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IN THE SUPREME COURT OF THE STATE OF DELAWARE

QUADRANT STRUCTURED PRODUCTS COMPANY, LTD., Individually and Derivatively on Behalf of Athilon Capital Corp.,	)	No. 338,2012
Plaintiff Below/Appellant,	)	Case Below:
v.	)	Court of Chancery Civil Action No. 6990-VCL
VINCENT VERTIN, MICHAEL SULLIVAN, PATRICK B. GONZALEZ, BRANDON JUNDT, J. ERIC WAGONER, ATHILON CAPITAL CORP., ATHILON STRUCTURED INVESTMENT ADVISORS LLC, and EBF & ASSOCIATES, LP,	)	
Defendants Below/Appellees.	)	

APPELLEES' ANSWERING SUPPLEMENTAL MEMORANDUM

Collins J. Seitz, Jr. (#2237)
Garrett B. Moritz (#5646)
Eric D. Selden (#4911)
SEITZ ROSS ARONSTAM & MORITZ LLP
100 S. West Street, Suite 400
Wilmington, DE 19801
(302) 576-1600

Attorneys for Defendant Below/Appellee EBF & Associates, LP

Philip A. Rovner (#3215)
POTTER ANDERSON & CORROON LLP
Hercules Plaza
P.O. Box 951
Wilmington, DE 19899-0951
(302) 984-6000

OF COUNSEL:

Philippe Z. Selendy
Nicholas F. Joseph
Sean P. Baldwin
QUINN EMANUEL URQUHART & SULLIVAN, LLP
51 Madison Avenue, 22nd Floor
New York, New York 10010-1601
(212) 849-7000

Dated: August 9, 2013

Attorneys for Defendants Below/Appellees Athilon Capital Corp., Athilon Structured Investment Advisors LLC, Vincent Vertin, Michael Sullivan, Patrick B. Gonzalez, Brandon Jundt and J. Eric Wagoner

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PRELIMINARY STATEMENT

In the decision under appeal, the Court of Chancery, relying on well-established Delaware authority interpreting New York law, correctly dismissed all claims of Plaintiff Below/Appellant Quadrant Structured Products, Ltd. ("Quadrant") against Defendants Below/Appellees Vincent Vertin, Michael Sullivan, Patrick B. Gonzalez, Brandon Jundt, J. Eric Wagoner, Athilon Capital Corp. ("Athilon"), Athilon Structured Investment Advisors LLC, and EBF & Associates, LP (collectively, "Defendants"), because Quadrant had not complied with the applicable no-action clause. This Court remanded for consideration of a single question, which the Court of Chancery made clear was never raised by Quadrant in opposition to the original motion to dismiss: "the significance (if any) under New York law of the differences between the no-action clauses in the *Lange* and *Feldbaum* indentures and the Athilon Indenture." Remand Order (D.I. 39), Feb. 12, 2013, at 5. The answer to this question has been provided by the courts of New York: none. In coming to the contrary conclusion in its June 20, 2013 Report Pursuant to Delaware Supreme Court Rule 19(c) (D.I. 42) ("Report"), the Court of Chancery did not apply that precedent, gave no effect to more than two-thirds of the language in the no-action clause, failed to take into account any other provisions in the Indenture, and created confusion in an otherwise settled area of law. The Court of Chancery's original dismissal should be affirmed.

ARGUMENT

I. ALL OF QUADRANT'S CLAIMS ARE BARRED BY THE NO-ACTION CLAUSE

A. The Plain Language Of The No-Action Clause Bars All Of Quadrant's Claims Because They Are Common To All Noteholders

The plain language of the Athilon no-action clause covers every claim a noteholder holds as a noteholder, whether contractual or otherwise, according to New York state and Delaware authority applying New York law. Each of the three parts of this clause encompasses rights held by noteholders by virtue of their status as noteholders—not just claims for breach of the Indenture, as Quadrant contends. *See* Appellees' Supplemental Appendix ("ASA") at 61-63 (Defendants' Opening Brief Regarding Issues On Remand).

First (adopting the Report's terminology), subpart 1.0, which reads "[a]ny right by virtue or by availing of any provision of this Indenture," Report at 11, captures any claim that derives from a noteholder's status as a noteholder and cannot be limited to claims "availing of" the Indenture—that is, to claims for breach of the Indenture. As Vice Chancellor Glasscock held, this phrase standing alone covers a non-contractual claim because "'by virtue of the Indenture' indicates coverage of such causes of action available to a plaintiff by virtue of its status as a Note holder." *Tang Capital Partners v. Norton*, 2012 WL 3072347 at *5 (Del. Ch. July 27, 2012). Otherwise, these two phrases – "by virtue . . . of" and

"availing of" – would have the same meaning, rendering one of them superfluous. *Id.*[1] As the Court of Chancery acknowledged, Report at 45, such a construction is not permissible under New York law, which requires that courts "give meaning to every sentence, clause and word" of a contract, *Travelers Cas. and Sur. Co. v. Certain Underwriters at Lloyd's of London*, 760 N.E.2d 319, 326 (N.Y. 2001), and holds that "an interpretation which renders language in the contract superfluous is unsupportable," *Suffolk Cty. Water Auth. v. Vill. of Greenport*, 800 N.Y.S.2d 767 (N.Y. App. Div. 2005). *Second*, subpart 2.0 covers "any action or proceeding at law or in equity or in bankruptcy or otherwise." Report at 11. The New York Supreme Court explicitly held that this phrase broadly defined the scope of a materially identical no-action clause. *Greenwich Fin. Servs. v. Countrywide Fin. Corp.*, No. 650474/2008, slip op. at 6-7 (N.Y. Sup. Ct. Oct. 7, 2010).[2]

Third, subpart 3.0 covers "any right . . . upon or under or with respect to this Indenture." Report at 11. This includes any right a noteholder has (or alleges it has) relating to the Indenture – in other words, every right a noteholder possesses. This phrase is similarly not limited to breaches of the Indenture, which would be

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[1] In certifying *Tang* for appeal to this Court, Vice Chancellor Glasscock made clear that he was not persuaded by the Report. *See Tang Capital Partners LP v. Norton*, C. A. No. 7476, Letter Opinion at 6 n.14 (Del. Ch. July 12, 2013).

[2] The no-action clause provided in relevant part: "No Certificateholder shall have *any right by virtue or by availing itself of any provisions of this Agreement* [the Pooling and Servicing Agreement] to institute *any suit, action or proceeding in equity or at law upon or under or with respect to this Agreement . . .*" *Id.* (emphases added).

covered if the no-action clause merely applied to "any right . . . under this Indenture." *See Travelers Cas.*, 760 N.E.2d at 326. The other two phrases – "upon or . . . with respect to this Indenture" – necessarily capture more than simple claims for breach of the Indenture. Otherwise, they would be rendered superfluous, an "unsupportable" interpretation of the contract. *Suffolk Cty.*, 800 N.Y.S.2d at 767.

The reading of the no-action clause put forward by Quadrant, by contrast, fails to give any meaning to more than two-thirds of the language. *See* ASA at 63-64, 80-83 (Defendants' Reply Brief Regarding Issues On Remand). According to Quadrant, subpart 1.0 alone defines the actions to which the no-action clause is applicable: those seeking to enforce breaches of the Indenture. Under Quadrant's reading, subparts 2.0 and 3.0 of the clause—including the bar on requests for receivership—have no effect on its coverage and could be stricken from the clause with no effect on its meaning, which, as the Court of Chancery recognized, is contrary to New York law. Report at 45-46. Quadrant's excision of subpart 2.0 from the no-action clause is also expressly contradicted by *Greenwich*, which defined the scope of a materially identical no-action clause not by looking to subpart 1.0, as Quadrant does, but to subpart 2.0. *Greenwich Fin. Servs.*, No. 650474/2008, slip op. at 6-7.

Finally, in its parsing of subpart 1.0, Quadrant provides no meaning at all to the phrase "by virtue or by availing of." Quadrant belatedly attempted to remedy

this defect on remand; but its interpretation was absurd, the Court of Chancery did not accept it, and Quadrant does not advance it here. Instead, the Court of Chancery frankly acknowledged that Quadrant's interpretation renders this language superfluous. Report at 45-46.

Under Quadrant's reading, then, the operative portion of the no-action clause could be reduced to "No holder of any Security shall have any right by availing of any provision of this Indenture to institute any action unless . . ." – removing a total of 44 words, more than two thirds of the clause – without changing its meaning at all. Such a reading is improper under New York law. *Beal Sav. Bank v. Sommer*, 865 N.E.2d 1210, 1213 (N.Y. 2007) ("[t]he court should 'construe the agreements so as to give full meaning and effect to the material provisions,'" and "[a] reading of the contract should not render any portion meaningless."). Under "established precedent," courts must "give meaning to every *sentence, clause and word* of a contract." *Travelers Cas.*, 760 N.E.2d at 326 (emphasis added). Against this uniform authority, the Court of Chancery cites a contrary Delaware Court of Chancery case and a writing guide, Report at 46, neither of which can contradict well-established New York law, as articulated by New York State's highest court.

B. The Absence Of "Securities" From The No-Action Clause Does Not Affect Its Coverage

In defense of its decision to assign no meaning to a significant part of the no-action clause, the Court of Chancery first inserts the phrase "or the Notes" into the

Athilon no-action clause, and then asserts that Defendants' reading of "by virtue or by availing" makes "or the Notes" inoperative. Report at 45. But this argument misunderstands the contractual interpretation proffered by Defendants, and does not take into account the definition of "Securities" in the Indenture.

First, this explanation requires inserting language from the *Feldbaum* no-action clause, which makes particularly little sense here because the Athilon no-action clause contains broadening language not present in the *Feldbaum* clause.[3] This broadening language—"by virtue or by availing"—is the functional equivalent of, and a *substitute for* the alternative phrase "or the Notes." This scope is confirmed by the broadening language in the rest of the clause, none of which Quadrant mentions.

Second, the Indenture and New York authority confirm "Indenture" is the broader term, and that it encompasses the term "Securities." Under the Indenture here, "Securities" is defined as "the Series A and the Series B Notes." Appendix to Appellant's Opening Brief ("Op. App'x") (D.I. 11) at A91, 188. Quadrant's assertion that this definition does not refer to the Indenture, Appellant's Supp. Mem., (D.I. 47) at 5, is belied by a turn of the page. The Indenture goes on to

[3] The Court of Chancery asserts that *Tang* violates the no-surplusage rule because "[i]f applied to a no-action clause that already included [the words 'or the Notes'], the reasoning in *Tang* would render them meaningless because the phrase 'by virtue of . . . the Indenture' takes care of the note-based claims." Report at 45. But the no-surplusage rule directs the Court to give meaning to every word in the contract at issue, not to other contracts between other parties. *See Travelers*, 760 N.E.2d at 326.

define "Series A Notes" as "the Subordinated Deferrable Interest Notes, Series A, in the aggregate principal amount of $75 million, authenticated and delivered *under this Indenture*," Op. App'x at 92, 188 (emphasis added), and "Series B Notes" substantively identically. Op. App'x. at 92, 188.

Third, securities are creatures of the indenture, as New York courts have long held. *See, e.g.*, *Greene v. New York United Hotels*, 260 N.Y.S. 405, 407 (N.Y. App. Div. 1932) (dismissing bondholder complaint in its entirety because plaintiff "holds his securities subject to the condition of this underlying trust agreement and can maintain an action only upon the conditions specified in the trust agreement."), *aff'd*, 185 N.E. 798, 799 (N.Y. 1933); *Relmar Holding Co. v. Paramount Publix Corp.*, 263 N.Y.S. 776, 778 (N.Y. Sup. Ct. 1932) (same). "Indenture" is thus the broader term and encompasses "Securities."

Fourth, New York courts do not require parties to use particular "magic words" in order to obtain the contractual coverage they desire, *Lerner v. Lerner*, 508 N.Y.S.2d 191, 194 (N.Y. App. Div. 1986) ("The law has outgrown its primitive stage of formalism when the precise word was the sovereign talisman, and every slip was fatal.") (quoting *Wood v. Lucy, Lady Duff-Gordon*, 118 N.E. 214, 214 (N.Y. 1917) (Cardozo, J.)), but instead look to the intentions of the parties, as expressed by the language they chose and the purpose for which they chose it, *Wuhan Airlines v. Air Alaska, Inc.*, 1998 WL 689957, at *3 (S.D.N.Y.

Oct. 2, 1998). Quadrant's insistence that only the insertion of "Securities" can cover its claims is thus contrary to New York law.[4]

C. New York State Authority Establishes The Broad Coverage Of The No-Action Clause

No speculation, historical exhumation, or scholarly recourse is necessary to determine how a New York State court would interpret the no-action clause here. The New York Supreme Court, affirmed by the Appellate Division, clearly stated the rule this Court must follow: *Feldbaum*.

In *Walnut Place v. Countrywide Home Loans* ("*Walnut Place I*"), 2012 WL 1138863 (N.Y. Sup. Ct. Mar. 28, 2012), *aff'd*, *Walnut Place II*, 948 N.Y.S.2d 580, 581 (N.Y. App. Div. 2012), the New York Supreme Court held that a no-action clause materially identical to the one here (and notably referring only to the governing agreement, not the securities) barred an attempt by certificateholders to bring a derivative claim on behalf of the trust for breach of the governing contract, the Pooling and Servicing Agreement ("PSA"). While the action was based on a breach of the PSA, plaintiffs did not pursue this breach under the contract, but rather derivatively, based on their status as certificateholders. *See Walnut Place I*, 2012 WL 1138863 at *1. *Walnut Place* thus considered a certificateholder status

[4] Any doubt as to the coverage of the no-action clause is resolved by the Private Placement Memoranda for the Securities, which say that no-action clauses cover "rights under the Indenture and the Notes," the exact language Quadrant asserts is required to cover its claims. Joint Appendix To Appellees' Answering Briefs ("Ans. App'x") (D.I. 19) at B266 and 373.

claim, just like the noteholder status claims Quadrant asserts here, in that the plaintiffs had the right to bring their derivative claim solely on the basis of their ownership of the certificates—not under the contract. The Supreme Court dismissed the claim and explicitly endorsed "the holding in *Feldbaum v. McCrory Corporation, supra,* 1992 WL 119095 at *6–7, in which the Court, applying New York law, upheld a no-action clause providing that securityholders must give notice of an Event of Default, on the grounds that 'if the trustee is capable of satisfying its obligations, then any claim that can be enforced by the trustee on behalf of all bonds . . . is subject to the terms of a no-action clause.'" *Walnut Place I,* 2012 WL 1138863 at *5. The Court further explained that the only exception to this rule was when the plaintiff alleged misconduct against the trustee. *Id.* at *5-6. The Appellate Division affirmed. *Walnut Place II,* 948 N.Y.S.2d at 581.

Similarly, in *Emmet & Co. v. Catholic Health E.*, 951 N.Y.S.2d 846 (N.Y. Sup. Ct. 2012), interpreting a no-action clause which barred actions "to enforce the Indenture," *id.* at 849, the New York Supreme Court explicitly endorsed the rule in *RBC Capital Mkts., LLC v. Educ. Loan Trust IV*, 2011 WL 6152282 (Del. Ch. Dec. 6, 2011), following *Feldbaum*: "'[i]f a predicate to recovery is proving a breach of legal obligations other than those directly addressing the payment of principal and interest,' then the no-action clause applies," *Emmet*, 951 N.Y.S.2d at 851.

Neither the New York Supreme Court nor the Appellate Division distinguished the types of claims covered by the no-action clause, much less by parsing the clause as Quadrant does. This is consistent with *Feldbaum*, which, as the Court of Chancery recognized, held that "a no-action clause would apply to any remedy sought on behalf of all bondholders." Report at 24. Were a New York State court addressing Quadrant's claims, then, it would ask whether (1) the remedy was sought on behalf of all noteholders, (2) the trustee was capable of bringing the claims the plaintiff asserts, and (3) the trustee was disabled by a conflict. As explained below, the answer to the first and second questions here is yes; to the third, no. The no-action clause thus bars all of Quadrant's claims.

First, there is no dispute that Quadrant seeks remedies on behalf of all noteholders. The Court of Chancery explicitly found as much, Report at 47-54, and Quadrant has never disputed the point.

Second, the Trustee could bring Quadrant's claims under at least two provisions of the Indenture. All Quadrant was required to do was make a proper demand. The first is the no-action clause itself.[5] The requirement of demand in a

[5] The no-action clause requires notice only of a "default," not the defined term "Event of Default," and Quadrant has conceded that this at least includes a breach of the Indenture that does not rise to an Event of Default. Appellant's Consol. Reply Br. (D.I. 29) at 7. Quadrant has alleged such a breach: of the covenant of good faith and fair dealing, in Count VII, which is a breach of contract. *See, e.g.*, *ABN AMRO Bank v. MBIA Inc.*, 952 N.E.2d 463, 475 (N.Y. 2011). The Court of Chancery agreed this claim was based on a breach of the Indenture, and recommended it be dismissed. Report at 50-52. Quadrant has offered no argument in opposition to dismissal, and, consequently, the claim should be dismissed.

no-action clause implicitly recognizes the power of the Trustee to bring suit upon proper demand. *Van Wezel v. McCord Radiator*, 20 N.Y.S.2d 91, 97 (N.Y. City Ct. 1939) ("provisions barring bondholders from resorting to the courts other than through the trustee naturally result in the conclusion that the trustee has discretion to do what is forbidden to bondholders in order to 'enforce any right' 'with respect to the debentures or coupons'"); *U.S. Bank Nat'l Ass'n. v. U.S. Timberlands Klamath Falls, LLC* ("*Timberlands II*"), 864 A.2d 930, 941-42 (Del. Ch. 2004).

The second provision under which Quadrant could have brought its claims (through proper demand) is Section 7.08 of the Indenture, which provides that noteholders may direct the Trustee to take any action, including bringing suit, without limitation: "the holders of a majority of the aggregate principal amount of such series of Securities at the time Outstanding shall have the right to direct the time, method, and place of conducting any proceeding for any remedy available to the Trustee, or exercising any trust or power conferred on the Trustee by this Indenture," under certain conditions. Op. App'x. at 132-133, 230.[6]

Third, Quadrant has never alleged – nor could it – that the Trustee would be unable to pursue its claims due to a conflict of interest. None of its claims is

[6] That the Trustee has these powers is further reinforced by Section 7.02(f) of the Indenture, which provides that "[a]ll rights of action and of asserting claims under this Indenture, *or under any of the relevant series Securities*, may be enforced by the Trustee without the possession of any such Securities." (emphasis added). This provision uses the exact word – "Securities" – Quadrant asserts is necessary to cover its claims.

against the Trustee, and none of its claims allege – or even suggest – complicity by the Trustee in any of the supposed wrongdoing. Without such allegations, any argument Quadrant now sees fit to adopt must be rejected. *Tomczak v. Trepel*, 724 N.Y.S.2d 737, 738 (N.Y. App. Div. 2001).[7]

D. Quadrant's Reading Is Inconsistent With New York State Authority, And *Victor* and *Cruden* Are Not Good Law

The Court of Chancery was required to give effect to the rule articulated by the Supreme Court in *Walnut Place*, but did not. Instead, the Court of Chancery attempted to make a distinction between the facts considered by the New York Supreme Court and the Appellate Division and those before it. Report at 26-27. That distinction is wrong, as shown in Section I.C., above. Moreover, New York State courts have clearly articulated how they would decide this case. The Court of Chancery was not free to ignore that guidance. When interpreting the laws of a

[7] Quadrant's specific assertions as to the supposed futility of any demand upon the Trustee – made for the first time during rebuttal oral argument on remand – are specious. *First*, Quadrant suggested a demand on the Trustee was futile because an indenture trustee is not compensated sufficiently to bring claims. ASA at 161. The New York Supreme Court has rejected the argument that the nature of an indenture trustee's fees can create a conflict. *Walnut Place I*, 2012 WL 1138863, at *6. *Second*, Quadrant argued demand was futile because the Trustee lacked the power to bring the claims Quadrant has asserted. ASA at 162. Not only is this wrong, as shown above, but Quadrant is incapable of making a proper demand, not because of any supposed limit on the Trustee's powers, but rather because Quadrant does not own, or otherwise have the support of, the majority of notes necessary to direct the Trustee. That does not excuse compliance with the no-action clause, because it is not caused by Defendants. *See Walnut Place II*, 96 A.D.3d at 685 ("The 'prevention/impossibility' doctrine, upon which plaintiffs' argument relies, only applies, where, unlike here, nonperformance of a condition precedent was caused by the party insisting that the condition be satisfied").

sister state, a Delaware court should issue a cautious decision that closely applies the sister state's decisions, not engage in a wholesale reinterpretation of them.[8]

Instead of applying the rule set out by New York State courts, the Court of Chancery relied on two federal district court opinions, *Cruden* and *Victor*. This was wrong for two reasons. *First*, a court should not follow federal authority when there is contrary state authority. *See Marsich v. Eastman Kodak Co.*, 279 N.Y.S. 140, 143 (N.Y. App. Div. 1935) ("A federal decision contrary in principle *is not binding upon a state court in respect of a state statute or of a domestic* doctrine not involving a Federal question.") (emphasis added), *aff'd*, 200 N.E. 27 (N.Y. 1936); *accord Viking Pump*, 2 A.3d at 116 ("This method of interpretation is reflected in an abundance of insurance decisions by New York state courts and it is the one I follow here. In so approaching the issue, I explicitly eschew reliance on a contrary approach taken by certain federal court decisions that purport to apply New York law. . . . [M]y role is to apply New York law in the manner most faithful to the teachings of its own courts.").

Second, neither is good law. The Court of Chancery draws support from a single sentence in the District Court's opinion in *Cruden*, but that holding is flawed

[8] *See RBC*, 2011 WL 6152282 at *6 n.43 ("My duty here is to show comity and respect by carefully and cautiously applying New York law. Our courts should never serve or be seen to serve as a way to bypass the precedent of the courts of the sovereign whose law governs the case."); *Viking Pump, Inc. v. Century Indem. Co.*, 2 A.3d 76, 117 n. 144 (Del. Ch. 2009) ("Under principles of comity and the Constitution's Full Faith and Credit Clause, it is my duty to respect our sister state New York by applying its law in the manner most faithful to my understanding of how the New York Court of Appeals would.").

in multiple ways. *First*, the *Cruden* court interpreted the no-action clause before it without citation to any New York authority, or even a discussion of the relevant contractual language or the claims asserted by the plaintiffs. *See Cruden v. Bank of N.Y.* ("*Cruden I*"), 1990 WL 131350 at *12 (S.D.N.Y. Sept. 4, 1990). *Second*, the Second Circuit, in reviewing the District Court's decision, did not mention such a distinction, much less rely on it. Instead, the Second Circuit excused compliance with the no-action clause because the defendant there was the trustee. *Cruden v. Bank of N.Y.* ("*Cruden II*"), 957 F.2d 961, 968 (2d Cir. 1992).[9]

Nor can *Victor* support the weight Quadrant puts on it. *First*, the *Victor* court purported to distinguish the no-action clause before it and the one in *Cruden* based upon whether they mentioned "securities." *Victor v. Riklis*, 1992 WL 122911 at *7 n.7 (S.D.N.Y. 1992). Chancellor Allen recognized that the court in *Victor* was wrong to rely upon such a distinction, and instead noted the correct rationale: that, in *Cruden*, the claims the Second Circuit considered were against a conflicted trustee. *See Feldbaum v. McCrory Corp.*, 1992 WL 119095 at *11 n.12 (Del. Ch. June 27, 1992).

Second, the New York Supreme Court has disavowed the reasoning behind *Victor*. In *Walnut Place*, the plaintiff argued the Court should follow *Metropolitan*

[9] The Second Circuit did not remand for trial, as the Court of Chancery asserts. To the contrary, it "remanded for further proceedings consistent with [its] opinion," *Cruden II*, 957 F.2d at 978, which is hardly an endorsement of the District Court's opinion.

West Asset Management, LLC v. Magnus Funding, 2004 WL 1444868 (S.D.N.Y. June 25, 2004), one of the only cases to follow *Victor*'s restrictive view of the coverage of no-action clauses. *Walnut Place I*, 2012 WL 1138863 at *5; *Metro. West*, 2004 WL 1444868 at *5. But the New York Supreme Court rejected plaintiff's argument, instead adopting the rule in *Feldbaum*. *Walnut Place I*, 2012 WL 1138863 at *5. Neither *Victor* nor *Cruden* is thus a correct statement of New York law.[10]

E. Quadrant's Reading Is Unsupported By The History Of No-Action Clauses

Quadrant cannot contradict controlling New York State authority with potted history. Quadrant focuses on cases prior to the passage of the Trust Indenture Act ("TIA") in 1939 in an attempt to show that collective rights – such as the ones asserted here – are not subject to no-action clauses. But New York authority makes clear that only rights individual to the noteholder receive special protection. This is the rule articulated in *Feldbaum*, and Quadrant has provided no reason to depart from a century of New York law. *See* ASA at 181-86 (Defendants' Additional Brief Regarding Issues On Remand).

[10] At oral argument on remand, Quadrant conceded that its position was inconsistent with *Feldbaum*, even though *Feldbaum* is the law in New York State. *See* ASA at 104-06 ("we disagree with the proposition that even that language [the addition of "Securities"] would cover a noncontractual claim.").

Before the TIA was passed, some no-action clauses sought to restrict securityholders' rights to bring suit to receive principal and interest on their bonds. Courts were concerned about this, because the right to receive interest and principal is individual, not collective. *See, e.g.*, *Berman v. Consol. Nev.-Utah Corp.*, 230 N.Y.S. 421, 424 (N.Y. Sup. Ct. 1928). Thus, courts imposed notice requirements, requiring clear statements of the restriction on the bonds themselves, and also carefully interpreted the language of the no-action clauses to ensure that such a restriction was in fact what the drafters had intended. *See, e.g.*, *Cunningham v. Pressed Steel Car Co.*, 265 N.Y.S. 256 (N.Y. App. Div. 1933).

Congress intervened in 1939, writing into the TIA a prohibition on any restriction of the right to receive principal and interest. *See* S. Rep. No. 76-248, at 26 (1939), *codified at* 15 U.S.C. §§ 77ppp(b). Post-TIA authority fully accounts for this distinction. In *Feldbaum*, the Chancellor held, and the New York Supreme Court later explicitly endorsed, the same distinction between individual and collective rights found in the pre-TIA cases: "if the trustee is capable of satisfying its obligations, then any claim that can be enforced by the trustee on behalf of all bonds, *other than a claim for the recovery of past due interest or principal*, is subject to the terms of a no-action clause of this type," because that is not only what the Indenture provides, but also because that is what the TIA requires. 1992 WL 119095 at *6 (emphasis added). The court explained that claims that affect

bondholders individually, such as fraudulent inducement, are also not covered by the no-action clause. *Id.* at *5; *see also RBC*, 2011 WL 6152282 at *5 (declining to follow case "pre-dat[ing]" the TIA which "shed[s] light on the distinction between direct claims made for principal and interest payments and derivative claims brought under an indenture that are properly subject to the approval of a majority of the noteholders."); *Campbell v. Hudson & Manhattan R. Co.*, 102 N.Y.S.2d 878, 881 (N.Y. App. Div. 1951) (reviewing pre-TIA cases and concluding that no-action clauses "are intended to operate for the benefit . . . of all of the bondholders acting through the trustee, so as to restrain actions in the bondholders' individual rights").[11]

F. Quadrant's Reading Disrupts Settled Law

Quadrant's interpretation of the no-action clause disrupts settled law concerning receiverships. Quadrant's reading requires that the clause's scope be limited to contractual claims, but neither New York nor Delaware courts have endorsed this distinction. Instead, courts have barred claims for receivership

[11] The majority of the cases the Court of Chancery relies on have not been cited by any New York courts for 70 years—underscoring the fact that the TIA rendered them largely moot. *See, e.g.*, *Berman*, 230 N.Y.S. 421 (uncited by any court since the TIA); *Brown v. Mich. R.R. Co.*, 207 N.Y.S. 630 (N.Y. City Ct. 1924) (uncited by any court since 1943, and uncited by New York courts since the TIA); *Deutsch v. Gutehoffnungshutte, Aktienverein Fur Bergbau Und Huttenbetrieb*, 6 N.Y.S.2d 319 (N.Y. Sup. 1938) (uncited by any court since 1940); *Regan v. Prudence Co.*, 17 N.Y.S.2d 422 (N.Y. Sup. Ct. 1939) (uncited by any New York court); *Jennings v. Studebaker Corp.*, 165 A. 631 (N.J. Ch. 1933) (cited by only three courts, all pre-TIA, uncited by any New York courts); *Tachna v. Pressed Steel Car Co.*, 163 A. 806 (N.J. Ch. 1933) (cited by only four courts, all pre-TIA, and uncited by any New York courts); *Marlor v. Tex. & Pac. Ry. Co.*, 19 F. 867 (C.C.S.D.N.Y. 1884) (uncited since 1926).

regardless of whether the right derived from contract or from some other source, even where the no-action clause referred only to rights under the Indenture. *See, e.g.*, *Greene*, 260 N.Y.S. at 406-07 (barring claim for receivership where no-action clause covered any action "under or growing out of any provision of this Indenture, or for the enforcement thereof"); *Ernst v. Film Prod. Co.*, 264 N.Y.S. 227 (N.Y. Sup. Ct. 1933) (barring claim for statutory receivership where no-action clause covered rights under the Indenture and the bonds). Neither *Greene* nor *Ernst* turned on the specific wording of the no-action clause, as they would have were Quadrant's argument correct; the *Ernst* court did not even cite the language of the no-action clause. Instead, both *Ernst* and *Greene* held that, where the bondholder asserted rights common to all bondholders, the no-action clause applied to bar the request for receivership. *See Greene*, 260 N.Y.S. at 407 ("individual creditor holding this small number of bonds had no capacity to maintain this action."); *Ernst*, 264 N.Y.S. at 229 ("The nature of [plaintiffs'] action shows that they are presuming to speak for all the bondholders and not for themselves alone. They are attempting to protect their rights under the indenture, but to be permitted to do so they must not contravene its terms.").

The Delaware statutory receivership cases cited by the Court of Chancery have similarly held that requests for statutory receivership are barred by no-action clauses, regardless of wording. In *Elliott Associates, L.P. v. Bio-Response, Inc.*,

1989 WL 55070 (Del. Ch. May 23, 1989), plaintiff brought a statutory receivership claim in the face of a no-action clause substantively identical to the one here. *Id.* at *1-2. The *Elliott* court reasoned that "there is nothing in this Indenture reserving to plaintiffs the right to commence an action, 'so long as the procedure they adopt is not under the Indenture,'" *id.* at *7, and held that the no-action clause barred even the statutory receivership claim, *id.* at *5; *see also Tang*, 2012 WL 3072347 at *5-6 (dismissing statutory receivership claim as barred by substantively identical no-action clause); *Tietjen v. United Post Office*, 167 A. 846, 848 (Del. Ch. 1933) (holding that no-action clause barred statutory receivership request). None of these cases limit their reasoning or application to statutory receivership claims, a post-hoc distinction the Court of Chancery attempts to impose upon them here. Report at 36, 46-47. Quadrant's reading of the no-action clause would throw this area of the law into confusion, making the continuing validity of these cases unclear.

G. Quadrant's Reliance On Delaware Authority Is Misplaced

Because New York authority answers the sole question presented here, this Court need not look to Delaware authority not clearly interpreting New York law. *See* Report at 27-28 ("these decisions have not made clear whether the indentures in question were governed by New York law."). But Quadrant finds even less support there, as this Delaware case law barely touches upon the coverage of the no-action clauses. In *Harff v. Kerkorian*, neither the Court of Chancery nor the

Supreme Court interpreted the no-action clause. *Harff I*, 324 A.2d 215, 222 (Del. Ch. 1974) (having dismissed plaintiff's claim, "[t]he effect of the 'no action' clause . . . need not be determined."); *Harff II*, 347 A.2d 133, 134 (Del. 1975) ("We abstain from passing at this stage upon the various collateral questions presented by the parties, here and below."). For this very reason, *Lange v. Citibank*, No. Civ.A. 19245-NC, 2002 WL 2005728 (Del. Ch. Aug. 13, 2002), rejected Quadrant's proffered interpretation of *Harff*. *Lange*, 2002 WL 2005728, at *7 n.21 ("To wit, did [*Harff*] hold that a no-action clause could not bar a bondholder suit alleging fraud or that the issuer was insolvent? . . . [N]o."). The Court of Chancery acknowledges that "the appellate decision [in *Harff*] did not comment on the no-action clause analysis," Report at 30, but nevertheless argues that the decision "implie[d]" that a Delaware court would agree with its interpretation of the Athilon no-action clause, *id.* at 30. But how a Delaware court would interpret the clause is not relevant here.[12]

[12] Quadrant's other authority does not support its arguments. *Lange* rejected the same argument advanced by Quadrant here: that *Continental Illinois National Bank and Trust Co. of Chicago v. Hunt International Resources Corp.*, Nos. 7888, 7844, 1987 WL 55826 (Del. Ch. Feb. 27, 1987), excuses compliance with a no-action clause for fraud claims. *Lange*, 2002 WL 2005728, at *7 & n.21. *Continental* also considers a no-recourse provision, not a no-action clause. *See Timberlands II*, 864 A.2d at 950 (citation to cases on no-action clauses "inexplicable" in the no-recourse context). In *Mann v. Oppenheimer & Co.*, 517 A.2d 1056 (Del. 1986), this Court did not even address the no-action clause that had been interpreted by the Court of Chancery below, Report at 31, which in any event was limited only to enforcement of remedies "under the Indenture," and did not cover those which were "by virtue or by availing of," or "upon . . . or with respect to" the indenture. *Mann v. Oppenheimer & Co.*, No. 7275, 1985 WL 11555, at *3 (Del. Ch. Apr. 4, 1985). In *Mabon, Nugent & Co. v. Texas Am. Energy Corp.*, 1988 WL 5492

H. Quadrant's Reading Is Inconsistent With The Court-Articulated Purpose Of No-Action Clauses

New York courts have long recognized that the purpose of no-action clauses is to discourage unmeritorious suits – one that would be subverted if Quadrant's proposed limitation to contractual claims were accepted. As the New York Supreme Court recently explained: "Barriers to action by individual bondholders serve an important purpose by both preventing expensive lawsuits that do not have the support of a substantial portion of the creditors while also centralizing the prosecution of lawsuits whose benefits should properly accrue to all bondholders." *Emmet*, 951 N.Y.S.2d at 860-61; *see also Walnut Place*, 2012 WL 1138863 at *3 (purpose of no-action clauses is to "prevent . . . individual bondholders from pursuing an individual course of action and thus harassing their common debtor and jeopardizing the fund provided for the common benefit, deter individual debenture holders from bringing independent law suits which are more effectively brought by the indenture trustee, and protect against the risk of strike suits.") (internal cites and quotations omitted). If any party other than the trustee is permitted to bring suit, that would "open a Pandora's box[.]" *MASTR Adjustable Rate Mortgage Trust 2006-OA1 and Fed. Hous. Fin. Agency v. UBS Real Estate Sec. Inc.*, No. 651282/2012 (N.Y. Sup. Ct.) H'g Tr., June 12, 2013, at 21:22.

(Del. Ch. Jan. 27, 1988), the Court did not quote the no-action clause, and cited no New York authority in support of its holding. *Id.* at *2.

This has been the purpose of no-action clauses since their inception. No-action clauses "avoid[] a multiplicity of suits and a disastrous race of diligence by the individual bondholders by substituting the inexpensive and just plan of extending the trusteeship to the deficit." Leonard A. Jones, *A Treatise on the Law of Corporate Bonds and Mortgages* v (Bobbs-Merrill Co. Publishers 1907), §340a at 378. The only exception to this requirement – then as now – was when the trustee was acting adverse to the interests of the bondholders. *Id.* §388 at 427.

This purpose is clear from the Athilon Indenture itself, which makes the Trustee the representative of all interests noteholders may assert to protect their collective interests. The Trustee is given standing to assert all claims "under this Indenture, or under any of the relevant series of Securities," so that it can maintain any action or proceeding "for the ratable benefit of the holders of such Securities." Op. App'x at 130, § 7.02(f). This power makes it unnecessary "to make any holders of such Securities parties to any such proceedings." *Id.* § 7.02(g).

Individual holders, by contrast, never have the right to take any action that affects all of them ratably unless they secure the consent of a majority (by principal balance). *See, e.g.*, *id.* at 126-27, § 7.01(f) (declaration of principal immediately due and payable requires consent of a majority of noteholders), *id.* at 135, § 8.02(f) (Trustee not required to make a factual investigation prior to an Event of Default unless directed by a majority of noteholders), *id.* at 138, § 8.09(c) (majority of

noteholders may remove Trustee), *id.* at 143, § 10.02 (majority of noteholders may amend Indenture). This requirement prevents minority holders from imposing their preferences on an unwilling majority.

Quadrant relies on one of the very small number of contrary voices in the secondary literature, the commentary to the 2000 Model Indenture. But that commentary is directly contradicted not just by *Feldbaum*, but also by *Victor* and *Cruden*. While the no-action clause in the 2000 Model included the word "Securities," the commentators said that it nevertheless covered only "contractual" claims, citing only cases under the federal securities laws or for past-due interest, neither of which would be covered by the *Feldbaum* rule in any event. *Revised Model Simplified Indenture*, 55 Bus. Law. 1115, 1137-38, 1191-92 (2000). The commentators did not acknowledge, much less explain, the extensive authority confirming that no-action clauses indistinguishable from their model cover non-contractual claims. Nor does Quadrant explain how a commentary that is directly contradicted by later, controlling New York authority—and even by the cases on which Quadrant itself relies—can support any position, especially when it concerns a model no-action clause the Athilon drafters did not use.

Other deleterious effects necessarily follow from Quadrant's attempt to remove non-contractual claims from the scope of the no-action clause. *First*, it results in "inefficient claim splitting," *Timberlands II*, 864 A.2d at 942 n.39, and

has in fact done so here, *see* Report at 47-54. *Second*, Quadrant's proposed interpretation also allows for competing suits by different noteholders based on the same facts and even asserting the same claims, with no procedure for deciding which noteholder suit should go forward, or which noteholder should control the litigation if the suits are combined. *Third*, broad coverage of no-action clauses allows for the efficient resolution of complex cases, serving the purpose of no-action clauses, which are meant to save issuers, noteholders, and the courts the expense of unpopular litigation. Then-Vice Chancellor Strine noted how complex the legal issues were in *Lange*, but was able to resolve the case on the no-action clause, which "disposes of the motion most efficiently." 2002 WL 2005728, at *5.

Quadrant, by contrast, has never explained why its rule would ever be adopted by contracting parties. There is a simple reason for this. The only beneficiaries of Quadrant's rule would be minority noteholders who wish to bring claims the majority does not.

CONCLUSION

For the foregoing reasons, the Court should affirm the order below.

SEITZ ROSS ARONSTAM & MORITZ LLP

By: */s/ Garrett B. Moritz*
Collins J. Seitz, Jr. (#2237)
Garrett B. Moritz (#5646)
Eric D. Selden (#4911)
100 S. West Street, Suite 400
Wilmington, DE 19801
(302) 576-1600

Attorneys for Defendant Below/Appellee EBF & Associates, LP

POTTER ANDERSON & CORROON LLP

By: */s/ Philip A. Rovner*
Philip A. Rovner (# 3215)
Jonathan A. Choa (#5319
Hercules Plaza
P.O. Box 951
Wilmington, DE 19899-0951
(302) 984-6000

OF COUNSEL:

QUINN EMANUEL URQUHART & SULLIVAN, LLP
Philippe Z. Selendy
Nicholas F. Joseph
Sean P. Baldwin
51 Madison Avenue, 22nd Floor
New York, New York 10010-1601
(212) 849-7000

Attorneys for Defendants Below/Appellees Athilon Capital Corp., Athilon Structured Investment Advisors LLC, Vincent Vertin, Michael Sullivan, Patrick B. Gonzalez, Brandon Jundt and J. Eric Wagoner

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CERTIFICATE OF SERVICE

I hereby certify that on August 9, 2013, a copy of the within document was served electronically by File&ServeXpress on the following attorneys of record:

Lisa A. Schmidt, Esq.
Catherine G. Dearlove, Esq.
Russell C. Silberglied, Esq.
Susan M. Hannigan, Esq.
Richards, Layton & Finger, P.A.
One Rodney Square
920 N. King Street
Wilmington, DE 19801

/s/ Philip A. Rovner
Philip A. Rovner (#3215)