15-1771

In the United States Court of Appeals for the Second Circuit

In the Matter of: MPM Silicones, L.L.C.,
Debtor.

U.S. Bank National Association, as indenture trustee,
Plaintiff-Appellant,

v.

Wilmington Savings Fund Society, FSB, as successor indenture trustee,
Momentive Performance Materials Incorporated,
Ad Hoc Committee of Second Lien Noteholders,
Apollo Management, LLC, and certain of its affiliated funds,
Defendants-Appellees.

On Appeal from the United States District Court
for the Southern District of New York

REPLY BRIEF OF PLAINTIFF-APPELLANT
U.S. BANK NATIONAL ASSOCIATION

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The basic textual question in this case is simple: Does "in any respect" actually mean "in *one particular* respect?" Not to most English speakers. So Appellees labor to change the plain meaning by constructing a "context" in which a supposedly key distinction between "lien subordination" and "payment subordination" of indebtedness is all that matters. Br. 24, 30, 32. That effort ignores the law and blinks reality. Liens have *everything* to do with the nature of the indebtedness they secure; and, if there were any doubt, the Indenture and Intercreditor Agreement cement that bond repeatedly.

Appellees give little heed to governing canons of contract interpretation. Drafters mean different things when they use different terms—as they did here when distinguishing subordination "in right of payment" from subordination "in any respect." Drafters are assumed to follow industry usage—like the Fitch report that proposed using "in any respect" precisely to avoid what Appellees claim the Indenture allows, and the ABA model indenture provision that would have achieved Appellees' result but is glaringly absent here. And Appellees' resort to extrinsic evidence (which, tellingly, Appellees do not claim is legally relevant) is a mere distraction. The words mean what they say.

Appellees' brief is a master class in how *not* to interpret a contract. Endorsing their view would destabilize the ability of bond investors—and parties to contracts generally—to rely on the written word.

Equally unavailing is Appellees' effort to dodge this appeal on grounds of equitable mootness. All of the so-called *Chateaugay* factors point decisively against equitable mootness here. Indeed, Appellees do not even address the factor—diligence in seeking a stay—that this Court has described as the "chief" consideration. And they no longer even argue that reversal on appeal could harm third parties. Their argument reduces to the proposition that, notwithstanding U.S. Bank's express statutory right to appeal, plan proponents are entitled to keep the spoils of an unlawful plan lest an illegal bargain be upset. To state that proposition is to refute it.

ARGUMENT

I. The Second-Lien Notes Are Not "Senior Indebtedness"

A. The Indenture Unambiguously Excludes The Second-Lien Notes From Senior Indebtedness

It is undisputed that the Second-Lien Noteholders cannot receive a penny from the bulk of Debtors' assets until the Senior-Lien Note-holders are paid in full. JA-693. This junior status, imposed by the

Intercreditor Agreement, exists even if the Senior-Lien Noteholders' liens on the Common Collateral are *invalidated* or their claims are *rejected*. JA-709. And it even requires the Second-Lien Noteholders to give the Senior-Lien Noteholders recoveries the former may acquire from liens on *any* of Debtors' property (not only the Common Collateral) and imposes duties on the Second-Lien Noteholders in their capacity as unsecured creditors. JA-698 & JA-703. The Second-Lien Noteholders are thus junior to the Senior-Lien Noteholders in every meaningful sense.

The central dispute is whether all of that renders the Second-Lien Debt "by its terms . . . subordinate or junior *in any respect* to any other Indebtedness or obligation" (emphasis added). That should be an easy question. The Second-Lien Debt is "Indebtedness"; the "terms" of that "Indebtedness" include the Intercreditor Agreement provisions cited above; and those terms make the Second-Lien Debt "subordinate or junior" to the Senior-Lien Noteholders in *multiple* respects. It is that simple.

Faced with this unambiguous contractual language, Appellees conjure up a supposedly strict and crucial distinction (unstated in the contract) between lien and payment subordination of indebtedness, which (Appellees claim) somehow renders the Second-Lien Notes not subordinate "in *any* respect." Appellees' reliance on that distinction, however, is misplaced as a matter of theory and precedent. It is also incompatible with the Indenture, which explicitly rejects this distinction. Committed to their flawed premise, Appellees have no choice but to rewrite critical terms of the Indenture, blowing past settled rules of contract interpretation and inventing new ones.

1. Appellees' Argument Rests On An Incorrect And Irrelevant Premise About Subordination Of Indebtedness

Appellees' argument depends on a crucial premise: that, "when the Indenture refers to the subordination of Indebtedness, it must be read as subordination in right of payment, not subordination with respect to liens." Br. 26. This rigid distinction is the entire basis for Appellees' insistence that subordination of the Second-Lien Notes to the Senior-Lien Notes under the Intercreditor Agreement does not constitute subordination "in any respect." But there is no basis for such a crabbed definition of how indebtedness can be subordinated.

For starters, it is simply untrue that debt is unaffected by liens securing it. "[L]ien status is as integral to the character and quality of the loan as the rate of interest and duration of the loan." *Lawyers Title Ins. Corp. v. Norwest Corp.*, 493 S.E.2d 114, 117 (Va. 1997). Accordingly, it is black-letter law that debt secured by a junior lien is subordinate or junior in a material respect. *See Black's Law Dictionary* 489 (10th ed. 2014) (defining "subordinate debt" as debt that "may be unsecured *or have a low-priority claim against property secured by other debt instruments*" (emphasis added)); *Roswell Capital Partners LLC v. Beshara*, 436 F. App'x 34, 35 (2d Cir. 2011); *Good Hill Partners L.P. ex rel. Good Hill Master Fund, L.P. v. WM Asset Holdings Corp. CI 2007-WM2*, 583 F. Supp. 2d 517, 518 (S.D.N.Y. 2008).

This principle accords with common sense. Nothing is more important to indebtedness than its satisfaction, and junior liens go to the heart of how debt is satisfied. There is no sound basis for the view that subordination of indebtedness must—due to some theoretical conception about the ineffable nature of debt—refer solely to subordination in right of payment. Subordination of a lien is, in a very real sense, subordination of the debt it secures—not least in the eyes of any party holding a junior lien. Thus, lien and payment subordination are often recognized as distinct *forms* of subordination, but both necessarily result—through different mechanisms—in subordination of the associated indebtedness in certain respects.

Indeed, the Indenture itself rejects Appellees' premise in favor of a pragmatic approach: Its definition of "Indebtedness" includes "Indebtedness of another Person *secured by a Lien* on any asset owned by such Person." JA-328 (emphasis added). The amount of any such indebtedness, moreover, is effectively defined by reference to the lien. *See ibid.* Of course, a "lien" is not the *same* as "Indebtedness," and the Indenture defines each term separately, often referring to liens as securing indebtedness. *E.g.*, JA-335 to JA-337. But it does not follow, as Appellees suggest (at 25-26), that the Indenture treats liens as *irrelevant* to the nature of indebtedness. To the contrary, these terms affirmatively recognize the inextricable link between liens and debt—consistent with commercial reality. To subordinate a lien is to subordinate the debt it secures in that respect.

In arguing that the Indenture enshrines a rigid distinction between liens and debt, Appellees fundamentally misread it. On their view, because the Base Definition of Senior Indebtedness and several other terms refer to the subordination of Indebtedness in conjunction with "in right of payment," subordination of Indebtedness can refer *only* to payment subordination. Indeed, Appellees argue (at 24) that this conclusion is so obvious that it shifts the "onus" to U.S. Bank to explain why the Indenture encompasses any other kind of subordination.[1]

Not so. The Indenture uses the term "in right of payment" twenty times, ten of which include the full phrase "subordinated in right of payment." The Fourth Proviso, however, instead refers to indebtedness that is "subordinate or junior *in any respect*." Appellees would erase that glaring textual difference. But the rule is the opposite: Differences in language are presumed to mean something, especially when a specific point has been expressed with very different language elsewhere in a contract. *See Chesapeake Energy Corp. v. Bank of N.Y. Mellon Trust Co.*, 773 F.3d 110, 116 (2d Cir. 2014); *Novella v. Westchester Cty.*, 661 F.3d 128, 142 (2d Cir. 2011).

[1] If Appellees mean to suggest that U.S. Bank bears a burden of proof, they are clearly mistaken. *See, e.g.*, *In re Genco Shipping & Trading Ltd.*, 513 B.R. 233, 240 (S.D.N.Y. 2014) (plan proponents "bear the burden of establishing . . . that the Plan meets the requirements of Section 1129").

What is more, the Fourth Proviso is the *only* place the Indenture uses the broad phrase "in any respect." Instead of referring to subordination "in right of payment," or "in any material respect" (as other terms do), the drafters chose a different, unqualified phrase to capture *every* kind of subordination. Although "none of the Indenture's references to subordination mentions Liens" by name, Momentive Br. 32, "any" means "any," especially when used instead of narrower terms appearing elsewhere.

The Indenture thus eschews the distinction on which Appellees have built their interpretation. Avoiding specific reference to either lien or payment subordination, the "in any respect" provision—cast in the broadest possible terms—aims to capture *all* indebtedness subordinate *in any way* within the creditor hierarchy.

In this regard, the Indenture mirrors the Intercreditor Agreement. Appellees' characterization of the latter as producing mere "lien subordination" ignores the document's text. The Intercreditor Agreement enforces subordination with respect to the Common Collateral even if the Senior-Lien Noteholders' liens are invalidated, or if prior payment on the Senior-Lien Notes is set aside as fraudulent, and in certain circumstances it extends to liens on any Debtors' property or to the Second-Lien Noteholders' rights as unsecured creditors. This is truly a subordination of *indebtedness*.

The Indenture's rejection of Appellees' premise is further shown by its use of the very phrase—"subordinate in any respect"—developed in the bond industry to prevent issuers from demoting existing creditors by issuing second-lien debt. *See Chesapeake Energy*, 773 F.3d at 114. Before the Indenture was written, the Fitch Ratings Agency recommended that creditors replace "subordinated in right of payment" with "subordinated in any respect" specifically to "capture any new debt . . . structured with [] lien subordination." JA-769. Latham & Watkins made similar recommendations. *See* JA-857. The obvious reason to include the "in any respect" provision in the Indenture was to achieve the purpose publicly identified by its creators: excluding from the definition of Senior Indebtedness any obligation subject to either payment *or* lien subordination. *See Law Debenture Trust Co. of N.Y. v. Maverick Tube Corp.*, 595 F.3d 458, 466 (2d Cir. 2010).

The fact that Fitch and Latham & Watkins used "forward-looking" language (Br. 43) is no answer; this was specific terminology identified by key market actors to deal with a prominent issue. That suffices to "to raise a fair presumption that [this meaning] was known to both contracting parties and that they contracted in reference thereto." *Law Debenture Trust*, 595 F.3d at 466; *see also* Restatement (Second) of Contracts § 219 (1981). Further, placement of this phrase in the definition of Senior Indebtedness rather than in the anti-layering covenant is of no moment: It was hardly hidden, and in the context of this definitional provision it means the same thing it would anywhere else.

There is an irony to Appellees' position. As industry experts who sought to take advantage of the very debt-layering subterfuge that Fitch and Latham & Watkins warned against, Appellees now insist that they could not have foreseen what the "in any respect" provision meant. Yet the issue was well known and hotly debated in the industry; influential market advisers in that industry coined this exact phrase for a single purpose that struck at the heart of Appellees' chosen debt-layering technique; the "in any respect" provision appears in one of the most heavily scrutinized sections of the Indenture; Appellees do not point to any contract that uses "in any respect" to mean what they say it means; and Appellees declined to identify any custom that would explain why this term would be used for the textually improbable goals they ascribe to it.

The 2006 American Bar Association model indenture further demonstrates that the Indenture rejects Appellees' false premise about debt and liens. The ABA model provided a rule of construction declaring that "secured Indebtedness shall not be deemed to be subordinate or junior to any other secured Indebtedness merely because it has a junior priority with respect to the same collateral." JA-964. But the parties *omitted* that rule. With language tailor-made for Appellees' position right in front of the drafters, they did not use it.

Appellees note (at 46) that the ABA model itself does not claim to reflect market usage. Fair enough. But the parties to the Indenture incorporated seven other ABA model rules *verbatim*—including a rule governing the subordination of unsecured indebtedness. *This* contract therefore unmistakably evinces deliberate choices among the ABA model rules. Moreover, four other indentures in the 2006-2007 timeframe defined Senior Indebtedness to exclude debt that that was "subordinate or junior in any respect" but then *included* the ABA model provision omitted here—demonstrating a consensus about the significance of decisions whether to include that provision. *See Quadrant Structured Prods. Co. v. Vertin*, 16 N.E.3d 1165, 1172 (N.Y. 2014). Appellee Apollo was involved as a controlling party in two of those indentures. Appellees deny none of this.

Appellees suggest that there was no need to include this model rule because, as they read it, the Fourth Proviso already excludes senior debt secured by a junior lien. *See* Br. 47. Apparently this (overly) subtle logic eluded all parties to the other four indentures referenced above, twice including Appellee Apollo. And, given the raw breadth of its language, it is difficult to see how the Fourth Proviso erases the significance of the drafters' decision to exclude a term stating the central premise of Appellees' position.

Appellees briefly sketch one last argument: The Indenture permits the creation of liens; the anti-layering covenant restricts only the incurrence of debt subordinate in right of payment; and therefore the Indenture *must* allow the *unlimited* addition of senior debt secured by junior liens. Br. 26. The conclusion, however, is a *non sequitur*. U.S. Bank's interpretation has no effect on the creation of liens. Nor does it disrupt the anti-layering covenant's restrictions on incurring debt subordinate in right of payment. And there is no rule—either in general or in the Indenture—providing that *only* the anti-layering covenant can protect creditors, or that a term allowing the creation of junior liens prohibits *any* limits on the effects of those liens. Thus, the terms noted by Appellees can be read harmoniously—the Fourth Proviso means just what it says.[2]

2. Appellees Re-Write The Text, Rather Than Interpret It

Committed to a false premise about the nature of indebtedness, Appellees have no choice but to rewrite the Fourth Proviso. As discussed above, Appellees interpret "in any respect" to mean "in right of payment." Likewise, in an effort to avoid redundancy with the Base Definition of Senior Indebtedness (which already excludes any indebtedness "expressly . . . subordinated in right of payment"), Appellees swap "by its terms" for "implicitly" (or "not expressly").

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[2] Appellees err in suggesting (at 26) that U.S. Bank's interpretation would "convert[] permissibly issued senior debt into junior debt." The Second-Lien debt is still senior to the extent of its lien. It retains priority access (behind Senior-Lien Noteholders) to the Common Collateral, and is placed on *pari passu* status with respect to all remaining assets.

Specifically, Appellees rewrite the Fourth Proviso (JA-342) as follows:

> any Indebtedness . . . that ~~by its terms~~ implicitly is subordinate or junior ~~in any respect~~ in right of payment to any other Indebtedness or obligation.

In the most literal sense, this is a rewriting of the contract, not an interpretation of it. As we explain in further detail below, Appellees' efforts to jam a square peg into a round hole do violence to the text.

Appellees begin by quietly stepping away from the lower courts' view (SPA-234) that the provisos—which are introduced with the phrase "*provided, however,*"—can only "clarify or augment" the Base Definition. As Appellees acknowledge, "the Fourth Proviso must add a *limitation* on 'all Indebtedness' *separate and apart* from Indebtedness that is 'expressly . . . subordinated in right of payment.'" Br. 30 (emphasis added). That much is correct: a long line of precedent holds that language following "provided, however," overrides whatever precedes it. *E.g., Bank of N.Y. v. First Millennium, Inc.*, 607 F.3d 905, 917-918 (2d Cir. 2010). Therefore, the natural meaning of the Fourth Proviso—including its reference to subordination "in any respect"—must be respected even though it may deviate from the Base Definition.

But soon after acknowledging the effect of "provided, however," Appellees lapse back into the lower courts' error. They reason that the Base Definition refers to payment subordination, so this must also be true of the Fourth Proviso. Br. 32. That is wrong. It ignores a major and deliberate difference in language between the Base Definition and the Fourth Proviso, *see supra* at 7-8, and also inverts the settled purpose of a "provided, however," clause. *See* U.S. Bank Br. 35-37 (collecting cases). Relying on the Base Definition to impose a cramped reading on the Fourth Proviso is backward; the whole point of the provisos following the Base Definition is to impose additional, categorical limitations on the definition of Senior Indebtedness, *without regard* to what the Base Definition encompasses.

The other provisos support this conclusion. Despite its extremely broad language, Appellees read the Fourth Proviso as startlingly narrow, speculating that it may cover just two kinds of "implicit" (or "not express") payment subordination. This kind of hyper-technical narrowness is not otherwise characteristic of the provisos, which sweep across major categories of obligations: *any* intercompany obligations; *any* liability for taxes; *any* accounts payable or other liability to trade creditors; and *any* obligations with respect to any Capital Stock. JA-341 & JA-342. Indeed, the provisos make generous use of the broad word "any." If Appellees are correct, only in the Fourth Proviso would such expansive language—"any Indebtedness . . . subordinate or junior in any respect"—mean so little. And to the extent Appellees suggest that payment subordination sweeps across the provisos generally, no obligation covered in any other proviso makes sense on that view.

Lacking a workable theory of the interaction between provisos and base definitions, Appellees quickly retreat to the presumption against superfluity. Ultimately, this is the cornerstone of their textual analysis. If it crumbles, so falls the rest of their argument.

First, Appellees maintain that U.S. Bank's reading creates superfluity while their reading does not. Second, they assert that, even if their analysis does create surplusage, they should still prevail because they "minimize" it. Br. 37. For several *independently sufficient* reasons, every premise and every conclusion of this argument is mistaken.

To begin, the presumption against superfluity is not properly applied to cabin any redundancy resulting from a proviso's trumping language. *See Morse/Diesel, Inc. v. Trinity Indus., Inc.*, 67 F.3d 435, 439 (2d Cir. 1995); *Warberg Opportunistic Trading Fund, L.P., v. GeoResources, Inc.*, 973 N.Y.S.2d 187, 192 (1st Dep't 2013). To the extent a proviso creates an exception that overlaps with an exception built into the Base Definition, that reflects mere belt-and-suspenders drafting, and is permissible due to the "provided, however," clause.

Even if this canon applies here, it cuts both ways, *since no one's* reading avoids superfluity: Both proffered readings of the "in any respect" provision would wholly subsume the Base Definition's "in right of payment" provision. Appellees are mistaken that their reading of the Fourth Proviso avoids such surplusage. As they would have it, the Base Definition excludes any indebtedness "expressly" subordinate in right of payment, whereas the Fourth Proviso excludes indebtedness "by its terms" subordinate in right of payment. Br. 35-36. On inspection, this awfully fine distinction vanishes.

Starting with the text, "by its terms" naturally means "expressly," not "expressly or implicitly." *Cf. Jennings v. Univ. of N. Carolina*, 482 F.3d 686, 716 (4th Cir. 2007) ("While Title IX does not, *by its terms*, create a private cause of action against the funding recipient, the

Supreme Court has *implied* one." (emphasis added)). Moreover, as U.S. Bank observed in its opening brief (at 40-41)—*without response from Appellees*—defining "by its terms" to mean "not expressly" would give that term a very different meaning here than it carries throughout the rest of the Indenture. The Indenture and its attachments elsewhere use "by its terms" four times and "by the terms" eight times, but in none of those instances would it make sense to read the phrase to mean "not expressly." "By its terms" cannot have one meaning in the Fourth Proviso and another throughout the rest of the indenture. *See Chesapeake Energy*, 773 F.3d at 116.

Further, the examples offered by Appellees of this new genus—"by-its-terms-but-not-express subordination"—reflect nothing but speculation provoked by the crucible of appellate briefing. Nowhere in their district court or bankruptcy court briefing did Appellees mention "last-out facilities" or "Pari Passu Indebtedness," which they now brandish as self-evident "example[s]" of what the parties to the Indenture *must* have meant. Br. 31-32, 36. There is zero evidence—and no indication in the text—that any party to the Indenture intended the Fourth Proviso to encompass those arrangements under the guise of subordination "by its terms." And even if one could replace "by its terms" with "implicitly" in the first half of the Fourth Proviso, that does not explain how "in any respect" can mean "in right of payment" in the second half. Thus, all Appellees' reading does is suggest that Senior Indebtedness does not include debt that is "'implicitly' subordinate or junior in any respect."[3]

Accordingly, as a matter of text and context, both parties' interpretations of the Fourth Proviso render superfluous the Base Definition's exclusion of indebtedness expressly subordinate in right of payment. The Supreme Court has repeatedly held that the presumption against superfluity falls away when competing interpretations of a text *both* create surplusage. *See Marx v. Gen. Revenue Corp.*, 133 S. Ct. 1166, 1177 (2013) ("[T]he canon against surplusage 'assists *only* where

[3] Appellees observe that a last-out facility and *pari passu* indebtedness "would not contain a subordination provision as such." Br. 31. It does not follow that these instruments would be characterized as subordinate "in right of payment"; rather, they just contain another *form* of subordination. And the fact that subordination can be accomplished without a payment-subordination provision, and in ways *other* than textbook lien or payment subordination, is exactly *our* point. In attempting to give the phrase "by its terms" the unnatural meaning "not expressly," Appellees' thus adopt the very same practical approach that they eschew when asserting that liens do not affect the subordination of indebtedness.

a competing interpretation gives effect to *every* clause and word of a statute.'" (emphasis added) (quoting *Microsoft Corp. v. i4i Ltd. P'ship*, 564 U.S. 91, 106 (2011))).

Ignoring this precedent—but without citing any other authority—Appellees advance the novel proposition that their interpretation should still prevail because it seeks to "minimize any surplusage." Br. 37. Here, Appellees embrace the district court's suggestion that Appellee's reading should be preferred—even though it creates superfluity—because it is "easier to swallow." SPA-236.

Aside from being foreclosed by the Supreme Court precedent just cited, Appellees' argument rests on a mistaken assumption. By definition, *any* superfluous provision is replaceable with a broader provision—but it does not follow that the more "minimal" of two possible broader provisions is preferable. Rather, the proper inquiry is to consider the Indenture as a whole and to select an interpretation consistent with the rest of the document. *See Galli v. Metz*, 973 F.2d 145, 149 (2d Cir. 1992). But even applying Appellees' incorrect principle, their reading is not "easier to swallow." As explained above, it contravenes a battery of interpretive principles and gives the Fourth

Proviso a highly unnatural meaning. And the effect of Appellees' reading is hardly minimal; it resulted in the *total* exclusion of Senior Subordinated Noteholders from any recovery.

B. Appellees' Argument Based On Extrinsic Evidence Is Irrelevant, Incorrect, And Improper

Appellees devote an entire subsection of their brief to describing "surrounding circumstances." Br. 27. To Appellees, these circumstances include a series of statements in SEC filings and other financial documents in which Debtors articulated their current interpretation of the Indenture. Even as they pretend to disclaim reliance on this extrinsic evidence—which, tellingly, they do not argue is proper or relevant—Appellees wink and nod at the Court: *Apart from all these word games and troublesome interpretive canons, here's what really happened*.

Of course, when "a contract is unambiguous, courts are required to give effect to the contract as written and may not consider extrinsic evidence to alter or interpret its meaning." *U.S. Trust Co. of N.Y. v. Jenner*, 168 F.3d 630, 632 (2d Cir. 1999). Here, Appellees do not advance any contentions based on a theory of textual ambiguity. For that reason alone, this evidence is irrelevant.

Moreover, this extrinsic evidence consists principally of post hoc, self-serving statements by one party, and thus offers no reliable indication of the parties' *mutual* intent when the Indenture was signed. *See LaSalle Bank Nat'l Ass'n v. Nomura Asset Capital Corp.*, 424 F.3d 195, 208 n.10 (2d Cir. 2005). Indeed, there is no evidence that the Senior Subordinated Noteholders knew about or agreed with the Debtors' statements. *See SR Int'l Bus. Ins. Co. v. World Trade Ctr. Props., LLC*, 467 F.3d 107, 125 (2d Cir. 2006) (even with an ambiguous contract, one "party's uncommunicated subjective intent cannot supply the ultimate meaning"). The fact that Debtors arrived at their mistaken interpretation in 2009 does not make it correct; it is merely evidence that they have persisted in that convenient error.

It would be improper—and deeply destabilizing to bond markets—for the Court even to consider Appellees' "extrinsic evidence." There is *no* legal basis for requiring a creditor to engage in ongoing monitoring of its counterparty's post-contracting mischaracterizations of their bargain. Such a rule would allow bond issuers unilaterally to modify their contracts, and would force creditors to review not only their own indentures, but also SEC filings and any other document in which a counterparty might mischaracterize their bargain. And presumably courts would be littered with preemptive challenges to such mischaracterizations—even if a financial injury had yet to materialize—for fear that years later an issuer's statements would be deemed meaningful.

Equally irrelevant is the fact that some Senior Subordinated Noteholders exchanged their notes at a discount for the Debtors' 2009 second-lien notes. There is no record evidence about the relative size of the Common Collateral and Debtors' remaining assets; that inquiry was pretermitted by the bankruptcy court after it held that Appellees qualify as Senior Indebtedness. It is thus impossible to gauge the rationality of the Senior Subordinated Noteholders' discount rate, notwithstanding Appellees' conclusory assertions.

For example, suppose Debtors possessed $500 million in assets, of which $480 million was Common Collateral. A junior lien on the Common Collateral—plus *pari passu* status with the Senior Subordinated Noteholders for the $20 million remainder—might well have been worth substantially more than remaining as Senior Indebtedness. If it was expected that there would be sufficient Common Collateral remaining after Senior-Lien Noteholders were paid, a junior lien would prevent other creditors from claiming priority over those assets with its own lien. As Appellees acknowledge (at 26), the Indenture permitted such additional liens. Indeed, that is exactly what happened to the Senior Subordinated Noteholders here—any surplus Common Collateral is off-limits. The junior lien is thus a valuable bird-in-the-hand to Second-Lien Noteholders. Depending on how much surplus Common Collateral there is, they may wind up far better off for having taken a discounted claim in exchange for the lien. The commercial reasonableness of that decision simply cannot be judged without knowing these essential facts. It is pure conjecture for Appellees to claim that no rational bondholder would have done such a deal without being promised *both* a junior lien *and* retaining status as Senior Indebtedness.

C. The Senior Subordinated Noteholders' Interpretation Does Not Produce Illogical Consequences

Appellees lace their brief with arguments about the supposedly absurd results of U.S. Bank's interpretation. None holds water.

Appellees first argue that it makes no sense for the springing of a lien to terminate the Second-Lien Notes' status as Senior Indebtedness. Br. 40. But, as Appellees almost immediately concede, "'in the right circumstances, it *would* be perfectly rational to give up senior unsecured status for a junior secured status.'" *Ibid.* (quoting U.S. Bank Br. 60) (emphasis added). The relevant question, if any, is whether those circumstances were present here. As explained above, it is easy to imagine circumstances in which a junior lien on the bulk of a debtors' assets (plus *pari passu* status vis-à-vis all other assets) is more valuable than a senior claim to that debtors' other assets.

Appellees point out, correctly, that there is no record evidence proving that the circumstances in 2006 supported U.S. Bank's position. Br. 40. But there is also no record evidence support for their own position. *There is no record at all* on this issue; the bankruptcy court's error was one of law in interpreting the text. Appellees' unsupported assertions about the under-securitization of the Second-Lien Noteholders on the petition date are mere *ipse dixit*. Moreover, circumstances on the petition date are irrelevant; what matters are the circumstances when the Indenture was signed.

Appellees also argue that U.S. Bank's interpretation is "absurd" because it would mean that "*every* tranche of outstanding secured Indebtedness as of the filing of the bankruptcy petition would be excluded from the definition of Senior Indebtedness." Br. 41. Again, the relevance of the petition date is a mystery: This agreement was signed years earlier, *before* the layering of liens and springing liens that resulted in the current impasse. When the Indenture was signed, Senior Indebtedness was not a null set.

In any event, the fact that the Indenture describes a category of debt called Senior Indebtedness does not make it "absurd" for changed circumstances, years later, to have emptied that category. That is especially true here, where, due to intervening developments, lien seniority has largely replaced payment seniority in structuring the creditor hierarchy, and where the Common Collateral was large enough to cover the Senior-Lien Noteholders and leave assets remaining. Under U.S. Bank's interpretation, the Senior-Lien Noteholders get paid in full from the Common Collateral; Second-Lien Noteholders enjoy top-priority rights to all remaining Common Collateral assets; and all non-Common Collateral assets are divided on a *pari passu* basis between Second-Lien Noteholders and U.S. Bank (since neither qualifies as Senior Indebtedness). This is hardly an absurd or commercially irrational result; rather, it reflects the combined effect of the

Indenture's clear provisions excluding *any* subordinated indebtedness from Senior Indebtedness and also allowing *unrestricted* lien creation.

If anything, Appellees' interpretation is commercially irrational. When the Indenture was created in 2006, the use of junior liens to layer debt—to the profound economic detriment of existing creditors—had become common enough that Fitch had issued warnings. The parties to the Indenture knew about this trend: They included, *verbatim*, language proposed by Fitch to address it. Given all that, it would have made no sense for the Senior Subordinated Noteholders to sign an Indenture that foreseeably allowed exactly the outcome Appellees seek here: *All* surplus Common Collateral goes to Second-Lien Noteholders, and then *any* remaining assets go to Second-Lien Noteholders as Senior Indebtedness, leaving Senior Subordinated Noteholders out in the cold. The more natural conclusion—confirmed by text, context, and commercial reason—is that the Indenture meant what it said when it excluded from Senior Indebtedness all indebtedness subordinate "*in any respect*."

II. The Appeal Is Not Equitably Moot

U.S. Bank has amply demonstrated that this appeal is not equitably moot. Senior Subordinated Noteholders received nothing, and Second-Lien Noteholders got 100% of Momentive's common equity, because legal error afforded the Second-Lien Notes "Senior Indebtedness" status. This appeal will correct that error—and recalibrate the resulting misappropriation of recoveries—without upending Momentive's reorganization.

Appellees contend, however, that Second-Lien Noteholders' sponsorship of a Plan awarding themselves *other creditors' money* entitles them to keep that "benefit" of their illegal "bargain" or else "reopen[]" the bankruptcy from scratch. Br. 54. The lower courts have rejected this self-serving argument. The bankruptcy court concluded that "the risk of equitable mootness is not strong here" because relief "would come largely from a recalibration of the consideration provided to the second lien noteholders." JA-2095. That recalibration, the court observed, would *not* cause "the plan itself [to] fail." *Ibid.* The district court agreed that "the risk of equitable mootness here is not very great" because the bankruptcy court could "recalibrate the consideration provided to the second lien noteholders" and "restructure the plan on remand." JA-2192.

Those courts were right. The Second-Lien Noteholders can be ordered to turn over what they improperly received under the plan (or the proceeds thereof). Or the reorganized debtor could be ordered to provide equivalent remedies via cash payments or the issuance of new stock or debt. If necessary, some combination of the two can be crafted. Those remedies easily satisfy the relevant *Chateaugay* factors. These remedies are available and effective (factor one).[4] Likewise, these remedies would not adversely affect third parties (factor four); Appellees have stopped arguing otherwise.

The only seriously disputed factors point decisively in U.S. Bank's favor. These remedies would not entitle Second-Lien Noteholders to a do-over (factor two), or threaten Momentive's post-bankruptcy success (factor three). And the "chief consideration" militating against equitable mootness, *see In re Metromedia Fiber Network, Inc.*, 416 F.3d

[4] Contrary to Appellees' cursory contention (at 58 n.7), this factor requires only that a remedy is not impossible "in the sense that the [appeal is] constitutionally moot." *In re Charter Commc'ns, Inc.*, 691 F.3d 476, 484 (2d Cir. 2012). There is no plausible dispute that "effective" relief is possible.

136, 144 (2d Cir. 2005), is U.S. Bank's undisputedly diligent pursuit of a stay pending appeal (factor five). Tellingly, Appellees fail to address this factor *at all*.

A. U.S. Bank's Remedies Will Not Unravel The Plan

Appellees claim that granting U.S. Bank the recalibration remedy identified by the bankruptcy and district courts would unravel the entire Plan. It would not.

For starters, Appellees ignore numerous cases establishing that appeals seeking disgorgement (or its equivalent) from parties to the proceedings are not equitably moot. This Circuit's seminal equitable-mootness decision, *In re Chateaugay Corp.*, 10 F.3d 944, 953 (2d Cir. 1993) ("*Chateaugay II*"), held that appeals challenging recoveries "wrongfully distributed" to "one or more entities that are now before this Court" are not equitably moot because bankruptcy courts can recalibrate "erroneously disbursed" value. Appellees do not address *Chateaugay II*. *See also In re Tribune Media Co.*, 799 F.3d 272, 283 (3d Cir. 2015) (redistributing recoveries that recipients "were never entitled to" does not moot appeal).

It is no answer that recalibration would "reduce appreciably the creditor-Appellees' economic recovery." Momentive Br. 53. This appeal is premised on the over-generosity of the Second-Lien Noteholders' "economic recovery" *at the Senior Subordinated Noteholders' expense*. Restoring a lawful balance between those creditor groups is not inequitable. *See Charter*, 691 F.3d at 484.

Appellees' contrary position depends on characterizing their spoils as the *quid pro quo* of an inviolable, "highly complex economic settlement." Br. 52. That is wrong for at least two reasons:

First, no grand "bargain" or "settlement" by Second-Lien Noteholders justifies extinguishing U.S. Bank's statutory appellate rights. Appellees point (at 53) to their agreement to backstop (for a $30 million fee) and participate in (at a 15% discount) a $600 million rights offering that has been wildly profitable. If only all "compromises" were so lucrative. Appellees likewise tout (at 53) having forgone a "billion-dollar unsecured deficiency claim" to allow 100% recovery for general unsecured creditors. But the latter claims were worth just 2% of the Second-Lien Noteholder's claims (nowhere near a billion dollars). Paying small creditors for their goodwill is standard in large reorganizations, and U.S. Bank would gladly share *pro rata* in that trivial sacrifice. Finally, Appellees observe (at 52-53) that Second-Lien Noteholders accepted equity on their secured claims. But this appeal would not affect those claims or the equity noteholders elected to receive on them.[5]

Second, Appellees cannot show that *any* recalibration of recoveries—down to a single dollar—would send Second-Lien Noteholders scrambling for the exits. No Second-Lien Noteholder submitted an affidavit stating that anything less than 100% of Momentive's equity is unacceptable. In fact, the bankruptcy and district courts concluded that U.S. Bank *could* be compensated on appeal because Second-Lien Noteholders so "strongly support" the reorganization. JA-2192; *see also* JA-2095. Second-Lien Noteholders will still profit handsomely from a modified plan respecting Senior Subordinated Noteholders' claims. The record confirms as much: The Plan has a $200 million "toggle" for the

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[5] The significance of Second-Lien Noteholders' purported "compromises" is diluted further by Apollo's ownership of Momentive *and* a substantial amount of Second Lien Notes. Appellees rely (at 56) on the Debtor's two-member "Conflicts Committee," but offer no information about whether that Committee had independent advisors and took any active role in "negotiating the Plan" (an assertion not supported by the cited affidavit).

treatment of other notes, confirming that Second-Lien Noteholders are willing to accept *at least* $200 million less value under the reorganization.

Appellees' remaining arguments are likewise unavailing. Trading in Momentive's equity began in March 2016 (Br. 56-57 & n.6), but former holders can disgorge cash, or Momentive can participate in a remedy (its new shareholders having been warned of that possibility, *see Charter*, 691 F.3d at 484-85). It would be inequitable *to U.S. Bank* if Appellees' foot-dragging engineered circumstances amounting to equitable mootness. In the bankruptcy court, Appellees resisted efforts to have this dispute decided before confirmation (which would have allowed this appeal to proceed expeditiously). Similarly, despite warnings by both lower courts that this appeal likely would *not* be equitably moot, Appellees pressed ahead with their transactions (and waived a plan condition requiring finality on appeal *before* the plan's effectiveness). And in this Court, Appellees strategically delayed their motion to dismiss until *94 days* after the notice of appeal, and *one day before* U.S. Bank's opening brief was due. Even if granting relief imposed some discomfort on Appellees, they have earned it.

The fact that U.S. Bank opposed confirmation in the bankruptcy court on the ground it now presses on appeal does not change anything. The Court can *modify* a confirmed plan on appeal to correct a legal error that should have prevented confirmation—that's the point of statutory appellate rights. Nothing in the Plan dictates otherwise, or gives Appellees a remedial veto. Appellees cite (at 57) Section 2.1(m) of their Restructuring Support Agreement (JA-3805), but that pre-petition document has no bearing on what "the Plan" requires, nor does it restrict this Court's power to modify a confirmed Plan. Appellees also cite Section 14.6 of the Plan, which authorizes Debtors to make "appropriate technical adjustments" post-confirmation (JA-4161), but it does not require "Appellees' consent" to court-ordered remedies. Br. 57. Even if it did, a doctrine grounded in equity cannot permit plan proponents to frustrate appellate rights through provisions in their own illegal plans. *See Charter*, 691 F.3d at 485.

B. U.S. Bank's Remedies Will Not Frustrate Momentive's Successful Reemergence From Chapter 11

Appellees' assertion that any remedy would cause Momentive "debilitating financial uncertainty" relies principally on the premise—debunked above—that the bankruptcy court must "reopen" the entire

Plan to provide U.S. Bank any relief. Br. 58. Appellees' corresponding parade of horribles is thus illusory.

Appellees' remaining "debilitation" arguments assume that *every* possible remedy would require Momentive to "owe" Senior Subordinated Noteholders up to $382 million. *Id.* at 53. Not so. Remedies are also available from Second-Lien Noteholders, so Appellees' argument on the second *Chateaugay* factor also fails for that reason alone.

Even if Momentive must fully fund any remedy, however, Appellees merely *speculate* about how certain entities *might* react. The possibility of undetermined disgruntlement does not create inequitable "uncertainty" and "risk"; it does not establish, more particularly, that this appeal will prevent the "re-emergence of the debtor as a revitalized corporate entity." *Chateaugay II*, 10 F.3d at 953. This Court rightly discounts such "conclusory predictions or opinions that the requested relief would doom the reorganized company." *Charter*, 691 F.3d at 482.

Appellees also claim that the valuation hearing necessary to determine the extent to which recoveries must be recalibrated will *itself* be too "extensive" and "time-consuming." Br. 59-60. Such a hearing, however, is not an "unmanageable, uncontrollable situation"; it's what bankruptcy courts do every day. *Chateaugay II*, 10 F.3d at 953. Until that hearing occurs, Appellees cannot know the amount of any recalibrated recovery, and thus have no basis on which to insist that Momentive's contribution (if any) to that remedy will cause a "downgrade in Momentive's debt rating" and "major disruption." Br. 60.

C. U.S. Bank's Stay Requests, And Appellees' Strategic Behavior, Confirm That Adjudicating This Appeal Is Equitable

Appellees do not even address this Circuit's "chief" equitable-mootness consideration: the Senior Subordinated Noteholders' undisputed diligence in pursuing a stay. *Metromedia*, 416 F.3d at 144. The word "stay" appears in Appellees' brief only once, when they quote that element of the analysis before ignoring it. U.S. Bank's diligence in seeking a stay from three courts (U.S. Bank Br. 18-20) means that providing "finality in bankruptcy proceedings" is "not sufficient" to discard this appeal. *Chateaugay II*, 10 F.3d at 954.

Indeed, the bankruptcy and district courts *denied* U.S. Bank's stay requests in part by concluding that this appeal *would not be equitably moot* if the Plan were to be consummated. JA-2095, JA-2192. And Appellees have thrown up roadblock after roadblock to prevent prompt resolution of this dispute. *See* U.S. Bank Br. 17 & n.3; *supra* p. 33. It would be inequitable to reward Appellees' strategic behavior with a refusal to exercise the Court's jurisdiction to decide this appeal.

CONCLUSION

For the foregoing reasons, this Court should reverse the judgment below, and instruct the district court to remand this matter to the bankruptcy court to fashion appropriate relief for the Senior Subordinated Noteholders.

Dated: June 29, 2016

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I certify that this brief complies with the type-volume limitations set forth in Fed. R. App. P. 32(a)(7)(B) because this brief contains 6,996 words according to the count of Microsoft Word 2010, excluding those parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii). I further certify that this brief complies with the typeface requirements of Fed. R. App. 32(a)(5) and the type-style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface, 14-point Century Schoolbook, using Microsoft Word 2010.

Dated: June 29, 2016

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CERTIFICATE OF SERVICE

I hereby certify that on June 29, 2016, I electronically filed the foregoing brief and its accompanying Special and Joint Appendices using the Court's CM/ECF system, causing copies to be served by CM/ECF upon counsel of record for all parties.

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