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BUSINESS RESTRUCTURING REVIEW

FOREIGN DEBTORS' FORUM SHOPPING WARRANTED STAY OF U.S. AVOIDANCE LITIGATION

Dan T. Moss and **Mark G. Douglas**

Even if a U.S. court has jurisdiction over a lawsuit involving foreign litigants, the court may conclude that a foreign court is better suited to adjudicate the dispute because either: (i) it would be more convenient, fair, or efficient for the foreign court to do so (a doctrine referred to as "*forum non conveniens*"); or (ii) the U.S. court concludes that it should defer to the foreign court as a matter of international comity. Both of these doctrines were addressed in a ruling recently handed down by the U.S. Bankruptcy Court for the Southern District of New York (the "Bankruptcy Court"). In *In re National Bank of Anguilla (Private Banking Trust) Ltd.*, 580 B.R. 64 (Bankr. S.D.N.Y. 2018), the court, on grounds of *forum non conveniens* and comity, stayed litigation commenced in a chapter 11 case by two Anguillan banks to avoid fraudulent transfers in deference to the banks' Anguillan administration proceedings and litigation pending in an Anguilla court involving the same issues. The court concluded that the debtors, whose Anguillan administrations it had previously recognized under chapter 15, had engaged in forum shopping by filing the avoidance litigation in the U.S. after: (i) commencing chapter 11 cases for that purpose; and (ii) commencing litigation in Anguilla with the same parties regarding the same transactions and nucleus of facts.

FORUM NON CONVENIENS

The doctrine of *forum non conveniens* permits a court to dismiss litigation even if the court is a proper venue with jurisdiction over the claims asserted. Application of the doctrine to dismiss a case is committed to a court's broad discretion, which may be deployed "when considerations of convenience, fairness, and judicial economy so warrant." *Magi XXI, Inc. v. Sato della Citta del Vaticano*, 714 F.3d 714, 729 n.6 (2d Cir. 2013).

Courts in the Second Circuit apply a three-step process to determine whether an action should be dismissed under the doctrine. The court must: (i) determine the degree of deference to give the plaintiff's choice of forum; (ii) determine whether an adequate alternative forum exists; and (iii) balance the private interests of the parties in pursuing litigation in the competing forums against any public interests at stake. *See Iragorri v. United Techs. Corp.*, 274 F.3d 65, 73–74 (2d Cir. 2001).

A plaintiff's choice of forum is presumed to be adequate, and the defendant bears a heavy burden in seeking to have a case dismissed on the ground of *forum non conveniens*.

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A court will accord less deference to a plaintiff's choice of forum if it appears that the selection was motivated by forum shopping, because it "is much less reasonable to presume that the choice was made for convenience." *Id.* at 71. Other factors that courts consider in determining the degree of deference include: (i) the convenience of the plaintiff's residence in relation to the chosen forum; (ii) the proximity of the chosen forum to witnesses or evidence; (iii) the defendant's amenability to suit in the chosen forum; (iv) the availability of suitable legal assistance; and (v) other matters pertaining to convenience or expense. *Id.* at 72.

COMITY

A court may also choose not to exercise jurisdiction on the basis of principles of international comity. "Comity" is "the recognition which one nation allows within its territory to the legislative, executive or judicial acts of another nation, having due regard both to international duty and convenience, and to the rights of its own citizens or of other persons who are under the protection of its laws." *Hilton v. Guyot*, 159 U.S. 113, 164 (1895).

International comity has been interpreted to include two distinct doctrines: (i) "legislative," or "prescriptive," comity; and (ii) "adjudicative comity," or "comity among courts." *Maxwell Comm'n Corp. v. Societe Generale (In re Maxwell Comm'n Corp.)*, 93 F.3d 1036, 1047 (2d Cir. 1996).

The former "shorten[s] the reach of a statute"—one nation will normally "refrain from prescribing laws that govern activities connected with another state when the exercise of such jurisdiction is unreasonable." *Official Comm. of Unsecured Creditors of Arcapita Bank B.S.C.(C) v. Bahrain Islamic Bank (In re Arcapita Bank B.S.C.(C))*, 575 B.R. 229, 237 (Bankr. S.D.N.Y. 2017).

Adjudicative comity is an act of deference whereby the court of one nation declines to exercise jurisdiction in a case that is properly adjudicated in a foreign court. *Id.* at 238. U.S. courts generally extend comity whenever a foreign court has proper jurisdiction and "enforcement does not prejudice the rights of United States citizens or violate domestic public policy." *CT Inv. Mgmt. Co., LLC v. Cozumel Caribe, S.A. de C.V. (In re Cozumel Caribe, S.A. de C.V.)*, 482 B.R. 96, 114 (Bankr. S.D.N.Y. 2012).

Because a foreign nation's interest in the equitable and orderly distribution of a foreign debtor's assets is an interest deserving respect and deference, foreign bankruptcy proceedings are one category of foreign litigation that generally mandates dismissal of parallel U.S. district court litigation under adjudicative comity. *Royal and Sun Alliance Ins. Co. of Canada v. Century Int'l Arms*, 466 F.3d 88, 92–93 (2d Cir. 2006).

In this context, deference to the foreign court is warranted "so long as the foreign proceedings are procedurally fair and . . . do not contravene the laws or public policy of the United States." *Cozumel Caribe*, 482 B.R. at 114. Courts examine a number of factors in assessing procedural fairness, including:

> (1) whether creditors of the same class are treated equally in the distribution of assets; (2) whether the liquidators are considered fiduciaries and are held accountable to the court; (3) whether creditors have the right to submit claims which, if denied, can be submitted to a bankruptcy court for adjudication; (4) whether the liquidators are required to give notice to the debtor's potential claimants; (5) whether there are provisions for creditors meetings; (6) whether a foreign country's insolvency laws favor its own citizens; (7) whether all assets are marshalled before one body for centralized distribution; and (8) whether there are provisions for an automatic stay and for the lifting of such stays to facilitate the centralization of claims.

Finanz AG Zurich v. Banco Economico S.A., 192 F.3d 240, 249 (2d Cir. 1999).

BANK OF ANGUILLA

National Bank of Anguilla (Private Banking & Trust) Ltd. and Caribbean Commercial Investment Bank Ltd. (collectively, the "debtors") were Anguillan offshore banks (i.e., banks that operated within Anguilla but served only non-Anguillan customers).

Severely stressed by the 2008 financial crisis, the debtors' parent banks were placed into conservatorship in 2013 by the regulator of Anguilla's banking system, which replaced the parent banks' boards with conservator directors pending the preparation of rescue plans.

Concluding that certain funds had been commingled between the debtors and their parent banks, the conservator directors directed the debtors to transfer approximately $23 million to U.S. accounts maintained by the parent banks. In addition, from 2013 to 2016, the directors caused the parent banks to transfer more than $210 million to the Anguillan bank regulator.

The regulator placed the parent banks into receivership in 2016 and transferred their banking operations and deposits to a newly formed bank owned by the government of Anguilla.

The Anguilla High Court (the "Anguilla Court") entered an order in February 2016 placing the operations of the debtors under administration.

In May 2016, the debtors sued the parent banks and the successor bank in the Anguilla Court, alleging that the conservator directors and the bank regulator had breached their fiduciary duties by directing the transfers to the parent banks. The Anguilla Court dismissed the action because the receivership stayed litigation against the parent banks, the debtors failed to join the conservator directors as parties, and it was unclear whether the directors were immune from suit as government employees.

Certain of the debtors' depositors raised the same allegations in separate litigation commenced in June 2016. An appeal of the Anguilla Court's ruling that the defendants were not immune from suit was still pending as of January 2018.

The administrator filed separate petitions on behalf of the debtors in May and October 2016 in the Bankruptcy Court, seeking recognition of the Anguillan administrations under chapter 15 of the Bankruptcy Code. Different bankruptcy judges entered orders recognizing the administrations as "foreign main proceedings" in June and November 2016.

Post-recognition, each debtor separately filed a chapter 11 case and commenced an adversary proceeding against its parent bank, the successor bank, and the bank regulator (collectively, the "defendants"). Both of the complaints asserted claims: (i) to avoid and recover the funds upstreamed from the debtors to the parent banks and ultimately to the successor bank as actual or constructive fraudulent transfers under the Bankruptcy Code, New York law, and Anguillan law; and (ii) to impose liability on the bank regulator for breach of fiduciary duty, gross negligence, and aiding and abetting breach of fiduciary duty.

The chapter 11 filings were necessary to implement this strategy because, pursuant to section 1521(a)(7) of the Bankruptcy Code, a foreign representative in a chapter 15 case may not assert avoidance claims under section 544 or 548 in a chapter 15 case, but can assert such claims in a case under another chapter if the debtor is eligible for relief. In addition, Anguillan law does not recognize causes of action to avoid constructive fraudulent transfers, although it does recognize claims for avoidance of transfers made with the intent to defraud creditors.

In March 2017, the debtors filed an application in the Anguilla Court for judicial review of the circumstances surrounding the transactions effected in connection with the resolution plans for the parent banks. The Anguilla Court stayed the review proceedings pending the resolution of the U.S. adversary proceedings.

The defendants moved to dismiss the adversary proceedings on the ground of *forum non conveniens*. According to the defendants, the debtors were forum shopping by asserting their claims in U.S. courts for the purpose of asserting constructive fraudulent transfer claims that could not be brought under Anguillan law. The debtors countered that many of the transfers at issue occurred in New York and that the Anguilla Court sanctioned the U.S. litigation by authorizing the foreign representatives to commence foreign proceedings on the debtors' behalf and by staying the review proceedings pending the outcome of the U.S. adversary proceedings.

Certain of the defendants also argued that the court should dismiss the adversary complaints: (i) under principles of comity; (ii) under the Foreign Sovereign Immunities Act; (iii) for lack of personal jurisdiction; (iv) because the avoidance provisions of the Bankruptcy Code do not apply extraterritorially; and (v) for failure to adequately state a claim for avoidance under sections 544 and 548 of the Bankruptcy Code.

THE BANKRUPTCY COURT'S RULING

The two bankruptcy judges presiding over the debtors' chapter 11 and chapter 15 cases issued a joint opinion directing that, under the doctrines of *forum non conveniens* and comity, the adversary proceedings be stayed in favor of the Anguillan administrations and pending adjudication of the disputes in the Anguilla Court.

According to the bankruptcy judges, the debtors' choice of forum was not entitled to any deference because it was an exercise in forum shopping—i.e., it was motivated by the desire to find a forum in which the debtors could assert claims that did not exist under Anguillan law, had been stayed by the Anguilla Court, or had been appealed.

The judges found, among other things, that: (i) the debtors were incorporated in Anguilla and conducted no significant operations in the U.S.; (ii) the defendants and the key witnesses, many of whom were not within the Bankruptcy Court's subpoena power, were incorporated or resided in Anguilla or the eastern Caribbean; (iii) the majority of the evidence was located or accessible in Anguilla, but not in the U.S.; (iv) the defendants were amenable to suit, and had in fact already been sued, in Anguilla; and (v) the Anguilla Court had a greater interest in adjudicating a dispute involving Anguillan entities and issues of Anguillan law.

In addition, the bankruptcy judges concluded that the Anguilla Court was an adequate alternative forum despite the absence of a cause of action under Anguillan law to avoid constructively fraudulent transfers because, among other things, the Anguilla Court could grant the same remedy if the debtors prevailed on similar claims which were recognized under Anguillan law.

The bankruptcy judges accordingly ruled that the adversary proceedings would be stayed, rather than dismissed, under the doctrine of *forum non conveniens*. A stay was more appropriate than dismissal, the court explained, because there might still be issues to resolve after the Anguilla Court ruled in the pending litigation.

The court also held that staying the adversary proceedings was appropriate as a matter of comity. Deference to the debtors' Anguillan administrations was appropriate, the court explained, in the absence of any assertion that the administrations were procedurally unfair. Likewise, numerous factors supported deference as a matter of comity to the Anguilla Court litigation. These included: (i) the similarities between the issues and the parties; (ii) the fact that two of the three Anguillan lawsuits were filed before the adversary proceedings; (iii) the adequacy and competency of the Anguilla Court; (iv) inconvenience of the Bankruptcy Court to the defendants; and (v) Anguilla's overriding interest in adjudicating the issues.

Because the court stayed the adversary proceedings, it declined to address the remaining issues raised by the motions to dismiss.

OUTLOOK

An indispensable feature of cross-border bankruptcy law is the ability of foreign debtors to access U.S. bankruptcy courts for the purpose of safeguarding their U.S. assets from local creditors and otherwise enlisting the U.S. bankruptcy court's assistance for the debtor's foreign bankruptcy proceeding. As noted, chapter 15 expressly permits the representative of a foreign debtor to commence a case on the debtor's behalf under another chapter of the Bankruptcy Code after the court recognizes the debtor's foreign bankruptcy proceeding. This gives the representative access to many of the powers of a bankruptcy trustee, including the ability to prosecute certain claims under U.S. federal or state law that may not exist under foreign law.

Bank of Anguilla illustrates that, although a U.S. bankruptcy court may have jurisdiction in a cross-border bankruptcy case, it may decline to exercise such jurisdiction in circumstances where the court concludes that the foreign debtor's U.S. filings amount to forum shopping. *Bank of Anguilla* also demonstrates that access to the powers of a U.S. bankruptcy trustee may be restricted if adjudication of the claims in a foreign court is more appropriate.

THIRD CIRCUIT RULES THAT TRANSFER BY NONDEBTOR IS NOT AVOIDABLE AS FRAUDULENT TRANSFER UNDER DELAWARE UFTA

Rachel Biblo Block and **Mark G. Douglas**

In *Crystallex International Corp. v. Petróleos de Venezuela, S.A.*, 879 F.3d 79 (3d Cir. 2018), a divided U.S. Court of Appeals for the Third Circuit ruled that transfers by nondebtor subsidiary corporations to their ultimate parent corporation, which was alleged to be the Republic of Venezuela's alter ego, were not fraudulent transfers under the Delaware Uniform Fraudulent Transfer Act ("DUFTA"). The panel reversed a district court ruling declining to dismiss a cause of action to recover a judgment against Venezuela by avoiding transfers of funds out of the U.S. by entities allegedly controlled by the Venezuelan government. The Third Circuit ruled that the nondebtor transfers at issue could not be deemed fraudulent transfers under the language and structure of DUFTA.

THE DELAWARE UNIFORM FRAUDULENT TRANSFER ACT

Like section 548 of the Bankruptcy Code, state laws generally patterned on the Uniform Fraudulent Transfer Act (now known as the Uniform Voidable Transactions Act) provide for the avoidance of transfers or obligations that are actually or constructively fraudulent. For example, DUFTA provides that:

> A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if *the debtor* made the transfer or incurred the obligation . . . [w]ith actual intent to hinder, delay or defraud any creditor of the debtor [or] [w]ithout receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor [is or was rendered insolvent].

DEL. CODE ANN. tit. 6, § 1304(a) (West 2018) (emphasis added).

CRYSTALLEX

Canadian mining company Crystallex International Corp. ("Crystallex") owned the rights to a gold reserve in Venezuela. In 2011, Venezuela nationalized the country's gold mines and confiscated Crystallex's rights in the gold reserve. Thereafter, Crystallex initiated an arbitration proceeding against Venezuela in the World Bank. Finding that Venezuela had violated an investment treaty with Canada, the arbitrators awarded Crystallex $1.2 billion. The U.S. District Court for the District of Columbia confirmed the arbitration award in 2017.

PDV Holding, Inc. ("PDVH") and CITGO Holding, Inc. ("CITGO Holding" and, collectively, the "defendants"), both Delaware corporations, are direct or indirect subsidiaries of Petróleos de Venezuela, S.A. ("Petróleos"), a state-owned Venezuela company. According to Crystallex, Petróleos, which is Venezuela's alter ego, caused CITGO Holding to issue $2.8 billion in debt, the proceeds of which were later paid to its parent company, PDVH, as a dividend. PDVH then transferred this sum farther up the ladder and out of the U.S. by issuing a dividend in the same amount to its own parent, Petróleos. Crystallex alleged that this series of events was carried out in order to repatriate funds to Venezuela, where they would be safe from execution by U.S. creditors.

Crystallex sued the defendants in the U.S. District Court for the District of Delaware, seeking, among other things, to avoid the loan and dividend transaction under DUFTA as a fraudulent transfer. The defendants moved to dismiss the complaint, arguing that there was no "transfer" made under DUFTA because the transaction did not involve "property of" the judgment debtor (i.e., Venezuela or its alter ego, Petróleos) and that accordingly there was no relevant transfer made "by a debtor." In particular, they contended, because neither Venezuela nor Petróleos had any direct ownership interest in the defendants' assets, no "transfer" of debtor property occurred. By contrast, Crystallex urged the court to look at the "economic reality" of the transactions, arguing that the extraction of value by Venezuela's alter ego, Petróleos, from its subsidiaries diminished the value of Petróleos' equity interest in those subsidiaries and therefore qualified as a "transfer" of a debtor's property under DUFTA.

Initially, the district court noted that the Delaware Supreme Court (Delaware's highest court) has not ruled on whether a transfer by a nondebtor can be avoided under DUFTA. For this reason, the district court explained, the federal court's role is to predict how the state court would rule.

After examining the statute and relevant case law, the district court acknowledged that Crystallex's fraudulent transfer claim "strains the statute's structure." Even so, the court ruled that because the complaint alleged that property was transferred "at the debtor's behest," it properly alleged the existence of a fraudulent transfer under DUFTA. However, although the court concluded that PDVH, as a nondebtor transferor of debtor property, was an appropriate defendant, the court dismissed CITGO Holding from the case because it was not a party to a fraudulent transfer under DUFTA and could not be held

liable as an accomplice or co-conspirator. PDVH appealed the decision.

THE THIRD CIRCUIT'S RULING

A divided three-judge panel of the Third Circuit reversed.

The Third Circuit majority looked to other Delaware state courts for guidance. In particular, the Delaware Court of Chancery ruled in both *Edgewater Growth Capital Partners v. H.I.G. Capital, Inc.,* 2010 WL 720150 (Del. Ch. Mar. 3, 2010), and *In re Wickes Trust*, 2008 WL 4698477 (Del. Ch. Oct. 16, 2008), that transfers by nondebtors cannot be avoided under DUFTA.

In addition, the Third Circuit majority noted that the Delaware Chancery Court and federal courts interpreting federal and Delaware law have also rejected fraudulent transfer claims against nondebtor transferors under the analogous provision of the Bankruptcy Code (i.e., section 548). *See Spring Real Estate, LLC v. Echo/RT Holdings, LLC*, 2016 WL 769586 (Del. Ch. Feb. 18, 2016), *aff'd*, 2016 WL 7189917 (Del. Dec. 12, 2016) (rejecting a fraudulent conveyance claim against a nondebtor subsidiary of the debtor parent company); *Brandt v. B.A. Capital Co. (In re Plassein Int'l Corp.)*, 366 B.R. 318 (Bankr. D. Del. 2007), *aff'd*, 388 B.R. 46 (D. Del. 2008), *aff'd*, 590 F.3d 252 (3d Cir. 2009) (dismissing state and federal fraudulent transfer claims because the allegedly fraudulent transfer was made by a nondebtor).

The majority underscored that Crystallex did not allege that PDVH was a debtor or otherwise liable for the judgment Crystallex obtained against Venezuela. Instead, Crystallex characterized the transfers as being *to*, rather than *by*, the debtor, a circumstance that in the Third Circuit's view DUFTA does not contemplate.

The majority rejected a broad reading of the language "by the debtor" which would encompass a nondebtor subsidiary transferor (like PDVH) because such a construction would undermine Delaware corporate law's fundamental principle that parent and subsidiary corporations are separate legal entities. In addition, on the basis of the facts alleged by Crystallex, the Third Circuit was unwilling to disregard PDVH's distinct corporate identity.

The Third Circuit majority also rejected Crystallex's arguments that DUFTA's "broad remedial purpose" required a finding that the transactions at issue were fraudulent and that, because the intent of the series of transactions was to hinder creditors, equitable considerations mandated that it be subject to avoidance under the statute. The court wrote that "having broad latitude to craft a remedy for a DUFTA violation does not necessarily mean we have broad latitude to determine what fits within the contours of the statute in the first place." Moreover, it explained, Delaware's Chancery Court (a court of equity) had the opportunity to conclude, as a matter of equity, that DUFTA covers transfers by nondebtors but has not done so.

Finally, relying on Delaware court rulings invalidating theories of non-principal or aiding and abetting liability under DUFTA, the Third Circuit majority rejected the argument that DUFTA should apply to nondebtor transfers which are "orchestrated" by a debtor.

Accordingly, the Third Circuit reversed the district court's order and remanded the case below for further proceedings.

Circuit judge Fuentes dissented, writing that the majority misconstrued the language and purpose of DUFTA as well as the case law construing it. According to Judge Fuentes:

> [T]oday the majority signals that a party, such as [PDVH], may knowingly participate in a fraudulent transfer so long as it is not a debtor. Indeed, a consequence of the majority's holding is that, under [DUFTA], a foreign sovereign—such as Venezuela—is free to fraudulently repatriate assets, so long as the party making the transfer is a non-debtor. That result does not comport with—but rather is wholly contrary to—the Act's broad remedial purpose.

On February 5, 2018, the Third Circuit denied Crystallex's motion for reconsideration.

OUTLOOK

Crystallex illustrates that, although the ability to avoid fraudulent transfers is an important tool for both creditors and bankruptcy trustees, the remedy is limited to cases where the debtor transfers property or incurs an obligation either with the intent to defraud creditors or under circumstances meeting the element of constructive fraud. According to the Third Circuit majority, even though the transactions at issue may have been fraudulent, avoidance under DUFTA was not the proper remedy for the fraud because the judgment debtor (Venezuela) did not transfer any property.

While the result is undeniably frustrating for Crystallex—and, according to the dissent, contrary to the spirit of the avoidance statute—it does not preclude other avenues of attack. For example, Crystallex could argue that, because the subsidiary transferors were alter egos or mere instrumentalities of Venezuela, they should be deemed to be the "debtor[s]" for purposes of the statute. Moreover, creditors of the U.S. subsidiary transferors could conceivably file involuntary bankruptcy cases against the subsidiaries under an alter ego theory, and federal and state law claims could be asserted in those bankruptcy cases to avoid the upstream transfers. Because the funds have already been harbored in Venezuela, recovery on such avoidance claims may be difficult.

A LESSON IN DIP FINANCING DUE DILIGENCE

T. Daniel Reynolds

The Bankruptcy Code contains an array of provisions designed to encourage lenders to provide debtor-in-possession ("DIP") financing in chapter 11 cases, including authorization of "superpriority" administrative expense claims and "priming" liens designed to ensure that DIP loans are repaid. However, as illustrated by a ruling recently handed down by the U.S. Court of Appeals for the Seventh Circuit, these provisions do not relieve a DIP lender from its obligation to perform customary due diligence regarding the terms of the loan, including the extent and value of the collateral securing it. In *Banco Panamericano, Inc. v. City of Peoria*, 880 F.3d 329 (7th Cir. 2018), the Seventh Circuit held that a DIP lender with a superpriority claim secured by a "blanket lien" on all of the debtor lessee's assets did not have a "better claim" to property which automatically reverted to the lessor upon termination of a lease.

"ALL ASSET LIENS" AND DIP FINANCING

Under the Uniform Commercial Code (the "UCC"), in order for a security interest to attach to a debtor's property, the financing statement granting the security interest must clearly describe the property. *See* UCC § 9-203(B). However, section 9-504(2) of the UCC provides that a financing statement sufficiently identifies the collateral if the financing statement states that the security interest covers "all assets." If properly perfected, such a "blanket lien" will have priority over subsequent liens and security interests, with certain exceptions, including purchase money security interests, certain mechanic's and tax liens, and *pari passu* or priming liens securing DIP financing in a bankruptcy case.

The Bankruptcy Code provides that a bankruptcy trustee or DIP may obtain unsecured credit or financing in the ordinary course of business and that the resulting claims will be treated as administrative expenses. *See* 11 U.S.C. § 364(a). In addition, the bankruptcy court may authorize the trustee to obtain non-ordinary course unsecured credit or financing with administrative expense priority. If such unsecured financing is unavailable, the court, after notice and a hearing, may authorize the trustee or DIP to obtain: (i) unsecured financing with "superpriority" over other administrative expenses; or (ii) financing secured by a lien on unencumbered assets, a junior lien on already encumbered assets, a lien on already encumbered assets equal in priority to existing liens, or a "priming" lien on already encumbered assets, so long as the existing lien holder is provided with "adequate protection." *See* 11 U.S.C. § 364(c) and (d).

PANAMERICANO

In November 1995, the City of Peoria, Illinois, signed a lease with Resource Technology Corporation ("RTC"). RTC agreed to lease land in and beneath the city's public landfill to build and

operate a gas conversion system. This system captured methane gas from beneath the landfill's surface and transported the gas through an interconnect made up of three miles of wires, pipes, and utility poles. RTC then converted the gas into electricity and sold it to the local electric utility company.

Under the lease, RTC had the exclusive right to construct, operate, and maintain the conversion system and interconnect at its own expense. In exchange, RTC paid Peoria a 6 percent royalty on its electricity sales to the local utility company.

Peoria had the right to terminate the lease if RTC abandoned the gas conversion system. The lease provided that, within 30 days of termination, Peoria could notify RTC of any structures, equipment, and below-ground installations the city wished to retain, at no cost. Post-termination, Peoria also had the option to purchase any equipment that RTC wished to sell at a mutually agreed upon price. Finally, the lease provided that "[t]itle to and ownership of any of RTC's property which is not removed within ninety (90) days after termination passes to Peoria." RTC and Peoria initially agreed to a 10-year lease term.

In 1999, creditors filed an involuntary chapter 7 case against RTC in the Northern District of Illinois. After the bankruptcy court converted the case to chapter 11, the court authorized RTC to obtain DIP financing from Banco Panamericano ("BP"). The financing order provided that BP's claims would have superpriority administrative expense priority under section 364(c)(1) of the Bankruptcy Code and that the loans would be secured "by liens and security interests in essentially all of RTC's assets." The loan agreement defined BP's collateral to include "all of the assets of the Debtor ... including, but not limited to ... landfill gas rights and collection facilities leases ... and all of the Debtor's residual right in the underlying leased property."

RTC defaulted on its postpetition loan in 2004, and the bankruptcy court lifted the automatic stay to permit BP to proceed against its collateral. However, the stay relief order excluded certain assets from being deemed collateral, namely, the "electric generation equipment and contracts to sell electricity relating to the Debtor's facilities located in ... Peoria, Illinois."

The court converted RTC's chapter 11 case to a chapter 7 case in September 2005. The chapter 7 trustee operated the company for approximately one year before beginning to liquidate RTC's assets. During this time, RTC continued to operate its Peoria gas conversion program, and the bankruptcy court authorized RTC to extend its lease with Peoria. However, methane gas collection soon dwindled, and gas conversion stopped completely.

Peoria sent a formal termination letter in February 2008, citing RTC's failure to cure certain breaches of the 1995 lease. Additionally, Peoria notified RTC that, according to the terms of the 1995 lease, the city elected to keep all of RTC's "structures" and "below-grade installations and/or improvements." Peoria asked RTC to remove any equipment that it wished to retain from the gas conversion site as soon as possible. Thereafter, Peoria began operating the system itself.

BP sued Peoria in February 2013 in federal district court, alleging that the city unjustly enriched itself "by benefiting from the structures and installations that it retained after termination of the RTC lease." The bank claimed that its superpriority lien against all of RTC's assets gave it a "better claim" than Peoria had to the structures and installations. Both the bank and the city filed cross-motions for summary judgment.

In Illinois, a plaintiff claiming unjust enrichment must "allege that the defendant has unjustly retained a benefit to the plaintiff's detriment, and that the defendant's retention of the benefit violates the fundamental principles of justice, equity, and good conscience." *HPI Health Care Servs., Inc. v. Mt. Vernon Hospital, Inc.*, 131 Ill. 2d 145, 160 (1989). In cases where a plaintiff is seeking recovery of a benefit that was transferred to the defendant by a third party, the defendant's retention of the benefit is unjust when:

> (1) the benefit should have been given to the plaintiff, but the third party mistakenly gave it to the defendant instead ..., (2) the defendant procured the benefit from the third party through some type of wrongful conduct ..., or (3) the plaintiff *for some other reason had a better claim to the benefit* than the defendant.

Id. (emphasis added).

BP argued that the "other reason" it had a "better claim to the benefit" than Peoria was that BP had a superpriority claim against and a first priority lien on all of RTC's assets, which should supersede any claim the city had on the basis of its lease with RTC.

The district court ruled against BP, holding that Peoria had the "better claim" on the basis of the terms of the lease. BP appealed to the Seventh Circuit.

THE SEVENTH CIRCUIT'S RULING

A three-judge panel of the Seventh Circuit affirmed. The Seventh Circuit panel reasoned that the 1995 lease addressed three types of property—"equipment," "structures," and "below-grade installations and/or improvements"—but gave RTC post-termination rights only in the equipment. Once the lease was terminated, the court explained, RTC "retained a

property interest in the equipment at the gas collection project" because the lease stated that RTC had the option of either removing its equipment or selling it to Peoria. However, the lease did not provide RTC with any post-termination rights in the "structures" or "below-grade installations and/or improvements"—only post-termination duties (including the duty to restore the premises and to remove any structures that Peoria chose not to retain).

According to the Seventh Circuit panel, Peoria possessed the "better claim" because the plain language of the lease made it clear that the property automatically passed to Peoria 90 days after the termination of the lease. Because RTC never possessed any additional post-termination rights in the "structures" or "below-grade installations and/or improvements," the court reasoned, it was impossible for BP to possess "greater rights to the property than originally held by RTC," even with a superpriority claim and first priority lien in bankruptcy. Therefore, the Seventh Circuit panel held that the "bank's security interest could not reach the structures and installations at Peoria's landfill."

OUTLOOK

Panamericano is a cautionary tale for DIP lenders. First, it highlights the risks of collection following a failed chapter 11 case. BP evidently sued Peoria because, after RTC's bankruptcy case was converted to a chapter 7 liquidation, the estate lacked assets sufficient to repay the DIP financing.

Second, the case illustrates the importance of careful due diligence in assessing the collateral for a DIP loan. Simply put, if the debtor does not own some of the assets used in its business (either at the outset of the DIP loan or due to divestiture pursuant to the terms of a valid contract), superpriority claims or first priority blanket liens granted in connection with DIP financing will not bring such assets into the universe of the lender's collateral.

This article was prepared with the assistance of Meredith Collier.

FROM THE TOP IN BRIEF

On April 3, 2018, the U.S. Supreme Court issued an order that, in light of its recent ruling in *Merit Management Group LP v. FTI Consulting Inc.*, 138 S. Ct. 883, No. 16-784 (Feb. 27, 2018), the Court would defer consideration of a petition seeking review of a 2016 decision by the U.S. Court of Appeals for the Second Circuit in the Tribune Co. chapter 11 case ruling that the Bankruptcy Code's "safe harbor" shielding certain securities transactions from avoidance as fraudulent transfers preempts creditors' state law constructive fraudulent transfer claims and applies to any transfer which passes through a financial intermediary, regardless of whether the banks and brokers at issue had any beneficial interest in the funds. *See In re Tribune Co. Fraudulent Conveyance Litig.*, 818 F.3d 98 (2d Cir. 2016), *petition for cert. filed*, No. 16-317 (U.S. Sept. 9, 2016).

In ruling that the safe harbor—section 546(e) of the Bankruptcy Code—protects transfers even if the financial institution is a mere conduit, the Second Circuit in *Tribune* agreed with decisions issued by the Third, Sixth, Eighth, and Tenth Circuits and disagreed with the approach adopted by the Seventh Circuit (in *Merit*) and the Eleventh Circuit.

In *Merit*, the unanimous Court held that section 546(e) *does not* protect transfers made through a financial institution to a third party, regardless of whether the financial institution had a beneficial interest in the transferred property. Instead, the relevant inquiry is whether the transferor or the transferee in the transaction sought to be avoided is a financial institution.

According to the Supreme Court's order in *Tribune*, deferring consideration of whether the Court should review the merits of the Second Circuit's decision "will allow the Court of Appeals or the District Court to consider whether to recall the mandate, entertain a Federal Rule of Civil Procedure 60(b) motion to vacate the earlier judgment, or provide any other available relief in light of this Court's decision in [*Merit*]." *See Deutsche Bank Trust Company Americas v. Robert R. McCormick Foundation*, 138 S. Ct. 1162, 2018 WL 1600841, No. 16-317 (U.S. Apr. 3, 2018). The order also states that "[t]he Court of Appeals or the District Court could decide whether relief from judgment is appropriate given the possibility that there might not be a quorum in this Court."

On May 5, 2018, the Second Circuit issued an order recalling the mandate in its *Tribune* safe-harbor decision "in anticipation of further panel review." The order neither vacates the underlying decision nor establishes a schedule for further review.

NEWSWORTHY

Scott J. Greenberg (New York), ***Carl E. Black (Cleveland)***, ***Michael J. Cohen (New York)***, ***Daniel J. Merrett (Atlanta)***, ***Stacey L. Corr-Irvine (New York)***, ***Nicholas J. Morin (New York)***, and ***Genna L. Ghaul (New York)*** were part of Jones Day's team of professionals representing M&G USA Corp. in connection with the sale of its Corpus Christi, Texas, PET-PTA (polyethylene terephthalate and purified terephthalic acid) plant, which, when completed, will be among the largest of its kind in the world. The transaction was the product of an intensive auction process, and the winning bid involved more than $1 billion in cash and other capital contributions, including an approximately $60 million purchaser-provided DIP financing to bridge the case to a closing. The purchaser was Corpus Christi Polymers LLC, a joint venture between Alpek S.A.B. de C.V., Indorama Ventures Holdings LP, and Far Eastern Investment (Holding) Ltd. The sale transaction was approved by the U.S. Bankruptcy Court for the District of Delaware, which is presiding over M&G's chapter 11 case.

Kevyn D. Orr (Washington) served as cochair of the INSOL International Annual Regional Conference held in New York City from April 29 to May 1, 2018. ***Roger Dobson (Sydney)*** will serve as one of the technical-program cochairs for the 2019 INSOL International World Conference in Singapore.

Scott J. Greenberg (New York) was featured in The Deal's list of the Top Bankruptcy Lawyers for 2017.

Jones Day was ranked for "Restructuring/Insolvency" Europe-wide, as well as in France, the Netherlands, and the United Kingdom, in *Chambers Europe* 2018.

Paul M. Green (Houston) and ***Christopher DiPompeo (Washington; Issues & Appeals)*** have been named "Rising Stars" in the field of Bankruptcy for 2018 by *Super Lawyers*.

Bruce Bennett (Los Angeles and New York), ***Brad B. Erens (Chicago)***, ***Gregory M. Gordon (Dallas)***, ***Pedro A. Jimenez (Miami and New York)***, ***Thomas A. Howley (Houston)***, ***Corinne Ball (New York)***, ***Dan B. Prieto (Dallas)***, ***Carl E. Black (Cleveland)***, ***Brett P. Barragate (New York; Banking, Finance & Securities)***, ***Heather Lennox (Cleveland and New York)***, ***Scott J. Greenberg (New York)***, ***James O. Johnston (Los Angeles)***, ***Sidney P. Levinson (New York)***, ***Mark A. Cody (Chicago)***, ***Todd R. Geremia (New York; Issues & Appeals)***, ***Beth Heifitz (Washington; Issues & Appeals)***, and ***Rachel L. Rawson (Cleveland; Banking, Finance & Securities)*** were recognized in the field of Bankruptcy for 2018 by *Super Lawyers*.

Corinne Ball (New York) and ***Alain A. Dermarkar (Dallas; M&A)*** led Jones Day's team of professionals advising Oncor Electric Delivery Company LLC in connection with its $18.8 billion total enterprise value disposition of Oncor Electric Delivery Company ("Oncor"), by which a newly formed subsidiary of Sempra Energy acquired 100 percent of the equity of reorganized Energy Future Holdings Corp. ("EFH"), and certain of its direct and indirect subsidiaries, including EFH's approximately 80 percent indirect interest in Oncor. The definitive agreement was part of an overall plan of reorganization designed to allow EFH to emerge from chapter 11.

Kevyn D. Orr (Washington) spoke on "The Background of Detroit's Decline" at the Urban Land Institute's Spring Multifamily Product Council Day, held in Detroit on May 3, 2018.

Corinne Ball (New York), ***Dan T. Moss (Washington)***, and ***Caitlin K. Cahow (Chicago)*** were part of Jones Day's team of professionals representing PAG in connection with its investment in Key Safety Systems, a subsidiary of Chinese-based Ningbo Joyson Electronics Corp, to finance the acquisition of substantially all of the global assets of Japan-based Takata Corporation out of bankruptcy in the U.S. and Japan. The deal was structured to exclude the assumption of recall, product, and other liabilities associated with the phase-stabilized ammonium nitrate (PSAN) airbag inflators manufactured by Takata. PAG acquired a minority interest in the combined operations of Key Safety Systems and Takata, which will be headquartered in Auburn Hills, Michigan, operating under the name Joyson Safety Systems.

Kevyn D. Orr (Washington) was the facilitator at the JAMS 2018 ABA Section of Dispute Resolution Spring Conference in Washington, D.C., on April 5, 2018. He mediated a discussion entitled "The Detroit Bankruptcy: The Power of Mediation."

Jones Day acted as restructuring counsel for Nissan Motor Co., Ltd, and its worldwide subsidiaries in connection with the global restructuring of Takata Corporation. Jones Day's work for Nissan included the successful: (a) assumption and transfer of Nissan's agreements and contracts with Takata related to the sale of Takata's non-airbag businesses to Key Safety Systems; (b) restructuring of Takata to continue manufacturing PSAN airbag inflators, as well as the warehousing, storage, and disposal of recalled PSAN airbag inflators; and (c) negotiation of recoveries on account of Nissan's purchase of PSAN inflators from Takata, including the allocation of recoveries paid or to be paid to the group of original equipment manufacturers. Jones Day's team included ***Pedro A. Jimenez (Miami and New York)***, ***Amanda A. Parra Criste (Miami)***, ***Isel M. Perez (Miami)***, ***Timothy Hoffmann (Chicago)***, ***Rodrigo Gómez Ballina (Mexico City; Tax)***, ***Fernando Ballesteros (Mexico City; Global Disputes)***, ***Justin A. Conway (London; Banking, Finance & Securities)***, ***Sandra-Christiane Kamper (Frankfurt; Banking, Finance & Securities)***, ***Ryan C. Thomas (Washington; Antitrust & Competition Law)***, and ***Robert W. Hamilton (Columbus)***.

On April 25, 2018, ***Ben Rosenblum (New York)***, along with U.S. bankruptcy judge Robert D. Drain, spoke on "Current Jurisdictional and Procedural Issues—*Wellness Int'l*, *Stern v. Marshall*, *Madoff, et al*." for the PLI program Bankruptcy & Reorganizations 2018: Current Developments.

An article written by ***Charles M. Oellermann (Columbus)*** and ***Mark G. Douglas (New York)*** entitled "The Year in Bankruptcy: 2017" was posted on the *Harvard Law School Bankruptcy Roundtable* on April 17, 2018.

An article written by ***Jane Rue Wittstein (New York)*** and ***Mark G. Douglas (New York)*** entitled "Fraudulent Transfer Avoidance Recovery Not Limited to Total Amount of Creditor Claims" was posted on the *Harvard Law School Bankruptcy Roundtable* on March 27, 2018.

Sidney P. Levinson (New York), ***Bruce Bennett (Los Angeles and New York)***, ***Joshua M. Mester (Los Angeles)***, ***Genna L. Ghaul (New York)***, and ***Nicholas J. Morin (New York)*** were among Jones Day's professionals representing Second Lien Noteholders of The Bon-Ton Department Stores, Inc., in connection with the purchase, through an agency agreement, of substantially all of the Bon-Ton debtors' assets. Under a joint bid among affiliates of Great American Group, Tiger Capital Group, and the indenture trustee, the assets were acquired for $780 million, consisting of a cash purchase price, a wind-down payment, and a credit bid. Following an auction that concluded on April 17, 2018, the sale transaction was approved the next day by the U.S. Bankruptcy Court for the District of Delaware, and it closed on April 19, 2018.

BUSINESS RESTRUCTURING REVIEW

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Executive Editor: Charles M. Oellermann
Managing Editor: Mark G. Douglas

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