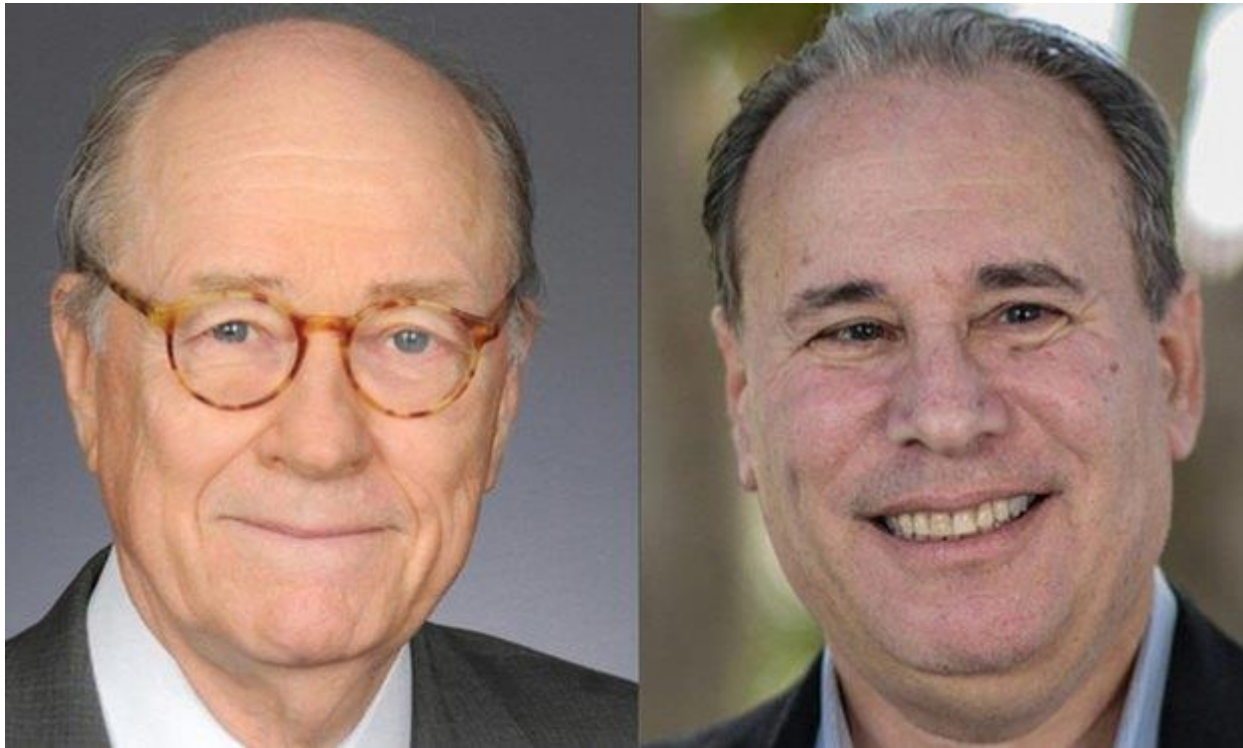


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How Extraordinary Is Extraordinary? Discretionary Limitations on Attachments

In their International Litigation column, Lawrence W. Newman and David Zaslowky discuss a recent decision of the U.S. Court of Appeals for the Second Circuit that opens the door for district courts to consider, in addition to the requirements of New York's attachment statute, "extraordinary circumstances," such as the potential impact of the proposed attachment on third parties as well as public policy

By **Lawrence W. Newman and David Zaslowky** | December 1, 2022 at 10:00 AM



As important as it is to have an award or judgment in one's favor, securing its enforcement is usually of equal importance to avoid achieving no more than a Pyrrhic victory. There is anecdotal and case evidence suggesting that arbitration award debtors today may be more unwilling or unable to pay awards than was the case decades ago. It, therefore, may be crucially important for a claimant, in anticipation of such a situation, to obtain an attachment of its respondent's assets in advance of an award in the claimant's favor. Although obtaining such a prejudgment attachment is a matter of complying with statutory requirements, a recent Second Circuit case, *Iraq Telecom Ltd. v. IBL Bank S.A.L.*, 43 F.4th 263 (2d Cir. 2022), allows courts to consider more subjective elements – ones described by the court as "extraordinary circumstances."

Rule 64 of the Federal Rules of Civil Procedure authorizes remedies like attachment to secure satisfaction of a potential judgment but defers the requirements for such relief to "the law of the state where the court is located." In New York, the CPLR permits a claimant in an existing or expected arbitration to obtain an attachment of a respondent's assets in aid of arbitration if the claimant shows: (i) a cause of action; (ii) a likelihood of success on the merits in the arbitration; (iii) that the amount of the claim exceeds any meritorious counterclaim; and, (iv) that the arbitral award may be rendered ineffectual absent an attachment. CPLR §§6201, 6212, and 7502(c).

These are the so-called "statutory factors." However, some parties have asked the courts to consider other factors ("non-statutory factors"), including the deleterious effect that the requested attachment will arguably have on persons apart from the respondent against whose assets relief is sought. For example, in *Capital Ventures Intl. v. Republic of Argentina*, 443 F.3d 214 (2d Cir. 2006) (*Capital Ventures I*), the Second Circuit upheld an order of attachment obtained by the plaintiff of Argentina's reversionary interest in the collateral securing payment of certain Argentine bonds. The Second Circuit determined that, since the statutory requirements to grant an attachment were satisfied, the district court did not have discretion to deny issuing an order of attachment to permit an exchange between holders of the bonds and Argentina "for some other reasons, at least absent extraordinary circumstances and perhaps even then." Because the Second Circuit saw no extraordinary circumstances, it did not address whether New York law allows discretionary denial of an otherwise appropriate attachment.

Later, in a proceeding dealing with a continuation of the dispute between Argentina and its creditors, *Capital Ventures Intl. v. Republic of Argentina*, 652 F.3d 266 (2d Cir. 2011) (*Capital Ventures II*), the district court modified the order of attachment that was the subject of *Capital Ventures I* because it was preventing Argentina and its bondholders from doing an exchange that would have as a side effect the taking away a reversionary interest in the collateral which Capital Ventures had attached. The district court modified the attachment order to permit the exchange deal. The Second Circuit reversed, finding that there were no "extraordinary circumstances." The fact that holders of Argentine bonds would have to wait another 12 years to access the collateral was "unfortunate" but not "dire" because they would ultimately get no less than what they bargained for. The court also rejected an argument based on Argentina's sovereign interest in "cleaning up" its balance sheet amid an economic crisis. The court said that there was no showing that an exchange amounting to roughly \$100 million dollars would substantially affect Argentina's finances.

In *Capital Ventures II*, the Second Circuit said it was again leaving open the issue of whether New York law allows discretionary denial (or modification or vacation) of an otherwise appropriate attachment based on public policy.

Now, more than a decade later, in *Iraq Telecom*, the Second Circuit has answered in the affirmative the question left open in *Capital Ventures*. The factual background of *Iraq Telecom* is complex but may be briefly summarized as follows. Iraq Telecom and Korek International, owned by a Mr. Barzani, were business partners. They owned 44% and 56% of the shares, respectively, of IHL, a company that owned Korek Telecom. Iraq Telecom lent \$285 million to Korek Telecom (through IHL). Later, IBL Bank (Lebanon) lent \$150 million to Korek Telecom. Iraq Telecom agreed to subordinate its loan to the IBL loan, as required by IBL. Barzani told Iraq Telecom that the IBL loan was unsecured, so Iraq Telecom agreed to the subordination. After Korek Telecom defaulted on its loan to IBL, it invoked the subordination agreement to stop paying Iraq Telecom, paying IBL Bank instead. Iraq Telecom later discovered that IBL Bank and Barzani had devised a scheme to defraud Iraq Telecom into subordinating its loan, to their mutual benefit. IBL secretly paid Barzani the interest Korek Telecom paid to IBL.

In 2018, Iraq Telecom brought an arbitration proceeding against IBL, Korek International, and IHL in Lebanon. Although Iraq Telecom initially sought damages, it later withdrew that claim and sought only declaratory relief "to eliminate any argument regarding double-recovery issues" in other proceedings.

In this first arbitration, in an award issued in 2021, the arbitral tribunal declared that IBL Bank had defrauded Iraq Telecom through a scheme that included IBL, IHL, and Korek International (owned and controlled by Barzani). Under the scheme, Iraq Telecom was deprived of \$97 million, representing interest payments that Korek Telecom made to IBL Bank that, but for the subordination agreement, would have been paid to Iraq Telecom. The award also declared that IBL paid to Barzani part of the \$148 million (\$5.92 million) paid by Korek Telecom to IBL. The award in this first arbitration also ordered IBL, IHL, and Korek International to pay \$3 million to Iraq Telecom in "attorney's fees," "jointly and severally."

In light of the tribunal's declaration in the first arbitration, Iraq Telecom brought a second arbitration, seeking \$97 million in damages from IBL. In connection with that arbitration, Iraq Telecom obtained an *ex parte* attachment order from the district court in New York against IBL Bank for \$100 million (comprising the \$3 million attorney's fees awarded in the first arbitration plus the \$97 million in damages sought in the second arbitration). As a result, Iraq Telecom was able to attach \$42 million in accounts that IBL Bank held in four New York banks.

Iraq Telecom initiated, as required under New York law, a proceeding to confirm the attachments and also moved to expand the attachment order to include all of IBL Bank's property in the Southern District of New York (without specifying an amount). IBL Bank opposed the motion and cross-moved to vacate the *ex parte* attachments. In response, the district court reduced the amount to "no more" than \$8.92 million, and then further reduced it to \$3 million. Why? Among other reasons, because of "extraordinary circumstances," such as the possibility that IBL Bank would be forced into insolvency, which could adversely affect Lebanon's "fragile" economy, and possibly undermine "confidence in New York's financial institutions."

More specifically, Lebanon was suffering from an economic crisis, part of which concerned severe foreign currency shortages. In response, the Lebanese central bank issued circulars requiring Lebanese banks to maintain the "liquidity necessary" in their offshore accounts to service withdrawals in U.S. dollars. According to the district court, IBL intended this liquidity to come from its bank accounts in New York. The court said that "[t]he continued attachment of \$42 million will cause IBL to fall out of compliance with crisis management regulations" imposed by the Lebanese central bank. Also, without access to the attached correspondent accounts, IBL would not be able to provide the international banking services in U.S. dollars on which its depositors rely. The district court held that these ancillary effects were a sufficient basis for the court to exercise discretion to refuse to confirm the attachment order.

On appeal, Iraq Telecom argued that the district court lacked authority, under applicable statutory law, to consider "extraordinary circumstances" to reduce the amount of the attachments. The Second Circuit explained that it had left this issue open in *Capital Ventures*. However, based on state court decisions and treatises that highlight the discretion given to courts in granting attachments, and a specific decision that held a court could consider the impact of an attachment on third parties, the Second Circuit held that a court has discretion to weigh extraordinary circumstances, even where the statutory requirements for attachment are satisfied.

As to the specific exercise of that discretion, recall that, in *Capital Ventures I* and *II*, which concerned property of the Republic of Argentina itself, the Second Circuit held that there was not a sufficient showing of "extraordinary circumstances" that could open the door for consideration of non-statutory factors.

In *Iraq Telecom*, in contrast, even though the attached bank accounts were those of a private bank and not of the government of Lebanon itself, the district court held that IBL satisfied the extraordinary circumstances standard.

The Second Circuit said that the district court's decision had weighed "fair considerations" that could be regarded as the kind of non-statutory "extraordinary circumstances" that courts may consider in determining whether to grant orders of attachment. The Second Circuit regarded as the important non-statutory considerations (i) the effect of attachments on the economy of the respondent's country and on "innocent third parties" and (ii) the impact of the attachments on the public confidence in New York's financial institutions.

At the same time, however, the district court abused its discretion in reducing the attachment to \$3 million. According to the Second Circuit, the district court's analysis was sufficient to hold that the attachment of \$42 million should be modified. But it had not sufficiently shown whether there was some amount that could be attached between \$3 million and \$42 million that might change the "extraordinary circumstances" analysis.

The significance of the *Iraq Telecom* decision is that, about 10 years after *Capital Ventures I* and *II*, the Second Circuit has now held that a district court may consider non-statutory factors when applying New York law to rule on attachment applications. We know that circumstances that have a potentially severe effect on a nation's

economy and/or have a negative impact on "confidence in New York's financial institutions" are the types of "extraordinary circumstances" that can be considered.

At the other end of the spectrum, every attachment of a debtor's assets affects other creditors, because there are fewer assets of the debtor for them to go against. Thus, one may query whether this consequence, by itself, should be a proper basis for a court to interfere with the normal application of the statutory attachment factors. Now that the door has been open, it will be interesting to see how "extraordinary" a set of circumstances the courts will require.

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