# COURT OF CHANCERY OF THE STATE OF DELAWARE

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VICE CHANCELLOR

New Castle County Courthouse
500 N. King Street, Suite 11400
Wilmington, Delaware 19801

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Decided: April 24, 2009

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***RE: Mitsubishi Power Systems Americas, Inc. v. Babcock & Brown Infrastructure Group US, LLC, Babcock & Brown, L.P., Babcock & Brown Holdings, Inc., Babcock & Brown Renewable Holdings, Inc., and Babcock & Brown International Party Ltd. C.A. No. 4499-VCL***

Dear Counsel:

I have read and considered the briefs and arguments regarding the plaintiff's motion for a temporary restraining order heard by telephonic conference on April 22, 2009. For the reasons set forth herein, the plaintiff's motion will be granted in part and denied in part. An implementing order is being entered contemporaneously with this ruling.

## I.

Mitsubishi Power Systems Americas, Inc. ("MPSA") is an industrial concern engaged in the manufacture and sale of, among other things, wind turbines used for the production of electrical power. The various Babcock & Brown defendant entities form part of a corporate group based in Australia which operates a global investment business through over 1500 worldwide subsidiaries (collectively "Babcock"). Until recently, the parent entity of the group, Babcock & Brown Limited ("BBL"), was publicly-traded on the Australian Stock Exchange.

Babcock's operations are managed by BBL's operating subsidiary, Babcock & Brown International Party Limited ("BBIPL"). Through BBIPL, Babcock capitalizes its various subsidiaries through the use of BBIPL's syndicated credit facility. In order to facilitate this, BBIPL maintains a treasury management policy in which excess cash balances in its subsidiaries are swept up to BBIPL, where they are used to maintain the credit facility obligations and provide capital for the various Babcock subsidiaries.

Among Babcock's various investment interests is the wind-power generation business. Although it ultimately operates this business through a number of special-purpose entities, it initiates each of these wind farm projects through its subsidiary Babcock & Brown Infrastructure Group US, LLC ("BBIG"), a Delaware limited liability company. Pursuant to that general practice, BBIG entered into a pair of Turbine Supply Agreements ("TSAs") in 2007 and 2008 with MPSA. Under those TSAs, MPSA was to manufacture and deliver a total of 456 wind turbines, for a total purchase price in excess of [redacted]. Because BBIG did not have its own source of capital sufficient to perform under the TSAs, MPSA required BBIPL to guarantee the obligation of BBIG under the TSAs. In return, so long as the BBIPL guarantee was in place, BBIG (and any entity succeeding to BBIG's rights by assignment under the TSA) had the right to assign its rights and obligations under the TSA to any affiliate entity without the consent of MPSA. The TSAs further provided that such assignments would have the effect of extinguishing BBIG's obligations to MPSA under the contract.

In order to manufacture and deliver wind turbines in the quantity required under the TSAs, MPSA was required to incur significant expenses. Thus, the TSAs provided for BBIG to make progress payments to MPSA upon the achievement of certain milestones. One such progress payment was due in May 2008 on the 2007 TSA, and another in August 2008 on the 2008 TSA, totaling [redacted]. Neither payment has been made. BBIG told MPSA that the non-payments were due to financial difficulties that it was working to resolve, and MPSA permitted work to continue on the wind turbines in reliance on these representations. On November 20, 2008, no progress payments having been made, MPSA informed BBIG that it was suspending production under the TSAs. MPSA and BBIG nevertheless continued to negotiate towards an amicable solution through the first quarter of 2009. As a result of the effective termination of the TSAs, MPSA now claims it has suffered nearly a billion dollars in damages.

BBIG's inability to make its progress payments to MPSA as they came due in 2008 apparently resulted from the effects of the current credit crisis on BBIPL's ability to finance its business. Last year, as credit markets contracted and economic conditions worsened, Babcock's credit ratings suffered a series of downgrades over the course of the summer. In July 2008, faced with the possible breach of certain covenants related to BBL's market capitalization under BBIPL's senior secured credit facility, BBIPL reached a deal with its lenders. Pursuant to that agreement, the lenders agreed to waive the covenant at issue in exchange for BBIPL's promise to prepay approximately $400 million of debt under the credit facility. Funding to accomplish that prepayment was to come from asset sales that Babcock planned to engage in over the following three months. Additionally, Babcock agreed to pay down approximately half of its $2 billion outstanding debt under the credit facility by 2011 through additional asset sales.

Babcock's financial fortunes continued to deteriorate through the first quarter of 2009. On February 6, 2009, BBIPL entered into a further agreement with the syndicate of lenders under its senior secured credit facility to sell all of BBIPL's and its subsidiaries' assets and provide the proceeds, net of expenses, to the senior secured lenders (the "Agreed Asset Sales Program"). Importantly however, the security interests of BBIPL's senior secured lenders do not appear to extend to the assets of BBIG. Finally, on March 13, 2009, following the rejection by noteholders of a proposed restructuring of the terms of certain unsecured notes of Babcock, the board of BBL placed the company in voluntary administration.[1]

After discovering that Babcock had been placed into administration, MPSA became concerned that assets of BBIG were being dissipated in order to pay off BBIPL's senior secured lenders.[2] Thus, as part of its ongoing discussions with BBIG to reach a settlement, in mid-March 2009 MPSA began asking BBIG for details of certain asset transfers that BBIG had made to affiliates over the course of

[1] Counsel for the Babcock entities has indicated that administration is generally the Australian equivalent to Chapter 11 of the Bankruptcy Code. *See generally* 11 U.S.C. § 1101 *et seq.*

[2] Among other things, MPSA noticed in a trial balance sheet it had been given for BBIG earlier that year that BBIG had made over [redacted] in distributions to its equity holders over the course of its lifetime.

the previous year.[3] Although communications between the two companies continued during this time, MPSA received no response to these inquiries.

Then, on April 8, 2009, MPSA learned from a trade publication that Babcock had taken steps to sell certain U.S. wind generating assets, and would be accepting a second round of bids for these assets on or about May 8, 2009. Concerned that these planned future sales would result in the continued dissipation of assets that MPSA believed should be available to satisfy the creditors of BBIG (including itself), MPSA filed a complaint in this court on April 9, 2009. The complaint alleges that BBIG had engaged in fraudulent transfers to affiliates of certain assets for less than fair value, that BBIG had made improper distributions under the Delaware Limited Liability Company Act,[4] and two alternative theories of its breach of contract claim against BBIG.

MPSA also filed a motion for expedited proceedings and a motion for preliminary injunction. Concerned that it be able to develop a fact record sufficient to support a preliminary injunction application in time to prevent the upcoming Babcock asset sales, MPSA also sought a highly expedited discovery schedule to be completed by May 6. During an April 13 teleconference to consider the motion to expedite, this court encouraged the parties to come to an agreement as to a status quo order and a less onerous discovery schedule, and suggested that if the parties could not do so the court would entertain a motion by MPSA for a temporary restraining order. The parties came to an agreement on a short-term status quo order, but were unable to agree as to a longer-term order to last until the matter could be made ready for a preliminary injunction proceeding. Meanwhile, expedited discovery began on April 13.

Concerned about the approaching April 22 expiration of the agreed upon status quo order, MPSA moved for a temporary injunction on April 20, 2009. In its application for a temporary restraining order, MPSA seeks to enjoin transfers by any of the Babcock defendants outside of the normal course of business, with the

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[3] MPSA appears to have been particularly concerned with BBIG's June 2008 sale of Trans Bay Funding LLC to Babcock & Brown Infrastructure Fund North America LP ("BIFNA"). BBIG received [redacted] in cash proceeds from the sale of Trans Bay. According to Babcock, it swept those proceeds upstream to BBIPL pursuant to its standard treasury management policy.
[4] *See* 6 *Del. C.* 18-607(a).

exception that sales of assets for fair value may be made by the defendants so long as the proceeds are then held in escrow.

## II.

"The essential predicate for issuance of [a temporary restraining order] is a threat of imminent, irreparable injury. Once that is shown, the remedy ought ordinarily to issue unless the Court is persuaded (1) that the claim asserted on the merits is frivolous or not truly litigable, (2) that the risk of harm in granting the remedy is greater than the risk to plaintiff of denying it, or (3) that plaintiff has not proceeded as promptly as it might, [and] has therefore contributed to the emergency nature of the application and is guilty of laches."[5]

For the purposes of an application for a temporary restraining order, the analysis of whether the claims asserted are meritorious generally requires nothing more than a showing "that a colorable claim has been made out if the facts alleged are true."[6] The defendants contend, however, because of MPSA's delay in bringing this application, the appropriate standard is the higher burden required to obtain a preliminary injunction—a "reasonable probability of success on the merits."[7] In support of this contention, the defendants cite *Insituform Technologies, Inc. v. Insitu, Inc.*[8] *Insituform*, however, stands for the proposition that "[w]here … the applicant [for a temporary restraining order] has had the opportunity to develop evidence and present a record from which the court may 'responsibly make a more informed judgment concerning the merits,' … 'the elements of the equitable test is something akin to the traditional preliminary injunction formulation.'"[9] There is no reason to believe here that the discovery process set in motion merely a week ago has been completed, nor that MPSA has had an opportunity to develop the fact record to the degree necessary for the court to "responsibly make a more informed judgment concerning the merits." Thus, the court will apply the normal "colorable claim" standard to the merits analysis here.

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[5] *Cottle v. Carr*, 1988 WL 10415, at *3 (Del. Ch.).
[6] *UIS, Inc. v. Walbro Corp.*, 1987 WL 18108, at *1 (Del. Ch.).
[7] Defs.' Br. in Opp'n 23-24. For the showing necessary to support an application for a preliminary injunction, see, for example, *Hecco Ventures v. Sea-Land Corp.*, 1986 WL 5840, at *3 (Del. Ch.).
[8] 1999 WL 240347 (Del. Ch.).
[9] *Id.* at *7 (citing *Newman v. Warren*, 684 A.2d 1239, 1244 (Del. Ch. 1996)).

MPSA alleges in its complaint that BBIG has breached its obligations under the TSAs, resulting in massive damages to MPSA. Although BBIG disputes the magnitude of the damages, BBIG tacitly acknowledges in its briefs that it did in fact breach the TSAs by failing to make certain progress payments under the agreements as they became due. MPSA has, therefore, stated a colorable claim for breach of contract against BBIG.

The threat of irreparable injury arises from a different source. MPSA further alleges that BBIG has engaged in fraudulent transfers to its affiliates and intends to do so again in the near future. The threat of a fraudulent transfer will constitute irreparable harm warranting injunctive relief.[10] Thus, MPSA's showing of imminent, irreparable harm hangs on its ability to demonstrate a colorable claim that BBIG intends to engage in one or more fraudulent transfers in the near future.

The Delaware Uniform Fraudulent Transfer Act (the "DUFTA") is codified at 6 *Del. C.* § 1301 *et seq.* Section 1305 of the DUFTA reads:

> (a) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor[11] whose claim arose before the transfer was made or the obligation was incurred if the debtor made the transfer or incurred the

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[10] See 6 *Del. C.* § 1307(a), which reads:

> In an action for relief against a transfer or obligation under this chapter, a creditor, subject to the limitations in § 1308 of this title, may obtain:
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> > . . .
> >
> > (2) An attachment or other provisional remedy against the asset transferred or other property of the transferee in accordance with the procedure prescribed by applicable law;
> >
> > (3) Subject to applicable principles of equity and in accordance with applicable rules of civil procedure:
> >
> > > a. An injunction against further disposition by the debtor or a transferee, or both, of the asset transferred or of other property;
> > >
> > > . . .
> > >
> > > c. Any other relief the circumstances may require.

[11] For purposes of the Act, a creditor is defined as "any person who has a claim." 6 *Del. C.* § 1301(4). A claim is defined as a "right to payment, whether or not the right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured or unsecured." 6 *Del. C.* § 1301(3). Thus, MPSA's unliquidated, contingent, disputed, unsecured right to payment under the TSAs is nevertheless a claim for purposes of the Act, and MPSA thereby a creditor of BBIG.

> obligation without receiving a reasonably equivalent value in exchange for the transfer or obligation and the debtor was insolvent at that time or the debtor became insolvent as a result of the transfer or obligation.
>
> (b) A transfer made by a debtor is fraudulent as to a creditor whose claim arose before the transfer was made if the transfer was made to an insider[12] for an antecedent debt, the debtor was insolvent at that time and the insider had reasonable cause to believe that the debtor was insolvent.

Section 1302 of the DUFTA defines "insolvent" for the purposes of the Act as follows:

> (a) A debtor is insolvent if the sum of the debtor's debts is greater than all of the debtor's assets, at a fair valuation.
>
> (b) A debtor who is generally not paying debts as they become due is presumed to be insolvent.

BBIG's assets at present appear to be on the order of $60 million or less.[13] BBIG's unpaid obligation to MPSA for the missed progress payments under the TSAs (ignoring any alleged setoffs) total $86 million. In addition, MPSA claims that BBIG owes it much greater damages for costs it incurred to begin the manufacturing process of the wind turbines, in reliance on BBIG's promises to pay, as well as MPSA's lost profits on the agreements. It thus appears, in all likelihood (and at the very least there is a colorable argument) that BBIG's debts exceed its assets, thereby making it insolvent. Moreover, BBIG has acknowledged that, at least with respect to MPSA, it failed to pay its debts as they became due with respect to the progress payments under the TSAs, leading to the presumption that BBIG is insolvent.

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[12] An insider is defined for purposes of the Act as, *inter alia*, a "person in control of the debtor." 6 *Del. C.* § 1301(7)(b)(3). Person is defined in the Act to generally encompass any legal person, natural or otherwise. *See* 6 *Del. C.* § 1301(9).

[13] Pl.'s Opening Br. Ex. F, App. D (summarizing the assets of BBIG).

Thus, MPSA has made a colorable claim that any future transfer by BBIG of assets for less than reasonably equivalent value would be fraudulent as to MPSA.[14] Moreover, if in fact BBIG is insolvent (and BBIG's parent entities have reasonable cause to believe so) any future transfer to BBIG's parent entities, as insiders, on account of preexisting intercompany debt would be fraudulent *per se*.[15]

Babcock states that, as a matter of standard operating procedure, material cash assets in its operating subsidiaries are swept up to BBIPL for redeployment elsewhere in the business, or, now, to repay BBIPL's senior secured debt. Although Babcock contends that it has no plans for any asset sales by BBIG in the near future, it became clear during oral argument that this is not entirely accurate. Rather, what emerged was that a sale is now being negotiated for BBIG's interest in BIFNA, which is expected to close in three to six weeks.[16] In addition, BBIG is seeking bidders for its interests in its "G3," "Pampa," and "Central Valley Transmission" projects. If BBIPL were to cause BBIG to transfer the proceeds of these sales upstream, as it would otherwise do, such transfers would arguably be fraudulent as to MPSA.[17]

MPSA also alleges that BBIG has already engaged in one fraudulent transfer, the so-called "Trans Bay Transaction." Babcock admits that on June 27, 2008, BBIG sold all of its interest in Trans Bay Funding LLC to BIFNA for [redacted] in cash.[18] "Per its treasury management policy, BBIG transferred those proceeds upstream to [Babcock & Brown, L.P., which in turn] transferred

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[14] *See* 6 *Del. C.* § 1305(a).
[15] *See* 6 *Del. C.* § 1305(b).
[16] It is expected that BBIG's [redacted] stake in BIFNA will yield approximately [redacted] in cash proceeds. Defs.' Co-Counsel's Letter to the Court of April 22, 2009.
[17] Babcock, in its brief, argues that in the context of a treasury management policy like the one it has implemented (in which a parent entity capitalizes its subsidiaries through the use of borrowing which solely obligates the parent), upstream transfers to the parent to repay such borrowings are in exchange for equivalent value because the subsidiary benefits indirectly from the parent's ability to borrow on the basis of the subsidiary's cash flows. Defs.' Br. in Opp'n 28-31. While this argument makes practical commercial sense in the context of a solvent enterprise, it can be seen as ignoring the boundaries between separate legal entities and an insolvent entity's obligations not to make distributions to equity holders. In any event, it is neither necessary nor appropriate to resolve that issue in the present context. All the court need determine today is that MPSA has stated a colorable claim. It has.
[18] Lillybeck Aff. ¶¶ 26-29.

those proceeds upstream to BBIPL."[19] BBIG had by this time already defaulted on one progress payment to MPSA, and shortly thereafter defaulted on the second. It is therefore at least colorable that BBIG was insolvent by the time the proceeds of the Trans Bay sale were swept up to BBIPL from BBIG. That transfer of funds, for the same reasons described above for the anticipated future transfers, was arguably fraudulent as to MPSA. Thus, in this respect also, the complaint states a colorable claim. Because a defrauded creditor may seek recovery not only from the transferor but from a transferee as well,[20] MPSA seeks to enjoin transfers by BBIPL and the entities it owns through which the Trans Bay funds passed.

Turning to the balancing of equities, the court may grant a temporary restraining order only if the risk to the defendant of an improvidently granted order is not greater than the risk to the plaintiff of denying the application. As to BBIG alone, the court is convinced that the equities of a temporary restraint against upstream transfers fall in MPSA's favor. Such a restraint would not prohibit BBIG from engaging in asset sales to third parties for fair value. It simply requires that the proceeds of such sales be placed in escrow pending further consideration of these claims on a motion for a preliminary injunction. This restraint also poses no creditable threat to Babcock since it would not appear to trigger any event of default under the Agreed Asset Sales Program.

As to a broader restraint, reaching the other Babcock entities, however, the equities fall firmly in the defendants' favor. As part of the terms of the Agreed Asset Sales Program, an injunction against any of BBIPL's Material Subsidiaries (defined in the agreement to include the other entities a broader restraint would reach, but not BBIG) would likely constitute an event of default. Such event of default would entitle the banks to immediately place BBIPL into receivership and begin a rapid liquidation of Babcock's assets at "fire sale" prices. Babcock argues convincingly that such a liquidation would be injurious not only to the Babcock entities and the current plan of orderly liquidation, but to many of the stakeholders in Babcock as well.[21] MPSA dismisses the risk of this "parade of horribles" as

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[19] *Id.* ¶ 29.

[20] *See, e.g.*, *August v. August*, 2009 WL 458778 (Del. Ch.).

[21] As an example of the harms that would occur as a result of BBIPL being placed in receivership, BBIPL would in all likelihood immediately cease to exist as a going concern, resulting in the immediate displacement of hundreds of present Babcock employees. Additionally, the severance payments to already laid-off Babcock employees that the banks are

remote and not in the economic interests of the banks. But the court is unwilling to expose Babcock to such potentially ruinous developments. In this connection, the court notes that MPSA entered into the TSAs in reliance on the credit of BBIPL, not BBIG, and yet has not sued BBIPL on its guarantee. That BBIG both retains any liability on the TSAs and has substantial asset to which MPSA can look to recover its loss are matters of mere happenstance. In the present circumstances, the court will act to protect MPSA's rights in the assets of BBIG, but it will not enlarge those rights in a manner that threatens the interests of all other stakeholders in Babcock.

* * *

Thus, the court concludes that MPSA is entitled to a temporary restraining order prohibiting BBIG from transferring any assets other than in the ordinary course, except that it may pursue third-party asset sales so long as any proceeds from those sales be kept in escrow. To that extent, MPSA's motion is GRANTED IN PART. To the extent that MPSA seeks injunctive relief against any of the other defendants, MPSA's motion is DENIED IN PART. An order implementing this decision will be entered contemporaneously with this opinion. MPSA will be required to post a $500,000 bond against any harm the defendants might suffer as a result of the improvident grant of the temporary restraining order. IT IS SO ORDERED.

/s/ Stephen P. Lamb
Vice Chancellor

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presently allowing Babcock to pay would likewise be immediately terminated as well. MPSA, if it is able ultimately to prove its case here, should be able to pursue the banks as transferees to recover any fraudulent transfers by BBIG. Clearly, MPSA faces significant risks in that approach as a result of possible differences between U.S. and Australian law. Nevertheless, the court will not risk causing the potential harm to the Babcock entities detailed above to save MPSA the risk of non-recovery, particularly on the basis of an emergency application.