WOLLMUTH MAHER & DEUTSCH LLP
500 Fifth Avenue
New York, New York 10110
Telephone: (212) 382-3300
Facsimile: (212) 382-0050
William A. Maher
Paul R. DeFilippo
William F. Dahill
Vincent T. Chang
Jason E. Glass
Mara R. Lieber

Counsel for Plaintiff
Lehman Brothers Special Financing Inc.

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re:	:	Chapter 11
LEHMAN BROTHERS HOLDINGS INC., *et al.*	:	Case No. 08-13555 (SCC)
Debtors.	:	
LEHMAN BROTHERS SPECIAL FINANCING INC.	:	
Plaintiff,	:	
− against −	:	Adversary Proceeding No.: 10-03547 (SCC)
BANK OF AMERICA NATIONAL ASSOCIATION, *et al.*,	:	
Defendants.	:	

MEMORANDUM OF LAW IN OPPOSITION TO THE MOTION OF THE PYXIS DEFENDANTS TO DISMISS THE PYXIS COUNTS IN THE FOURTH AMENDED COMPLAINT

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Case **Page(s)**

Other Authorities

Lehman Brothers Special Financing Inc. ("Plaintiff" or "LBSF"), through Lehman Brothers Holdings Inc. ("LBHI"), hereby submits this memorandum of law, together with the Declaration of Paul R. DeFilippo dated April 19, 2016 (the "DeFilippo Decl."), in opposition to the Motion of the Pyxis Defendants ("Movants," "Noteholders," "Pyxis Defendants," or "Pyxis Trustee") to Dismiss the Pyxis Counts in the Fourth Amended Complaint [ECF No. 1247] (the "Motion") and respectfully states as follows:

PRELIMINARY STATEMENT

The unique Pyxis claims, which are asserted against the Pyxis Defendants in addition to all of the other counts addressed in the Omnibus MTD,[1] are set out in Counts XX to XXIII of the FAC[2] (the "Pyxis Counts"). The Pyxis Counts provide bases for liability against the Pyxis Defendants which are nearly all independent of the outcome of the Omnibus Motion. Counts XX and XXI seek declaratory judgments that the Pyxis Defendants' actions violated both the Pyxis Credit Default Swap Agreement[3] and the Pyxis Indenture. Those declaratory judgment claims do not seek monetary recovery against the Pyxis Defendants, but rather a declaration that the Pyxis Defendants breached the Transaction Documents in various ways, including the following:

- The Trustee liquidated the Collateral in violation of §§ 5.4 and 5.5 of the Indenture;
- The Trustee breached § 5.2(c) of the Indenture when it terminated the CDS Agreement;
- The Noteholders breached § 13 of the Indenture by failing to perform in accordance with the subordination provisions; and
- Termination of the CDS Agreement and the Transactions thereunder breached the CDS Agreement by denying LBSF a bargained for cure right.

[1] The Omnibus Motion of the Noteholder Defendants to Dismiss the Fourth Amended Complaint, dated December 15, 2015 [ECF No. 1195] is referred to herein as the "Omnibus MTD."

[2] The Fourth Amended Complaint, dated October 13, 2015 [ECF No. 1156], is referred to herein as the "FAC."

[3] Capitalized terms are defined in the FAC, the Transaction Documents (as defined in the FAC) or below.

The balance of the Pyxis Counts seek damages for the assorted contractual breaches. The breach of contract claims state viable claims, as demonstrated by a straightforward reading of the Indenture and the Swap Agreement.

Movants ignore the events of February 2008, which are critical to understanding the Pyxis Defendants' liability. The Pyxis Transaction Documents were designed to provide additional protections to the Credit Swap Counterparty (LBSF) when the Pyxis transaction became stressed, and the Pyxis Defendants failed to perform in accordance with those additional protections. In February 2008, the Pyxis Trustee gave notice of an Event of Default as a result of the Issuer's failure to satisfy a collateral coverage test in the Pyxis Indenture. At that point, CIBC, the Controlling Class, directed the Trustee to accelerate the Notes, but elected not to seek the requisite approval from LBSF to dispose of the Collateral (which would have required the Controlling Class to make a large payment); as a result the Pyxis Trustee was required to retain the Collateral intact. Once the Collateral was retained, it could not be liquidated under the provision that the Pyxis Trustee later relied on in October 2008, and doing so breached the Indenture.

As the Pyxis Defendants do not deny, LBSF was deeply in-the-money on the Pyxis Swap in both February 2008, when the first default was declared because the Collateral fell in value, while LBSF's position in the Swap increased in value, and again in September 2008, when LBHI filed for chapter 11. Before application of the flip clauses, the Notes were worth a small fraction of their face amount, and the default that triggered the modification of LBSF's rights was based upon the commencement of a chapter 11 case. The Pyxis Defendants make no unique arguments to counter LBSF's showing that the reversal of priorities because of LBHI's bankruptcy resulted from application of impermissible *ipso facto* provisions.

Count XXIII of the FAC alleges that the Trustee and the Controlling Class failed to comply with the subordination of the Noteholders' rights to those of LBSF under § 13 of the Indenture. Movants' attack on Count XXIII grossly misreads the Pyxis Indenture. The Pyxis Noteholders

argue they were not signatories to the Pyxis Indenture and therefore not bound by its terms, (Moving Br.[4] at 23), but this contention ignores that the Notes which they hold make the Pyxis Indenture binding on the Noteholders. Their argument that LBSF cannot enforce the relevant provisions of the Indenture disregards § 14.8 of the Indenture, which makes LBSF an intended beneficiary of all of its terms. Once the unenforceability of the *ipso facto* clauses is determined and LBSF is restored to its position of priority over the Noteholders, the Pyxis Noteholders are in breach of § 13.1(a) and liable for damages for the funds wrongfully received, plus interest.

Movants' argument that the *Ballyrock*[5] opinion insulates them from liability for termination of the ISDA Master Agreement (rather than the Transactions), (Moving Br. at 14-17), in breach of § 5.2(c) of the Indenture also fails, for reasons set out at length below. Not only is *Ballyrock* factually distinguishable, that case did not even address the issues before the Court on this Motion.

Similarly, Movants' contention (*id.* at 17-18) that the Trustee properly liquidated the Collateral under § 5.5(a) fails. As shown below, the section the Trustee relied upon in liquidating the Collateral in the fall of 2008 does not apply and does not permit the challenged actions.

Counts XXI and XXIII also allege that § 7.5 of the Indenture was violated. The Pyxis Defendants admit that such a violation occurred if § 7.5 is read in isolation. However, the Pyxis Defendants unsuccessfully invoke § 12.2 of the Indenture in an effort to limit the scope of § 7.5. Section 7.5 cross-references one section of the Pyxis Indenture, but not § 12.2, which section has no bearing on, and cannot limit, § 7.5.

The FAC also states a viable claim that the Pyxis Trustee prematurely terminated the Transactions and the CDS Agreement. LBSF had a contractual right to a ten business-day period to cure the Ratings Event default which occurred on September 16, 2008. LBSF had a heavily in-the-

[4] The Motion of the Pyxis Defendants to Dismiss the Pyxis Counts in the Fourth Amended Complaint [ECF No. 1247-1], is referred to herein as "Moving Br."

[5] *Lehman Bros. Special Fin. Inc. v. Ballyrock ABS CDO 2007-1 Ltd. (In re Lehman Bros. Holdings Inc.)*, 452 B.R. 31 (Bankr. S.D.N.Y. 2011) ("*Ballyrock*").

money position of potential interest to purchasers. The Pyxis Trustee, however, purported to terminate the Transactions and the Swap Agreement when that cure period was still pending, making it impossible to effect the cure and thereby depriving LBSF of its benefits. The Pyxis Defendants admit their termination of the Transactions and the Swap Agreement pursuant to the ISDA Master Agreement precluded LBSF's exercise of the right to cure the Ratings Event in accordance with the Schedule, two rights which cannot be consistently exercised at the same time. The Trustee's abrogation of LBSF's contractual cure right disregards ISDA Master Agreement § 1(b), which stated the Schedule controls if the Schedule and Master Agreement are inconsistent.

Finally, Movants' contention that the Pyxis Counts should be dismissed because LBSF was not damaged by those breaches is without merit because (a) it is obvious that substantial damages accrued to LBSF from Movants' failure to comply with the subordination provisions and obstruction of the right to cure, both of which deprived LBSF of hundreds of millions of dollars, (b) the quantum of LBSF's damages from breach are not a proper subject of a motion to dismiss, and (c) the requirement that LBSF must have been damaged by the breaches is satisfied at this stage by the fact that nominal damages are recoverable on every Pyxis Count as a matter of law once a breach of contract is proven, and LBSF need not plead its theory of damages in order to withstand a motion to dismiss. LBSF will prove its damages at the appropriate time, but that time is not now.

As set out in greater detail below, the Pyxis Counts all state claims on which relief can be granted, and the Motion should be denied in its entirety.

STATEMENT OF FACTS

A. Overview of the Pyxis Transaction

In March 2007, Pyxis issued nine classes of notes in an aggregate principal amount of $1,489,000,000 pursuant to an indenture dated as of March 6, 2007 between Pyxis, the Co-Issuer

and LaSalle Bank National Association, as the Pyxis Trustee (the "Indenture"). Ex.[6] A. Also, on March 6, 2007, Pyxis and LBSF entered into a Credit Default Swap Agreement (the "Pyxis Credit Default Swap Agreement," "CDS Agreement," or "Swap") pursuant to which LBSF bought credit protection from Pyxis. The Pyxis Credit Default Swap Agreement consists of an ISDA Master Agreement, a Schedule and a Credit Support Annex. Ex. B. LBHI guaranteed LBSF's obligations under the Pyxis Credit Default Swap Agreement via a Guarantee dated March 6, 2007, and became LBSF's Credit Support Provider under the Credit Default Swap Agreement. The Pyxis Swap provides that Second Method applies, so that LBSF was entitled to the positive value of its Swap position on early termination of the Transactions, even if it was the Defaulting Party. *See id.* Master Agreement, § 1(e)(ii) (Loss and Second Method apply with respect to any Early Termination Date designated in respect of any Event of Default). The ISDA Master Agreement also provides that "In the event of any inconsistency between the provisions of the Schedule and the other provisions of this Master Agreement, the Schedule will prevail." *Id.* Master Agreement, § 1(b). New York law governs the CDS Agreement. *Id.* Schedule, Part 4(h).

The Pyxis Indenture requires application of New York law as well. Ex. A, § 14.10. In addition, it has a waterfall which prioritizes distributions to LBSF over those to the Noteholders in almost all circumstances, except for the flip clauses in §§ 11(i)(C) and (ii)(A) which provide for Noteholder priority over a Defaulted Synthetic Termination Payment, *i.e.*, a payment due to LBSF after an LBSF default under the Swap. *Id.* § 11. The modification of payment priorities under the Indenture which took place in October 2008 was caused solely by the commencement of LBHI's chapter 11 case. The Indenture also grants the Trustee a security interest in the Collateral for the Secured Parties' benefit, and § 5.4(a) provides that if an Event of Default has occurred and is continuing, and the Notes have been declared due and payable and such declaration and its

[6] References herein to "Ex." or "Exhibits" refer to the exhibits attached to the DeFilippo Decl.

consequences have not been rescinded and annulled, the Trustee "may not sell or liquidate the Collateral or institute Proceedings in furtherance thereof pursuant to this Section 5.4 except in accordance with Section 5.5(a)." *Id.* § 5.4. Section 5.5(a) in turn provides that after an Event of Default, if Notes are outstanding, the Trustee shall "retain the Collateral securing the Notes intact" unless one of three conditions exist. *Id.* § 5.5(a). Once the Collateral has been retained, retention may be rescinded only if subclauses (i) or (ii), but not subclause (iii), of § 5.5(a) are satisfied. Neither of the two available conditions were satisfied at the time the Collateral was liquidated.

LBSF and the Noteholders are both third party beneficiaries of "each agreement or obligation in this Indenture." *Id.* § 14.8. The form of Note attached to the Indenture as an Exhibit binds the Noteholders to the terms and conditions of the Indenture as well, as it provides: "Reference is made to the Indenture . . . for a statement of the respective rights, limitations of rights, duties and immunities thereunder of the Co-Issuers, the Trustee and the Holders of the Notes and the terms upon which the Notes are, and are to be, authenticated and delivered." Ex. C, A-2-5. Thus the Noteholders are bound by the Indenture even if they did not sign it.

B. An Event of Default Occurs under the Pyxis Indenture

On February 1, 2008, the Pyxis Trustee sent a notice to the Noteholders and LBSF advising that an Event of Default had occurred pursuant to § 5.1(h) of the Indenture because the Issuer failed to satisfy a collateral coverage test in the Indenture. Ex. D. On February 4, 2008, CIBC, representing a Majority of the Controlling Class under the Indenture (the "Controlling Class"), sent a notice to the Pyxis Trustee directing the acceleration of the maturity of the Notes (the "Notice of Acceleration"). Ex. E. However, at that time, CIBC elected not to exercise its right to cause the Trustee to seek LBSF's consent to direct the Pyxis Trustee to dispose of the Collateral in accordance with § 5.5(a)(iii). On or about March 1, 2008, when the value of LBSF's position in the Swap was substantially in-the-money (Ex. M), the Pyxis Trustee sent a notice to the Noteholders and LBSF advising that based on bids solicited to value the Collateral, the Pyxis Trustee could not

conclude that sufficient Collateral existed to pay the termination payment due to LBSF as well as to redeem the Notes, and therefore, the Pyxis Trustee retained the Collateral intact. Ex. F. If the Pyxis Credit Default Swap Transactions had been terminated then, CIBC would have been obligated to make advances to Pyxis under the Note Purchase Agreement to fund the shortfall between the proceeds from the sale of the Collateral and the termination payment owed to LBSF, up to $945 million. Ex. G, § 2.3(c)(ii). At the time of the February 2008 default, LBSF's position in the Swap was deeply in-the-money and the Collateral was worth less than what was required to pay the Notes and LBSF. Section 5.5(a) was carefully designed to protect LBSF in the circumstances of an Issuer default, since liquidation could occur under subclause (i) only if the Trustee determined that the Collateral fully covered LBSF and the Notes, and could occur under subclauses (ii) or (iii) only with the consent of the Noteholders and LBSF. Since none of the conditions allowing liquidation under § 5.5(a) prevailed in February 2008, the Trustee retained the Collateral intact.

C. The Pyxis Trustee Purports to Terminate the Credit Default Swaps

On September 15, 2008, LBHI filed a bankruptcy petition in the Southern District of New York. Under § 5(a)(vii) of the ISDA Master Agreement, the bankruptcy filing by LBSF's Credit Support Provider was an Event of Default under the Credit Default Swap Agreement, and but for the interference with the Ratings Event cure right, would have given Pyxis the right to terminate the Transactions. *See* Ex. B, Master Agreement, §§ 5(a)(vii) and 6(a). Following the bankruptcy filing by LBHI, on September 16, 2008, Standard & Poor's downgraded LBHI's long-term credit rating to below BBB+, resulting in a Ratings Event for purposes of Parts 5(k)(iii) and (iv) of the Schedule to the Credit Default Swap Agreement. *See* FAC ¶ 95; Ex. B, Schedule, Part 5(k)(iii) and (iv).

Following the occurrence of a Ratings Event, LBSF was protected by its right to locate a satisfactory substitute guarantor or assign the Transactions to a substitute counterparty within ten business-days, in this case by September 30, 2008. *See id.* Part 5(k)(iv).

Pyxis and the Pyxis Trustee issued several hasty and improper termination notices after September 15. Although the cure period did not expire before September 30, 2008, on September 19, 2008 the Pyxis Trustee sent a notice ("September 19 Notice") to LBSF setting September 19, 2008 as the Early Termination Date for all Transactions under the Swap Agreement, even though the cure period had not run. Ex. H. The September 19 Notice also terminated the Master Agreement. *Id*. On September 24, 2008, still well within the Ratings Event cure period, the Pyxis Trustee sent two separate notices, one to LBSF alone, (Ex. I) ("September 24 Notice 1"), and one to persons on Schedule I thereto, including LBSF, rating agencies and Noteholders, (Ex. J) ("September 24 Notice 2"). Notably, the September 24 Notice 1 made clear that the September 19 Notice was intended to terminate both Master Agreements, and all Transactions thereunder. The September 24 Notice 2, entitled "Notice of Direction to Liquidate the Collateral Under Section 5.5(a)(iii) of the Indenture," attached the September 23, 2008 direction to liquidate the Collateral, based on the February 2008 default and § 5.5(a)(iii). *Id*.

Delivery of these notices wrongfully denied LBSF an opportunity to protect its deeply in-the-money position by locating a substitute guarantor or assigning the Transactions in accordance with the cure provision of the Swap Agreement Schedule.

The September 23 direction to the Trustee to liquidate the Collateral under § 5.5(a)(iii) also cannot be squared with the last paragraph of § 5.5(a) of the Indenture, which allows rescission of retention under conditions (i) or (ii), but not (iii). In September 2008, the Event of Default that triggered the March 2008 notice was continuing and had not been cured. Nonetheless, the Pyxis Trustee impermissibly invoked § 5.5(a)(iii) even though the Pyxis Trustee had already retained collateral and thus could no longer rely on § 5.5(a)(iii).

On October 6, 2008, the Pyxis Trustee distributed approximately $388 million from the liquidation of Pyxis's portfolio to the Pyxis Noteholders. Ex. K. Despite LBSF's substantial in-the-money position, the Pyxis Trustee treated amounts due to LBSF as Defaulted Synthetic Termination

Payments, with a substantially reduced priority under §§ 11.1(i)(Q) and 11.1(ii)(N) of the Indenture.

ARGUMENT

When addressing a motion to dismiss, the Court must "accept as true all factual statements alleged in the complaint and draw all reasonable inferences in favor of the non-moving party." *McCarthy v. Dun & Bradstreet Corp*., 482 F.3d 184, 191 (2d Cir. 2007); *see also Limarvin v. Edo Rest. Corp*., No. 11 Civ. 7356(DAB), 2012 WL 3297734, at *1 (S.D.N.Y. Aug. 10, 2012) (all factual inferences must be resolved in favor of the plaintiff). A complaint "does not need detailed factual allegations," *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555 (2007); *see Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009), but "only enough facts to state a claim to relief that is plausible on its face." *Twombly*, 550 U.S. at 570. "[A] well-pleaded complaint may proceed even if it appears 'that a recovery is very remote and unlikely.'" *Id*. at 556 (citation omitted).[7]

In deciding a motion to dismiss in a breach of contract case, a court "should resolve any contractual ambiguities in favor of the plaintiff." *Subaru Distrib. Corp. v. Subaru of Am., Inc.*, 425 F.3d 119, 122 (2d Cir. 2005). The existence of questions of fact as to the meaning of an ambiguous contract requires denial of a motion to dismiss. *See, e.g.*, *Eternity Global. Master Fund Ltd. v. Morgan Guar. Trust Co. of N.Y.*, 375 F.3d 168, 178 (2d Cir. 2004) ("Unless for some reason an ambiguity must be construed against the plaintiff, a claim predicated on a materially ambiguous contract term is not dismissible on the pleadings."); *Atlas Partners, LLC v. STMicroelectronics, Int'l N.V.*, No. 14-cv-7134 VM, 2015 WL 4940126, at *6 (S.D.N.Y. Aug. 10, 2015) (citing *Sayers v. Rochester Tel. Corp. Supplemental Mgmt. Pension Plan*, 7 F.3d 1091, 1094 (2d Cir. 1993)).

[7] Plausibility "is not akin to a probability requirement," rather, plausibility requires "more than a sheer possibility that a defendant has acted unlawfully . . . . In deciding a 12(b)(6) motion, the court may not consider evidence proffered by any party. Rather, the court is limited to reviewing the complaint, any documents attached to that pleading or incorporation [sic] in it by reference, any documents that are integral to the plaintiff's allegations even if not explicitly incorporated by reference, and facts of which the court may take judicial notice." *Schenk v. Citibank/Citigroup/Citicorp*, No. 10 Civ. 5056(SAS), 2010 WL 5094360, at *1-2 (S.D.N.Y. Dec. 9, 2010). All of the documents submitted by Plaintiff are appropriately considered by the Court in opposition to the Motion.

Movants' argument to dismiss certain claims because LBSF has not been damaged is also not an appropriate subject of a Rule 12(b)(6) motion, which cannot challenge the demand for relief, *i.e.*, the damages sought. Such a motion only tests the legal sufficiency of allegations of which the demand for relief is not a part. *Alevsky v. GC Servs. Ltd. P'ship*, No. 13-CV-6793 JG, 2014 WL 1711682, at *1 (E.D.N.Y. Apr. 30, 2014). Generally a complaint's statement that plaintiff has been damaged in an amount to be determined at trial is sufficient. *Sibersky v. Borah, Goldstein, Altschuler & Schwartz, P.C.*, 242 F. Supp. 2d 273, 277-78 (S.D.N.Y. 2002).[8]

I. THE TRUSTEE AND NOTEHOLDERS BREACHED § 13.1(a) OF THE INDENTURE (Moving Br. 23-25)

Movants' arguments underlying their request for dismissal of the claims for breach of Section 13 of the Indenture are so infused with misreadings of the Indenture that it justifies addressing those contentions first.[9]

The Noteholders argue they were not signatories to the Pyxis Indenture and therefore not bound by it, (Moving Br. at 23), but this ignores that the Notes make the Pyxis Indenture binding on the Noteholders. *See* Ex. C, A-2-5 ("Reference is hereby made to the Indenture . . . for a statement of the respective rights, limitations of rights, duties and immunities thereunder of the Co-Issuers, the Trustee and the Holders of the Notes and the terms upon which the Notes are, and are to be,

[8] *Varghese v. China Shenghuo Pharm. Holding, Inc.*, 672 F. Supp. 2d 596, 611 (S.D.N.Y.2009) (holding that the plaintiff's claim should not be dismissed where plaintiff did not allege specific facts of damages because "damages issues are not properly resolved at the motion to dismiss stage").

[9] In § 13.1(a) of the Indenture, the Noteholders' rights to payment were expressly subordinated to LBSF's senior right to payment under the waterfall in § 11. Ex. A, § 13.1(a). The failure to respect LBSF's priority was based solely on an unenforceable *ipso facto* clause and if the Court holds that the Pyxis Priority Modification Provisions are unenforceable, then the subordination provisions of § 13 warrant holding the Noteholders liable for funds they wrongfully received, and the Trustee liable for failing to properly administer the Indenture after default. Accordingly, claims based on breach of § 13.1(a) should abide the Court's determinations on the *ipso facto* clause issues, and should not be dismissed. The express subordination provisions in § 13.1(a) provide LBSF with valuable rights against the Pyxis Noteholders. Section 13.1(a) provides that all payments to Noteholders "shall be subordinate and junior to the rights of . . . the Credit Default Swap Counterparty [LBSF]" with respect to payments made pursuant to certain waterfall provisions of the Indenture. Ex. A, § 13.1(a). The payments here fall squarely within § 13.1 because § 11.1(i)(C) is one of the unenforceable *ipso facto* clauses as it excludes "Defaulted Synthetic Termination Payments" from the normal operation of the waterfall, and thus deprived LBSF of its deeply in-the-money priority that it would have otherwise enjoyed on early termination of the Transactions, solely due to the LBHI bankruptcy.

authenticated and delivered."). The Noteholders can be liable for breach of Indenture provisions like § 13.1(a), which contains covenants and duties expressly applicable to them, and binding on them by virtue of their ownership of the Notes. *U.S. Trust Co. of N.Y. v. Jenner*, 168 F.3d 630, 632 (2d Cir. 1999) (Missouri and New York law "enforce" the "mandate" of certificate provisions making holders "bound by the indenture's terms").[10]

Movants also argue that LBSF was not a third party beneficiary of (and thus cannot enforce) all provisions of the Pyxis Indenture. This argument is foreclosed by § 14.8 of the Indenture, which states that LBSF is a third party beneficiary "of each agreement or obligation in this Indenture." Ex. A, § 14.8.

In § 13.1(a), the Noteholders themselves agree that for LBSF's benefit (as Credit Default Swap Counterparty) they hold "Subordinate Interests" junior to LBSF to the extent LBSF is entitled to priority of payment under § 11, and that "all amounts payable to the . . . Credit Default Swap Counterparty . . . shall be paid . . . before any further payment or distribution is made on account of the Subordinate Interests." *Id.* § 13.1(a). Section 13.1(a) specifically provides that payments to the Noteholders pursuant to §§ 11.1(i)(C) and 11.1(ii)(A) are subordinated to LBSF's interest. Critically, the first words of § 13.1(a) state that it applies "Anything in this Indenture or the Notes to the contrary notwithstanding." *Id.* "[P]rovisions of a . . . contract should be interpreted to give effect to all language employed, [and] to render all parts consistent with each other." *RJE Corp. v. Northville Indus. Corp.*, No. 01-cv-2749 (FB), 2002 WL 1396991, at *4-5 (E.D.N.Y. June 25, 2002) (holding that "notwithstanding" clause overrides inconsistent provisions).[11] The subordination

[10] *Jackson Nat'l Life Ins. Co. v. Ladish Co*., No. 92 CIV. 9358 (PKL), 1993 WL 43373, at *7 (S.D.N.Y. Feb. 18, 1993) (enforcing subordination provisions of indenture against noteholders based on provision of note stating that "this Note is issued subject to such provisions of the Indenture"); *see also York v. Guar. Trust Co. of N.Y.*, 143 F.2d 503, 519 n.22 (2d Cir. 1944) ("[T]he average noteholder . . . never reads such an indenture, yet all the noteholders are bound by its terms so far as they are valid."), *rev'd sub nom. on other grounds*, *Guar. Trust Co. of N.Y. v. York*, 326 U.S. 99 (1945).

[11] *See also Rio Sportswear, Inc. v. Partners in Progress*, No. 93 Civ. 0721 (JFK), 1993 WL 97317, at *3 (S.D.N.Y. Mar. 30, 1993) (notwithstanding clause "supersede[s] any possible contradictory clause[] in the [a]greement").

provision applies notwithstanding any other provision to the contrary and thus overrides the provisions cited by the Pyxis Defendants. Even if § 13.1(j), which requires Noteholders to hold wrongfully received payments in trust, does not apply to LBSF (which is not conceded),[12] the Noteholders' agreement in § 13.1(a) to subordinate their interests to LBSF, which bars Noteholders from retaining payments on account of their Subordinate Interests until LBSF is fully paid, is binding and enforceable on them. The Pyxis Defendants contend, (Moving Br. at 24-25), that §§ 11.1(i)(C) and 11.1(ii)(A) of the Indenture do not cover payments arising from termination of the transactions based upon LBSF's default. However, in relevant part, § 11 of the Indenture expressly excludes from LBSF's priority any Defaulted Synthetic Termination Payment, which is the definition of what LBSF would have been due under Second Method on early termination of the Transactions, but for the default under the Swap Agreement caused by LBHI's bankruptcy. Once the flip clause in the Pyxis Indenture is rendered unenforceable, LBSF is entitled to priority over the Noteholders under the waterfall, and the Noteholders can be ordered to give effect to the subordination of their interests under an Indenture covenant directly applicable to them, by repaying funds wrongfully distributed to them, plus interest. Accordingly, claims against the Noteholders under § 13.1(a) state a claim on which relief can be granted. Likewise, as set forth below, the Trustee can be liable for failing to properly administer the Indenture by making payment to Noteholders in violation of the last sentence of § 13.1(a).

II. LBSF ADEQUATELY PLED THAT THE TRUSTEE'S LIQUIDATION OF COLLATERAL BREACHED THE INDENTURE (Moving Br. 22-23)

Section 5.4(a) of the Indenture states that after an Event of Default the Trustee *may not* sell or liquidate the Collateral except in accordance with § 5.5(a). This represents another provision designed in part to protect LBSF when the collateral is worth less than what is required to satisfy

[12] LBSF reserves its right to contend that omission of the Credit Default Swap Counter Party from § 13.1(j) was a scrivener's error, especially since LBSF was also the Hedge Counterparty.

the Notes and LBSF. The Trustee breached this provision of the Indenture because it liquidated the Collateral without complying with § 5.5(a). LBSF is entitled as a third party beneficiary of the Indenture to remedies for the Trustee's breach.

Section 5.5(a) of the Indenture provides that if an Event of Default has occurred and is continuing and any Class of Notes is Outstanding, then "the Trustee shall retain the Collateral securing the Notes intact" unless one of the three conditions in §§ 5.5(a)(i), (ii) or (iii) are met. However, if the Trustee has retained Collateral and given notice of same, as the Trustee did here, then such Collateral retention may only be rescinded if conditions (i) or (ii) apply, but not (iii). There is no basis for a finding on this Motion that (a) either of the conditions in §§ 5(a)(i) or (ii) were either invoked or satisfied in connection with the liquidation, or (b) § 5.5(a)(iii) was available as a basis to liquidate the Collateral due to the bankruptcy of LBHI. In addition to being prohibited by the Indenture's plain language, liquidation of the Collateral was improper for other reasons.

First, because the Pyxis Trustee retained the Collateral in February 2008 rather than directing its Disposition, the Pyxis Defendants are bound by that election of remedies and could not later choose to seek liquidation of the Collateral. *See* Point II(A), *infra*.

Second, the non-waiver clause, Indenture § 5.12, protects the Controlling Class only against waiver, not election of remedies, defeating the Pyxis Defendants' argument. *See* Point II(B)(1), *infra*.

Third, the bankruptcy of LBHI was not a permissible basis for liquidation of the Collateral under § 5.5(a)(iii) after September 15, 2008. *See* Point II(C), *infra*.

Contrary to the Pyxis Defendants' argument, LBSF has the requisite privity of contract to maintain the claims for breach of §§ 5.4 and 5.5(a). *See* Point II(E), *infra*.

Finally, the Pyxis Defendants are wrong in contending that LBSF suffered no damages because it would have been subordinated in any event. If LBSF proves a breach of contract,

nominal damages are presumed as a matter of New York law, and LBSF is not required to plead its theory of actual damages to survive a motion to dismiss. *See* Point II(F), *infra*.

A. The Failure to Direct the Disposition of the Collateral upon an Event of Default Foreclosed the Later Exercise of that Right With Respect to that Event of Default (Moving Br. 22)

The election of remedies in February 2008 not to seek Disposition of the Collateral eliminated the right to direct Disposition of the collateral in September 2008 in reliance on § 5.5(a)(iii). On February 1, 2008, the Pyxis Trustee gave notice that an Event of Default had occurred, and on February 4, 2008, the Controlling Class directed the acceleration of the Notes' maturity. *See* Exs. D; E. LBSF was not the Defaulting Party under the Pyxis Credit Default Swap Agreement in February 2008, and LBSF would have been entitled to be paid the value of its position in the Swap if early termination of the Transaction occurred at that time. In addition, in February 2008, LBSF's consent was required for a Disposition of the collateral under both §§ 5.5(a)(ii) and (iii), as the conditions in § 5.5(a)(i) were not satisfied at that time. If the Controlling Class had exercised its right to direct Disposition of the Collateral, Pyxis would have had to negotiate a consensual termination of the transactions under the Credit Default Swap Agreement with LBSF because the transactions were then deep "in-the-money" to LBSF—far more than the value of Pyxis's assets. Such a termination would have required a substantial out-of-pocket payment to be made to LBSF. *See* Statement of Facts, *supra*. Due to the foregoing election the Pyxis Trustee retained the Collateral pursuant to § 5.5(a). As described below, this election could not be rescinded in September 2008, and therefore disposition of the Collateral based on § 5.5(a)(iii) was unavailable, despite the Pyxis Trustee's reliance on that provision.[13]

[13] The last parenthetical of § 5.5(a)(iii) apparently provides that consent from LBSF is not required if the amount was insufficient to pay a "Defaulted Swap Termination Payment." However, the term "Defaulted Swap Termination Payment" is not defined in the Indenture and thus this clause cannot defeat the other portions of § 5.5 which require LBSF's consent. In any event, at most, the last parenthetical of 5.5(a)(iii), with its undefined term, creates an ambiguity which cannot be resolved on this motion. *Rokeach v. Hanover Ins. Co*., No. 1:13-CV-5011-GHW, 2015 WL 2400097, at *6 (S.D.N.Y. May 19, 2015) ("the meaning of the undefined term 'occurrence' . . . is ambiguous"); *Tranzact Techs.*,

1. Rights Under § 5.5(a)(iii) of the Indenture Are Not Continuing, Once the Pyxis Trustee Retained the Collateral After an Event of Default

Section 5.5(a) requires the Trustee to retain the Collateral if an Event of Default has occurred and is continuing, unless one of three conditions in § 5.5(a) are met. Once the Pyxis Trustee retained the Collateral, and the Event of Default was continuing, the last paragraph of § 5.5(a) was triggered. That section provides that "[s]o long as such Event of Default is continuing, any such retention pursuant to this Section 5.5(a) may be rescinded at any time when the conditions specified in clause (i) or (ii) exist." Ex. A, § 5.5(a). Clause (iii) is omitted from this list, and the only rational interpretation of § 5.5(a) is that on these facts § 5.5(a)(iii) provided no basis for the Pyxis Trustee to liquidate the Collateral after September 15, 2008. CIBC's September 23 direction to liquidate only references § 5.5(a)(iii). The omission of clause (iii) from the last paragraph of § 5.5(a) means the rights under § 5.5(a)(iii) do not continue in effect once the Trustee has retained the Collateral. Thus, the provision on which the Pyxis Trustee relied to liquidate the Collateral after September 23, § 5.5(a)(iii), was unavailable for that purpose.

Accordingly, the Pyxis Trustee's subsequent liquidation of the Collateral and distribution of proceeds to Noteholders, contravened §§ 5.4 and 5.5(a) and LBSF's rights as a Secured Party and express third party beneficiary under the Indenture. LBSF has stated a viable claim for that breach.

B. Election of Remedies Forecloses Movants' Contention (Moving Br. 22-23)

The Controlling Class elected to save itself hundreds of millions of dollars, the amount it would have had to pay if it directed liquidation of the Collateral in response to the February 2008 default. The Trustee is bound by that election, and New York's "election of remedies" doctrine applies with full force here. That doctrine provides that "'one may not both affirm and disaffirm a

Ltd. v. Evergreen Partners, Ltd., No. 00 C 3215, 2001 WL 1035338, at *6 (N.D. Ill. Sept. 7, 2001) ("There was no meeting of the minds . . . because the material term . . . 'Transaction Value,' was left undefined."). Nor can this court rely on the plain meaning of "Defaulted Swap Termination Payment" because that term has no ordinary meaning. Accordingly the Court cannot find on this Motion that LBSF's consent was not required under § 5.5(a)(iii).

contract . . . or take a benefit under an instrument and repudiate it.'" *Sofi Classic S.A. de C.V. v. Hurowitz*, 444 F. Supp. 2d 231, 238 (S.D.N.Y. 2006) (alterations in original) (citation omitted). New York law bars the pursuit of alternative relief after a party has "chosen one of two or more co-existing inconsistent remedies, and in reliance upon that election, that party . . . gained an advantage, or the opposing party . . . suffered some detriment." *Id.* at 238 (citation omitted).[14]

The Pyxis Defendants contend that the Pyxis Trustee's Notice of Retention following the February 2008 Event of Default stated that § 5.5(a)(iii) might be a basis for future disposition of the collateral legitimized the later use of that section. Moving Br. at 22-23. This argument also fails. The Indenture squarely forecloses the use of § 5.5(a)(iii) as a ground for disposition of the collateral after the Pyxis Trustee had retained the collateral. The Pyxis Defendants do not even try to support the untenable contention that the Indenture could be unilaterally modified by the Pyxis Trustee's incorrect recitation of CIBC's rights in the Notice of Retention.

1. The Non-Waiver Clause of the Indenture Does Not Excuse the Failure of the Controlling Class to Exercise Its Rights Under § 5.5(a)(iii)

The Pyxis Defendants also assert that the non-waiver clause in the Indenture, Ex. A, § 5.12, excuses the Controlling Class's election not to exercise its rights in February 2008. Moving Br. at 22. This argument cannot be squared with the plain language of § 5.5(a) itself, which specifies what must be, but what was not, done in order to dispose of Collateral after its retention. A "no

[14] *MBIA Ins. Corp. v. Patriarch Partners VIII, LLC*, 842 F. Supp. 2d 682, 709 (S.D.N.Y. 2012) ("a party may not 'exercise two alternative or inconsistent rights or remedies'" (citation omitted)). Even if the "election of remedies" doctrine does not apply here, the vast majority of cases on the issue of waiver still defeat the Pyxis Defendants' arguments. *See Golfo v. Kycia Assocs., Inc.*, 791 N.Y.S.2d 577, 578 (2d Dep't 2005); *Kistela v. Ahlers*, 802 N.Y.S.2d 729, 729-30 (2d Dep't 2005) (where seller did not exercise cancellation right, issue of fact as to whether the seller waived the closing date and instead elected to continue to perform the contract); *Delpozo v. Impressive Homes, Inc.*, 815 N.Y.S. 2d 200, 200 (2d Dep't 2006) (issue of fact existed as to whether a seller waived its right to cancel where seller waited long after deadline expired). Waiver may be proven by various types of evidence, including "by declarations, by acts and by non-feasance, permitting differing inferences and which do not directly, unmistakably or unequivocally establish it." *Sillman v. Twentieth Century-Fox Film Corp.*, 3 N.Y.3d 295, 403 (N.Y. 1957) (finding issues of fact existed and sustaining denial of summary judgment); *see also Spectrum Painting Contractors v. Kreisler Borg Florman GC*, 883 N.Y.S.2d 262, 270 (2d Dep't 2009) (issues of fact as to waiver of written provision); *N.Y. Tel. Co. v. Jamestown Tel. Co.*, 282 N.Y. 365, 372-73 (N.Y. 1940) (where a party has knowledge that an agreement is being breached and accepts the benefits of the contract, continuing performance may waive the breach).

waiver" provision does not apply if there was no right to waive: the Trustee had no right to act under § 5.5(a)(iii) following retention and therefore had nothing to waive.

In *ESPN, Inc. v. Office of Comm'r of Baseball*, 76 F. Supp. 2d 383, 389-90 (S.D.N.Y. 1999)[15] the court held that a "standard 'no-waiver' provision" does not excuse parties from the consequences of an election of remedies, like that made by the Controlling Class and which is binding on the Trustee. *Id.* at 390.[16]

C. LBHI's Bankruptcy Was Not A Basis For Using § 5.5(a)(iii) To Liquidate Retained Collateral (Moving Br. 22-23)

In order for § 5.5(a)(iii) to be available as a basis for the liquidation of Collateral, several things must occur:

1. A "Control Event" must have occurred and be continuing;

2. A Majority of the Class A-1 Notes when they are the Controlling Class must have directed Disposition of the Collateral (with exceptions not relevant here); and

3. LBSF shall have consented if the aggregate proceeds of Disposition would be insufficient to pay any amounts due to LBSF under the CDS Agreement (other than Defaulted Swap Termination Payments (a term that the Indenture does not define).

Putting aside the other elements, here, the bankruptcy of LBHI was not a Control Event allowing use of § 5.5(a)(iii).

> 'Control Event' means, at any time when the Class A-1 Notes is the Controlling Class, the occurrence and continuance of an Event of Default (1) under clause (a) of the definition of 'Event of Default' with respect to amounts owing to the Class A-1 Notes, the Class S Notes, the Class A-2 Notes or the Class B Notes on any Distribution Date, (2) under clause (b) of the definition of 'Event of Default' or (3) under clause (h) of the definition of 'Event of Default.'

[15] In *ESPN*, the defendant sought to terminate an agreement based on an alleged breach, however, the plaintiff argued that such termination was barred by the election of remedies doctrine because defendants had continued to perform and accept performance under the agreement subsequent to the alleged breach. *See ESPN*, 76 F. Supp. 2d at 388. The defendant countered that although it continued to perform under the contract after the breach, its ability to terminate the agreement based on those breaches was preserved by the contract's "no waiver" provision, which contained language almost identical to the non-waiver provision of the Indenture. *Compare id.* at 391 *with* Ex. A, § 5.12.

[16] The Court stated, "waiver and election are distinct principles that do not overlap but rather control different phases of the contractual relationship." *Id*. at 390. Waiver governs the parties' right to seek remedies for non-performance and determines whether something has occurred to "alter or eliminate a term of the parties' agreement or an available remedy." *Id.* In contrast, election occurs when parties exercise remedies in "a consistent and binding manner." *Id.*

Ex. A, §1.1. Clauses (a) and (b) of the definition of Event of Default relate to payment defaults which are not even alleged to have occurred. Clause (h) of the definition of Event of Default relates solely to the collateral coverage default that arose in February 2008. The LBHI bankruptcy was not a Control Event and was not one of the possible grounds for invocation of § 5.5(a)(iii). To the extent Movants imply that there were grounds other than the February 2008 default on which the Pyxis Trustee could base liquidation under § 5.5(a)(iii), (Moving Br. at 22-23), they are wrong. As noted above, after the Trustee retained the Collateral following the February 2008 default, it could no longer rely on subclause (iii) to liquidate it in October 2008. Accordingly, to the extent the Pyxis Trustee complied with a direction to liquidate under § 5.5(a)(iii) based on a default caused by the LBHI bankruptcy, it was not entitled to do so and thereby breached § 5.4 of the Indenture.

D. The Swap Transactions Were Wrongfully Terminated under § 12.1(a) of the Indenture

Section 12.1(a) of the Indenture states that "Except as otherwise expressly permitted or required by this Indenture, the Issuer will not sell or otherwise Dispose of any Collateral Debt Security." This section then goes on discuss certain Dispositions (not at issue here) that are permitted when no Event of Default has occurred and is continuing.

The Indenture defines "Collateral Debt Security" to include a "Synthetic Security," and the definition of "Synthetic Security" includes any "CDS Agreement Transaction." Ex. A, § 1.1. "Disposition" includes any termination of a Collateral Debt Security. *Id.* Absent valid action under another Indenture provision, § 12.1(a) prohibits the termination of the Swap Transactions. Thus, the Pyxis Trustee violated § 12.1(a) when it terminated the Swap Transactions in breach of the Indenture in September 2008, as no Indenture provision authorized that action. As detailed below,

the Pyxis Trustee's actions caused such default and the Pyxis Trustee cannot hide behind its alleged status as agent for a disclosed principal. Moving Br. at 13.[17]

E. LBSF Has the Requisite Contractual Relationship to the Pyxis Defendants (Moving Br. 12-14, 21)

The Pyxis Defendants claim that only the Issuer, Pyxis, and not the Pyxis Trustee or the Noteholders can be liable for breach of the Indenture and the Swap. Moving Br. at 21. The Pyxis Defendants also claim that LBSF lacked privity with the Noteholder Defendants and the Pyxis Trustee. Moving Br. at 12-14. These contentions fail for several reasons.

First, the Noteholders are not "non-parties" to the Indenture. Moving Br. at 21. As noted above, the Notes they hold provide that a holder of the Notes is subject to and bound by the rights and obligations in the Indenture. This creates the necessary connectivity to hold the Noteholders liable for breaches of the Indenture.

Second, LBSF was an express third party beneficiary of all of the Indenture's provisions. Nothing in the Pyxis governing documents allows the Pyxis Defendants to selectively exclude LBSF from certain of the Indenture's protections. Section 14.8 specifically provides that LBSF, as the Credit Default Swap Counterparty, is a "third party beneficiary of each agreement or obligation in this Indenture." Ex. A, § 14.8. Thus, LBSF has the full right to enforce the Indenture. *See, e.g.*, *Flickinger v. Harold C. Brown & Co*., 947 F.2d 595, 600 (2d Cir. 1991) (noting that a third party may enforce a contract if it was an intended beneficiary).

Third, the Trustee breached its contractual and extra-contractual duties to perform its non-discretionary ministerial tasks with due care. *See Phoenix Light SF Ltd. v. Bank of N.Y. Mellon*, No.

[17] To the extent the Trustee contends it cannot be liable for breach of the Issuer's obligations to LBSF under either the Swap or the Indenture, LBSF requests the ability to amend the Complaint to add claims against the Trustee that its actions intentionally interfered with LBSF's contractual rights, a cause of action recognized in New York and viable on the facts alleged. *Petrohawk Energy Corp. v. Law Debenture Trust Co. of N.Y*., No. 06-cv-6404, 2007 WL 211096, at *6 (S.D.N.Y. Jan. 29, 2007) ("To establish tortious interference, a plaintiff must show (1) the existence of a valid contract between plaintiff and a third party; (2) the defendant's knowledge of that contract; (3) the defendant's intentional procuring of the breach, and (4) damages." (citation omitted)).

14-CV-10104 (VEC), 2015 WL 5710645, at *5 (S.D.N.Y. Sept. 29, 2015); *LNC Inv., Inc. v. First Fid. Bank, N.A.*, 935 F. Supp. 1333, 1347 (S.D.N.Y. 1996) (citing *N.Y. State Med. Care Facilities Fin. Agency v. Bank of Tokyo Trust Co.*, 621 N.Y.S.2d 466, 470-71 (N.Y. Sup. Ct. 1994) (holding trustee liable for failure to notify bondholders of early redemption call)); *see also* Restatement (Third) of the Law of Trusts § 76(1) (2007) ("The trustee has a duty to administer the trust, diligently and in good faith, in accordance with the terms of the trust and applicable law."); *id.* cmt. b ("[A] trustee may commit a breach of trust by improperly failing to act, as well [as] by improperly exercising the powers of the trusteeship.").[18] And § 5.4 of the Indenture says the Trustees may exercise remedies "to the extent permitted by applicable law," implying a duty on the party of the Trustee to make certain that its behavior was lawful before acting. Ex. A, § 5.4; *see also id.* § 5.13(a) (any direction to the Trustee "shall not conflict with any rule of law or with this Indenture").

LBSF has pled a claim against the Pyxis Trustee because it has pled facts that plausibly demonstrate that the Pyxis Trustee's actions or omissions in administering the Indenture were improper. FAC ¶¶ 92-113. Indenture §§ 5.4 and 5.5 impose direct obligations on the Pyxis Trustee, not the Issuer. Accordingly, the Pyxis Trustee's conduct can form the basis for breach and liability under those sections.

In addition, all of the Pyxis Trustee's actions in this case occurred after an Event of Default and so the Pyxis Trustee was bound by the heightened duties owed to its beneficiaries, the Secured Parties, including LBSF, under the Prudent Man rule. Ex. A, § 6.1(b). As such the Pyxis Trustee owed LBSF a duty to ensure that the Pyxis Trustee's actions on behalf of the Issuer did not run afoul of the Indenture terms applicable to the Issuer. *Id.* § 5.13(a). After default the Pyxis Trustee's

[18] *See also Royal Park Invs. SA/NV v. HSBC Bank USA, N.A.*, 109 F. Supp. 3d 587, 597 (S.D.N.Y. 2015); *U.S. v. Michel*, 879 F. Supp. 2d 291, 303-04 (E.D.N.Y. 2012) ("A trustee is under a duty to employ diligence and prudence in the management of the trust estate" (citations omitted)).

duties more closely resemble those of an ordinary fiduciary. *Peak Partners, LP v. Republic Bank*, 191 F. App'x 118, 122 (3d Cir. 2006) (discussing New York law); *Howe v. Bank of N.Y. Mellon*, 783 F. Supp. 2d 466, 483-84 (S.D.N.Y. 2011) (trustee's post default obligations "more closely . . . resemble those of an ordinary fiduciary" (alterations in original)); *Beck v. Mfrs. Hanover Trust Co*., 632 N.Y.S.2d 520, 527 (1st Dep't 1995). That includes the duty to act prudently to safeguard trust assets for the benefit of the beneficiaries. *LNC Invs., Inc. v. First Fid. Bank, N.A. N.J.*, 173 F.3d 454, 461-62 (2d Cir. 1999).[19] If the Pyxis Trustee wrongly applied Indenture provisions in taking actions on behalf of the Issuer it should be liable. Ex. A, § 5.13(a).

LBSF has also alleged that the Pyxis Trustee is liable for causing Pyxis to take action in violation of the CDS Agreement, by terminating the CDS Agreement during the Ratings Event cure period, and by causing Pyxis to breach the Indenture covenants applicable to the Issuer. The Pyxis Trustee claims that it is not liable for the Issuer's breach of covenants whose breach was clearly caused by the Pyxis Trustee, under the theory that it was an agent for a disclosed principal. Moving Br. at 14. This argument cannot withstand analysis. The Issuer-Trustee relationship had none of the hallmarks of a true agency, and labeling the Pyxis Trustee as the Issuer's agent cannot obscure that fact. As alleged in the FAC (*see* FAC ¶ 68), the Pyxis Trustee exercised exclusive control over the Collateral, including the Swap Agreement, and over the Issuer's actions; in a true agency, the principal, and not the agent is in charge. Pyxis had no ability to take or refrain from taking action under any of the agreements to which it was subject, including the Indenture and the Swap Agreement. The Issuer had no ability to revoke the Pyxis Trustee's agency, (as the appointment of the Trustee as agent is stated to be irrevocable, *see* Ex. A, Granting Clause), and the right of

[19] *Blackrock Core Bond Portfolio v. U.S. Bank Nat'l Ass'n*, No. 14-cv-9401 (KBF), 2016 WL 796848, at *20 (S.D.N.Y. Feb. 26, 2016) ("[F]ollowing an Event of Default, a trustee takes on a special duty to secure the assets of the trust and act with undivided loyalty to trust beneficiaries.").

termination is a hallmark of the agency relationship.[20] The Issuer's inability to control its own actions, fire the agent, or decide what provisions of the agreements to enforce or not, should trigger the rule that an agent is not protected from liability for acting when the principal lacks the capacity to act or contract. *See* Restatement (Third) of Agency § 6.04 (2016).[21] The rule protecting the agent from liability when it acts for a disclosed principal is based on the notion that the principal could control the agent and that therefore only the principal should be liable for what the agent does. Here, the principal (Pyxis, the Issuer) had no power or ability to direct or control the Pyxis Trustee in any respect, and any actions taken by Pyxis were necessarily taken by the Pyxis Trustee. This is so because there is no provision in the Indenture for the Issuer to direct the Trustee's actions. Thus, no true agency relationship existed. *See In re Ames Dep't Stores, Inc*., 274 B.R. 600, 617-18 (Bankr. S.D.N.Y. 2002) (opining that trustee is not necessarily an "agent" and that it is "the element of continuous subjection to the will of the principal that distinguishes an agent from other fiduciaries;" "the sufficiency of control is a question of fact"), *aff'd sub nom.*, *LFD Operating, Inc. v. Ames Dep't Stores, Inc*., No. 01-42217 (REG), 2004 WL 1948754 (S.D.N.Y. Sept. 1, 2004), *aff'd sub nom.*, *In re Ames Dep't Stores, Inc*., 144 F. App'x 900 (2d Cir. 2005). Moreover, the disclosed principal rule is not absolute, and can be overcome by custom and usage. *Cf. E. River Sav. Bank v. Bevona*, No. 94 Civ. 4508 (SAS), 1995 WL 266944, at *5 n.9 (S.D.N.Y. May 5, 1995).[22] Accordingly, that principle should not bar suits against the Pyxis Trustee for wrongful termination

[20] *United Ins. Co. Ltd. v. World Wide Web*, No. 11-cv-1177 (CBA) (JMA), 2011 WL 1870599, at *2 (E.D.N.Y. Apr. 27, 2011) ("New York law clearly provides that a principal has an inviolate right to revoke its agency at any time." (citing *American Home Assurance Co. v. Starr Tech. Risks Agency, Inc.*, No. 600263/06, 2006 WL 304746, at *3 (N.Y. Sup. Ct. Feb. 8, 2006))).

[21] A party asserting an agency relationship bears the burden of establishing its existence. *See Courthouse Corp. Center, LLC v. Schulman*, 902 N.Y.S.2d 160, 162 (2d Dep't 2010). Here since the Issuer lacked capacity to take on the actions at issue it could not appoint an "agent" to do such actions. *Cf. Miner v. N.Y. State Dep't of Corr. Servs.*, 479 N.Y.S.2d 703, 704 (N.Y. Sup. Ct. 1984) (a principal may only do through an agent those things that he may do personally); *U.S. v. Roberts*, 322 F. App'x 175, 177 (3d Cir. 2009) (same); *U.S. v. Craig*, 896 F. Supp. 85, 89 (N.D.N.Y. 1995).

[22] *Fairchild Publ'ns Div. of Capital Cities Media, Inc. v. Rosston, Kremer & Slawter, Inc.*, 584 N.Y.S.2d 389, 391 (N.Y. Sup. Ct. 1992) (same).

of the Swap. Even if it does, the Trustee may still be liable for intentionally interfering with LBSF's contract with the Issuer. *Petrohawk Energy Corp.*, 2007 WL 211096, at *6.

In the Omnibus Motion and in the Reply Brief[23] (p. 19), Defendants argue that the Trustees were assignees of the Issuer's rights under the Swap Agreement. While not conceded, if this is so, then the Trustee "stands in the shoes of the assignor and subject to all equities against the assignor." *Enron Corp. v. Springfield Assocs. (In re Enron Corp.)*, 379 B.R. 425, 435-36 (S.D.N.Y. 2007) (cited in Reply Brief p. 19). That includes being subject to claims against the Issuer for breach of the Swap terms applicable to the Issuer.

Finally, the Pyxis Trustee's position here that it is not in privity with LBSF for purposes of the claims for breaches of the Swap Agreement conflicts with another of its positions in the Omnibus MTD. In the Omnibus MTD, Bank of America, which is the Pyxis Trustee (as successor to LaSalle), argued that the Trustees were swap participants by virtue of the Bankruptcy Code's definition of "Swap Agreement," which includes the Indentures, to which the Trustees were parties.[24] Bank of America now argues that as Pyxis Trustee, it was not a swap participant and was merely the Issuer's agent with no obligations to perform under the Swap Agreement (except for three limited provisions identified in the Schedule). Bank of America cannot have it both ways. Its position is diametrically opposed to its contentions in the Omnibus MTD where it claimed to be a swap participant, and therefore party to a swap agreement with LBSF.[25]

[23] The Reply of the Noteholders in Further Support of the Omnibus Motion to Dismiss the Fourth Amended Complaint [ECF No. 1308] is referred to herein as the "Reply Brief."

[24] "The term 'swap participant' means an entity that, at any time before the filing of the petition, has an outstanding swap agreement with the debtor." 11 U.S.C. § 101(53C).

[25] In the Reply Brief, defendants further contended that the Trustee was a swap participant, arguing (pp. 18-19) that the relevant Indenture provisions constitute part of the Swap Agreement so that the Trustee, as a party to the Indenture, was a Swap Participant. They also argued that the Trustees were assignees and "stands in the shoes of the assignor." *Id.* at 19; *see also* Reply of Certain Trustee Defendants to LBSF's Memorandum of Law in Opposition to the Joinder of Certain Trustee Defendants to the Omnibus Motion of the Noteholder Defendants to Dismiss the Fourth Amended Complaint [ECF No. 1310].

F. LBSF Suffered Damages as a Result of Pyxis Defendants' Breach of § 5.5(a) (Moving Br. 23)

The Pyxis Defendants contend that LBSF was not harmed by the liquidation of the Collateral, (Moving Br. at 23), but that ignores that nominal damages are always available in breach of contract actions, and when a breach is proven, Plaintiff is entitled as a matter of law to recover at least nominal damages. *Luitpold Pharm., Inc. v. Ed. Geistlich Söhne A.G. Für Chemische Industrie*, 784 F.3d 78, 87 (2d Cir. 2015) (alleging a speculative measure of damages in a breach of contract action does not justify dismissal under Rule 12(b)(6) because nominal damages are available under New York law).[26] Thus, the Court should not dismiss the claims based on LBSF's alleged failure to have suffered damages, as nominal damages for breach are presumed. LBSF is not required to plead its damages theory, or to prove its actual damages, to survive a motion to dismiss.

III. THE TRUSTEE'S EARLY TERMINATION OF THE SWAP AGREEMENT WAS PROHIBITED (Moving Br. 14-21)

The Pyxis Defendants contend without any support that the "Pyxis Counts are nothing more than an attempt by LBSF to rewrite the unequivocal terms of the CDS Agreement and the Indenture." Moving Br. at 8. To the contrary, the Defendants did not satisfy any of the preconditions for termination of the Swap Agreement under § 5.2, § 7.5(f), or § 7.8(a)(xi).

Once default occurred because the value of the Collateral dropped below an amount sufficient to protect both the Noteholders and LBSF, § 5.2(c) of the Indenture prohibited termination of the CDS Agreement unless liquidation of the Collateral had begun and the declaration of acceleration of the Notes was no longer capable of being rescinded. There is no basis to find liquidation of the Collateral had "begun," as was required under § 5.2(c), because (i) there is

[26] *Errant Gene Therapeutics, LLC v. Sloan-Kettering Inst. for Cancer Research*, No. 15-cv-2044 (AJN), 2016 WL 205445, at *7 (S.D.N.Y. Jan. 15, 2016); *LNC Invs., Inc. v. First Fid. Bank*, No. 92 Civ. 7584, 1994 WL 73648, at *5 (S.D.N.Y. Mar. 3, 1994) ("plaintiffs sue [the indenture trustees] for failing to comply with a term in the Indenture which required defendants to act prudently. Because the Indenture is a contract governed by New York law, the uncertainty of the damages requested by plaintiffs does not preclude plaintiffs from bringing this action."); *Kronos, Inc. v. AVX Corp*., 81 N.Y.2d 90, 95 (N.Y. 1993).

no evidence that by the date of either the September 19 or September 24 termination notice, the liquidation of Collateral had commenced, and (ii) any liquidation contravened Indenture § 5.5(a), and so had not properly begun.

Additionally, no judgment was obtained that could have foreclosed rescission of acceleration and thus, under § 5.2(c), the declaration of acceleration was capable of being rescinded.

Further, § 7.8(a)(xi) of the Indenture is a negative covenant and does not override the prohibition against termination in § 5.2(c); further that provision could only be satisfied if the Transactions under the Swap Agreement were properly terminated, which they were not.

Finally, Pyxis failed to comply with § 7.5(f), which required that Pyxis attempt to enter into a replacement agreement. The Pyxis Defendants claim that no replacement agreement could have been made because such an agreement would violate § 12.2 in that the Reinvestment Period had already ended. This position both misreads § 12.2 and improperly imports it into § 7.5(f).

A. Termination Was Improper Because the Conditions of § 5.2(c) of the Indenture Were Not Satisfied (Moving Br. 14-18)

The purported termination of the Swap Agreement was improper because the two preconditions to terminate the Swap Agreement in § 5.2(c) of the Indenture were not fully satisfied at the time of termination on September 19, 2008. Here, even if the Court gives credence to the argument that liquidation "began" when a direction to liquidate was given, the liquidation of the Collateral could not have "begun" by September 19, 2008, the date of the first termination notice. This is so because (a) the only basis to liquidate the Collateral under § 5.5(a)(iii) was the February 2008 default (*see* Point II(A)-(C), *supra*), (b) the Pyxis Trustee advised the parties it was retaining the Collateral and not liquidating it in February 2008, and (c) the Controlling Class did not give its first direction to liquidate the Collateral until September 23, 2008. Accordingly, it was a temporal and physical impossibility for liquidation of the Collateral to have begun by the time the CDS Agreement was terminated. There is no basis on this record to disregard the effectiveness of the

September 19 Notice, especially given the reaffirmation of that notice on September 24, 2008. Nor is there any basis for a finding that actual liquidation of the Collateral, rather than issuance of a mere direction to begin liquidation, had begun by September 24.

1. Section 5.2(c) of the Indenture Was Applicable (Moving Br. 14-17)

The Pyxis Defendants contend that § 5.2(c) does not apply because the claims here "only concern the termination of the CDS Agreement not the Transactions" and because § 5.2(c) does not "extend to or limit the separate right to terminate the Transactions themselves." Moving Br. at 16 (citing *Ballyrock*, 452 B.R. at 43). The Pyxis Defendants ignore the allegations of the FAC that charge the Trustee with wrongful termination of both the CDS Agreement and the Transactions.

First, the Trustee's September 19 Notice unequivocally purports to terminate both the Transactions and the Master Agreement ("Party B hereby elects to terminate the Master Agreement and all Transactions thereunder immediately"). Ex. H. Movants fail to mention the September 19 termination notice, claiming that termination occurred pursuant to the September 24 notice, but the Court cannot find on this Motion that the September 19 Notice was not effective. Indeed, on September 24 the Pyxis Trustee clarified that its intent in issuing the September 19 Notice was to terminate *both* Master Agreements and all Transactions arising thereunder. For purposes of this Motion, all inferences must be drawn in favor of LBSF in connection with factual issues and therefore the Court must conclude that (i) the September 19 Notice effectively terminated the Master Agreement, and (ii) the Trustee had not begun to liquidate the Collateral as of either September 19 or September 24, as required by § 5.2(c). Since at least for purposes of this Motion the September 19 Notice effectively terminated the CDS Agreement (which is what that notice clearly says) Movants' contention that the liquidation of the Collateral had begun as of the date of termination, as § 5.2(c) requires, must be rejected.

Second, while the Pyxis Defendants contend that LBSF must also show that the termination of the underlying Transactions was improper,[27] there is no such requirement in the Indenture. The termination of the Swap Agreement, standing alone, violated §§ 5.2 and 7.5(f). *See* Point III(C), *infra*.

Third, the Transactions were improperly terminated because the termination breached LBSF's Ratings Event cure right under 5(k)(iv) of the Schedule. *See* Point IV, *infra.*

The Pyxis Defendants rely on Judge Peck's *Ballyrock* decision, (Moving Br. at 14-17), but *Ballyrock* is distinguishable from this case. Unlike *Ballyrock*, here the Pyxis Trustee issued two separate and unequivocal notices terminating the Master Agreement. Moreover, the *Ballyrock* complaint contained no allegation that any term in the *Ballyrock* Indenture similar to § 5.2(c) of the Pyxis Indenture was breached. In dismissing Count II of the *Ballyrock* Complaint, Judge Peck did not have occasion to consider the effect of a provision similar to § 5.2(c) of the Pyxis Indenture, Ex. L, thus *Ballyrock* lacks any precedential or persuasive value as to LBSF's claims for breach of § 5.2(c) in ¶¶ 106-110 and Counts XXI and XXIII of the FAC.

Moreover, there is no indication in *Ballyrock* that the termination of the Swap Agreement, rather than the Transactions, deprived LBSF of some right under the Swap. Unlike in *Ballyrock*, LBSF alleges in Count XXII that it was damaged by the premature termination of the Swap Agreement because it deprived LBSF of its contractual right to cure a Ratings Event by assigning the Swap to a creditworthy party. *Ballyrock* did not address that issue; thus, that case provides no guidance on that point. Moreover, LBSF alleged that termination of the Transactions was improper to the extent the right to cure the Ratings Event was inconsistent with the right to terminate the Transactions, an issue that *Ballyrock* likewise did not address. And, *Ballyrock* does not address LBSF's right as a matter of law to nominal damages if breach is proven, thus foreclosing any

[27] The Pyxis Defendants assert termination of the Transactions would alone be sufficient to establish a right to the termination payments at issue in the Adversary Proceeding. Moving Br. at 15 (citing *Ballyrock*, 452 B.R. at 41).

argument that *Ballyrock* requires dismissal because LBSF allegedly was not harmed by the Swap termination; this Motion is not the time to evaluate the legal sufficiency of LBSF's damages theory.

2. The Declaration of Acceleration Was Capable of Being Rescinded (Moving Br. 17-18)

The Pyxis Defendants assert that the declaration of acceleration was not capable of being rescinded because Pyxis had not paid or deposited with the Pyxis Trustee sufficient funds to make certain payments on the Notes. Moving Br. at 18. The Pyxis Defendants also assert that the Pyxis Trustee had not determined that all Events of Default had been cured. *Id.* However, § 5.2(b) plainly provides that acceleration was *capable o*f being rescinded "[a]t any time" before the Pyxis Trustee has obtained a judgment or decree for payment of the cash due pursuant to the Indenture. Since no such judgment was obtained, the notice of acceleration was capable of being rescinded. Moreover, the deposit of funds and the determination that Events of Default were cured were steps to effectuate the rescission. Because no judgment had been rendered, nothing prevented the parties from taking those steps, and thus the acceleration was "capable" of being rescinded on that date.[28]

B. Section 7.8(a)(xi) of the Indenture Was Not Satisfied (Moving Br. 20-21)

The Pyxis Defendants breached § 7.8(a)(xi)(B) of the Indenture by failing to enter into a replacement agreement. The Pyxis Defendants' sole response is that no transactions were "outstanding" under the meaning of § 7.8(a)(xi). Moving Br. at 20-21. However, this contention rises or falls upon whether the terminations were proper, but for reasons set out in Point III(A), *supra*, the terminations were improper and breached § 7.8(a)(xi)(B).

[28] The word "capable" means that rescission was "possible," not probable or likely. *Madison Gas & Elec. Co. v. S.E.C.*, 168 F.3d 1337, 1340 (D.C. Cir. 1999) (a requirement that electrical systems of merging utilities be "capable of physical interconnection" means that it is "possible to interconnect them," not that they be connected); *cf. Spancrete Ne., Inc. v. Occupational Safety & Health Review Comm'n*, 905 F.2d 589, 594 (2d Cir. 1990) (the term "'feasible' means 'possible' or 'capable of being done'"); *U.S. v. Mike*, 655 F.3d 167, 174 (3d Cir. 2011) (finding a gun without its firing bolt and was therefore inoperable was still "capable" of firing a bullet). Merriam-Webster's dictionary defines "capable" as "having traits conducive to or features permitting." *Capable Definition*, MERRIAM WEBSTER ONLINE DICTIONARY, http://www.merriam-webster.com/dictionary/capable (last visited April 15, 2016).

C. Section 7.5(f) of the Indenture Was Not Satisfied (Moving Br. 18-20)

The Pyxis Defendants conceded that Pyxis violated § 7.5(f) if that provision can be read "in isolation." Moving Br. at 18-19. Section 7.5(f) required that Pyxis attempt to enter into a replacement agreement and it is conceded that Pyxis failed to comply with this requirement. Lacking any other answer to § 7.5(f), the Pyxis Defendants argue that the Reinvestment Period ended by September 2008, when Pyxis terminated the Transactions and the Pyxis Credit Default Swap Agreement. Moving Br. 19. The Pyxis Defendants contend that because the Reinvestment Period had ended Pyxis did not need to comply with § 7.5(f). This argument fails for two reasons.

First, Movants' argument that the Issuer could not enter into a replacement Swap because the Trustee had terminated the Reinvestment Period ignores the provision in § 12.2 that the Issuer may enter into Synthetic Securities both during the Reinvestment Period and after the Reinvestment Period if it had committed to do so before the end of the Reinvestment Period. Section 7.5(f) constitutes such a commitment by the Issuer (undertaken long before the Reinvestment Period) to use reasonable efforts to enter into a replacement Swap. In any event, allowing a cure of the Ratings Event would not implicate the Reinvestment Period since it would not constitute a reinvestment, only the continuation of an existing investment.

Second, § 7.5(f) does not refer to § 12.2, nor suggest that by § 12.2 could alter its clear mandate. Ex. A, § 7.5(f). In fact, § 7.5(f) does contain a clear cross reference to § 12.3(d), but no cross reference at all to § 12.2. *Id.* Thus, the drafters must be presumed to have made a conscious decision to avoid importing the limitations of § 12.2 into § 7.5. *Cf. Kaplan v. First Options of Chicago, Inc.*, 19 F.3d 1503, 1515 (3d Cir. 1994), *aff'd*, 514 U.S. 938 (1995) ("The absence of . . .

a cross-reference . . . unambiguously shows their limited contractual obligation to provide funds to MKI was separate from and independent of MKI's obligations . . . .").[29]

IV. LBSF ADEQUATELY PLED THAT THE PYXIS CREDIT DEFAULT SWAP WAS TERMINATED IN BREACH OF THE CURE PROVISION IN THE SCHEDULE (Moving Br. 9-14)

A. The Pyxis Trustee Wrongfully Denied LBSF the Agreed Upon Cure Period Following the Ratings Event (Moving Br. 9-11)

The Pyxis Defendants contend that § 6(a) of the Master Agreement permitted termination of Transactions under the Swap Agreement, without regard to the ten business-day period to cure a Ratings Event in the Schedule. *See* Ex. B, Schedule, Part 5(k)(iv). The Pyxis Defendants' position fails because Part 5(k)(iv), which the parties specifically negotiated, explicitly controls over inconsistent provisions such as § 6(a) of the Master Agreement. *See id.* Master Agreement, § 1(b).

LBHI's September 15, 2008 bankruptcy filing was an Event of Default under the Pyxis Master Agreement. *See id.* § 5(a)(vii)(4). The next day, credit rating agencies downgraded LBHI, triggering a Ratings Event pursuant to the Schedule. *See id.* Schedule, Part 5(k)(iii). After a Ratings Event, the Schedule provides that LBSF, with assistance of Pyxis, has ten business-days (in this case, until September 30, 2008) in which it could obtain (i) an Eligible Guarantee of its obligations from a guarantor that satisfied the Required Ratings, or (ii) a substitute counterparty that satisfied the Required Ratings (*i.e.*, assign its position under the Swap Agreement to an eligible counterparty). *Id.* Part 5(k)(iv).

The right to cure the Ratings Event under Part (5)(k)(iv) is "inconsistent" with exercise of the right to terminate for Default.[30] The occurrence of an Event of Default coincided with a Ratings

[29] *MJCM, LLC. v. First Ga. Bank, Inc*., 392 F. Supp. 2d 901, 906 (S.D. Tex. 2005) (omission of cross reference "indicates an intent to separate a change of ownership from other types of terminating events" (internal quotations omitted)), *aff'd sub nom., MJCM, L.L.C. v. United Cmty. Banks, Inc*., 212 F. App'x 323 (5th Cir. 2007); *cf. U.S. v. Wray*, 776 F.3d 1182, 1188 (10th Cir. 2015) ("If the . . . Commission wanted to cross-reference to the definition . . . it easily could have done so.").

[30] "Inconsistent" means "containing incompatible elements." *Inconsistent Definition*, MERRIAM WEBSTER ONLINE DICTIONARY, http://www.merriam-webster.com/dictionary/inconsistent (last visited April 15, 2016).

Event, which put the rights to terminate under § 6(a) of the Master Agreement in direct conflict with Part 5(k)(iv) of the Schedule. As set out below it would be "inconsistent" with Part 5(k)(iv) to allow the Trustee to designate an Early Termination Date and deprive LBSF of its ten-day cure period based upon the same events that had already given rise to the Ratings Event and cure period. In the event of such inconsistency the Schedule controls. *See* Ex. B, Master Agreement § 1(b). Accordingly, the Trustee's failure to give LBSF the right to cure materially breached both the Swap Agreement and the Indenture provisions prohibiting termination of the Swap Agreement. *Filmline (Cross-Country) Prods., Inc. v. United Artists Corp.*, 865 F.2d 513, 518 (2d Cir.1989).[31]

B. The Termination Notices Violated Part 5(k)(iv) of the Schedule (Moving Br. 10-12)

In breach of Part 5(k)(iv) of the Schedule, on September 19, 2008, the Pyxis Trustee issued a termination notice which informed market participants that the CDS Agreement and all Transactions thereunder were terminated, thereby actively thwarting LBSF's ability to exercise its assignment or cure rights under the Schedule, when seven business (and eleven calendar) days remained in the cure period. Ex. H. On September 24, 2008, the Pyxis Trustee issued another flawed termination notice, which reiterated termination of the Swap Agreement, Ex. I, even though five business (and seven calendar) days remained in the Ratings Event cure period. In doing so, the Pyxis Trustee improperly abrogated LBSF's ability to exercise its rights pursuant to the Schedule, thereby breaching the Indenture and the Swap.

The Pyxis Defendants argue that a Ratings Event was merely an Additional Termination Event meant to protect Pyxis from a deterioration of LBSF's creditworthiness. Moving Br. at 12. The Pyxis Defendants further argue that LBSF's position would mean that the Ratings Event

[31] *See also Needham v. Candie's, Inc*., No. 01 Civ. 7184 LTS FM, 2002 WL 1896892, at *3 (S.D.N.Y. Aug. 16, 2002), *aff'd*, 65 F. App'x 339 (2d Cir. 2003); *Point Prods. A.G. v. Sony Music Entm't, Inc.*, 93 Civ. 4001(NRB), 2000 WL 1006236, at *3 (S.D.N.Y. July 20, 2000).

"improved" LBSF's position to the detriment of Pyxis, thereby "depriving" Pyxis of its termination right under Swap Agreement § 6(a) based on the LBHI Bankruptcy Event of Default. *Id.*

However, the parties specifically contemplated that a Ratings Event could occur when the transactions under the Credit Default Swap Agreement were deeply "in-the-money" to LBSF. Otherwise, LBSF would not have bargained for the right to assign its swap positions. Thus the parties agreed that in that situation LBSF could extract the value of its position. In fact, the value of LBSF's position as of the purported Early Termination Date was significantly more than the value of Pyxis's assets (Ex. M), which means the Controlling Class would have been contractually required to make up any shortfall up to a cap. *See* Ex. G, § 2.3(c)(ii). For this reason, the Controlling Class did not elect to exercise its right to terminate the swap transactions and liquidate the Collateral after the February 1, 2008 Event of Default. FAC ¶ 92.

1. The Coincidence of an Event of Default with a Ratings Event Does Not Alter LBSF's Right to Assign Its Position Under the Pyxis Credit Default Swap Agreement (Moving Br. 10-12)

As the Pyxis Defendants do not deny, a Ratings Event, standing alone, could trigger Part 5(k)(iv) of the Schedule and provide LBSF with a ten business-day window to assign or cure. Similarly, LBSF does not deny that an Event of Default, occurring in isolation, would give the non-defaulting party the right to terminate the Swap. *See* Ex. B, Master Agreement § 6. In this case, however, the Ratings Event had occurred and the cure period had already commenced when the Trustee purported to terminate the CDS Agreement and the Transactions thereunder. The right to terminate and the right to cure cannot co-exist and are therefore inconsistent with each other. Section 1(b) of the Master Agreement provides that in the event of such an inconsistency the rights arising under the Schedule controls over the rights arising under the Master Agreement. The only reasonable reading which gives effect to all of the terms of the agreement, as Defendants claim is required, would defer the right to terminate for default until after the Ratings Event Cure Period had expired, or a cure had been effected. If a cure was effected, then the counterparty would not be

prejudiced and would have received the full benefit of its bargain when a creditworthy party was substituted in place of LBHI.[32] Denying LBSF its ability to cure by a hasty termination, however, eliminates one of LBSF's bargained for rights which takes precedence over the termination right.

The Pyxis Defendants argue that termination based upon a Ratings Event (Ex. B, Schedule Part 5(k)(iv)) and termination based upon an Event of Default (*Id.* Master Agreement § (6)(a)) are "independent termination right[s]," (Moving Br. at 9), and that the "cure provision" does not pertain to, or limit, terminations under § 6(a). *Id.* at 10. But, the Event of Default does not change the fact that the Ratings Event gave LBSF rights and remedies under Schedule Part 5(k), including the right to a ten business-day cure period to obtain an Eligible Guarantee or substitute counterparty. It does not matter that the Ratings Event occurred one day after the Event of Default because the Event of Default did not terminate LBSF's rights under the Swap Agreement and Schedule. Automatic Early Termination did not apply under the Pyxis Swap, and thus notice was required to effect termination. Ex. B, Schedule, Part 1(d). Accordingly, on the date of the Rating Event, LBSF still possessed all of its rights, including its right to the ten business-day cure period. In short, where, as here, a Rating Event followed an Event of Default and occurred before notice of termination was given, LBSF's extant rights to cure by assignment and substitution under Parts 5(k)(iv) and 5(e) of the Schedule overrode the Pyxis Trustee's right to terminate the Master Agreement. Any other result fails to give effect to the Schedule's predominance over the Master Agreement.

2. LBSF's Position is Commercially Reasonable (Moving Br. 12)

The Pyxis Defendants baldly assert that LBSF's position is "absurd, commercially unreasonable, or contrary to the reasonable expectations of the parties." Moving Br. at 12. There is no basis for such conclusions to be drawn on this Motion. If the Court finds no ambiguity in the

[32] The Court may take judicial notice that in other proceedings in the LBHI chapter 11 cases, the Court approved the substitution of Deutsche Bank for LBSF and LBHI as Swap Counterparty and Guarantor, which shows that cure was possible had it not been undermined by the Trustee's notices. *See* Ex. N, May 8, 2009 Tr. of Hr'g, at 57:8:58:2 (the Court will enter an order approving agreement substituting Deutsche Bank for LBSF and LBHI in swap agreement).

agreements, it can interpret them on this Motion, and LBSF's interpretation makes more sense than Movants'. If the Court finds the agreements to be ambiguous, then any determination of commercial unreasonableness or failure to adhere to the parties' contractual intent cannot be made without considering evidence of the agreements' meaning, which the Court may not do on this Motion. *See* pp. 9-10, *supra*. As noted above, LBSF protected its position in the event of a downgrade by obtaining the ability to assign its position in the CDS Agreement. Moreover, this power is found in the Schedule and departs from the standard terms of the ISDA Master Agreement. It was thus a product of the parties' negotiations and reasonable expectations. The right to cure a Ratings Event is enhanced by the protections in the Indenture against premature termination of the Swap Agreement and the Transactions. *See* Ex. A, § 5.2

The Pyxis Defendants illogically argue that giving effect to LBSF's cure right is commercially unreasonable, or would upset the parties' expectations. Moving Br. at 12. In fact, it is the Pyxis Defendants' position that leads to absurd results. The Pyxis Defendants assert that no conditions other than notice limit Pyxis's alleged right to terminate all transactions upon an Event of Default. Moving Br. at 10. However, if after a Ratings Event the Pyxis Trustee could simply terminate the transactions under the Credit Default Swap Agreement (as it did here) with no cure period before LBSF could try to find an Eligible Guarantor or substitute counterparty, then the cure right would be ephemeral and Part 5(k)(iv) would be meaningless.[33]

In any event, the Pyxis Defendants' contention that LBSF's position leads to "absurd" and "commercially unreasonable" results, (Moving Br. 12), raises a question of fact as to whether LBSF's position comports with the business purpose behind the "Downgrade Provisions" in Part 5(k) of the Schedule, and whether, at a minimum, the covenant of good faith and fair dealing prevents the Pyxis Defendants from taking actions which "have the effect of destroying or injuring

[33] The Pyxis Defendants cite one irrelevant case where the court held the term "Schedule" was ambiguous. *Homeward Residential, Inc. v. Sand Canyon Corp*., 298 F.R.D. 116, 130 (S.D.N.Y. 2014) (denying dismissal of contract claims).

the right of [LBSF] to receive the fruits of the contract." *Claridge v. N. Am. Power & Gas, LLC*, No. 15-cv-1261 PKC, 2015 WL 5155934, at *6 (S.D.N.Y. Sept. 2, 2015) (citation omitted).

Contrary to the Pyxis Defendants' position, (Moving Br. at 10-11), it is the Pyxis Defendants' interpretation, not LBSF's, that would render Part 5(k)(iv) of the agreement superfluous. To avoid such an outcome, this Court should find that the parties' rights when a Ratings Event coincides with an Event of Default must be harmonized by § 1(b) of the Swap Agreement, which provides that the provisions of the Schedule prevail.

CONCLUSION

For the foregoing reasons, LBSF respectfully requests that the Court deny the Pyxis Defendants' Motion to Dismiss the Pyxis Counts in the Fourth Amended Complaint.

Dated: New York, New York
April 19, 2016

By: /s/ Paul R. DeFilippo
William A. Maher
Paul R. DeFilippo
William F. Dahill
Vincent T. Chang
Jason E. Glass
Mara R. Lieber

WOLLMUTH MAHER & DEUTSCH LLP
500 Fifth Avenue
New York, New York 10110
(212) 382-3300

Counsel for Plaintiff Lehman Brothers Special Financing Inc.