**UNITED STATES BANKRUPTCY COURT**
**DISTRICT OF MAINE**

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| In re:<br><br>MONTREAL MAINE & ATLANTIC RAILWAY, LTD.<br><br>Debtor. | Bk. No. 13-10670<br>Chapter 11 |

**TRUSTEE'S OBJECTION TO WHEELING & LAKE ERIE RAILWAY COMPANY'S MOTION TO ENFORCE CASH COLLATERAL ORDERS**

Robert J. Keach, the trustee (the "Trustee") of Montreal Maine & Atlantic Railway, Ltd. (the "Debtor"), by and through his undersigned counsel, hereby objects to *Wheeling & Lake Erie Railway Company's Motion to Enforce Cash Collateral Orders* [D.E. 603] (the "Motion"), filed by Wheeling & Lake Erie Railway Company ("Wheeling"). In support of this objection, the Trustee states as follows:

## PRELIMINARY STATEMENT

1. After months of knowing that the proceeds of the accounts receivable of Montreal Maine & Atlantic Canada Co. ("MMA Canada") were not being segregated and remitted, Wheeling now is attempting to assert a security interest in such proceeds—which are property of an affiliate of the Debtor, not the Debtor itself—beyond its rights and the explicit terms of orders of this Court. In fact, the Motion is a collateral effort by Wheeling to obtain a finding on an issue that is the subject of an adversary proceeding brought by Wheeling in this case. *See* Wheeling & Lake Erie Railway Co. v. Keach, et al. (In re Montreal Maine & Atlantic Railway, Ltd.), Adv. Proc. No. 13-1033-LHK (Bankr. D. Me.) (filed October 10, 2013) (the "Adversary Proceeding"). Whether considering Wheeling's claim in the Adversary Proceeding or its request in the Motion, the fundamental reality is the same: the proceeds of the accounts receivable of

MMA Canada are not property of the Debtor, and Wheeling has no right to or interest in them as cash collateral under the Sixth Interim Order Authorizing Debtor to Use Cash Collateral and Granting Adequate Protection [D.E. 376] (the "Sixth Order"), or any of the other cash collateral orders of this Court. The Trustee has complied fully with the Court's cash collateral orders, including the Sixth Order, and the relief demanded by Wheeling in the Motion is unfounded and should be denied.

## ARGUMENT

2. The Trustee and the Debtor have complied fully with each of the Court's cash collateral orders, including the Sixth Order. Among other things, the Sixth Order requires that as of October 18, 2013 (the "Closing Date"), the proceeds of the Debtor's receivables created on or before the Closing Date be segregated and remitted to Wheeling, and that the Trustee provide Wheeling with weekly accounting summaries of such funds. *See* Sixth Order, at ¶ 5. To this day, the Trustee has done and continues to do precisely as the Sixth Order requires.[1] Wheeling seeks performance from the Trustee and Debtor beyond the scope and requirements of the Sixth Order—it demands payment by the Trustee of the accounts receivable proceeds of MMA Canada (the "Canadian A/R"), the Debtor's foreign affiliate and a separate legal entity. Motion, at 1 (emphasis in original).[2] Wheeling justifies its demand by asserting that the Canadian A/R "are accounts receivable ***of the Debtor***" and, therefore, subject to Wheeling's security interest in cash collateral under the Sixth Order. Motion, at ¶ 17 (emphasis in original). However, the Canadian

[1] Since the Closing Date, the Trustee has remitted approximately $1.15 million to Wheeling and another $200,000 has been escrowed for Wheeling's benefit. While $1.35 million may seem like a relatively small percentage of Wheeling's total claim (approximately $6.0 million), Wheeling has fared better than most creditors of the estate at this point in the case. With the exception of some employee-related obligations and some relatively minor pre-petition taxes, most pre-petition claims have not received anything in this case. The Trustee expects that distributions will be made to creditors under a confirmed plan, and the Trustee has been negotiating with certain creditor constituencies about the contours of a plan or plans. Wheeling has opposed every effort by the Trustee to liquidate property of the estate, and the Motion is just the latest maneuver in that campaign.

[2] Capitalized terms not otherwise defined in this Objection shall have the same meaning ascribed to them in the Motion.

A/R is generated by MMA Canada, not the Debtor, and thus is not property of the Debtor's estate or subject to the Sixth Order, which only applies to the Debtor's estate.

3. These facts notwithstanding, Wheeling attempts to employ its motion to enforce a cash collateral order to extract a declaratory judgment regarding the rights of both the Debtor and MMA Canada in the Canadian A/R. Such relief cannot be obtained through the Motion, as it would require separate orders of both this Court and the Quebec Superior of Justice (Commercial Division) (the "Canadian Court"), where MMA Canada has filed for protection under Canada's *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "CCAA"). While Wheeling's rights to the property of the Debtor are currently at issue in the ongoing Adversary Proceeding in this case, the Court has issued no declaration of those rights as yet, and no similar proceeding is before the Canadian Court, nor has MMA Canada been joined in the Adversary Proceeding. The Debtor and MMA Canada are separate and distinct corporate entities, and any determination as to MMA Canada's property rights in the Canadian A/R is within the exclusive jurisdiction of the Canadian Court. A separate declaratory judgment would be necessary from the Canadian Court for Wheeling to establish an interest in the Canadian A/R, and far short of obtaining that, Wheeling has not participated in any meaningful way, if at all, in the CCAA proceeding. In fact, upon information and belief, Wheeling has failed to perfect its security interest in the property of MMA Canada, and thus its status as a secured creditor of MMA Canada is questionable. Furthermore, in light of the cross-border protocol adopted by this Court and the Canadian Court, adjudication of the dispute over the Canadian A/R requires coordination between this Court and the Canadian Court to avoid conflicting rulings and a duplication of efforts.

4. Wheeling attempts to sidestep the CCAA proceeding (perhaps for obvious reasons) by asserting that MMA Canada is essentially an alter ego of the Debtor, and as such, the Canadian A/R is actually the property of the Debtor. It would be an extraordinary feat indeed if

Wheeling were able to substantively consolidate the Debtor with a foreign affiliate through a motion to enforce a cash collateral order in the Debtor's chapter 11 case. Understandably, the Motion does not point to even a hint of legal precedent or authority for such relief in this context.

5. Even in the event the Court determines the Canadian A/R is property of the Debtor, the relief Wheeling requests in the Motion is unavailable to it. First, under the equitable doctrines of waiver, estoppel, and laches, Wheeling has lost any right to object to the Trustee's compliance with the Sixth Order by failing to act for over thirteen weeks, despite having known that the Canadian A/R was not being segregated or remitted, but instead was being used to operate the business. Second, even if Wheeling is able to prevail on all of the claims in the Motion and it rightly may claim the Canadian A/R under the Sixth Order, funds that have already been disbursed cannot be channeled retroactively into a segregated account. At best, Wheeling would be entitled to an allowed superpriority claim under 11 U.S.C. § 507(b), a claim that could and would be paid in full under a confirmed plan.

**A. The Debtor and Trustee Have Complied With Each of the Cash Collateral Orders, Which Do Not Apply to MMA Canada.**

6. The Court has entered six orders granting the Debtor, and then the Trustee, the authority to use Wheeling's cash collateral (the "Cash Collateral Orders"), the presently applicable order being the Sixth Order. [D.E. 51, 98, 173, 255, 374, and 376]. The Debtor and the Trustee have complied fully with each of the Cash Collateral Orders. The first five of the Cash Collateral Orders granted Wheeling adequate protection in the form of replacement liens in "all accounts, inventory, and proceeds of accounts generated by the Debtor on or after the petition date." [D.E. 374]. The Sixth Order mandates the creation of a segregated escrow account to hold "any and all amounts collected by the Trustee, without deduction, from the payments of all accounts receivable that were created at any time prior to the [Closing Date]." Sixth Order, at ¶ 5. The Sixth Order further requires the Trustee to "remit the proceeds of any

and all Pre-Closing A/R to Wheeling on or before the 5th of each month" and extends "the same reporting requirements" as the previous Cash Collateral Orders. Sixth Order, at ¶ 5. Those reporting requirements include the weekly submission of a:

> report on the balances . . . in each of the Debtor's . . . accounts, the balance of the Debtor's accounts receivable, and an aging report of all outstanding accounts receivable, and the balances of all inventory; and . . . a rolling forward projection of sources and uses of cash, and balance sheet accounts for cash, accounts receivable and inventory for the ensuing thirteen (13) week period.

[D.E. 374]. The Trustee has properly escrowed the proceeds of the Debtor's receivables as required, remitted those funds to Wheeling, and circulated the required weekly reports accounting for Wheeling's cash collateral. Attached hereto as **Exhibit A** is a weekly report, submitted to Wheeling on October 25, 2013, showing that the Canadian A/R is not segregated or remitted. Accordingly, as of October 25, Wheeling had notice that the Trustee was not treating the Canadian A/R as Wheeling's cash collateral.

7. Wheeling claims that the Trustee has not complied with the Cash Collateral Orders for failing "to escrow and turn over to Wheeling the proceeds of collection of ***all*** accounts receivable" (emphasis in original), namely, the Canadian A/R, plus "potentially other collections of Wheeling collateral" to which Wheeling fleetingly refers but does not describe further. Motion, at ¶¶ 13, 15. However, as Wheeling correctly observes in the Motion, the Canadian A/R were generated by the provision of services to Canadian customers. As Wheeling admits, the Sixth Order only grants Wheeling a replacement lien "in all accounts receivable generated *by the Debtor*[.]" Motion, at ¶ 8 (emphasis added); *see also* Motion, at ¶¶ 10-11, 13. Furthermore, the Sixth Order was issued by a U.S. bankruptcy court in the Debtor's chapter 11 case—it cannot apply to the foreign property of a foreign affiliate such as MMA Canada. The Debtor and Trustee have properly segregated and remitted only the funds of the Debtor required under the Sixth Order and have therefore complied with the Cash Collateral Orders.

**B. Any Dispute Over the Rights of the Debtor, MMA Canada, and Wheeling in the Canadian A/R Must Be Resolved by Declaratory Judgment.**

8. In an attempt to circumvent the obvious flaw in its argument—that the Canadian A/R is property of MMA Canada, not the Debtor—Wheeling cites testimony and exhibits from an unrelated hearing for the proposition that "it is clear that (a) the so-called Canadian Receivables are accounts receivable ***of the Debtor***; and (b) that the payment proceeds of the same are Wheeling's cash collateral." Motion, at ¶ 17 (emphasis in original). Obviously, the Trustee does not agree that the Canadian Receivables are property of the Debtor. In any case, the issue is not as straightforward as Wheeling suggests. The Debtor is organized under Delaware law. MMA Canada is organized under Nova Scotia law. Each entity has its own bank accounts. MMA Canada has its own employees, and the Debtor has its own employees. MMA files income tax returns in the United States; MMA Canada files its tax returns in Canada. The railroad in Canada is owned by MMA Canada and the railroad in the U.S. is owned by the Debtor. While certain financial information is reported to third parties (including creditors) on a consolidated basis, the Debtor and MMA Canada each have their own general ledgers. Direct items are recorded to each general ledger and adjusting journal entries are made periodically in order to allocate certain corporate items (including freight revenue). MMA Canada does not have its own accounting and finance functions; historically, the Debtor has provided those services in a fairly typical manner. While there is no dispute that the business is integrated, there is no reasonable way to leap immediately—as Wheeling urges—to the conclusion that all of the receivables are owed by the Debtor.

9. While Wheeling may not wish to label its argument as such, Wheeling indeed is arguing that MMA Canada is the alter ego of the Debtor, that MMA Canada should be substantively consolidated with the Debtor, and that the property of MMA Canada, including the Canadian A/R, is property of the Debtor and constitutes Wheeling's cash collateral under the

Sixth Order. A demand of such momentous consequence for two separate legal entities is commonly not found in a motion to enforce a cash collateral order, likely because the necessary findings and adjudications of the Court require significantly more attention, evidence, and consideration.

10. The irony of Wheeling's confidence that "it is clear" that the Canadian A/R is property of the Debtor likely is not lost on the Court, as the Adversary Proceeding initiated by Wheeling has yet to resolve, *inter alia*, this very issue. *See* Adv. Pro. D.E. 18, 26, 28. Even if the dispute concerned only a determination of the property rights in the Canadian A/R as between Wheeling and the Debtor, the relief Wheeling seeks would have to be obtained through a declaratory judgment in the Adversary Proceeding, not through a ruling on the Motion. However, the dispute also involves the rights of MMA Canada in the Canadian A/R, and MMA Canada is not a party to the Adversary Proceeding, so a judgment in that matter still would not be sufficient for Wheeling's requested relief.

11. As the Court is aware, on August 7, 2013, MMA Canada filed for protection from creditors under Canada's CCAA. As set forth in the initial order (the "Initial Order") of the Canadian Court in that proceeding (the "Canadian Case"), a stay was granted precluding any "proceeding or enforcement process" against MMA Canada or any action affecting MMA Canada's "Property" (the "Canadian Stay"). Initial Order, at ¶ 7. The term "Property" is defined in the Initial Order as MMA Canada's "present and future assets, rights, undertakings and properties of every nature and kind whatsoever and wherever situated, including all profits thereof." Initial Order, at ¶ 9. Accordingly, any proceedings affecting MMA Canada's property rights are within the exclusive jurisdiction of the Canadian Court, and such determinations presently are subject to the Canadian Stay. There is no question, therefore, that the relief requested in the Motion, which depends upon an adjudication of both the Debtor's and MMA

Canada's property rights in the Canadian A/R, requires an application to the Canadian Court for either relief from the Canadian Stay or a declaratory judgment as to MMA Canada's rights to the Canadian A/R.[3]

12. Moreover, as the Court is aware, the cross-border protocol (the "Protocol") adopted both by this Court and the Canadian Court, governs the conduct of all parties in interest in the Debtor's case and the Canadian Case. [D.E. 168]. The general purpose of the Protocol is to promote coordination of the cases and to avoid conflicting rulings, and the Protocol contemplates that this Court and the Canadian Court will, as necessary and when appropriate, conduct joint hearings where such a joint hearing may be "necessary or advisable." Protocol, at ¶ 11(d). Adjudication of the dispute over the Canadian A/R requires, if not a joint hearing, coordination between this Court and the Canadian Court at the very least, to avoid precisely the kinds of conflicts and duplication of efforts that could arise from independent resolution of the matter.

13. Thus, the relief requested in Wheeling's Motion not only is improperly before the Court as to the rights of MMA in the Canadian A/R, which should be resolved in the Adversary Proceeding, but such relief cannot be obtained without a separate, and perhaps joint, determination by the Canadian Court as to MMA Canada's rights in the same.

### C. Wheeling Has Waived Its Rights to the Canadian A/R and Its Claim Is Barred By Equitable Estoppel and the Doctrine of Laches.

14. Even in the event that the Court determines Wheeling to have an interest in the Canadian A/R, the Motion must nevertheless be denied due to Wheeling's excessive delay in prosecuting its rights under the Sixth Order. Under three separate equitable doctrines—waiver,

[3] The Trustee also notes that the Initial Order grants MMA Canada's legal counsel or other professionals a security in MMA Canada's Property, as defined therein (the "Administrative Charge"). *See* Initial Order, at ¶ 41. Any rights the Canadian Court may determine Wheeling to have with respect to the Canadian A/R, therefore, are likely to be eliminated by operation of the Administrative Charge.

equitable estoppel, and laches—Wheeling cannot now enforce a right that it knew it had thirteen weeks ago and failed to assert every week since.

15. First, a party may waive its right to enforce an obligation of another if the party acts in a way "inconsistent with an intent to enforce that right." Saverslak v. Davis–Cleaver Produce Co., 606 F.2d 208, 213 (7th Cir. 1979); *see also* In re Baptiste, 430 B.R. 507, 511-12 (Bankr. N.D. Ill. 2010) (holding that plaintiff "acted in a manner inconsistent with intent to enforce contract provisions as to payment" by refusing to act upon twenty-one separate improper payments and thus had waived its rights). Waiver is an equitable principle designed to "prevent a party from insisting on a right upon which he could have insisted earlier but has been found to have surrendered." L. Orlik Ltd. v. Helme Prods. Inc., 427 F. Supp. 771, 776 (S.D.N.Y. 1977); *see* Gonyea v. John Hancock Mut. Life Ins. Co., 812 F. Supp. 445, 450 (D. Vt. 1993). The First Circuit has recognized waivers in circumstances similar to those presented here, where a secured creditor has failed to take necessary action to protect its rights to collateral. *See* In re Cross Baking Co., Inc., 818 F.2d 1027 (1st Cir. 1987). In Cross Baking, the First Circuit found that the secured creditor failed to seek or obtain a cash collateral order that extended its lien to post-petition account receivables, and ruled that the secured creditor therefore did not have a lien on "the cash generated by [the debtor's] post-petition receivables." Id., at 1032.

16. Second, in the event that enforcement of a previously unenforced right by a party would negatively prejudice the counterparty, and the counterparty has acted in reliance on the right not being enforced, equitable estoppel may lie against the enforcing party even absent intent to waive. *See* Saverslak, 606 F.2d at 213; Beneficial Finance Co. of Virginia v. Lazrovitch, 47 B.R. 358, 363 (D.D.C. 1983) (holding that equitable estoppel only requires "that the person estopped, by his statements or conduct, misled another to his prejudice"); In re Lafayette Radio Electronics Corp., 7 B.R. 189, 193 (Bankr. E.D.N.Y. 1980) (stating that a

bankruptcy court "inherently possesses the powers of equity [and] it may employ the equitable estoppel doctrine in a manner not inconsistent with the Code").

17. Third, the equitable doctrine of laches allows a court to dismiss a claim "where a party's delay in bringing suit was (1) unreasonable, and (2) resulted in prejudice to the opposing party." Iglesias v. Mutual Life Ins. Co., 156 F.3d 237, 243 (1st Cir. 1998). As with waiver and equitable estoppel, laches is an equitable doctrine, and a bankruptcy court "should invoke equitable principles and doctrines, refusing to do so only where their application would be 'inconsistent' with the Bankruptcy Code." In re Myrvang, 232 F.3d 1116, 1124 (9th Cir. 2000) (*citing* SEC v. United States Realty & Improvement Co., 310 U.S. 434, 455 (1940)). Thus, "the equitable doctrine of laches, which has as its goal the prevention of prejudicial delay in the bringing of a proceeding, is a relevant and necessary doctrine in the bankruptcy context." In re Beaty, 306 F.3d 914, 922 (9th Cir. 2002).

18. Here, Wheeling was aware in October 2013 that the Trustee did not consider the Canadian A/R to be property of the Debtor and subject to Wheeling's security interest, and thus, the claim that Wheeling now pursues arose months ago. As Wheeling acknowledges, the Trustee and/or his professionals have provided Wheeling with weekly reports regarding the Debtor's accounts receivable (the "Summaries") since October 25, 2013, pursuant to the Sixth Order. *See* Motion, at ¶ 12. The Summaries clearly indicate that the Trustee is retaining and using the proceeds of the Canadian A/R, and specifically, the Summaries identify certain amounts, including the proceeds of the Canadian A/R, as "Deposits not Escrowed." *See* Exhibit A. Having received the Summaries, Wheeling was therefore on notice, as of October 25, 2013, that the proceeds of the Canadian A/R were not being segregated as cash collateral pursuant to the Sixth Order. Likewise, the Trustee has not been remitting any of those funds to Wheeling as part of its monthly payments under the Sixth Order.

19. Yet, Wheeling only now seeks to enforce its rights under the Sixth Order with respect to the Canadian A/R. Wheeling's motivation for delay in the prosecution of its claim may be illuminated by the current status of the Adversary Proceeding. Wheeling has not achieved its goal in the Adversary Proceeding, which was stayed on January 21, 2014 [Adv. Pro. D.E. 28], and suddenly has awakened to its alleged rights under the Sixth Order, seeking to use enforcement of those rights as a proxy to adjudicate a substantive consolidation. Meanwhile, the Debtor and MMA Canada have proceeded with their use of receivables and cash collateral under the belief that Wheeling has no rights to the Canadian A/R and that, by its failure to object to thirteen separate Summaries stating so, Wheeling agreed.

20. It would be inequitable for Wheeling to obtain relief after such an unreasonable delay, and the Debtor would certainly be prejudiced by the immense disruption to the Debtor's post-petition finances that surely would result from granting Wheeling's demand. Wheeling conveyed an intent to waive its rights under the Sixth Order by receiving thirteen payments and weekly statements clearly omitting the Canadian A/R and failing to raise an objection at any point. Wheeling likewise should be equitably estopped from enforcing its rights, regardless of its intent to waive them, because the Debtor and the Trustee have relied on Wheeling's failure to object as an implicit agreement that the Canadian A/R was not subject to the Sixth Order, and the Debtor would be significantly prejudiced and damaged by the sudden enforcement of those rights. Finally, because of Wheeling's unreasonable idleness and the substantial prejudice that the Debtor would suffer, the doctrine of laches demands that Wheeling forfeit any rights to the Canadian A/R under the Sixth Order.

**D. Wheeling's Claim Under the Motion, If Any, Should Be Limited to a Superpriority 507(b) Claim.**

21. In the event that the Court determines Wheeling to have an interest in the Canadian A/R, the proper avenue for Wheeling to collect on that claim is through asserting a

superpriority 507(b) claim. There is no dispute that the Trustee and Debtor have not segregated the Canadian A/R, and thus those funds have been used for the continuing operation of MMA Canada—they are not *available* for collection by Wheeling even if it is victorious in its Motion. However, section 507(b) allows for "priority over every other claim allowable" where, despite adequate protection securing a claim, such protection proves inadequate and the stay of action against the collateral results in a claim under section 507(a)(2). 11 U.S.C § 507(b).

22. To the extent that MMA Canada's use of the Canadian A/R creates such a claim for Wheeling, that claim will be entitled to superpriority status, and there is no reason to believe that it would not be paid under a confirmed plan. In fact, this is precisely the relief established for Wheeling in the Sixth Order:

> If, notwithstanding the grant of adequate protection provided in this Order, Wheeling has a claim arising under Section 507(b) of the Bankruptcy Code, from the use of Cash Collateral pursuant to this Order and allowable under Section 507(a)(2) of the Bankruptcy Code, then, such claim shall have priority over all other claims arising under Section 507(b) and all claims allowable under Section 507(a)(2).

Sixth Order, at ¶ 10. Thus, in the event that Wheeling is successful on the Motion, Wheeling's relief must be limited to the assertion of a superpriority claim under section 507(b).

23. Additionally, the extent of Wheeling's superpriority claim under section 507(b) cannot be determined summarily. The purpose of a superpriority claim is to compensate the holder of a secured claim when a prior award of adequate protection fails. *See* 11 U.S.C. § 507(b). Adequate protection is designed to ensure that the secured creditor's position is not eroded as a result of the imposition of the automatic stay. Accordingly, the Court would need to determine, based on evidence, two amounts: first, the amount that Wheeling would have realized on account of its collateral in the absence of the automatic stay, and second, the amount that Wheeling actually has realized on account of its secured claim. Wheeling would only be entitled to an allowed superpriority claim if—and then only to the extent that—the first amount

is greater than the second amount. Those determinations cannot be made by the Court based solely on the allegations in the Motion. There are several reasons why that is true, including, without limitation, that Wheeling's asserted rights in other collateral have not been determined and there is not a shred of evidence regarding what Wheeling would have received if it had been able to liquidate its collateral under state law in the absence of a bankruptcy filing.

## CONCLUSION

WHEREFORE, the Trustee requests that this Court deny the Motion at a hearing on March 12, 2014. In the event that the Court does not so deny the Motion, the Trustee requests that the Court treat the issue as a contested matter and schedule a final evidentiary hearing and grant other relief as this Court may deem just and proper.

Dated: March 5, 2014

ROBERT J. KEACH,
CHAPTER 11 TRUSTEE OF MONTREAL MAINE & ATLANTIC RAILWAY, LTD.

By his attorney:

*/s/ Michael Fagone, Esq.*

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