[*1]

SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: BERNARD J. FRIED J.S.C. PART 60

Index Number : 601380/2005

TRILOGY PORTFOLIO COMPANY LLC.

VS

TRANSAMERICA OCCIDENTAL LIFE

Sequence Number : 001

PARTIAL SUMMARY JUDGMENT

INDEX NO. 601380/05

MOTION DATE 1/20/06

MOTION SEQ. NO. 1

MOTION CAL. NO. _____

The following papers, numbered 1 to _____ were read on this motion to/for _____

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	
Answering Affidavits — Exhibits	
Replying Affidavits	

Cross-Motion: ☐ Yes ☐ No

Upon the foregoing papers, it is ordered that this motion

FILED
JAN 23 2006
COUNTY CLERK'S OFFICE
NEW YORK

This motion is decided in accordance with the accompanying memorandum decision.

SO ORDERED

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

Dated: 1/20/06

BERNARD J. FRIED J.S.C.

Check one: ☐ FINAL DISPOSITION ☒ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 60

----------X

TRILOGY PORTFOLIO COMPANY, LLC, HARBERT DISTRESSED INVESTMENT MASTER FUND, LTD., and FREEDOM POWER CORP.,

Plaintiffs,

Index No. 601380/05

-against-

TRANSAMERICA OCCIDENTAL LIFE INSURANCE CO., MONUMENTAL LIFE INSURANCE CO., BEAR, STEARNS & CO., MERRILL LYNCH CREDIT PRODUCTS, LLC, LONGACRE CAPITAL CORP., J.P. MORGAN LVELEC CORP., AND LIBERTY ELECTRIC PA., LLC

Defendants.

----------X

FRIED, J.:

Defendants Transamerica Occidental Life Ins. Co. (Occidental), Monumental Life Ins. (Monumental) Co., Bear Stearns & Co. (Bear, Stearns), Merrill Lynch Credit Products, LLC (Merrill Lynch) and Longacre Capital Corp. (Longacre) move, pursuant to CPLR 3212, for an order granting them summary judgment dismissing the complaint of plaintiffs Trilogy Portfolio Co.(Trilogy), LLC, Harbert Distressed Investment Master Fund, Ltd. (Harbert) and Freedom Power Corp. (Freedom).

Plaintiffs have discontinued the action against Occidental and Monumental, as well

as against the Bank of New York (BONY). Bear Stearns, Merrill Lynch and Longacre, collectively referred to as the Member Defendants, remain in the case.[1]

Plaintiffs are "Tranche A" debt holders of Liberty Electric PA,, LLC (Borrower), and the Member Defendants hold Tranche B debt of Borrower. Borrower is a wholly owned subsidiary of LEP Holdings, LLC. (LEP). In other words, LEP's sole asset is the equity of Borrower. Borrower, in turn, owns Liberty Electric Power, LLC (Project Company). Project Company and Borrower are referred to as the Obligors. Project Company owns an electric generating plant in Pennsylvania (Project).

The Project generates electricity by burning fuel. Towards that end, Borrower entered into an agreement with a company called PG & E Energy Trading Power, L.P. (Counterparty), under which the Counterparty had the right to supply the Project with fuel, which the Project would then convert into electricity for the Counterparty in exchange for pre-arranged fees to be paid by the Counterparty to the Borrower. The term of the Tolling Agreement was to extend to 2016, with a two-year extension available at the option of the parties. The Counterparty is an affiliate of a company called PG & E National Energy Corp.

The Project was financed under a series of agreements which were made in 2000. There were a Master Agreement, a Credit Agreement, a Note Purchase Agreement, a Collateral Agency and Intercreditor Agreement, and a Pledge and Security Agreement.

The project finance arrangements included a bank facility, as evidenced by the Credit Agreement. This represents the Tranche A Debt. The Credit Agreement provided for a loan

---

[1]According to the papers, Harbert has actually purchased some Tranche B, debt, but Harbert nevertheless supports the position of Trilogy regarding the instant dispute.

of up to $168.5 million. The Tranche A lenders, Borrower, and an Administrative and Collateral Agent were parties to the Credit Agreement.

In addition, there was a long-term loan provided by institutional investors, evidenced by the Note Purchase Agreement. This loan constitutes the Tranche B debt. The Note Purchase Agreement called for a loan of up to $165 million, maturing in 2026. Under the Note Purchase Agreement, Borrower is required to make payments of principal and interest, and Project Company is the guarantor.

The institutional investors contemplated that the loan would be less profitable if it were repaid, prior to maturity, at a time when interest rates were low. In other words, if the proceeds of repayment were re-loaned to a new debtor, at a lower interest rate than that previously paid by Borrower, the institutional lenders would make smaller profits. Accordingly, the institutional investors obtained, in the Note Purchase Agreement, a formula to compensate them for the difference between the contract rate of interest and the market rate of interest at the time of repayment. The formula, known as the Make-Whole Amount, is contained in Annex I to the Note Purchase Agreement:

> With respect to any Note, an amount equal to the excess, if any, of the Discounted Value of the Remaining Schedule Payments with respect to the Called Principal of such Note over the amount of such Called Principal, PROVIDED that the Make-Whole Amount may in no event be less than zero.

The Master Agreement ties the project financing arrangements together. The Master Agreement was made by Borrower, Project Company, and some of the bank lenders and institutional investors.

Section 9.1 of the Master Agreement enumerates twenty-two events of default. Subsections (a) and (b) provide, in pertinent part, that if "the Borrower shall default in the payment when due of any principal under any Loan Agreement whether at maturity, at a date fixed for payment, or otherwise" or if "the Borrower shall default in the payment when due of interest under any Loan Agreement or any fee," then an Event of Default has occurred. Other Events of Default include circumstances under which the Tolling Agreement is no longer a valid and binding agreement and is not replaced with terms acceptable to the Administrative Agent within 20 days, or the bankruptcy of the Counterparty's parent company.

Upon the occurrence of any of the listed Events of Default, the loan may be accelerated by the Administrative Agent. If the loans are accelerated, the Borrower, becomes obligated to pay the Tranche B lenders the Make-Whole Amount. The only exception (Exception) to the Make-Whole provision is that the Borrower is not obligated to pay the Make-Whole amount where "*the Event of Default that resulted in acceleration or termination was not solely or in a material part attributable to the actions or omissions of one of more of the Obligors* [emphasis supplied]..."

The Counterparty supplied fuel to the Borrower until mid-2003. At that point, the Counterparty and its affiliate both filed for bankruptcy.

The Tranche A and B Debt went into default in 2003, and was accelerated in 2004. In a consensual workout proceeding, certain of the Tranche A and B holders became

members of LEP Holdings, LLC (LEP), the parent company of Borrower[2] There were several events leading up to this action. Borrower had failed to make payments of principal and interest. Moreover, the Counterparty and its affiliate filed for Chapter 11 bankruptcy. In the Counterparty's bankruptcy action, it rejected the Tolling Agreement. When Borrower and the Project Company failed to find a replacement for the Tolling Agreement within 120 days of its rejection, an Event of Default was deemed to have occurred under the terms of the Master Agreement.

In late 2004, the holders of two-thirds of the loans (including some of the Tranche A Debt holders) instructed JP Morgan Chase, which was then the Administrative Agent (later replaced by BONY) to accelerate the loan.

As a result of the Counterparty's rejection of the Tolling Agreement, Borrower brought an arbitration proceeding. Borrower received an award of $153 million, of which $140 million has been paid. The instant dispute relates to the distribution of the $140 million in proceeds. The money is currently being held by the BONY, which intends to withdraw as administrative agent but which continues to hold the proceeds until a successor is named.

The Member Defendants contend that they are entitled to the Make-Whole Amount. Plaintiffs, on the other hand, contend that the events of default which led to the acceleration were not due to the acts or omissions of Borrower, and that the Make-Whole provision does not apply. The complaint alleges that the Member Defendants are unlawfully attempting to procure the payment of the Make Whole Amount to the Tranche B holders. Counts I and

---

[2] According to plaintiffs' response to defendants' Rule 19-a statement, Trilogy is a member; Harbert is not itself a member, but its affiliate, Freedom Power, is a member).

II, which are brought derivatively on behalf of LEP, allege a breach of fiduciary duty. Counts III and IV, which are asserted on behalf of plaintiffs individually, also allege a breach of fiduciary duty. In Counts V and VI, plaintiffs allege that payment of the Make-Whole Amount would constitute a breach of contract; plaintiffs seek declaratory and/or injunctive relief.

Defendants make the following arguments in support of their contention that the exception does not apply:

(1) The Note Purchase Agreement itself contains unconditional promises to pay interest and fees (Note Purchase, § 2.3 and 2.4). Had the parties intended to make payment of principal and interest conditional upon the continued vitality of the Tolling Agreement, they could have done so.

(2) The notes do not mature until 2026, yet the Tolling Agreement expires in 2016. Had the parties intended to make the payments of interest, principal or fees conditional upon the continued vitality of that agreement, they would have provided some sort of protective provision, e.g. for deferment or a moratorium on payments for Borrower in the event that the Tolling Agreement was not renewed.

(3) By defendants' definition, any failure of Borrower to pay the loan, regardless of the economic cause of that failure, constitutes an act or omission of the Borrower.

(4) The Make-Whole Amount (Annex 1 to Note Purchase Agreement, Renwick affidavit, Exhibit 3), requires that payments that would have been made except for the pre-payment be discounted under the defined "Reinvestment Yield." The Reinvestment Yield changes depending on whether the Tolling Agreement is in effect. Before expiration of the initial and

extended "Tolling Periods," the Reinvestment Yield is one figure (1.0% over yield to maturity). After expiration of the Tolling Period, it is a different figure(.5% over yield). "Tolling Period is defined as "any time when the Tolling the Agreement, or an Alternative Power Agreement, is in full force and effect [Master Agreement, Appendix A, page 89]." In other words, in defendants' view, the parties must have intended that the Make-Whole provision was intended to apply even if the Tolling Agreement revenue ceased, because the parties agreed on a rate that was to apply if there were no Tolling Agreement in effect.

(4) Some of the defaults listed in § 9.1 of the Master Agreement specifically arise from actions of third parties, and might not be solely or in material part due to the actions or omissions of Borrower. Here are a few examples: (a) the uncured default of any Major Project Party other than the Obligors; (b) the commencement of a proceeding, without the consent of Obligors, seeking, among other things, liquidation, reorganization or dissolution; and (c) the taking of any portion of the Project by the Government through eminent domain. In other words, to defendants, it is significant that the parties enumerated situations in which defaults would result without the fault of Borrower, but did not indicate that there were any situations under which the Borrower's failure to pay principal, interest and fees would not be deemed to be the fault of Borrower.

(5) The mere loss of the Tolling Agreement is not an automatic default. It can become a default, however, if the agreement is not replaced in a 120-day period. Although the Tolling Agreement has a default provision, the payment obligations in § 9.1(a) and (b) of the Master Agreement do not contain any kind of cross-reference or other linkage with the Tolling Agreement.

(6) In several other places, i.e., §§ 9.1(e), (f), (g) and (m) of the Master Agreement, the provisions contain exceptions under which the acceleration would not occur. In other words, where the parties made defaults conditional upon other events, they specifically said so. Therefore, in defendants' view, since no conditions appeared in subsections (a) and (b) (referring to interest and fees), this must have meant that the defaults would be deemed to occur regardless of any conditions such as the loss of the Tolling Agreement.

Plaintiffs argue as follows:

(1) The fact that Section 9.1(i) and (l) itself make the bankruptcy of the Counterparty an event of default meant that lenders recognized a direct linkage between the continued vitality of the Tolling Agreement and the ability of the Obligors to repay the loan.

(2) If the defendants wanted the result sought here, they should have insisted upon specific language in §§ 9.1(a) and (b) to the effect that any failure to pay would trigger the Make-Whole Amount. No such language appears in those subsections.

(3) Since the words "solely or in a material part attributable to the actions or omissions of one of more of the Obligors" are not defined, it is improper to classify strictly the Events of Default as fault or no-fault on the part of Borrower. In other words, it is significant that the Make-Whole provision does not expressly delineate between the various subsections of § 9.1.

(4) Under § 9.1(h) of the Master Agreement, one possible default scenario is where the Counterparty is forced into Bankruptcy, and that bankruptcy can be expected to result in a Material Adverse Effect." In the Master Agreement, "Material Adverse Effect" includes:

> a material effect on (a) the ability of an Obligor to perform

> any of its material obligations under the Financing Documents or the Major Project Documents to which it is a party...[Master Agreement, p. 79, Appendix A, definition of "Material Adverse Effect"].

Under 9.1(h), defendant concedes that the Make-Whole Amount is not payable where the Counterparty is subject to an involuntary bankruptcy proceeding that can reasonably be expected to affect, adversely, Borrower's ability to make principal, interest or fee payments. The bankruptcy of the Counterparty is not itself a cause of default, but, by reason of its effect, can lead to other default-causing events (see p. 13 of plaintiff's brief for provision).

(5) Under Section 7.19 of the Master Agreement, not later than six months before the end of the "initial Tolling Period," e.g. the term of the Tolling Agreement, Liberty is required to submit to the Administrative Agent for approval "proposed energy management procedures and general contract terms for the sale of electric power and the purchase of natural gas during any period in which a Tolling Period is not in effect." These proposals presumably might have included a new tolling agreement or alternative ways of selling Borrower's power generating capacity. In plaintiff's view, if the Tolling Agreement ended (by expiration of its terms or by breach) and Borrower failed to make a reasonable effort to find an alternative buyer for electricity, the Borrower's inability to make loan payments would be due to Borrower's own act or omission. However, in the arbitration proceeding against the Counterparty, the arbitrator found that Borrower made a reasonable effort to obtain an alternate buyer, but was unsuccessful. Although the arbitrator's award is not binding on the Member Defendants with respect to this issue, there is at least a triable issue of fact as to

whether Borrower made a reasonable effort to mitigate damages when the Counterparty repudiated the Tolling Agreement.

Where the language of the governing provisions is clear and unambiguous, the determination of the parties' intent is a question of law for the courts, which may be decided on a motion for summary judgment (Chimart Assocs. v Paul, 66 NY2d 570 [1986]). This is particularly true where the agreement is between sophisticated commercial entities and sets forth the parties' entire agreement (Vermont Teddy Bear Co. v 538 Madison Realty Co., 1 NY3d 470 [2004]).

The contract, by its express terms, provides that the Make-Whole provision is not applicable where "the Event of Default that resulted in acceleration or termination was not solely or in a material part attributable to the actions or omissions of one of more of the Obligors." It is correct, as the Member Defendants point out, that several of the defaults enumerated in Section 9.1 of the Master Agreement provide for certain conditional defaults, while no conditions are contained in the payment default provisions, 9.1(a) and (b). However, since the Exception to the Make-Whole provision does not contain any limitations on its applicability, it applies to any situation where a "default" occurred despite Borrower's efforts to prevent or minimize the problem. In other words, even though Section 9.1 of the Master Agreement contains subsections specifying defaults which might potentially occur without any wrongful conduct on the part of Borrower, nothing in the language of Section 9.1 provides that those are the only "non-fault" defaults that might occur.

At the time of the execution of the loan agreements, plaintiffs and defendants were lenders, not equity owners. The Borrower, not the lenders, assumed the risk that the revenue

stream provided under the Tolling Agreement might be lost if the Counterparty became financially distressed. The loan agreements contained unconditional promises by Borrower to pay principal and interest, whether or not the expected Tolling Agreement revenue stream continued to flow. However, the Make-Whole provision stands on an entirely different footing. It represents an extra payment to the Tranche B debtors, to give them the benefit of the higher interest rates provided under the Note Purchase Agreement, even if market interest rates have fallen at the time that the loan is accelerated. The Make-Whole amount was designed to discourage Borrower from voluntarily pre-paying the loan, or from allowing the loan to go into default by reason of an affirmative act or a neglect to act.

When the Counterparty declared bankruptcy, and this led to the loss of the Tolling Agreement, Borrower's source of revenue was cut off. If Borrower made no effort to find a substitute buyer for the electricity, then the default in payment of principal, interest and fees (Master Agreement Sections 9.1 [a] and [b]) may be the fault of Borrower. In such a case, the Make-Whole provision likely would be applicable. On the other hand, if, despite best efforts, Borrower was unable to find a suitable substitute Buyer for the electricity, then the default may not solely or in a material part due to the actions or omissions of Borrower, and in that case, the Make-Whole provision likely would not apply.

In Borrower's successful prosecution of the arbitration proceeding against the Counterparty, the arbitration award contained a finding that Borrower made reasonable, albeit unsuccessful, efforts to find a substitute buyer for electricity who would have provided the same revenue as that previously earned under the Tolling Agreement Since the Member Defendants were not parties to the arbitration proceeding, this finding does not have a res

judicata or collateral estoppel effect against them (see e.g., Goepel v. City of New York, 23 AD3d 344 [2d Dept 2005]). Therefore, since there is an issue of fact as to whether Borrower's default in payment of principal and interest was due to an act or omission of Borrower. This case cannot be decided on the basis of the affidavits and exhibits submitted.

Accordingly, it is

ORDERED that the defendants' motion for summary judgment is denied, and it is further

ORDERED that a conference will be held on February 8, 2006 at 10 a.m., in Part 60, Room 540, 60 Centre Street, New York, NY.

Dated: 1/20/06

J.S.C.

BERNARD J. FRIED
J.S.C.

FILED
JAN 23 2006
COUNTY CLERK'S OFFICE
NEW YORK