AMERICAN BANKRUPTCY INSTITUTE
JOURNAL
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Feature

By Luke A. Barefoot and Matthew J. Livingston

Unjust Enrichment or Fraudulent Transfer? Try Both

Luke A. Barefoot
Cleary Gottlieb Steen & Hamilton LLP
New York

Matthew J. Livingston
Cleary Gottlieb Steen & Hamilton LLP
New York

Luke Barefoot is a partner and Matthew Livingston is an associate in the Bankruptcy and Restructuring Goup of Cleary Gottlieb Steen & Hamilton LLP in New York.

While practitioners may have taken solace in the rule that distressed counterparties could generally not pursue unjust-enrichment claims where there was a valid contract in place, a recent opinion should give defendants new reasons to worry. Specifically, the *Fisker Automotive* bankruptcy permits the liquidating trust to pursue both fraudulent-transfer and unjust-enrichment claims arising from pre-petition transfers made by the debtor to one of its key suppliers.[1] While trustees and debtors in possession regularly attempt to avoid allegedly fraudulent transfers made by the debtor prior to a chapter 11 filing, pleading unjust-enrichment claims in the alternative for the same transfers has been much less common.

The *Fisker* opinion is significant in that it will likely lead to more frequent pleading of unjust-enrichment claims and might have a significant impact on settlement negotiations and discovery costs for defendants faced with fraudulent transfer claims. This is particularly the case for foreign defendants, where the *Fisker* opinion also adds another opinion to the growing division on whether § 548 of the Bankruptcy Code applies to extraterritorial transfers, and raises new questions about the enforceability of judgments under the doctrine of international comity.

Background

In 2007, Fisker Automotive Holdings Inc. and Fisker Automotive Inc. (together, "Fisker") were formed to manufacture plug-in hybrid vehicles. By 2011, Fisker had begun to sell its flagship Karma sedan and hoped to expand by offering multiple other plug-in hybrid models. In 2011, as part of its expansion plans, Fisker entered into supply contracts with BMW under which BMW provided Fisker with certain engines and other parts for Fisker's plug-in vehicles, and Fisker agreed to pay BMW certain amounts at signing and at regular intervals throughout the production process. These supply contracts were governed exclusively by German law, with a forum-selection clause pointing to Munich, Germany.

Prior to its bankruptcy filing in November 2013, Fisker made payments to BMW under the supply contracts totaling more than $32 million (the "transfers"). After its bankruptcy filing, the Fisker debtors rejected the supply contracts and were then liquidated, with their assets placed into a trust overseen by a liquidating trustee.

The Complaint and Motion to Dismiss

In November 2015, the trustee initiated an adversary proceeding against BMW seeking to recover the payments made by Fisker to BMW. The complaint alleged that the transfers were fraudulent transfers under §§ 548 and 544 of the Bankruptcy Code and California or Delaware state law. The complaint also asserted one count of unjust enrichment, stating that BMW "has unjustly retained the Transfers at the expense of the Debtors' estates" and requesting that it return those amounts.

BMW moved to dismiss the complaint and argued, *inter alia*, that the transfers were not fraudulent because § 548 did not apply extraterritorially, and that even if it did, there was no evidence presented that Fisker did not receive reasonably equivalent value for the transfers. BMW also argued that avoidance of the vast majority of transfers was time-barred as the transfers took place prior to § 548's two-year look-back period. BMW also argued that under § 544, German law applied and provided no remedy for allegedly constructively fraudulent transfers.

1 *Emerald Capital Advisors Corp. ex rel. FAH Liquidating Trust v. Bayerische Motoren Werke Aktiengesellschaft (In re FAH Liquidating Corp.)*, No. 13-13087 (KG), Adv. Pro. No. 15-51898 (KG) (Bankr. D. Del. June 13, 2017) (the "Opinion").

As to the unjust-enrichment claims, BMW argued that the supply contracts were valid, negotiated contracts between Fisker and BMW, and that under black-letter law, "[a] claim for unjust enrichment is not available if there is a contract that governs the relationship between the parties that gives rise to the unjust-enrichment claim."[2] Specifically, BMW noted that Fisker's rejection of the contract was itself evidence that the contract was valid and argued that the debtor can hardly reject contracts — breaching them — and then argue for "unjust enrichment" because there are no contracts.

The Opinion

On June 13, 2017, the court issued its opinion, granting in part and denying in part the motion to dismiss.[3] The court held that § 548 applied extraterritorially, but limited the potential avoidance of the transfers under § 548 to the $793,761.87 of transfers made within two years of the Fisker filing date. The court agreed with BMW that German law (1) should control the § 544 fraudulent-transfer analysis and (2) would not permit a claim for constructive fraudulent transfer. Finally, the court held that the unjust-enrichment claim would survive the motion to dismiss, finding that the unjust-enrichment claim should survive where it was plausible that the trustee's other claims would fail. Interestingly, neither the court nor the parties raised the possibility that German law should also control the unjust-enrichment claim.[4]

Unjust Enrichment

In finding that the unjust-enrichment claim would survive the motion to dismiss, the court focused on the fact that the trustee could potentially be left without a remedy at law (*e.g.*, if the trustee could not prove the insolvency of the debtor at the time of the transfers). On this basis, the survival of the unjust-enrichment claim was appropriate at the motion-to-dismiss stage. The court also noted that courts have found that even inconsistent claims, such as breach of contract and unjust enrichment, can be pleaded in the alternative and potentially survive a motion to dismiss.[5] This had the practical effect of keeping alive more than $30 million in potential damages for purposes of discovery and settlement negotiations, otherwise the liquidating trustee would have been limited to less than $1 million.

While the *Fisker* opinion cited to *Green Field Energy*,[6] the *Fisker* court appeared to use a different standard regarding the requirements for pleading in the alternative. In *Green Field Energy*, the court stated that a trustee "may plead alternative claims for relief at this stage in the proceeding so long as each is supported by sufficient factual material to move the needle from possible to plausible."[7] In *Fisker*, however, the court held only that it is "entirely acceptable to pursue alternative theories" and then concluded that the "[t]he unjust-enrichment claim in Count V is significant because it keeps alive the claim for the entire amount [that] the Trustee has placed at issue," without any finding that the unjust-enrichment claim was itself "supported by sufficient factual material to move the needle from possible to plausible."[8]

Although the *Fisker* court seems to have implicitly concluded that the unjust enrichment met the plausibility standard, the fact that the court did not address BMW's rejection of the supply contracts by Fisker during the bankruptcy is clearly significant. BMW had asserted that rejection of the contract by Fisker was itself an acknowledgment of the existence of the contract and that Fisker did not argue that the supply contracts were invalid or unenforceable.

If the unjust-enrichment claim was sufficiently plausible to survive the motion to dismiss, it is significant that this finding must have rested on grounds other than a dispute between the parties over whether the supply contracts governed the transfers. Under the opinion's rationale, a debtor's rejection of a contract in no way insulates counterparties to that contract from unjust-enrichment claims, at least not at the critical motion-to-dismiss stage.

Impact of the Survival of an Unjust-Enrichment Claim

Although trustees and debtors may cheer the fact that the *Fisker* court permitted the unjust-enrichment claim to survive a motion to dismiss, recovery on a claim for unjust enrichment is still likely to be relatively infrequent, especially in cases in which the debtor is unable to contest the existence of a contractual relationship governing the transfers in question. Instead, the impact of the *Fisker* opinion is likely to be felt most acutely by defendants who must weigh the costs of settling unjust-enrichment and fraudulent transfer claims or subject themselves to the costs of discovery and litigation.

In *Fisker*, the court acknowledged that the survival of the unjust-enrichment claim was "significant because it keeps alive the claim for the entire amount which the Trustee has placed at issue, namely $32,579,798.87." Rather than pursuing only the surviving $793,761.87 of fraudulent transfer claims, the trustee in *Fisker* can now negotiate a settlement or continue litigating in the shadow of a potential judgment in excess of $32 million. While defendants will certainly discount settlement terms based on the perceived likelihood of success, the fact that unjust-enrichment claims can successfully survive a motion to dismiss — even in the presence of a rejected contract — is perhaps *Fisker*'s most important lesson in fraudulent transfer litigation dynamics.

Section 548 and Extraterritoriality

The second significant aspect of the opinion is the court's finding that § 548 applies extraterritorially. Although the Southern District of New York has been split on this issue, the *Fisker* court is the first in the District of Delaware to address the issue, providing important (albeit flawed) guidance for pending and future claims brought there.

Section 548 states that a trustee "may avoid any transfer ... of an interest of the debtor in property, or any obligation ... incurred by the debtor, that was made or incurred on or within 2 years before the date of the filing of the petition."[9] While the two-year limitation period is straightfor-

2 *See, e.g., Kuroda v. SPJS Holdings LLC*, 971 A.2d 872, 891 (Del. Ch. 2009).
3 D.I. 39 (the "Opinion").
4 As discussed *infra*, issues of international comity may arise if a significant unjust-enrichment claim under U.S. law were to be imposed on a foreign corporation that entered into a contract containing non-U.S. governing law.
5 *Id.* at 25 (citing *Pedrick v. Roten*, 70 F. Supp. 3d 638, 653 (D. Del. 2014)).
6 *Halperin v. Moreno (In re Green Field Energy Servs. Inc.)*, 2015 WL 5146161 (Bankr. D. Del. Aug. 31, 2015).
7 *Id.* at 10.
8 Op. at 25.
9 11 U.S.C. § 548.

ward, courts have been split on whether § 548 should apply to extraterritorial transfers outside the U.S., such as the transfers from Fisker to BMW.[10]

In finding that § 548 applies extraterritorially, the *Fisker* court was not persuaded by the reasoning of the Southern District of New York in *Maxwell* and *Spizz*, each finding that there was no indication of congressional intent that § 548 should apply extraterritorially and that therefore the strong presumption in U.S. law against the application of statutes extraterritorially should guide courts to limit § 548 to domestic transfers.[11]

Instead, the *Fisker* court followed the *Lyondell* opinion from the Southern District of New York in looking to other Bankruptcy Code provisions that do have extraterritorial effect, primarily § 541, which defines property of the estate as, *inter alia*, all "interests of the debtor in property." Clinging to the slim reed that § 548 also includes the phrase "interest of the debtor in property," these courts concluded that Congress likely intended for § 548 to apply to extraterritorial transfers.[12]

While the *Spizz* court's reasoning finding no indication of congressional intent regarding extraterritorial application of § 548 is more persuasive, the *Fisker* court has established that District of Delaware courts are willing to apply § 548 extraterritorially. In light of this, at least until the division in authority is resolved, defendants should take note that all worldwide transactions with potentially insolvent entities are likely to be scrutinized as potential fraudulent transfers and should not count on the extraterritorial nature of transactions to provide a reliable defense to fraudulent transfer claims. In addition, particularly if the *Lyondell* decision is ultimately overturned on appeal, the *Fisker* opinion might drive debtors with significant foreign fraudulent transfer claims to seek a Delaware bankruptcy forum.

International Comity

One final implication of the opinion that was never addressed by the court or parties relates to the enforceability of judgments under the doctrine of international comity. Comity — the doctrine that the courts of one country will enforce the judgments of another[13] — is inherently implicated in cross-border fraudulent transfer litigation if a plaintiff seeks to enforce a judgment in a foreign jurisdiction. In light of the opinion, if the trustee were to be successful on its unjust-enrichment claim and seek to enforce the judgment in a German court, the German court might be hesitant to enforce the judgment given the existence of a clear contract underlying the transfers.

Insofar as the underlying contract specified that German law would govern and be the exclusive forum for resolving disputes under the contract, the German court might be troubled in deferring to the doctrine of comity to enforce a significant judgment under a U.S. equitable doctrine against a German company that successfully negotiated for a contract governed by German law. Similarly, U.S. courts might be wary of a foreign trustee asking a U.S. court to enforce a large judgment against a U.S. company where the U.S. company appears to have negotiated a contract to be governed by U.S. law and a foreign court nevertheless imposes an equitable judgment on the U.S. company. Although the doctrine of comity is ordinarily respected by foreign courts, it is not ironclad, and foreign and U.S. courts may decline to enforce a judgment on comity grounds if enforcement of the judgment would be contrary to public policy.[14] Depending on the jurisdiction where a foreign defendant's major assets are located, this might provide some potential salve for the wounds that *Fisker* inflicts.

Conclusion

The *Fisker* opinion is significant for counsel involved in cross-border fraudulent transfer litigation for two primary reasons: it establishes (1) precedent in the District of Delaware for an interpretation of § 548 that permits its application extraterritorially and (2) that unjust-enrichment claims can survive a motion to dismiss when pleaded in the alternative to fraudulent transfer claims, even if the transfers were made based on a contractual relationship. Plaintiffs and defendants involved in fraudulent transfer litigation should closely monitor developments in this area of law, as the outcomes of the few cases to address these issues are likely to have a significant impact on litigation strategy, forum selection and settlement negotiations going forward. abi

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10 *Compare, e.g., Weisfelner v. Blavatnik (In re Lyondell)*, 543 B.R. 127 (Bankr. S.D.N.Y. 2016) (finding that § 548 applies extraterritorially), *with Spizz v. Goldfarb Seligman & Co. (In re Ampal-Am. Israel Corp.)*, 562 B.R. 601, 612 (Bankr. S.D.N.Y. 2017) (finding that § 548 does not apply extraterritorially).

11 *Maxwell Commc'n Corp. plc v. Societe Gen. plc (In re Maxwell Commc'n Corp. plc)*, 186 B.R. 807 (S.D.N.Y. 1995), *aff'd*, 93 F.3d 1036 (2d Cir. 1996); *Spizz v. Goldfarb*, 562 B.R. 601, 605.

12 Op. at 12 (citing *Lyondell*, 543 B.R. 127, 155).

13 *See, e.g., Gross v. German Found. Indus. Initiative*, 456 F.3d 363, 392 (3d Cir. 2006) ("Generally, [U.S.] courts will not review acts of foreign governments and will defer to proceedings taking place in foreign countries, allowing those acts and proceedings to have extraterritorial effect in the [U.S.].").

14 *See, e.g., Philadelphia Gear Corp. v. Philadelphia Gear de Mexico SA*, 44 F.3d 187, 191 (3d Cir. 1994) ("'In general, '[u]nder the principle of international comity, a domestic court normally will give effect to executive, legislative, and judicial acts of a foreign nation.' More specifically, we have stated that '[c]omity should be withheld only when its acceptance would be contrary or prejudicial to the interest of the nation called upon to give it effect.'" (internal citations omitted)).