IN THE UNITED STATES DISTRICT COURT
DISTRICT OF PUERTO RICO

U.S. Bank Trust National Association, Plaintiff, v. The Commonwealth of Puerto Rico, *et al.*, Defendants.	:	Civil No. 16-2510 (FAB)

REPLY OF PLAINTIFF U.S. BANK TRUST NATIONAL ASSOCIATION TO DEFENDANTS' OPPOSITION [ECF NO. 33]

Plaintiff U.S. Bank Trust National Association ("Trustee"), hereby replies to the opposition [ECF No. 33] (the "Opposition") filed by the Commonwealth and the Governor, to which defendants UPR and Dr. Celeste Freytes González have joined, to the Trustee's Motion [ECF No. 2] for (i) relief from the PROMESA stay and (ii) preliminary injunctive relief.[1]

I. The Trustee Has Shown Cause to Lift the PROMESA Stay to Permit its Preliminary Injunction Application to Proceed

Defendants contest none of the key facts, set forth in the Motion, that demonstrate the existence of cause to lift the PROMESA stay:

- The UPR Bonds are secured by revenues that UPR collects from third parties, including student tuition and fees. UPR is required to transfer all such Pledged Revenues to the Trustee to hold as collateral for the UPR Bonds.

[1] Capitalized terms not defined herein shall have the meanings given them in the Memorandum of Law [ECF No. 3].

- Since June 2016, UPR has transferred no Pledged Revenues to the Trustee, in violation of its obligations under the Trust Agreement. As a result, the Bond Service Account currently has a balance of zero.

- UPR receives a large portion of its annual tuition and fee revenues in September and October. Consequently, UPR has already received and diverted substantial amounts of such revenues, and prompt relief is needed to prevent its continued diversion of these funds.

- Once the Trustee's collateral has been diverted, it is gone forever. The after-the-fact relief provided by the Moratorium Act is grossly inadequate – e.g., an unsecured second-priority claim against the Commonwealth (which has defaulted on its debts and been adjudged insolvent), in place of cash collateral that, if not diverted, would assure full payment of the UPR Bonds.

- Honoring its legal obligations to the Trustee will cause UPR little harm, since the Pledged Revenues required to satisfy debt service on the UPR Bonds constitute less than 3% of UPR's budget for the current fiscal year.

See Trustee's moving brief ("Br.") at 4-12, 16-17.

These undisputed facts constitute ample cause to lift the stay.

Indeed, Defendants do not dispute that bankruptcy courts applying the "cause" standard of Bankruptcy Code § 362, on which PROMESA's stay provisions were modeled, have uniformly held that that a secured creditor's loss of collateral constitutes cause to lift the stay. *See* Br. 11-12.

Defendants contend that the Trustee "has shown no harm to the UPR Bonds from the automatic stay, let alone *irreparable* harm," but merely a "delay in recouping" the Pledged Revenues that UPR is now diverting. (Opp. 5; emphasis in original.) This overlooks the obvious: UPR's diversion of tuition, fees and other Pledged Revenues does not merely delay the Trustee's receipt of such funds; it permanently deprives the Trustee of this promised collateral. As noted in our moving brief – and not disputed by Defendants – the only remedies provided by

the Moratorium Act for this taking of the Trustee's collateral are (i) a potential claim against the Commonwealth that would be junior in priority to general obligation debt claims, which the Commonwealth says it cannot pay;[2] and (ii) a potential "adequate protection" claim that is worth little because the only substitute collateral UPR could offer is the future revenues that it hopes to receive from the Commonwealth. *See* Br. 16-17. These remedies are no substitute for the collateral for which the UPR Bondholders bargained, which if not diverted would have assured full payment of the UPR Bonds.

It is true, but of no moment, that under the Moratorium Act the UPR Bonds will continue to accrue interest, and the Trustee's claims and liens will be preserved, rather than discharged. *See* Opp. 5 (citing Moratorium Act §§ 202, 204(a), 405(k)). These provisions do not protect the Trustee from the plundering of its collateral, which if not halted will transform the Trustee from a fully secured creditor entitled to be paid in full to a second-priority unsecured creditor that may eventually be paid pennies on the dollar.

Defendants' contention that, "if UPR bondholders . . . can lift the stay based solely on the alleged insolvency of their debtor, then any bondholder whose payments may have been suspended during the emergency period . . . would have equal grounds to lift the stay" (Opp. 6) betrays a similar confusion. The Trustee is entitled to stay relief because it is a secured creditor whose collateral is being taken – a harm that unsecured bondholders do not face. The Commonwealth's status as an adjudged insolvent does not by itself entitle the Trustee to stay relief; rather, it heightens the Trustee's need for stay relief by making inadequate any after-the-fact remedy for the taking of the Trustee's collateral.

[2] The one after-the-fact remedy provided by PROMESA § 407 – a potential damages claim against the recipient of unlawfully transferred collateral – is similarly inadequate (as Defendants again do not dispute), given the asserted inability of the Commonwealth and its instrumentalities to pay their debts. *See* Br. 17.

Defendants' contention that the standards for stay relief under PROMESA differ from those under the Bankruptcy Code is equally unsupported.

Defendants point, first, to the fact that PROMESA § 405(e) does not *expressly* state that the absence of adequate protection constitutes "cause." But the absence of such language does not mean that Congress meant to exclude the taking of a secured creditor's collateral from the circumstances that can constitute cause. To the contrary, such a reading of cause would contravene the established tenet of statutory construction that Congress should not be presumed to modify longstanding principles of law – here, the long-settled principle that the taking of collateral is a quintessential type of cause[3] – unless Congress clearly indicates its intent to do so. *See, e.g., Cohen v. de la Cruz*, 523 U.S. 213, 221 (1998) (courts should not read the Bankruptcy Code to "erode past bankruptcy practice absent a clear indication that Congress intended such a departure.") (citation omitted).

Far from supporting such an interpretation, PROMESA's legislative history makes clear that Congress did *not* intend to narrow the meaning of cause to exclude harms to secured creditors. The House Report for PROMESA states unequivocally and without exception that irreparable harm constitutes cause under § 405(e). *See* H.R. Rep. No. 114-602, 114th Cong., 2d Sess. at 51 (2016) ("If a party is determined to be subject to irreparable damage because of the imposition of the stay, the District Court is authorized to grant relief from the stay to such party."). As shown in our moving brief (at 20-21), the courts have uniformly held that depriving a secured creditor of its collateral constitutes irreparable harm.

[3] The concept of adequate protection "is derived from the Fifth Amendment protection of property interests." H.R. Rep. No. 95-595, 95th Cong., 1st Sess. at 339 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5787, 6295. "Case law had made adequate protection of the secured creditor a major consideration long before the draft predecessor of the [1978 Bankruptcy Code] proposed to codify it as a requirement." *In re Timbers of Inwood Forest Associates, Ltd.*, 793 F.2d 1380, 1390 (5th Cir. 1986), *aff'd*, 484 U.S. 365 (1988).

Similarly, Defendants have it backwards when they argue that lifting the stay to remedy UPR's taking of the Trustee's collateral "would . . . fly in the face of the choices that Congress made in enacting PROMESA," in that it would "pretermit the Oversight Board's review." Opp. 7-8. PROMESA's provisions are carefully designed to preserve the status quo during the period prior to the commencement of a Title III restructuring. To this end, PROMESA provides for the creation of an automatic stay (§ 405(b)), which is to be lifted for cause (§ 405(e)). At the same time, PROMESA expressly protects creditors from unlawful transfers (§ 407(a)) and the impairment of obligations and liens securing such obligations (§ 405(k)). If the stay is not lifted in the present case, the Trustee will be without redress for UPR's taking of its collateral – and the Commonwealth and UPR will have been allowed to alter the status quo in their favor, without judicial review, before the Oversight Board can act. In contrast, the relief the Trustee seeks will simply preserve the status quo for which the parties bargained.

Finally, Defendants argue that lifting the stay in this case could lead other plaintiffs to seek to lift the stay with respect to their claims, which in turn could lead to a multiplicity of actions and could divert the Commonwealth's attention from restructuring negotiations. Opp. 8. This ignores this Court's ability and broad discretion to manage stay litigation and any resulting merits litigation appropriately and efficiently, so as to minimize the burden on the Court and the parties. Moreover, Defendants should not be permitted to use PROMESA as a shield to protect their unlawful conduct from judicial review, nor should they be heard to complain of litigation burdens caused by their own misconduct.

II. Defendants Do Not Dispute the Existence of Cause to Lift the PROMESA Stay to Permit the Application of Trust Funds in the Trustee's Possession

We noted in our moving brief (at 23-24) that the Commonwealth does not appear to have any objection to the Trustee's application of funds in its possession for uses permitted by the

Trust Agreement, and that the Moratorium Act excludes such funds from its scope. Neither the Commonwealth nor UPR has objected to our request for such stay relief, and we respectfully request entry of an order granting such relief.

III. The Factual Record Establishing Cause to Lift the Stay Also Demonstrates the Need For the Prompt Issuance of a Preliminary Injunction

As shown in our opening brief (at 14-22), the same facts that warrant a lifting of the stay also demonstrate the need for and the appropriateness of a preliminary injunction requiring Defendants to transfer pledged tuition and fees to the Trustee during the pendency of this case.

As noted above (at pp. 1-2), Defendants contest none of those key facts.

At the hearing scheduled to commence later this week, Defendants have said they intend to present four witnesses to respond to the stay requests of the Trustee and the plaintiffs in the three other consolidated cases. But the Trustee's case for relief from the stay is identical to the Trustee's case for a preliminary injunction – the allegations are the same, the law is the same and the Defendants' burden to rebut, with evidence, the Trustee's evidence (based on the defendants' own documents) is the same. Given the identical factual and legal issues raised by the Trustee's lift-stay and preliminary injunction requests, a duplicative and unnecessary second hearing should not be required to grant the Trustee's preliminary injunction application. Such duplicative and unnecessary process would allow the Defendants to continue the expropriation of collateral that justified relief from the stay in the first place, further prejudicing the Trustee.

We therefore request that, at this week's hearing, the Court hear the parties' evidence on all aspects of the Motion. If at the close of the hearing the Court finds that the facts and law warrant such relief, we ask that the Court enter both an order granting relief from the PROMESA stay and a preliminary injunction as requested in the Motion.

CONCLUSION

For the reasons set forth above and in the Motion, the Trustee requests entry of an order, in the form attached to the Motion, (i) granting relief from the PROMESA stay and (ii) requiring Defendants to transfer pledged tuition and revenues to the Trustee, to the extent necessary to satisfy the Bond Service Account Requirement and the Reserve Account Requirement, subject to reversion to the extent required by any final judgment in this case.

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 notify the attorneys of record.

RESPECTFULLY SUBMITTED.

In San Juan, Puerto Rico, today September 19, 2016.

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