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Turning Paper into Cash: Post-Judgment Collection Methods

Michael T. Benz and Mark A. Silverman*

In this article, the authors explain the post-judgment collection process and describe a recent U.S. Court of Appeals for the Seventh Circuit case addressing post-judgment fraudulent transfers.

Picture this: your company spends two years and thousands of dollars on legal fees to obtain a final money judgment against a defendant in a complex commercial litigation matter. Not surprisingly, the defendant does not immediately fork over the judgment amount to you. Now your attorney tells you that your company needs to spend additional funds to begin "post-judgment collection proceedings" to collect on the judgment. The thought of more litigation can be intimidating, but through awareness of the process, working with your attorney to focus the issues, and analyzing the possibility of a recovery, the process can be mastered and work in your favor to turn your paper judgment into cash.

POST-JUDGMENT COLLECTION METHODS

In Illinois, after a judgment becomes final and appealable, a judgment creditor can choose to initiate a citation to discover assets against the judgment debtor. These "supplementary proceedings" are governed by statute and the Illinois Supreme Court Rules.[1] Once a citation is issued and properly served, a judgment creditor may begin an intensive fact-finding mission to determine where the judgment debtor is holding assets.

The judgment creditor typically attaches a document rider to the citation requesting the production of the judgment debtor's financial records.[2] After the judgment debtor produces the documents for review, the judgment creditor can conduct the judgment debtor's citation examination under oath.[3] Think of the citation examination as a deposition centered solely around the judgment debtor's current financial condition.

At the citation examination, the judgment debtor and his or her attorney are present, along with a court reporter. During the examination, the judgment creditor is free to ask any questions that are relevant to the judgment debtor's assets and financial condition. In most cases, the judgment creditor attempts to secure information that would be useful for the turnover of assets (e.g., subsequent third

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[1] *See* 735 ILCS 5/2 1402; Ill. Sup. Ct. R. 277.

[2] *See* Ill. Sup. Ct. R. 204(a)(4).

[3] *See* 735 ILCS 5/4 1402(b).

party citations to discover assets to freeze a judgment debtor's accounts at a bank, a wage garnishment to garnish a percentage of the judgment debtor's non-exempt wages, or a forced sale of the judgment debtor's real or personal property with the proceeds paid to the judgment creditor).

During the citation examination the judgment creditor is also on the lookout for potential red flags relating to the judgment debtor's testimony, including, but not limited to, issues involving fraudulent conveyances to third parties, shifting of assets to a shell corporation, or hidden assets in offshore trusts. If the citations examination reveals transfers of funds from the judgment debtor to third parties without the judgment debtor receiving reasonably equivalent value in exchange for the transfers, and the judgment debtor did not have the financial wherewithal to pay its liabilities at the time of the transfers, it may be possible to unwind some of those transactions through separate fraudulent conveyance litigation.

In order to claw back some of those transferred funds you will need to discuss with your attorney the possibility of filing a lawsuit alleging a violation of the Uniform Fraudulent Transfer Act. Pursuing this type of action requires that you file a new complaint (with its attendant costs) naming the transferee. Once the complaint is filed, the case proceeds as a typical lawsuit (i.e., complaint, answer/motion to dismiss, discovery, depositions, possible summary judgment, trial, etc.).

THE FRAUDULENT TRANSFER ACT

Two Types of Fraud

There are two types of fraud under the Uniform Fraudulent Transfer Act: actual fraud and constructive fraud.[4] In order to successfully establish actual fraud, the plaintiff must show that there was a transfer of assets "with actual intent to hinder, delay, or defraud any creditor."[5] To successfully establish constructive fraud, the plaintiff must show that there was a transfer of assets "without receiving reasonably equivalent value in exchange for the transfer or obligation, and the debtor . . . intended to incur, or believed or reasonably should have believed that he would incur, debts beyond his ability to pay as they became due."[6] A recent Seventh Circuit opinion addressed this very topic.

Centerpoint Energy Servs., Inc. v. Halim

In *Centerpoint Energy Servs., Inc. v. Halim*,[7] a final judgment was entered against the defendant LLC in favor of the plaintiff. The plaintiff (now judgment creditor) then sought to collect the judgment amount from the judgment debtor LLC. The judgment creditor was unable to collect from the judgment debtor because the

[4] *See* 740 ILCS 160/5(a)(1)–(2).

[5] 740 ILCS 160/5(a)(1).

[6] 740 ILCS 160/5(a)(2)(B).

[7] No. 13-1797 (7th Cir. Feb. 18, 2014).

judgment debtor had shifted all of its financial and other assets, along with all of its contracts and employees, to a new company. Each LLC at issue was wholly owned by the same individuals. Essentially, the judgment debtor was playing a shell game to avoid paying the judgment amount.

Upon discovering that information, the judgment creditor initiated a lawsuit against the transferee LLC and the LLC owners in federal court, alleging a violation of the Uniform Fraudulent Transfer Act, successor liability, and alter ego liability. The district court granted summary judgment in favor of the plaintiff and entered a final judgment, plus post-judgment interest. The judgment debtor then appealed the decision.

The Seventh Circuit considered whether the judgment debtor committed actual or constructive fraud when it moved its assets. The court analyzed the transferred assets and determined that the owners of each LLC utilized them as personal piggy banks, meaning that the LLC would have a "zero balance" at all times. Essentially, the owners would put money in to pay the LLC's debts, and any excess funds after the debts were paid would be transferred to the owners' personal accounts. On top of that, once the initial LLC had the judgment entered against it, the owners caused all assets and liabilities (obligations) to be transferred to a new LLC.

Based on the fact that the judgment debtor LLC transferred all of its assets to a new LLC without receiving reasonably equivalent value, the Seventh Circuit ruled that the plaintiff proved constructive fraud. Because all of the judgment debtor LLC's rights and obligations were transferred to the new LLC, the court ruled that the plaintiff proved successor liability. Finally, because the owners comingled their assets with the assets of the LLC(s) without formal documentation, the court explained that the plaintiff's alter ego claim was a "strong claim," but did not analyze it further, given the court's ruling on plaintiff's successor liability claim.

The court also analyzed two additional issues—post-judgment interest and attorneys' fees—which are helpful to a judgment creditor when analyzing its post judgment collection strategy. In Illinois, "judgments recovered in any court shall draw interest at the rate of 9% per annum from the date of the judgment until satisfied."[8] In the current low interest rate environment, and assuming the judgment is ultimately collectible, this is a potential benefit to a judgment creditor, given that post-judgment proceedings can take some time to complete. During the entirety of that time, interest continues to accrue at nine percent.

With respect to attorneys' fees, in the *Centerpoint Energy Servs.* case, the contract language provided that the executing party was liable "for all costs and expenses incurred by [plaintiff] (including reasonable attorney fees) to collect amounts due and owing." The defendant argued that the specific attorney fee contract language is extinguished when a final judgment is entered on the contract, but the Court explained that entry of a judgment "does not merge a contractual right to attorneys'

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[8] 735 ILCS 5/2-1303.

fees into a judgment when the fees are 'ancillary to the primary cause of action.' "[9] Thus, because enforcing the state court judgment (even through a separate lawsuit) was "ancillary to the fees incurred in the primary proceeding," the court ruled that the plaintiff was entitled to recoup reasonable attorneys' fees incurred during the fraudulent conveyance suit.

CONCLUSION

A final judgment is often not the end of the litigation, but rather signals the beginning of a different phase in the attempt to collect the debt. By following the post judgment procedure outlined above, employing a sound post-judgment litigation strategy, and setting realistic expectations, a judgment creditor can best position itself to collect some, if not all, of the judgment amount (including post-judgment interest and attorneys' fees).

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[9] *Centerpoint Energy Servs.*, *supra* n. 7 (citing *Stein v. Spainhour*, 196 Ill. App. 3d 65, 553 N.E.2d 73, 76 (Ill. App. Ct. 1990)).