

# 2022 WINTER WORKSHOP

Discussion of Efforts to Improve Statutory  
Lien Status; Bankruptcy Issues

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## CONTENTS

LIENS. ....	1
STATUTORY LIENS. ....	1
EXAMPLES OF STATUTORY LIEN STATUTES. ....	1
Example of a Bond Revenue Lien .....	1
Example of a Bond Mortgage Lien.....	2
Example if GO Statutory Lien .....	2
Example of Mortgage Lien on System – .....	2
Example General Statutory Lien.....	3
Example Statutory Lien Receipts .....	4
Example Statutory Lien Net Revenues .....	5
Puerto Rico § 3192 Statutory lien on the restructuring property	5
Does this statute create a statutory lien?.....	5
NEW STATUTORY LIEN STATUTES .....	6
§ 41-10-472. Pledge and lien for benefit of bonds.....	6
Michigan 123.961d. Bonds; ordinance or resolution authorizing issuance, lien on cash rental payments.....	6
UNDERSTANDING BANKRUPTCY PRIORITIES .....	7
STATUTORY LIENS IN BANKRUPTCY.....	8
Court Determines Statutory Lien.....	9
Special Fund Doctrine Liens.....	9
Bankruptcy Treatment of Statutory Liens.....	10
Statutory Lien Avoidable if not perfected. ....	13
PERFECTION .....	13
UCC-1 PERFECTION .....	13
UCC Article 9 State Statutes that don't file UCC-1s.....	14
PERFECTION THE OLD WAY - THE FIELD CODE.....	19
Field Code State Statutes .....	20
North Dakota 35-03-10. Mortgage for purchase price of real property prior to all liens. ....	20
Oklahoma Title 42-1.....	20
Montana 71-3-114. Priority of purchase money mortgage.....	21

South Dakota 44-2-2. Purchase price of real property--Mortgage given for at time of conveyance--Vendor's lien--Priority over other liens--Operation of recording laws.....	21
Idaho § 45-112. Priority of purchase money mortgage .....	21
Cal. Civ. Code § 2898.....	21
State Recording Requirements. ....	21
Alabama Code § 11-49A-12 Statutory mortgage lien; creation; filing of notice. ....	21
§ 35-01-09. Recorder to file and index lien .....	22
65 Ill. Comp. Stat. Ann. 5/8-13-11 .....	22
STATE LAW POWER TO FILE FOR BANKRUPTCY .....	24
Michigan Chapter 9.....	24
Nebraska Chapter 9 .....	24
REQUIREMENTS FOR FILING CHAPTER 9.....	25
MUNICIPAL BANKRUPTCY.....	26
Definitions.....	26
APPENDIX .....	28
PUERTO RICO COURT RECOGNIZES LIMIT TO BANKRUPTCY CODE'S STATUTORY LIEN DEFINITION.....	28
In re Financial Oversight and Management Board for Puerto Rico, 899 F.3d 1 (2018) .....	32

## LIENS.

A “Lien” means charge against or interest in property to secure payment of a debt or performance of an obligation. In general, the three types of liens are:

1. security interests,
2. judicial liens, and
3. statutory liens.

## STATUTORY LIENS.

Security interests are created by contract, judicial liens are created by the court, and statutory liens are created by statute. Statutory liens include:

- mechanic’s liens
- a bailee’s lien for labor and services,
- a creditor’s privilege lien,
- contractors’ liens,
- a receiver’s lien,
- statutory liens,
- federal tax liens,
- bond statutory revenue liens, and
- bond statutory mortgage liens.

## EXAMPLES OF STATUTORY LIEN STATUTES.

### *Example of a Bond Revenue Lien*

Sec. 9. The net revenues which are pledged shall be and remain subject to the statutory lien until the payment in full of the principal of and interest upon the bonds unless the authorizing ordinance provides for earlier discharge of the lien by substitution of other security. The holder of the bonds, representing in the aggregate not less than 20% of the entire issue then outstanding, may protect and enforce the statutory lien and enforce and compel the performance of all duties of the officials of the borrower, including the fixing of sufficient rates, the collection of revenues, the proper segregation of revenues, and the proper application of the revenues. The statutory lien shall not be construed to give a holder or owner of a bond or coupon authority to compel the sale of the public

improvement, the revenues of which are pledged to the improvement. Mich. Comp. Laws Ann. § 141.109 (West)

### *Example of a Bond Mortgage Lien*

There shall be a statutory mortgage lien upon such utility and the extensions, additions, and improvements thereto acquired pursuant to this chapter, in favor of and for the equal benefit of the lawful holders of bonds issued pursuant to this chapter and interest coupons and each of them, but no such lien shall attach to or become a charge upon or against any property or utility or any part thereof previously owned by such municipality by whatever means or funds acquired. Until all such bonds are fully paid with interest, the municipality shall not sell or otherwise dispose of said utility and shall not establish, authorize, or grant a franchise for the operation of any other utility for supplying like products or services in competition therewith. S.D. Codified Laws § 9-40-25

### *Example if GO Statutory Lien*

(a) General obligation bonds issued and sold by or on behalf of a local agency shall be secured by a statutory lien on all revenues received pursuant to the levy and collection of the tax. The lien shall automatically arise without the need for any action or authorization by the local agency or its governing body. The lien shall be valid and binding from the time the bonds are executed and delivered. The revenues received pursuant to the levy and collection of the tax shall be immediately subject to the lien, and the lien shall immediately attach to the revenues and be effective, binding, and enforceable against the local agency, its successors, transferees, and creditors, and all others asserting rights therein, irrespective of whether those parties have notice of the lien and without the need for any physical delivery, recordation, filing, or further act.

(b) This section is not intended to supplement or limit a local agency's power to issue general obligation bonds conferred by any other law.

(c) For purposes of this section, both of the following definitions apply:

(1) “General obligation bonds” means bonds, warrants, notes, or other evidence of indebtedness of a local agency payable, both principal and interest, from the proceeds of ad valorem taxes that may be levied pursuant to paragraphs (2) and (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution.

(2) “Local agency” means any city, county, city and county, school district, community college district, authority, or special district. Cal. Gov't Code § 53515 (West)

### *Example of Mortgage Lien on System –*

N.H. Rev. Stat. Ann. § 444:4-a

§ 51-8-41. Creation of statutory lien

There is hereby created a statutory lien in the nature of a mortgage lien upon any system or systems acquired or constructed in accordance with this chapter, including all extensions and improvements thereof or combinations thereof subsequently made, which lien shall be in favor of the holder or holders of any bonds issued pursuant to said sections, and all such property shall remain subject to such statutory lien until the payment in full of the principal of and interest on said bonds. Any holder of said bonds or any of the coupons representing interest thereon may, either at law or in equity, by suit, action, mandamus or other proceedings, in any court of competent jurisdiction, protect and enforce such statutory lien and compel the performance of all duties required by said sections, including the making and collection of sufficient rates for the service or services, the proper accounting thereof, and the performance of any duties required by covenants with the holders of any bonds issued in accordance herewith.

If any default is made in the payment of the principal of or interest on such bonds, any court having jurisdiction of the action may appoint a receiver to administer said district and said system or systems, with power to charge and collect rates sufficient to provide for the payment of all bonds and obligations outstanding against said system or systems, and for payment of operating expenses, and to apply the income and revenues thereof in conformity with the provisions of this chapter and any covenants with bondholders. Miss. Code. Ann. § 51-8-41 (West)

*Example General Statutory Lien.*

Louisiana § 504. Statutory lien

A. It is the intention of the legislature that bonds issued by a governmental entity under this Part, or under any other statutory authority referenced herein, shall be secured debt entitled to the highest possible protection and priority afforded by the bankruptcy laws of the United States and this state. Therefore, the owner or owners of any such bonds are hereby granted and shall have a statutory lien on and a security interest in such taxes, income, revenues, net revenues, monies, payments, receipts, agreements, contract rights, funds, or accounts as are pledged to the payment of such bonds, to the fullest extent and in the manner stated in this Part and in the proceedings authorizing such bonds, and any pledge or grant of a lien or security interest in such taxes, income, revenues, net revenues, monies, payments, receipts, agreements, contract rights, funds, or accounts made by a governmental entity in connection with the issuance of bonds shall be valid, binding, and perfected from the time when the pledge or grant of lien or security interest is made. Such taxes, income, revenues, net revenues, monies, payments, receipts, agreements, contract rights, funds, or accounts shall immediately be subject to the lien of such pledge and security interest without any physical delivery therefor or further act and the lien of such pledge and security interest shall be first priority and valid and binding as against all parties having claims of any kind in tort, contract, bankruptcy, or otherwise against the governmental entity, whether or not such parties have notice thereof. The owner or owners of bonds shall be secured creditors with respect to such taxes, income, revenues, net revenues, monies, payments, receipts, agreements, contract rights, funds, or accounts, as the case may be.

B. Any bond issued under this Part or any other statutory authority referenced herein may contain a recital that refers to the statutory lien created by this Section and describes the taxes, income, revenues, net revenues, monies, payments, receipts, agreements, contract rights, funds, or accounts to which such statutory lien applies; however, the failure to include the aforesaid recital shall not affect the validity or efficacy of the statutory lien granted by this Section and by the proceeds authorizing such bonds.

C. No notice, filing, or other proceedings under Chapter 9 of the Louisiana Commercial Laws, R.S. 10:9-101 et seq., or any other provision of law for the perfection or priority of such pledge and security interest shall be necessary to perfect the statutory lien granted by this Section and by the proceedings authorizing such bonds.

D. The statutory lien shall also apply to and secure any administrative fees owed to the Clean Water State Revolving Fund or the Drinking Water Revolving Loan Fund, in connection with bonds that evidence an obligation to repay a loan from one of said revolving funds. La. Stat. Ann. § 39:504

#### *Example Statutory Lien Receipts*

Illinois 13-11. Liens for obligations.

(a) As used in this Section, “statutory lien” has the meaning given to that term under 11 U.S.C. 101(53) of the federal Bankruptcy Code.

(b) Obligations issued by an issuing entity shall be secured by a statutory lien on the transferred receipts received, or entitled to be received, by the issuing entity that are designated as pledged for such obligations. The statutory lien shall automatically attach from the time the obligations are issued without further action or authorization by the issuing entity or any other entity, person, governmental authority, or officer. The statutory lien shall be valid and binding from the time the obligations are executed and delivered without any physical delivery thereof or further act required, and shall be a first priority lien unless the obligations, or documents authorizing the obligations or providing a source of payment or security for those obligations, shall otherwise provide.

The transferred receipts received or entitled to be received shall be immediately subject to the statutory lien from the time the obligations are issued, and the statutory lien shall automatically attach to the transferred receipts (whether received or entitled to be received by the issuing entity) and be effective, binding, and enforceable against the issuing entity, the transferring unit, the State entity, the State of Illinois, and their agents, successors, and transferees, and creditors, and all others asserting rights therein or having claims of any kind in tort, contract, or otherwise, irrespective of whether those parties have notice of the lien and without the need for any physical delivery, recordation, filing, or further act.

The statutory lien imposed by this Section is automatically released and discharged with respect to amounts of transferred receipts reconveyed to the transferring unit pursuant to Section 8-13-10 of this Code, effective upon such reconveyance.

(c) The statutory lien provided in this Section is separate from and shall not affect any special revenues lien or other protection afforded to special revenue obligations under the federal Bankruptcy Code. 65 Ill. Comp. Stat. Ann. 5/8-13-11

### *Example Statutory Lien Net Revenues*

Michigan 141.109. Statutory lien on net revenues; duration; enforcement

Sec. 9. The net revenues which are pledged shall be and remain subject to the statutory lien until the payment in full of the principal of and interest upon the bonds unless the authorizing ordinance provides for earlier discharge of the lien by substitution of other security. The holder of the bonds, representing in the aggregate not less than 20% of the entire issue then outstanding, may protect and enforce the statutory lien and enforce and compel the performance of all duties of the officials of the borrower, including the fixing of sufficient rates, the collection of revenues, the proper segregation of revenues, and the proper application of the revenues. The statutory lien shall not be construed to give a holder or owner of a bond or coupon authority to compel the sale of the public improvement, the revenues of which are pledged to the improvement. Mich. Comp. Laws Ann. § 141.109 (West)

### *Puerto Rico § 3192 Statutory lien on the restructuring property*

The restructuring bonds and the financing costs shall automatically, upon the issuance of the restructuring bonds, be secured by a statutory lien on the restructuring property in favor of the indenture trustee for the benefit of the holders of the restructuring bonds, which shall be senior to any other lien encumbering the restructuring property (except for valid liens and encumbrances existing as of the effective date of this act or that arise in the ordinary course of business after the effective date of this act and are existing as of the closing date, in each case with respect to any real estate assets and any personal property assets related thereto that are part of the restructuring property) and may be enforced pursuant to the terms of the ancillary agreements. Such statutory lien shall occur automatically and shall automatically be perfected, valid and binding from and after the closing date, in any case without any further act or agreement. No instrument needs to be delivered or recorded in any official record or in any government registry or office in order to perfect or continue such statutory lien or to establish or maintain the priority thereof. No commingling of any restructuring property with any other property of GDB or any other party shall limit, defeat, impair or interfere with such statutory lien. § 3192 Statutory lien on the restructuring property, 7 L.P.R.A. § 3192

### *Does this statute create a statutory lien?*

Any resolution of the board or trust indenture under which bonds may be issued pursuant to the provisions of this chapter may contain provisions creating a statutory mortgage lien, in favor of the holders of such bonds and of the interest coupons applicable thereto, on the transit systems, or any thereof (including any after-acquired property) out of the revenues from which such bonds are made payable. The said resolution of the board or the said trust indenture may provide for the

filing for record in the office of the judge of probate of each county in which any part of such transit system, or any thereof, may be located of a notice containing a brief description of such systems, a brief description of such bonds, and a declaration that said statutory mortgage lien has been created for the benefit of the holders of such bonds and the interest coupons applicable thereto, upon such systems, including any additions thereto and extensions thereof. Each judge of probate shall receive, record and index any such notice filed for record in his office. The recording of such notice, as herein provided, shall operate as constructive notice of the contents thereof. Alabama Code § 11-49A-12 Statutory mortgage lien; creation; filing of notice.

## NEW STATUTORY LIEN STATUTES

### *§ 41-10-472. Pledge and lien for benefit of bonds.*

In the proceedings authorizing the issuance of any of its bonds, the authority is authorized and empowered to pledge for the payment of the principal of and interest on such bonds at the respective maturities of said principal and interest, and to agree to use solely for such purpose, all the revenues which under the provisions of Section 41-10-471 are provided for the payment of the said principal and interest, subject to prior pledges thereof as and to the extent the authority may provide. In said proceedings the authority may further provide and create, as security for the payment of said principal and interest, a statutory lien upon the buildings and properties, other than the State Capitol, for the acquisition and construction or renovation of which the bonds are issued. Such statutory lien shall not be subject to foreclosure and, in the event of default in the payment of any such principal or interest, the remedies thereunder shall be limited to a remedy by way of mandamus and to the appointment, as a matter of right, by any court having equity powers and having jurisdiction over the authority, of a receiver in equity with all the powers of such a receiver, except the power to sell the said buildings and properties. Upon the issuance of any bonds pursuant to this article the authority may file in the office of the Judge of Probate of Montgomery County, Alabama, an instrument reciting the issuance of such bonds and the pledge of said revenues and the creation of said statutory lien, if any, as security therefor, and the filing of such instrument shall constitute constructive notice of said pledge and lien, if any. Such instrument shall be received and recorded by said judge of probate upon the payment of the fee for the recording of mortgages but no tax shall be payable with respect thereto. Ala. Code § 41-10-472

### *Michigan 123.961d. Bonds; ordinance or resolution authorizing issuance, lien on cash rental payments*

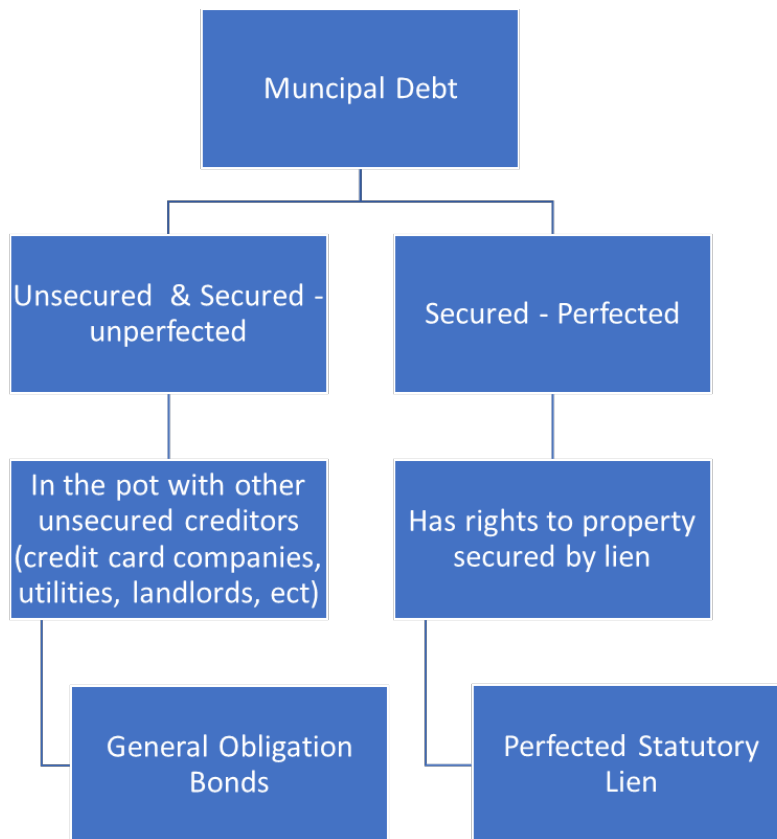
Sec. 11d. There shall be created in the authorizing ordinance or resolution a lien by this act made a statutory lien upon the cash rental payments required to be paid by the contract of lease which are pledged to the payment of the principal of and interest on the bonds to and in favor of the holders of the bonds and the interest coupons pertaining thereto. The amounts so pledged shall be and remain subject to the statutory lien until the payment in full of the principal of and interest on the bonds. The holder or holders of bonds representing in the aggregate not less than 20% of the entire issue then outstanding may by suit, action, or other proceedings protect and enforce such statutory lien and enforce and compel the performance of all duties of the officials of the authority, including, but not limited to, compelling the incorporating unit or units by proceedings

in a court of competent jurisdiction or other appropriate forum to make the cash rental payments required to be made by the contract of lease, and requiring the incorporating unit or units to certify, levy, and collect appropriate taxes as herein authorized and as may be required by the contract of lease to be so certified, levied, and collected by the incorporating unit or units for the payment of the cash rental required to be paid by the contract of lease. Mich. Comp. Laws Ann. § 123.961d (West)

## UNDERSTANDING BANKRUPTCY PRIORITIES

There are a number of general rules:

- **Perfect is the best.** A creditor with a valid and perfected security interest has recourse to its collateral.
- **First in time-first in right.** If two or more creditors are properly perfected, then the priorities among such competing secured creditors is spelled out in the UCC, but the general rule is that the first to perfect has priority, whether the competing security interests and liens are consensual or nonconsensual. The general rule does not apply in instances where the UCC specifies that perfection by possessions trumps an earlier filing; there are other exceptions to the first in time rule.
- **Perfect has priority over unperfected.** Although an unperfected security interest may be enforceable against the debtor, a properly perfected security interest will have priority over such unperfected interest.
- **Trustee has perfected creditor status.** Under the Bankruptcy Code, a trustee or debtor in possession has the rights of a perfected lien creditor and an unperfected security interest may be avoided, so that the underlying claim is treated as a general unsecured claim in bankruptcy.



## STATUTORY LIENS IN BANKRUPTCY

A statutory lien remains unaltered as a result of a bankruptcy petition and although there could be some delay in payment to bondholders due to the automatic stay in bankruptcy, the lien and rights to the particular revenue stream should remain unaltered without deduction for “necessary operating expenses,” as would be the case for a pledge of special revenues. 2017 WL 4476302, at \*3

The Court first looked at whether the plaintiff had made the initial showing that the 1968 Bonds were secured by a pledge of special revenues exempt from the automatic stay provisions of the Bankruptcy Code. The Court then reviewed whether the plaintiff had established a likelihood of success on the merits that the 1968 Bonds were secured by a statutory lien.

2017 WL 4476302, at \*3

The court then determined that the plaintiff's assertion that the 1968 Resolution created a statutory lien was not likely to succeed because the 1968 Resolution was not a statute. 13

Any assertion of a statutory lien must be closely examined for “mandatory” language, and should flow from an actual statute, rather than a consensual agreement with the issuer. 2017 WL 4476302, at \*3

### *Court Determines Statutory Lien*

As regarding provision of this section allowing trustee to avoid fixing of certain statutory liens on debtor's property to extent of that lien, state law is relevant in that determination of whether a state regulatory lien is perfected or enforceable against a bona fide purchase is generally determined by reference to laws of state which created the lien. In re Cambron Corp., Bkrty.E.D.Mich.1983, 27 B.R. 723. Bankruptcy Key Number Symbol 2580.1

Under Wisconsin law, statutory lien arose in favor of city for delinquent water use charges only after service was provided, when charges remained unpaid, notice was given, and city comptroller placed charges on tax roll, and did not relate back to time prior to debtor/property owner's Chapter 11 filing; accordingly, lien could be avoided in exercise of debtor's strong-arm power. Bankr.Code, 11 U.S.C.A. §§ 545(2), 546(b). In re U.S. Leather, Inc., 271 B.R. 306 (Bankr. E.D. Wis. 2001)

### *Special Fund Doctrine Liens.*

In a state that has adopted the “special fund doctrine” ... (e.g., Washington in 1895), pertinent statutes (for each type of local government) provide that the governing body that proposes to issue bonds, (1) by resolution shall create a special fund or funds, (2) by resolution obligate and bind the governmental unit to set aside and pay all or a portion of gross revenue into the special

fund for the purpose of paying such bonds as they become due; (3) by resolution provide that the special funds shall be drawn upon solely for the purposes of paying such bonds. The statute further provides that if the elected officials fail to pay and set aside the promised revenues, the owner of the bonds may bring suit to compel compliance with the provisions of the resolution.

This statute should be construed to create a statutory lien. (even if the statute does not use the term “lien”, and in our view, the “lien” is created by the adoption of the resolution that authorizes the issuance of the bonds. This is based on the distinction between a consensual (contractual) lien vs a “lien” or binding pledge with respect to a revenue stream that is established in accordance with the terms of a statute.

### *Bankruptcy Treatment of Statutory Liens*

The Bankruptcy Code defines a lien as a “charge against or interest in property to secure payment of a debt or performance of an obligation.” 11 U.S.C. § 101(37). The Code classifies liens into three (3) categories:

- judicial liens,
- statutory liens, and
- security interests.

A statutory lien is defined as “**a lien arising solely by force of a statute on specified circumstances or conditions**, or lien of distress for rent, whether or not statutory, but does not include security interest or judicial lien, whether or not such interest or lien is provided by or is dependent on a statute and whether or not such interest or lien is made fully effective by statute.” 11 U.S.C. § 101(53). On the other hand, the Code defines a security interest as a “lien created by an agreement,” 11 U.S.C. § 101(51),

and a judicial lien as a “lien obtained by judgment, levy, sequestration, or other legal or equitable process or proceeding,” 11 U.S.C. § 101(36). See In Re Cruz, 75 B.R. 56 (Bankr. D.P.R. 1987). “The Code thus contemplates that liens created consensually (such as mortgage liens or UCC security interests) or by judicial action (such as judgment liens, attachments, equitable liens or levies) are not “statutory liens,” while liens that come into being as a result of statutory operation, without consent or judicial action, are “statutory liens.” Klein v. Civalo & Trovato (In re Lionel Corp.), 29 F.3d 88, 94, (2d Cir. 1994). Statutory liens are recognized in bankruptcy subject to the trustee's avoidance powers under Section 545. In re Figueroa, 1985 Bankr. LEXIS 6901 (Bankr. D.P.R. 1985).

“A statutory lien is limited and quantified; if certain events or circumstances occur as articulated in the statute, a lien arises that is statutory in nature and unavoidable.” In re Leaks, 552 B.R. 741, 747 (Bankr. E.D. Ark. 2016). See *a/so* Braxton v. Bureau of Unemployment Compensation Benefits & Allowances (In re Braxton), 224 B.R. 564 (Bankr. W.D. Pa. 1998).

The United States Court of Appeals for the First Circuit recently discussed statutory liens and described its principal characteristics in the bankruptcy setting:

“Under the Code, a statutory lien “aris[es] solely by force of a statute on specified circumstances or conditions.” 11 U.S.C. § 101(53) (emphasis added). In other words, a statute can create a lien outright or it can establish that a lien will attach automatically upon an identified triggering event other than an agreement to grant the lien. See S. Rep. No. 95-989, at 27 (1978) (“A statutory lien is ... one that arises automatically, and is not based on an agreement to give a lien or on

judicial action.”); see also Klein v. Civale & Trovato, Inc. (In re Lionel Corp.), 29 F.3d 88, 94 (2d Cir. 1994) (characterizing statutory liens as “liens that come into being as a result of statutory operation, without consent or \*855 judicial action”). Take two examples: contractors' liens and tax liens. See 2 Collier, *supra*, ¶ 101.53 (identifying contractors' liens and tax liens as “[g]ood examples of statutory liens”); see also S. Rep. No. 95-989, at 27 (same). Contractors' liens, also known as mechanics' liens, “are creatures of statute,” in that they “arise and are created by force of statute.” 53 Am. Jur. 2d Mechanics' Liens § 3. Every state has a mechanics' lien law. *Id.* § 6. While these laws vary considerably across jurisdictions, *id.* § 8, and often require certain procedures for recording and enforcing the lien, the general concept is that when an individual supplies labor, materials, or services to improve the property of another, his claim for payment becomes a lien on the owner's property. *Id.* § 12; see also *id.* § 1. Once a worker furnishes labor or materials, a statutory lien often arises automatically without any further action. See *id.* § 1. The same is true of a tax lien in favor of the federal government. See 26 U.S.C. § 6321 (establishing that when an individual liable for taxes “neglects or refuses to pay the same after demand, the amount ... shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person”). For both mechanics' liens and tax liens, the relevant statute specifies a circumstance or condition (the furnishing of labor or the refusal to pay taxes after demand) and provides (often through the use of mandatory “shall” language) that when the specified circumstance or condition is satisfied, the lien attaches. Fin. Oversight

& Mgmt. Bd. v. Fin. Oversight & Mgmt. Bd. (In re Fin. Oversight & Mgmt. Bd.),  
899 F.3d 1, 11-12 (1st Cir. 2018).

“A lien created by statute is limited in operation and extent by the terms of the statute and can arise and be enforced only in the event and under the facts provided for in the statute.” Fonseca v. Gov’t Emples. Ass’n (AEELA), 542 B.R. 628, 634 (1st Cir. BAP 2015) *citing* Fleet Credit Corp. v. TML Bus Sales, Inc., 65 F.3d 119 (9th Cir. 1995).

*Statutory Lien Avoidable if not perfected.*

Section 545(2) grants the trustee power to avoid the fixing of a certain statutory liens:

The trustee may avoid the fixing of a statutory lien on property of the debtor to the extent that such lien—

....

(2) is not perfected or enforceable at the time of the commencement of the case against a bona fide purchaser that purchases such property at the time of the commencement of the case, whether or not such a purchaser exists.

In re Sheldahl, Inc., 298 B.R. 874, 876 (Bankr. D. Minn. 2003)

## PERFECTION

Statutory Liens may be perfected by filing a UCC-1 in states which have adopted the most current version of Article 9.

### *UCC-1 PERFECTION*

**General Rule.** Article 9 uses the term “attach” to describe the point at which property becomes subject to a security interest. The requisites for attachment are stated in Section 9-203. When it attaches, a security interest may be either perfected or unperfected. “Perfected” means that the security interest has attached and the secured party has taken all the steps required by this Article as specified in Sections 9-310 through 9-316. A perfected security interest may still be or become subordinate to other interests. See, e.g., Sections 9-320, 9-322. However, in general,

after perfection the secured party is protected against creditors and transferees of the debtor and, in particular, against any representative of creditors in insolvency proceedings instituted by or against the debtor. See, e.g., Section 9-317.

### **UCC Article 9 State Statutes that don't file UCC-1s.**

<u>UCC Not Applicable</u>	<u>UCC-1 States</u>
Alabama	
Alaska	
Arizona	
Arkansas	
California	
Colorado	
Connecticut	
	Delaware
Florida	
Georgia	
Hawaii	
	Idaho
Illinois	
Indiana	
Iowa	
Kansas	
Kentucky	
	Louisiana
	Maine
	Maryland
	Massachusetts
Michigan	
	Minnesota
Mississippi	
Missouri	
Montana	
	Nebraska
Nevada	
	New Hampshire
New Jersey	
New Mexico	
	New York
North Carolina	
North Dakota	
Ohio	

	Oklahoma
	Oregon
	Pennsylvania
	Rhode Island
South Carolina	
South Dakota	
	Tennessee
	Texas
	Utah
Vermont	
Virginia	
Washington	
West Virginia	
	Wisconsin

“This article does not apply to the extent that:”

**Alabama.** (14) to a security interest created in connection with any of its securities by this State, any municipal corporation, county, public authority, public corporation or other similar public or governmental agency or unit in this State, or any political subdivision of any thereof, or by any educational institution or educational corporation organized under the laws of this State, whether such institution or corporation is public or private. Ala. Code § 7-9A-109

**Alaska.** (14) notwithstanding (c)(2) of this section, a transfer by a government or governmental subdivision or agency. Alaska Stat. Ann. § 45.29.109 (West)

**Arizona.** 14. A transfer, pledge, assignment, grant or similar action by this state, another state or a governmental unit of this state or another state; Ariz. Rev. Stat. Ann. § 47-9109

**Arkansas.** (14) a transfer by a government or governmental unit. Ark. Code Ann. § 4-9-109 (West)

**California.** (17) A transfer by a government or governmental unit. Cal. Com. Code § 9109 (West)

**Colorado.** (e) The creation, perfection, priority, and enforcement of a security interest, lien, or pledge created by this state or a governmental unit of this state shall be governed by section 11-57-208(2), C.R.S., and this article shall not apply to such a security interest, lien, or pledge regardless of whether, pursuant to section 11-57-204(1), C.R.S., the state or such governmental unit elected to apply part 2 of article 57 of title 11, C.R.S., to such a security interest, lien, or pledge. Colo. Rev. Stat. Ann. § 4-9-109 (West)

**Connecticut.** (14) A pledge or other lien by this state or a government subdivision or agency of this state in existence on or after October 1, 2003, in connection with a bond or note issue of this state or of a government subdivision or agency of this state, which pledge or other lien is governed by a statute of this state that (A) provides for the creation of a pledge or other lien by this state or a government subdivision or agency of this state in connection with any bond or note issued by this state or a government subdivision or agency of this state, and (B) expressly states

that such pledge or lien shall be valid and binding as against other parties; Conn. Gen. Stat. Ann. § 42a-9-109 (West)

**Florida.** (n) Any transfer by a government or governmental unit; Fla. Stat. Ann. § 679.1091 (West)

**Georgia.** (16) A security interest created by or affecting property of this state or any governmental unit of this state in any public finance transaction, other than a security interest created by: (A) An authority activated under Chapter 62 of Title 36, the “Development Authorities Law”; or (B) A local authority having as its principal function the stimulation of industrial growth and the reduction of unemployment. Ga. Code Ann. § 11-9-109 (West)

**Hawaii.** (14) A transfer by a governmental unit; Haw. Rev. Stat. Ann. § 490:9-109 (West)

**Illinois.** (13) a transfer by a government or governmental subdivision or agency; 810 Ill. Comp. Stat. Ann. 5/9-109

**Indiana.** (14) the creation, perfection, priority, or enforcement of a security interest created by the state, another state, or a foreign country, or a governmental unit of the state, another state or a foreign country; Ind. Code Ann. § 26-1-9.1-109 (West)

**Iowa.** n. a transfer, other than a transfer pursuant to chapter 419, by this state or a governmental unit within this state in connection with a public-finance transaction or a transaction that would be a public-finance transaction but for failure to meet the criterion set forth in section 554.9102, subsection 1, paragraph “bo”, subparagraph (2); Iowa Code Ann. § 554.9109 (West)

**Kansas.** (15) a transfer by a government or governmental agency or subdivision; Kan. Stat. Ann. § 84-9-109 (West)

**Kentucky.** (q) A public-finance transaction or a transfer by a government or governmental unit. Ky. Rev. Stat. Ann. § 355.9-109 (West)

**Michigan.** (m) A transfer by a governmental unit or governmental subdivision or agency. Mich. Comp. Laws Ann. § 440.9109 (West)

**Mississippi.** (13) To a transfer by this state or a governmental unit of this state. Miss. Code. Ann. § 75-9-109 (West)

**Missouri.** (16) A transfer by a government or governmental subdivision or agency; Mo. Ann. Stat. § 400.9-109 (West)

**Montana.** (m) a transfer by a government or governmental subdivision or agency; Mont. Code Ann. § 30-9A-109 (West)

**North Carolina.** (14) The creation, perfection, priority, or enforcement of any lien on, assignment of, pledge of, or security in, any revenues, rights, funds, or other tangible or intangible assets created, made, or granted by this State or a governmental unit in this State, including the assignment of rights as secured party in security interests granted by any party subject to the provisions of this Article to this State or a governmental unit in this State, to secure, directly or indirectly, any bond, note, other evidence of indebtedness, or other payment obligations for borrowed money issued by, or in connection with, installment or lease purchase

financings by, this State or a governmental unit in this State. However, notwithstanding this subdivision, this Article does apply to the creation, perfection, priority, and enforcement of security interests created by this State or a governmental unit in this State in equipment or fixtures; N.C. Gen. Stat. Ann. § 25-9-109

**Navaho Nation.** E. To a transfer by a government or governmental subdivision, official or agency except to the extent that such entity has made an effective waiver of its sovereign immunity in accordance with 7 N.N.C. § 621 et seq. § 9-104. Transactions excluded from Article, 5A NAVAJO CODE § 9-104.

**Nevada.** (n) A transfer by a government or governmental unit. Nev. Rev. Stat. Ann. § 104.9109 (West)

**New Jersey.** (14) a transfer by a government or governmental unit. N.J. Stat. Ann. § 12A:9-109 (West)

**New Mexico.** (14) a public-finance transaction or other transfer by a state or a governmental unit of a state. N.M. Stat. Ann. § 55-9-109 (West)

**North Dakota.** m. A transfer by this state or a governmental unit of this state. N.D. Cent. Code Ann. § 41-09-09 (West)

**Ohio** (14) A transfer by a government, state, or governmental unit. Ohio Rev. Code Ann. § 1309.109 (West)

**South Carolina** (14) a transfer by a government or governmental unit. S.C. Code Ann. § 36-9-109

**South Dakota** (13) A transfer or security interest made or created by a state or any governmental unit; S.D. Codified Laws § 57A-9-109

**Vermont.** (14) a transfer by this State or a subdivision, agency, department, county, municipality, or other unit of the government of this State; Vt. Stat. Ann. tit. 9A, § 9-109 (West)

**Virginia.** (e) Except as provided below, the creation, perfection, priority and enforcement of a security interest, lien or pledge created, made or granted by the Commonwealth or a governmental unit of the Commonwealth to pay or secure any bonds, notes, obligations or other debt securities issued thereby shall be governed by § 2.2-4902.1 and this title shall not apply to such a security interest, lien or pledge. Security interests, liens or pledges created by the Commonwealth or a governmental unit of this Commonwealth in goods or software, or the proceeds thereof, shall be governed by this title. Va. Code Ann. § 8.9A-109 (West)

**Washington.** (14) A transfer by this state or a governmental unit of this state; Wash. Rev. Code Ann. § 62A.9A-109 (West)

**West Virginia.** (14) A transfer by a government or a governmental unit; W. Va. Code Ann. § 46-9-109 (West)

**Wyoming.** (xiv) Notwithstanding paragraph (c)(ii) of this section, a transfer by this state or governmental unit of this state. Wyo. Stat. Ann. § 34.1-9-109 (West)

Where to perfect will depend on your state's UCC code. The new Uniform Commercial Code applies to State and local governments. The old UCC Code specifically

(c) [Extent to which article does not apply.] This article does not apply to the extent that:

(1) a statute, regulation, or treaty of the United States preempts this article;

(2) another statute of this State expressly governs the creation, perfection, priority, or enforcement of a security interest created by this State or a governmental unit of this State;

(3) a statute of another State, a foreign country, or a governmental unit of another State or a foreign country, other than a statute generally applicable to security interests, expressly governs creation, perfection, priority, or enforcement of a security interest created by the State, country, or governmental unit;

**Governmental Debtors.** Former Section 9-104(e) excluded transfers by governmental debtors.

It has been revised and replaced by the exclusions in new paragraphs (2) and (3) of subsection (c). These paragraphs reflect the view that Article 9 should apply to security interests created by a State, foreign country, or a “governmental unit” (defined in [Section 9-102](#)) of either except to the extent that another statute governs the issue in question. Under paragraph (2), this Article defers to all statutes of the forum State. (A forum cannot determine whether it should consult the choice-of-law rules in the forum's UCC unless it first determines that its UCC applies to the transaction before it.) Paragraph (3) defers to statutes of another State or a foreign country only to the extent that those statutes contain rules applicable specifically to security interests created by the governmental unit in question.

If a transaction does not bear an appropriate relation to the forum State, then that State's Article 9 will not apply, regardless of whether the transaction would be excluded by paragraph (3).

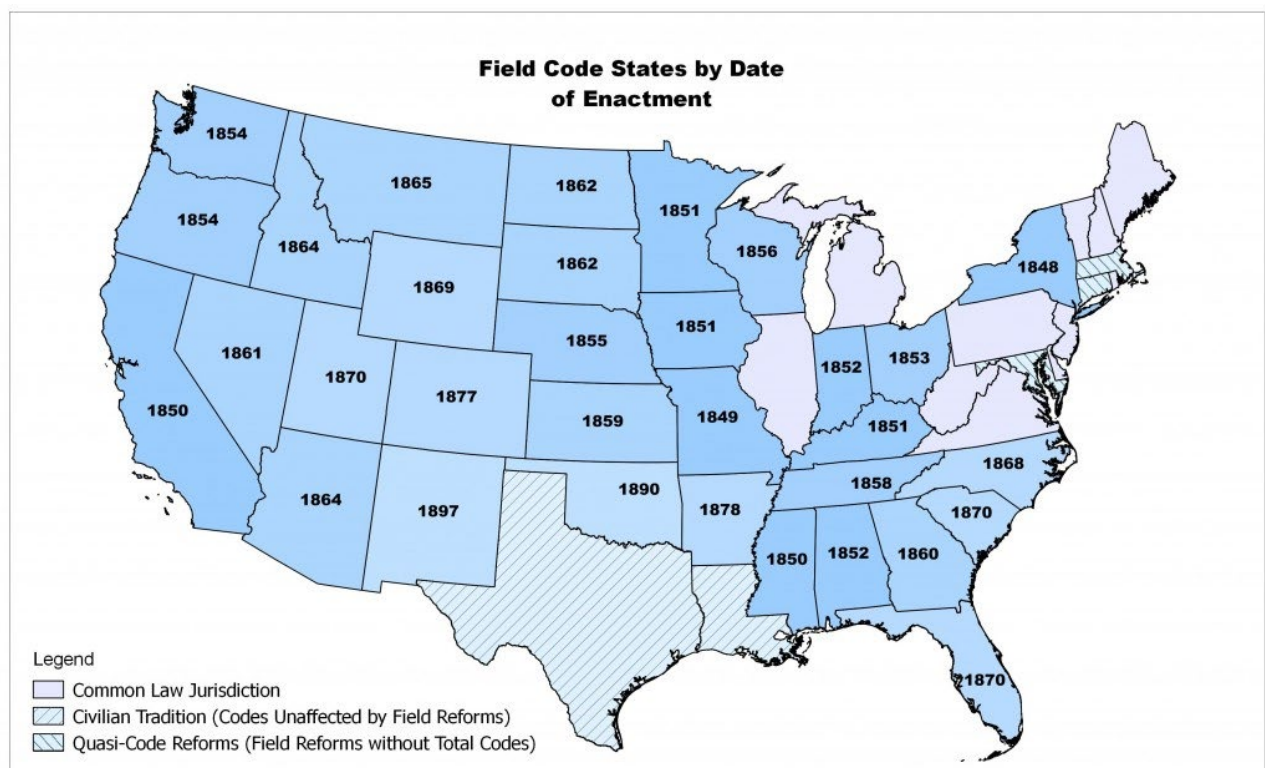
**Example 4:** A Belgian governmental unit grants a security interest in its equipment to a Swiss secured party. The equipment is located in Belgium. A dispute arises and, for some reason, an action is brought in a New Mexico state court. Inasmuch as the transaction bears no “appropriate

relation” to New Mexico, New Mexico’s UCC, including its Article 9, is inapplicable. See [Section 1-105\(1\)](#). New Mexico’s [Section 9-109\(c\)](#) on excluded transactions should not come into play. Even if the parties agreed that New Mexico law would govern, the parties’ agreement would not be effective because the transaction does not bear a “reasonable relation” to New Mexico. See [Section 1-105\(1\)](#).

Conversely, Article 9 will come into play only if the litigation arises in a UCC jurisdiction or if a foreign choice-of-law rule leads a foreign court to apply the law of a UCC jurisdiction. For example, if issues concerning a security interest granted by a foreign airline to a New York bank are litigated overseas, the court may be bound to apply the law of the debtor’s jurisdiction and not New York’s Article 9.

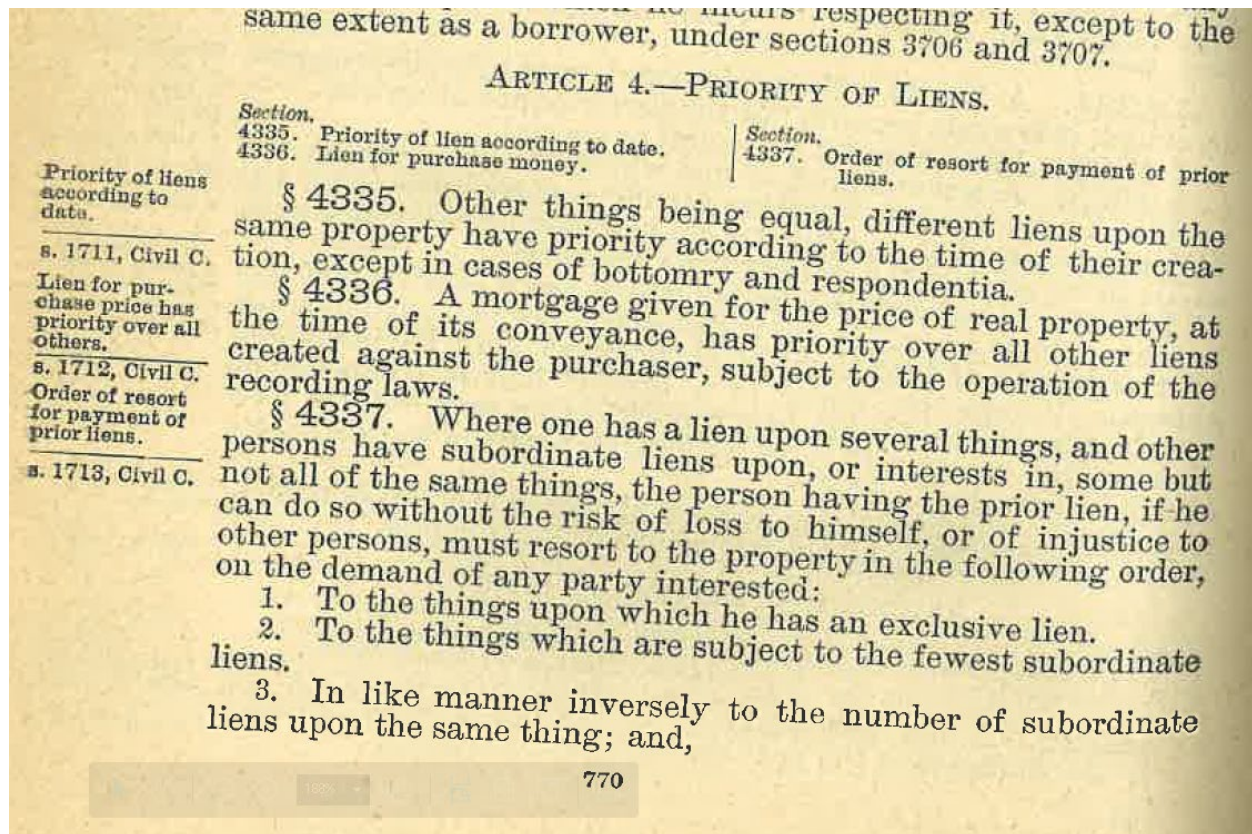
### PERFECTION THE OLD WAY - THE FIELD CODE

States adopted the civil procedure portion of the field code starting with New York in 1848 and California in 1850. However, the Civil, political, criminal, criminal procedure code were first adopted by Dakota Territory (South Dakota and North Dakota) in 1865 and California adopted a Modified Field Code in 1872.



## Field Code State Statutes

Here is an excerpt from the 1887 Dakota Territory Field Code, note §4336.



? **bottomry** (17c) Maritime law. A contract by which a shipowner pledges the ship as security for a loan to finance a voyage (as to equip or repair the ship), the lender losing the money if the ship is lost during the voyage. • The term refers to the idea that the shipowner pledges the ship's bottom, or keel. Cf.

? **respondentia** (ree-spon-den-shee-ə or res-pon-) [Law Latin fr. Latin respondere “to answer”] (17c) A loan secured by the cargo on one's ship rather than the ship itself.

### *North Dakota 35-03-10. Mortgage for purchase price of real property prior to all liens.*

A mortgage given for the purchase price of real property at the time of its conveyance has priority over all other liens created against the purchaser, subject to the operation of the recording laws.

### *Oklahoma Title 42-1*

#### § 16. Priority of mortgage for price of realty

A mortgage given for the price of real property, at the time of its conveyance, has priority over all other liens created against the purchaser, subject to the operation of the recording laws.

***Montana 71-3-114. Priority of purchase money mortgage***

Except as otherwise provided by law, a mortgage given for the price of real property at the time of its conveyance has priority over all other liens created against the purchaser, subject to the operation of the recording laws.

South Dakota 44-2

***South Dakota 44-2-2. Purchase price of real property--Mortgage given for at time of conveyance--Vendor's lien--Priority over other liens--Operation of recording laws***

A mortgage given for the price of real property at the time of its conveyance and the vendor's lien for unpaid purchase price of real property have priority over all other liens created against the purchaser subject to the operation of the recording law.

***Idaho § 45-112. Priority of purchase money mortgage***

A mortgage given for the price of real property, at the time of its conveyance, has priority over all other liens created against the purchaser, subject to the operation of the recording laws.

***Cal. Civ. Code § 2898***

(a) A mortgage or deed of trust given for the price of real property, at the time of its conveyance, has priority over all other liens created against the purchaser, subject to the operation of the recording laws.

(b) The priority of the lien of a mortgage or deed of trust on an estate for years in real property shall be determined in the same manner as for determining the priority of a lien of a mortgage or deed of trust on real property.

***State Recording Requirements.***

States have specific recording requirements.

***Alabama Code § 11-49A-12 Statutory mortgage lien; creation; filing of notice.***

Any resolution of the board or trust indenture under which bonds may be issued pursuant to the provisions of this chapter may contain provisions creating a statutory mortgage lien, in favor of the holders of such bonds and of the interest coupons applicable thereto, on the transit systems, or any thereof (including any after-acquired property) out of the revenues from which such bonds are made payable. The said resolution of the board or the said trust indenture may provide for the filing for record in the office of the judge of probate of each county in which any part of such transit system, or any thereof, may be located of a notice containing a brief description of such systems, a brief description of such bonds, and a declaration that said statutory mortgage lien has been created for the benefit of the holders of such bonds and the interest coupons applicable thereto, upon such systems, including any additions thereto and extensions thereof. Each judge of probate shall receive, record and index any such notice filed for record in his office. The recording of such notice, as herein provided, shall operate as constructive notice of the contents thereof.

§ 11-81-178. Statutory mortgage lien of bondholders -- Creation generally; filing, recordation, etc., of notice thereof.

(a) In the authorizing proceedings or in the trust indenture, if any, under which bonds may be issued pursuant to the provisions of this article, there shall be created a statutory mortgage lien in favor of the holders of such bonds and of the interest coupons applicable thereto on each system or systems (including any additions thereto and extensions thereof that may be thereafter made) out of the revenues from which such bonds are made payable.

(b) The authorizing proceedings or such trust indenture may provide for the filing for record in the office of the judge of probate of each county in which any part of such system or systems may be located of a notice containing a brief description of such system or systems, a brief description of such bonds and a declaration that said statutory mortgage lien has been created for the benefit of the holders of such bonds and the interest coupons applicable thereto upon such system or systems, including any additions thereto and extensions thereof. Each judge of probate shall receive, record and index any such notice filed for record in his office. The recording of such notice as provided in this subsection shall operate as constructive notice of the contents thereof.

*§ 35-01-09. Recorder to file and index lien*

The recorder shall file and index a statutory lien upon personal property required by law to be filed in the recorder's office, designating the person filing the lien as lien creditor and the person against whom the lien is filed as debtor.

*65 Ill. Comp. Stat. Ann. 5/8-13-11*

5/8-13-11. Liens for obligations

§ 8-13-11. Liens for obligations.

(a) As used in this Section, "statutory lien" has the meaning given to that term under 11 U.S.C. 101(53) of the federal Bankruptcy Code.

(b) Obligations issued by an issuing entity shall be secured by a statutory lien on the transferred receipts received, or entitled to be received, by the issuing entity that are designated as pledged for such obligations. The statutory lien shall automatically attach from the time the obligations are issued without further action or authorization by the issuing entity or any other entity, person, governmental authority, or officer. The statutory lien shall be valid and binding from the time the obligations are executed and delivered without any physical delivery thereof or further act required, and shall be a first priority lien unless the obligations, or documents authorizing the obligations or providing a source of payment or security for those obligations, shall otherwise provide.

The transferred receipts received or entitled to be received shall be immediately subject to the statutory lien from the time the obligations are issued, and the statutory lien shall automatically attach to the transferred receipts (whether received or entitled to be received by the issuing entity) and be effective, binding, and enforceable against the issuing entity, the transferring unit, the State entity, the State of Illinois, and their agents, successors, and transferees, and creditors, and all others asserting rights therein or having claims of any kind in tort, contract, or otherwise,

irrespective of whether those parties have notice of the lien and without the need for any physical delivery, recordation, filing, or further act.

The statutory lien imposed by this Section is automatically released and discharged with respect to amounts of transferred receipts reconveyed to the transferring unit pursuant to Section 8-13-10 of this Code, effective upon such reconveyance.

(c) The statutory lien provided in this Section is separate from and shall not affect any special revenues lien or other protection afforded to special revenue obligations under the federal Bankruptcy Code.

## STATE LAW POWER TO FILE FOR BANKRUPTCY

### *Michigan Chapter 9*

141.1566. Power of local government to file chapter 9 bankruptcy; resolution; contents; approval by governor; contingencies; selection of other local options

Sec. 26. (1) With the written approval of the governor, a local government may file a petition under chapter 9 and exercise powers pursuant to federal bankruptcy law if the local government adopts a resolution, by a majority vote of the governing body of the local government, that declares a financial emergency in the local government. Except as otherwise provided in this subsection, if the local government has a strong mayor, the resolution requires strong mayor approval. The resolution shall include a statement determining that the financial condition of the local government jeopardizes the health, safety, and welfare of the residents who reside within the local government or service area of the local government absent the protections of chapter 9 and that the local government is or will be unable to pay its obligations within 60 days following the adoption of the resolution.

(2) If the governor approves a local government to proceed under chapter 9, the governor shall inform the local government in writing of the decision. The governor may place contingencies on a local government in order to proceed under chapter 9 including, but not limited to, appointing a person to act exclusively on behalf of the local government in the chapter 9 bankruptcy proceedings. If the governor does not appoint a person to act exclusively on behalf of the local government in chapter 9 bankruptcy proceedings, the chief administrative officer of the local government shall act exclusively on behalf of the local government in chapter 9 bankruptcy proceedings. Upon receipt of the written approval and subject to this subsection, the local government may proceed under chapter 9 and exercise powers under federal bankruptcy law.

(3) If the governor does not approve a local government to proceed under chapter 9, the local government shall within 7 days select 1 of the other local options as provided in section 7.1.

***Mich. Comp. Laws Ann. § 141.1566 (West)***

### *Nebraska Chapter 9*

13-402. Political subdivisions, state agency; authorized to file petition in United States Bankruptcy Court; limitation; governing body; duties

(1) Any county, city, village, school district, agency of the state government, drainage district, sanitary and improvement district, or other political subdivision of the State of Nebraska is hereby permitted, authorized, and given the power to file a petition in the United States Bankruptcy Court under 11 U.S.C. chapter 9 and any acts amendatory thereto and supplementary thereof and to incur and pay the expenses incident to the consummation of a plan of adjustment of debts as contemplated by such petition.

(2)(a) The authority and power to file a petition provided for in subsection (1) of this section shall not apply to any city or village that, at the time of its governing body authorizing the filing of such petition, has its defined benefit retirement plan, if any, with a funded ratio of the actuarial value of assets less than fifty-one and sixty-five hundredths percent for any such petition to be

filed during the period between January 1, 2020, and January 1, 2023; fifty-four and forty-one hundredths percent for any such petition to be filed during the period between January 1, 2023, and January 1, 2026; fifty-eight and twenty-one hundredths percent for any such petition to be filed during the period between January 1, 2026, and January 1, 2029; sixty-three and forty-one hundredths percent for any such petition to be filed during the period between January 1, 2029, and January 1, 2032; seventy and seventy-one hundredths percent for any such petition to be filed during the period between January 1, 2032, and January 1, 2035; eighty and sixty-one hundredths percent for any such petition to be filed during the period between January 1, 2035, and January 1, 2038; and ninety percent thereafter.

(b) Within ninety days prior to taking action authorizing the filing of such petition, the governing body of any city or village that has a defined benefit retirement plan shall conduct an actuarial valuation to determine the funded ratio of such defined benefit retirement plan. Such determination shall be prima facie evidence in establishing the authority of the city or village to exercise authority under this section.

(c)(i) A city or village that does not have a defined benefit retirement plan may by ordinance declare and affirm that its general obligation bonds, whether existing before, after, or at the time of such ordinance, shall, unless otherwise provided in the related authorizing measure, be equally and ratably secured by a statutory lien on all ad valorem taxes levied and to be levied from year to year by such city or village and on all proceeds derived therefrom. The statutory lien authorized hereunder shall be deemed to attach and be continuously perfected from the time the bonds are issued without further action or authorization by the city or village. The statutory lien is valid and binding from the time the bonds are issued without any physical delivery thereof or further act required. No filing need be made under the Uniform Commercial Code or otherwise to perfect the statutory lien on any ad valorem taxes or proceeds derived therefrom in favor of any general obligation bonds. Bonds so secured shall have a first priority lien on such ad valorem taxes so levied and on all proceeds derived therefrom and shall have priority against all parties having claims of contract or tort or otherwise against the city or village, whether or not the parties have notice thereof. The absence of such declaration or affirmation shall not reduce or degrade the priority or secured status of such bonds otherwise existing under law.

(ii) For purposes of this subdivision, statutory lien shall have the meaning given to that term under 11 U.S.C. 101(53) of the federal Bankruptcy Reform Act of 1994, as it existed on August 24, 2017.

(d) An actuary performing actuarial valuations pursuant to this subsection shall be a member of the American Academy of Actuaries and shall meet the academy's qualification standards to render a statement of actuarial opinion. *Neb. Rev. Stat. Ann. § 13-402 (West)*

## REQUIREMENTS FOR FILING CHAPTER 9

“[Section 109\(c\) of the Bankruptcy Code](#) sets forth the statutory criteria for eligibility as a chapter 9 debtor.”). The statute requires that a chapter 9 debtor must:

- (1) be a municipality;
- (2) be “specifically authorized, in its capacity as a municipality or by name, to be a debtor under such chapter by State law, or by a governmental officer or organization empowered by State law to authorize such entity to be a debtor under such chapter”;
- (3) be insolvent;
- (4) “desire[ ] to effect a plan to adjust such debts; and”
- (5) have
  - A. “obtained the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair \*264 under a plan in a case under such chapter;
  - B. has negotiated in good faith with creditors and has failed to obtain the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter;
  - C. is unable to negotiate with creditors because such negotiation is impracticable; or
  - D. reasonably believes that a creditor may attempt to obtain a transfer that is avoidable under [section 547](#) of this title.”

## MUNICIPAL BANKRUPTCY

### *Definitions*

- (27) The term “governmental unit” means United States; State; Commonwealth; District; Territory; municipality; foreign state; department, agency, or instrumentality of the United States (but not a United States trustee while serving as a trustee in a case under this title), a State, a Commonwealth, a District, a Territory, a municipality, or a foreign state; or other foreign or domestic government.
- (31) The term “insider” includes--(D) if the debtor is a municipality, elected official of the debtor or relative of an elected official of the debtor;
- (13) The term “debtor” means person or municipality concerning which a case under this title has been commenced.
- 11 U.S.C.A. § 101 (West) (32) The term “insolvent” means-- ...
- (C) with reference to a municipality, financial condition such that the municipality is--

(i) generally not paying its debts as they become due unless such debts are the subject of a bona fide dispute; or

(ii) unable to pay its debts as they become due.

(37) The term “lien” means charge against or interest in property to secure payment of a debt or performance of an obligation.

(40) The term “municipality” means political subdivision or public agency or instrumentality of a State.

## APPENDIX

### 14 No. 11 Westlaw Journal Bankruptcy 2

Westlaw Journal Bankruptcy

\*1

October 5, 2017

#### Expert Analysis

By Laura Appleby, Esq., Michael Friedman, Esq., Jim Heiser, Esq., and Frank Top, Esq., Chapman and Cutler LLP<sup>aa1</sup>

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#### ***PUERTO RICO COURT RECOGNIZES LIMIT TO BANKRUPTCY CODE'S STATUTORY LIEN DEFINITION***

Laura Appleby, Michael Friedman, Jim Heiser and Frank Top of Chapman and Cutler LLP examine a Puerto Rico federal judge's recent decision permitting the island's Highways & Transportation Authority to continue to divert revenues pledged to bondholders.

Following a recent decision by the Court overseeing the Commonwealth of Puerto Rico's bankruptcy-like Title III proceeding, bondholders should continue to pay close attention to the pledge securing their bonds to determine how those bonds would be treated in a bankruptcy proceeding.

In the case of *Peaje Investments LLC v. Puerto Rico Highways & Transportation Authority*, the court denied a preliminary injunction sought by Peaje Investments LLC, the plaintiff, finding that because the lien did not arise from specific statutory language, it is unlikely that the bonds in question are secured by a statutory lien and, thus, the Puerto Rico Highways & Transportation Authority ("PRHTA") was permitted to continue to divert revenues pledged to bondholders for other uses.<sup>1</sup>

Readers are cautioned, however, that the Court has not issued a decision on the merits of the plaintiff's argument, but rather has determined that it is unlikely that the plaintiff would succeed on the merits of its claim.

Additionally, other parties-in-interest in the PRHTA proceeding have separately challenged the PRHTA's diversion of revenues.

The plaintiff has filed a notice of appeal to the U.S. Court of Appeals for the First Circuit.

#### ***Background***

The plaintiff in *Peaje* is the beneficial owner of approximately \$65 million of bonds issued pursuant to a 1968 resolution (the "1968 Resolution") authorizing the issuance of bonds (the "1968 Bonds") by the PRHTA.

Under the 1968 Resolution, the PRHTA covenanted to deposit certain revenues, including "Toll Revenues" with a fiscal agent on a monthly basis.

The 1968 Bonds, according to the 1968 Resolution, "are payable solely from Revenues and from any funds received by [the PRHTA] for that purpose from the Commonwealth which Revenues and funds are hereby pledged to the payment thereof in the manner and to the extent hereinabove particularly specified."<sup>2</sup>

In short, holders of the 1968 Bonds are secured by the gross toll revenues of the PRHTA.

In April 2016, the Commonwealth of Puerto Rico enacted a moratorium -- the Puerto Rico Emergency Moratorium and Financial Rehabilitation Act (the “Moratorium Act”) -- under which the Commonwealth suspended the obligations of the PRHTA to deposit revenues with a fiscal agent for the ultimate payment of holders of the 1968 Bonds.

**\*2** Rather than paying bondholders, the PRHTA was ostensibly permitted under the Moratorium Act to divert the pledged revenues for other purposes.

The PRHTA asserted that the revenues it retained were necessary to ensure that the PRHTA’s traffic facilities and other transportation infrastructure remained in good working order.<sup>3</sup>

The plaintiff brought its adversary proceeding challenging the moratorium and failure of the PRHTA to deposit the revenues subject to the pledge established in the 1968 Resolution with the fiscal agent.

With respect to the court’s recent decision that is the subject of this client alert, the plaintiff had sought a court order directing the PRHTA to resume depositing toll revenues with the fiscal agent due to the statutory lien that the plaintiff asserted was attached to those toll revenues.<sup>4</sup>

The court denied the plaintiff’s motion in its entirety, finding that the plaintiff had not demonstrated a likelihood of success on the merits of its argument that the bonds issued under the 1968 Resolution are secured by a statutory lien.

### ***Pledge of special revenues vs. statutory lien***

The plaintiff’s arguments relate to certain provisions of the U.S. Bankruptcy Code (the “Bankruptcy Code”) that were incorporated by Congress into the Puerto Rico Oversight, Management, and Economic Stability Act (“PROMESA”) pursuant to which the PRHTA’s Title III proceeding had been brought.<sup>5</sup>

Specifically, under the Bankruptcy Code, in a municipal bankruptcy (Chapter 9) proceeding, holders of bonds issued by a municipal debtor are entitled to special protections depending on the nature of the pledge securing those bonds.

Those holders may receive special protections if the underlying bonds are secured by a pledge of “special revenues” or a statutory lien.

[Section 902\(2\) of the Bankruptcy Code](#) enumerates five types of revenues that are “special revenues” under the Bankruptcy Code.

With respect to a pledge of special revenues, [Section 928\(a\) of the Bankruptcy Code](#) provides certain protections to the holders of such pledge in that special revenues acquired by a debtor after a bankruptcy petition has been filed remain subject to such pre-petition lien on special revenues.

However, under [Section 928\(b\)](#), any such lien on special revenues derived from a project or system is subject to the “necessary operating expenses of the project or system.”

Finally, under section 922(d), the filing of a bankruptcy petition does not operate as a stay of the application of pledged special revenues to pay bonds secured by those revenues in a manner that is consistent with [Section 928](#).

A municipal bond may also be secured by a statutory lien, that is, a lien arising solely by force of statute on specific circumstances and conditions.<sup>6</sup>

A statutory lien is created where the force and effect of a state statute’s language creates a charge against or interest in specific property, such as a revenue stream. A consensual lien, alone, does not create a statutory lien, but the existence of a consensual lien does not automatically preclude a statutory lien finding.<sup>7</sup>

**\*3** Generally, a consensual lien on property acquired by the debtor before the case was filed does not attach to property that the debtor acquires after the case is filed.<sup>8</sup>

However, a statutory lien should remain unaltered as a result of a bankruptcy petition and although there could be some delay in payment to bondholders due to the automatic stay in bankruptcy, the lien and rights to the particular revenue stream should remain unaltered without deduction for “necessary operating expenses,” as would be the case for a pledge of special revenues.<sup>9</sup>

It was with these background facts and legal predicates that the plaintiff in *Peaje* brought its motion for a preliminary injunction.

### ***Decision***

In the *Peaje* opinion, the Court first looked at whether the plaintiff had made the initial showing that the 1968 Bonds were secured by a pledge of special revenues exempt from the automatic stay provisions of the Bankruptcy Code.<sup>10</sup>

The Court found that the defendants had not contested that the toll revenues in question were “pledged special revenues” and concluded that the plaintiff had demonstrated a likelihood of success on the merits with respect to the first part of its claim.<sup>11</sup>

The Court then reviewed whether the plaintiff had established a likelihood of success on the merits that the 1968 Bonds were secured by a statutory lien.

The plaintiff specifically asserted that the 1968 Bonds were secured by a statutory lien arising from Puerto Rico Act 74-1965 (the “HTA Enabling Act”), and the 1968 Resolution itself.

With respect to the HTA Enabling Act, the Court found that a “grant of authority to create liens does not make liens that [PRHTA] subsequently decided to create statutory in nature.”<sup>12</sup>

The court then determined that the plaintiff’s assertion that the 1968 Resolution created a statutory lien was not likely to succeed because the 1968 Resolution was not a statute.<sup>13</sup>

The court noted that the PRHTA was a corporation and instrumentality of the Commonwealth of Puerto Rico, and not a legislature.

For these reasons, the court found that there was little likelihood that the plaintiff would succeed on the merits of its claim that the 1968 Bonds were secured by a statutory lien, and denied its motion for a preliminary injunction.

### ***Conclusion***

The *Peaje* court’s decision is a helpful reminder to bondholders and municipal entities alike to closely examine the security provided for any bond issuance.

As noted above, there could be significant differences between a statutory lien, which provides bondholders with significant protections in the event of a bankruptcy proceeding and a pledge of special revenues which provides some protections but are subject to certain carveouts and deductions.

Any assertion of a statutory lien must be closely examined for “mandatory” language, and should flow from an actual statute, rather than a consensual agreement with the issuer.

\*4 As noted, the plaintiff has appealed the Court’s ruling to the U.S. Court of Appeals for the First Circuit.

### **Footnotes**

<sup>1</sup> *Opinion and Order Denying Motion for Preliminary Injunction and Motion for Relief from the Automatic Stay, Peaje*

*Investments LLC v. Puerto Rico Highways & Transportation Authority (In re the Financial Oversight and Management Board for Puerto Rico, as representative of the Commonwealth of Puerto Rico)* Case No. 17-151 (Dkt. No. 240) (Sept. 8, 2017) (the “Peaje Op.”).

<sup>2</sup> *Peaje Op.* at 6.

<sup>3</sup> *Id.*

<sup>4</sup> The Court’s order was on the Motion of the Plaintiff (A) for Temporary Restraining Order and Preliminary Injunction, and (B) for Relief from Stay or, Alternatively, Adequate Protection.

<sup>5</sup> Law 114-187.

<sup>6</sup> *Peaje Op.* at 11; [11 U.S.C. § 101\(53\)](#).

<sup>7</sup> For further information regarding statutory liens, see *Municipalities in Distress? How State and Investors Deal with Local Governmental Financial Emergencies*, 2d. 2016, published by Chapman and Cutler LLP.

<sup>8</sup> [11 U.S.C. 552\(a\)](#).

<sup>9</sup> The interplay between statutory liens and [Section 928\(b\) of the Bankruptcy Code](#) has never been analyzed by a court. However, the existence of a valid lien may create a constitutionally protected property interest under the Fifth Amendment that cannot be impaired without providing just compensation. *See, e.g., Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555 (1935). Thus, if a statutory lien existed, appropriating the revenues for payment of “necessary operating expenses” would likely not be permitted.

<sup>10</sup> *Peaje Op.* at 10.

<sup>11</sup> *Id.*

<sup>12</sup> *Id.* at 12-13.

<sup>13</sup> *Id.* at 13.

<sup>aa1</sup> **Laura Appleby** is a partner in **Chapman and Cutler LLP**’s bankruptcy and restructuring group in New York. She represents financial institutions, bondholders, hedge funds and other creditors in complex bankruptcy proceedings, out-of-court restructurings and distressed transactions involving for-profit and nonprofit entities, as well as municipalities. **Michael Friedman** is a partner and the co-practice group leader of the firm’s bankruptcy and restructuring group in New York. He focuses his practice on bankruptcy, financial restructurings and special situation transactions including the representation of investors and debt holders in bankruptcy proceedings, financial restructurings, event driven merger and acquisition transactions, and debt financings. As a partner in Chapman’s bankruptcy and restructuring group in Chicago, **Jim Heiser** helps clients find cost-effective solutions to complex bankruptcy, restructuring and litigation disputes. He regularly advises and represents corporate and municipal creditors, indenture trustees, agent banks, backup and master servicers, institutional investors, and equipment lessors in a variety of financings and related litigation disputes across a wide range of business sectors. **Frank Top** is a Chicago-based partner in the firm’s banking and financial services department and the co-practice group leader of the bankruptcy and restructuring group. He has experience working in the areas of bankruptcy, creditor rights, restructuring and litigation, and he has appeared in cases of national prominence. A version of this expert analysis appeared on the firm’s website Sept. 14. Republished with permission.

*In re Financial Oversight and Management Board for Puerto Rico, 899 F.3d 1 (2018)*

899 F.3d 1

United States Court of Appeals, First Circuit.

IN RE: The FINANCIAL OVERSIGHT  
AND MANAGEMENT BOARD FOR  
PUERTO RICO, as representative for [the  
Commonwealth of Puerto Rico](#); The  
Financial Oversight and Management  
Board for Puerto Rico, as representative  
for the Puerto Rico Highways &  
Transportation Authority, Debtors.  
Peaje Investments LLC, Plaintiff,  
Appellant,

v.

The Financial Oversight and  
Management Board for Puerto Rico, as  
representative for the Puerto Rico  
[Highways & Transportation Authority](#);  
Hon. Carlos Contreras–Aponte, in his  
official capacity as Executive Director of  
Puerto Rico [Highways & Transportation  
Authority](#); The Financial Oversight and  
Management Board for Puerto Rico, as  
representative for [the Commonwealth of  
Puerto Rico](#); Hon. Ricardo Rossello  
Nevarés, in his official capacity as  
Governor of [the Commonwealth of  
Puerto Rico](#); Hon. Raul Maldonado  
Gautier, in his official capacity as  
Secretary of Treasury of the  
Commonwealth of Puerto Rico; Hon.  
Jose Ivan Marrero Rosado, in his official  
capacity as Executive Director of the  
Office of Management & Budget; Puerto  
Rico Fiscal Agency and [Financial  
Advisory Authority](#); Hon. Gerardo Jose  
Portela Franco, in his official capacity as  
Executive Director of the Puerto Rico  
Fiscal Agency and [Financial Advisory  
Authority](#), Defendants, Appellees.

Nos. 17-2165, 17-2166, 17-2167

August 8, 2018

**Synopsis**

**Background:** In jointly administered debt adjustment

cases of the Commonwealth of Puerto Rico and the Puerto Rico Highways and Transportation Authority (HTA) under Title III of the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA), beneficial owner of approximately \$65 million in bonds issued by the HTA in 1968 brought adversary proceeding against the HTA and others in which it asserted certain “lien rights” in connection with the bonds. Arguing that it held statutory lien on the HTA’s toll revenues, owner moved for preliminary injunction enjoining the HTA from continuing to divert toll revenues from fiscal agent and sought relief from the automatic stay or, alternatively, adequate protection. Defendants moved, on waiver grounds, to strike from owner’s reply brief all assertions related to its alternative argument that it held non-statutory lien. The United States District Court for the District of Puerto Rico, [Laura Taylor Swain](#), J., sitting by designation, entered orders granting the motion to strike and, after evidentiary hearing, denying owner’s requests for injunctive and other relief, [301 F.Supp.3d 290](#). Owner appealed.

**Holdings:** The Court of Appeals, [Kayatta](#), Circuit Judge, held that:

the district court did not abuse its discretion in limiting owner to its argument that it held a statutory lien on certain toll revenues of the HTA;

the HTA’s Enabling Act, by itself, did not create a statutory lien on the toll revenues; and

the Enabling Act, together with the 1968 Resolution providing for the HTA’s issuance of bonds, did not create a statutory lien on the toll revenues.

Affirmed in part, vacated in part, and remanded.

See also [2018 WL 3751014](#).

**\*3** APPEALS FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF PUERTO RICO [Hon. [Laura Taylor Swain](#), U.S. District Judge]

**Attorneys and Law Firms**

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[Stephen L. Ratner](#), [Mark D. Harris](#), New York, NY, [Michael A. Firestein](#), [Lary A. Rappaport](#), Los Angeles, CA, [John E. Roberts](#), Proskauer Rose LLP, Hermann D. Bauer, and O'Neill & Borges LLC, San Juan, PR, were on brief, for appellees The Financial Oversight and Management Board for Puerto Rico, as representative of the Commonwealth of Puerto Rico and the Puerto Rico Highways and Transportation Authority.

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Raul Castellanos and Development & Construction Law Group LLC on brief for appellee Hon. Carlos Contreras Aponte.

Wanda Vázquez Garced, Secretary of Justice, Luis R. Román Negrón, Solicitor General of Puerto Rico, Department of Justice, on brief for appellees Hon. Ricardo Antonio Roselló Nevares, Hon. Raúl Maldonado Gautier, and Hon. José Iván Marrero Rosado.

Before [Howard](#), Chief Judge, [Kayatta](#), Circuit Judge, and Torresen, Chief U.S. District Judge.™

## Opinion

[KAYATTA](#), Circuit Judge.

\*4 We are asked for the second time to weigh in on Peaje Investments LLC's claim that what it characterizes as its "collateral" is being permanently impaired. Peaje is the beneficial owner of \$65 million of uninsured bonds issued by the Puerto Rico Highways and Transportation Authority ("Authority"). Peaje alleges that its bonds are secured by a lien on certain toll revenues of the Authority and that, in response to Puerto Rico's financial crisis, the Authority and the Commonwealth of Puerto Rico ("Commonwealth") are diverting funds to which Peaje believes it is entitled under the lien and using them for purposes other than paying the bonds. Because both the Authority and the Commonwealth have commenced bankruptcy cases under Title III of the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA"), [48 U.S.C. §§ 2101–2241](#), Peaje instituted the adversary proceedings now on consolidated appeal to challenge this diversion. Despite the novelty and complexity of the bankruptcies from which this case arose, three narrow rulings dispose of the appeal now before us: First, the district court did not abuse its discretion in limiting Peaje to its argument that it holds a statutory lien on certain toll revenues of the Authority. Second, Peaje does not hold such a lien. And third, we vacate the district court's alternative reasons for denying relief so that they may be reconsidered de novo on a comprehensive, updated record now that it is clear that Peaje has no statutory lien.

## I.

The Authority was formed in 1965 as a public corporation and instrumentality of the Commonwealth. Pursuant to its enabling act ("Act" or "Enabling Act"), it \*5 may borrow money, issue bonds, and secure those bonds with pledges of revenues. [P.R. Laws Ann. tit. 9 § 2004\(l\)](#). In 1968, the Authority adopted Resolution No. 68-18 (the "1968 Resolution" or the "Resolution"). See Puerto Rico Highway Authority, Resolution No. 68-18, available at [http://gdb.pr.gov/investors\\_resources/documents/FIRMD\\_M-12808969-v1-PRHTA1968Resolution.pdf](http://gdb.pr.gov/investors_resources/documents/FIRMD_M-12808969-v1-PRHTA1968Resolution.pdf). In order to provide additional funds for the construction of roads, bridges, and other facilities, the 1968 Resolution provided for the issuance of bonds. *Id.* Art. II, § 201.

The Resolution guaranteed that the Authority would "promptly pay the principal of and the interest on every bond issued," but that it would do so "solely from Revenues and from any funds received by the Authority for that purpose from the Commonwealth which Revenues and funds are hereby pledged to the payment thereof in the manner and to the extent" provided by the Resolution. *Id.* Art. VI, § 601. The Resolution established a special account called the "Sinking Fund," which itself contains three separate accounts: the Bond Service Account, the Redemption Account, and the Reserve Account. *Id.* Art. IV, § 401. The revenues (and any other pledged funds) deposited in these accounts were to be held in trust by the "Fiscal Agent," a bank or trust company appointed by the Authority, until, in the case of the Bond Service Account, they were applied to the principal and interest due on the bonds. *Id.* Art. IV, § 402. Pending the application of these funds, the Resolution provided that the money "shall be subject to a lien and charge in favor of the holders of the bonds ... and for the further security of such holders until paid out or transferred." *Id.* Art. IV, § 401. Peaje is the beneficial owner of various bonds issued pursuant to the 1968 Resolution, with maturity dates ranging from 2023 to 2036. Peaje's basic position is that it holds, as security for its bonds, a lien on toll revenues generated from three specific highways maintained by the Authority. It further contends that its lien extends not just to toll revenues currently held by the Fiscal Agent, but also to the Authority's toll revenues before they are deposited with the agent.<sup>1</sup>

In April 2016, in response to growing economic problems in Puerto Rico, the Commonwealth enacted the Puerto Rico Emergency Moratorium and Financial Rehabilitation Act, pursuant to which then-Governor Alejandro García-Padilla issued several executive orders that suspended the Authority's obligation to deposit toll revenues with the Fiscal Agent. Peaje contends that, as a result, the Authority and the Commonwealth began using the toll revenues for

purposes other than those allowed by the Resolution, including to pay operating expenses. In July 2016, Peaje filed suit in district court to challenge this diversion of funds. But Congress had just enacted PROMESA, instituting a temporary stay of all proceedings against the Commonwealth and its instrumentalities. See 48 U.S.C. § 2194(b). Peaje therefore requested relief from the temporary stay, pursuant to PROMESA section 405(e)(2), 48 U.S.C. § 2194(e)(2), patterned after section 362(d) of the bankruptcy code (“Code”), 11 U.S.C. § 362(d). The district court denied relief, Peaje Invs. LLC v. García-Padilla, Nos. 16-2384-FAB, 16-2696-FAB, 2016 WL 6562426, at \*6 (D.P.R. Nov. 2, 2016), and we affirmed in relevant part, Peaje Invs. LLC v. García-Padilla, 845 F.3d 505, 514, 516 (1st Cir. 2017) (Peaje I).

\*6 After PROMESA’s temporary stay expired, Peaje filed a second action in district court in May 2017 seeking similar relief. But soon afterward, the Authority, acting through the Financial Oversight and Management Board, filed a bankruptcy petition under Title III of PROMESA. (The Commonwealth had already filed its Title III petition.) This petition triggered an automatic stay (this time for the pendency of the bankruptcy case) of all actions against the Authority, including Peaje’s second suit. See 11 U.S.C. §§ 362(a), 922(a); see also 48 U.S.C. § 2161(a) (incorporating 11 U.S.C. §§ 362(a) and 922(a) into PROMESA).<sup>2</sup> Peaje then timely exercised its right to file an adversary proceeding seeking declaratory and injunctive relief in the jointly administered bankruptcy cases of the Authority and the Commonwealth.<sup>3</sup>

Specifically, Peaje asserted the following claims in two identical verified complaints, filed in the respective Title III cases of the Authority and the Commonwealth: (1) a declaration that the Authority’s toll revenues qualify as “pledged special revenues” under Code section 922(d); (2) adequate protection or, in the alternative, relief from the stay; (3) a declaration that Code section 922(d) preempts fiscal plan implementation; (4) a declaration that Code section 922(d) requires the Authority to deposit toll revenues with the Fiscal Agent; (5) a declaration that neither Code section 552 nor 928(b) apply to its bonds; (6) a declaration that to the extent Code section 928(b) applies to its bonds, netting out “necessary operating expenses” would constitute a taking in violation of the Constitution; (7) relief from the stay so that it can challenge, on constitutional grounds, the diversion of toll revenues; and (8) injunctive relief requiring the Authority to resume depositing the toll revenues with the Fiscal Agent.

Along with its complaints, Peaje filed a motion for a temporary restraining order (“TRO”) enjoining the Authority from continuing to divert the toll revenues.<sup>4</sup> The motion also sought relief from the automatic bankruptcy stay or, in the alternative, adequate protection. As we discuss more fully below, Peaje argued in its request for a TRO that it was entitled to relief because it holds a statutory lien on the Authority’s toll revenues. The district court, to

which we will hereinafter refer as the Title III court, held a preliminary hearing on Peaje’s motion and defendants then filed an opposition brief in which they challenged Peaje’s assertion of a statutory lien on the merits.<sup>5</sup>

After Peaje filed its Reply in the Title III court, defendants moved, on waiver \*7 grounds, to strike from that brief all assertions related to Peaje’s alternative argument that it holds a non-statutory lien. The Title III court, relying on Local Civil Rule 7(c), granted the motion to strike on the grounds that Peaje had failed to argue, prior to its Reply, that it holds a non-statutory lien. See P.R.L.Cv.R. 7(c) (a reply memorandum “shall be strictly confined to replying to new matters raised in the objection or opposing memorandum”); see also P.R. LBR 1001-1(b) (incorporating local rules of the District of Puerto Rico into the local bankruptcy rules). After an evidentiary hearing, the Title III court issued a second order denying both Peaje’s request for a preliminary injunction and its request for adequate protection or, alternatively, relief from the stay. See Peaje Invs. LLC v. P.R. Highways & Transp. Auth., 301 F.Supp.3d 290, 293 (D.P.R. 2017). Peaje appeals from both orders.

## II.

We turn first to the Title III court’s decision to grant defendants’ motion to strike. We have previously reviewed similar orders for abuse of discretion. See Amoah v. McKinney, 875 F.3d 60, 62 (1st Cir. 2017); Turner v. Hubbard Sys., Inc., 855 F.3d 10, 12 (1st Cir. 2017). Presented with no argument to the contrary, we assume that the same standard applies here.

Some statutory context is necessary to understand Peaje’s potential waiver. As we explain more fully in the next section of this opinion, the Code divides liens into three mutually exclusive categories, two of which are relevant here: statutory liens and security interests.<sup>6</sup> Two provisions of the Code, incorporated into PROMESA, see 48 U.S.C. § 2161(a), single out certain types of liens (specifically, security interests) for special treatment. First, Code section 552(a) establishes a general rule, subject to several exceptions not relevant here, see 11 U.S.C. § 552(b), that property acquired by the debtor after the commencement of the bankruptcy case “is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case.” 11 U.S.C. § 552(a); see also Assured Guar. Corp. v. Commonwealth of Puerto Rico (In re Fin. Oversight and Mgmt. Bd. of P.R.), 582 B.R. 579, 593 (D.P.R. 2018). Second, Code section 928(a) provides an exception to section 552(a)’s general rule for “special revenues acquired by the debtor after the commencement of the case.” 11 U.S.C. § 928(a). Such revenues “shall remain subject to any lien resulting from any security agreement entered into by the debtor before

the commencement of the case.” *Id.* Code [section 928\(b\)](#) allows debtors to offset “necessary operating expenses” from “[a]ny such lien on special revenues.” *Id.* § [928\(b\)](#). As the text of both provisions makes clear, the general rule of [section 552\(a\)](#) and its exception in [section 928\(a\)](#) apply only to a “lien resulting from [a] security agreement.”<sup>7</sup> *Id.* §§ [552\(a\)](#), [928\(a\)](#). Neither provision applies to statutory liens. See 5 *Collier on Bankruptcy* ¶ 552.01[2] (16th ed.); 6 *id.* ¶ 928.02[2]. Thus, Peaje’s rights in the Title III proceeding differ considerably depending on \*8 whether it possesses a statutory lien or a lien resulting from a security agreement (i.e., a security interest).

With this framework in mind, we find that the district court did not abuse its discretion in granting the motion to strike. We begin where these adversary proceedings began, with the filing of the verified complaints. In its complaints, Peaje alleged, among other things:

[T]he 1968 Bondholders’ lien results from both the Enabling Act that created HTA and the binding municipal resolution governing Plaintiff’s Bonds. Thus, that lien is a “statutory lien” within the meaning of [Section 101\(53\) of the Bankruptcy Code](#), [11 U.S.C. § 101\(53\)](#).

Peaje then went on to explicitly disclaim that Code [sections 928](#) and [552\(a\)](#) applied to its lien:

As a result, [Section 552 of the Bankruptcy Code](#) does not apply to Plaintiff’s Bonds, as the application of that provision is limited to “lien[s] resulting from any security agreement ...[.]” see [11 U.S.C. § 552\(a\)](#).... Nor does [Section 928\(b\) of the Bankruptcy Code](#) apply to those Bonds. That provision in some instances subordinates a bondholder’s lien on “special revenues” to the “necessary operating expenses” of the “project or system” that generates those revenues, but is also limited in application to “lien[s] resulting from any security agreement[.]”....

Later in its complaints, Peaje reaffirmed that its lien was “unaffected by [Section 928\(b\)](#) because that lien does not result from a security agreement within the meaning of that provision.” Peaje made similar statements regarding [section 552](#).

Next, in its application for a TRO, filed the same day as the verified complaints, Peaje again argued that its “lien on the Toll Revenues [was] unaffected by [Section 928\(b\)](#) because that lien does not result from a security agreement within the meaning of that provision.”

Then in the initial hearing on Peaje’s request for a TRO, held on June 5, 2017, Peaje’s attorney stated:

There is not a security interest here. There is not a voluntary security agreement like you would see under Article 9.... This is not a security agreement or security interest under Article 9. This is a lien that is established pursuant to a municipal ordinance.

So, in three separate contexts prior to filing its Reply, Peaje explicitly denied that it held a security interest.

And yet, as Peaje points out, the comments quoted above from the June 5 hearing were sandwiched between two statements suggesting a broader assertion of lien rights. First, Peaje stated: “We don’t say in our papers that we have a statutory lien or nothing. We say that we have a lien. We say that this lien arises from a municipal ordinance.” And later, it continued: “We say this is a lien, first and foremost.”

On the other hand, had Peaje been proceeding on the alternative theory that it should be granted relief to protect its interests secured by a security agreement rather than a statutory lien, one would have expected to see an explanation for how to accommodate the effects of Code [section 928\(b\)](#), including an analysis of what constituted necessary operating expenses. And while Peaje’s attorney asserted in the June 5 hearing that to the extent the Authority could surcharge its lien, it could do so only to a limited extent to account for the expenses necessary for generating the revenue stream, this argument was absent from Peaje’s actual filing. In its motion for a TRO, Peaje rested primarily on its position that Code [sections 552](#) and [928\(b\)](#) left its lien “unaffected” \*9 because it is a statutory lien. To the extent it offered any alternative argument, it argued only that the application of [section 928\(b\)](#) would be unconstitutional because it would convert Peaje’s gross lien into a net lien. The constitutional argument, whether correct or not, is hardly so self-evident as to have avoided any need to engage more seriously with the potential application of [section 928\(b\)](#) in order to advance the alternative argument that Peaje held a security interest. Peaje also did not explain why the sources that allegedly established its lien (the Enabling Act and the 1968 Resolution) supported the contention that Peaje’s lien should be categorized alternatively as a security interest. All of this puts Peaje’s claim of preservation on precarious grounds. Moreover, Peaje clearly understood how to adequately preserve an alternative argument, as evidenced by its very different approach on another issue: the application of the automatic stay to its claims, a question we need not reach today. In its motion for TRO, Peaje explicitly and repeatedly argued that the automatic stay did not apply to its case. But it also argued that, to the extent the stay did apply, it sought “out of an abundance of caution” relief from that stay.

Peaje argues that defendants conceded, both in this case and in related proceedings, that Peaje holds a lien of some type. There are, indeed, documents in the record, including bond offering statements from the Authority, reflecting that bonds issued under the 1968 Resolution are secured by a pledge of certain revenues of the Authority. But even assuming that defendants to some extent have conceded the existence of a lien, Peaje does not argue, nor could it, that defendants have conceded that Peaje holds a lien on the post-petition revenues it now seeks to obtain. *Cf.* [Peaje I](#),

[845 F.3d at 514](#) (“While Peaje may have had a contractual right to monthly deposits with the fiscal agent and the maintenance of the accounts at particular levels, its protected interest for purposes of the lift-stay motion was limited to its interest in repayment of the debt owed.”). Nor does Peaje contend that defendants conceded the existence of a particular type of lien, which, as noted, has important consequences for the issues in this case.

In sum, whether Peaje waived its non-statutory lien argument is admittedly a close call. One can easily see why the statements to which the Title III court pointed made it appear that Peaje was limiting itself to asserting a statutory lien. At the same time, however, the mutually exclusive nature of a security interest and a statutory lien under the Code invited Peaje’s counsel to characterize its lien as statutory (and thus by definition not a security interest), without intending to waive the logically alternative argument, which defendants’ prior statements in [Peaje I](#) had not made an obvious subject of dispute. See [Peaje I](#), [845 F.3d at 510](#) (observing without deciding that Peaje’s bonds are secured by a lien on toll revenues without specifying the nature of the lien).

Ultimately, what gives us confidence that the Title III court did not abuse its discretion in granting the motion to strike is the fact that any waiver here is not permanent, a point that the Title III court itself made. Moreover, even were we to rule in favor of Peaje on this issue, and thus consider the other issues on appeal based on the premise that Peaje holds a security interest, the most Peaje could realistically expect to gain is a remand to take a renewed shot at obtaining relief on a supplemented record that reflects where matters now stand. For the reasons we explain in Part IV of this opinion, that is exactly what Peaje gets.

**\*10** We therefore affirm the Title III court’s holding that, for purposes of the motion now on review, Peaje has limited itself to arguments predicated upon its claim that it holds a statutory lien on the Authority’s toll revenues.

### III.

We turn now to the pivotal issue that Peaje presented below and raises on appeal: Does it have a statutory lien on any property of the Authority? The district court resolved this issue in the context of analyzing Peaje’s request for a preliminary injunction, a ruling that we review overall for abuse of discretion. See [Waldron v. George Weston Bakeries Inc.](#), [570 F.3d 5, 8 \(1st Cir. 2009\)](#). But since the proper classification of Peaje’s purported lien is a legal question, we review it de novo. See [id.](#) (“Within that [abuse of discretion] framework, we scrutinize the district court’s ... handling of abstract legal questions de novo.”).

The Code defines a lien as a “charge against or interest in

property to secure payment of a debt or performance of an obligation.” [11 U.S.C. § 101\(37\)](#). It then divides liens into three mutually exclusive categories: judicial liens, statutory liens, and security interests. The Code defines a statutory lien as:

a lien arising solely by force of a statute on specified circumstances or conditions, or lien of distress for rent, whether or not statutory, but does not include security interest or judicial lien, whether or not such interest or lien is provided by or is dependent on a statute and whether or not such interest or lien is made fully effective by statute.

[Id. § 101\(53\)](#) (footnote omitted). [Collier on Bankruptcy](#) describes the “essence” of a statutory lien as “the need, or lack of need, for an agreement or judgment to create the lien.” 2 [Collier](#), [supra](#), ¶ 101.53. It goes on:

If the lien arises by force of statute, without any prior consent between the parties or judicial action, it will be deemed a statutory lien.... If the creation of the lien is dependent upon an agreement, it is a security interest even though there is a statute which may govern many aspects of the lien. The fact that a statute describes the characteristics and effects of a lien does not by itself make the lien a statutory lien.

[Id.](#)

Peaje argues that it holds a statutory lien by virtue of the Enabling Act. See [P.R. Laws Ann. tit. 9 §§ 2001–2035](#). It points to various provisions of the Act that it claims “provide[ ] for [its] lien on the circumstances and conditions identified in its provisions.” But none of the provisions Peaje cites supports this assertion. Under the Act:

[T]he Authority is hereby empowered to ... borrow money for any of its corporate purposes, and to issue bonds of the Authority in evidence of such indebtedness and to secure payment of bonds and interest thereon by pledge of, or other lien on, all or any of its properties, revenues or other income....

[P.R. Laws Ann. tit. 9 § 2004, \(l\)](#). The Act further specifies that “the Authority may from time to time issue and sell its own bonds,” [id.](#) § 2012(a), and that those bonds “may be authorized by resolution or resolutions of the Authority,” [id.](#) § 2012(b). As to the pledging of revenues, the Act provides:

Any resolution or resolutions authorizing any bonds may contain provisions, which shall be a part of the contract with the holders of the bonds:

(1) As to the disposition of the entire gross or net revenues and present or future income or other funds of the Authority, **\*11** including the pledging of all or any part thereof to secure payment of the principal of and interest on the bonds....

[Id.](#) § 2012(e). Finally, section 2015 of the Act provides that, with some limited exceptions, the bonds issued by the

Authority shall not be a debt of the Commonwealth, “nor shall such bonds or the interest thereon be payable out of any funds other than those pledged for the payment of such bonds and interest thereon pursuant to the provisions of [§ 2004\(l\)](#) of this title.” *Id.* § 2015.

As the Title III court found, these provisions permit the Authority to secure the payment of bonds by making a pledge of revenues, but they do not require that it do so. Even the language of section 2015 of the Act applies only to funds “pledged ... pursuant to ... [§ 2004\(l\)](#),” *id.* § 2015, and such pledges are voluntary. *See id.* § 2004(l) (the Authority is “empowered” to issue bonds and secure them with pledges of revenues); *see also id.* § 2012(e) (a resolution authorizing bonds “may contain provisions” pledging revenues (emphasis added) ). We therefore agree with the district court that “[n]o lien arises solely by force of [these] statutory provision[s].”

Peaje counters that a statutory lien need not be specified “exclusively and formally in some statutory text.” Rather, Peaje argues, the Code provides that a statutory lien can arise from specified circumstances or conditions and, in its view, these include “regulatory elaboration and agency action.” Peaje is correct about the definition but wrong about its application.

Under the Code, a statutory lien “aris[es] solely by force of a statute on specified circumstances or conditions.” [11 U.S.C. § 101\(53\)](#) (emphasis added). In other words, a statute can create a lien outright or it can establish that a lien will attach automatically upon an identified triggering event other than an agreement to grant the lien. *See S. Rep. No. 95-989, at 27* (1978) (“A statutory lien is ... one that arises automatically, and is not based on an agreement to give a lien or on judicial action.”); *see also Klein v. Civile & Trovato, Inc. (In re Lionel Corp.)*, 29 F.3d 88, 94 (2d Cir. 1994) (characterizing statutory liens as “liens that come into being as a result of statutory operation, without consent or judicial action”). Take two examples: contractors’ liens and tax liens. *See 2 Collier, supra*, ¶ 101.53 (identifying contractors’ liens and tax liens as “[g]ood examples of statutory liens”); *see also S. Rep. No. 95-989, at 27* (same). Contractors’ liens, also known as mechanics’ liens, “are creatures of statute,” in that they “arise and are created by force of statute.” [53 Am. Jur. 2d Mechanics’ Liens § 3](#). Every state has a mechanics’ lien law. *Id.* § 6. While these laws vary considerably across jurisdictions, *id.* § 8, and often require certain procedures for recording and enforcing the lien, the general concept is that when an individual supplies labor, materials, or services to improve the property of another, his claim for payment becomes a lien on the owner’s property. *Id.* § 12; *see also id.* § 1. Once a worker furnishes labor or materials, a statutory lien often arises automatically without any further action. *See id.* § 1. The same is true of a tax lien in favor of the federal government. *See 26 U.S.C. § 6321* (establishing that when an individual liable for taxes “neglects or refuses to pay the same after demand, the

amount ... shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person”). For both mechanics’ liens and tax liens, the relevant statute specifies a circumstance or condition (the furnishing of labor or the refusal to pay taxes after demand) and provides (often through the use of mandatory, \*12 “shall” language) that when the specified circumstance or condition is satisfied, the lien attaches.

The Enabling Act differs from these statutes in an important respect: A pledge of revenues does not attach automatically when the Authority passes a resolution issuing bonds. Rather, it arises only when the Authority chooses to grant it. Because the Act does not automatically trigger a lien upon the performance of a specified condition, apart from the Authority’s decision to grant a lien, it does not create a statutory lien.<sup>8</sup>

Perhaps aware that it faces an uphill battle, Peaje’s backup argument is that, even if the Enabling Act does not by itself create a statutory lien, the Act together with the 1968 Resolution does. Peaje is correct that the Resolution contains mandatory language suggestive of lien creation. *See* 1968 Resolution, Art. IV, § 401 (funds held by the Fiscal Agent “shall be subject to a lien and charge in favor of the holders of the bonds issued and outstanding under this Resolution and for the further security of such holders until paid out or transferred as herein provided”); *id.* Art. VI, § 601 (with some exceptions, “the principal, interest and premiums [of the bonds] are payable solely from Revenues and from any funds received by the Authority for that purpose from the Commonwealth which Revenues and funds are hereby pledged to the payment thereof”). But the Resolution poses a new problem for Peaje—to quote the Title III court, “the 1968 Resolution is not a statute.”

Peaje’s only response is to point to a case holding that a regulation adopted by a Commonwealth regulatory agency, the Department of Natural and Environmental Resources, had “the same legal status as a law passed by the legislature.” [Armstrong v. Ramos](#), 74 F.Supp.2d 142, 149 (D.P.R. 1999). The Title III court was unpersuaded by the force of this analogy between an environmental regulation and a bond resolution passed by a public authority. The latter regulates no third-party conduct, imposes no burden on anyone other than the entity that issues it, and need not satisfy the public notice requirements generally applicable to agency regulations. *Cf. Int’l Union, United Mine Workers of Am. v. Mine Safety and Health Admin.*, 407 F.3d 1250, 1259 (D.C. Cir. 2005) (APA notice and comment requirements serve to, among other things, “ensure fairness to affected parties” and give them an opportunity to object to a proposed rule). A resolution issued by a public corporation is much more akin to a resolution adopted by the board of a private corporation: The state grants the corporation the power to issue bonds and grant security interests, and the corporation then resolves whether and how to do so. Peaje offers no reason

to view the origin of its bonds in any materially different manner.

In sum, Peaje does not hold a statutory lien. As anticipated by the parties, this conclusion, together with our conclusion that the Title III court did not abuse its discretion in construing the limited nature of Peaje's motion, resolves this appeal. With the only asserted lien (a statutory lien) found not to exist, for purposes of this appeal Peaje claims no relevant property interest necessary to compel relief from the automatic stay. See \*13 [11 U.S.C. § 362\(d\)\(1\)](#) (requiring the bankruptcy court to grant relief from the automatic stay "for cause, including the lack of adequate protection of an interest in property of [a] party in interest" (emphasis added) ); *id.* [§ 922\(b\)](#) (incorporating [section 362\(d\)](#) into [section 922](#)). Similarly, Peaje cannot establish a likelihood of success on the merits of its claims for declaratory and injunctive relief without an interest in the underlying toll revenues and was therefore not entitled to a preliminary injunction on the basis requested. See [Bruns v. Mayhew](#), 750 F.3d 61, 65 (1st Cir. 2014) ("Because we hold that the appellants cannot succeed on the merits of their claim, we need not consider the likelihood of irreparable harm.").

#### IV.

Before concluding, we address the Title III court's alternative bases for denying relief as set forth briefly in the court's opinion: that Peaje failed to establish irreparable harm and that defendants established adequate protection of Peaje's interests. Peaje's contention on appeal that the district court "inverted" the burden of proof for the adequate protection analysis is defied by the district court's conclusion "that the Defendants have met their burden of showing that Peaje's interest is adequately protected." Nevertheless, for two reasons, we think it necessary for the Title III court to revisit these rulings anew should Peaje on remand renew its requests for relief consistent with this opinion. First, we find it difficult to evaluate such a brief treatment of two critical issues without understanding, at least, the Title III court's view as to the precise nature and extent of Peaje's collateral, its value at the time the Authority filed the bankruptcy petition, and the percentage of the toll revenues required in order to allow the toll highways to operate so as to generate future revenues. Second, the Title III court's analysis was necessarily sensitive to its view of how events would unfold, and much has transpired since September 2017, when it issued the order. We therefore vacate these two alternative findings, solely to make clear that they have no preclusive effect on remand. All that being said, nothing in this opinion should be read as implying any decision not expressly addressed within it.

#### V.

For the foregoing reasons, we affirm both the Title III court's order granting defendants' motion to strike and the primary grounds for its order denying Peaje's request for a preliminary injunction and relief from the stay. We otherwise vacate and remand for further proceedings consistent with this opinion, including the resolution of any updated motions for relief Peaje should choose to file. No costs are awarded.

#### All Citations

899 F.3d 1, 66 Bankr.Ct.Dec. 2