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## Fifth Circuit Curtails Remand and Abstention Remedy for U.S. Litigation Broadly Related to Foreign Debtor Chapter 15 Bankruptcy Proceedings

On June 5, 2015, a three judge panel for the United States Court of Appeals for the Fifth Circuit (the “Court”) held that a district court may not discretionarily abstain from and equitably remand a properly removed state court action when the case relates to an ongoing chapter 15 bankruptcy proceeding. Firefighters’ Ret. Sys. v. Citco Grp. Ltd., No. 14-30857, 2015 WL 3540718 (5th Cir. June 5, 2015) (the “Opinion”). The Court gave a broad reading to the exception to a court’s discretionary abstention powers codified in 28 U.S.C. § 1334(c)(1)<sup>1</sup> that applies “with respect to a case under chapter 15,” and concluded that both discretionary abstention and equitable remand are not proper either in a chapter 15 case itself or in other litigation and proceedings “arising in or related to” a chapter 15 case. The Opinion represents an issue of first impression by a federal appellate court, and if other courts of appeal follow suit, it would allow actions that relate to a pending chapter 15 case – whether or not the foreign debtor or its foreign representative are party to the litigation – to be removed to and maintained in federal district court without being subject to potential remand to the state court in which they were originally commenced.

### **Background and Procedural History**

The appeal centers on a state court litigation commenced by three Louisiana retirement systems that provide pension benefits to New Orleans public employees (collectively, the “Retirement Systems”). Firefighters’ Ret. Sys. v. Citco Grp. Ltd., Civil Action No. 13-373-SDD-SCR, 2014 WL 3565716, at \*2 (M.D. La. July 18, 2014). In 2008, the Retirement Systems made a significant investment (such invested money, the “Funds”) with FIA Leveraged Fund (“Leveraged”), a Cayman entity. Id. Leveraged was part of a family of investment entities that included Fletcher Income Arbitrage Fund, Ltd. (“Arbitrage,” another Cayman Islands entity), Fletcher International, Inc. (“FII”) and Fletcher International, Ltd. (“FIL”). Id. Following the Retirement Systems’ initial investment, the Funds were passed through an investment chain, as Leveraged invested the Funds with Arbitrage, Arbitrage invested the funds with FII, and FII invested the Funds with FIL. Id. at \*3.

Following unsuccessful attempts to redeem their notes and seeing no return on their initial investment, the Retirement Systems took several steps to recover the Funds. First, in 2012, the Retirement Systems filed petitions in the Cayman Islands, and secured the appointment of liquidators for Leveraged and Arbitrage (the “Liquidators”). Id. at \*4. Shortly

<sup>1</sup> 28 U.S.C. § 1334(c)(1) states that “[e]xcept with respect to a case under chapter 15 of title 11, nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11” (emphasis added).

thereafter, in 2013, they filed the instant action in state court (the “Louisiana Case”) against certain related funds and administrators of Leveraged and Arbitrage (the “Defendants”), alleging various state law statutory, contract and tort causes of action. None of Leveraged, Arbitrage, FIL or the master fund FIL were named as defendants in that action. Id. at \*2-3.

In parallel, in 2012, FIL commenced a chapter 11 bankruptcy case in the United States Bankruptcy Court for the Southern District of New York (the “Bankruptcy Court,” and such bankruptcy, the “FIL Chapter 11 Bankruptcy”). Id. at \*2 n.6. Each of the Retirement Systems, the Liquidators and certain of the Defendants filed proofs of claims in the FIL Chapter 11 Bankruptcy (the “Proofs of Claims”). Id. at \*5. The Retirement Systems alleged that FIL was the alter-ego of Leveraged, and since they were unable to recover the Funds from Leveraged, they should be entitled to recover from FIL. Id. One of the Liquidators asserted a claim on behalf of Leveraged on similar grounds and certain of the Defendants asserted indemnification claims. Id. The Bankruptcy Court confirmed FIL’s plan of reorganization in early 2014 through a confirmation order (the “Confirmation Order”). Id. at \*18. FIL’s plan did not purport to release or limit the claims asserted in the Louisiana Case.

In June 2013, the Defendants removed the Louisiana Case to the District Court for the Middle District of Louisiana (the “District Court”). The Plaintiffs sought remand of the case back to the Louisiana state court under the federal statutory permissive abstention and equitable remand provisions contained in 28 U.S.C. §§ 1334(c)(1) and 1452(b).<sup>2</sup> While the remand motion was pending and prior to the District Court’s ruling on the motion, the Liquidators commenced chapter 15 cases on behalf of Leveraged and Arbitrage in the Bankruptcy Court in furtherance of their Cayman proceedings (the “Chapter 15 Cases”). Id. at \*14 n.36.

In addressing the Retirement Systems’ motion for abstention and remand, the District Court first addressed whether it had continued subject matter jurisdiction over the Louisiana Case given that the case was removed to federal court as being related to the FIL Chapter 11 Bankruptcy, but the Bankruptcy Court already had issued the Confirmation Order by the time the abstention and remand motion was being considered. The court concluded that since at the time of removal, resolution of the Louisiana Case would have impacted the value and validity of the Proofs of Claims, the Louisiana Case was sufficiently “related to” the FIL Chapter 11 Bankruptcy so as to confer subject matter jurisdiction on the District Court pursuant to 28 U.S.C. § 1334(b).<sup>3</sup> Id. at \*13-15.

However, relying on its conclusion that the Louisiana Case was “related to” the FIL Chapter 11 Bankruptcy, the District Court concluded that it could use the grants of authority in 28 U.S.C. §§ 1334(c)(1) and 1452(b) to discretionarily abstain and equitably remand the Louisiana Case back to the state court, notwithstanding section 1334(c)(1)’s explicit language that such discretionary abstention is not available “with respect to a case under chapter 15.” Without considering the impact of the Chapter 15 Cases on its decision to abstain and remand,

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<sup>2</sup> 28 U.S.C. § 1452(b) states in relevant part that “[t]he court to which such claim or cause of action is removed may remand such claim or cause of action on any equitable ground.”

<sup>3</sup> 28 U.S.C. § 1334(b) states in relevant part that “the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or *related to cases under title 11*” (emphasis added).

the District Court held that abstention and remand were appropriate in this instance given Louisiana's interest in adjudicating state law claims brought by state-created pension funds, and the fact that following the Confirmation Order, resolution of the Louisiana Case would no longer impact the administration of the estate in the FIL Chapter 11 Bankruptcy. Id. at \*18-20. Defendants appealed the order for abstention and remand.

### **The Decision**

The Court overturned the District Court's ruling that it would abstain and remand the case back to the Louisiana state court, based on its conclusion that the District Court did not have the authority to discretionarily abstain or equitably remand the Louisiana Case.<sup>4</sup>

The Court addressed the District Court's purported authority for discretionary abstention, noting the "two possible interpretations of [28 U.S.C. § 1334(c)(1)]," and explaining that the phrase "except with respect to a case under chapter 15 of title 11" that carves back a federal court's abstention powers could be read to "mean that § 1334(c)(1) only excepts the Chapter 15 bankruptcy itself" from a potential abstention request, or it "could mean that both the Chapter 15 case itself and cases 'arising in or related to' Chapter 15 cases are excluded" from section 1334(c)(1)'s grant of authority to discretionarily abstain. Opinion at \*3.

In determining which alternative reading was correct, the Court looked to the plain language and purpose of section 1334(c)(1). In an effort to read the word "case" consistently throughout, it interpreted the chapter 15 exception to abstention to apply to proceedings "arising in or related to" a case under chapter 15 of title 11, since the operative phrase functions as an explicit limitation on the broad grant of discretionary abstention authority with respect to proceedings "arising in or related to a case under title 11," and not merely to the chapter 15 case itself. Id.

Building on its interpretation of section 1334(c)(1), the Court then addressed the District Court's purported authority to equitably remand the case under section 1452(b). Explaining that sections 1334(c)(1) and 1452(b) must be read together, the Court concluded that "the prohibition against abstention from proceedings related to Chapter 15 cases also applies to bar the equitable remand of those proceedings under § 1452." Id. at \*4.

Finally, the Court addressed the Retirement Systems' argument that the chapter 15 exception to abstention and remand is not applicable to the Louisiana Case, since the Chapter 15 Cases were filed after the motion for removal. Making quick work of this argument, the Court clarified that the determination of whether a proper factual basis existed for a remand order "is judged at the time of that order, not the time of the original removal." Id.

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<sup>4</sup> While orders for remand are usually unreviewable, the Court concluded that it has authority to hear the appeal based on its right to consider the appeal where a district court has exceeded its statutorily defined authority. The Court explained that "[d]efendants base their challenge to the [D]istrict [C]ourt's order on the argument that [the statutory authority for remand] does not apply in this case, rather than on the court's reasons for remand. We conclude that Defendants' challenge to the remand order thus falls within an exception to nonreviewability." Opinion at \*3.

Concluding its analysis, the Court remanded the case back to the District Court for proceedings consistent with its ruling, and explicitly held that “a district court cannot permissively abstain from exercising jurisdiction in proceedings related to Chapter 15 cases.” *Id.* at \*5.

### **Significance of the Decision**

*Citco* is important because it provides guidance on the scope of a district court’s authority to discretionarily abstain from hearing or equitably remand litigation proceedings related to an ongoing chapter 15 case that have been removed from state court. The Fifth Circuit’s broad interpretation of the exception to the general right of the court to remand such proceedings back to state court – including for cases to which the foreign debtor and its foreign representative are not parties – may provide defendants an opportunity to opt to have their cases determined by a federal court to the extent a connection can be shown to a pending chapter 15 proceeding. Given the rise in international insolvencies and chapter 15 filings, this decision provides helpful clarity on the management of litigation in U.S. state and federal courts related to such foreign insolvencies.

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