DIL Agreement) with plaintiffs pursuant to which the plaintiffs agreed to deliver the deeds to Wade Park in exchange for approximately \$140.1 million in total debt relief.¹³ Gamma Lending Omega agreed to delay recording the deeds for six weeks to allow Thomas even more time to secure financing. Around the same time, the parties also entered into a buy-back agreement that provided that the plaintiffs could repurchase the properties for about \$150 million within a month of signing the buy-back agreement.¹⁴ Ultimately, Thomas was again unable to secure financing to repurchase the properties.

Plaintiffs initially filed the complaint as an adversary proceeding in the U.S. Bankruptcy Court for the Northern District of Georgia, where WP Land and WPL Holdings had filed Chapter 11 petitions, asserting eighteen causes of action against the defendants, including fraudulent transfer claims.¹⁵ Plaintiffs

then moved to withdraw the reference to the bankruptcy court and have the matter heard in the U.S. District Court for the Northern District of Georgia.¹⁶ The case was then transferred to the Southern District of New York, on motion by the defendants and pursuant to a forum selection clause.¹⁷ On March 4, 2022, the Southern District dismissed the complaint with prejudice, but granted the plaintiffs leave to amend their complaint to replead their fraudulent transfer claims.¹⁸

THE DISTRICT COURT'S DECISION

After the plaintiffs repleaded their fraudulent conveyance claims, the District Court again granted defendants' motion to dismiss, holding that it was "utterly implausible that the transfer was for anything other than reasonably equivalent value."¹⁹ The District Court ran through a number of facts that, when taken together, underscored that the transfer pursuant to the DIL Agreement was for reasonably equivalent value.

In reaching its decision, the District Court focused on the extensive history of Thomas's attempts to obtain financing to repay the bridge loan, as well as the affidavits signed by plaintiffs in connection with the DIL Agreement, which stated that they believed that the "consideration [for the deeds] represents the fair market value of the property," even though the plaintiffs were aware of the appraisal values.²⁰ The District Court also pointed to the plaintiffs' right to sell, refinance or buy back the properties for a period of time after signing the DIL Agreement, and the defendants' offer of a buy-back agreement at \$150 million, none of which rights were exercised by the plaintiffs, in concluding that the "only inference to be drawn is that in 2019, as in the over one year period

prior, there was no buyer or lender who would value the property at \$565 million, or anywhere close."²¹

In the face of these facts, the District Court dispensed with the BBG Appraisal of \$565 million. Given that plaintiffs failed to introduce the full appraisal, and that the cover letter the plaintiffs did introduce included only conclusory opinions about the value of Wade Park, the District Court held that the appraisal was insufficient to "create a plausible inference that the DIL Agreement was for other than reasonably equivalent value," even at the motion to dismiss stage.²² The District Court also noted that appraisals are generally "worth only as much as their models and assumptions are worth."²³ Here, the appraisal cover letter did not include any detail of the credentials of the appraiser, the methodology used, or any underlying assumptions.²⁴

The District Court likewise dispensed with the plaintiffs' attempt to rely on the Sage Appraisal of \$466.8 million, noting it predated the deed-in-lieu transfer by more than two years.²⁵ As such, the Sage Appraisal was insufficient to support a plausible inference that the DIL Agreement was for other than reasonably equivalent value.²⁶

Finally, the District Court addressed the allegations of interference by the defendants with the plaintiffs' attempts to obtain financing.

First, the District Court concluded that no interference was alleged during the months surrounding the DIL Agreement or buy-back agreement.²⁷

Second, the District Court found that there was "no reasonable basis to infer anything other than that Defendants were simply insist-

ing on being paid for the debt that was owed to them.”²⁸

As such, the District Court concluded that the allegations were “insufficient to establish that Defendants acted with the intention of preventing Plaintiffs from obtaining financing.”²⁹

THE SECOND CIRCUIT’S DECISION

In its summary order, the Second Circuit affirmed the District Court’s decision, largely adopting the same reasoning. The Second Circuit’s review focused on whether the District Court gave proper weight to the two appraisals, whether the District Court accurately accounted for Thomas’s ability to obtain financing or sell the property, and the representations made in connection with the DIL Agreement.³⁰

Regarding the appraisals, the Second Circuit affirmed the District Court’s holding that the “values stated in the Sage and BBG Appraisals were not plausible when viewed in light of other allegations in the complaint - in particular, the conduct of the parties and Thomas’s inability to refinance Wade Park.”³¹ Like the District Court, the Second Circuit noted that appraisals are only as valuable as the methodology and assumptions used, and here, the Second Circuit found that those were “questionable,” calling out the heavy reliance on Thomas himself for estimates used in the appraisals.³²

The Second Circuit also similarly focused on the history of Thomas’s failures to obtain financing and stated that Thomas’s inability to refinance the properties reinforced the conclusion that they were worth no more than \$150 million.³³ The Second Circuit was also unmoved by the plaintiffs’ allegations that the defendants interfered with their financing ef-

orts, noting it was entirely in Gamma’s interest to allow refinancing so that they could be paid what they were owed.³⁴

Further, the Second Circuit stated that Gamma’s conduct was inconsistent with it believing that Wade Park was worth more than the value reflected in the DIL Agreement and that Gamma’s offer to allow Thomas to buy the property back at \$150 million “would have been irrational if Gamma believed that the property was worth much more.”³⁵

Finally, the Second Circuit held that the transfer pursuant to the DIL Agreement was for reasonably equivalent value for an additional reason - Gamma provided reasonably equivalent value “in the form of the opportunity to retain ownership of Wade Park.”³⁶

KEY TAKEAWAYS

Although non-precedential in nature, the Second Circuit’s summary order is notable given that it dismissed fraudulent conveyance claims on a motion to dismiss. While in other contexts fraudulent conveyance claims may be difficult to dismiss at this early stage, the Second Circuit’s order and the District Court’s underlying decision indicate that courts are amenable to dismissing frivolous challenges to deeds-in-lieu in certain circumstances. These circumstances include where questions exist on whether reasonably equivalent value was received, notwithstanding higher appraisal values and allegations of lender misconduct, and when it can be established that the borrower agreed to a deed-in-lieu instead of effectuating an alternative transaction, such as a sale, consent to foreclosure, or refinancing that could have preserved additional value had it existed.

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NOTES:

¹*In re Wade Park Land Holdings, LLC*, 2024 WL 3024648 (2d Cir. 2024) (summary order) [hereinafter the Second Circuit Order].

²*Wade Park Land Holdings, LLC v. Kalikow*, 2023 WL 2614243 (S.D. N.Y. 2023), *aff'd*, 2024 WL 3024648 (2d Cir. 2024) at 2 [hereinafter the District Court Opinion].

³District Court Opinion at 2.

⁴District Court Opinion at 2.

⁵District Court Opinion at 2.

⁶District Court Opinion at 9.

⁷District Court Opinion at 3.

⁸District Court Opinion at 3–4.

⁹District Court Opinion at 4.

¹⁰District Court Opinion at 5.

¹¹District Court Opinion at 6.

¹²District Court Opinion at 8–9.

¹³District Court Opinion at 7.

¹⁴District Court Opinion at 8.

¹⁵Second Circuit Order at 7.

¹⁶Second Circuit Order at 7.

¹⁷District Court Opinion at 11.

¹⁸District Court Opinion at 13.

¹⁹District Court Opinion at 28, 30.

²⁰District Court Opinion at 30, 33.

²¹District Court Opinion at 32.

²²District Court Opinion at 34.

²³District Court Opinion at 37.

²⁴District Court Opinion at 38. The District Court separately addressed whether plaintiffs should be allowed to replead with the full appraisal report attached to the amended complaint. However, the District Court noted that the statements of value in the report were conclusory and supported by assumptions and explanation that were “either absent or informed by the developer itself.” District Court Opinion at 42.

²⁵District Court Opinion at 38–39.

²⁶District Court Opinion at 39.

²⁷District Court Opinion at 40.

²⁸District Court Opinion at 41.

²⁹District Court Opinion at 39.

³⁰Second Circuit Order at 9.

³¹Second Circuit Order at 10.

³²Second Circuit Order at 13–14.

³³Second Circuit Order at 12.

³⁴Second Circuit Order at 12.

³⁵Second Circuit Order at 12–13.

³⁶Second Circuit Order at 15.