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Secured Lending to Foreign Borrowers: UCC Perfection, Enforcement Risks, and Conflict-of-Laws Issues

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Today's faculty features:

Matthew G. Bouslog, Attorney, **Gibson, Dunn & Crutcher LLP**, Irvine, CA
Edwin E. Smith, Partner, Morgan, **Lewis & Bockius LLP**, New York and Boston
Steven O. Weise, Partner, **Proskauer Rose LLP**, Los Angeles

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Secured Lending to Foreign Borrowers and Foreign Collateral of US Borrowers: UCC Perfection, Enforcement Risks, and Conflict-of-Laws Issues

Matthew G. Bouslog

Gibson, Dunn & Crutcher LLP

Edwin E. Smith

Morgan, Lewis & Bockius LLP

Steven O. Weise

Proskauer Rose LLP

Agenda

- Foreign debtor
- Tangible collateral of a U.S. debtor located in a foreign country
- Foreign account debtors of a U.S. debtor
- Tangible collateral of a foreign debtor located in the U.S.
- Enforcement issues
- Specific types of collateral

Foreign Debtor

- Note, Article 9 (including its choice of law rules) does not apply at all unless there is “an appropriate relation” to the forum state (§ 9-307, Comment 3)
- The perfection of a non-possessory security interest in the assets of a foreign debtor is governed by the law of the jurisdiction in which the debtor is “located” (§ 9-301(1))
 - A foreign debtor cannot be a “registered organization” (§ 9-102(a)(71))
- Look initially to the jurisdiction of the debtor’s place of business or, if more than one, its chief executive office (§ 9-307(b))

Foreign Debtor (cont'd)

- But remember that § 9-307(b) starts off with “[e]xcept as otherwise provided in this section...”
- § 9-307(c) contains a special rule for foreign debtors that overrides § 9-307(b)
- § 9-307(c) requires us to ask the following question:

Foreign Debtor (cont'd)

- Is the jurisdiction determined under § 9-307(b) one “whose law *generally* requires information concerning the existence of a nonpossessory security interest to be made *generally* available in a filing, recording or registration system as a condition or result of the security interest’s obtaining priority over the rights of a lien creditor *with respect to the collateral*”?

Foreign Debtor (cont'd)

- If the answer to the question is “yes”, the debtor is “located” in that jurisdiction, and perfection by filing based on “location” of the debtor is determined by compliance with the law of that jurisdiction, *e.g.*, filing
- If the answer to the question is “no”, the debtor is “located” in Washington, D.C., and perfection by filing is determined by complying with the D.C. filing requirements

Foreign Debtor (cont'd)

- What jurisdictions meet the requirements of § 9-307(c)?
- What does “generally” mean?
 - In Country A a corporate debtor is subject to the filing requirements but not an individual debtor or other non-corporate debtor
- What does the reference to “the collateral” mean?
 - Collateral located outside of Country A not subject to filing requirement under Country A law
 - *Danka & Hackett v. Del Monte Fresh Produce N.A., Inc.*, 228 Ariz. 533, 538, 269 P.3d 709 (App. 2012) (country must have filing system for collateral generally, and not just specific collateral at issue) (review denied May 31, 2012).
- What is the relevance of a UCC filing if a dispute or insolvency arises in the debtor’s foreign location?
 - Tangible collateral
 - Intangible collateral

Foreign Debtor (cont'd)

- Example 1: Debtor organized under non-US law with chief executive office located in Ontario, Canada, which is generally recognized as having a UCC-type filing system
 - Where to file financing statement?
 - In Ontario, Canada **and**, out of an abundance of caution, in the District of Columbia (§ 9-307(c))
- Example 2: Debtor organized under non-US law and chief executive office in Texas
 - Where to file financing statement?
 - In Texas **and**, out of an abundance of caution, in the District of Columbia (§ 9-307(b)(3))
- Example 3: Debtor organized under non-US law and chief executive office in Germany, which is generally recognized as not having a UCC-type filing system
 - Where to file financing statement?
 - In the District of Columbia (§ 9-307(c))

Tangible Foreign Collateral of US Debtor

- Debtor is a Delaware corporation that owns equipment located in Country B
- What jurisdiction's law determines perfection under Article 9?
- What jurisdiction's law determines priority under Article 9?
- § 9-301(3): “Except as otherwise provided in paragraph (4) [dealing with wellheads and mineheads], while negotiable documents, goods, instruments, money, or tangible chattel paper is located in a jurisdiction, the local law of that jurisdiction governs: ...
 - (C) the **effect** of perfection or nonperfection and the priority of a **nonpossessory** security interest in the collateral.”
- § 9-301(2) includes a similar rule for **possessory** security interests **and** for perfection by **possession**

Tangible Foreign Collateral (cont'd)

- What if the jurisdiction whose law determines priority does not distinguish perfection from priority?
- What is the relevance of a UCC filing if a dispute or insolvency arises in a foreign location?

Foreign Account Debtors

- Debtor is a Delaware corporation. Debtor's assets include accounts owed to Debtor by account debtors located in Country C
- Secured Party files a financing statement in Delaware covering accounts
- Is Secured Party's security interest perfected under Article 9?
- Will the Secured Party prevail over a creditor using Country C judicial process to garnish the accounts?
- United Nations Convention on the Assignment of Receivables in International Trade
- May Secured Party's security interest be challenged under Bankruptcy Code § 544(a)?
 - "Section 544(a)(3) modifies similar provisions contained in the House bill and Senate amendment so as not to require a creditor to perform the impossible in order to perfect his interest. Both the lien creditor test in section 544(a)(1), and the bona fide purchaser test in section 544(a)(3) should not require a transferee to perfect a transfer against an entity with respect to which applicable law does not permit perfection." [Legislative Statement concerning § 544]

Foreign Debtor/U.S. Collateral

- Debtor is an Ontario corporation with its chief executive office in Toronto. Debtor's assets include equipment located in New York
- Under Ontario law, perfection is determined by the law of the jurisdiction where the equipment is located
- Under New York law, perfection (nonpossessory) is determined by the law of the jurisdiction where the debtor is "located"

Enforcement Issues

- Relevance of § 1-301 in a foreign jurisdiction
 - Contract issues
 - Property issues
 - Availability of self-help
 - Penalties for secured party misbehavior

Enforcement Issues (cont'd)

- Conflict-of-Laws Analysis
 - New York governing law provision will be applied if you are in New York
 - N.Y. Gen. Oblig. § 5-1401
 - Generally applies to transactions in excess of \$250,000
 - However, UCC §§ 1-301 and 9-301 – 9-307 govern if applicable
 - *See also SunEdison, Inc. v. GCL-Poly Energy Holdings Ltd. (In re SunEdison, Inc.)*, 577 B.R. 120, 128 (Bankr. S.D.N.Y. 2017) (“the Court must abjure a conflicts analysis or consider foreign law or foreign public policy, and must instead apply New York substantive law”); *Hemlock Semiconductor Pte. Ltd. v. Jinglong Indus. & Commerce Grp. Co.*, 51 N.Y.S.3d 818, 827-28 (N.Y. Sup. Ct. 2017) (rejecting constitutional challenge and enforcing New York choice of law provision in contract between Singapore company and Chinese company)

Enforcement Issues (cont'd)

- Conflict-of-Laws Analysis (cont'd)
 - Other U.S. state courts will not necessarily apply a New York choice-of-law provision
 - *Rincon EV Realty LLC v. CP III Rincon Towers, Inc.*, 8 Cal. App. 5th 1, 18 (2017) (applying California law to invalidate jury waiver)
 - *ABF Capital Corp. v. Grove Properties Co.*, 126 Cal. App. 4th 204, 223 (2005) (applying California law to attorneys' fee provision)
 - Even less certainty whether a foreign court will apply New York (or U.S.) law
 - Involve foreign counsel at the beginning of a transaction and in connection with enforcement

Indirectly-held securities – Hague Securities Convention

- Scope
 - Nature of the rights acquired in securities held with an intermediary
 - Nature and effects against the intermediary and third persons of a disposition of, or the creation or transfer of an interest in, securities held with an intermediary
 - Article 2(1) issues
- Primary rule
 - Law ***in force*** in the State ***expressly*** agreed in the account agreement
 - Qualifying office
 - Filing rules
- Fall-back rule

Contracts subject to anti-assignment terms

- Choice of law
- § 9-401, Comment 3
 - Apply law that governs the contract, not the law that governs the security agreement

Intellectual property

- Jurisdiction where IP is protected
- May require filings in multiple jurisdictions

Cape Town Convention on International Interests in Mobile Equipment

- Aircraft Equipment
- Railway Rolling Stock
- Space Assets
- Mining, Agricultural and Construction Equipment

Other Specific Types of Collateral

- Real estate
- Goods in transit and documents of title
- Promissory notes and drafts (including bills of exchange)
- Directly-held securities
- Deposit accounts
- Virtual currency

Thank You

Matthew G. Bouslog

Gibson, Dunn & Crutcher LLP

mbouslog@gibsondunn.com

Edwin E. Smith

Morgan, Lewis & Bockius LLP

edwin.smith@morganlewis.com

Steven O. Weise

Proskauer Rose LLP

sweise@proskauer.com