UNITED STATES DISTRICT COURT
DISTRICT OF PUERTO RICO

AUTONOMOUS MUNICIPALITY OF SAN JUAN, Plaintiff, -against- THE FINANCIAL OVERSIGHT AND MANAGEMENT BOARD FOR PUERTO RICO, GOVERNMENT DEVELOPMENT BANK OF PUERTO RICO, and PUERTO RICO FISCAL AGENCY AND FINANCIAL ADVISORY AUTHORITY, Defendants.	No. 17-cv-02009 (LTS)
THE FINANCIAL OVERSIGHT AND MANAGEMENT BOARD FOR PUERTO RICO Movants, v. AUTONOMOUS MUNICIPALITY OF SAN JUAN, MUNICIPALITIES OF JUANA DÍAZ AND CABO ROJO, MUNICIAPLITIES OF HOMRIGUEROS AND SAN GERMÁN, MUNICIPLAITY OF LUQUILLO, MUNICIPALITY OF SAN LORENZO, and MUNICIAPLTY OF MAYAGUEZ Respondents.	

MOTION TO DISMISS PLAINTIFF'S AMENDED COMPLAINT PURSUANT TO FED. R. CIV. P. 12(b)(1) and (b)(6)

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To The Honorable United States District Judge Laura Taylor Swain:

Defendant, the Financial Oversight and Management Board for Puerto Rico (the "FOMB" or the "Board"), respectfully submits this memorandum in support of its motion to dismiss the Amended Complaint filed by the Autonomous Municipality of San Juan ("San Juan") (Dkt. No. 88) (the "Complaint") and hereby avers as follows:[1]

PRELIMINARY STATEMENT

As the Court is aware, in PROMESA section 405(m) Congress declares the Commonwealth to be in a state of fiscal emergency, necessitating a significant restructuring of its debt. An integral piece of this effort includes restructuring the debt of the Government Development Bank of Puerto Rico ("GDB"). GDB owes many Commonwealth entities the amounts of their deposit accounts, and owes billions in bond debt to local and external creditors. Conversely, many Commonwealth entities have loans from the GDB.

Since January 2017, GDB and the Puerto Rico Fiscal Agency and Financial Advisory Authority ("AAFAF") have worked with creditors to develop a voluntary debt restructuring under Title VI of the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA"), resulting in the Restructuring and Support Agreement dated May 15, 2017 (the "RSA"). The FOMB certified the proposed modification on July 12, 2017, making it a "Qualifying Modification" under Title VI, which may be submitted to the district court for

[1] Other municipalities have intervened in this action, including the municipalities of Juana Díaz and Cabo Rojo (Dkt. Nos. 15, 80), Homrigueros and San Germán (Dkt. No. 17), Luquillo (Dkt. Nos. 19, 33), San Lorenzo (Dkt. Nos. 20, 34), and Mayaguez (Dkt. Nos. 21, 89) (the "Intervenor Municipalities") per this Court's order (Dkt. 82) (the "Intervention Order"). All the Intervenor Municipalities filed complaints merely adopting the same causes of action that San Juan asserted in its original complaint. The Intervenor Municipalities have not filed anything to join in San Juan's amended complaint. But since the causes of action asserted in San Juan's original complaint are subsumed within the amended complaint, and because the Intervention Order expressly states that the Intervenor Municipalities shall not argue beyond the scope of the allegations in the amended complaint, the Intervenor Municipalities' complaints should be dismissed for the same reasons that warrant dismissal of San Juan's amended complaint.

approval after voting is completed and a number of events and conditions have occurred, as described herein.

Due to the disruptions and devastation caused by Hurricane Maria, on October 20, 2017, GDB and the supporting creditors amended the RSA to extend deadlines by sixty days for achieving certain milestones, such as commencing solicitation of the vote on the Qualifying Modification. On December 20, 2017, the RSA was amended once again to extend these deadlines, including the deadline to commence solicitation of the vote, to March 20, 2018.

Despite the fact that solicitation of the vote on the Qualifying Modification had not even begun, San Juan, one of GDB's many claimholders, sought a declaration in its original complaint that the RSA violates PROMESA. Additionally, San Juan sought an injunction barring the FOMB, GDB, and AAFAF from continuing with the RSA approval process. On September 27, 2017, the Court denied San Juan's motion for a preliminary injunction, holding San Juan failed to demonstrate it was entitled to a setoff under § 3222 of the Puerto Rico Civil Code on the theory that its future loan payment represented a current obligation. The FOMB, GDB, and AAFAF also moved to dismiss San Juan's original complaint.

On December 1, 2017, rather than oppose those motions, San Juan filed an amended complaint, asserting many of the same claims in its original complaint, notwithstanding that those claims suffer from the same defects. San Juan also now brings five new causes of action (Counts V, VII, VIII, IX, and X), as well as a renewed request to enjoin the FOMB, AAFAF, and the GDB from continuing with the RSA approval process. All San Juan's claims fail as a matter of law for a number of reasons.

First, San Juan does not have standing to bring claims challenging the RSA. In Counts I through III, San Juan alleges that the RSA does not comply with PROMESA. The recently-

enacted GDB Restructuring Act (Act 109-2017, enacted August 24, 2017) ("Act 109"), however, explicitly divests San Juan and other government entities of standing to challenge the RSA.

Seeking to avoid the effects of Act 109, San Juan asserts that Act 109 (1) does not preclude San Juan from challenging the RSA prior to it being approved by the Court, and (2) is preempted by PROMESA to the extent it does bar San Juan from challenging the RSA. Both of these arguments fail. The plain language of Act 109 precludes San Juan from challenging the RSA before it is approved by the Court, and because PROMESA does not purport to restrict the Commonwealth's power to control its municipalities and instrumentalities, it does not conflict with Act 109, and Act 109 is not preempted. As a result, Count V, which seeks declaratory relief that PROMESA preempts Act 109, also fails to state a claim.

Second, Counts I through III are not ripe. PROMESA states that in any bond restructuring process under Title VI, the court must approve the Modification before it becomes binding on non-consenting creditors. Thus, the appropriate time for any creditor to challenge the Modification is at the court-approval stage, not beforehand. The standard for judicial review, moreover, requires the court to judge whether the Modification is "manifestly inconsistent" with § 601 of PROMESA. That standard requires the entire process subject to court approval to be complete before a creditor may challenge whether the statute has been followed.

In addition, under ordinary ripeness principles, San Juan's first three causes of action turn on events that have not yet occurred, and may never occur—principally, ratification of the RSA by the requisite creditor votes. If the RSA is not approved, then no harm would come to pass for San Juan. Accordingly, San Juan's claims in Counts I through III are not ripe.

Third, Counts I and II allege that CAE funds and Excess CAE funds (as defined herein) are not "Bond Claims" as defined under Title VI because they are allegedly tax revenues held in

trust for San Juan. These claims fail, however, because the CAE funds and Excess CAE funds were deposited in a GDB *deposit account*, pursuant to the Trust Agreement between the Municipal Revenues Collection Center (the "CRIM") and GDB (the "Trust Agreement," attached as Exhibit A to the Complaint). As general deposits, the CAE funds and Excess CAE funds legally constitute a loan to GDB under Puerto Rico law. Therefore, these funds fall within the ambit of PROMESA's definition of "Bond," which is defined broadly to include any "bond, *loan*, letter of credit . . ." (*see* PROMESA § 5(2) (emphasis added)). As a "Bond" under PROMESA, the CAE and Excess CAE are subject to modification under Title VI.

Fourth, Count III fails to state a claim. In Count III, San Juan alleges it has purported "statutory security arrangements" (such as alleged setoff rights or lien rights) that require it to be placed in a separate voting pool. But San Juan has no such special rights. San Juan does not satisfy the criteria for setoff under Puerto Rico law, nor does San Juan have a statutory lien or any other secured interest. Without those rights and interests, San Juan is not entitled to a separate voting pool.

Fifth, Count IV seeks a declaratory judgment that the FOMB violated PROMESA by improperly using executive sessions and "closed door meetings" with professionals not employed by the Board. Yet nothing in PROMESA or the FOMB's bylaws prohibits it from including professionals not employed by the Board in its executive session meetings. Even if outside professionals were precluded from attending the meeting, San Juan alleges no basis under PROMESA for invalidating the FOMB's contingent approval of the RSA simply because an outside professional allegedly participated in one meeting. Indeed, would San Juan prefer the FOMB to work on complex matters without the expertise it requires?

Sixth, Count VI alleges that certain moratorium acts and orders issued by the Commonwealth are preempted by PROMESA § 303(3). The Complaint, however, wholly fails to allege how these moratorium acts and orders are inconsistent with PROMESA. Therefore, there is no basis to support this claim.

Seventh, in Count IX, San Juan seeks a constructive trust on "escrowed funds" that it allegedly has on deposit at the GDB. This claim must also be dismissed, as claims for a constructive trust are no longer recognized under Puerto Rico law following the passage of the Trust Act, Act 219-2012 ("Act 219") in 2012. Thus, Count IX fails to state a claim as a matter of law.

Finally, Counts VII, VIII, and X fail as well. Because those counts are directed at the GDB or AAFAF – not the FOMB – the FOMB incorporates and joins in the arguments made by GDB and AAFAF in their motion to dismiss.

Accordingly, all claims made in the Complaint fail. For all these reasons, the Complaint should be dismissed with prejudice.

BACKGROUND

A. The PROMESA Title VI Process

In 2016, Congress enacted PROMESA and created the FOMB to resurrect Puerto Rico's economy by establishing oversight of the government's budget and fiscal policies and by providing a way for the Commonwealth to modify or restructure its debts. PROMESA §§ 101(a), 201(b)(2). PROMESA provides two mechanisms for the Commonwealth and its instrumentalities to restructure their debt: Title III creates a court-supervised process similar to a chapter 9 and 11 bankruptcy case; and Title VI establishes a voluntary process for debt restructuring based on affirmative votes of two-thirds the total principal amount voted in each

pool, and court review of the Modification's compliance with § 601. PROMESA §§ 301-317, 601.

As the Complaint recognizes, the Title VI restructuring process involves numerous steps before a Qualifying Modification, like the proposed RSA here, becomes binding on non-consenting creditors. Those steps run as follows:

1. GDB, as a territorial instrumentality and issuer of bond debt, must be authorized by the FOMB, in FOMB's role as "Administrative Supervisor," to propose a Modification of bond debt. PROMESA §§ 601(a)(1), (2), (8), (9); 601(e); 601(g). (Am. Compl. ¶¶ 59-60.) GDB was so authorized by the Administrative Supervisor and proposed the Modification at issue here under PROMESA's voluntary agreement process. PROMESA § 601(g)(2).

2. The FOMB must determine whether the Modification meets the requirements for "certification," under either the Consultation Process or the Voluntary Agreement Process, § 601(g)(1) or (2), respectively. The requirements for certification under the Voluntary Agreement Process are met if the FOMB certifies that (a) all holders of Bonds of any series in a Pool affected by the Modification are offered the same consideration pursuant to § 601(g)(1)(B); (b) the Modification is consistent with the certified Fiscal Plan and provides for a sustainable level of debt (PROMESA §§ 601(g)(2), 104(i)(2)(A) (Am. Compl. ¶ 60)); and (c) the Issuer has reached agreement with creditors holding a majority of the amount of bond claims (PROMESA §104(i)(2)(B)). Once certified, the proposed Modification becomes a Qualifying Modification. PROMESA § 601(g). (Am. Compl. ¶ 61). On July 12, 2017, the FOMB certified the RSA, making it a Qualifying Modification under Title VI. (Am. Compl. ¶ 3.)

3. The FOMB, in consultation with the Issuer of the bond, must divide creditors into separate voting pools corresponding to the relative priority or security arrangements of their

bonds. PROMESA § 601(d)(3). This stage has not yet occurred and is unlikely to occur until February 2018 at the earliest.

4. The Issuer of the debt must provide a variety of information to affected creditors through an "Information Agent," including a description of the Issuer's economic and financial circumstances, the Issuer's existing debts, and the impact of the proposed Qualifying Modification on the public debt. PROMESA §§ 601(f), (h). (Am. Compl. ¶ 61). This stage has also not yet occurred and the Complaint does not allege otherwise. Indeed, the Issuer has not even provided the FOMB with the final solicitation materials as required under PROMESA § 601(f). The Complaint does not allege otherwise.

5. Creditor votes must be solicited to approve or reject the Qualifying Modification. PROMESA § 601(j). (Am. Compl. ¶ 61). For a Qualifying Modification to be binding, two voting thresholds must be met: (a) creditors holding at least two-thirds of the outstanding principal amount of all bonds in each Pool that have voted must vote to accept the proposal; and (b) creditors holding a majority of the outstanding principal amount of all bonds in each Pool must vote to accept the proposal. *Id.* All Pools must meet both voting thresholds. *Id.* This stage has also not yet occurred and the Complaint does not allege otherwise.

6. If the Qualifying Modification receives the requisite votes under § 601(j), the FOMB may further certify that: (a) the Title VI voting requirements have been met; (b) the Qualifying Modification meets the requirements of § 104(i)(1) (*i.e.*, the Qualifying Modification provides for a sustainable level of debt for the Issuer and is consistent with the certified Fiscal Plan); and (c) any conditions on the effectiveness of the Qualifying Modification have been satisfied or waived. PROMESA § 601(m)(1)(B). (Am. Compl. ¶ 65). This stage has also neither occurred nor been alleged to have occurred.

7. If the Qualifying Modification receives the requisite votes from creditors (Step 5) and further certification from the FOMB (Step 6), the Issuer must submit to this Court an application for an order approving the Qualifying Modification. PROMESA § 601(m)(1)(D). This stage has also neither occurred nor been alleged to have occurred.

As San Juan recognizes, several critical stages in the RSA approval process — including the creditor vote (Step 5) — have not occurred, and are not expected to occur for some time. (*See* Am. Compl. ¶ 110.) If the RSA does not receive the requisite votes (Step 5), there will be no Modification for the FOMB to certify (Step 6), nor will the confirmation stage (Step 7) set forth in § 601(m)(1)(D) occur, and the RSA will not become binding on non-consenting creditors. *See* PROMESA § 601(m). Indeed, San Juan's request for a future injunction (Am. Compl., Prayer for Relief, ¶ vi), is both a concession that these events have not occurred and an admission that San Juan wants the Court to make sure they do not occur.

B. The CAE Funds, the Excess CAE Funds, and the Trust Agreement

GDB is the trustee of the Municipal Public Debt Redemption Fund (the "Redemption Fund"), in which each municipality's Additional Special Contribution ("CAE") tax funds are deposited. (Am. Compl. ¶ 18.) The CAE tax is imposed to service the municipalities' general obligation bonds or notes. (*Id.*) From time to time, the amount of the CAE in the Redemption Fund may exceed the debt service for that year (the "Excess CAE"). (*Id.*) Count I of the Complaint alleges that the Excess CAE funds are not subject to modification under Title VI because they are not "Bond Claims" to which Title VI applies, and Count II makes the same claim with respect to the CAE funds.

Pursuant to the Trust Agreement, on which San Juan relies in its Complaint, GDB was required to maintain *as deposits* the initial capital of the trust fund into which were deposited the CAE funds and Excess CAE funds, which capital was already held in GDB. (Am. Compl., Ex.

A, § VII, at 39 ("The parties agree that said funds, derived from the [CAE], which, upon the execution of this instrument, are deposited with the Bank, shall immediately be transferred to the SAT-GDB Sub-fund *and be maintained invested in deposits of the Bank* until such time as the [CRIM] and the Bank agree otherwise.") (emphasis added).) As for the CAE funds and Excess CAE funds collected afterward, the Agreement provides GDB shall invest those funds "in accordance with, and in investment instruments that are consistent with, the Investment Guidelines in force" (*id.* § IX, at 40-41), which in turn require "invest[ment] in deposits within [GDB] itself" (*id.* § VI.A, at 54-55). Thus, at all times, GDB was required to invest the CAE funds and Excess CAE funds in general deposit accounts provided by GDB.

LEGAL STANDARD

Federal Rule 12(b)(1) is "a 'large umbrella, overspreading a variety of different types of challenges to subject-matter jurisdiction,' including ripeness, mootness, the existence of a federal question, diversity, and sovereign immunity." *Ivyport Logistical Servs., Inc., v. Caribbean Airport Facilities, Inc.*, 502 F. Supp. 2d 227, 230 (D.P.R. 2007) (quoting *Valentin v. Hosp. Bella Vista*, 254 F.3d 358, 362-63 (1st Cir. 2001)). Taking the "jurisdictionally-significant facts as true," the Court should "assess whether the plaintiff has propounded an adequate basis for subject-matter jurisdiction." *Id.*

A complaint should also be dismissed if it fails "to state a claim upon which relief can be granted." Fed. R. Civ. P. 12(b)(6). In the First Circuit, courts follow a two-pronged approach to resolve a motion to dismiss. *Ocasio-Hernández v. Fortuño-Burset*, 640 F.3d 1, 12 (1st Cir. 2011). First, courts should "isolate and ignore statements in the complaint that simply offer legal labels and conclusions or merely rehash cause-of-action elements." *Vazquez v. Surrillo-Ruiz*, 76 F. Supp. 3d 381, 387 (D.P.R. 2015) (internal citation omitted). Legal conclusions must be supported by factual allegations. *Ashcroft v. Iqbal*, 556 U.S. 662, 679 (2009). Even then,

"factual allegations may be so 'threadbare' that they are in essence conclusory even if they include more than an assertion that an element of a cause of action was satisfied." *Vazquez*, 76 F. Supp. at 388 (quoting *Penalbert-Rosa v. Fortuno-Burset*, 631 F.3d 592, 595 (1st Cir. 2011)).

Second, courts should "take the complaint's well-pled (*i.e.*, non-conclusory, non-speculative) facts as true, drawing all reasonable inferences in the pleader's favor, and see if they plausibly narrate a claim for relief." *Id.* at 388. In doing so, the court may "consider (a) 'implications from documents' attached to or fairly 'incorporated into the complaint,' (b) 'facts' susceptible to 'judicial notice,' and (c) 'concessions' in plaintiff's 'response to the motion to dismiss.'" *Id*. (quoting *Arturet–Velez v. R. J. Reynolds Tobacco Co.*, 429 F.3d 10, 13 n.2 (1st Cir. 2005)).

ARGUMENT

I. SAN JUAN DOES NOT HAVE STANDING TO CHALLENGE THE RSA.

In August 2017, the Commonwealth enacted Act 109, which explicitly divested San Juan and other government entities of standing to challenge the RSA. In its motion to dismiss San Juan's original complaint, the FOMB argued that Act 109 deprived San Juan of standing to assert certain of its claims. Nothing has changed since the FOMB made that argument, as the provision of Act 109 that eliminates standing for municipalities to challenge the RSA has not been repealed. Yet rather than respond to this argument on its face, San Juan's amended complaint merely repeats its assertion that San Juan somehow retains standing to bring its claims. (Am. Compl. ¶ 113.) In support, San Juan alleges that Act 109 is not currently effective against Commonwealth municipalities (*id.* ¶ 12) and that it is preempted by PROMESA (*id.* ¶¶ 114, 149-151). Neither of these arguments is correct.

A. By its plain language, Act 109 divests San Juan of standing to challenge the RSA (Counts I, II, III).

Act 109 establishes the legal framework for restructuring GDB's debt under Title VI of PROMESA. Article 703 of Act 109, titled "Lack of Authority and Standing of Government Entities," provides that "no Government Entity shall have authority or standing to challenge this Act, *the Restructuring Transaction*, or the other transactions contemplated in this Act in any local or federal court." 2017 P.R. Laws Act 109, art. 703 (emphasis added). The term "Restructuring Transaction" is defined to include all transactions contemplated by or in furtherance of the "Qualifying Modification," which in turn is defined to mean the Restructuring Support Agreement dated May 17, 2017—*i.e.*, the RSA at issue here. *Id.*, art. 103(ii), 103(pp). Additionally, Act 109 defines "Government Entity" to include municipalities of Puerto Rico. *Id.*, art. 103(w). Accordingly, on its face, Article 703 of Act 109 deprives San Juan (and the Intervenor Municipalities) of standing and authority to bring Counts I, II, and III, since those claims seek to challenge the RSA.

Act 109 is a valid exercise of the Commonwealth's power over its municipalities and instrumentalities. The Legislative Assembly has authority to approve, amend, or repeal laws that affect the powers or privileges granted to municipalities by law or contract. *See Gobierno de Ponce v. Caraballo*, 166 D.P.R. 723 (P.R. 2006) ("the Legislative Assembly has the authority to revoke any delegation of competence previously assigned to municipalities") (certified translation);[2] *see also City of Trenton v. N.J.*, 262 U.S. 182, 187 (1923) ("A municipality is merely a department of the state, and the state may withhold, grant or withdraw powers and privileges as it sees fit."). Accordingly, the Legislative Assembly may impose specific restrictions on the general power to sue and be sued that it has bestowed on municipalities. *See*

[2] A certified translation of *Gobierno* can be found at Dkt. No. 55-1.

21 L.P.R.A. § 4051 (granting municipalities power to sue and be sued in any court of justice or administrative body).

B. Act 109 is effective and is not preempted by PROMESA (Count V).

In its amended complaint, San Juan alleges that "[b]y its terms, Act 109 is simply an enabling statute that provides for the implementation of the RSA if and when it has been approved by this Court, but does not preclude challenges to the RSA prior to its approval." (Am. Compl. ¶ 12.) San Juan also alleges that, to the extent Act 109 is deemed to preclude it from challenging the RSA now, before it has been approved, it is preempted by PROMESA. (*Id.* ¶¶ 149-51). In making these arguments, San Juan ignores the relevant provisions of both Act 109 and of PROMESA itself.

1. The limitation on municipal standing in Act 109 took effect immediately.

Contrary to San Juan's protestations, Article 703 of Act 109 serves to deprive it and other Commonwealth entities of standing to challenge the RSA prior to the RSA's approval. The plain language of Act 109 makes this clear. First, the effective date of Act 109 as a whole was the date of its enactment. Act No. 109-2017, art. 708. Second, while certain provisions within Act 109 expressly became effective only upon the "Closing Date" of the RSA (that is, the date when the RSA becomes binding under PROMESA § 601(m), *see* 2017 P.R. Laws Act 109, art. 103(j), (o)), Article 703 does not contain any such time limitation. Thus, there is no basis for San Juan's assertion that it somehow retains standing to bring claims challenging the RSA at this stage.

2. Act 109 is not preempted by PROMESA.

In Count V, San Juan also seeks a declaration that, to the extent Act 109 precludes it from challenging the RSA, such preclusion is preempted by PROMESA. (Am. Compl. ¶¶ 149-151.) In particular, San Juan states the "mechanism for San Juan and other interested parties to

challenge the RSA under Title VI" provided in PROMESA preempts Act 109. (Am. Compl. ¶ 12.) Yet San Juan does not allege which specific provision of PROMESA conflicts with Act 109, nor how such a provision would lead to such a conflict. Thus, it has not adequately pled the allegations supporting Count V.

Even if San Juan had provided more than conclusory allegations regarding its preemption claim, it cannot withstand a motion to dismiss. Act 109 does not prohibit or prevent San Juan from voting on the RSA. As to "objecting" to the RSA, no provision in PROMESA contains any explicit language touching on whether Congress's intent was to deprive the Commonwealth of its ability to control its municipalities. Assuming that the language that San Juan claims preempts Act 109 is PROMESA § 601(n), there also is no conflict. PROMESA § 601(n)(2) generally provides that "there shall be a cause of action to challenge unlawful application of this section." But a general acknowledgment that individuals can bring a private right of action does not say anything about whether certain specific entities, such as municipalities, are able to bring a lawsuit in all circumstances.

Furthermore, there is no suggestion that the goals of PROMESA, including § 601(n)(2), and Act 109 are in conflict. It is not physically impossible to comply with both the federal statute and state law, and Act 109 does not stand as an obstacle to the objective of PROMESA as a whole. The objective of Title VI of PROMESA is to provide a mechanism for the voluntary restructuring of debt by agreement. While it divests Puerto Rico's municipalities of standing to challenge the RSA, Act 109 does not frustrate any part of PROMESA or Title VI.

Lastly, Act 109's deprivation of municipalities' standing to challenge the RSA is reinforced by PROMESA § 303. This section, which has an analog in the Bankruptcy Code, states that nothing in PROMESA is intended to "limit or impair the power of [the

Commonwealth] to control, by legislation or otherwise, the territory or any territorial instrumentality thereof in the exercise of [its] political or governmental powers." PROMESA § 303. This language bolsters Puerto Rico's ability to enact laws such as Act 109 that deprive its municipalities of standing in limited situations. The generic statement in PROMESA § 601(n)(2) that creates a private right of action therefore cannot possibly mean that all municipalities must be able to assert any claims that they so choose, because such a reading would render it inconsistent with the powers reserved by the Commonwealth in § 303, and because the Commonwealth could exercise the standing it has denied to San Juan.[3] This is not a situation where a statute has eliminated the possibility of remedy. Rather, it controls who can request the remedy.

As a result, Count V, which seeks a declaration that PROMESA preempts Act 109, fails as a matter of law.

II. CLAIMS CHALLENGING THE RSA ARE NOT RIPE FOR ADJUDICATION (COUNTS I, II, III).

A. Under PROMESA, judicial review of a Qualifying Modification is available only when the Issuer applies for an order approving it.

Both the structure and the text of PROMESA make clear the proper time for any entity with standing to bring a challenge to the RSA approval process is when the Issuer applies for approval of a Qualifying Modification, not before the vote has occurred, let alone before the voting pools have even been finalized. Counts I, II, and III all assert claims reviewable only

[3] Relatedly, San Juan cannot challenge Act 109 under the Supremacy Clause of the U.S. Constitution, because as a political subdivision of the Commonwealth, San Juan "lacks standing under federal law to challenge the constitutionality of a state statute." *Burbank-Glendale-Pasadena Airport Auth. v. City of Burbank*, 136 F.3d 1360, 1362 (9th Cir. 1998); *see also Town of Charlestown v. United States*, 696 F. Supp. 800, 806 (D.R.I. 1988) ("'municipal corporations have regularly been denied standing in the federal courts to attack state legislation as violative of the federal Constitution, on the ground that they have no rights against the state of which they are a creature'") (quoting Hart & Wechsler, *The Federal Courts and the Federal System* 182 (2d ed. 1973)).

once the Issuer applies for approval, which has not happened yet. Accordingly, all are premature.

Section 601 provides that the final step to render binding a Qualifying Modification is the district court's approval and the entry of an order that the requirements of the section have been satisfied. PROMESA § 601(m)(1)(D). At that stage, the Qualifying Modification is deemed "conclusive and binding." *Id.* § 601(m)(2). The fact the statute built a judicial-approval stage into the RSA process itself is a strong signal Congress intended it to be the exclusive avenue for creditors to bring challenges.[4]

The standard of review to be applied by this Court reinforces this conclusion. The district court may nullify a Modification if and only if it determines that the Modification is "manifestly inconsistent" with § 601. *Id.* § 601(n)(3). Although not defined in the statute, "manifest inconsisten[cy]" undoubtedly imposes a high burden on creditors, requiring them to show that the Modification facially and unambiguously violates § 601's strictures in material ways. More important, the standard indicates that review is available only once the RSA process is complete. A court cannot determine whether a Modification is manifestly inconsistent with § 601 until it is able to review everything required to occur under § 601, and then assess whether as a whole the Modification follows the statute. That can be done only when the Issuer applies for approval.

B. San Juan's challenges to the RSA approval process turn on future events currently contingent and uncertain.

Counts I through III are also unripe because they allege uncertain, contingent events in the future that must occur before San Juan can suffer harm. Under established ripeness doctrine,

[4] San Juan's challenge to the RSA prior to completion of each stage in § 601 is akin to seeking judicial review of a regulation prior to final agency action. Courts regularly hold such challenges are not ripe for judicial review. *W.R. Grace & Co. v. EPA*, 959 F.2d 360, 364-65 (1st Cir. 1992) (holding claim based on interim EPA action was not fit for judicial review, reasoning ripeness test considers "the degree to which any challenged agency action is final").

such claims cannot be brought now.

Ripeness "has roots in both the Article III case or controversy requirement and in prudential considerations." *Reddy v. Foster*, 845 F.3d 493, 500 (1st Cir. 2017) (citation omitted). The Supreme Court has held the purpose of the ripeness doctrine is to prevent the adjudication of claims relating to "contingent future events that may not occur as anticipated, or indeed may not occur at all." *Id.* (quoting *Texas v. United States*, 523 U.S. 296, 300 (1998)).

The test for ripeness is whether "there is a substantial controversy, between parties having adverse legal interests, of sufficient immediacy and reality to warrant the issuance of a declaratory judgment." *McInnis-Misenor v. Maine Med. Ctr.*, 319 F.3d 63, 70 (1st Cir. 2003) (quoting *Lake Carriers' Ass'n v. MacMullan,* 406 U.S. 498, 506 (1972)). Where those conditions are not met, courts should avoid "entangling themselves in abstract disagreements." *Id.* (quoting *Abbott Labs. v. Gardner,* 387 U.S. 136, 148 (1967)).

Determining ripeness involves a dual inquiry: evaluating "the fitness of the issues for judicial decision" — that is, whether they turn on events that have already occurred — and "the hardship to the parties of withholding court consideration" — that is, whether the parties have already suffered injury. *McInnis-Misenor*, 319 F.3d at 70. Both prongs of the test must be satisfied. *Id.* Counts I through III of the Complaint satisfy neither.

1. There is no certainty creditors holding sufficient claims will vote for the RSA.

San Juan's claims in Counts I through III are not fit for judicial review because they are based on a "hypothetical occurrence of future events" that may not occur — namely, the RSA receiving the necessary votes for approval. *New Progressive Party (Partido Nuevo Progresista) v. Colon*, 779 F. Supp. 646, 655 (D.P.R. 1991). Resolving San Juan's claims prior to successful voting raises the risk the Court's decision could be rendered unnecessary — a result that should

be avoided. *McInnis-Misenor*, 319 F.3d at 70 ("fitness prong" focuses on the "policy of judicial restraint from unnecessary decisions").

As noted above, and as the Complaint recognizes, the Title VI restructuring process involves numerous steps before a Qualifying Modification is judicially approved. San Juan admits that many of those steps have not yet occurred, and may never occur. The voting process outlined in § 601(j) has not begun. (*See* Am. Compl. ¶ 110.) Nor has the confirmation stage under § 601(m)(1)(D) taken place. *Id*. It is unavoidably uncertain whether the Qualifying Modification will receive the requisite percentage of votes, even if the voting pools are eventually constituted as alleged in the Complaint. Moreover, changes could be negotiated between now and then.

This Court and the First Circuit have found a lack of ripeness where the claim was dependent on the outcome of an upcoming vote or some other contingent approval. *City of Fall River v. FERC*, 507 F.3d 1 (1st Cir. 2007) (dismissing as unripe a challenge of a conditional approval to build a natural gas terminal, because claim was contingent on approval by federal agencies); *New Progressive Party*, 779 F. Supp. at 655 (finding claim not ripe where dependent on a referendum receiving sufficient votes, reasoning that "[t]o make this decision before the referendum is held would be the equivalent of an advisory opinion," which "federal courts are not empowered to do"). Numerous circuit courts from around the country are in accord.[5]

[5] *See also Parrish v. Dayton*, 761 F.3d 873, 876 (8th Cir. 2014) (dismissing claim to block union where vote in favor of unionization had not yet occurred) (citation omitted); *Harris v. Quinn*, 656 F.3d 692, 700 (7th Cir. 2011), *aff'd in relevant part*, 134 S. Ct. 2618 (2014) (dismissing claims as unripe because there was no certainty that potential union members would approve the vote to unionize, in which case plaintiff would not suffer the harm alleged); *Addington v. U.S. Airline Pilots Ass'n*, 606 F.3d 1174, 1179-80 (9th Cir. 2010) (dismissing claim as unripe where the collective bargaining agreement at issue would not affect the plaintiffs until it was approved by the union's members, reasoning that approval of the CBA was a contingency that made the plaintiffs' claim speculative); *Friends of Marolt Park v. U.S. Dep't of Transp.*, 382 F.3d 1088, 1094 (10th Cir. 2004) (finding claim not ripe where outcome was dependent upon voter approval of the proposed highway construction project); *Pub. Water Supply Dist. No. 10 of Cass Cty. v. City of Peculiar*, 345 F.3d 570, 572 (8th Cir. 2003) (dismissing claim as unripe where the alleged harm was contingent on the passage of a law by a two-thirds public vote).

Similar to the cases above, Counts I through III of the Complaint are dependent on the outcome of a vote that may render those claims moot. Accordingly, Counts I through III are not ripe.

2. San Juan has suffered no injury to date.

In addition, Counts I through III do not allege a direct and immediate injury to San Juan, which is a requirement for satisfying the hardship prong of the ripeness test.

The hardship prong evaluates "the extent to which withholding judgment will impose hardship" — an inquiry that asks "whether plaintiff is suffering any present injury from a future contemplated event." *McInnis-Misenor*, 319 F.3d at 70 (citation omitted). A "mere possibility of future injury, unless it is the cause of some present detriment, does not constitute hardship." *Sindicato Puertorriqueno de Trabajadores v. Fortuno*, 699 F.3d 1, 9 (1st Cir. 2012). Similarly, the hardship inquiry is "unconcerned with wholly contingent harm" (*McInnis-Misenor*, 319 F.3d at 73) and instead "concerns the harm to the parties seeking relief that would come to those parties from our 'withholding of a decision' at this time." *Reddy*, 845 F.3d at 501.

San Juan has not alleged any basis for finding it is at risk of any "direct and immediate" harm if the court withholds judgment. *See McInnis-Misenor*, 319 F.3d at 70. In and of itself, classification in the wrong voting pool or improper attendance at an executive session does not constitute injury — again, not unless and until the RSA receives the requisite votes from creditors. *See Sindicato*, 699 F.3d at 9; *McInnis-Misenor*, 319 F.3d at 73. Because San Juan does not allege any direct and immediate hardship, but only the possibility of future, contingent harm, it cannot satisfy the hardship prong of the ripeness test.

Not only would San Juan not suffer any harm if this Court withheld judgment, but granting San Juan the relief sought would impose a significant hardship on Defendants. Allowing creditors to challenge every step of the Qualifying Modification process would

significantly increase litigation expenses by subjecting Defendants to multiple proceedings brought by multiple creditors. Such piecemeal challenges would be far less efficient and cost-effective than the statutorily-mandated judicial-review process, which allows the Court to hear all objections in a uniform and organized manner at the conclusion. Accordingly, because there is no hardship, and none alleged, from the Court withholding judgment, Counts I through III must be dismissed for lack of ripeness.

III. COUNTS I AND II FAIL BECAUSE CAE FUNDS AND EXCESS CAE FUNDS CONSTITUTE "BONDS" THAT CAN BE RESTRUCTURED UNDER TITLE VI.

In Counts I and II, San Juan alleges that CAE funds and Excess CAE funds are not subject to a Qualifying Modification under Title VI because they are not "Bond Claims." (Am. Compl. ¶¶ 120, 126.) Rather, San Juan contends that those funds are moneys in which it has a "direct property interest under Puerto Rican law" and under the terms of the Trust Agreement, making them "San Juan's property." (Am. Compl. ¶¶ 123, 129.) San Juan is wrong. The Trust Agreement provides that GDB was required to deposit CAE funds and Excess CAE funds in general deposit accounts of GDB, making them like all other funds in deposit accounts provided by GDB — that is, as a matter of law, loans subject to Title VI modification.[6]

The Trust Agreement provides the initial capital of the trust (the initial Excess CAE funds) shall "be maintained invested in deposits of the Bank." (Dkt. No. 88-1, § VII, at 39.) With respect to additional CAE and Excess CAE funds, the Trust Agreement provides GDB shall invest the funds "in accordance with, and in investment instruments that are consistent with, the Investment Guidelines in force." (*Id.*, § IX, at 40-41.) Section VI of the Investment Guidelines, which are part of the Trust Agreement, provides that the CAE funds and Excess

[6] The Trust Agreement is attached to and cited in the Complaint. Accordingly, it is appropriate on a motion to dismiss for the Court to examine the Trust Agreement's provisions. *See Freeman v. Town of Hudson*, 714 F.3d 29, 35 (1st Cir. 2013) ("On a motion to dismiss, a court ordinarily may only consider facts alleged in the complaint and exhibits attached thereto.") (citation omitted).

CAE funds shall be "invested in deposits within [GDB] itself." (*Id.*, § VI.A, at 54-55.) Thus, GDB was required to invest all CAE funds and Excess CAE funds in general GDB deposit accounts.

It is well established under Puerto Rico law that general deposits have the status of "loans" to the bank.[7] *Santos v. Banco Popular*, 172 D.P.R. 759, 774 (P.R. 2007) (holding that the "relationship between a bank and a depositor is a loan agreement that is governed by the provisions of the [Puerto Rico] Civil Code," and that a deposit constitutes "a loan agreement where there is a creditor-debtor relationship"); *Portilla v. Banco Popular*, 75 D.P.R. 100, 113 (P.R. 1953) ("[O]ur Civil Code defines the contract used to establish a checking account as a loan contract, not merely a deposit contact [sic], since the depository bank has, in addition to its obligation to keep and return the money deposited, or its value, the authority to use the thing deposited.").[8] As loans, the CAE funds and Excess CAE funds fall squarely in the definition of "Bonds" that can be restructured under Title VI, because PROMESA defines "Bond" broadly to include any "bond, *loan*, letter of credit . . ." PROMESA § 5(2) (emphasis added). Thus, the RSA properly treats the CAE funds and Excess CAE funds as "Bonds," subject to modification under Title VI, and Counts I and II must therefore be dismissed.

IV. COUNT III FAILS BECAUSE SAN JUAN DOES NOT POSSESS SETOFF RIGHTS OR A STATUTORY LIEN ENTITLING IT TO A SEPARATE VOTING POOL.

In Count III, San Juan contends the RSA contemplates pooling San Juan with unsecured creditors for voting purposes, which it claims is improper because San Juan (and the other Intervenor Municipalities) are allegedly the holders or beneficiaries of certain security

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[7] This is the law throughout the United States. *See, e.g.*, *Barnhill v. Johnson*, 503 U.S. 393 (1992); *Shaw v. United States*, 137 S. Ct.462 (2016).

[8] A certified translation of *Santos* can be found at Dkt. No. 55-2. A certified translation of *Portilla* can be found at Dkt. No. 62-5.

arrangements. (Am. Compl. ¶¶ 130-140.) First, San Juan argues that because it has deposits at GDB, it is entitled to set off those deposits against the loans it has received. (*Id.* ¶¶ 88, 134.) Second, San Juan argues that Article 20 of the Municipal Financing Act imposes a statutory lien on the CAE funds held in trust at GDB and that San Juan is the beneficiary of that lien. (*Id.* ¶¶ 36, 94-95, 135.) Third, San Juan makes a threadbare allegation that it is entitled to an equitable lien on funds placed in escrow. (*Id.* ¶ 136.) Based on those alleged security arrangements, San Juan argues it possesses setoff and lien rights entitling it to be assigned to a different voting pool from the unsecured creditors under PROMESA § 601(d)(3). (*Id.* ¶¶ 139-140.) None of these positions, however, are correct.

A. San Juan does not possess setoff rights under Puerto Rico law.

San Juan's depositor setoff claim turns on § 3222 of the Puerto Rico Civil Code, which authorizes an automatic setoff only if *all* the following criteria are met:

> (1) That each of the [entities] bound should be so principally, and that [each] be at the same time the principal creditor of the other;
>
> (2) That both debts consist of a sum of money or, when the things due are perishable, that they be of the same kind and also of the same quality, if the latter should have been stipulated;
>
> (3) That both debts are due;
>
> (4) That they be determined and demandable; and
>
> (5) That none of them is subject to any retention or suit instituted by a third person, and of which due notice has been given the debtor.

31 L.P.R.A. § 3222.

San Juan fails to allege facts sufficient to meet the third and fifth criteria. Subsection (3) is not met because San Juan does not allege that GDB's loans to San Juan are currently "due." Indeed, as the Court found in its order denying San Juan's motion for a preliminary injunction, there is no basis to allege that "both debts are due" since interest and principal payments on San

Juan's loan come due on a biannual basis over the next twenty-plus years, meaning that there is no current mutual obligation.[9] (Dkt. No. 72 at 15.) Additionally, subsection (5) is not met because GDB's loans are in fact subject to claims and lawsuits by other GDB creditors. (*Id.*); *see also* Complaint, *Brigade Leveraged Capital Structures Fund v. Padilla*, No. 16-01610 (FAB) (D.P.R. April 4, 2016) (Dkt. No. 1) (seeking to enjoin GDB from making any payments to creditors, including municipal depositors, on ground that such preferential payments would prejudice bondholders). Therefore, San Juan does not hold the setoff rights that it alleges under Puerto Rico law. Instead, it is merely the holder of unsecured debt.

PROMESA provides where two or more sets of bondholders both hold unsecured debt that does not have priority, is not guaranteed, and is not senior or subordinated debt, they should be grouped in the same Pool, as they maintain the same "priority or security arrangements." PROMESA § 601(d)(3). As such, GDB is statutorily required to pool San Juan's depositor claims with those of other creditors with "identical rights in security or priority." PROMESA § 601(d)(3)(E). Because San Juan does not have setoff rights, it must necessarily be grouped with the other unsecured creditors, as the RSA has properly done.

B. San Juan does not hold a lien against any funds.

1. 21 L.P.R.A. § 6016(c) does not create a "statutory lien."

San Juan's only alleged statutory basis for the existence of a "statutory lien" is 21 L.P.R.A. § 6016(c). (Am. Compl. ¶¶ 36, 94.) But the lien at issue does not arise *solely* from the force of that statute; instead, it relies on a separate trust agreement. Hence, it does not qualify as a statutory lien.

[9] Further, while San Juan admits only "a portion of its debt to the GDB is due bi-annually," San Juan seeks to set off the full amounts of their outstanding loans, which is not permissible under 31 L.P.R.A. § 3222.

11 U.S.C. § 101(53) defines "statutory lien" as a "lien arising *solely by force of a statute*." Put another way, a statutory lien is involuntary; it "arises automatically, and is not based on an agreement to give a lien or on judicial action." H.R. Rep. No. 95-595, at 314 (1977). Following that definition, courts have found statutory liens only when the underlying statute contains mandatory, self-executing "shall" language or its equivalent. The self-executing requirement is important. Statutory language requiring, for instance, that an entity *shall* place funds in a trust, simply creates an obligation. It nowhere imposes a lien, let alone a self-executing lien. In contrast, for example, the self-executing language in Cal. Gov't Code § 20574 providing that the California Public Employees' Retirement System (CalPERS) board "*shall have* a lien on the assets of a terminated [contracting] agency" withdrawing from CalPERS has been held to create a statutory lien. *In re City of Stockton*, 526 B.R. 35, 57 (Bankr. E.D. Cal. 2015) (emphasis added); *see also In re Ball*, No. 05-24915, 2006 WL 4847274, *3 (Bankr. D. Utah May 4, 2006) ("An attorney *shall have a lien* for the balance of compensation due from a client on any moneys or property owned by the client that is the subject of or connected with work performed for the client . . . .") (emphasis added); *In re Stern*, 44 B.R. 15, 18 (Bankr. D. Mass. 1984) ("The unit owner's share of the common expenses *shall constitute a lien* upon his unit and *shall be enforced* in the manner provided in section five of the chapter 254.") (emphasis added); *Fonseca v Gov't Emps. Ass'n*, 542 B.R. 628, 634 (B.A.P. 1st Cir. 2015).

Here, the statute San Juan cites (Am. Compl. ¶ 34) as forming the basis of its alleged statutory lien — 21 L.P.R.A. § 6016(c) — contains no affirmative language creating a lien. To the extent that provision contains any mandatory language, it is the following: "The [CRIM] shall deposit the proceeds of the special surtax in the account of the municipality in the Redemption Fund." 21 L.P.R.A. § 6016(c) (emphasis added). But the statutes make clear that

the Redemption Fund is a trust that the CRIM needs to establish at GDB; it does not come into existence on its own.[10] Thus, the lien that results from establishing that trust does not arise "solely by force of" the statute. Moreover, it is a situation where GDB holds funds in trust, and is directed to have the trust place the funds on deposit with the GDB. Thus, the question is only whether a statutory lien is imposed on the deposit (a loan to the GDB), and it is not. Additionally, that GDB holds funds in trust does not create a statutory lien either.

Additionally, the statutory definition of statutory liens expressly excludes "security interests," defined in turn as "lien[s] created by an agreement," such as exist here. 11 U.S.C. § 101(51); *see also Young v. 1200 Buena Vista Condos.*, 477 B.R. 594, 598 (W.D. Pa. 2012) (citing to Bankruptcy Code legislative history that a lien "cannot be both a statutory lien and a security interest"); *In re DBSI, Inc.*, 432 B.R. 126, 134 (Bankr. D. Del. 2010). Therefore, since the trust agreements are alleged to be integral to the creation of the asserted liens (Am. Compl. ¶ 94), the latter cannot be statutory liens under 11 U.S.C. § 101(53).

Finally, 21 L.P.R.A. § 5816 provides for payment of an "order of priority." A statutory priority provision for the payment of debt out of particular assets does not create a "statutory lien." *Strom v. Peikes*, 123 F.2d 1003, 1005 (2d Cir. 1941) (there is a "distinction to be drawn between statutes creating priority of distribution and statutes providing security for a creditor by awarding him a lien," and "[a] statute providing for priority in distribution . . . does not appear to create a lien"). Accordingly, 21 L.P.R.A. § 6016(c) does not create a statutory lien.

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[10] The Redemption Fund is defined as that fund "*established* by the [CRIM] with the [GDB]." 21 L.P.R.A. § 6002 (emphasis added). The trust is "established" under 21 L.P.R.A. § 5803(c) (Am. Compl. ¶ 30), which provides that "[t]he [CRIM shall have the following general powers and duties: … (c) *Establish* a trust with the [GDB] to receive all revenues collected from property taxes . . . ." 21 L.P.R.A. § 5803 (emphasis added). That section in turn ties to 21 L.P.R.A. § 5816, which provides that "the funds in the general trust that the [CRIM] *establishes* with the Government Development bank for Puerto Rico, pursuant to § 5803(c) of this title, shall be distributed by the CRIM in the following *order of priority*:…" 21 L.P.R.A. § 5816 (emphasis added). Thus, both § 5803 and § 5816 provide that a trust needs to be "establish[ed]."

2. Any lien that may be created by 21 L.P.R.A. § 6016(c) works in favor of the creditors of San Juan and not San Juan itself.

San Juan alleges that a statutory lien arises out of 21 L.P.R.A. § 6016(c). (Am. Compl. ¶ 36.) But any such lien would work in favor of the *creditors* of San Juan, not San Juan itself. That statutory provision makes clear that any resulting lien would ensure payment of municipal general obligation bonds. For example, subsection (c) refers to "the first lien." 21 L.P.R.A. § 6016(c).[11] That language refers to the guarantee to make principal and interest payments on "general obligations bonds or notes and the interest on obligations evidenced by notes in advance of municipal general obligation bonds which the municipality may incur."[12] Accordingly, the lien would secure the payment of obligations of the municipality. It would not secure any obligations of GDB to San Juan.

San Juan makes no allegation that it has the right to enforce any statutory lien in favor of its creditors. Indeed, San Juan cannot assert rights that a secured creditor has to collateral. *See* UCC § 9-601(a) (debtor cannot require secured party to foreclose on collateral); *In re Center Wholesale, Inc.*, 788 F.2d 541 (9th Cir. 1986). Therefore, San Juan cannot get the benefits of a lien (if one exists) that secures a debt owed to its creditors.

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[11] Section 6016(c) states that "[i]f the [GDB] determines that the deposits in said account in the Redemption Fund are not sufficient to cover any payment of the principal or interest on any outstanding municipal general obligation bonds or notes or any payment of the interest on any outstanding note in advance of municipal general obligation bonds, the [GDB] shall notify the [CRIM] and the [CRIM] shall deposit in said account an amount proceeding from other income to *the first lien established by this section* that, together with the deposits in said fund, shall be sufficient to make said payment…." 21 L.P.R.A. § 6016(c) (emphasis added). Further, nobody else, including municipal bondholders, has any statutory lien for the reasons discussed above, but that is not at issue in this brief since San Juan has no standing to assert such rights.

[12] When 21 L.P.R.A. § 6016(c) refers to "the first lien," it is referencing 21 L.P.R.A. § 6016(b)'s statement "[t]o make *this guarantee* effective . . . " Section 6016(b)'s use of "*this guarantee*," in turn, refers to § 6016(a), which provides that "[t]he good faith, credit and the power of the municipality to levy unlimited taxes are hereby committed for the prompt payment of the principal and interest on all obligations evidenced by general obligations bonds or notes and the interest on obligations evidenced by notes in advance of municipal general obligation bonds which the municipality may incur."

For all of the above reasons, it is clear that San Juan is not the holder of any statutory lien.

C. San Juan does not possess an equitable lien on funds placed in escrow, nor it is entitled to an equitable lien.

San Juan alleges vaguely that it is "entitled to an equitable lien on the funds placed in escrow." (Am. Compl. ¶ 136.) This argument fails for three reasons: (1) San Juan has not adequately pled the existence of any funds in escrow; (2) equitable liens do not exist under current Puerto Rico law; and (3) even if Puerto Rico law did recognize equitable liens, San Juan has not met the requirements to establish one.

First, beyond mere conclusory statements, the amended complaint never alleges the existence of an escrow. To show an escrow exists, San Juan would need to allege it delivered funds to GDB for GDB to hold until the "occurrence or nonoccurrence of a specified event." RESTATEMENT (THIRD) AGENCY § 8.06, cmt. d ("A holder of an escrow contracts to hold money, a deed, or some other asset until the occurrence or nonoccurrence of a specified event before a specified date."). Here, the Complaint contains no such allegations. Rather, it merely refers to "the funds placed in escrow" in conclusory terms (Am. Compl. ¶ 136), and then again mentions such "escrowed funds" without elaboration (*id.* ¶¶ 169-71). That is insufficient to plead escrowed funds exist.

Second, the Supreme Court of Puerto Rico does not recognize the doctrine of equitable liens.[13] As that court held long ago, "the doctrine of equitable liens . . . is not in force in Puerto Rico" and "no legal existence is recognized to implied liens, created by presumptions, such as equitable liens." *Rodriguez v. Solivellas & Co.*, 49 P.R.R. 618, 621 (P.R. 1936); *see also*

[13] A court's determination of a creditor's entitlement to an equitable lien on property must be made in accordance with applicable state law. *See Admiral Drywall, Inc. v. Cullen*, 56 F.3d 4, 4 (1st Cir. 1995).

Cornier v. Superior Court, 96 P.R.R. 246, 249 (P.R. 1968) (holding that there can be no attorney's lien on money obtained in a judgment or settlement because no statutory provision in Puerto Rico establishes the same).[14]

Third, even in jurisdictions that do recognize the doctrine of equitable liens, there are specific requirements that must be met: (1) the written contract must indicate the intention to charge particular property with a debt, or (2) the court may grant an equitable lien to ensure justice in a particular case. *See Beacon Tr. Co. v. Dolan*, 27 F.2d 247, 248 (1st Cir. 1928). Furthermore, (3) an equitable lien is available only when there is a "nexus" of particular property to a claim of unjust enrichment arising from a right to that property. *See* RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 56, cmt. a. Here, none of these conditions are satisfied. San Juan fails to allege which contractual agreement, if any, it is referring to with respect to funds in escrow giving rise to an equitable lien. And to the extent San Juan is referring to the CAE funds, the contractual agreement between GDB and San Juan expressly stated that GDB was required to deposit CAE funds and Excess CAE funds in general deposit accounts, making them like all other funds in deposit accounts — that is, as a matter of law, loans subject to Title VI modification.

Finally, an equitable lien is an extraordinary remedy that should not be applied where an adequate remedy at law exists. 53 C.J.S. Liens § 19 (2017). The First Circuit has rejected attempts to provide equitable remedies where other remedies are available, even if the creditor in question has failed to qualify for them. *See Uniroyal, Inc. v. Universal Tire & Auto Supply Co.*, 557 F.2d 22, 23 (1st Cir. 1997) ("Efforts by courts to fashion equitable solutions to mitigate the hardship on particular creditors of literal application of statutory filing requirements would have

[14] The official English translations of *Rodriguez* and *Cornier* are attached to the accompanying Declaration of Mark D. Harris (the "Harris Decl.") as Exhibits A and B, respectively.

the deleterious effect of undermining the reliance which can be placed upon them. The harm would be more serious than the occasional harshness resulting from strict enforcement."). If San Juan is able to prove its breach of trust claims against the GDB, it will have an adequate remedy at law under the contract. (*See* Am. Compl. ¶¶ 163-27.) Therefore, San Juan's equitable lien claim should be dismissed because San Juan has failed to properly plead the grounds for such extraordinary relief.

D. Even if San Juan were entitled to setoff, it would not hold a secured claim.

Even if San Juan held setoff rights, it would not hold a secured claim entitling it to be placed in a separate voting pool. According to San Juan, "analogous bankruptcy law establishes that any claim subject to a valid right of setoff is secured to the extent of the amount of the setoff." (Am. Compl. ¶ 133.) While San Juan does not cite any "analogous bankruptcy law," it presumably relies on §§ 506 and 553 of Chapter 11 for its assertion that setoff rights equal a secured claim. *See* 11 U.S.C. § 553 ("this title does not affect any right of a creditor to offset a mutual debt owing by such creditor to the debtor . . ."); 11 U.S.C. § 506(a)(1) ("An allowed claim . . . that is subject to setoff under section 553 of this title, is a secured claim . . .").

While it may be true in the Chapter 11 context that §§ 506 and 553 provide that a setoff claim is a secured claim, those sections have no application in this Title VI case. Section 301 of PROMESA expressly incorporates §§ 506 and 553 from Chapter 11, but those sections are only incorporated in Title III cases. *See* PROMESA § 301 (sections 506 and 553 of title 11 "apply in a case *under this title*") (emphasis added). Thus, while a right to setoff may entitle a creditor to a secured claim under Title III, San Juan's claim arises under Title VI, and San Juan alleges no basis to support its claim that it holds a secured claim under Title VI.

Therefore, Count III must be dismissed.

V. COUNT IV DOES NOT STATE A CLAIM BECAUSE PROMESA AND THE FOMB'S BYLAWS PERMIT OUTSIDE PROFESSIONALS TO PARTICIPATE IN EXECUTIVE SESSIONS.

In Count IV, San Juan contends "on information and belief" that the FOMB inappropriately held "closed door meetings with professionals not employed by the Board." (Am. Compl. ¶ 146.) According to San Juan, PROMESA and the FOMB's bylaws supposedly allow only professionals "under the FOMB's employ" to attend executive sessions of the FOMB. (*Id.*) That claim utterly fails, however, because there is no such limitation.

Section 101(h)(4) of PROMESA allows the FOMB to conduct an executive session attended by its own voting members as well as "*any* professionals the Oversight Board determines necessary." PROMESA §101(h)(4) (emphasis added). The text of the statute says nothing about how those professionals must be employed. Rule 4.7 of the FOMB's bylaws makes the broad scope of §101(h)(4) even clearer. That Rule authorizes the FOMB to include "any professionals of the Board, *including staff and advisers*, [that] the Board determines necessary." (Am. Compl., Ex. K (Dkt. 88-11), Rule 4.7 (emphasis added).) Thus, the Rule explicitly contemplates attendance by professionals who are *not* staff and advisers — that is, professionals who are not employed by the FOMB. San Juan is trying to read into these provisions a restriction simply not there.

Even if there were some requirement that outside professionals could not participate in an executive session unless they were employed by the FOMB, San Juan offers no basis to conclude the RSA should be invalidated merely if one were present. The Modification may be nullified if and only if it is "manifestly inconsistent" with § 601. Therefore, even if an executive session were improperly held (it was not), there is no basis to invalidate the vote or the certification on this basis alone. For these reasons, Count IV must be dismissed.

VI. COUNT VI DOES NOT STATE A CLAIM BECAUSE THE MORATORIUM ACTS AND ORDERS ARE NOT PREEMPTED BY PROMESA.

In Count VI, the Complaint alleges that a number of moratorium acts and orders issued by Puerto Rico are preempted by PROMESA § 303(3).[15] As the Complaint correctly acknowledges, those legislative and executive measures were implemented to stop certain municipal withdrawals and transfers out of GDB. *See, e.g.*, 2017 P.R. Laws 5 § 204 (granting the Governor the authority to order "the limitation, postponement or suspension of any payment . . . to address the Bank's liquidity needs or facilitate the Bank's ability to carry out its operations"). (Am. Compl. ¶ 49.)

Not only does the Complaint fail to allege *how* the Moratorium Acts and Orders are inconsistent with § 303(3), but in fact the contrary of San Juan's arguments is true: § 303 actually *authorizes* the actions taken in those measures. Thus, there is no basis for San Juan's claim of preemption.

Section 303(3) of PROMESA contains a general reservation of territorial power to Puerto Rico, which explicitly includes the power to control its instrumentalities. The very title of that section is: "Reservation of territorial power to control territory and *territorial instrumentalities*." PROMESA § 303(3) (emphasis added). Likewise, the preamble recites that PROMESA does not limit or impair the power of a covered territory to "control, by legislation or otherwise, the territory or any territorial instrumentality." *Id*. San Juan is included in the statutory definition of a territorial instrumentality, of course, as is GDB itself. *See id.* § 5(19)(A) (defining the term as "any political subdivision . . . including any instrumentality that is also a bank"). Thus, on its

[15] *See* Puerto Rico Financial Emergency Moratorium and Financial Rehabilitation Act (2016 P.R. Laws Act 21, the "Moratorium Act"), the Puerto Rico Financial Emergency and Fiscal Responsibility Act (2017 P.R. Laws Act 5, the "Fiscal Responsibility Act"), and several executive orders issued under those acts (EO 2016-10, EO 2016-14, and EO 2017-31 (collectively, the "Moratorium Acts and Orders")).

face, § 303(3) explicitly recognizes Puerto Rico's authority to "control" San Juan and prevent it from depleting GDB's limited monetary reserves.

To be sure, § 303 contains certain limitations on that reservation of territorial power, including an exclusion of "unlawful executive orders" that alter the "rights of holders of any debt of the territory or territorial instrumentality." PROMESA § 303(3). But San Juan has not shown anything unlawful about these executive orders. Finally, accepting San Juan's claim that the Moratorium Acts and Orders unlawfully prohibit municipalities from withdrawing their funds would render Title VI meaningless in this case. If all municipalities could simply run to GDB to withdraw their funds, a restructuring under Title VI could never be achieved. Such an interpretation must be rejected.[16]

VII. COUNT IX FAILS TO STATE A CLAIM BECAUSE PUERTO RICO NO LONGER RECOGNIZES CLAIMS FOR CONSTRUCTIVE TRUSTS.

In Count IX, San Juan seeks a constructive trust on "approximately $83.3 million in escrowed funds it has on deposit at the GDB." (Am. Compl. ¶ 169.) As discussed above (*see supra* at Point IV, C), the Amended Complaint does not adequately plead the existence of an escrow in the context of Count III; it merely includes conclusory allegations regarding purportedly escrowed funds. (Am. Compl. ¶¶ 136, 168-73.) As a result, it is unclear whether the allegedly escrowed funds San Juan seeks an equitable lien against in Count III are the same

[16] Unlike the first three counts, each of which concludes with a paragraph describing the declaratory relief that San Juan seeks regarding the RSA, it is not clear what relief San Juan seeks in Count VI. The final paragraph of that Count appears to claim that the RSA is invalid "to the extent that it purports to restructure San Juan's deposits at the GDB." (Am. Compl. ¶ 156.) San Juan should be disqualified from asserting that aspect of Count VI because it is a challenge to the RSA (*see* Point I *supra*), and also because it is not ripe, as it is based on future, contingent events, namely approval of the RSA (*see* Point II *supra*).

However, Count VI may also be challenging certain Moratorium Acts and Orders that allegedly prevent San Juan from withdrawing municipal deposits from the GDB, even though San Juan does not specifically allege that it attempted to make such withdrawals and was unable to do so. In that aspect, while San Juan may have standing to bring the claim, and it may be ripe, Count VI should be dismissed on grounds that it fails to state a claim, as discussed here (Point VI).

funds San Juan seeks a constructive trust against in Count IX. Either way, the claim for a constructive trust fails as a matter of law.

Under the Civil Code of Puerto Rico of 1931, certain common-law concepts such as constructive trusts were codified into Puerto Rico's statutory code. Almost from the outset, however, the Supreme Court of Puerto Rico criticized constructive trusts as unnecessary, because they were subsumed under the doctrine of unjust enrichment (which was also incorporated into the Civil Code). *Ruiz v. Ruiz*, 61 P.R.R. 794 (1943); *Luperena v. Autoridad de Transporte*, 79 D.P.R. 464 (P.R. 1956) (stating that "[a]lthough this Court has been willing to 'import' that doctrine into our civil law to prevent unjust enrichment, its application must be confined, in any event, to situations unforeseen by our positive law") (internal citation omitted).[17] Later, the Supreme Court of Puerto Rico limited the doctrine of constructive trusts even further, indicating that the doctrine had no place in Puerto Rico law. *See Rossy v. Superior Court*, 80 D.P.R. 729, 751 (P.R. 1958); Guaroa Velázquez, *El Fideicomiso (Trust) en Puerto Rico*, XXXV Rev. Jur. UPR. Vol. 2, 253; 259 (1966) (stating the notion of constructive trusts had been reduced to almost negligible terms and was essentially encompassed by the claim for unjust enrichment);[18] *Karon Bus. Forms, Inc. v. Skandia Ins Co Ltd.*, 80 F.R.D. 501, 506 (D.P.R. 1978) (providing constructive trusts are a common law principle unsuitable to an action brought under the civil law of Puerto Rico).[19]

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[17] The official English translations of *Ruiz* and *Luperena* are attached to the Harris Decl. as Exhibits C and D, respectively.

[18] The official English translation of *Rossy* and a certified English translation of *El Fideicomiso* are attached to the Harris Decl. as Exhibits E and F, respectively.

[19] The constructive trust sought here would not even qualify under the unjust enrichment doctrine. Under Puerto Rico law, the doctrine of unjust enrichment will only apply under a strict set of limited circumstances: (1) the existence of an enrichment, (2) a correlative impoverishment, (3) a connection between the enrichment and the impoverishment, (4) a lack of cause to justify the enrichment, and (5) a lack of an applicable legal precept. *See Hatton v. Mun. of Ponce*, 134 D.P.R. 1001, 1010 (P.R. 1994); *Ocasio v. Alcalde Mun. de Maunabo*, 121 D.P.R. 37, 54 (P.R. 1988). GDB's Enabling Act and the Municipal Finance Act create a concrete and precise statutory scheme

In 2012, Puerto Rico repealed the articles of the Civil Code that regulated trusts, specifically the requirements for the constitution and regulation of trusts. *See* Act 219. The purpose of that enactment was to supersede all prior civil code legislation and case law, including that allowing constructive trusts. Accordingly, after 2012, constructive trusts are flatly unavailable under Puerto Rico law.

Accordingly, San Juan's claim seeking a constructive trust fails as a matter of law.

VIII. THE FOMB JOINS IN GDB'S AND AAFAF'S ARGUMENTS FOR DISMISSAL OF COUNTS VII, VIII, AND X OF THE AMENDED COMPLAINT.

In Count VII, San Juan alleges that GDB breached its fiduciary duty under the Trust Agreement. (Am. Compl. ¶¶ 157-62.) In Count VIII, San Juan alleges that GDB breached the Trust Agreement. (*Id*. ¶¶ 163-67.) In Count X, San Juan alleges that GDB and AAFAF failed to disburse funds to San Juan in contravention of Act 5 of 2017. (*Id*. ¶ 174-79.)

None of these purported claims contain any allegations against the FOMB but are instead directed solely at the GDB or AAFAF. The FOMB joins in, and expressly incorporates, the arguments to dismiss these counts that are contained in GDB's and AAFAF's concurrently filed motion to dismiss the Amended Complaint.

CONCLUSION

For the foregoing reasons, San Juan's Complaint should be dismissed in its entirety. Because San Juan has already amended its complaint once, it should not have a second opportunity to do so. Therefore, the Complaint should be dismissed with prejudice.

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governing the deposited funds, which allows for and provides for legal remedies when necessary. Therefore, San Juan cannot meet the fifth criterion for unjust enrichment.

Dated: January 8, 2018
New York, NY

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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/ Carla García-Benítez
Carla García-Benítez