

“HOME FIELD ADVANTAGE”
VENUE LITIGATION LESSONS FROM *PATRIOT COAL AND EFH*

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Litigation Lessons and Other Points of Interest from Patriot Coal Corporation's Venue Hearing						
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Can a debtor establish venue in a district where it is not “domiciled” and has no “residence” by creating a new entity in that district on the eve of bankruptcy?

In *In re Patriot Coal Corp.*, Case No. 12-12900 (Bankr. S.D.N.Y. July 9, 2012), the debtors did just that.

- Neither Patriot nor any of its subsidiaries had **offices** or **employees** in New York.
- Neither Patriot nor any of its subsidiaries was **domiciled** in New York.
- About **6 weeks** prior to filing its chapter 11 petition, Patriot incorporated PCX Enterprises, Inc. under New York law.
- About **2 weeks later**, Patriot created Patriot Beaver Dam Holdings, LLC under New York law.

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- On July 9, 2012, PCX filed for bankruptcy in New York. Patriot Beaver Dam filed next. Both entities based New York venue on their New York domicile.
 - The parent, Patriot Coal Corp., was the third to file, and based its venue on affiliation with entities that had filed in New York.
 - The Debtors later stipulated that they formed PCX and Patriot Beaver Dam to ensure that the provisions of Section 1408(1) of the venue statute were satisfied, **and for no other purpose.**

Requirements of 28 U.S.C. 1408

Section 1408 provides that a case **may** be commenced

(1) in the district in which the **domicile, residence, principal place of business, or principal assets **of the person or entity that is the subject of such case have been located for:****

- the one hundred and eighty days immediately preceding such commencement,
- or for a **longer portion of such one-hundred-and-eighty-day period than the domicile, residence, or principal place of business, or principal assets of such person were located in any other district;** or

(2) in which there is pending a case under title 11 concerning such person's affiliate, general partner, or partnership.

- Courts find that a corporation's domicile is its state of incorporation.
- PCX and Patriot Beaver Dam, which were created 6 and 4 weeks prior to the filing, respectively, were domiciled in New York for longer than in any other district during the 6 months preceding the filing.
- The parent, Patriot Coal Corp., was the third to file, and based its venue on affiliation with entities that had filed in New York.

Has any other debtor succeeded in doing this?

Winn-Dixie:

- A New York corporation, Dixie Stores, Inc., was created 12 days before the filing. DSI had no prepetition creditors; only assets are \$100K in a New York bank account. Debtors stipulated that DSI was formed solely to establish venue in NY.
- Evidence that half of employees, 40% of stores, and all of management located in Florida, and that all of the substantial assets were in southeastern states.
- Debtors consented to transfer, and stipulated that they believe they can achieve a successful reorganization in Florida and that they believe it may be less expensive to administer the case there.
- Chapman: “I mean, those facts [in Winn-Dixie] are so unique. They are so unique and, frankly, bizarre to have a debtor who makes a venue choice, things don’t go well, it gets really ugly. They change their mind. The debtor makes a venue motion to transfer its own case, gets opposed by the creditors’ committee. I mean, it’s a law school hypothetical.”

Has any other debtor succeeded in doing this?

Winn-Dixie:

“Given the circumstances here, first and foremost, and really solely the following factor, that DSI was formed solely to establish venue in New York, I conclude that the transfer of venue here would be in the interests of justice under Section 1412. . . I think that the interests of justice require transfer of venue where, again, the facts were created to fit the statute. In that sense, you are building the shop that you choose to act in as opposed to going to it. **On that sole basis, and none other, I will grant the motion.**”

Patriot Coal Corporation – Background

- Patriot is a leading producer and marketer of coal in the United States.
- Patriot was created on Oct. 31, 2007, as a spin-off from Peabody Coal, at that time the world's largest private-sector coal company. As a result of the spin-off, many retiree obligations remained with Patriot.
- On July 23, 2008, Patriot Coal acquired Magnum Coal (which had on its balance sheets substantial assets and liabilities previously acquired from Arch Coal), one of the largest coal producers in Appalachia.

Patriot Coal Corp. – Background (cont'd)

■ Headquarters

- - St. Louis

■ Operations

- - Of 12 active mining complexes, 9 are in West Virginia and 3 are in Kentucky.

■ Employees

- - Employees include miners, engineers, truck drivers, mechanics, electricians, administrative support staff, managers, directors, and executives.
- - 42% are unionized (compared to an average of 11.4% in the industry).

Patriot Coal Corp. – Background (cont'd)

■ Assets

- - The Debtors own or lease coal reserves, surface property and other real estate interests in many states, including Illinois, Indiana, Kentucky, Missouri, Ohio, Pennsylvania, and West Virginia.

■ Customers

- - Geographically dispersed customers: Patriot sells metallurgical and thermal coal to steel mills and electricity generators on 5 continents and in at least 15 states.
- - 78% of coal sales in 2011 were pursuant to long-term coal supply agreements.

Patriot Coal Corp. – Background (cont'd)

- **Creditors** include, among others
 - - \$802m DIP, with agents for both facilities located in NYC.
 - - Approximately \$360m drawn on prepetition secured facilities, which was rolled up in the DIP.
 - - Prepetition agent has an office in NYC.
 - - \$250m senior notes & \$200m convertible notes
 - - Wilmington Trust Company, based in DE, is the indenture trustee for the senior notes.
 - - Epiq determined that NY entities hold almost \$100m of the senior notes and convertible bonds.
 - - 10 of the top-50 unsecured creditors, holding approximately \$10m in claims in the aggregate, are located in WV; remainder are geographically dispersed across the country.
 - - Top-5 secured creditors located in California, Illinois, Missouri, New Jersey, and Ohio.

Patriot Coal Corp. – Background (cont'd)

■ Reorganization Needs

- - Decreased demand for coal, due in part to declining natural gas prices and more burdensome environmental and other government regulations.
- - Debtors' liabilities have increased, due in part to costs of compliance with environmental regulations.
- - As a result of the spin-off from Peabody and the acquisition of Magnum, the Debtors assumed liabilities to retirees of Peabody and Arch.
- “Especially in an era of declining demand and price for coal, there is a mismatch between the cost of legacy obligations and ongoing ability to generate revenue. The Debtors' long-term viability depends on their ability to achieve savings with respect to these liabilities.”
 - - Liabilities for benefits required by the CBA are estimated to exceed \$1.3 billion in the aggregate.
 - - Potential Coal Act and Black Lung liabilities also number in the hundreds of millions of dollars.

Where else could Patriot have filed?

- Among others:



- The Eastern District of Missouri (8th Circuit), in St. Louis, MO, where Patriot is headquartered;

- - The Southern District of West Virginia (4th Circuit), in Charleston, WV, near the majority of Patriot's operations; or

- - The District of Delaware (3rd Circuit), in Wilmington, DE, where Patriot Coal Corporation is incorporated.

Did Patriot have *any* connections to New York?

- Nearly 2/3 of sales contracts governed by NY law.
- As stated, many creditors, including agents for the DIP and prepetition secured facilities and many of the bondholders, are located in New York.
- Counsel for many parties that appeared in the cases, including the Debtors' counsel DPW and even the Union's counsel, located in New York.

Motions to Transfer Venue

- The **United Mine Workers of America** and certain **Sureties** moved to transfer venue pursuant to 28 U.S.C. 1412, arguing that the cases must be transferred to the **Southern District of West Virginia** in the **interest of justice** and for the **convenience of the parties**.
- The **United States Trustee** moved, also pursuant to 28 U.S.C. 1412, for a transfer of venue to **any other proper forum**, arguing that the **interest of justice** required such a transfer because of the way venue was obtained in these cases.

Motions to Transfer Venue (cont'd)

- No party argued that the requirements of the venue statute, 28 U.S.C. 1408, were not satisfied.
- No party contested the Debtors' good faith, and, indeed, all conceded at the hearing that there was no evidence of bad faith.

Motions to Transfer Venue (cont'd)


- Certain additional parties either joined or supported the motions to transfer venue:
 - The State of West Virginia
 - The Kentucky Department of Natural Resources
 - The UMWA Pension & Benefit Plans
 - Three Utility Companies, including AEP (a member of the Creditors' Committee and a top-50 creditor)
 - An Ad Hoc Group of Shareholders

Section 1412 – Legal Standards

- 28 U.S.C. 1412 provides that a district court ***may*** transfer a case or proceeding under title 11 to a district court for another district, in the ***interest of justice*** or for the ***convenience of the parties***.
- The movants have the burden of proof.
- The cases find that this is a heavy burden, and that the debtor's choice of forum, if proper, is entitled to substantial weight and deference.

Factors Considered in Connection with a Motion to Transfer for the Convenience of the Parties

1. Proximity of creditors of every kind to the court;
2. Proximity of the debtor to the court;
3. Proximity of witnesses necessary to administration of the estate;
4. Location of assets;
5. What will promote the economic and efficient administration of the estate; and
6. Whether there is a potential need for ancillary administration.

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- Movant must show that the balance of convenience clearly weighs in its favor.
 - Courts find that, of the six factors, the economic and efficient administration of the estate is the most important.
 - Courts place little emphasis on the location of the assets or the need for ancillary administration of the estate where the debtor seeks to reorganize, rather than liquidate.

Factors considered in connection with a motion to transfer venue in the interest of justice:

The interest of justice prong is a **broad and flexible standard** that is applied on the **facts and circumstances of each case**.

Courts consider what will promote:

1. the economic and efficient administration of the estate;
2. judicial economy;
3. timeliness; and
4. fairness.

Some courts have also considered whether there is a local interest in having localized controversies decided at home.

Debtors' Response

- The Debtors' lengthy response focused on, among other things, the cost of administering the cases in Charleston, West Virginia.
- The Debtors contrasted New York City, a global transportation hub, with Charleston, WV, and argued that:
 - - there is just one direct flight each day from NY (on a plane with fewer than 40 seats)
 - - there are no direct flights at all to Charleston from many other cities where parties in interest are located
 - - flights to and from Charleston are often exceedingly expensive, costing many hundreds of dollars (and more than \$2,200 at times) for a refundable, round-trip ticket.
- In its reply, the Union responded that the Debtors had exaggerated costs and inconvenience of flights, and also that Charleston, WV is relatively inexpensive, such that parties' professionals would save on hotel costs. The Union attached print-outs from Expedia.com as evidence.

Debtors' Response (cont'd)

- In response to the U.S. Trustee's motion, the Debtors argued that they satisfied Section 1408(1) and that, in good faith, they filed in New York because they believed that a NY venue was in the best interests of the estates.
- The Debtors distinguished *Winn-Dixie* on its facts, argued that Judge Drain's decision in that case was based on a misinterpretation of 2nd Circuit precedent, and noted that the U.S. Trustee had actually *opposed* transfer in that case, calling on the court to rule on the basis of the preferences of the largest creditors.

Joinders to the Debtors' Response

- Creditors' Committee
- Indenture Trustee for Senior Notes
- Ad Hoc Group of Senior Notes Holders
- First Out DIP Agent
- Second Out DIP Agent
- Three other creditors, including Caterpillar, a top-50 creditor, filed unique joinders

Template Joinders & Statements of Support

- 29 identical joinders were filed by creditors the Debtors' contacted for support.
- These creditors used, and did not deviate from, a form template prepared by the Debtors.
- 14 additional creditors elected not to file formal joinders but authorized the Debtors to represent their support for the Debtors' position.
- The Debtors later represented that they contacted 80 creditors in total, with Patriot employees reaching out to creditors with whom they had "pre-existing working relationships."



Litigation Lesson 1

“Yes, evidence; I’m really big on evidence.”

Litigation Lesson 1 (cont'd)

- Prior to the hearing, the parties entered into a Stipulation of Facts.
- The Debtors stipulated that the two NY entities were created for the sole purpose of satisfying Section 1408(1).
- The parties agreed that all declarations and exhibits would be admitted, without any cross-examination of any of the witnesses.

Litigation Lesson 1 (cont'd)

- “There’s a burden of proof here, and my job, when we’re done, is going to be to comb through the record and determine whether the burden of proof was carried. . . . As we’re proceeding, if we identify factual issues that aren’t covered by the record, what happens?”
- Judge Chapman implied, through questioning, that the record did not support the Union’s assertion that “most of the employees are located in West Virginia.” When counsel for the Union could not point to record support for the assertion, Judge Chapman stated, “Well, this is exactly what my concern was about the stipulation.”
- With respect to the Union’s statement that a transfer to WV would reduce the costs of administration of the estate, Judge Chapman stated “There is no evidence on that. There is no evidence. . . . A lot of statements have been made about the costs. A lot of hypotheses have been offered. But there’s no evidence as to the cost of the case in one venue versus another. There is speculation about the use of local counsel. There’s speculation about travel time, hotel rooms, costs of flights, but no one’s presented me with a coherent or cohesive model of what would actually happen.”

Litigation Lesson 2

- Cross-examine opponents' witnesses.

Litigation Lesson 2 (cont'd)

- The Debtors' first day declaration stated that "[t]he Debtors determined that the SDNY is the optimal venue for the Debtors' chapter 11 cases and is in the best interests of the Debtors, their creditors and other stakeholders and these estates. . . . I believe that had we filed in one of the other jurisdictions that were also available to us (i) most of our domestic and foreign creditors would have been inconvenienced and (ii) the costs and inefficiency of the administration of the estates would have materially increased."
- Because the Movants waived their right to cross-examine Mr. Schroeder, this testimony as to the estates' best interests and costs of administration was unrefuted.

Litigation Lesson 2 (cont'd)

- In closing argument, the Union argued that the costs of proceeding in NY vs. WV were “unknowable.” The court responded, “No, but that’s the problem that I have is that all I have is what the parties tell me, and here have the debtor telling me they determined this, and I would have been very happy to listen to lengthy cross-examination of Mr. Schroeder on this point; indeed, I was looking forward to it, but it didn’t happen.”
- The Debtors argued, “[a]nd the movants had a burden to show X. They decided not to serve discovery. They could have said we think you did this for the wrong reasons; we want discovery. We think you did this to run from something; we want discovery. We think you did this to disadvantage a specific creditor; we want discovery. We think you did this to get a forum that’s going to be unduly, sleazily in your favor. They could have asked us a million things. What they did instead was they agreed that the facts are we did it in the best interest of the estate, in the best interest of creditors, with cost and efficiency, and to make it convenient for creditors.”

Litigation Lesson 3

- Avoid creating an implication of bias or favoritism.

Litigation Lesson 3 (cont'd)

- The Union was attacked by opponents and the Court for stating, in their reply papers, that “Judges in the Southern District of West Virginia live near coal miners, grew up with them, worship with them, and break bread with them.”
- The Court stated, “in my mind, this issue that you’re raising, the familiarity – the judges grew up with coal miners, they live among coal miners – it gives me some pause, I have to say, because, in my mind, the most ancient traditions of justice require that the tribunal be completely impartial.”

Litigation Lesson 3 (cont'd)

- Counsel for the Union also stated at the hearing that Union members would want the case to be transferred to WV even if, all other things being equal, administration of the cases would cost less in New York.
- Counsel for the Union also stated that negotiations with Union members would “be that much more difficult” if the Court denied their motion, because the Union members would perceive the denial as the Court being unfair to them.

Litigation Lesson 4

- Don't insult the judge.

Litigation Lesson 4 (cont'd)

- The Union and Sureties argued, in part, that the complexities of the coal mining industry and related regulatory landscape were reasons to transfer the case to WV, where judges would be more familiar with these issues.
- When the Sureties argued that any asset sale would involve a fight over whether environmental liabilities could be satisfied, which fight would require the testimony of engineers, Judge Chapman responded that she “had an A+ average when she was an engineering student at Cornell University.”
- Judge Chapman also questioned the premise that local courts are better equipped to hear local controversies, stating repeatedly, “what I’m trying to understand is the notion that, because of the intense local interest, why it inexorably follows that a local court would be the best place to resolve this when I’ve identified so many different conflicting interests.”

Litigation Lesson 5

- Beware the use of “template” joinders.

Litigation Lesson 5 (cont'd)

- With respect to the joinders, in response to a statement by Debtors' counsel that the Debtors reached out to a small group of creditors for support, Judge Chapman stated, "But I have a problem with that, because sometimes to ask the question is to imply the answer, all right. So I don't know how many parties the debtor reached out to, how many parties said, sure, we want to help you. To me, it possibly is a heavy-handed question to ask a business counterparty for their help, because it could imply that, if you want to keep doing business with us . . . we need your help. In addition, it creates an impression that may not be accurate. . . . So the process that you're describing makes it very difficult and challenging for me to know how much weight to give these joinders."

Litigation Lesson 6

- Don't rely on website print-outs to prove critical facts.

Litigation Lesson 6 (cont'd)

- The court criticized the Debtors' arguments regarding limited direct flights to Charleston, WV, stating that this case is not going to turn on the number of seats on a plane. "It's just not."
- The court also criticized the use of web print-outs from Expedia.com as evidence. "[E]verybody sent me reams of submissions from Expedia and other travel web sites about the costs of various flights, and I don't know when hearings would take place, so I don't know if the cost would vary. What I'm trying to say to you in the nicest possible way is that there is no coherent cost model that's been presented on which I can conclude that the statement that you made is supported by the facts or what actually would occur."

Litigation Lesson 7

- If you take a position that is the opposite of your previous position, have a good explanation.

Litigation Lesson 7 (cont'd)

- The court was not impressed that the U.S. Trustee was now taking the opposite position from its position in *Winn-Dixie*.
- In that case, the U.S. Trustee stated, “The debtors’ support of the transfer may not be dispositive since the committee and what I have calculated to be almost 600 million of debt have objected to the transfer. So the U.S. Trustee encourages the Court to apply the standard under 1412 to allow the true stakeholders in this case to be heard.”
- Judge Chapman asked, “What led you to take that – you, meaning your office, to take that position then – and how I can make a reasoned conclusion from what you did there ... [and] you’re taking a different position here. You are urging on me what I view as kind of a per se rule.”



Who should win?


There Are Two Kinds of Venue Transfer Motions Before the Court:

- The first is more traditional, arguing that there is something about this industry and this company's operations and reorganization needs that make this a West Virginia issue, that should be litigated at home in West Virginia.
- The second cannot succeed unless the Court agrees that:
 - - the Debtors' good faith venue selection, based on a reasoned analysis of various factors, and the Debtors' unrefuted determination that administration of the estates will cost less in NY, are not relevant.
 - - that it is only if a corporation has chosen the laws of a particular state to govern for general corporate purposes, for reasons unrelated to bankruptcy venue, may it enjoy venue in that state in bankruptcy.

Additional Litigation Lessons from the Recent EFH Venue Hearing						

In re Energy Future Holdings Corp., et al., **Case No. 14-10979 (Bankr. Del.)**

- EFH and certain of its affiliates filed Chapter 11 petitions in the District of Delaware based upon the domicile of certain of the Debtors.
- None of the Debtors had assets, offices, operations, customers, or employees in Delaware.
- Wilmington Savings Fund Society, FSB, the Second Lien Indenture Trustee, filed a motion to transfer venue on the first day of the case.

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- Contemporaneously with the petitions, the Debtors filed motions seeking customary first day relief (as well as certain motions seeking non-customary relief).
 - The Texas PUC filed a statement in support of certain first day relief.

In re Energy Future Holdings Corp., et al., **Case No. 14-10979 (Bankr. Del.)**

- Wilmington Savings requested transfer to the Northern District of Texas on the basis that (i) it was more convenient for the parties, including Debtors' management and trade creditors, (ii) Texas regulators and Texas litigants had a substantial interest in the case, and (iii) the Northern District of Texas was a more appropriate forum to conduct a valuation hearing.
- Only two parties filed joinders to the motion to transfer: Ad Hoc Committee of TCEH Unsecured Noteholders and "Neighbors for Neighbors."
- Multiple parties joined the Debtors in opposing the motion to transfer.



Litigation Lesson 1

- It matters who argues.

Litigation Lesson 1 (cont'd)

- The movant, Wilmington Savings, was based in the city where the case was filed.
- Neither Wilmington Savings' attorneys nor those of any other party arguing the motion were from Texas.
- No Texas trade creditor or litigant, parties whose interests Wilmington Savings had espoused, appeared to request a venue transfer.
- The State of Texas did not oppose venue in Delaware.

Litigation Lesson 2

- The requested remedy should match the injury.

Litigation Lesson 2 (cont'd)

- Wilmington Savings requested a venue transfer.
- What does Wilmington Savings really want in the case?