

Bond Case Briefs

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BANKRUPTCY - PUERTO RICO

In re Financial Oversight and Management Board for Puerto Rico

United States District Court, D. Puerto Rico - February 27, 2018 - F.Supp.3d - 2018 WL 1475387

Financial guarantee insurer that insured certain bonds issued by Puerto Rico Highways and Transportation Authority (PRHTA) brought action challenging Financial Oversight and Management Board's certification of fiscal plans pursuant to Title III of Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) permitting PRHTA to default on scheduled bond payment.

Defendants moved to dismiss.

The District Court held that:

- Insurer had standing to bring action;
- Insurer's claim for declaratory judgment regarding PRHTA's right to prohibit disbursement of reserve account did not present justiciable issue to extent that claim was premised on insurer's assertion of lien interest in reserve account funds;
- Insurer's takings claim was not ripe for adjudication;
- District court lacked subject matter jurisdiction over claims seeking invalidation of Financial Oversight and Management Board's certification of fiscal plan;
- Board's fiscal plan was not "state law" within meaning of Contracts Clause;
- Puerto Rico's adoption of Puerto Rico Emergency Moratorium and Financial Rehabilitation Act and related actions did not violate Contracts Clause;
- PROMESA did not preempt Puerto Rico Emergency Moratorium and Financial Rehabilitation Act; Bondholders could not bring suit under PROMESA so long as automatic stay was in effect;
- PRHTA was not required to turn over pledged special revenues to bondholders; and Bondholders did not have outright ownership interest in funds held in reserve accounts.

Financial guarantee insurer that insured certain bonds issued by Puerto Rico Highways and Transportation Authority (PRHTA) sufficiently pled redressable injury to support its standing to bring action alleging that Financial Oversight and Management Board's certification of fiscal plans pursuant to Title III of Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) permitting PRHTA to default on scheduled bond payment, even though fiscal plan and fiscal plan compliance law did not discharge debt or eliminate liens, fiscal plan served merely as "blueprint" or "business plan," and insured was being paid from reserve accounts at time it commenced action, where funds that were originally available to service PRHTA's debt had been diverted as result of fiscal plan and fiscal plan compliance act, PRHTA defaulted on \$219 million bond payment, causing insurer to pay \$52 million in claims on certain financial guaranty insurance policies, as result of clawbacks effected through moratorium orders and moratorium legislation, and subordinate or junior obligations would effectively be afforded priority over PRHTA debt.

Claim by insurer that insured certain bonds issued by Puerto Rico Highways and Transportation

Authority (PRHTA) for declaratory judgment regarding PRHTA's right to prohibit disbursement of reserve account presented justiciable issues to extent that insurer asserted that PRHTA had insufficient property interests to prevent payments, but not to extent that claim was premised solely on insurer's assertion of lien interest in reserve account funds, where determination of lien interest, standing alone, would not resolve conclusively question of whether, when, and from what, if any, funds PRHTA bondholders were entitled to be paid.

Claim by insurer that insured certain bonds issued by Puerto Rico Highways and Transportation Authority (PRHTA) that Puerto Rico government's moratoriums on payments to holders of PRHTA bonds pursuant to Title III of Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) violated Takings Clause by depriving it and PRHTA bondholders of their senior secured property interests in PRHTA pledged special revenues without providing them with just compensation was not ripe for adjudication, where PROMESA Title III contemplated that oversight board would propound plans of adjustment for Commonwealth and PRHTA, but no final resolution had yet been made.

District court lacked subject matter jurisdiction over claims by insurer that insured certain bonds issued by Puerto Rico Highways and Transportation Authority (PRHTA) seeking invalidation of Financial Oversight and Management Board's certification of fiscal plan pursuant to Title III of Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) permitting PRHTA to default on scheduled bond payment; under PROMESA's statutory framework, it was only at plan confirmation stage that court could determine whether proposed plan of adjustment complied with provisions of Title 11 made applicable by PROMESA.

Fiscal plan adopted by Financial Oversight and Management Board pursuant to federal Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) was not "state law" within meaning of Contracts Clause.

Financial guarantee insurer that insured certain bonds issued by Puerto Rico Highways and Transportation Authority (PRHTA) failed to establish that Puerto Rico's adoption of Puerto Rico Emergency Moratorium and Financial Rehabilitation Act authorizing its governor to prioritize payment of essential services over covered obligations, governor's issuance of executive orders thereunder declaring moratoriums on PRHTA bonds, and Puerto Rico's adoption of fiscal plan compliance act adjusting territory's existing legal and juridical framework to ensure full compliance with fiscal plan certified by Financial Oversight and Management Board pursuant to Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) were unreasonable or unnecessary to effectuate important government purpose, as required to state claim under Contracts Clause, despite insurer's contention that less drastic alternatives were available, where Puerto Rico legislature passed legislation to address health, safety, welfare, and economic crises facing Puerto Rico, and Congress enacted PROMESA to "protect a basic societal interest."

Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) section providing that territory law prescribing method of composition of indebtedness or moratorium law could not bind non-consenting creditor did not preempt Puerto Rico Emergency Moratorium and Financial Rehabilitation Act authorizing its governor to prioritize payment of essential services over covered obligations or governor's issuance of executive orders thereunder declaring moratoriums on bonds issued by Puerto Rico Highways and Transportation Authority (PRHTA), where legislation and executive orders only authorized temporary extensions of PRHTA insurer's obligations, did not empower commonwealth to discharge, cancel, or force surrender of any bonds, and neither prohibited payment of principal and interest nor purported to bind creditors to any reduction of outstanding obligations.

Holders of bonds issued by Puerto Rico Highways and Transportation Authority (PRHTA) could not bring suit under provision of Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) permitting actions to recover property of any territorial instrumentality of Puerto Rico transferred in violation of applicable law under which creditors had valid pledge of, security interest in, or lien on such property, or which deprived any such territorial instrumentality of property in violation of applicable law so long as stay was in effect pursuant to Bankruptcy Code, as made applicable by PROMESA.

Puerto Rico Highways and Transportation Authority (PRHTA) was not required to turn over pledged special revenues allegedly securing PRHTA bonds to PRHTA bondholders during pendency of proceeding under Title III of Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) imposing moratorium on PRHTA bond payments.

Puerto Rico Oversight, Management, and Economic Stability Act's (PROMESA) prohibitions on interference with debtor property interests, revenues, and use and enjoyment of income-producing property deprived district court of power to interfere with bondholders' dealings with Puerto Rico Highways and Transportation Authority (PRHTA) bonds' reserve fund property, where resolutions pursuant to which PRHTA issued bonds contemplated that PRHTA had title or at minimum some contingent reversionary beneficial interest in trust corpus.