Hearing Date: October 3, 2018 at 2:00 p.m. (prevailing Eastern Time)

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF PUERTO RICO

In re GOVERNMENT DEVELOPMENT BANK OF PUERTO RICO, Applicant.	PROMESA Title VI Case No. 18-1561
Official Committee of Unsecured Creditors for the Title III Debtors,[1] Putative Objectant, vs. The Financial Oversight and Management Board for Puerto Rico, Title VI Administrative Supervisor and Respondent.	**Re: ECF No. 59**

OBJECTION OF FINANCIAL OVERSIGHT AND MANAGEMENT BOARD FOR PUERTO RICO AS THE ADMINISTRATIVE SUPERVISOR OF THE GOVERNMENT DEVELOPMENT BOARD FOR PUERTO RICO TO THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS' NOTICE OF INTENTION TO OBJECT TO QUALIFYING MODIFICATION FOR GOVERNMENT DEVELOPMENT BANK

[1] On May 3, 2017, a voluntary petition for relief under section 304(a) of PROMESA was filed in the United States Bankruptcy Court for the District of Puerto Rico for the Commonwealth of Puerto Rico (the "Commonwealth") (Bankruptcy Case No. 17-BK-3283 (LTS)). Thereafter, Title III cases were commenced for (i) Employees Retirement System of the Government of the Commonwealth of Puerto Rico ("ERS") (Bankruptcy Case No. 17-BK-3566 (LTS)), (ii) Puerto Rico Highways and Transportation Authority ("HTA") (Bankruptcy Case No. 17-BK-3567 (LTS)), and (iii) Puerto Rico Electric Power Authority ("PREPA") (Bankruptcy Case No. 17 BK 4780 (LTS)). The Office of the United States Trustee for the District of Puerto Rico has appointed the Committee in the Title III cases of the Commonwealth, ERS, HTA, and PREPA (collectively, the "Title III Debtors").

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To the Honorable United States District Court Judge Laura Taylor Swain:

The Financial Oversight and Management Board for Puerto Rico (the "Oversight Board") in its capacity as the Administrative Supervisor in the Title VI Case regarding the Government Development Bank for Puerto Rico ("GDB") pursuant to section 601(a)(1) of the *Puerto Rico Oversight, Management, and Economic Stability Act* ("PROMESA")[1] and in its capacity as representative of the Commonwealth of Puerto Rico (the "Commonwealth") in its Title III case pursuant to PROMESA section 315(b), respectfully submits this objection (the "Standing Objection") to the *Official Committee of Unsecured Creditors' Notice of Intention to Object Regarding Purported Qualifying Modification for Government Development Bank* [ECF No. 59] (the "UCC Notice") filed by the Official Committee of Unsecured Creditors (the "UCC"), and respectfully represents as follows:

PRELIMINARY STATEMENT

1. PROMESA section 315(b) renders the Oversight Board the sole representative of each Title III Debtor. The UCC's stated intent to object to the GDB Restructuring[2] in the interest of the Title III debtors would usurp the Oversight Board's role as their sole Title III representative and is *ultra vires.* That the UCC represents claimholders of the Title III Debtors gives the UCC the same standing shareholders of a corporation have to speak for the corporation – none.

2. Through the UCC Notice, the UCC lodges another component of its efforts to derail the GDB Restructuring,[3] even though the Title III Debtors do not even have net positive claims

[1] PROMESA has been codified in 48 U.S.C. §§ 2101-2241.

[2] Capitalized terms used but not defined herein shall have the meaning given to them in the UCC Notice (defined below).

[3] *See Urgent Motion of Official Committee of Unsecured Creditors, Pursuant to Bankruptcy Code Sections 105(a) and 362, For Entry of Order Enforcing Automatic Stay and Court's June 29, 2017 Order Confirming Application of Automatic Stay With Respect to GDB Restructuring* [ECF No. 3797 in Case

against GDB in the first place.[4] As such, no actual, cognizable harm will befall the UCC's constituents as a result of the GDB Restructuring.

3. The UCC also intends to object to the Qualifying Modification because its approval triggers the releases of third parties under the GDB Restructuring Act. In doing so the UCC doubles down on its lack of standing. Not only does the UCC not represent the Title III Debtors, it does not represent GDB's creditors. Moreover, while the third party releases the UCC complains about are triggered by the effectiveness of the Qualifying Modification, they only arise under the GDB Restructuring Act. Worse yet, if GDB's creditors (which the UCC is not) sue the released parties, GDB will have to expend resources it would otherwise pay its creditors to defend and

No. 17-bk-3283] (the "UCC Stay Motion") at ¶ 3 ("The Committee generally opposes the GDB Restructuring, and will be seeking other relief related to the GDB Restructuring in both the Title III cases and the Title VI case. This motion is one of the various components of the Committee's opposition to the GDB Restructuring.).

[4] Specifically, (i) HTA owes GDB over $1.933 billion, while having a demand deposit claim of, if anything, under $33 million, (ii) the Commonwealth Treasury Department (Hacienda) owes GDB over $884 million, while its demand deposit claim was $568 million, (iii) PREPA owes GDB over $324 million because notwithstanding section 562 of the GDB Enabling Act, a minimum of approximately $324 million was withdrawn by PREPA while GDB was insolvent and, in addition, PREPA owes over $43 million for money borrowed, while its demand deposit claim is only $152 million, and (iv) ERS has a $33 million demand deposit claim against GDB for funds on deposit at GDB, which funds Act 106 of August 2017 and Joint Resolution 188 mandate to be transferred to the Commonwealth to help pay pension claims. Demand deposit amounts and liabilities for loans from GDB are taken from the GDB fiscal plan certified April 20, 2018 at pp. 37-38. We understand the Commonwealth actually owes GDB substantially more than reflected above. *See* Proof of Claim No. 29485, filed in Case No. 17-03283 (D.P.R. filed May 25, 2018) (asserting claim of not less than $2,231,033,108 by GDB against the Commonwealth); Proof of Claim No. 29533, filed in Case No. 17-03567 (D.P.R. filed May 25, 2018) (asserting claim of $2,355,974,556.98 by GDB against HTA); Proof of Claim No. 29617, filed in Case No. 17-04780 (D.P.R. filed May 25, 2018) (asserting claim of $41,357,139.80 by GDB against PREPA); Proof of Claim No. 151149, filed in Case No. 17-03567 (D.P.R. filed Jun. 29, 2018) (asserting claim of $2,355,974,556.98 by GDB against HTA).

indemnify its officers and directors.[5] The bottom line is the UCC is not simply doing more harm than good, it is doing only harm and no good – without statutory authority.

4. GDB is not a Title III debtor, and the UCC does not and cannot represent GDB creditors.[6] Moreover, the UCC, which is created by Title III, is limited to taking actions within the Title III Cases for which it has been appointed. It has no mandate or standing to appear or be heard in the Title VI Case (which is independent and outside of the Title III Cases) and certainly cannot assert the Title III Debtors' rights. It is likely for this reason that the UCC has sought to use its standing within the Title III cases to block the GDB Restructuring by purporting to enforce the Title III stay. *See* UCC Stay Motion [ECF No. 3797 in Case No. 17-bk-3283].

5. Despite being acutely aware that the issue of standing "will be an important threshold issue in this action," and that it anticipates "an objection to the Committee's standing will be forthcoming," (Procedures Objection at 1-2) [ECF No. 69 in Case No. 18-cv-1561], the UCC makes no more than a passing attempt to justify its standing on the naked grounds that the GDB Restructuring implicates the Due Process Clause of the Fifth Amendment. This argument stumbles out the gate. The UCC is a statutory vehicle for representing its constituents *within* Title III. The UCC's assertion that it has standing under the Due Process clause is preposterous. The Due Process clause does not grant a statutory creditors' committee created to represent interests of claimholders of Title III Debtors extra powers to represent creditors of a Title VI debtor, including the Title III debtors themselves.

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[5] *See*, P.R. Act No. 17-1948, Government Development Bank for Puerto Rico Enabling Act (the "GDB Enabling Act"), § 18 (indemnifying GDB directors, officers, and employees for actions taken or not taken in good faith in their capacity and authority).

[6] The Title VI Case concerns GDB's financial debt and provides for a Qualifying Modification to restructure that debt. The UCC does not represent GDB bondholders who will be subject to the Qualifying Modification. The UCC, by definition, does not hold any claim, and is not a GDB bondholder.

6. The UCC's intended objections fail to assert any direct claims it or its constituents have against the GDB. The reason for this is obvious: the UCC's constituents are no more than a creditors of a creditor of GDB (which, in this case, happen to be net debtors to the GDB). Its interest in the GDB Restructuring is derivative of the interests of the Title III Debtors. Such interest is insufficient to establish standing.

7. The UCC appears to hang its Due Process standing assertion on a misreading of PROMESA that the Qualifying Modification will have a binding and conclusive effect on the unsecured creditors of the Commonwealth. This is not true: PROMESA binds the creditors of the "Issuer" (*i.e.* GDB), and not the creditors of the territorial government (*i.e.* the Commonwealth).

8. The UCC is unable to articulate any Fifth Amendment claim. The supposed "property" of its constituents are the alleged unsecured claims the Title III Debtors may have against GDB. If the GDB Restructuring has any effect on claimholders of the Title III Debtors, it will be a function of their recoveries on their claims against the Title III Debtors, which will remain intact and untouched. Courts have consistently held that actions by a debtor that may affect unsecured claimholder recoveries do not implicate the Fifth Amendment.[7]

9. Absent the ability to assert their standing directly, the framing of the UCC's intended objections indicate it may attempt to assert the rights of the Title III Debtors vis-à-vis GDB. By doing so, the UCC would seek to invade the Oversight Board's exclusive role as representative of the Title III Debtors and the only entity charged with ensuring the Commonwealth and its instrumentalities achieve fiscal responsibility and access to the capital markets. PROMESA § 101(a). The UCC would need to obtain a derivative standing order from

[7] *See, e.g. In re Varanasi*, 394 B.R. 430, 438 (Bankr. S.D. Ohio 2008) ("[u]nsecured creditors do not have interests in any of a debtor's property prior to the debtor filing bankruptcy," but rather "simply a right to collect payment from the debtor.").

the Title III Court to pursue causes of action on behalf of the Title III Debtors in the Title VI. However, as discussed below, in Title III, causes of action are property of the debtor, and the Court, absent authorization in PROMESA, cannot issue an order interfering with property of the debtor unless the Oversight Board consents pursuant to PROMESA section 305.

10. But even if the Court were able to consider the UCC's request for derivative standing, the only provision in PROMESA that permits a type of derivative standing is Bankruptcy Code section 926. This provision only enables standing for a very limited category of claims, i.e. avoidance claims, and the UCC's intended objections do not fit within this scope. Section 926 is the section that sets the rule. Thus, the UCC has no standing and no ability to procure derivative standing.

BACKGROUND

I. The Title III Cases.

11. On June 30, 2016, the Oversight Board was established under PROMESA § 101(b). Pursuant to PROMESA § 315(b), "[t]he Oversight Board in a case under this title is the representative of the debtor" and "may take any action necessary on behalf of the debtor to prosecute the case of the debtor, including filing a petition under section 304 of [PROMESA] . . . or otherwise generally submitting filings in relation to the case with the court."

12. On May 3, 2017, the Oversight Board issued a restructuring certification pursuant to PROMESA §§ 104(j) and 206 and filed a voluntary petition for relief for the Commonwealth pursuant to PROMESA § 304(a), commencing a case under title III thereof.

13. Thereafter, Title III cases were commenced for (i) ERS (Case No. 17-BK-3566 (LTS)), (ii) HTA (Case No. 17-BK-3567 (LTS)) and (iii) PREPA (Case No. 17-BK-4780 (LTS)).

14. On June 15, 2017, the Office of the United States Trustee for the District of Puerto Rico (the "U.S. Trustee") filed a *Notice of Appointment of Official Committee of Unsecured*

Creditors in the Commonwealth of Puerto Rico [ECF No. 338 in Case No. 17-cv-3283]. The U.S. Trustee subsequently appointed the Committee in the Title III cases of the ERS, HTA, and PREPA.

II. The GDB Restructuring.

15. Concurrently with the commencement of the Title III Cases, on May 15, 2017, the GDB, the Puerto Rico Fiscal Agency and Financial Advisory Authority ("AAFAF"), and certain supporting creditors entered into a Restructuring Support Agreement (the "RSA") concerning GDB's financial obligations to its creditors.

16. On July 12, 2017, the Oversight Board certified the RSA as a "Voluntary Agreement" under PROMESA § 104(i)(1) and as a Qualifying Modification pursuant to PROMESA § 601(g)(2)(A).

17. On August 24, 2017, the Governor of Puerto Rico signed Act 109-2017, the GDB Restructuring Act, into law.

18. On May 8, 2018, the Oversight Board recertified the RSA as amended on October 20, 2017, December 20, 2017, March 20, 2018, and April 6, 2018, pursuant to PROMESA § 104(i)(1).

19. On August 10, 2018, GDB and AAFAF commenced a case under PROMESA Title VI by filing an application with the United States District Court for the District of Puerto Rico (the "Title VI Court") to approve the Qualifying Modification pursuant to PROMESA § 601(m)(1)(D) [ECF No. 1 in Case No. 18-cv-1561] (the "Title VI Case").

20. On August 22, 2018, the UCC filed in the Title VI Case the *Official Committee of Unsecured Creditors' Notice of Intention to Object Regarding Purported Qualifying Modification for Government Development Bank* [ECF No. 59 in Case No. 18-cv-1561] ("UCC Notice"). Pursuant to the Title VI Court's order, GDB and AAFAF must file any objections related to the

standing of a party to object to the Qualifying Modification on or before 5:00 p.m. AST on September 1, 2018. [ECF No. 29 in Case No. 18-cv-1561].

21. On the same day the UCC filed the UCC Notice, the UCC filed the *Urgent Motion of Official Committee of Unsecured Creditors, Pursuant to Bankruptcy Code Sections 105(a) and 362, for Entry of Order Enforcing Automatic Stay and Court's June 29, 2017 Order Confirming Application of Automatic Stay With Respect to GDB Restructuring* in the Commonwealth's Title III Case. [ECF No. 3797 in Case No. 17-bk-3283] (the "UCC Stay Motion").

22. On August 24, 2018, the UCC filed in the Title VI Case the *Official Committee of Unsecured Creditors' Objection to Motion for an Order Approving Procedures and Setting Schedule for Approval of Qualifying Modification for Government Development Bank for Puerto Rico* [ECF No. 69 in Case No. 18-cv-1561] (the "Procedures Objection").

ARGUMENT

23. The UCC cannot object to the Qualifying Modification because it lacks standing in the Title VI Case. *First*, the UCC represents claimholders of Title III Debtors, not the Title III debtors themselves, and its mandate does not extend beyond the Title III Cases for which it is appointed—it cannot engage in activities independent and outside of such cases. *Second*, the UCC cannot assert the individual claims of its constituents, including supposed Fifth Amendment rights, and even if it could, courts have consistently held that the reduction of a recovery of an unsecured claim is not protected by the Fifth Amendment. *Third*, the UCC's intended objections demonstrate the UCC is attempting to exercise derivative standing of the Title III Debtors, without any court order granting it such standing to represent the Title III Debtors in the Title VI case. As a representative of claimholders of Title III Debtors which are net debtors of GDB, the UCC has no direct standing and is confined to seeking derivative standing—something the Court is precluded from granting under PROMESA section 305 absent Oversight Board consent. Thus, even if the

Title III Debtors were net creditors of GDB, the UCC would have no better entitlement to derivative standing.

I. The UCC Lacks Independent Standing to Object to the Qualifying Modification

A. The UCC's Mandate is Confined to Activities in the Title III Cases

24. The UCC, as purely a creature of the Title III Cases, has no statutory authority to act in the Title VI Case because such proceeding is independent and outside the Title III Cases for which it has been appointed.

25. The UCC was appointed in the Title III Cases pursuant to Bankruptcy Code section 1102, as incorporated into Title III through PROMESA section 301. Bankruptcy Code section 1103(c) defines the entire universe of actions that a statutory creditors' committee may engage in during the course of a bankruptcy case:

> A committee appointed under section 1102 of this title may—
>
> > (1) consult with the trustee or debtor in possession concerning the administration of the case;
> >
> > (2) investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business and the desirability of the continuance of such business, and any other matter relevant to the case or to the formulation of a plan;
> >
> > (3) participate in the formulation of a plan, advise those represented by such committee of such committee's determinations as to any plan formulated, and collect and file with the court acceptances or rejections of a plan;
> >
> > (4) request the appointment of a trustee or examiner under section 1104 of this title;[8] and
> >
> > (5) perform such other services as are in the interest of those represented.

11 U.S.C. § 1103(c).

[8] Bankruptcy Code section 1104 is not applicable in PROMESA.

26. No provision in section 1103(c) permits the UCC to engage in litigation independent and outside of the bankruptcy case. Indeed, provisions (1)-(4) specifically limit the UCC to activities that necessarily occur within the bankruptcy proceeding which spawned the committee (e.g. consulting with a trustee or debtor in possession concerning administration of the case).[9] The UCC may assert section 1103(c)(5) grants it authority to object to GDB's Qualifying Modification, but that is demonstrably wrong because services "in the interest of those represented" cannot include usurping the Oversight Board's exclusive statutory role as sole representative of each Title III Debtor. Put differently, if section 1103(c)(5) allows the UCC to step into the Title III Debtors' shoes as alleged creditors of GDB, then the UCC might as well take over representation of GDB itself and repudiate the Qualifying Modification. Both those roles of the UCC could theoretically be described as actions "in the interest of those represented" by the UCC. But, both those roles require the UCC to take on the powers and status of either the Title III Debtors or GDB itself. That is the proof that section 1103(c)(5) is not the UCC's salvation.

27. Even though courts have acknowledged that section 1103(c)(5) permits a committee to take an active role in many important matters within the bankruptcy case,[10] they have nonetheless placed limits on the scope of this provision.[11] For example, although it might be

[9] As observed by the court in *In re Dow Corning Corp.*, "[e]ach of these powers relates to actions which intimately involve the core of the reorganization process; and without the existence of a chapter 11 case, these powers would be meaningless." 199 B.R. 896, 902 (Bankr. E.D. Mich. 1996).

[10] *Official Unsecured Creditors' Comm. v. Stern (In re SPM Mfg. Corp.)*, 984 F.2d 1305, 1315 (1st Cir.1993) (not contested that creditors' committee had authority, per § 1103(c)(5), to enter contract with secured creditor concerning further distribution of proceeds paid by estate to secured creditor); *Creditors' Comm. v. Parks Jaggers Aerospace Co. (In re Parks Jaggers Aerospace Co.)*, 129 B.R. 265, 267 (M.D. Fla.1991) (creditors' committee can have standing to act after confirmation of a chapter 11 plan but before its consummation).

[11] *Assured Guar. Corp. v. Fin. Oversight & Mgmt. Bd. for P.R. (In re Fin. Oversight & Mgmt. Bd. for P.R.)*, 872 F.3d 57, 64 (1st Cir. 2017) ("The precise scope of the UCC's intervention is a matter committed to the district court's 'broad discretion.'. . . Courts have exercised that discretion to limit the participation of intervenors as of right in a number of ways.")

in the best interests of the estate to sell an asset, an official committee cannot usurp the power of management (trustee or debtor-in-possession) to make that choice. *See In re Calvary Temple Evangelistic Ass'n,* 47 B.R. 520 (Bankr. D. Minn. 1984). Importantly, courts have determined that a statutory committee's powers under § 1103(c)(5) do not extend to activities either taken or to be taken outside of the case itself, even where the specified actions are broadly in interest of the committee's constituents. *See In re Johns–Manville Corp.*, 52 B.R. 879, 884 (Bankr. S.D.N.Y. 1985) (explaining that "[w]hile § 1103 contemplates a committee taking an active role in the reorganization proceedings, it does not grant a committee blanket authority to represent its constituency in matters outside and independent of the bankruptcy case."), *aff'd,* 60 B.R.892 (S.D.N.Y. 1986), *rev'd on other grounds*, 801 F.2d 60 (2d Cir. 1986).

28. In assessing the scope of section 1103(c)(5), the bankruptcy court in *In re Dow Corning Corp.* observed that if the provision were interpreted as permitting an official committee to do anything that is "in the interest of" its constituency then § 1103(c)(1)–(4) would become unnecessary and meaningless. 199 B.R. 896, 899 n.3 (Bankr. E.D. Mich. 1996). The court applied *ejusdem generis*—a well-settled canon of statutory construction meaning "of the same kind, class, or nature,"—which provides that "where general words follow specific words in a statutory enumeration, the general words are construed to embrace only objects similar in nature to those objects enumerated by the preceding specific words." *Official Comm. of Tort Claimants v. Dow Corning Corp. (In re Dow Corning Corp.)*, 142 F.3d 433 (6th Cir. 1998). Because Paragraphs (1)-(4) all relate to activities within the bankruptcy case, paragraph (5) must similarly be limited to actions within the proceeding. 199 B.R. at 899-900. On this basis, the bankruptcy court concluded that "[w]hile the limits of § 1103(c)(5) are not precisely defined, there is a clear line of separation between the ability of a creditors' committee to act within the bankruptcy case and the ability to

act independent of and outside the case. And this line of separation is reasonable." *Id.* at 902. The Sixth Circuit, agreeing with the bankruptcy court's invocation of *ejusdem generis* as an interpretative aid, affirmed its holding as the "rational conclusion." 142 F.3d 433.

29. Moreover, the UCC's authority to appear in Title III cases is derived from Bankruptcy Code section 1109(b), which provides that "[a] party in interest, including . . . a creditor's committee . . . may raise and may appear and be heard on any issue *in a case under this chapter*." 11 U.S.C. § 1109(b) (emphasis added). Thus, section 1109(b) underscores that the UCC's ability to appear is limited to the Title III Cases for which it is appointed.

30. Accordingly, aside from the UCC being unauthorized by anything to usurp the Oversight Board's role as representative of the Title III debtors, because the Title VI Case is independent of the Title III Cases for which the UCC has been appointed, the UCC lacks standing to object to the Qualifying Modification.

B. The GDB Restructuring Does Not Implicate Direct Rights of the UCCs' Constituents

31. Even if the UCC had the authority to operate outside the Title III Cases (and it does not), it would still lack standing to assert its objections to the Qualifying Modification. The UCC is not a creditor of the GDB or the Title III Debtors. Nor does it represent the unsecured creditors of the GDB. It is merely a creature of the Bankruptcy Code authorized to give voice to the Title III Debtors' unsecured claimholders as a whole within the Title III Cases.[12] The UCC has no assets

[12] *In re Drexel Burnham Lambert Grp., Inc.*, 138 B.R. 717, 722 (Bankr. S.D.N.Y.), *aff'd*, 140 B.R. 347 (S.D.N.Y. 1992) ("Counsel for the ... committee do not represent any individual creditor's interest in [a] case; they were retained to represent the entire ... class. Therefore, counsel for the creditors' committee do not owe a duty to [one creditor] to maximize its interest at the expense of the remaining creditors in the represented class.") (alterations in original) (citing *Matter of Levy*, 54 B.R. 805, 807 (Bankr. S.D.N.Y. 1985)); *In re W.R. Grace & Co.*, 475 B.R. 34, 204 (D. Del. 2012) ("it is established that a Creditor's Committee owes a fiduciary duty to the unsecured creditors as a whole, not to the individual members") (citing In re Kensington Int'l Ltd., 368 F.3d 289, 315 (3d Cir. 2004)).

or liabilities and it cannot assert or control its constituents' individual claims nor their constitutional rights outside a bankruptcy case and against non-debtors.[13] Indeed, the UCC's role as a representative and not as the owner of claims is particularly important here. As explained above, the UCC's antics here are not designed to help anyone. If it objects to the releases of third parties, it will cause GDB to expend resources defending and indemnifying certain third parties entitled to such rights against GDB, and creditors of GDB will obtain less. If the UCC objects to the Qualifying Modification on behalf of the Title III Debtors, it will not help those debtors because they are net debtors to GDB. In other words, the UCC's intended acts would not help its constituency.

32. In addition to being unable to assert or control its constituents' claims, the UCC has not articulated any *direct* claims creditors in the Title III Cases have against GDB. In the UCC Notice, the UCC lists a number of bases for its intended objection. Each of the bases fails to demonstrate how the rights of the unsecured claimholders the UCC represents are directly (as opposed to indirectly or derivatively) implicated by the Qualifying Modification. As such, the UCC's logic is that, by affecting the property of certain Title III Debtors, the amount unsecured claimholders recover on their claims may be altered.

33. Such an argument underscores that the UCC cannot satisfy the prudential standing requirement, which requires a claimant to demonstrate that its claims are premised on its own legal rights (as opposed to those of a third party). *Latin Am. Music Co. v. Archdiocese of San Juan of the Roman Catholic & Apostolic Church*, 499 F.3d 32, 46 (1st Cir. 2007) ("[A] party generally

[13] *In re Residential Capital, LLC*, 480 B.R. 550, 559 (Bankr. S.D.N.Y. 2012) ("Indeed, a committee cannot advocate on behalf of individual constituents for policy as well as practical reasons—if a [] Committee was appointed for such a purpose, '[n]either the committee nor its lawyers could function if each constituent was a client.'") (citing *In re The Circle K Corp.*, 199 B.R. 92, 99–100 (Bankr. S.D.N.Y. 1996), *aff'd*, No. 96 CIV. 5801, 1997 WL 31197 (S.D.N.Y. Jan. 28, 1997)).

must assert his own legal rights and interests, and cannot rest his claim to relief on the legal rights or interests of third parties.") (quoting *Kowalski v. Tesmer*, 543 U.S. 125, 129 (2004)). Here, the UCC cannot demonstrate that its intended objections are premised on its own claims because (1) it does not own or control any of its constituents' claims and (2) its constituents are at most creditors of a creditor (*i.e.* the Title III Debtors) whose claims are derivative of the Title III Debtors. Indeed, this Court has recognized that a creditor of a creditor does not have prudential standing to intervene where it had no direct relationship to the funds at issue between the creditor and debtor. *See BNYM v. COFINA (In re Fin. Oversight & Mgmt. Bd. for P.R.)*, 301 F. Supp. 3d 306, 312 (D.P.R. 2017).

34. The UCC Notice reveals that none of the intended objections are direct claims of the UCC's constituents, and, at best, are derivative of the Title III Debtors' rights:

- The first objection the UCC intends to assert involves numerous supposed violations of statutes. For example, it claims that the GDB Restructuring, by allegedly "giving all assets to a sub-set of unsecured creditors while leaving other unsecured creditors [*i.e.* the Title III Debtors] with no assets to satisfy their claims" violates the Fifth and Fourteenth Amendments to the U.S. Constitution and the Due Process Clause of the Puerto Rico Constitution. UCC Notice at 2-3. Thus, the UCC acknowledges that its constituents are only affected *derivatively* by the GDB Restructuring, *i.e.* the GDB Restructuring affects property rights of certain Title III debtors which could then impact the assets available for their unsecured claimholders to satisfy their claims.

- The UCC further claims that the GDB Restructuring Act violates the Bankruptcy Clause and Contracts Clause of the U.S. Constitution and section 303(1) of PROMESA because it is a moratorium law that binds non-consenting creditors. *Id.* at 3. But without showing that the GDB Restructuring Act directly implicates its constituents' rights or property, the UCC does not have a cognizable Article III injury.[14]

[14] *See Steel Co. v. Citizens for a Better Env't*, 523 U.S. 83, 107 (1998) ("[A]lthough a suitor may derive great comfort and joy from the fact that the United States Treasury is not cheated, that a wrongdoer gets his just deserts, or that the Nation's laws are faithfully enforced, that psychic satisfaction is not an acceptable Article III remedy because it does not redress a cognizable Article III injury.").

- The UCC also intends to assert that "[c]ash that the Commonwealth and other Title III Debtors transferred to GDB from the public fisc is not GDB's property…and cannot be confiscated by GDB to pay certain of its creditors at the expense of the Title III Debtors and their creditors." *Id.*. Here, the "cash" that is the subject of this objection belongs to the Commonwealth and other Title III Debtors, and not the claimholders of the Title III Debtors. The UCC lacks a direct interest in the cash as any of its constituents' interests are derivative of each Title III Debtor's interest. In the same vein, the UCC also intends to object to "any effort by GDB to shift liability for federal funds on deposit" to the Commonwealth. *Id.* Again, the UCC is urging the interests of creditors of a purported creditor.

- The UCC also intends to object to the extent the GDB Restructuring "seeks to modify any rights that the Title III Debtors or the unsecured claimholders of the Title III Debtors may have against GDB or persons acting on behalf of GDB, including, but not limited to, claim against current and former officers, directors, and employees of GDB." *Id.* at 3-4. To the extent the UCC objections based on the "rights of the Title III Debtors," such an objection would require derivative standing. Further, as explained below, the Qualifying Modification does not and cannot bind creditors of the Title III Debtors.[15]

C. The Due Process Clause of the Fifth Amendment is Inapplicable

35. The only ground for standing the UCC raises is the naked assertion that it has standing to appear and be heard under the Due Process Clause of the Fifth Amendment. Procedures Objection at 1-2. Such argument is curious because the UCC does not own any "property," it cannot assert or control the individual claims of its constituents (including their supposed "property" rights), and the GDB Restructuring has no bearing on the claims of unsecured claimholders of the Title III Debtors—if it has any impact, it would be confined to the recoveries on those claims.

36. As a preliminary matter, the UCC appears to base its assertion of standing on a misinterpretation of the effects of PROMESA section 601(m)(2). The UCC cites PROMESA

[15] While the Title III Qualifying Modification include releases, those releases are mutual and consensual (i.e. contractual in nature). The releases the UCC actually complains about are a function of the GDB Restructuring Act, not the Qualifying Modification, and therefore the UCC would need to challenge the statute itself. The Title VI Case is not the appropriate venue for such challenge. And, as explained above, if the releases are not granted, GDB will have indemnity liabilities that reduce creditor recoveries.

section 601(m)(2) for the proposition that the GDB Restructuring will be "full, final, complete, binding, and conclusive as to the territorial government Issuer, other territorial instrumentalities of the territorial government Issuer, and any creditors of such entities." *Id*. On the basis of this language, the UCC concludes that "any Title VI approval order entered by this Court will have preclusive and binding effect on the *unsecured creditors of Puerto Rico.*" Procedures Objection, at 2 n.3 (emphasis added). However, such interpretation in incorrect. The "territorial government Issuer" is not the Commonwealth in this instance, but rather GDB as the issuer of the bonds subject to the Qualifying Modification. *See* Section 601(a)(8)(defining "Issuer" as the Territory Government Issuer or an Authorized Territorial Instrumentality, as applicable). The UCC reaches this faulty conclusion by defining Issuer as the "Territorial Government Issuer" (*see id.*), *i.e.* the Government of Puerto Rico, when the applicable definition in this instance is Authorized Territorial Instrumentality, *i.e.* GDB.

37. Because the GDB Restructuring does not have a conclusive and binding effect on the unsecured claimholders of the Title III Debtors, the UCC cannot assert a Due Process Clause violation. Put another way, because the Qualifying Modification does not affect any of the direct property interests of the unsecured claimholders of the Title III Debtors, there is no taking or deprivation of property to base standing on. To extent the UCC argues that the GDB Restructuring has a binding and conclusive effect on Title III Debtors' property, they are inappropriately attempting to assert rights belonging to the Title III Debtors and not those of its constituents.

38. To extent the UCC attempts to assert it has standing on account of its constituents' "property" rights, such argument is without merit. Unsecured claimholders do not possess a Fifth Amendment right to receive a certain percentage recovery from a debtor on account of their claims, and cannot complain, on the basis of the Fifth Amendment, if a debtor takes actions which impair

their anticipated recovery. For example, in *In re Garland Corp.* the debtor's unsecured creditors' committee challenged the debtor's use of previously unencumbered assets as collateral for postpetition operating loans, when the debtor had already burnt through millions in postpetition financing and continued to operate at a loss. 6 B.R. 456, 458-460 (B.A.P. 1st Cir. 1980). The committee was concerned "the satisfaction of unsecured claims may be delayed, diminished or rendered impossible as a result of the authorization," *id.* at 461, and contended such a result would violate their asserted 'property rights' under the Fifth Amendment. *Id.* at 462. The Bankruptcy Appellate Panel for the First Circuit disagreed. The court pointed out it had not been shown "any authority for the proposition that holders of unsecured claims possess constitutionally protected substantive rights in property of the estate of a reorganization debtor." *Id.* The Bankruptcy Code could "extinguish[] the recovery rights of holders of unsecured claims, because an unsecured claim confers no right in specific property of the obligor." *Id.* at 462-63.

39. Similarly, in *In re Delta Financial Services, Inc.*, No. 89-35552, 1990 U.S. App. LEXIS 22109 (9th Cir. Dec. 18, 1990), the debtor sought approval of two settlements containing indemnification provisions. The unsecured creditors' committee objected, arguing the settlements violated the unsecured creditors' "substantive due process" rights as they "would reduce the amount of assets held by [the debtor] available to pay off creditors." *Id.* at *14. The Ninth Circuit rejected this claim, holding that it "lack[ed] merit" because "[a]n unsecured claim confers no rights in specific property of the obligor" and "[t]he committee cannot claim an interest in specific funds [the debtor] would use" to pay the indemnities. *Id.*

40. Indeed, the jurisprudence makes pellucid the fact unsecured claimholders have no substantive rights under the Fifth Amendment to specific treatment in a bankruptcy (or similar) proceeding. *See, e.g., Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555, 588-90 (1935)

(noting that only a secured creditor with "substantive rights in specific property" is substantively protected by the Fifth Amendment in bankruptcy as "the position of a secured creditor, who has rights in specific property, differs fundamentally from that of an unsecured creditor, who has none"); *In re Varanasi*, 394 B.R. 430, 438 (Bankr. S.D. Ohio 2008) (holding "[t]he [unsecured] creditors in this case do not have any vested rights in specific property nor possess any of the interests described in and protected by the Fifth Amendment."); *Credit All. Corp. v. Dunning-Ray Ins. Agency* (*In re Blumer)*, 66 B.R. 109, 114 (B.A.P. 9th Cir. 1986) ("Unsecured creditors have no rights to substantive due process since an unsecured claim confers no rights in specific property of the obligor."); *Commonwealth Nat'l Bank v. United States* (*In re Ashe*), 712 F.2d 864, 867, 869 (3d Cir. 1983) (rejecting claim "predicate[d]" on the due process clause of the Fifth Amendment as creditor was not a secured creditor with substantive rights in specific property); *Bank of N. Y. v. Treco (In re Treco)*, 240 F.3d 148, 161 (2d Cir. 2001) (holding unsecured claims are "not 'property' for purposes of the Takings Clause."). Indeed, if a statutory committee had independent standing by dint of the Due Process rights of its constituents, there would be no reason for section 1109 to confer it standing to appear and be heard within the bankruptcy cases for which it has been appointed.

41. As such, the UCC's claims to possess standing under the Fifth Amendment on account of the proposed treatment of Title III Debtors' unsecured claims in the Title VI modification must be rejected.

II. The UCC Cannot Assert Rights Belonging to Title III Debtors

42. The UCC's attempt to derail the GDB Restructuring amounts to an effort to control what the Commonwealth can and cannot do with its property (including its intergovernmental claims). There is no statutory authority under PROMESA or otherwise, nor does the UCC cite

any, that grants the UCC such right. In the absence of the applicability of Bankruptcy Code section 363, and in light of PROMESA's protection of governmental and political powers, the Commonwealth and other Title III Debtors are entitled to use their net positive unsecured claims against GDB (if they had any, which they do not) to facilitate repayment of bondholders in their discretion.

A. The Commonwealth Retains Discretion Over the Use of Its Property

43. The Commonwealth and its instrumentalities, are endowed, subject to the limitations detailed in PROMESA, with the sovereign authority to utilize their property as they deem fit. Congress specifically reserved to the Commonwealth the power to exercise political and governmental powers subject to the Oversight Board's authority. PROMESA § 303. As this Court knows, Congress found "a fiscal emergency in Puerto Rico" that required "[a] comprehensive approach" for Puerto Rico "to restructure debts in a fair and orderly process." PROMESA § 405(m). The GDB Restructuring and Title VI application are a valid exercise of the Commonwealth's power to redress Puerto Rico's fiscal emergency. The GDB Restructuring Act articulates the Commonwealth's governmental and political determination to trade the Title III debtors' demand deposit claims for reductions in the amounts they owe GDB. Indeed, the Puerto Rico Legislature passed the GDB Restructuring Act after making the following findings:

- it "has a public purpose and is in the best interests of the people of Puerto Rico,"
- "is fair and equitable for all creditors of GDB,"
- "is necessary to ensure compliance with the GDB Fiscal Plan,"
- "achieves fiscal responsibility for the people of Puerto Rico by providing for an orderly restructuring of the liabilities of GDB,"
- "settles and resolves potential claims between GDB and other Government Entities," and

- "permits the provision of essential public services by the Government of Puerto Rico and Other Government Entities."

To the extent the GDB Restructuring Act includes anything inconsistent with certified fiscal plans or budgets, the FOMB would exercise appropriate remedies. But, the statute's support of the GDB qualifying modification is not inconsistent. The UCC might have a different economic point of view as to the appropriate disposition of the GDB. That difference, however, is a difference over policy, and one which the Commonwealth (with the Oversight Board's supervision), and not the UCC, is empowered to determine.

44. Here, the Title III Debtors and the Oversight Board have all agreed to the disposition of their property under the GDB Restructuring. The Governor, GDB, and AAFAF together negotiated the consensual solution memorialized in the RSA. The Legislature consented to the agreement and established the legislative framework for implementing it. And the Oversight Board consented to the GDB Restructuring when it certified the Qualifying Modification and the GDB Fiscal Plan.

45. The structure of Title III further underscores that the UCC is not empowered to second guess a Title III Debtors' use of its property. Section 363 of the Bankruptcy Code, which requires court approval, after notice and hearing, for uses of property outside the ordinary course, is not incorporated into PROMESA. The inapplicability of section 363 thereby deprives the UCC of any rights to challenge the Title III debtors' governmental and political judgments about the use of their property. In any event, section 305 bars orders permitting the UCC to interfere with the Title III Debtors' property, even if failure to do so could adversely impact the Title III Debtors. *See In re City of Stockton*, 486 B.R. 194, 198 (Bankr. E.D. Cal. 2013) (Section 904 precludes a

bankruptcy court from preventing a government debtor from using its property, even "in a manner that disadvantages other creditors.").[16]

B. The Court Should Not Empower the UCC to Interfere with the GDB Qualifying Modification or the GDB Restructuring Act

46. As demonstrated above, the UCC lacks standing in its own capacity to appear in the Title VI Case and to object to the Qualifying Modification. The framing of the UCC's intended objections, however, indicate that it intends to inappropriately assert the rights of the Title III Debtors.

47. The UCC's attempt to step into the shoes of the Title III Debtors to pursue its intended objections is foreclosed by PROMESA. Only the Oversight Board may assert causes of action belonging to the Title III Debtors, which constitute property of the debtor.[17] Through PROMESA section 315(b), Congress expressly rendered the Oversight Board the representative of each Title III Debtor. Moreover, under PROMESA section 301(c)(7), the Oversight Board serves as the "trustee" of the Title III Debtors for purposes of the Bankruptcy Code sections incorporated into Title III (with the exception of Bankruptcy Code section 926, discussed below).

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[16] *See also Assured Guar. Corp. v. Commonwealth of P.R. (In re Fin. Oversight & Mgmt. Bd. for P.R.),*, 582 B.R. 579, 598-99 (D.P.R. 2018) (dismissing claim seeking declaration that funds in HTA Reserve Accounts belonged to HTA bondholders because "PROMESA Section 305's prohibitions on interference with Debtor property interests, revenues and use and enjoyment of income-producing property deprive this Court of power to interfere with the Debtors' dealings with the Reserve Fund property."); *In re Sanitary & Improvement Dist. No. 7*, 96 B.R. 967, 972 (Bankr. D. Neb. 1989) ("The debtor is free to use its property and the bankruptcy court cannot approve or disapprove such use."); *In re Richmond Unified Sch.Dist.*, 133 B.R. 221, 225 (Bankr. N.D. Cal. 1991) ("Section 904 also prohibits the court from interfering with 'any of the property or revenues of the debtor' or with 'the debtor's use or enjoyment of any income producing property.").

[17] It is well settled that causes of action are property of a debtor's estate and the trustee has exclusive standing to assert such claims. *See Schertz-Cibolo-Universal City Indep. Sch. Dist. v. Wright (In re Educators Grp. Health Tr.),* 25 F.3d 1281, 1284 (5th Cir. 1994) (citing *Matter of S.I. Acquisition, Inc.*, 817 F.2d 1142, 1153-54 (5th Cir.1987)).

48. Nor does the doctrine of derivative standing aid the UCC here. While the First Circuit has never conclusively addressed the issue of derivative standing for creditors, it has recognized that "creditors only have standing to pursue [] claims during bankruptcy proceedings when a trustee or debtor in possession unjustifiably fails to pursue the claim." *Morley v. Ontos, Inc. (In re Ontos, Inc.)*, 478 F.3d 427, 431–32 (1st Cir. 2007) (finding that such circumstances were not present in the case). Bankruptcy courts within the First Circuit have permitted a derivative action where there was a colorable claim for relief, the trustee had knowledge of the case and failed to intervene, and the litigation presented no burden to the estate. *Campana v. Pilavis (In re Pilavis)*, 233 B.R. 1, 3–4 (Bankr. D. Mass. 1999). The UCC cannot assert colorable claims for relief or an unjustifiable refusal to pursue such claims because there has been no unreasonable refusal to prosecute claims: it is beyond credulity that the Commonwealth, HTA, and PREPA have meritorious claims against the governmental entity that loaned them money and kept them afloat at the request of the Puerto Rico government.[18]

49. Even if the Committee attempts to meet the derivative standing standard to pursue causes of action on behalf of the Title III Debtors, the Court could not grant derivative standing without the Oversight Board's consent in light of PROMESA section 305. In chapter 11, an estate is created under 541 which holds the claims and causes of action of the debtor. PROMESA does not incorporate section 541, and PROMESA section 301(c)(5) defines "property of the estate" as "property of the debtor." Because there is no estate, all claims and causes of action that can be

[18] *See* Commonwealth of Puerto Rico, Financial Information and Operating Data Report (Dec. 18, 2016), at 189, *available at* http://bgfpr.com/documents/CommonwealthofPuertoRicoFinancialInfoFY201612-18-16.pdf ("GDB loans were also used to cover operational deficits of the Commonwealth and its instrumentalities."); P.R. Act No. 31-2013, Statement of Motives, at 1-2 ("[HTA] operates with a deficiency of approximately $355 million annually, which has been corrected in the past by means of loans granted by the Government Development Bank for Puerto Rico (BGF) to continue operating and meeting its obligations to its creditors. This practice began in 2008, when [HTA] resorted to financing to cover its operations.").

asserted by the Title III Debtors constitute "property of the debtor." As discussed above, the Title III Court cannot issue any order interfering with property of the debtor (including an order granting a committee derivative standing to pursue the causes of action) unless the Oversight Board consents.

C. Derivative Standing under Bankruptcy Code Section 926 Does Not Apply

50. Derivative standing is only applicable in limited circumstances under PROMESA. Bankruptcy Code section 926, as made applicable to Title III pursuant to PROMESA section 301(a), provides, in relevant part "If the debtor refuses to pursue a cause of action under section 544, 545, 547, 548, 549(a), or 550 of this title, then on request of a creditor, the court may appoint a trustee to pursue such cause of action."

51. Because section 926 is the only provision in PROMESA that specifically provides for derivative standing, the UCC may only petition the court to appoint a trustee in conformance with this section. By incorporating section 926 into PROMESA, Congress intended to create a limited exception for non-debtors to prosecute certain types of the debtor's causes of action and thus foreclosed other forms of derivative standing. *United States v. Johnson*, 529 U.S. 53, 58 (2000) ("When Congress provides exceptions in a statute, it does not follow that courts have authority to create others. The proper inference, and the one we adopt here, is that Congress considered the issue of exceptions and, in the end, limited the statute to the ones set forth."); *Perez Santana v. Holder*, 731 F.3d 50, 56 (1st Cir. 2013) (refusing to imply additional exception to statute as "[t]he absence of such a limitation, despite the explicit enumeration of others, serves as a strong indication that Congress imposed the restrictions that it deemed important and declined to impose others."). Such standing should not be granted lightly, and must take into account the same considerations of sovereignty and autonomy over property that permeate PROMESA. For example, in *In re New York City Off-Track Betting Corp.*, No. 09-17121 MG, 2011 WL 309594,

at *4 (Bankr. S.D.N.Y. Jan. 25, 2011), the court denied a motion by former employees of a chapter 9 debtor to appoint a trustee, noting "[c]ourts should be loath to appoint a trustee given that the court's limited powers in a chapter 9 case are best understood as operating within the context of constitutional and federalism concerns."

52. Importantly, standing under section 926 is a limited right which provides for a closed list of actions, none of which the UCC has implicated in its intended objections. *See In re Yasin*, 179 B.R. 43, 48 n.6 (Bankr. S.D.N.Y. 1995) ("In chapter 9, the court can appoint a trustee solely for the purpose of bringing certain avoiding actions. The chapter 9 trustee can neither assume nor reject unexpired leases or executory contracts or be compelled to do so; only the debtor can."). The UCC could only pursue section 926 standing for claims that properly fall within section 544, 545, 547, 548, 549(a), or 550 of the Bankruptcy Code. None of the UCC intended objections do so.

WHEREFORE the Oversight Board respectfully requests that the Court enter an order finding the UCC lacks standing to participate in this Title VI Case, and specifically, to object to the Qualifying Modification and the GDB Restructuring Act, and grant the Oversight Board such other and further relief as is just.

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Dated: September 1, 2018
San Juan, Puerto Rico

Respectfully submitted,

/s/ Martin J. Bienenstock

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CERTIFICATE OF SERVICE

I hereby certify that, on this same date, I electronically filed the foregoing with the Clerk of the Court using the CM/ECF system, which will send notifications of such filing to all CM/ECF participants in this case.

/s/ Hermann D. Bauer
Hermann D. Bauer