

**IN THE UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF PUERTO RICO**

\_\_\_\_\_  
In re: )  
 )  
 ) PROMESA  
THE FINANCIAL OVERSIGHT AND )  
MANAGEMENT BOARD FOR PUERTO RICO, ) Title III  
 )  
 ) Case No. 3:17-bk-03283 (LTS)  
as representative of )  
 )  
THE COMMONWEALTH OF PUERTO RICO, *et al.*, )  
 )  
Debtors. )  
 )

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In re: )  
 )  
 ) PROMESA  
THE FINANCIAL OVERSIGHT AND )  
MANAGEMENT BOARD FOR PUERTO RICO, ) Title III  
 )  
 ) Case No. 3:17-bk-03566 (LTS)  
as representative of )  
 )  
THE EMPLOYEES RETIREMENT SYSTEM OF THE )  
GOVERNMENT OF THE COMMONWEALTH OF )  
PUERTO RICO, )  
 )  
Debtor. )  
 )

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**MOTION OF CERTAIN SECURED CREDITORS  
OF THE EMPLOYEES RETIREMENT SYSTEM OF THE  
GOVERNMENT OF THE COMMONWEALTH OF PUERTO RICO  
FOR APPOINTMENT AS TRUSTEES UNDER 11 U.S.C. § 926**

**TABLE OF CONTENTS**

	<b>Page</b>
TABLE OF AUTHORITIES .....	iii
PRELIMINARY STATEMENT .....	1
JURISDICTION AND VENUE .....	3
FACTUAL BACKGROUND.....	4
A. From Its Creation, ERS Was Intended To Be A Trust Independent From The Commonwealth.....	4
B. Congress Enacts PROMESA And The Oversight Board Begins Representing Both The Commonwealth And ERS.....	6
C. The Commonwealth And The Oversight Board Pass Legislation Dismantling ERS And Seizing Its Assets While ERS Is A Title III Debtor Protected By The Automatic Stay.....	7
ARGUMENT .....	8
THE COURT SHOULD APPOINT THE BONDHOLDERS TRUSTEES UNDER § 926 OF THE BANKRUPTCY CODE.....	8
A. Section 926 Permits A Title III Court To Appoint A Trustee To Pursue Avoidance Actions On Behalf Of The Debtor.....	9
B. ERS Has Claims Against The Commonwealth Under § 549 And § 544 That The Oversight Board Has Unjustifiably Failed To Pursue.....	10
1. A Trustee Could Avoid The Transfers Effected By The Post- Petition Legislation Under § 549 .....	10
2. A Trustee Could Also Avoid The Transfers Effected By The Post-Petition Legislation Under § 544.....	12
C. The Oversight Board Is Laboring Under A Deeply Problematic And Unresolvable Conflict Of Interest Because It Is Representing Parties With Opposing Interests In The Same Case And Disregarding The Best Interest Of One Of Those Parties.....	14
1. The Oversight Board Has Ignored ERS’s Independent Status Under PROMESA And Puerto Rico Law, As Well As ERS’s Fiduciary Duties To Its Creditors .....	14
2. The Conflict Is Actual, Not Theoretical .....	16
3. Elsewhere The Oversight Board Has Acknowledged That It Cannot Represent Both Sides To A Controversy .....	17
4. This Court Too Has Recognized The Danger Of Conflicts Of Interest.....	18

**TABLE OF CONTENTS**  
(continued)

	<b>Page</b>
D. Timely Appointment Of A Trustee Is Crucial Because The Statute Of Limitations Expires Two Years From The Commencement Of The Case Or The Date Of The Transfer.....	19
E. The Court Should Appoint The ERS Bondholders Trustees; In The Alternative, The Court Should Appoint A Trustee Approved By The Bondholders To Pursue ERS’s Claims .....	20
CONCLUSION.....	20

**TABLE OF AUTHORITIES**

	<b>Page(s)</b>
<b>CASES</b>	
<i>Acands, Inc. v. Travelers Cas. &amp; Sur. Co.</i> , 435 F.3d 252 (3d Cir. 2006).....	17
<i>Aurelius Inv., LLC v. Puerto Rico</i> , No. 18-1671, 2019 WL 642328 (1st Cir. Feb. 15, 2019).....	19, 20
<i>Commodity Futures Trading Comm’n v. Weintraub</i> , 471 U.S. 343 (1985).....	15
<i>De Jesus Diaz v. Carrero</i> , 12 P.R. Offic. Trans. 786 (P.R. 1982).....	13
<i>In re Bankvest Capital Corp.</i> , 375 F.3d 51 (1st Cir. 2004).....	10
<i>In re Delco Oil, Inc.</i> , 599 F.3d 1255 (11th Cir. 2010) .....	11
<i>In re Gibson Grp., Inc.</i> , 66 F.3d 1436 (6th Cir. 1995) .....	10
<i>In re Lopez-Soto</i> , 764 F.2d 23 (1st Cir. 1985).....	17
<i>In re Marrero</i> , 382 B.R. 861 (B.A.P. 1st Cir. 2008).....	10, 11
<i>In re Merry-Go-Round Enters., Inc.</i> , 400 F.3d 219 (4th Cir. 2005) .....	12
<i>In re N.Y. City Off-Track Betting Corp.</i> , No. 09-17121, 2011 WL 309594 (Bankr. S.D.N.Y. Jan. 25, 2011) .....	10
<i>In re Owens Corning</i> , 419 F.3d 195 (3d Cir. 2005).....	15, 16
<i>In re Sepulveda Figueras</i> , 193 B.R. 118 (Bankr. D.P.R. 1996).....	13
<i>In re Tougas</i> , 338 B.R. 164 (Bankr. D. Mass. 2006) .....	10
<i>In re WHET, Inc.</i> , 750 F.2d 149 (1st Cir. 1984).....	15
<i>In re WM Distribution, Inc.</i> , 571 B.R. 866 (Bankr. D.N.M. 2017) .....	16
<i>U.S. Fid. &amp; Guar. Co. v. Guzman</i> , Nos. 10-1078 & 11-1415, 2012 WL 4790314 (D.P.R. 2016).....	13

**TABLE OF AUTHORITIES**

(continued)

	<b>Page(s)</b>
<i>Woods v. City Nat’l Bank &amp; Tr. Co. of Chi.</i> , 312 U.S. 262 (1941).....	15
<b>STATUTES AND RULES</b>	
3 L.P.R.A. § 761 .....	4
3 L.P.R.A. § 763 .....	4
3 L.P.R.A. § 775 .....	4
3 L.P.R.A. § 781 .....	8
3 L.P.R.A. § 787f.....	4
3 L.P.R.A. § 787q.....	4
31 L.P.R.A. § 3028 .....	12
31 L.P.R.A. § 3492 .....	12
11 U.S.C. § 301.....	19
11 U.S.C. § 362.....	3, 7, 12
11 U.S.C. § 544.....	<i>passim</i>
11 U.S.C. § 545.....	9
11 U.S.C. § 546.....	19
11 U.S.C. § 547.....	9
11 U.S.C. § 548.....	9
11 U.S.C. § 549.....	<i>passim</i>
11 U.S.C. § 550.....	3, 9
11 U.S.C. § 926.....	<i>passim</i>
28 U.S.C. § 1331.....	3
28 U.S.C. § 1391.....	3
48 U.S.C. § 301.....	17
48 U.S.C. § 2141.....	15
48 U.S.C. § 2161.....	<i>passim</i>
48 U.S.C. § 2162.....	6
48 U.S.C. § 2164.....	7, 15
48 U.S.C. § 2166.....	3
48 U.S.C. § 2167.....	3

**TABLE OF AUTHORITIES**

(continued)

	<b>Page(s)</b>
48 U.S.C. § 2175.....	6
48 U.S.C. § 2195.....	3, 15
Joint Resolution for Other Allocations for Fiscal Year 2017–2018 (“Joint Resolution 188” or “J.R. 188”).....	<i>passim</i>
Law to Guarantee Payment to Our Pensioners and Establish a New Plan for Defined Contributions for Public Servants (“Act 106”).....	<i>passim</i>
Puerto Rico Oversight, Management, and Economic Stability Act, Pub. L. No. 114-187, 130 Stat. 549 (2016), <i>codified at</i> 48 U.S.C. §§ 2101–2241.....	<i>passim</i>
Fed. R. Bankr. P. 6001.....	10
<b>OTHER AUTHORITIES</b>	
Collier on Bankruptcy (16th ed. rev. 2018).....	9, 10
Commonwealth of Puerto Rico, Financial Information and Operating Data Report (Oct. 30, 2014).....	4, 5
Commonwealth of Puerto Rico, Financial Information and Operating Data Report (Dec. 18, 2016).....	5
Emps. Ret. Sys. of the Gov’t of the Commw. of P.R., Annual Financial Information: Fiscal Year 2016.....	5

Movants (hereinafter the “Bondholders” or “ERS Bondholders”),<sup>1</sup> all of whom are secured creditors of the Employees Retirement System of the Government of the Commonwealth of Puerto Rico (“ERS”), respectfully move the Court for entry of an order appointing them as trustees, pursuant to § 926 of title 11 of the United States Code (the “Bankruptcy Code”), to pursue the claims in the attached proposed Complaint (Exhibit A) on behalf of ERS against the Commonwealth of Puerto Rico (the “Commonwealth”) or, in the alternative, appointing, with the Bondholders’ approval, an independent third-party fiduciary as trustee to pursue those claims in consultation with the Bondholders. In support of the motion, the ERS Bondholders state as follows:

### **PRELIMINARY STATEMENT**

The ERS Bondholders respectfully ask this Court to appoint them trustees under 11 U.S.C. § 926 to pursue avoidance claims against the Commonwealth under 11 U.S.C. §§ 549 and 544. Such relief is necessary because the Financial Oversight and Management Board (“Oversight Board” or “Board”) has refused to litigate those claims. That is unsurprising, because the claims arise from Commonwealth legislation, enacted *after* the commencement of ERS’s Title III case

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<sup>1</sup> Movants include Andalusian Global Designated Activity Company, Crown Managed Accounts for and on behalf of Crown/PW SP, Glendon Opportunities Fund, L.P., LMA SPC for and on behalf of Map 98 Segregated Portfolio, Mason Capital Master Fund LP, Oaktree-Forrest Multi-Strategy, LLC (Series B), Oaktree Opportunities Fund IX, L.P., Oaktree Opportunities Fund IX (Parallel 2), L.P., Oaktree Value Opportunities Fund, L.P., Oceana Master Fund Ltd., Ocher Rose, L.L.C., Pentwater Merger Arbitrage Master Fund Ltd., PWCM Master Fund Ltd., Puerto Rico AAA Portfolio Bond Fund, Inc., Puerto Rico AAA Portfolio Bond Fund II, Inc., Puerto Rico AAA Portfolio Target Maturity Fund, Inc., Puerto Rico Fixed Income Fund, Inc., Puerto Rico Fixed Income Fund II, Inc., Puerto Rico Fixed Income Fund III, Inc., Puerto Rico Fixed Income Fund IV, Inc., Puerto Rico Fixed Income Fund V, Inc., Puerto Rico GNMA & U.S. Government Target Maturity Fund, Inc., Puerto Rico Investors Bond Fund I, Puerto Rico Investors Tax-Free Fund, Inc., Puerto Rico Investors Tax-Free Fund, Inc. II, Puerto Rico Investors Tax-Free Fund III, Inc., Puerto Rico Investors Tax-Free Fund IV, Inc., Puerto Rico Investors Tax-Free Fund V, Inc., Puerto Rico Investors Tax-Free Fund VI, Inc., Puerto Rico Mortgage-Backed & U.S. Government Securities Fund, Inc., SV Credit, L.P., Tax-Free Puerto Rico Fund, Inc., Tax-Free Puerto Rico Fund II, Inc., and Tax-Free Puerto Rico Target Maturity Fund, Inc.

and *at the Oversight Board's behest*, purporting to dismantle ERS and transfer all of ERS's assets, including its revenues and its right to receive revenues, to the Commonwealth. And despite the fact that ERS was a debtor in its own Title III case and was an independent entity to which the Commonwealth owed statutory financial obligations, neither the Board's fiduciary duty to ERS nor ERS's fiduciary duty to its creditors appears to have been recognized or to have played any role in the Board's decisionmaking. Section 926 was designed for just such circumstances, in which a conflict of interest has disabled a debtor or its representatives from pursuing claims in the debtor's own best interest or that of its creditors.

Elsewhere the Oversight Board has recognized the impossibility of simultaneously representing the Commonwealth and other entities with interests adverse to those of the Commonwealth. For instance, in a dispute between the Puerto Rico Sales Tax Financing Corporation ("COFINA") and the Commonwealth—both of which the Board represents—the Board sought appointment of independent representation for COFINA (selected by COFINA creditors) and the Commonwealth (in the case of the Commonwealth, an official committee that did not have a disabling conflict) so that both COFINA and the Commonwealth would have loyal representatives and advisors. But here the Board has steadfastly refused to chart a similar course, even though the conflict in COFINA's case was in many respects less severe than the Board's total plundering and destruction of ERS at the hands of the Commonwealth.<sup>2</sup>

Congress provided tools for remedying such unusual and problematic situations in the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA"), Pub. L. No.

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<sup>2</sup> Neither the Official Committee of Unsecured Creditors nor the Official Committee of Retired Employees of the Commonwealth of Puerto Rico would be a suitable representative of ERS, because both committees represent both creditors of the Commonwealth and creditors of ERS, and therefore have the same conflicts as the Board and the Puerto Rico Fiscal Agency and Financial Advisory Authority.



114-187, 130 Stat. 549 (2016), *codified at* 48 U.S.C. §§ 2101–2241. *First*, PROMESA’s automatic-stay provision prohibits any attempt to gain possession of or control over a debtor’s property. 11 U.S.C. § 362(a)(3). The automatic stay forbids the Board and the Commonwealth’s actions destroying ERS and seizing its property. *Second*, PROMESA allows a debtor to avoid and recover the value of an unauthorized or fraudulent transfer of property. *See id.* §§ 544(b), 549(a), 550. The relevant provisions allow ERS to invalidate the Commonwealth’s legislation and recover ERS’s transferred property. *And third*, as noted, PROMESA allows a Title III court, on request of a creditor, to appoint a trustee to pursue avoidance claims where the debtor has refused to do so itself. *Id.* § 926(a). That appointment power was designed for just such cases as this one, where a debtor is unwilling or unable to sue a transferee, notwithstanding the debtor’s own best interest or that of its creditors.<sup>3</sup>

The Bondholders have attached a proposed Complaint setting forth ERS’s claims against the Commonwealth. The Bondholders have asked the Board to pursue these claims, as set forth in the attached letter, but the Board has failed to respond. Absent relief under § 926, neither interested parties nor the Court can be assured of a fair outcome, because they will not have benefited from the zealous advocacy on which our adversarial system relies. And time is of the essence, because the periods prescribed by the applicable statutes of limitations under PROMESA on these two claims expire in several months.

### **JURISDICTION AND VENUE**

This Court has jurisdiction over this motion pursuant to 28 U.S.C. § 1331 and 48 U.S.C. § 2166(a). Venue is proper pursuant to 28 U.S.C. § 1391(b) and 48 U.S.C. § 2167(a).

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<sup>3</sup> This list is not exhaustive. For example, PROMESA also provides a protection against inter-debtor transfers that is enforceable if the automatic stay is lifted. 48 U.S.C. § 2195.

## FACTUAL BACKGROUND

### A. From Its Creation, ERS Was Intended To Be A Trust Independent From The Commonwealth

In 1951, ERS was created by legislation as an independent, self-governing trust to provide pension and other benefits to officers and employees of the Commonwealth government, members and employees of the Legislative Assembly, and officers and employees of Commonwealth public corporations and municipalities. *See* 3 L.P.R.A. §§ 761, 775. ERS’s Enabling Act established a Board of Trustees responsible for setting policy for ERS and overseeing the operations of ERS consistent with the Act. *Id.*

Until legislation that took effect on July 1, 2017, *see infra* pp. 7–8, ERS was funded by employer contributions, employee contributions, and its investment earnings. *See, e.g.*, 3 L.P.R.A. §§ 763(42), 787f, 787q. Employers were required to pay monthly contributions to ERS. ERS’s “statutory right to receive [e]mployer[] [c]ontributions [was] an obligation of the [e]mployers and a legal asset of [ERS].” Bond Resolution VI-1, Adversary Compl., Ex. A, *Altair Glob. Credit Opportunities Fund (A), LLC v. Puerto Rico*, Adv. Proc. Nos. 3:17-ap-219 & 3:17-ap-220 (D.P.R. July 27, 2017), ECF No. 1-1 (“Bond Resolution”).

The Commonwealth was ERS’s largest participating employer. Historically, the Commonwealth was responsible for approximately 59 percent of employer contributions, while Puerto Rico municipalities and public corporations were responsible for the remainder. *See, e.g.*, Commonwealth of Puerto Rico, Financial Information and Operating Data Report 88 n.6, 130 (Oct.

30, 2014); Commonwealth of Puerto Rico, Financial Information and Operating Data Report 228 (Dec. 18, 2016).<sup>4</sup>

ERS had the statutory authority to compel the payment of unpaid employer contributions, and any contributions in arrears for more than 30 days had priority over any other outstanding debt of a public employer. Puerto Rico law also provided for criminal penalties for the failure to remit employer contributions to ERS in a timely manner.

Despite the importance of employer contributions to ERS, the Commonwealth has never paid ERS enough to satisfy its statutory contribution requirements. By the date of ERS's Title III petition, the Commonwealth owed ERS more than \$411 million. ERS, Annual Financial Information: Fiscal Year 2016, at 13 n.1.<sup>5</sup> ERS never used its statutory ability to enforce those obligations.

Consequently, ERS was forced to seek outside funding to continue paying pension benefits. In 2008, ERS issued bonds pursuant to and governed by a Pension Funding Bond Resolution. *See* Bond Resolution. The majority of ERS bonds were sold to individual Puerto Rico residents and local businesses, and many are still held by those persons and entities.

An integral part of ERS's bond issuance was an extensive security package designed to protect the bondholders' investment. ERS granted bondholders, through a Fiscal Agent, a security interest in and lien on certain ERS property, including, *inter alia*, all employer contributions received by ERS, all "right, title, and interest of [ERS] in and to" those contributions, and "all rights to receive [those contributions]." Bond Resolution § 501, at VI-8 & Ex. B, VI-36. That

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<sup>4</sup> Online at <http://www.gdb.pr.gov/documents/CommonwealthReport-October302014.pdf> and <http://www.gdb.pr.gov/documents/CommonwealthofPuertoRicoFinancialInfoFY201612-18-16.pdf>.

<sup>5</sup> Online at <https://emma.msrb.org/ER1050099-ER822796-ER1223828.pdf>.

property was to remain “free and clear of any other pledge, lien, charge, or encumbrance,” *id.* § 705, at VI-15, and was to be used to make timely principal and interest payments on ERS Bonds, *id.* § 501, at VI-8. Notably, ERS pledged its statutory right to collect employer contributions to secure the bonds, and that right was exercisable upon default. *Id.* § 501, at VI-8; *id.* § 1102, at VI-22. ERS further promised bondholders that it would “oppose any attempt by the Legislature of the Commonwealth to reduce the Employers’ Contribution Rate or to make any other change in ... relevant legislation that would have a material adverse effect on Bondholders.” *Id.* § 709(2), at VI-16.

**B. Congress Enacts PROMESA And The Oversight Board Begins Representing Both The Commonwealth And ERS**

On June 30, 2016, Congress enacted PROMESA. Under the financial restructuring authority provided by Title III of PROMESA, the Oversight Board filed petitions on behalf of both the Commonwealth and ERS on May 3 and 21, 2017, respectively, *see In re Fin. Oversight & Mgmt. Bd. ex rel. Puerto Rico (Puerto Rico)*, No. 17-bk-3283 (D.P.R.), ECF No. 1; *In re Fin. Oversight & Mgmt. Bd. ex rel. Emps. Ret. Sys. (ERS)*, No. 17-bk-3566 (D.P.R.), ECF No. 1; 48 U.S.C. §§ 2162, 2175, purporting to serve as each debtor’s representative despite ERS’s and the Commonwealth’s directly conflicting interests—as noted, the Commonwealth owes ERS vast sums of money. The Oversight Board continues to represent both debtors simultaneously—in some cases, even by the very same lawyers.

Notwithstanding the Oversight Board’s simultaneous representation of ERS and the Commonwealth, PROMESA treats each debtor as a separate entity. Territories and covered territorial instrumentalities are considered separate entities, 48 U.S.C. § 2162(1), and each entity gets to decide for itself whether it “desires to effect a plan to adjust its debts,” *id.* § 2162(3). And although the Oversight Board is the representative of each debtor, *id.* § 2175(b), PROMESA states

that “nothing in [Title III] shall be construed as authorizing substantive consolidation of the cases of affiliated debtors,” *id.* § 2164(f), even if the cases are administered jointly, *id.* § 2164(g).

**C. The Commonwealth And The Oversight Board Pass Legislation Dismantling ERS And Seizing Its Assets While ERS Is A Title III Debtor Protected By The Automatic Stay**

The filing of ERS’s Title III petition on May 21, 2017, triggered the operation of the automatic stay to protect ERS’s property. 11 U.S.C. § 362; 48 U.S.C. § 2161(a) (incorporating § 362 into PROMESA). On June 25, 2017, in total disregard of the ERS automatic stay, however, the Puerto Rico Legislative Assembly passed Joint Resolution for Other Allocations for Fiscal Year 2017–2018 (“Joint Resolution 188” or “J.R. 188”) pursuant to the Fiscal Plan the Oversight Board had approved and certified for the Commonwealth. On June 30, 2017, the Oversight Board adopted the resolution on behalf of the Governor, who subsequently signed it. Joint Resolution 188 required ERS to sell its assets and transfer the net proceeds, plus any available funds, into the Commonwealth’s General Fund. J.R. 188, §§ 1–3.<sup>6</sup> The resolution also required employers to make contributions directly to the Commonwealth’s General Fund rather than to ERS. *Id.* §§ 1–4.

On August 23, 2017, with the automatic stay still in effect, the Governor signed a Law to Guarantee Payment to Our Pensioners and Establish a New Plan for Defined Contributions for Public Servants (“Act 106”). Act 106 further implemented Joint Resolution 188. The law stated that Joint Resolution 188 “eliminated” “the employer contributions being made until now,” and purported to set up a new “Pay-Go’ Fee” that employers must pay directly into the Commonwealth’s General Fund. Act 106, § 1.4, pp. 13–14. As suggested by the title of the legislation, the “Pay-Go’ Fee” is nothing new, however, because the employers required to pay it

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<sup>6</sup> In its most recent fiscal plan, the Commonwealth admits that “[s]ince FY2018 ... the majority of the liquid assets in the retirement system have been depleted.” New Fiscal Plan for Puerto Rico 29 (Oct. 23, 2018).

are the same government entities (including the Commonwealth, public corporations, and municipalities) that were previously obligated to make contributions to ERS; indeed, even the “contributions” are the same obligations. *See id.* § 1.6(g), p. 15 (requiring payments from “entities considered employers under the [ERS]”); *compare id.* § 2.1(b), p. 17, with 3 L.P.R.A. § 781(a) (2008). Finally, Act 106 required ERS’s Board of Trustees to dissolve by December 31, 2017, so a new board could be formed to dispose of ERS’s property. Act 106, §§ 4.2, 5.1–5.3.

Act 106 and Joint Resolution 188 (together, the “Post-Petition Legislation”) were in the best interest of no one except the Commonwealth, which wanted ERS’s assets and property for other politically expedient purposes. The legislation, which dismantled ERS and seized its assets, was certainly not in ERS’s best interest. Nor was the Post-Petition Legislation in the best interest of ERS’s creditors. Instead, the Post-Petition Legislation purported to change the Commonwealth’s financial relationship with ERS by transferring all of ERS’s assets to the Commonwealth for its own purposes.

On January 28, 2019, the ERS Bondholders asked the Oversight Board to pursue on behalf of ERS the claims identified in this motion and the attached proposed Complaint. *See* Letter from Bruce S. Bennett and John K. Cunningham to Martin J. Bienenstock (Exhibit B). The Board acknowledged receipt of the letter on the same day, but has not responded.

## ARGUMENT

### **THE COURT SHOULD APPOINT THE BONDHOLDERS TRUSTEES UNDER § 926 OF THE BANKRUPTCY CODE**

The Oversight Board has declined to pursue ERS’s claims against the Commonwealth because it is suffering from an incurable conflict of interest given its simultaneous representation of both the Commonwealth and ERS and its role in mandating the Post-Petition Legislation. The Board’s inaction is deeply inequitable to both ERS and its creditors, to whom ERS owes a fiduciary

duty. But this Court can remedy the situation. By incorporating § 926 of the Bankruptcy Code, PROMESA authorizes a Title III court to appoint a trustee to prosecute certain types of avoidance actions the debtor has refused to pursue. The ERS Bondholders' proposed complaint identifies two such causes of action, one each under § 549 and § 544 of the Bankruptcy Code, that the Oversight Board should have asserted against the Commonwealth based on the Post-Petition Legislation's transfer of ERS's assets to the Commonwealth. A trustee appointed by this Court under § 926 would be able to avoid those transfers and recover their value for ERS and its creditors. The Oversight Board's conflict of interest in representing both the Commonwealth and ERS is the only possible explanation for its refusal to bring those valuable claims. Accordingly, the Court should appoint the Bondholders trustees under § 926. Alternatively, the Court should appoint an independent third-party fiduciary approved by the Bondholders as trustee to pursue those claims in consultation with the Bondholders.

**A. Section 926 Permits A Title III Court To Appoint A Trustee To Pursue Avoidance Actions On Behalf Of The Debtor**

Section 926 provides that “[i]f the debtor refuses to pursue a cause of action under section 544, 545, 547, 548, 549(a), or 550 of [the Bankruptcy Code], then on request of a creditor, the court may appoint a trustee to pursue such cause of action.” 11 U.S.C. § 926(a); *see* 48 U.S.C. § 2161(a) (incorporating § 926(a) into PROMESA). As relevant here, §§ 549 and 544 allow the debtor to avoid unlawful postpetition transfers, and § 550(a) allows the debtor to recover the transfers or their value from the transferee.

A conflict of interest is ample reason to appoint a trustee. *See generally* 6 Collier on Bankruptcy ¶ 926.02 (16th ed. rev. 2018) (“The reason for section 926(a) derives from the possible reluctance of a debtor to bring an action against one of its creditors during the course of a chapter 9 case,” whether because “the debtor actually favors the transfer rather than opposes it” or because

the debtor is unwilling, “while it is attempting to negotiate a plan, to antagonize its creditors.”). “Section 926 explicitly anticipates and is intended to address those scenarios in which the debtor does not consent to the pursuit of a cause of action.” *In re N.Y. City Off-Track Betting Corp.*, No. 09-17121, 2011 WL 309594, at \*6 (Bankr. S.D.N.Y. Jan. 25, 2011). As courts have recognized in the analogous context of derivative standing, a debtor abuses its discretion and acts unjustifiably where it “acts under the influence of conflicts of interest” and “favor[s] certain creditors over others.” *In re Gibson Grp., Inc.*, 66 F.3d 1436, 1441 (6th Cir. 1995). And where appointment of a trustee is warranted, “the court is given unfettered discretion in determining whom to appoint as a trustee.” 6 Collier, *supra*, ¶ 926.02[3].

**B. ERS Has Claims Against The Commonwealth Under § 549 And § 544 That The Oversight Board Has Unjustifiably Failed To Pursue**

**1. A Trustee Could Avoid The Transfers Effected By The Post-Petition Legislation Under § 549**

a. “[S]ection 549 of the Bankruptcy Code ... provides that a trustee may avoid certain post-petition transfers of property.” *In re Bankvest Capital Corp.*, 375 F.3d 51, 62 (1st Cir. 2004). The statute provides, in relevant part, that a “trustee may avoid a transfer of property ... that occurs after the commencement of the case; and ... that is not authorized under [the Bankruptcy Code] or by the court.” 11 U.S.C. § 549(a)(1), (2)(B). PROMESA expressly makes that power available to a trustee appointed under Bankruptcy Code § 926. *See id.* § 926(a) (trustee may pursue action under § 549(a)); 48 U.S.C. § 2161(a) (incorporating §§ 549(a) and 926 into PROMESA).

To establish a § 549(a) claim, the trustee must allege that (1) property of the debtor (2) was transferred (3) after commencement of the case, and that (4) the transfer was not authorized by either the Bankruptcy Code or the court. *See In re Tougas*, 338 B.R. 164, 177–78 (Bankr. D. Mass. 2006); *accord In re Marrero*, 382 B.R. 861, 865–66 (B.A.P. 1st Cir. 2008). The burden of proof then shifts to the “entity asserting the validity of [the] transfer.” Fed. R. Bankr. P. 6001; *see, e.g.*,



*Marrero*, 382 B.R. at 865 (“no error of law in the bankruptcy court’s conclusion that [creditor] failed to meet its burden of showing that the delivery of the new mortgage was not a transfer of estate property subject to avoidance under § 549(a)”); *In re Delco Oil, Inc.*, 599 F.3d 1255, 1259 (11th Cir. 2010).

b. Those requirements are easily met here. *First*, by way of the Post-Petition Legislation, the Commonwealth seized and transferred ERS’s property to itself, as the Oversight Board has recently admitted. *See* Board’s Mot. Dismiss Pls.’ Compl. 6, *Am. Fed’n of Teachers v. Commonwealth of Puerto Rico*, Adv. Proc. No. 3:18-ap-134 (D.P.R. Jan. 8, 2019), ECF No. 11 (“Mot. Dismiss Am. Fed’n Teachers’ Compl.”) (“Pursuant to Law 106, participants no longer make contributions to (or accumulate benefits in) the retirement systems established in 1951 [*i.e.*, ERS], and their employers have ceased to make contributions to those systems . . . . Instead, participants now contribute to the Defined Contribution Plan.”); *supra* pp. 7–8. The Post-Petition Legislation dismantled ERS, seized its assets, and redirected its contribution streams into the Commonwealth’s General Fund. *See supra* pp. 7–8. *Second*, that legislation and the resulting transfers of ERS’s property occurred well after the filing of ERS’s Title III petition on May 21, 2017. Joint Resolution 188 was passed by the Puerto Rico Legislative Assembly on June 25, 2017, and adopted on June 30, 2017, by the Oversight Board on behalf of the Governor, who subsequently signed it. Act 106 was signed by the Governor on August 23, 2017. *See supra* p. 7. *Finally*, the transfers of ERS’s property were unauthorized by either the Bankruptcy Code or the Court. Nothing in PROMESA or the Bankruptcy Code allows the seizure of a Title III debtor’s property without authorization.

In fact, the automatic stay triggered by the filing of ERS’s Title III petition on May 21, 2017, *prohibits* such post-petition transfers by enjoining “any act to obtain possession of [ERS’s]

property ... or to exercise control over [ERS's] property.” 11 U.S.C. § 362(a)(3). It is difficult to imagine a more egregious stay violation than the Commonwealth and Oversight Board’s working together to dismantle ERS and take all of its assets by enacting the Post-Petition Legislation.

The Oversight Board cannot defend the validity of the transfers effected by the Post-Petition Legislation. The Board has never disputed that the transfers occurred or that they occurred *after* the filing of ERS’s Title III petition. And because the transfers were seizures of ERS’s property that violated the automatic stay, the Oversight Board cannot carry its “burden of proving that the transfers were ‘authorized.’” *In re Merry-Go-Round Enters., Inc.*, 400 F.3d 219, 225 (4th Cir. 2005).

**2. A Trustee Could Also Avoid The Transfers Effected By The Post-Petition Legislation Under § 544**

Section 544(b)(1) of the Bankruptcy Code provides that a “trustee may avoid any transfer of an interest of the debtor in property ... that is voidable under applicable law by a creditor holding an [allowable] unsecured claim.” PROMESA expressly gives that authority to a trustee appointed under § 926. *See* 11 U.S.C. § 926(a) (trustee may pursue action under § 544(b)); 48 U.S.C. § 2161(a) (incorporating §§ 544(b) and 926 into PROMESA).

In this case, the “applicable law” is Puerto Rico fraudulent transfer law, including Articles 1064 and 1243 of the Civil Code of Puerto Rico, 31 L.P.R.A. §§ 3028, 3492. Article 1064 of the Civil Code of Puerto Rico allows creditors to “impugn the acts which the debtor may have performed in fraud of [a creditor’s] right.” 31 L.P.R.A. § 3028. Article 1243 of the Civil Code of Puerto Rico allows transfers executed in fraud of creditors to be rescinded when creditors “cannot recover, in any other manner, what is due them.” 31 L.P.R.A. § 3492(3). “Actions to rescind a fraudulent conveyance ... are evaluated with reference to the principles of contract law derived

from the Puerto Rico Civil Code.” *U.S. Fid. & Guar. Co. v. Guzman*, Nos. 10-1078 & 11-1415, 2012 WL 4790314, at \*6 (D.P.R. 2016).

Courts consider various factors to determine whether a transfer is fraudulent under Puerto Rico law. The debtor need not have “intended to harm his creditors”; it is enough “that he knew of the results of his action.” *In re Sepulveda Figueras*, 193 B.R. 118, 120–21 (Bankr. D.P.R. 1996). Courts also consider whether the transfer was for inadequate consideration, whether the transfer was made in haste, and the debtor’s insolvency; courts additionally assess the relationship between the debtor and the transferor as well as the state of the business of the debtor and of the judicial claims against him. *See De Jesus Diaz v. Carrero*, 12 P.R. Offic. Trans. 786, 789, 795 (P.R. 1982); *Guzman*, 2012 WL 4790314, at \*6 (citing *In re El Mundo Corp.*, 208 B.R. 781, 783 & n. 1 (D.P.R. 1997)).

Under that rubric, the Post-Petition Legislation effected fraudulent transfers of ERS’s property. *First*, ERS received no or inadequate consideration, because the Commonwealth transferred all or substantially all of ERS’s property without assuming all of ERS’s obligations, including its obligations to the Bondholders. *Second*, the transfers were executed by the Commonwealth, an insider of ERS and one that owed substantial funds to ERS. *Third*, at the time the transfers were made, ERS was experiencing severe underfunding caused, in large part, by the Commonwealth’s own failure to make hundreds of millions of dollars in statutorily required contributions. *See supra* pp. 4–5. The transfers effectuated by the Post-Petition Legislation left ERS insolvent. *Finally*, at the time of the transfers, the Commonwealth was aware of ERS’s obligations to its bondholders and enacted the Post-Petition Legislation as a means to avoid those obligations and instead use those assets for other purposes.

**C. The Oversight Board Is Laboring Under A Deeply Problematic And Unresolvable Conflict Of Interest Because It Is Representing Parties With Opposing Interests In The Same Case And Disregarding The Best Interest Of One Of Those Parties**

Even though ERS, as an independent, self-governing trust separate from the Commonwealth, has claims against the Commonwealth, the Oversight Board has refused to pursue those claims. *See supra* pp. 4, 8; Part B. That refusal is inexcusable given the Oversight Board's responsibility for representing ERS in its Title III case. But it is also unsurprising given the Oversight Board's simultaneous representation of the Commonwealth. The Board's representation of both sides means that it cannot possibly be acting with undivided loyalty in the best interest of ERS, and the circumstances make clear that the Board has chosen ERS and its creditors for unfavorable treatment. And although that structural conflict alone should be disqualifying, the Oversight Board's role in promulgating and defending the Post-Petition Legislation—which, if not invalidated, will destroy ERS entirely—provides still further reason to appoint the ERS Bondholders as trustees to prosecute these claims on ERS's behalf. The Oversight Board cannot be both pillager (for the Commonwealth) and fiduciary to the victim (for ERS).

**1. The Oversight Board Has Ignored ERS's Independent Status Under PROMESA And Puerto Rico Law, As Well As ERS's Fiduciary Duties To Its Creditors**

The Oversight Board's role in prompting the Post-Petition Legislation demonstrates its refusal to treat ERS as the independent entity that both Puerto Rico law and PROMESA recognize it to be. *See e.g.*, Mot. Dismiss Am. Fed'n Teachers' Compl. 6 (“The first Commonwealth fiscal plan the Governor proposed in March 2017 included reforms of retirement benefits. ... The Oversight Board modified the plan and called for prompt legislation to effectuate, among other things, a transition to defined-contribution accounts.”). Puerto Rico law established ERS as an independent trust, with a statutory right to collect employer contributions from the Commonwealth

and other government employers. *See supra* pp. 4–5. And PROMESA recognizes the independence of each debtor. For example, fiscal plans under PROMESA are expressly required to ensure that “assets, funds, or resources” of ERS are not to be “transferred to, or otherwise used for the benefit of” the Commonwealth. 48 U.S.C. § 2141(b)(1)(M). Similarly, PROMESA provides a cause of action to protect creditors from inter-debtor transfers. *See id.* § 2195. Indeed, PROMESA goes so far as to state that “nothing in [Title III] shall be construed as authorizing substantive consolidation of the cases of affiliated debtors.” *Id.* § 2164(f); *see supra* p. 6. Even under background principles, “substantive consolidation is extreme (it may affect profoundly creditors’ rights and recoveries) and imprecise,” and so “this ‘rough justice’ remedy should be rare.” *In re Owens Corning*, 419 F.3d 195, 199, 211 (3d Cir. 2005), *as amended* (Nov. 1, 2007). The Post-Petition Legislation, however, disregards that independence and, when combined with the Oversight Board’s irreconcilable conflict and position, operates to substantively consolidate ERS’s case into the Commonwealth’s.

That course of action is improper. In addition to having its own interests, ERS owes its own fiduciary duty to its creditors, including the Bondholders. The Board, as ERS’s representative, has those same obligations. *See, e.g., Commodity Futures Trading Comm’n v. Weintraub*, 471 U.S. 343, 355 (1985) (“[I]f a debtor remains in possession—that is, if a trustee is not appointed—the debtor’s directors bear essentially the same fiduciary obligation to creditors and shareholders as would the trustee for a debtor out of possession.”); *In re WHET, Inc.*, 750 F.2d 149, 149 (1st Cir. 1984) (per curiam) (trustee “owes a fiduciary duty to debtor and creditors alike to act fairly and protect their interests”). But ERS and its representative cannot fulfill those duties if they are simultaneously beholden to the Commonwealth’s conflicting interests. *See, e.g., Woods v. City Nat’l Bank & Tr. Co. of Chi.*, 312 U.S. 262, 269 (1941) (“A fiduciary who represents security

holders in a reorganization may not perfect his claim to compensation by insisting that although he had conflicting interests, he served his several masters equally well or that his primary loyalty was not weakened by the pull of his secondary one. Only strict adherence to these equitable principles can keep the standard of conduct for fiduciaries ‘at a level higher than that trodden by the crowd.’”); *In re WM Distribution, Inc.*, 571 B.R. 866, 872 (Bankr. D.N.M. 2017) (“Simultaneous representation of two related debtors presents a potential for an actual conflict of interest. Often inter-company transfers will exist, resulting in each debtor holding a claim against the other. Courts often find such dual representation a disqualifying actual conflict.”). And PROMESA’s disapproval of substantive consolidation is especially relevant here, where creditors like the ERS Bondholders “relied on the separateness of” ERS and the Commonwealth, *Owens Corning*, 419 F.3d at 210, in lending money to ERS.

## **2. The Conflict Is Actual, Not Theoretical**

The Oversight Board’s conflict of interest is not only structural. It has also clearly affected the Board’s decisions not to bring the claims identified in the Bondholders’ proposed Complaint. As noted, both those claims are against the Commonwealth and also concern the Oversight Board itself, whose Post-Petition Legislation purports to do nothing less than destroy ERS by seizing all its assets and ordering the dissolution of its Board of Trustees. But the conflict is still worse than that. It infects not just the Oversight Board’s decisions to enact and defend the Post-Petition Legislation, but also the Board’s arguments in support of that legislation.

For instance, the Oversight Board has contended that there can be no automatic stay violation because ERS could seek to nullify the automatic stay retroactively. Board Mot. Dismiss Pls.’ Amended & Supplemented Compl. 15–16, *Altair*, Adv. Proc. Nos. 3:17-ap-219 & 3:17-ap-220 (Nov. 17, 2017), ECF No. 41. *But see* ERS Bondholders’ Opposition 28–30, *Altair*, Adv. Proc. Nos. 3:17-ap-219 & 3:17-ap-220 (Dec. 20, 2017), ECF No. 50. Not only is that meritless

contention indicative of the Board's serious conflict, but it also deprives the Court of the benefit of zealous advocacy on ERS's behalf. In any event, the automatic stay protects *creditors* as well as debtors, *In re Lopez-Soto*, 764 F.2d 23, 27 (1st Cir. 1985) (Breyer, J.); consequently, it "may not be waived and its scope may not be limited by a debtor," *Acands, Inc. v. Travelers Cas. & Sur. Co.*, 435 F.3d 252, 259 (3d Cir. 2006) (Alito, J.). And if not for the Oversight Board's effort to defend its own conduct and that of the Commonwealth in enacting the Post-Petition Legislation, there is no conceivable reason why the Board would *want* ERS to waive the automatic stay. Indeed, the Oversight Board cannot explain how, consistent with ERS's duties the Bondholders and its prior representations regarding the Bondholders' liens and bonds, ERS could consent to legislation that dismantles it, requires it to transfer its property to the Commonwealth, and eliminates the ability of the ERS Bondholders to recover the amounts ERS owes to them.

**3. Elsewhere The Oversight Board Has Acknowledged That It Cannot Represent Both Sides To A Controversy**

The Oversight Board cannot seriously dispute that a serious conflict inheres in its simultaneous representation of ERS and the Commonwealth. Indeed, elsewhere the Board *requested* and *consented to* the appointment of independent representatives for COFINA (selected by COFINA creditors) and the Commonwealth to resolve a dispute between COFINA and the Commonwealth. Stipulation & Order Approving Procedure Resolve Commonwealth-COFINA Dispute 4, ¶ 4(b), *Puerto Rico*, No. 17-bk-3283, ECF No. 996. The controversy concerned whether sales and use taxes, which were pledged to secure COFINA bonds, were property of the Commonwealth or COFINA. Mot. of Debtors for Order Approving Procedure to Resolve Commonwealth-COFINA Dispute 8, ¶ 17, *Puerto Rico*, No. 17-bk-3283, ECF No. 303. In its motion for approval of procedures to resolve the Commonwealth-COFINA dispute, the Oversight Board requested appointment of independent Commonwealth and COFINA representatives on the

ground that it was “prudent to establish an independent debtor representative for the Commonwealth and COFINA to fully advocate, at arm’s length, on behalf of each Debtor to reach a fair resolution.” *Id.* at 13, ¶ 34. The Board clearly recognized that there was no legitimate alternative to affording each debtor independent representation to pursue its individual interests. There is no principled reason for the Board’s willingness to appoint an independent fiduciary in the COFINA dispute but not for ERS.

#### **4. This Court Too Has Recognized The Danger Of Conflicts Of Interest**

COFINA is not alone in experiencing the distorting effects of the Board’s conflicts of interest. Earlier in these Title III proceedings, this Court rejected the Board’s initial proposal, on behalf of the Puerto Rico Electric Power Authority (“PREPA”), to obtain \$1 billion in debtor-in-possession financing from the Commonwealth. Feb. 15, 2018, Hr’g Tr. 232:10–12, *Puerto Rico*, No. 17-bk-3283, ECF No. 2579. The Court held the motion in abeyance pending an amended proposal. *Id.* at 232:10–12.

The Court found that although the cooperative approach between the Commonwealth and PREPA, both represented by the Oversight Board, “might be [admirable] under other circumstances in aid of other aspects of Puerto Rico’s renewal and debt adjustment process, it [did] not meet the threshold requirements of [Bankruptcy Code] Section 364 and [did] not provide the required predicate for Court approval of the proposed credit facility.” *Id.* at 232:4–12. Recognizing the inherent conflict of interest, the Court concluded “that a business judgment standard focused solely on rationality from a PREPA business point of view is inappropriate and that fairness to the body of PREPA stakeholders and, in particular, the bondholders, must be considered in light of the fact that this is a transaction in which the parties to the proposed credit are closely related and in which the decision-making is intertwined.” *Id.* at 232:25–233:7. The circumstances here are far



worse—the decisionmaking is completely one-sided and in disregard of ERS’s bondholders, and yet is purportedly being conducted on behalf of both the Commonwealth and ERS.

**D. Timely Appointment Of A Trustee Is Crucial Because The Statute Of Limitations Expires Two Years From The Commencement Of The Case Or The Date Of The Transfer**

The applicable statutes of limitations permit avoidance actions under §§ 549 and 544 within limited periods only. With each passing day, the Oversight Board’s failure to pursue those actions prejudices ERS and its creditors and threatens to shut the door permanently. And there certainly can be no assurance that the Oversight Board will take any action prior to the statutes of limitations’ expiring given its conflicting representation of the ERS and the Commonwealth.

The statute of limitations for an action or proceeding under § 549 is “two years after the date of the transfer sought to be avoided.” 11 U.S.C. § 549(d). The Post-Petition Legislation went into effect between July 1, 2017, and August 23, 2017. As a result, any § 549(a) claims will be barred no later than August 23, 2019, and perhaps earlier. Yet the Oversight Board, despite having more than a year to analyze and bring a § 549 claim, has done nothing. As a result, only a matter of months remain for an appointed trustee to bring such avoidance actions.

The limitations period under § 544 is even stricter—*i.e.*, two years after the commencement of the case. *See id.* § 546(a) (“2 years after the entry of the order for relief”); *id.* § 301(b) (“The commencement of a voluntary case under a chapter of this title constitutes an order for relief . . .”). Because the Oversight Board filed ERS’s Title III Petition on May 21, 2017, only three months remain for an appointed trustee to bring a § 544(b) avoidance action. The appointment of a trustee is crucial in order to ensure that such an action is brought by May 21, 2019.

The First Circuit’s recent ruling that the Board’s members were appointed in violation of the Constitution’s Appointments Clause, *Aurelius Inv., LLC v. Puerto Rico*, No. 18-1671, 2019 WL 642328, at \*17 (1st Cir. Feb. 15, 2019), makes appointment of an independent trustee all the

more urgent. Although the First Circuit stayed its mandate for 90 days, *id.*, it is not at all certain whether the Board will be in a position to “continue to operate,” *id.*, to timely file and prosecute ERS’s claims. An independent trustee appointed under § 926 would present no such difficulties.

**E. The Court Should Appoint The ERS Bondholders Trustees; In The Alternative, The Court Should Appoint A Trustee Approved By The Bondholders To Pursue ERS’s Claims**

The foregoing circumstances amply warrant appointment under § 926 of a trustee to pursue ERS’s claims against the Commonwealth. And the Bondholders are the most appropriate entities to serve as trustees. They are the primary remaining stakeholders who still seek payment from ERS, and the Bondholders’ motivation to zealously pursue this litigation will ensure that this Court benefits from proper adversarial testing of ERS’s claims.

In the alternative, as was done in the COFINA Title III case, the Court should appoint an independent third-party fiduciary approved by the Bondholders as trustee. As the primary remaining stakeholders, and as parties with deep experience in this litigation and the underlying issues, the Bondholders should be permitted to weigh in on the selection of a trustee as well to consult with the trustee during the prosecution of ERS’s claims.

**CONCLUSION**

For the foregoing reasons, the Bondholders respectfully request that the Court enter an order appointing them trustees to pursue the claims set forth in the proposed Complaint (Exhibit A) on behalf of ERS and against the Commonwealth, and any further relief as the Court may deem proper. In the alternative, the Bondholders respectfully seek appointment of an independent third-party trustee for ERS to pursue ERS’s claims set forth in the proposed Complaint (Exhibit A) in consultation with the Bondholders. A proposed order is attached as Exhibit C.

In San Juan, Puerto Rico, today February 19, 2019.

By:

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# **EXHIBIT A**

**IN THE UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF PUERTO RICO**

	X	
In re:	)	PROMESA
THE FINANCIAL OVERSIGHT AND MANAGEMENT BOARD FOR PUERTO RICO,	)	Title III
as representative of	)	Case No. 3:17-bk-03283 (LTS)
THE COMMONWEALTH OF PUERTO RICO, <i>et al.</i> ,	)	(Jointly Administered)
Debtors. <sup>1</sup>	)	
	)	
	X	
ANDALUSIAN GLOBAL DESIGNATED ACTIVITY COMPANY, CROWN MANAGED ACCOUNTS FOR AND ON BEHALF OF CROWN/PW SP, GLENDON OPPORTUNITIES FUND, L.P., LMA SPC FOR AND ON BEHALF OF MAP 98 SEGREGATED PORTFOLIO, MASON CAPITAL MASTER FUND LP, OAKTREE-FORREST MULTI-STRATEGY, LLC (SERIES B), OAKTREE OPPORTUNITIES FUND IX, L.P., OAKTREE OPPORTUNITIES FUND IX (PARALLEL 2), L.P., OAKTREE VALUE OPPORTUNITIES FUND, L.P., OCEANA MASTER FUND LTD., OCHER ROSE, L.L.C., PENTWATER MERGER ARBITRAGE MASTER FUND LTD., PWCM MASTER FUND LTD., PUERTO RICO AAA PORTFOLIO BOND FUND, INC., PUERTO RICO AAA PORTFOLIO BOND FUND II, INC., PUERTO RICO AAA PORTFOLIO TARGET MATURITY FUND, INC., PUERTO RICO FIXED INCOME FUND, INC., PUERTO RICO FIXED INCOME FUND II, INC., PUERTO RICO FIXED INCOME FUND III, INC., PUERTO RICO FIXED INCOME FUND IV, INC.,	)	Adversary No. _____
	)	<b>ADVERSARY COMPLAINT</b>

<sup>1</sup> The Debtors in these Title III cases, along with each Debtor’s Bankruptcy Court case number and last four (4) digits of each Debtor’s federal tax identification number are (i) The Commonwealth of Puerto Rico (Bankr. Case No. 17-bk-3283 (LTS)) (Last Four Digits of Federal Tax ID: 3481); (ii) The Employees Retirement System of the Government of the Commonwealth of Puerto Rico (Bankr. Case No. 17-bk-3566 (LTS)) (Last Four Digits of Federal Tax ID: 9686); (iii) Puerto Rico Sales Tax Financing Corporation (Bankr. Case No. 17-bk-3284 (LTS)) (Last Four Digits of Federal Tax ID: 8474); (iv) Puerto Rico Highways and Transportation Authority (Bankr. Case. No. 17-bk-3567 (LTS) (Last Four Digits of Federal Tax ID: 3808).

PUERTO RICO FIXED INCOME FUND V, INC., )  
PUERTO RICO GNMA & U.S. GOVERNMENT TARGET )  
MATURITY FUND, INC., PUERTO RICO INVESTORS )  
BOND FUND I, PUERTO RICO INVESTORS TAX-FREE )  
FUND, INC., PUERTO RICO INVESTORS TAX-FREE )  
FUND, INC. II, PUERTO RICO INVESTORS TAX-FREE )  
FUND III, INC., PUERTO RICO INVESTORS TAX-FREE )  
FUND IV, INC., PUERTO RICO INVESTORS TAX-FREE )  
FUND V, INC., PUERTO RICO INVESTORS TAX-FREE )  
FUND VI, INC., PUERTO RICO MORTGAGE-BACKED )  
& U.S. GOVERNMENT SECURITIES FUND, INC., SV )  
CREDIT, L.P., TAX-FREE PUERTO RICO FUND, INC., )  
TAX-FREE PUERTO RICO FUND II, INC., and TAX- )  
FREE PUERTO RICO TARGET MATURITY FUND, )  
INC., )

Plaintiffs, )

-against- )

THE COMMONWEALTH OF PUERTO RICO, THE )  
FINANCIAL OVERSIGHT AND MANAGEMENT )  
BOARD OF THE COMMONWEALTH OF PUERTO )  
RICO, THE PUERTO RICO FISCAL AGENCY AND )  
FINANCIAL ADVISORY AUTHORITY, GOVERNOR )  
RICARDO ROSSELLÓ NEVARES in his official capacity )  
as the Governor of the Commonwealth of Puerto Rico, )  
[ ] in her official capacity as the )  
Secretary of Treasury of the Commonwealth of Puerto Rico, )

Defendants. )

-----X

**ADVERSARY COMPLAINT**

TO THE HONORABLE COURT:

NOW COME Plaintiffs Andalusian Global Designated Activity Company, Crown  
Managed Accounts for and on behalf of Crown/PW SP, Glendon Opportunities Fund, L.P., LMA  
SPC for and on behalf of Map 98 Segregated Portfolio, Mason Capital Master Fund LP, Oaktree-  
Forrest Multi-Strategy, LLC (Series B), Oaktree Opportunities Fund IX, L.P., Oaktree  
Opportunities Fund IX (Parallel 2), L.P., Oaktree Value Opportunities Fund, L.P., Oceana

Master Fund Ltd., Ocher Rose, L.L.C., Pentwater Merger Arbitrage Master Fund Ltd., PWCM Master Fund Ltd., Puerto Rico AAA Portfolio Bond Fund, Inc., Puerto Rico AAA Portfolio Bond Fund II, Inc., Puerto Rico AAA Portfolio Target Maturity Fund, Inc., Puerto Rico Fixed Income Fund, Inc., Puerto Rico Fixed Income Fund II, Inc., Puerto Rico Fixed Income Fund III, Inc., Puerto Rico Fixed Income Fund IV, Inc., Puerto Rico Fixed Income Fund V, Inc., Puerto Rico GNMA & U.S. Government Target Maturity Fund, Inc., Puerto Rico Investors Bond Fund I, Puerto Rico Investors Tax-Free Fund, Inc., Puerto Rico Investors Tax-Free Fund, Inc. II, Puerto Rico Investors Tax-Free Fund III, Inc., Puerto Rico Investors Tax-Free Fund IV, Inc., Puerto Rico Investors Tax-Free Fund V, Inc., Puerto Rico Investors Tax-Free Fund VI, Inc., Puerto Rico Mortgage-Backed & U.S. Government Securities Fund, Inc., SV Credit, L.P., Tax-Free Puerto Rico Fund, Inc., Tax-Free Puerto Rico Fund II, Inc., and Tax-Free Puerto Rico Target Maturity Fund, Inc. (collectively, the “Bondholders” or “ERS Bondholders”), as court-appointed trustees on behalf of the Employees Retirement System of the Government of the Commonwealth of Puerto Rico (“ERS”), by and through their attorneys, and respectfully state, allege, and pray as follows:

### **PRELIMINARY STATEMENT**

1. On \_\_\_\_\_, 2019, the Court entered an order appointing the Bondholders as trustees to pursue the claims set forth in this complaint on behalf of ERS and against the Commonwealth of Puerto Rico (the “Commonwealth”). ECF No. \_\_\_\_\_ (granting *Motion of Certain Secured Creditors of the Employees Retirement System of the Government of the Commonwealth of Puerto Rico for Appointment as Trustees Under 11 U.S.C. § 926*).

2. This is an action for avoidance and recovery brought pursuant to §§ 544(b), 549(a), and 550 of title 11 of the United States Code (the “Bankruptcy Code”).



3. Plaintiffs are the holders of bonds issued by ERS in 2008 and are therefore creditors of ERS. The proceeds of those bonds (the “ERS Bonds” or the “Bonds”) were used to pay benefits to retirees and to reduce ERS’s unfunded accrued actuarial liabilities. The ERS Bonds were secured by collateral that included, among other things, all employer contributions from Puerto Rico government employers (including municipal employers, public corporations and the central government of Puerto Rico) and ERS’s legal right to receive those contributions.

4. On June 30, 2016, Congress enacted the Puerto Rico Oversight, Management, and Economic Stability Act (“PROMESA”), Pub. L. No. 114-187, 130 Stat. 549 (2016), *codified at* 48 U.S.C. §§ 2101–2241. PROMESA created a federal Financial Oversight and Management Board for Puerto Rico (the “Oversight Board” or “Board”) and conferred broad sovereign powers on the Board. Using these statutory powers, the Oversight Board worked with and through the Commonwealth to transfer ERS’s property to the Commonwealth for no or inadequate consideration.

5. In June 2017, the Puerto Rico legislature passed, and the Oversight Board adopted, Joint Resolution 188 for Other Allocations for Fiscal Year 2017–2018 (“Joint Resolution 188” or “J.R. 188”). Joint Resolution 188 required ERS to liquidate its assets for distribution to the Commonwealth’s General Fund, and directs participating employers to make future employer contributions to the Commonwealth’s General Fund, rather than to ERS. The purpose and effect of Joint Resolution 188 was to strip ERS of its property and to divert ERS’s employer contributions away from ERS, all of which was pursued with the purpose of evading ERS’s obligations to its creditors.

6. On August 23, 2017, the Governor signed a Law to Guarantee Payment to Our Pensioners and Establish a New Plan for Defined Contributions for Public Servants (“Act 106”),

which further implemented Joint Resolution 188. Act 106 stated that Joint Resolution 188 “eliminated” “the employer contributions being made until now,” and purported to set up a new “‘Pay-Go’ Fee” that employers must pay directly into the Commonwealth’s General Fund. Act 106, § 1.4, pp. 13–14. The “‘Pay-Go’ Fee” is nothing new, however, because the employers required to pay it are the same government entities that were previously obligated to make contributions to ERS; indeed, even the “contributions” are the same obligations. *Id.* § 1.6(g), p. 15 (requiring payments from “entities considered employers under the [ERS]”); *compare id.* § 2.1(b), p. 17, with 3 L.P.R.A. § 781(a) (2008). Finally, Act 106 required ERS’s Board of Trustees to dissolve by December 31, 2017, so a new board could be formed to dispose of ERS’s property. Act 106, §§ 4.2, 5.1–5.3.

7. In this action, the Bondholders, appointed as trustees for ERS under 11 U.S.C. § 926, seek to avoid the transfers effected by Joint Resolution 188 and Act 106 (collectively, the “Post-Petition Legislation”) under 11 U.S.C. §§ 549 and 544 and to recover the value of those transfers under 11 U.S.C. § 550.

#### **THE PARTIES**

8. Plaintiff Andalusian Global Designated Activity Company is a designated activity company, limited by its shares, incorporated under the laws of Ireland and located at 70 Sir John Rogerson’s Quay, Dublin 2, Ireland.

9. Plaintiff Crown Managed Accounts for and on behalf of Crown/PW SP is a corporation organized and existing under the laws of the Cayman Islands and located at Grand Pavilion, Commercial Centre, 1st Floor, 802 West Bay Road, George Town, Grand Cayman KY1-1207, Cayman Islands.

10. Plaintiff Glendon Opportunities Fund, L.P., is a limited partnership organized and existing under the laws of the Cayman Islands and located at Ugland House, South Church Street, Grand Cayman KY1-1104, Cayman Islands.

11. Plaintiff LMA SPC for and on behalf of Map 98 Segregated Portfolio is a corporation organized and existing under the laws of the Cayman Islands and located at Cayman Corporate Centre, 27 Hospital Road, George Town, Grand Cayman KY1-9008, Cayman Islands.

12. Plaintiff Mason Capital Master Fund LP is a limited partnership organized and existing under the laws of the Cayman Islands and with an address at PO Box 309, Ugland House, George Town, Grand Cayman KY1-1104, Cayman Islands.

13. Plaintiff Oaktree-Forrest Multi-Strategy, LLC (Series B), is a limited liability company organized and existing under the laws of Delaware with its principal place of business at 333 South Grand Avenue, 28th Floor, Los Angeles, CA 90071.

14. Plaintiff Oaktree Opportunities Fund IX, L.P., is a limited partnership organized and existing under the laws of the Cayman Islands with its principal place of business located at 333 South Grand Avenue, 28th Floor, Los Angeles, CA 90071.

15. Plaintiff Oaktree Opportunities Fund IX (Parallel 2), L.P., is a limited partnership organized and existing under the laws of the Cayman Islands with its principal place of business at 333 South Grand Avenue, 28th Floor, Los Angeles, CA 90071.

16. Plaintiff Oaktree Value Opportunities Fund, L.P., is a limited partnership organized and existing under the laws of the Cayman Islands with its principal place of business at 333 South Grand Avenue, 28th Floor, Los Angeles, CA 90071.

17. Plaintiff Oceana Master Fund Ltd. is a partnership organized and existing under the laws of the Cayman Islands and located at 190 Elgin Avenue, George Town, Grand Cayman KY1-9005, Cayman Islands.

18. Plaintiff Ocher Rose, L.L.C., is a limited liability company organized and existing under the laws of Delaware and located at P.O. Box 1226, New York, NY 10150.

19. Plaintiff Pentwater Merger Arbitrage Master Fund Ltd. is a partnership organized and existing under the laws of the Cayman Islands and located at 190 Elgin Avenue, George Town, Grand Cayman KY1-9005, Cayman Islands.

20. Plaintiff PWCM Master Fund Ltd. is a partnership organized and existing under the laws of the Cayman Islands and located at 190 Elgin Avenue, George Town, Grand Cayman KY1-9005, Cayman Islands.

21. Plaintiff Puerto Rico AAA Portfolio Bond Fund, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza, 10th Floor, 250 Munoz Rivera Ave., San Juan, Puerto Rico 00918.

22. Plaintiff Puerto Rico AAA Portfolio Bond Fund II, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza, 10th Floor, 250 Munoz Rivera Ave., San Juan, Puerto Rico 00918.

23. Plaintiff Puerto Rico AAA Portfolio Target Maturity Fund, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza, 10th Floor, 250 Munoz Rivera Ave., San Juan, Puerto Rico 00918.

24. Plaintiff Puerto Rico Fixed Income Fund, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza, 10th Floor, 250 Munoz Rivera Ave., San Juan, Puerto Rico 00918.

25. Plaintiff Puerto Rico Fixed Income Fund II, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza, 10th Floor, 250 Munoz Rivera Ave., San Juan, Puerto Rico 00918.

26. Plaintiff Puerto Rico Fixed Income Fund III, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza, 10th Floor, 250 Munoz Rivera Ave., San Juan, Puerto Rico 00918.

27. Plaintiff Puerto Rico Fixed Income Fund IV, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza, 10th Floor, 250 Munoz Rivera Ave., San Juan, Puerto Rico 00918.

28. Plaintiff Puerto Rico Fixed Income Fund V, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza, 10th Floor, 250 Munoz Rivera Ave., San Juan, Puerto Rico 00918.

29. Plaintiff Puerto Rico GNMA & U.S. Government Target Maturity Fund, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza, 10th Floor, 250 Munoz Rivera Ave., San Juan, Puerto Rico 00918.

30. Plaintiff Puerto Rico Investors Bond Fund I is an investment trust organized and existing under the laws of Puerto Rico with its principal place of business at Banco Popular Center, Suite 1112, 209 Munoz Rivera Avenue, Hato Rey, Puerto Rico 00918.

31. Plaintiff Puerto Rico Investors Tax-Free Fund, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at Banco Popular Center, Suite 1112, 209 Munoz Rivera Avenue, Hato Rey, Puerto Rico 00918.

32. Plaintiff Puerto Rico Investors Tax-Free Fund, Inc. II, is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at Banco Popular Center, Suite 1112, 209 Munoz Rivera Avenue, Hato Rey, Puerto Rico 00918.

33. Plaintiff Puerto Rico Investors Tax-Free Fund III, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at Banco Popular Center, Suite 1112, 209 Munoz Rivera Avenue, Hato Rey, Puerto Rico 00918.

34. Plaintiff Puerto Rico Investors Tax-Free Fund IV, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at Banco Popular Center, Suite 1112, 209 Munoz Rivera Avenue, Hato Rey, Puerto Rico 00918.

35. Plaintiff Puerto Rico Investors Tax-Free Fund V, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at Banco Popular Center, Suite 1112, 209 Munoz Rivera Avenue, Hato Rey, Puerto Rico 00918.

36. Plaintiff Puerto Rico Investors Tax-Free Fund VI, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at Banco Popular Center, Suite 1112, 209 Munoz Rivera Avenue, Hato Rey, Puerto Rico 00918.

37. Plaintiff Puerto Rico Mortgage-Backed & U.S. Government Securities is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza, 10th Floor, 250 Munoz Rivera Ave., San Juan, Puerto Rico 00918.

38. Plaintiff SV Credit, L.P., is a limited partnership organized and existing under the laws of Delaware and located at 1209 Orange Street, Wilmington, New Castle County, DE 19801.

39. Plaintiff Tax-Free Puerto Rico Fund, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza Building, 10th Floor, 250 Munoz Rivera Avenue, San Juan, Puerto Rico 00918.

40. Plaintiff Tax-Free Puerto Rico Fund II, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza Building, 10th Floor, 250 Munoz Rivera Avenue, San Juan, Puerto Rico 00918.

41. Plaintiff Tax-Free Puerto Rico Target Maturity Fund, Inc., is a corporation organized and existing under the laws of Puerto Rico with its principal place of business at American International Plaza Building, 10th Floor, 250 Munoz Rivera Avenue, San Juan, Puerto Rico 00918.

42. Defendant the Commonwealth of Puerto Rico is a United States territory subject to the laws of the United States and the plenary jurisdiction of Congress.

43. Defendant the Oversight Board is an entity of the United States created pursuant to PROMESA to assist the Commonwealth, including its instrumentalities, in managing its public finances, and for other purposes.

44. Defendant the Puerto Rico Fiscal Agency and Financial Advisory Authority (“AAFAF”) is an entity created pursuant to the Puerto Rico Emergency Moratorium and Financial Rehabilitation Act, P.R. Act No. 21-2016, for the purpose of acting as fiscal agent, financial advisor, and reporting agent of the Commonwealth, its agencies, instrumentalities, subdivisions, public corporations, and municipalities.

45. Defendant Ricardo Rosselló Nevaes is the Governor of the Commonwealth of Puerto Rico and is being sued in his official capacity.

46. Defendant [ \_\_\_\_\_ ] is the Secretary of Treasury of the Commonwealth of Puerto Rico and is being sued in her official capacity.

### **JURISDICTION AND VENUE**

47. This action seeks avoidance of transfers pursuant to §§ 549 and 544 of the Bankruptcy Code and to recover the value of those transfers pursuant to § 550.

48. This Court has jurisdiction over all claims and causes of action in this adversary proceeding pursuant to 48 U.S.C. § 2166(a)(2) because they arise in or are “related to” the above-captioned Title III cases. This Court has personal jurisdiction over all of the Defendants pursuant to 48 U.S.C. § 2166(c).

49. Venue is proper under 48 U.S.C. § 2167 because this adversary proceeding is brought in a Title III case.

### **FACTUAL ALLEGATIONS**

#### **I. ERS**

##### **A. The ERS Enabling Act**

50. ERS is a trust created by Act No. 447 of May 15, 1951, of the Legislature of the Commonwealth (the “ERS Enabling Act”) to provide pension and other benefits to officers and employees of the Commonwealth, members and employees of the Legislature, and officers and employees of certain public corporations and municipalities of the Commonwealth. 3 L.P.R.A. § 761. ERS was established as an independent, self-governing entity separate from the Commonwealth and from the Commonwealth’s other agencies and instrumentalities. *Id.* § 775. The ERS Enabling Act provided for ERS to be governed by an eleven-member Board of Trustees responsible for setting policy for, and overseeing the operations of, ERS. *Id.*

51. The ERS Enabling Act gave the Board of Trustees blanket authorization to incur debt on behalf of ERS and to secure such debt with ERS’s assets. Specifically, the act authorized



the Board of Trustees to “seek a loan ... through the direct placement of debts, securing said debt with the assets of the [ERS].” *Id.* § 779(d).

**B. Employer Contributions**

52. Until the Post-Petition Legislation, ERS was funded by employer contributions, employee contributions, and investment earnings on its undistributed funds. Employer contributions were the largest component of this income stream, and they constitute a legal asset of ERS. ERS has a statutory right to receive employer contributions, and employers were required by statute to make them.

53. ERS received employer contributions from the Commonwealth and from various municipalities within, and public corporations of, the Commonwealth. The Commonwealth was responsible for approximately 59 percent of the employer contributions ERS received, while municipalities and public corporations accounted for the rest. As of the commencement of ERS’s Title III case, the Commonwealth did not hold or own any interest in employer contributions owed by municipalities or public corporations to ERS.

54. The critical importance of employer contributions to ERS, and ERS’s authority to enforce its rights, were reflected in a series of provisions in the ERS Enabling Act. For example, an employer’s failure to pay timely its contributions to ERS was punishable as a misdemeanor. 3 L.P.R.A. § 781a(e), (f). If an employer’s contributions to ERS were in arrears for more than 30 days, ERS’s claim to those contributions had priority over any other outstanding debt of that employer. *Id.* § 781a(h). If a municipality failed to make its employer contributions to ERS, ERS had the power to intercept or garnish the municipality’s property tax revenues. *Id.* § 781a(g). If agencies, public corporations, and instrumentalities of the Commonwealth failed to make employer contributions, ERS was authorized to issue a certificate of debt for immediate payment

of the arrearages from the Department of Treasury. *Id.* § 781a(h). ERS also was entitled to receive interest on these delinquent contributions. *Id.*

55. Despite the importance of employer contributions to ERS, the Commonwealth has never paid ERS enough to satisfy its statutory contribution requirements. By the date of ERS's Title III petition, *see infra* ¶¶ 60–63, the Commonwealth owed ERS more than \$411 million.

## **II. PENSION FUNDING BONDS ISSUED BY ERS**

56. In 2008, ERS issued bonds pursuant to the authority of a resolution (the “ERS Bond Resolution”) of its Board of Trustees. *See* Pension Funding Bond Resolution (Jan. 24, 2008). ERS issued the following bonds on the following dates:

- a. “Series A” Bonds totaling \$1,588,810,799.60 on January 31, 2008.
- b. “Series B” Bonds totaling \$1,058,634,613.05 on June 2, 2008.
- c. “Series C” Bonds totaling \$300,202,930 on June 30, 2008.

57. Most of the ERS Bonds were sold to individual residents of the Commonwealth and to local businesses.

58. All of the bond issues' net proceeds (after costs of issuance and required reserves) were used to pay benefits to retirees or invested to provide for future benefit payments.

59. An integral part of ERS's bond issuance was an extensive security package designed to protect the bondholders' investment. ERS granted bondholders, through a Fiscal Agent, a security interest in and lien on certain ERS property (“Pledged Property”), including (a) all “Revenues,”—among other things, all employer contributions received by ERS or the Fiscal Agent “and any assets in lieu thereof or derived thereunder which are payable to [ERS] pursuant to [the Enabling Act]”; (b) “[a]ll right, title and interest of [ERS] in and to” the property described in (a) and “all rights to receive the same”; (c) the funds, accounts, and subaccounts held by the Fiscal Agent; (d) any and all other rights and personal property of every kind pledged

and assigned by ERS for additional security; and (e) “any and all cash and non-cash proceeds, products, offspring, rents and profits from any of the Pledged Property ... ,” including, without limitation, those from the sale, exchange, transfer, collection, loss, damage, disposition, substitution or replacement of” such property. *Id.* § 501, at VI-8 & Ex. B, VI-36. ERS pledged its statutory right to collect employer contributions to secure the bonds, and that right was exercisable upon default. *Id.* § 501, at VI-8; *id.* § 1102, at VI-22.

### **III. PROMESA AND THE TITLE III CASES**

60. On June 30, 2016, Congress passed PROMESA. The stated purpose of PROMESA was to “establish an Oversight Board to assist the Government of Puerto Rico, including instrumentalities, in managing its public finances, and for other purposes.” H.R. 5278, 114th Cong. pmb. (2016).

61. Title III of PROMESA authorized the Oversight Board to file a petition to restructure the debts of a government instrumentality in a court-supervised adjustment process similar to Chapter 9 of the Bankruptcy Code.

62. On May 3, 2017, the Oversight Board approved and certified the filing of a PROMESA Title III petition for the Commonwealth.

63. On May 21, 2017, the Oversight Board approved and certified the filing of a separate PROMESA Title III petition for ERS.

64. PROMESA incorporates the automatic stay provisions of § 362 of the Bankruptcy Code. 48 U.S.C. § 2161(a). Pursuant to those provisions, the filing of ERS’s Title III case on May 21, 2017, operated as a stay against all efforts by any person (including the Commonwealth) to obtain or exercise control over property of ERS. That automatic stay has remained in effect during all times relevant to this action.

#### IV. JOINT RESOLUTION 188

65. The Puerto Rico legislature passed Joint Resolution 188 on June 25, 2017, and the Oversight Board adopted it on behalf of the Governor on June 30, 2017.<sup>2</sup>

66. The actual purpose and purported effect of Joint Resolution 188 were to seize ERS's property and the ERS Bondholders' collateral. Joint Resolution 188 ordered ERS to sell its assets and to transfer the net cash proceeds, in addition to any available funds, into the Puerto Rico Treasury Secretary's account as part of the General Fund for fiscal year 2017–2018 to make benefit payments to pensioners. Joint Resolution, 188 §§ 1–3. And the resolution requires employers to make increased employer contributions directly to the Commonwealth's General Fund.

67. Section 4 of Joint Resolution 188 also provides in relevant part that:

- a. the Commonwealth would assume any payments that Puerto Rico's retirement systems, including ERS, could not make;
- b. ERS would continue to meet its obligations to beneficiaries and pensioners by contributing its available funds and any funds arising from its asset sales to the Commonwealth's General Fund;
- c. the Commonwealth, its public corporations, and its municipalities would stop making employer contributions to ERS;

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<sup>2</sup> The Oversight Board adopted House Resolution 186, House Resolution 187, and House Resolution 188 as part of the Commonwealth's budget pursuant to §§ 202(d)(2) and 202(e)(3) of PROMESA. The Board "deemed" the budget, along with the various resolutions, "to be approved by the Governor and the Legislature" and "in full force and effect beginning on July 1, 2017." Resolution No. 3, at 2, *in* Letter from Fin. Oversight & Mgmt. Bd. to Gov. Rosselló, Ex. A (June 30, 2017), [https://drive.google.com/file/d/14rwf4d-I3xBl\\_jNyg-ggYJMh1UfInkj5Y/view](https://drive.google.com/file/d/14rwf4d-I3xBl_jNyg-ggYJMh1UfInkj5Y/view) (access to Oversight Board files is available at <https://oversightboard.pr.gov/documents/>). House Resolution 186 and House Resolution 187 address other matters related to the Commonwealth's budget, but they also include the full text of House Resolution 188. To avoid repetition, the Complaint refers to House Resolution 188 only.

d. AAFAF would establish procedures so that the Commonwealth, its public corporations, and its municipalities would make employer contributions to the Commonwealth.

68. No or inadequate consideration was provided to ERS in exchange for the property transferred to the Commonwealth's General Fund.

69. Joint Resolution 188 was approved by the Puerto Rico legislature pursuant to the Fiscal Plan approved and certified by the Oversight Board. *Id.* § 4.

70. Upon information and belief, at the time Joint Resolution 188 was passed, ERS and the Commonwealth knew and, indeed, intended, that the transfer effectuated by Joint Resolution 188 would hinder, delay, defraud, or otherwise harm ERS's creditors.

## V. ACT 106

71. The Puerto Rico legislature passed Act 106 on August 18, 2017, and the Governor signed it into law on August 23, 2017.

72. Act 106 established procedures for increasing employer contributions to make payments equal to the obligations to employees, as mandated by the Fiscal Plan for Puerto Rico and established in Joint Resolution 188. The law declares that "as of July 1, 2017, in accordance with House Joint Resolution 188 of 2017, as certified by the Fiscal Oversight Board, on July 13, 2017 the Government of Puerto Rico became the direct payer of our retirees' pensions." Act 106, § 1.4.

73. Act 106 contains provisions that specify the mechanisms by which the Commonwealth will pay all of the benefits due to employees each year. For example, the act provides for the treatment and the payment terms of accumulated pensions and associated accounts, *id.* at ch. 2; establishes a defined-contribution program, *id.* ch. 3; creates a retirement board to replace the existing boards of the retirement systems, *id.* ch. 4; provides transition rules,

*id.* ch. 5; and makes changes to existing laws, *id.* ch. 6. Act 106 also reiterates that the Commonwealth, in accordance with Joint Resolution 188, will assume any payments that ERS could not make, that ERS would contribute its assets to the Commonwealth, and that the Commonwealth, its public corporations, and its municipalities would stop making employer contributions to ERS. *See id.* §§ 1.3, 1.4.

74. Act 106 also states that unless an extension is granted, the Board of Trustees for ERS is to be dissolved by December 31, 2017, *id.* § 5.1(b), that the new retirement board will have the authority to dispose of all of ERS's property and equipment, *id.* §§ 4.2 and 5.3, and that all of ERS's employees will be terminated and transferred to other posts, *id.* § 5.2.

75. Upon information and belief, at the time Act 106 was enacted, ERS and the Commonwealth knew and, indeed, intended that the transfer effectuated by Act 106 and Joint Resolution 188 would hinder, delay, defraud, or otherwise harm ERS's creditors.

76. Upon information and belief, the transfers required under Joint Resolution 188, Act 106, and related legislation have been effectuated.

77. Upon information and belief, the transfers effectuated by Act 106 and Joint Resolution 188 rendered ERS insolvent.

### **FIRST CLAIM FOR RELIEF**

#### **Request for Avoidance of Transfers Effectuated by the Post-Petition Legislation Under 11 U.S.C. § 549**

78. Plaintiffs reallege and incorporate by reference all of the allegations set forth in paragraphs 1 through 77 above.

79. Section 549 of the Bankruptcy Code provides that a "trustee may avoid a transfer of property ... that occurs after the commencement of the case; and ... that is not authorized under [the Bankruptcy Code] or by the court." 11 U.S.C. § 549(a)(1), (2)(B).

80. Joint Resolution 188 purports to (i) require ERS to liquidate its assets and transfer the proceeds to the Commonwealth; and (ii) divert employer contributions to which ERS has a statutory right away from ERS to the Commonwealth.

81. Act 106 reiterates those requirements and provides procedures to further implement the increase in amount of employer contributions.

82. The Post-Petition Legislation was enacted by the Commonwealth after the commencement of the ERS Title III case.

83. The transfers of ERS's property pursuant to the Post-Petition Legislation were unauthorized by either the Bankruptcy Code or the Court.

84. The transfers effected by the Post-Petition Legislation should be avoided pursuant to § 549(a) of the Bankruptcy Code.

85. ERS is entitled to the value of the transfers under § 550 of the Bankruptcy Code.

## **SECOND CLAIM FOR RELIEF**

### **Request for Avoidance of Transfers Effected by the Post-Petition Legislation Under 11 U.S.C. § 544**

86. Plaintiffs reallege and incorporate by reference all of the allegations set forth in paragraphs 1 through 77 above.

87. Section 544(b) of the Bankruptcy Code provides that a “trustee may avoid any transfer of an interest of the debtor in property ... that is voidable under applicable law by a creditor holding an [allowable] unsecured claim.”

88. Article 1064 of the Civil Code of Puerto Rico allows creditors to “impugn the acts which the debtor may have performed in fraud of [a creditor's] right.” 31 L.P.R.A. § 3028.

89. Article 1243 of the Civil Code of Puerto Rico provides that transfers executed in fraud of creditors can be rescinded when creditors “cannot recover, in any other manner, what is due them.” 31 L.P.R.A. § 3492(3).

90. The transfers effected by the Post-Petition Legislation from ERS to the Commonwealth are voidable under Puerto Rico law as fraudulent transfers.

91. The transfers were executed in fraud of ERS’s creditors.

92. Joint Resolution 188 purports to (i) require ERS to liquidate its assets and transfer the proceeds to the Commonwealth; and (ii) divert employer contributions to which ERS has a statutory right away from ERS to the Commonwealth.

93. Act 106 reiterates those requirements and provides procedures to further implement the increase in amount of employer contributions.

94. Joint Resolution and Act 106 were executed by the Commonwealth, a separate entity that owed substantial funds to ERS.

95. At the time of the transfers, ERS was experiencing severe underfunding caused, in large part, by the Commonwealth’s own failure to make hundreds of millions of dollars in statutorily required contributions.

96. ERS received no or inadequate consideration for the transfers. Through the Post-Petition Legislation, the Commonwealth emptied ERS’s coffers without assuming all of ERS’s obligations—including its obligations to the Bondholders.

97. Upon information and belief, at the time of the transfer, the Commonwealth and the ERS were aware of ERS’s obligations to its bondholders as well as the harm that its bondholders would suffer, and enacted the Post-Petition Legislation as a means to avoid those obligations and instead use those assets for other purposes.



98. Upon information and belief, the transfers effectuated by Act 106 and Joint Resolution 188 rendered ERS insolvent.

99. The transfers effected by the Post-Petition Legislation should be avoided pursuant to § 544(b) of the Bankruptcy Code and Puerto Rico law as a fraudulent transfer.

**PRAYER FOR RELIEF**

**WHEREFORE**, based on the above and foregoing, plaintiffs pray that this Honorable Court enter an order:

- a. Avoiding the transfers effected by the Post-Petition Legislation pursuant to § 549(a) of the Bankruptcy Code.
- b. Avoiding the transfers effected by the Post-Petition Legislation pursuant to § 544(b) of the Bankruptcy Code and Puerto Rico law.
- c. Recovering the value of the transfers pursuant to § 550 of the Bankruptcy Code.

**RESPECTFULLY SUBMITTED.**

In San Juan, Puerto Rico, today February 19, 2019.

By:

/s/ Alfredo Fernández-Martínez

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# **EXHIBIT B**

**WHITE & CASE**

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**JONES DAY**

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January 28, 2019

VIA E-MAIL AND MAIL

Martin J. Bienenstock  
Proskauer Rose LLP  
Eleven Times Square  
New York, New York 10036

Re: Demand that Avoidance Claims Be Asserted on Behalf of the Employees Retirement System of the Government of the Commonwealth of Puerto Rico (“ERS”) Against the Commonwealth of Puerto Rico

Dear Martin:

We write on behalf of certain holders (the “Bondholders”) of senior pension funding bonds (“ERS Bonds”) issued by ERS pursuant to Act No. 447 of May 15, 1951, as amended, of the Commonwealth of Puerto Rico (the “Commonwealth”) and the general resolution adopted by ERS’s Board of Trustees on January 24, 2008, and later supplemental resolutions.

We write to demand that ERS pursue certain avoidance actions arising from transfers made under or in connection with the Joint Resolution for Other Allocations for Fiscal Year 2017–2018 (“Joint Resolution 188” or “J.R. 188”) of the Puerto Rico Legislative Assembly and the Law to Guarantee Payment to Our Pensioners and Establish a New Plan for Defined Contributions for Public Servants (“Act 106”) enacted by the Commonwealth.<sup>1</sup> Specifically, ERS possesses avoidance claims against the Commonwealth for fraudulent transfers and unauthorized post-petition transfers under sections 544(b) and 549 of title 11 of the United States Code (the “Bankruptcy Code”), as incorporated in the Title III case of ERS (the “ERS Title III Case”) by section 301 of the Puerto Rico Oversight, Management, and Economic Stability Act, Pub. L. No. 114-187, 130 Stat. 549 (2016), *codified at* 48 U.S.C. §§ 2101–2241 (“PROMESA”).

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<sup>1</sup> While this demand focuses on avoidance actions under sections 544(b) and 549 of the Bankruptcy Code, ERS possesses additional causes of action against the Commonwealth and others that ERS and the Financial Oversight and Management Board for Puerto Rico (the “Oversight Board”) have failed to pursue on behalf of ERS. The Bondholders reserve their right to seek appropriate relief with respect to these claims at a later date.

January 28, 2019  
Page 2

Those claims are based on the following timeline and core facts:

- May 21, 2017: The Oversight Board filed a petition for relief under Title III of PROMESA on behalf of ERS, thereby commencing the ERS Title III Case. Commencement of the ERS Title III Case by the Oversight Board triggered the operation of the automatic stay to protect ERS's property wherever located. 11 U.S.C. § 362(a); 48 U.S.C. § 2161(a).
- June 25, 2017: The Puerto Rico Legislative Assembly passed Joint Resolution 188 pursuant to the Fiscal Plan previously approved and certified for the Commonwealth by the Oversight Board.
- June 30, 2017: The Oversight Board adopted Joint Resolution 188 on behalf of the Governor, who subsequently signed it.
- August 23, 2017: The Governor signed Act 106 into law.

Joint Resolution 188, which was passed in violation of the automatic stay applicable in the ERS Title III Case, required ERS to sell its assets and transfer the net proceeds, plus any available funds, into the Commonwealth's General Fund. J.R. 188, §§ 1–3. Joint Resolution 188 also required employers to make contributions directly to the Commonwealth's General Fund rather than to ERS. *See id.* §§ 1–4.

Act 106, also in violation of the ERS automatic stay, further implemented Joint Resolution 188. The Act stated that Joint Resolution 188 “eliminated” “the employer contributions being made until now,” and purported to set up a new “‘Pay-Go’ Fee” that employers must pay directly into the Commonwealth's General Fund. Act 106, § 1.4, pp. 13–14. The “‘Pay-Go’ Fee” was nothing new, however, because the employers required to pay it are the same government entities, including the Commonwealth, that were previously obligated to make employer contributions to ERS; indeed, even the “contributions” are the same obligations. *See id.* § 1.6(g), p. 15 (requiring payments from “entities considered employers under the [ERS]”); *compare id.* § 2.1(b), p. 17, with 3 L.P.R.A. § 781(a) (2008). Finally, Act 106 required ERS's Board of Trustees to dissolve by December 31, 2017, so that a new board could be formed to dispose of ERS's property. Act 106, §§ 4.2, 5.1–5.3.

The effect of Joint Resolution 188 and Act 106 was to transfer all of ERS's assets to the Commonwealth, which wanted ERS's assets for its own purposes. The legislation was certainly not in the best interests of ERS or its creditors.

The undisputed facts outlined above provide a clear basis for avoidance claims by ERS against the Commonwealth. Put simply, (i) the transfer of ERS's property to the Commonwealth,

January 28, 2019  
Page 3

including the post-petition transfer of hundreds of millions of dollars of employer contributions owed to ERS, and (ii) the liquidation of ERS's assets and transfer of such assets to the Commonwealth during the pendency of the ERS Title III Case prior to any confirmed plan of adjustment for ERS, constitute fraudulent transfers avoidable by ERS under section 544(b) of the Bankruptcy Code and unlawful post-petition transfers avoidable under section 549(a) of the Bankruptcy Code. The ERS automatic stay expressly enjoins "any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate[.]" 11 U.S.C. § 362(a). The foregoing post-petition acts by the Commonwealth to exercise control over ERS's property constitute clear violations of the ERS automatic stay.

The Oversight Board has no legally justifiable reason for failing to pursue the foregoing avoidance claims on behalf of ERS. There are two presumptive reasons why the Oversight Board has failed to zealously advocate on ERS's behalf. First, the Oversight Board has a simultaneous interest in representing the Commonwealth, as the beneficiary of the transfer. Second, the Oversight Board has an interest in defending Joint Resolution 188 and Act 106, which the Oversight Board itself required the Commonwealth to enact. The Oversight Board's conflict of interest is disqualifying. And conflicts of interest equally preclude the Official Committee of Unsecured Creditors, the Official Committee of Retired Employees of the Commonwealth of Puerto Rico, the Puerto Rico Fiscal Agency and Financial Advisory Authority, and all of the professionals employed by any of those entities from representing ERS.<sup>2</sup>

We demand that the Oversight Board respond to this letter no later than Friday, February 1, 2019. Given the possible application of statute of limitations for avoidance actions under sections 546(a) and 549(d) of the Bankruptcy Code, applicable to the ERS Title Case by section 301 of PROMESA, time is of the essence.

All rights of the Bondholders are reserved, including seeking the appointment of a trustee in the ERS Title III Case to pursue such avoidance actions pursuant to section 926 of the Bankruptcy Code, made applicable by section 301 of PROMESA.

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<sup>2</sup> In light of the Oversight Board's role in the unlawful transfers and its other disqualifying conflicts, the Bondholders believe that any demand requirement is discharged as futile.

January 28, 2019  
Page 4

Very truly yours,

/s/ Bruce S. Bennett

Bruce S. Bennett

JONES DAY

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*Counsel for the ERS Bondholders Group*

/s/ John K. Cunningham

John K. Cunningham

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Miami, FL 33131

*Counsel for the Puerto Rico Funds*



# **EXHIBIT C**

**IN THE UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF PUERTO RICO**

_____	)	
In re:	)	
	)	PROMESA
THE FINANCIAL OVERSIGHT AND	)	Title III
MANAGEMENT BOARD FOR PUERTO RICO,	)	
	)	Case No. 3:17-bk-03283 (LTS)
as representative of	)	
THE COMMONWEALTH OF PUERTO RICO, <i>et al.</i> ,	)	
	)	
Debtors.	)	
_____	)	
	X	
In re:	)	
	)	
THE FINANCIAL OVERSIGHT AND	)	PROMESA
MANAGEMENT BOARD FOR PUERTO RICO,	)	Title III
	)	
as representative of	)	Case No. 3:17-bk-03566 (LTS)
	)	
THE EMPLOYEES RETIREMENT SYSTEM OF THE	)	
GOVERNMENT OF THE COMMONWEALTH OF	)	
PUERTO RICO,	)	
	)	
Debtor.	)	
-----	)	
	X	

**ORDER GRANTING MOTION OF CERTAIN SECURED CREDITORS  
OF THE EMPLOYEES RETIREMENT SYSTEM OF THE  
GOVERNMENT OF THE COMMONWEALTH OF PUERTO RICO  
FOR APPOINTMENT AS TRUSTEES UNDER 11 U.S.C. § 926**

Upon consideration of the *Motion of Certain Secured Creditors of the Employees Retirement System of the Government of the Commonwealth of Puerto Rico for Appointment as Trustees Under 11 U.S.C. § 926* (the “Motion”)<sup>1</sup> filed by Movants (hereinafter the “Bondholders” or “ERS Bondholders”)<sup>2</sup> for appointment as trustees, pursuant to § 926 of title 11 of the United States Code, to pursue the claims in the proposed Complaint attached as Exhibit A to the Motion on behalf of the Employees Retirement System of the Government of the Commonwealth of Puerto Rico (“ERS”) against the Commonwealth of Puerto Rico; the Court having reviewed the Motion and the relief requested; the Court having jurisdiction over this matter pursuant to 28 U.S.C. § 1331 and 48 U.S.C. § 2166(a); the Court determining that venue of this proceeding and the Motion in this District is proper under 28 U.S.C. § 1391(b) and 48 U.S.C. § 2167(a); notice of the Motion being adequate and proper under the circumstances; upon the record of the hearing on the Motion; and after due deliberation and sufficient cause appearing; therefore, it is hereby ORDERED that:

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<sup>1</sup> Capitalized terms not otherwise defined herein have the respective meanings given to them in the Motion.

<sup>2</sup> Movants include Andalusian Global Designated Activity Company, Crown Managed Accounts for and on behalf of Crown/PW SP, Glendon Opportunities Fund, L.P., LMA SPC for and on behalf of Map 98 Segregated Portfolio, Mason Capital Master Fund LP, Oaktree-Forrest Multi-Strategy, LLC (Series B), Oaktree Opportunities Fund IX, L.P., Oaktree Opportunities Fund IX (Parallel 2), L.P., Oaktree Value Opportunities Fund, L.P., Oceana Master Fund Ltd., Ocher Rose, L.L.C., Pentwater Merger Arbitrage Master Fund Ltd., PWCM Master Fund Ltd., Puerto Rico AAA Portfolio Bond Fund, Inc., Puerto Rico AAA Portfolio Bond Fund II, Inc., Puerto Rico AAA Portfolio Target Maturity Fund, Inc., Puerto Rico Fixed Income Fund, Inc., Puerto Rico Fixed Income Fund II, Inc., Puerto Rico Fixed Income Fund III, Inc., Puerto Rico Fixed Income Fund IV, Inc., Puerto Rico Fixed Income Fund V, Inc., Puerto Rico GNMA & U.S. Government Target Maturity Fund, Inc., Puerto Rico Investors Bond Fund I, Puerto Rico Investors Tax-Free Fund, Inc., Puerto Rico Investors Tax-Free Fund, Inc. II, Puerto Rico Investors Tax-Free Fund III, Inc., Puerto Rico Investors Tax-Free Fund IV, Inc., Puerto Rico Investors Tax-Free Fund V, Inc., Puerto Rico Investors Tax-Free Fund VI, Inc., Puerto Rico Mortgage-Backed & U.S. Government Securities Fund, Inc., SV Credit, L.P, Tax-Free Puerto Rico Fund, Inc., Tax-Free Puerto Rico Fund II, Inc., and Tax-Free Puerto Rico Target Maturity Fund, Inc.

1. The Motion is GRANTED as set forth herein.
2. The ERS Bondholders are hereby appointed as trustees for ERS to pursue the claims set forth in the proposed Complaint attached as Exhibit A to the Motion.
3. The Clerk shall file the proposed Complaint attached as Exhibit A to the Motion.
4. The Court shall retain jurisdiction to hear and determine all matters arising from the implementation of this order.

Dated: \_\_\_\_\_  
San Juan, Puerto Rico

\_\_\_\_\_  
UNITED STATES DISTRICT JUDGE