

**Edgewater Growth Capital Partners, L.P. v Allied
Capital Corp.**

2008 NY Slip Op 33021(U)

November 3, 2008

Supreme Court, New York County

Docket Number: 600919/08

Judge: Richard B. Lowe

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SCANNED ON 11/7/2008
[*1]
SUPREME COURT OF THE STATE OF NEW YORK – NEW YORK COUNTY

PRESENT:

HON. RICHARD B. LOWE, III

PART 56

Justice

Index Number : 600919/2008

EDGEWATER GROWTH CAPITAL PARTNERS

VS.

ALLIED CAPITAL CORPORATION

SEQUENCE NUMBER : # 001

DISMISS COMPLAINT

INDEX NO. 600919-08

MOTION DATE

MOTION SEQ. NO. #001

MOTION CAL. NO.

are 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
NOV 07 2008
COUNTY CLERK'S OFFICE
NEW YORK

MOTION IS DECIDED IN ACCORDANCE
WITH ACCOMPANYING MEMORANDUM DECISION

Dated: 11/3/08

HON. RICHARD B. LOWE, III

J.S.C.

Check one: FINAL DISPOSITION NON-FINAL DISPOSITION

Check if appropriate: DO NOT POST REFERENCE

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

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 56

-----X
EDGEWATER GROWTH CAPITAL PARTNERS, L.P.,

Index No. 600919/08

Plaintiff,

- against -

ALLIED CAPITAL CORPORATION and MAPS
CLO FUND I, LLC,

Defendants.

FILED
NOV 07 2008
COUNTY CLERK'S OFFICE
NEW YORK

Hon. Richard B. Lowe, III:

Defendants move to dismiss the complaint, pursuant to CPLR 3211 (a) (1).

Background

Plaintiff Edgewater Growth Capital Partners, L.P. (Edgewater) and defendants Allied Capital Corporation (Allied) and Maps Clo Fund I, LLC (Maps) are the junior lenders to a group of companies making up the nation's largest independent service provider for automated teller machines and other cash security provided by banks and other retail establishments (the Company or the Borrower). Allied holds approximately 80% of the junior loans and Maps and Edgewater hold approximately 10% each. As the administrative agent and collateral agent for the junior lenders, Allied holds an agent's lien on the collateral securing the junior loans.

The junior lenders' relationship is governed by their Credit Agreement and its amended versions. Edgewater was not an original maker of the Credit Agreement. Edgewater became party to that agreement by entering into a Fourth Amendment to the Credit Agreement.

In addition to owing money for loans made by the junior lenders, the Company owes

money for loans made by senior lenders. The senior lenders' loans are secured by a first lien on the Company's assets, and the junior loans are secured by a second lien on the same assets.

About December 2007, the senior lenders decided to foreclose on the Company's assets and scheduled a public auction for March 2008. Upon learning of this plan to foreclose, Allied, in its role as agent for the junior lenders, contacted the senior lenders with objections. Defendants, the Company, and the senior lenders negotiated a Settlement Agreement, whereby defendants agreed not to contest the foreclosure sale. The senior lenders agreed to afford each junior lender, including plaintiff, a post-foreclosure sale opportunity to exchange its share of the junior loans for stock in the Proposed Buyer (an entity identified by name in the Settlement Agreement as the buyer at the foreclosure sale) or to sell its junior loans to the senior lenders.

As stated in the Settlement Agreement, as of March 18, 2008, the approximate principal and interest owed to Allied was \$43 million, to Maps, \$5 million, to Edgewater, \$4.8 million, and to the senior lenders \$90 million (Settlement Agreement, ¶¶ 7 [c], 9 [c]). Edgewater chose not to enter into the Settlement Agreement, on the basis that the foreclosure was a sham. According to Edgewater, the senior lenders designed the foreclosure sale so that the Proposed Buyer, an entity that they control, could purchase the Company's assets at an artificially low price. The sale is allegedly designed to prevent bidding by any other entity. Edgewater's complaint claims that defendants, by entering into the Settlement Agreement with the senior lenders, breached the junior lenders' Credit Agreement.

The Credit Agreement provides that no party may, without the consent of all of the junior lenders, release any lien on the collateral securing the junior loans, release the Company from any of its obligations, or reduce the amounts payable on the loans. Edgewater alleges that the

Settlement Agreement does all these things, to which Edgewater did not consent. Regarding the provision that the junior lenders may exchange their loans after the foreclosure sale takes place, Edgewater claims that such an action will strip the Borrower of its assets. The Borrower will then be unable to pay its obligations.

Defendants move to dismiss the complaint on the basis of documentary evidence, arguing that the agreements belie the allegations in the complaint. First, defendants claim that the Settlement Agreement does not release collateral, release the Company from its obligations, or reduce the amounts payable on the junior loans, and that it does not affect Edgewater's right to full repayment of its loans. Second, they argue that, even if the Settlement Agreement did release liens on the collateral, that would not violate the Credit Agreement, because the Fourth Amendment to the Credit Agreement allows defendants to release collateral without Edgewater's consent.

Discussion

On a motion to dismiss pursuant to CPLR 3211, the allegations in the complaint must be accepted as true, and the court must grant plaintiffs the "benefit of every possible inference, and determine only whether the facts as alleged fit within any cognizable legal theory" (*Goldman v Metropolitan Life Ins. Co.*, 5 NY3d 561, 570-71 [2005] [quotation marks and citations omitted]). Under CPLR 3211 (a) (1), a dismissal "may be granted where documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law" (*id.* at 571 [citation omitted]). Since the parties' arguments center around the interpretation of the Credit Agreement, the Fourth Amendment to the Credit Agreement, and the Settlement Agreement, the relevant provisions of these contracts must be closely examined.

Count one of the complaint alleges that Allied breached section 15.12 of the Credit Agreement by releasing its agent's lien on the collateral securing the junior lenders' loans. That section provides that Allied may not release a lien on any of the collateral securing junior loans without the prior written consent of all the junior lenders. Upon a request by the Agent, the lenders will confirm in writing the agent's authority to release said liens, "provided, however, that (1) Agent shall not be required to execute any document necessary to evidence such release on terms that, in Agent's opinion, would expose Agent to liability or create any obligation or entail any consequence other than the release of such Lien without recourse, representation, or warranty, and (2) such release shall not in any manner discharge, affect, or impair the Obligations or any Liens (other than those expressly being released) ... " (Credit Agreement, ¶ 15.12).

According to defendants, section 4 (o) of the Fourth Amendment, which recites that it amends section 14.1 of the Credit Agreement, changes the requirement that Edgewater must consent to Allied's release of a lien. Section 14.1 of the Credit Agreement provides that the junior loans may not be amended or waived without the written consent of the junior lenders, and that such consent is effective only in the specific instance for which it is given, "provided, however, that no such waiver, amendment, or consent shall, unless in writing and signed by all of the Lenders" do any of the activities listed from (a) to (k) (Credit Agreement, ¶ 14.1). The prohibited activities pertinent to this motion are: part (c), "reduce the principal of, or the rate of interest on, any loan or other extension of credit hereunder, or reduce any fees or other amounts payable hereunder or under any other Loan Document"; part (f), "other than as permitted by Section 15.12, release Agent's Lien in and to any of the Collateral"; part (i), "release any

Borrower or any guarantor of all or any part of the Obligations from any obligation for the payment of money”; and part (k), “amend any of the provisions of Section 15”(id.).

The Fourth Amendment provides that its section 4 (o) is added to the end of section 14.1 of the Credit Agreement. The amendment names Edgewater alone of the junior lenders. It provides that Edgewater shall not have “voting or consent rights ... except for such voting and consent rights inuring to all the Lenders directly affected thereby relating to the matters described in clauses (a), (b), (c), (e) (as it relates to the amendment of this Section 14.1 only), (g) and (i) of this Section 14.1” (Fourth Amendment, 4 [o]). This means that Edgewater loses its consent rights to the activities in sections (f), and (k) of section 14.1 of the Credit Agreement.

Count one of the complaint implicates section (f), which provides that the agent may not release a lien without Edgewater’s consent, other than as permitted in section 15.12. Section 15.12 says that all the lenders must consent to the agent’s release of a lien. The Fourth Amendment changes that and provides that Edgewater’s consent is not required for such release. Also modified is section 14.1 (k) of the Credit Agreement, which prohibits the amendment of section 15.12 without Edgewater’s consent. The Fourth Amendment allows section 15.12 of the Credit Agreement to be amended without Edgewater’s consent.

Section 3 of the Settlement Agreement recites that Allied shall release its agent’s lien on the collateral under certain conditions, such as the foreclosure sale being conducted in accordance with the Settlement Agreement. Therefore, assuming that Allied released its lien on collateral, such an action did not violate section 15.12 of the Credit Agreement. Count one of the complaint must be dismissed.

Count two of the complaint alleges breaches of sections (c) and (i) of section 14.1 of the

Credit Agreement. As stated already, section (c) provides that the junior lenders' consent is required for any reduction of the amounts due on the junior loans. Section (i) provides that the junior lenders' consent is required for any release of the Borrower from any part of its obligation to pay back the loans.

Defendants claim that they did not release any of the junior loans. Section 4 of the Settlement Agreement is entitled "Releases." It states that the parties to the Settlement Agreement release and discharge the Borrower from claims related to any breach of the Credit Agreement and the Foreclosure Agreement, so long as the foreclosure sale is conducted in accordance with the terms of the Settlement Agreement (Settlement Agreement, ¶ 4 [a]). Section 4 further states that the Borrower is not released from any breach of the Settlement Agreement or from any claim held by any junior lender not party to said agreement (*id.*). Nothing in the Settlement Agreement "shall be construed as releasing, discharging or satisfying, in whole or part, the indebtedness of any Loan Party respecting any Senior Loan or Junior Loan" (*id.*).

Thus, the Settlement Agreement recites that it does not release the Borrower from the junior loans held by Edgewater or discharge the loans. But it also recites that defendants release the Borrower from the Credit Agreement. Section 14.1 (i) of the Credit Agreement, which provides that the Borrower may not be released from any obligations without the consent of all the junior lenders, was not amended. To the extent that the Settlement Agreement accomplishes the release of the Borrower, it violates section 14.1 (i) of the Credit Agreement. The Settlement Agreement also violates the part of the Credit Agreement at section 14.1 that precedes the alphabetical list of prohibited actions and that is a general ban on amending any part of the junior loans. The Settlement Agreement constitutes an amendment of the Credit Agreement.

Defendants contend that the Credit Agreement does not bar them from consenting to a release or reduction. It merely provides that any such consents are not effective until Edgewater consents. Therefore, defendants argue, any release in the Settlement Agreement does not violate the Credit Agreement. This argument implies that the Settlement Agreement is not binding on defendants until Edgewater consents, which does not appear to be the parties' intent. The Settlement Agreement does not state that it is subject to Edgewater's consent. It says that it is valid and binding on defendants (Settlement Agreement, ¶ 9 [b]). Although, as defendants contend, they may be able to show that their release of the Borrower did not injure Edgewater, at this stage of the litigation Edgewater has a cause of action for breach of contract.

Defendants also claim that the Settlement Agreement does not affect Edgewater's right to payment of its loans. But Edgewater claims that the post-foreclosure exchange of junior loans will strip the Borrower of all assets, rendering any remaining obligations of the Borrower unenforceable. Thus, according to Edgewater, the Settlement Agreement reduces the Borrower's obligations.

The Settlement Agreement identifies defendants as the Releasing Second Lien Lenders. If Edgewater became a party to the Settlement Agreement, it would be considered a Releasing Second Lien Lender, as well (Settlement Agreement, ¶ 4 [b]). The Settlement Agreement gives each Releasing Second Lien Lender two choices for disposing of their junior loans after the foreclosure sale. One option entitles each Releasing Second Lien Lender to exchange its junior loans for a pro rata share of 10% of the equity (10,000 shares of common stock) of the Proposed Buyer (*id.*, ¶ 5 [a]). This option would be available if the Proposed Buyer purchased the Borrower's assets at the foreclosure sale (*id.*). In the case of a Releasing Second Lien Lender

who decided to exchange for equity, the exchange would occur after said releasing lender applied the proceeds of the foreclosure sale, if any, to the junior loans (seeming to mean all the junior loans, not only those by Allied and Maps) (*id.*, ¶ 5 [d]). The second option would become available if another party purchased the assets, and the sale proceeds at the foreclosure sale did not exceed the aggregate amount of the senior loans (*id.*, ¶ 5 [b]). In that case, each Releasing Second Lien Lender could exchange its junior loans for a pro rata share of \$1.5 million, referred to as the Cash Payment (*id.*). The senior lenders would buy the junior loans from such junior lender for such Cash Payment. (*id.*).

Edgewater sufficiently alleges that the proposed exchanges reduce the Borrower's ability to pay its debt to Edgewater. It may be, as Edgewater claims, that the Settlement Agreement renders repayment impossible. To show that Edgewater's claims are not valid, defendants submit a transcript of a proceeding in the Chancery Court in Delaware where Edgewater attempted to obtain a temporary restraining order enjoining the senior lenders from conducting the foreclosure sale. Edgewater alleged that the sale was not commercially reasonable in that another buyer who was willing to pay more for the Company assets than the Proposed Buyer was shut out from the sale. The Delaware Court denied Edgewater's motion.

That Edgewater's request was denied does not, by itself, prove that Edgewater's complaint lacks merit. "Whether a plaintiff can ultimately establish its allegations is not part of the calculus in determining a motion to dismiss" (*EBC I, Inc. v Goldman, Sachs & Co.*, 5 NY3d 11, 19 [2005]). Therefore, applying this standard, the allegations of breach of contract in the second cause of action survive defendants' motion to dismiss.

Conclusion

In conclusion, it is

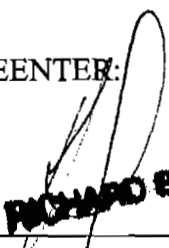
ORDERED that defendants' motion to dismiss the complaint is granted as to the first cause of action, which is hereby severed and dismissed, and is otherwise denied; and it is further

ORDERED that remainder of the complaint shall continue; and it is further

ORDERED that defendants are directed to serve an answer to the complaint within 10 days after service of a copy of this order with notice of entry.

Dated: November 3, 2008

EENTER:


~~HON. RICHARD B. LOWE, JR.~~
J.S.C.

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