I. Introduction

Modernity, one will study the law of contracts as a homogeneous body of law.\(^1\) The conceptualization is helpful in creating an appearance of order,
allowing for the development of analytical frameworks. The construct breaks down, however, on detailed inspection. This article provides an illustration by examining aspects of the law governing corporate finance—legal principles at the intersection of the law of contracts and corporation law.

This article examines the application of contract doctrine to corporate financing transactions to a number of ends. First, it illustrates substantial

outline, and later for Williston to elaborate the theory ‘in meticulous, although not always accurate, scholarly details’ (pp. 13-14). After its brief flowering in the early twentieth century, the general theory of contracts weakened and proceeded to its ultimate collapse under the impact of new and vigorous principles of unjust enrichment and promissory estoppel (pp. 55-85).”

The instruments examined in this article primarily comprise securities (stock and bonds), although some authority addressing credit agreements is also examined. In this author’s experience, in large firms with transactional corporate practices representing those providing financing, these forms of financings are negotiated by different groups of lawyers. Those lawyers representing investment banks in securities offerings typically do not represent banks in extensions of credit and vice versa, although on the borrower or issuer’s side, it may well be the same counsel. Interpretative norms, insofar as they are co-extensive with practice groups, may vary between these two sets of instruments. Cf. infra notes 274-75 and accompanying text (rejecting application of trade practice in bond market for purpose of construing preferred stock).

In general, those differences are not parsed in this article, primarily for reasons of ease of illustration.

The idiosyncrasies in the law of corporate finance examined in this article primarily involve matters of interpretation. That is not to say only matters of contract interpretation receive idiosyncratic treatment in the law of contracts depending on the context. For example, unique principles govern the application of consideration in the context of non-competition agreements. See, e.g., Davies & Davies Agency, Inc. v. Davies, 298 N.W.2d 127, 130 (Minn. 1980) (collecting authority reaching inconsistent conclusions concerning whether continued employment constitutes consideration supporting a non-compete agreement). See generally 2 Arthur L. Corbin, Corbin on Contracts § 6.19 (Joseph M. Perillo, ed., John E. Murray, Jr., supp.) (LEXIS through release 13S1, June 2013) (discussing alternative approaches); 6 Richard A. Lord, Williston on Contracts § 13:13 (Westlaw through July 2013) (discussing consideration in this context); Ferdinand S. Tinio, Annotation, Sufficiency of Consideration for Employee’s Covenant Not to Compete, Entered into after Inception of Employment, 51 A.L.R.3d 825 (1973) (collecting authority).

The law governing satisfaction of conditions provides a second illustration, where the pertinent principles appear to change markedly in different contexts. Compare Moran v. Erk, 901 N.E.2d 187 (N.Y. 2008) (discussing an attorney approval condition in a real estate contract; concluding that buyers are not required to purchase even though they prevented satisfaction of the condition by advising lawyer not to approve) with AquaSource, Inc. v. Wind Dance Farm, Inc., 833 N.E.2d 535 (Ind. Ct. App. 2005) (discussing a corporate obligation conditioned on approval by its board; concluding that the failure to present it to the board made obligation unconditional). But see S. Internet Sys., Inc. v. Pritula, 856 So. 2d 1125 (Fla. Dist. Ct. App. 2003) (holding that the failure to present to the board was not a breach because there was no contract to which a duty of good faith could appertain).
inconsistencies in the application of contract doctrine depending on the subject matter.\(^4\) Principles applied to interpret corporate financing instruments are different from those typically applied modernly to interpret other agreements. Second, this article illustrates the inherent impracticability of achieving the goals justifying the use of different interpretive principles. The putative rationale for applying different interpretive principles is to assure consistency and predictability in interpretation. However, that goal is not achieved. Different interpretive principles apply to different parts of corporate financing agreements, yielding an incoherent interpretative mosaic and ongoing uncertainty as to whether anomalous interpretive principles will continue to be applied in particular contexts. Third, this article notes that the idiosyncratic interpretative principles applied to corporate financing instruments impede investors’ ability to diversify and increase the extent to which the law reaches erroneous interpretative conclusions.

It is helpful to put this overview in context. Consider two cases. In, *Reiss v. Financial Performance Corp.*,\(^5\) the New York Court of Appeals held that the number of shares purchasable on exercise of warrants (stock purchase rights) outstanding prior to a reverse split—a transaction in which outstanding shares of stock are reclassified into a smaller number of shares with each shareholder retaining the same proportionate interest and, therefore, not materially influenced by the event—are not affected by the reverse split. Of course, absent some


The division in the authority appears to concern the extent literalism will bend to the evident purposes expressed in the writing by referencing the writing as a whole to determine the purposes of the provisions and give effect to those provisions. Authority that would fully extend “neoclassical” interpretative approaches to corporate financing instruments, and the attendant jury determination of the meaning with full reference to objective manifestations of assent in agreements considered ambiguous under otherwise contemporary norms, seems infrequent.

adjustment, holders of options to purchase the stock would have their option values changed. The court concluded no implied adjustment was warranted.\(^6\)

That interpretation substantially increases the value of the warrants. Common stock represents simply a proportionate interest in the residual value of the firm, with the relative as opposed to the actual number of shares being significant.\(^7\) An actual reason why parties would have bargained for this result is missing.\(^8\) The outcome, even if a better literal reading of the contract, disregards this basic nature of stock.\(^9\)

On the other hand, a second case involving a similar issue but not involving a dispute between an issuer and a securityholder, *Cofman v. Acton Corp.*,\(^10\) reached the opposite result. The case involved a settlement agreement, under which one party provided others various contractual rights similar to warrants. The U.S. Court of Appeals for the First Circuit affirmed the trial court’s determination that an adjustment should be made in the rights granted under the settlement agreement as a consequence of a reverse split, even though the agreement did not expressly provide for such an adjustment. The court expressly stated interpretive principles applicable to corporate financing instruments should not be applied to a settlement agreement.\(^11\) This pair of cases expressly indicates

\(^6\) *Id.* at 959-60.

\(^7\) This observation was made long ago. *See*, e.g., VICTOR MORAWETZ, A TREATISE ON THE LAW OF PRIVATE CORPORATIONS § 347, at 353 (1882) (“If then a corporation having power to increase its nominal or share capital has accumulated a surplus which it would be entitled to distribute among its shareholders, it may issue to the shareholders new paid-up shares, to the extent of the surplus on hand . . . .”). The stockholders do not in reality gain thereby, but the number of their shares is increased in proportion as their value is diminished. The relative rights and powers of the several stockholders thus remain unaltered.

\(^8\) *See generally infra* note 290 (quoting Berle to the effect that “[i]t is believed” a court would make an equitable adjustment).

\(^9\) Note the result of the type reached in *Reiss* is not constrained to avoiding implying terms benefiting an issuer whose actions trigger the problem. Other cases apply similar literal interpretations where the adversely affected party is the securityholder. *See infra* note 162.

\(^10\) 958 F.2d 494 (1st Cir. 1992).

\(^11\) *Id.* at 497 n.5 (“We do not pause over Partnership’s sought analogy to convertible debentures, where the rule is that anti-dilution must be expressly stated. These are formal, and complicated commercial structures, prepared with care for the general public. Purchasers have the bonds in any event. Here we have a simple agreement between individuals, not even assignable.”) (citing Broad v. Rockwell Int’l Corp., 642 F.2d 929, 940-45 (5th Cir. 1981); Parkinson v. W. End St. Ry., 53 N.E. 891 (Mass. 1899)).
that interpretative principles applied to corporate financing instruments are different from those customarily applied in contractual interpretation.

Literal interpretation of corporate financing instruments traces back at least to *Parkinson v. West End St. Ry. Co.*,\(^\text{12}\) where the Massachusetts Supreme Judicial Court, per Justice Holmes, also implemented a formal, literal interpretation of a corporate financing instrument, justifying the outcome “not because the law has not machinery for keeping such a right alive, but because, not being bound to do so, [the issuer] has made dispositions which manifestly take no account of it.”\(^\text{13}\) One may describe continued adherence to this interpretative approach as *vestigial literalism*.

A modern approach to contract interpretation de-emphasizes literalism and gives great weight to the parties’ evident purposes.\(^\text{14}\) Illustrative in addition to *Cofman* is *Van Gemert v. Boeing Co.*,\(^\text{15}\) which involved a claim that an issuer of convertible debentures\(^\text{16}\) (meaning debentures that give a holder the right to have the debentures exchanged for common stock) failed to give adequate notice of a redemption. The redemption terminated the conversion right. Holders objected to the inadequate notice, because those failing to convert received cash worth about one-third of the value that they could have received on conversion.\(^\text{17}\) The U.S. Court of Appeals for the Second Circuit did not limit the promisee-debentureholders rights to the express literal terms. It found an implied duty to give reasonable notice and stated, as to the notice actually given, “While it may have conformed to the requirements of the Indenture it was simply insufficient to give fair and reasonable notice to the debenture holders.”\(^\text{18}\)

The primary justification for the vestigial literalism sometimes followed is an asserted enhanced desirability of consistency in the construction of corporate financing instruments, even at the expense of reaching the “correct”

\(^\text{12}\) 53 N.E. 891 (Mass. 1899).
\(^\text{13}\) *Id.* at 892.
\(^\text{14}\) *See, e.g.*, [RESTATEMENT (SECOND) OF CONTRACTS § 202(1) (1981)] (“Words and other conduct are interpreted in the light of all circumstances, and if the principal purpose of the parties is ascertainable it is given great weight.”).
\(^\text{15}\) 520 F.2d 1373, 1383 (2d Cir. 1975).
\(^\text{16}\) *Id.* at 1374.
\(^\text{17}\) *Id.* at 1374-75.
\(^\text{18}\) *Id.* at 1383.
interpretation. However, for a number of reasons, predictability is not achieved, and is perhaps even suppressed.

First, deference more often is given to outcomes in prior cases than to the principles that yielded those outcomes. The interpretive principles applied to corporate financing instruments sometimes deemphasize the actual language used. Some cases reflect a sequence in which a court first interprets a provision, relying on the precise language or the context to support the conclusion, and then another court, in another case, elides the basis for the initial decision and extends the interpretative outcome to a case where the significant context or particulars in language are not present.

Second, the modern outcome depends on whether the issue was first litigated long ago. Over time, courts increasingly have emphasized seeking to give effect to the parties’ evident purposes, de-emphasizing a literalism that courts formerly followed to a greater extent. When an issue was litigated long ago, the literalism of the nineteenth century governing its interpretation often will continue to be followed today. However, where the issue was not litigated long ago, a court may apply modern interpretative principles, emphasizing implementation of the evident purposes, as in Van Gemert. The result is a mosaic of modern corporate finance jurisprudence that is path-dependent based on whether a particular issue happens to have been litigated long ago.

19 See infra note 29 and accompanying text.

20 See infra Part IV.B.


22 For example, In re Hennepin County 1986 Recycling Bond Litigation, 540 N.W.2d 494, 501-03 (Minn. 1995), held that securityholders adequately alleged a breach of contract and the implied covenant of good faith against an issuer that sought to trigger a redemption, on terms not otherwise permitted under the instruments, by arranging a default. This is a purpose-centric interpretation. See id. at 500-01 (“Logically, one must ask why the parties would have painstakingly negotiated an economic risk allocation in the bond agreements, permitting the County to redeem at its option prior to the October 1, 2000, maturity if it were willing to pay a premium to do so, but simultaneously permitting the County to redeem at the expiration of the Letter of Credit, without a premium penalty, simply by blocking renewal or extension of the Letter of Credit.”). The case inhibits a promisee’s terminating duties by an intentional default, extending old authority holding an acceleration provision in a note that by its terms provides for an automatic acceleration upon a default simply creates an option to accelerate. See, e.g., Richardson v. Warner, 28 F. 343, 344 (D. Neb. 1886) (“A provision in a mortgage that, upon default in the payment of interest due on any of the notes secured thereby, the entire debt shall immediately become due and payable, does not, of itself, cause the notes to mature, so as to start the running of the statute of limitations. The stipulation is permissive only, and simply gives a privilege to the mortgagee.”); In re Premier Entm’t Biloxi LLC, 445 B.R. 582, 627-28 (Bankr. S.D. Miss. 2010) (referencing
Third, deference is not consistently applied. For example, the intermediate appellate court in Reiss implemented modern interpretative principles, but on appeal, the New York Court of Appeals rejected that approach.\(^{23}\) A second example is provided by a number of modern cases discussed below that do not defer to prior authority construing the import of indenture covenants addressing distribution of SEC filings to bondholders.\(^{24}\)

Fourth, a more subtle point illustrates that the result of this anomalous interpretive approach creates a type of uncertainty not fully addressed by the authority. Certainty at the time litigation is commenced may be at the expense of certainty as of the time an agreement is drafted. It is not clear why the former should be promoted at the expense of the latter.

To illustrate this distinction, it may be noted that one supposes when it becomes clear litigation may ensue concerning interpretation of a corporate financing instrument in a particular context, the lawyers responsible for litigating the matter can undertake an extensive search for authority addressing the matter. However, at least in this author’s experience negotiating these kinds of corporate financing instruments, during the negotiation the participants do not extensively research how courts have construed all possible ways in which particular terms could be written. Rather, those negotiating these instruments become aware of certain interpretations of particular provisions, in the course of their professional reading, and proceed in drafting based on extrapolating from principles evidenced by authority with which they are familiar. The intermittent application of vestigial interpretive principles produces a mosaic of law that is not predictable to draftsmen from knowledge of only selected interpretations. Because the application of vestigial interpretive principles is path-dependent based on whether

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\(^{23}\) Reiss v. Fin. Performance Corp., 279 A.D.2d 13, 19, 715 N.Y.S.2d 29 (2000) (“[P]laintiffs and the dissent assert that a literalistic approach to the interpretation of the warrants is compelled as a matter of law. We cannot agree. Surely a court is not required to disregard common sense and slavishly bow to the written word where to do so would plainly ignore the true intentions of the parties in the making of a contract. Such formalistic literalism serves no function but to contravene the essence of proper contract interpretation, which, of course, is to enforce a contract in accordance with the true expectations of the parties in light of the circumstances existing at the time of the formation of the contract.” (citations omitted)), aff’d as modified, 764 N.E.2d 958 (N.Y. 2001).

\(^{24}\) See infra notes 36-39 and accompanying text.
a particular issue was litigated long ago, and that path-dependence is not predictable, there is an offsetting decrease in predictability to individuals negotiating these instruments.

Predictability is not the sole goal of contract interpretation. This failing attempt to assure predictability also impedes the realization of diversification—one of the benefits desired by those who enter into these contracts. Investors often will purchase a portfolio of securities in order to decrease the volatility of the aggregate value of their investments. However, this uniformity of interpretation produces the opposite result. If unusual deference is paid to the outcome reached in the first case to interpret a particular matter, a risk is created that is more difficult to mitigate through diversification because, by premise, the same result will govern other investments.

Moreover, the excessive deference is more likely to result in an average answer that is “wrong” or does not conform to ex ante expectations. That is because common law courts normally engage in iterative decision making. Subsequent decisions in other jurisdictions can correct mistakes. A wise initial decision is more likely to be followed than a poor one. Thus, the results reached in subsequent decisions are more likely to be correct than those initially reached. So a change in the development of common law doctrine under which enhanced deference is paid to initial decisions, even if not considered subsequently “correct” as an initial proposition, generally produces more incorrect outcomes. This change decreases the ability to diversify, and generally creates worse outcomes.

Part II of this article summarizes the reasons that courts have sought to use alternative interpretative principles in construing corporate financing instruments. Courts have concluded there is a heightened need for predictability and consistency in the interpretation of these instruments, which has had the effect of partially suppressing the development of contract doctrine as applied to interpretation of these instruments. The interpretative principles also appear to be influenced by the fact that the contracts implicate the rights of multiple parties, some of whom are not present at the time the contracts are negotiated. Additionally, interpretation of parallel language in statutory provisions that govern the transactions may influence interpretation of the contractual provisions. Multiple factors thus give rise to anomalies in the interpretation of these instruments.

Part III of this article details these anomalies. Subpart A first illustrates some circumstances where conventional principles are applied to interpret corporate financing instruments. Subpart B then identifies select individual issues that have given rise to inconsistent interpretative approaches. Subpart C collects
authority emphasizing interpretative principles that modernly have been discarded in other contexts. The complexity of these instruments may result in courts being unable to identify the evident purposes. Subpart D then collects authority where courts apparently retreat into tedious literalism because the evident purposes are difficult to grasp.

Part IV of this article addresses two additional anomalies. Subpart A examines the inconsistent application of contra proferentem. Subpart B then provides authority that curiously treats some provisions in corporate financing instruments as abstract concepts that are to be construed as divorced from the language actually used. Some concluding remarks then follow in Part V.

II. REASONS AND RATIONALE UNDERLYING INTERPRETATIVE PRINCIPLES AND IDIOSYNCRASIES

At least five categories of circumstances give rise to idiosyncrasies in the interpretation of corporate financing instruments:

1. There is an increased need for predictability and consistency, courts have concluded, in the interpretation of these instruments;

2. The rights of multiple parties, some of whom are not present when the instruments are negotiated and others who owe varying levels of duties to the individuals identified only later;

3. The agreements are interpreted in the shadow of statutory language regulating some of the covered transactions, including corporation law as well as components of the federal securities laws (including the Trust Indenture Act of 1939); and, in addition, other statutory language and concepts are reflected in the agreements, allowing for interpretation of statutory provisions to infiltrate interpretation of these agreements;

4. The large dollar amounts of the transactions, coupled with their sophistication in structure and frequency, results in lengthy documents addressing the transactions in extensive detail, memorializing understandings the purposes of which may be relatively less patent; and

The process of documenting these agreements results in contemporaneous descriptions not often available for interpreting other contractual agreements. This Part details those categories and the underlying rationales.

A. Heightened Need for Predictability and Consistency in Interpretation

Because corporate financing instruments often are designed to create rights intended to be traded, courts have concluded that certainty in interpretation of these instruments is of enhanced importance. Two of the prominent modern cases articulating this rationale are Broad v. Rockwell International Corp. and Sharon Steel Corp. v. Chase Manhattan Bank. In Broad, the U.S. Court of Appeals for the Fifth Circuit articulated the view and identified why the rationale applies to corporate financing instruments:

A large degree of uniformity in the language of debenture indentures is essential to the effective functioning of the financial markets: uniformity of the indentures that govern competing debenture issues is what makes it possible meaningfully to compare one debenture issue with another, focusing only on the business provisions of the issue (such as the interest rate, the maturity date, the redemption and sinking fund provisions and the conversion rate) and the economic conditions of the issuer, without being misled by peculiarities in the underlying instruments.

The U.S. Court of Appeals for the Second Circuit in Sharon Steel echoed this rationale, stating:

Whereas participants in the capital market can adjust their affairs according to a uniform interpretation, whether it be correct or not as an initial proposition, the creation of enduring uncertainties as to the meaning of boilerplate provisions would decrease the value of all debenture issues and greatly impair the efficient working of capital markets. Such uncertainties would vastly increase the risks and, therefore, the costs of borrowing with no offsetting benefits either in the capital market or in the administration of justice. Just such uncertainties would be created if interpretation of boilerplate

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26 642 F.2d 929 (5th Cir. 1981).
27 691 F.2d 1039 (2d Cir. 1982).
28 Rockwell, 642 F.2d at 943.
provisions were submitted to juries sitting in every judicial district in the nation.\textsuperscript{29}

These cases are widely cited,\textsuperscript{30} and have been the subject of recent commentary.\textsuperscript{31} Although the discussion in \textit{Sharon Steel} appears to be limited to standard provisions that are “found in virtually all indentures,”\textsuperscript{32} this approach has been referenced by some courts as to provisions that are not found in virtually all indentures.\textsuperscript{33}

\textsuperscript{29} \textit{Sharon Steel}, 691 F.2d at 1048. Accord \textit{Rievman v. Burlington N. R.R. Co.}, 618 F. Supp. 592, 601 (S.D.N.Y. 1985) (“In addition, at least one of the key cases relied on by plaintiffs cannot be effectively distinguished by the Railroad, and appears to govern this case . . . . The New York Court of Appeals seemed to be laying down a \textit{per se} rule: because of the ‘vast sums invested in railroad bonds’ and the need to insure investor confidence, railroad mortgage trustees may not ‘sell, change, or in any manner compromise the security except as authorized in express terms or by necessary implication’—even where the sale or change would not harm the bondholders’ interests.”); \textit{Bank of N.Y. Mellon Trust Co. v. Liberty Media Corp.}, 29 A.3d 225, 241 (Del. 2011) (“Courts endeavor to apply the plain terms of such provisions in a uniform manner to promote market stability.”). Authority identifying the preference for consistency in interpretation of standardized instruments is not, however, limited to interpretation of securities. \textit{See, e.g.}, Mass. Mut. Life Ins. Co. v. Certain Underwriters at Lloyd’s of London, No. 4791-VC, 2010 WL 2929552, at *5 n.1 (Del. Ch. June 23, 2010) (stating, in referencing the principle in connection with a fidelity bond, “The point applies equally to other standardized instruments.”). So, the law governing interpretation of corporate financing instruments is unusual but not unique.


This rationale—the need for certainty—also may be the basis for a determination that there is not an implied limit on the exercise of an express right. \textit{See Rievman}, 618 F. Supp. at 601, (referencing the “‘vast sums invested in railroad bonds’ and the need to insure investor confidence” in rejecting an implied right to alter collateral benefitting over-secured bondholders.) \textit{See infra} notes 172-177 and accompanying text.


\textsuperscript{32} \textit{Sharon Steel}, 691 F.2d at 1048.

\textsuperscript{33} \textit{See, e.g.}, \textit{Archer Daniels Midland}, 570 F. Supp. at 1539 (protection against re-financing with lower-interest-rate debt); \textit{Kaiser Aluminum}, 681 A.2d at 398 (quoting \textit{Sharon Steel} in discussing anti-destruction provisions that vary significantly among indentures; discussing provisions the court
There are two separate components to the predictability and certainty
promoted by this authority; they are, in fact, in some tension with each other. The Fifth Circuit in Broad identified a desire to promote fungibility as to certain
components of corporate financing instruments. The language from Sharon Steel
identified a preference for predictability in interpretation. Both components
attempt to implement a preference for facilitating, and decreasing the transaction
costs of, raising capital, by attempting to decrease the need to engage in valuation
activities that can be costly.

1. Fungibility

There are costs associated with assigning dollar values to various terms in
corporate financing instruments. If all issuers have the same terms as to a
particular issue, the valuation is less difficult and, hence, less costly.34

For example, consider “successor obligor” provisions in corporate bonds. Such provisions may allow, without bondholder consent, sale of all or
substantially all of an issuer’s assets where the buyer assumes the initial obligor’s obligations. An issue may arise concerning how multiple asset sales by the initial
obligor will be treated under such a covenant. Are they all integrated in some
way?

The possibility that an issuer of bonds will sell its assets to someone else is
present for most, perhaps essentially all, non-governmental issuers of bonds. If
contracts limiting these actions without bondholder consent have significantly
different terms, an investor choosing between prospective bond purchases may
need to reduce the impact of the variation to a dollar value. That may require
assessment of the relative likelihood that various prospective issuers would
engage in transactions that might trigger the need for protection. On the other
hand, if the terms are uniform and provide adequate protection, a prospective
investor may elide assessment of the differences in probabilities that the various
issuers may sell their assets.

The point is that prospective investors are choosing among investments
in various issuers. The choice is simplified if certain terms (non-financial terms)
are standardized, because this limits the number of dimensions on which one
should compare the various investments, and, therefore, simplifies the analysis. A
more complex analysis also creates greater uncertainty, which also increases the

34 See generally Marcel Kahan, Rethinking Corporate Bonds: The Trade-off Between Individual and Collective

describes as “hopelessly ambiguous”). The language of Broad, 642 F.2d at 943, quoted supra text
accompanying note 28, seems to be to a similar effect.
cost of capital. Increased complexity of analysis creates risk of error and also introduces variables that cannot be precisely quantified. Increased uncertainty increases the likelihood that a successful investor will pay more because it has made mistakes that others have not, over-valuing the investment—a winner’s curse. This ultimately results in decreased willingness to invest.

However, fungibility cannot be achieved. The drafting of these complex instruments is an iterative process. As issues arise in one deal, draftsmen seek to include in future transactions language addressing the matter, which may but need not provide for the treatment courts apply in litigation. The process of fixing problems made in prior generations of transactions necessarily results in a lack of fungibility. The goal of fungibility conflicts with the natural process of learning from the mistakes of others in drafting these complex instruments and fixing the problems.

2. Consistency and Predictability

The increased emphasis on certainty includes a desire for enhanced consistency—interpreting some particular language the same way in all disputes. Evidently, it is intended that, once language is interpreted all market participants, not just those involved in the first case to litigate the issue, are expected simply to move on, adjust their affairs in light of that interpretation, and pretermit litigation of the same issue by different parties in a different forum. The Sharon Steel court indicated that “participants . . . can adjust their affairs according to a uniform interpretation . . .” Clearly, this was envisioned to avoid costs of subsequent litigation by different parties and allow planning in the context of certainty.

As this article will discuss, that predictability is not achieved, and those costs are not saved. Matters are re-litigated by other parties, sometimes successfully, meaning that certainty for planning is not realized. For example, a series of cases in the last decade involved whether an issuer’s failure to make timely SEC filings and deliver copies to a trustee constituted a breach under an indenture. In an early case, Bank of New York v. BearingPoint, Inc., the New York Supreme Court granted summary judgment to the trustee on a claim that failure to deliver the filings breached the indenture. However, a number of cases

35 Sharon Steel, 691 F.2d at 1048; see supra text accompanying note 29. But see Kahan, supra note 34, at 1082 (arguing in favor of a change in a particular modern interpretation in light of claim outcome is unsatisfactory).


37 Id. at *9.
decided after *BearingPoint* declined to defer to the prior construction and reached the opposite conclusion in construing similar language. The outcomes in the latter cases reflect a somewhat strong failure to defer to prior authority, because the *BearingPoint* decision was of a New York court, and the subsequent decisions were from courts in other locations construing New York law.

Another part of this rationale is a desire for enhanced predictability—creating an environment in which one considering the application of particular language in an executed contract, or language proposed to be included in a contract being negotiated, can have increased confidence that the language will be interpreted in a particular fashion.

The preference for predictability sometimes results in courts increasingly relying on literalism in interpreting these instruments. Some argue a literal interpretation is more predictable and, thus, enhances predictability. In addition, the increased emphasis on literalism in part results from the fact that reference to older precedent is to authority decided when courts emphasized literalism of the type illustrated by *Parkinson v. West End St. Ry. Co.*

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39 *Affiliated Computer Services*, 565 F.3d at 928 (indenture governed by New York law); *UnitedHealth*, 548 F.3d at 1128; *Cyberonics*, 2007 WL 1729977, at *3, 5 (“Although it decides a similar issue, *BearingPoint* is an unpublished decision from a state trial court and is not binding on this Court. The case was initially appealed but then withdrawn; therefore, no New York appellate court reviewed that decision. Despite the *BearingPoint* decision, the Court is not persuaded that the agreement between Cyberonics and Wells Fargo imposed any obligation upon Cyberonics other than to provide Wells Fargo with copies of documents and reports after those documents and reports had been filed with the SEC. As required by New York law, this Court will enforce the agreement as it is written.”).

40 See *Bratton*, supra note 4, at 401 (“A three-pronged argument support’s *Broad’s* proposition that classically inspired rules promote certainty. First, classical rules restrict the scope of the interpretation inquiry. This limits the range of interpretations to which a given contract is legally susceptible . . . .”); Dick, supra note 31, at 1480-81 (stating, in reference to what that author identifies as a *Certainty Imperative*, “Consequently, a court adhering to the Imperative adopts a presumption that law reform or expansive analysis of any sort will impair market efficiency. Under this perspective, judicial decision-making in the financial realm poses a potentially dangerous externality. Thus, judicial decisions are narrowly tailored to strict construction and passive enforcement of contracts.”).

41 53 N.E. 891 (Mass. 1899). See *infra* notes 281-286 and accompanying text (discussing the case).
As discussed below, it is not clear that the adopted adjustments to interpretive principles in fact enhance certainty in interpretation of corporate financing instruments. The interpretation of an agreement involves balancing a literal reading with a reading reflecting the purposes evident from the language as a whole. Uncertainty arises from the need for a dividing line. Understanding that there has to be a dividing line—even older authority rejects complete literalism—predictability is not enhanced by merely moving the imprecise dividing line.

3. Impediment to diversification

It also bears mention that an approach involving enhanced deference to initial authority in fact can increase the cost of capital. Investors purchase a portfolio of securities for purposes of diversification (which decreases the risk of the portfolio as a whole) because that decreased risk is valuable. Enhanced deference to initial authority increases the risk.

In diminishing the importance of whether an initial interpretation is “correct or not as an initial proposition,” a court is decreasing the relevance of whether the outcome of the litigation respects the bargain that the parties understood they struck or the purposes the parties had in mind when they reached the deal.

See infra Part III.

See, e.g., supra note 22 (acceleration provisions not construed literally, based on longstanding authority); Bratton, supra note 4, at 403 (“Judges circumvented the strictures of the rules even in classicism’s palmy days.”).

As a theoretical matter, there may be circumstances in the law where the location of where one draws a line may in fact enhance certainty. Suppose that, at least some time before global positioning systems and sophisticated surveying, there may have been fewer disputes as to whether houses were on one person’s property where boundaries were drawn on the basis of a center of a waterway. Understanding that residences are not typically in water, it is possible that in some circumstances, uncertainty as to the precise boundary may have less impact because there are fewer disputes that arise because the boundaries have been located in this particular way. That kind of argument is not the extant claimed basis for increased certainty in interpretation of corporate financing instruments.

Following the summer submission of the manuscript for this article, Professor Kelli Alces published an essay generally examining the diversification of legal consequences. Kelli A. Alces, Legal Diversification, 113 Colum. L. Rev. 1977 (2013). But for this observation, the textual discussion in this article speaks as of summer 2013.
Some courts first hearing a matter will give effect to the intended bargain. Others will not properly identify what was sought to be achieved and will err. If the matter is capable of being re-litigated with another issuer in a different forum, that allows for diversification of investment risk. On the other hand, if all courts defer to the first to address the matter, that inhibits investment diversification.

In addition, one hopes that successive attempts by courts to interpret an issue will result in better subsequent decision making. Normal judicial decision making is not simply successive coin-flipping. Rather, one would expect it would settle over time on better answers—that initial decisions based on thoughtful insights would be respected. However, if a second look by a different court (perhaps one more experienced in the particular field) justifies its results in a more persuasive way, subsequent courts would be persuaded by the rationale of the latter, superior decision when faced with competing precedent. So, enhanced deference to precedent not only prevents diversification but also settles on an outcome that is less likely to be correct than the “average” outcome that would arise without this enhanced deference.

B. Multiple Parties

1. Increased complexity and interpretative principles incorporating parties’ roles

A typical corporate financing transaction involves multiple parties, only some of whom are present at the time the documents are negotiated and finalized. Common to all these transactions would be the issuer and the investors (or prospective investors). The initial investors often will not actually be present, or formally represented, in the negotiation of the instruments. Rather, the terms of the instruments are negotiated between representatives for the issuer and one or more investment banks that are to assist in the sale of the securities to investors, either as an underwriter or as a placement agent. If the securities are debt securities to be sold publicly, a bank acting as trustee will also be present.

This multiplicity of parties and roles has a number of implications. The trustee, if one is appointed, ultimately will assume conditional fiduciary duties to investors and will have certain rights, some of which are exclusive and others of

46 Cf. Bratton, supra note 4, at 405 (“Neoclassical analysis, by expanding the inquiry to include all real world expectations, requires courts to make judgments informed as much by business as by legal considerations. Such business judgments lie outside of what many judges like to see as the ordinary sphere of their competence.”).

which are not, to pursue remedies against the issuer in the case of default. This increases the complexity of the documents because the scope of the trustee’s obligations needs to be detailed, and the trustee’s exercise of remedies and the exercise of remedies by investors need to be coordinated by the documents.

The parties ultimately benefiting from promises made by issuers in corporate financing transactions often are not present when the agreements are negotiated. Most obviously, corporate financing instruments are designed to create contractual relationships that can be conveyed, and an active market in them often develops, either on a securities exchange or otherwise. By definition, those acquiring the interests through subsequent trading will not have been present. In addition, even the initial investors often are not present, depending on the nature of the transaction. Rather, it is often the case in public offerings of securities that the participants in the negotiations are the issuer; one or more investment banks; if the securities are public debt, a trustee; and, of course, counsel. The investment banks do not exclusively promote the interests of the future investors, because the issuer is also their client. This collection of relationships influences the extent to which some courts apply interpretative principles that incorporate the roles of the parties, such as contra proferentem.

2. Abstraction of negotiation; disregard of certain evidence

Corporate financing transactions often produce certain extrinsic manifestations of intent that are not generally the product of contract negotiation. The contractual provisions often will be summarized in a prospectus, offering memorandum, or offering circular. As to the description of the securities, careful practitioners may intentionally provide no insight by simply reproducing in the

48 See generally Bratton, supra note 4, at 377 (concluding, “We have seen that the most basic of rubrics—interpretation in accordance with the intention of the parties—cannot be applied literally in the interpretation of trust indentures.”).

49 See, e.g., Kaiser Aluminum Corp. v. Matheson, 681 A.2d 392, 398 (Del. 1996) (“Courts have disagreed, however, whether the principle should apply in the case of detailed indentures or similar documents. This reflects, in part, contrasting views regarding the respective roles played by underwriters and issuers. See, e.g., Simons v. Cogan, Del.Ch., 542 A.2d 785, 791 (1987), aff’d, Del.Supr., 549 A.2d 300 (1988) (“Underwriters of convertible securities do have an interest in negotiating protection on points regarded as material by ultimate purchasers of those securities.”); Metropolitan Life Ins. Co. v. RJR Nabisco, Inc., S.D.N.Y., 716 F.Supp. 1504, 1509 (1989) (“Since the underwriters must then sell or place the bonds, they necessarily negotiate in part with the interests of the buyers in mind.”) (footnote omitted)). See also infra note 232 and accompanying text.
offering documents selections from the underlying contractual relationships, \(^50\) precisely in order to avoid expressing an opinion concerning what the instruments mean. However, even if those documents are not illuminating as to an issue that becomes disputed, other contemporaneous documents may capture the parties’ intent, such as internal communications between various investment banks that are participating in marketing the securities \(^51\) or communications with rating agencies. \(^52\) Because these transactions are large, they may capture media attention that results in public communications relevant to construing the contractual terms. This collection of sources creates idiosyncratic issues of contract interpretation.

Objective manifestations of intent made during contract negotiation generally may be considered in interpreting ambiguous contracts. \(^53\) However, it is more problematic to reference those objective manifestations of intent in interpreting corporate financing agreements, where the persons on one side of the bargain are not present during the negotiations and not directly represented. That would support judicial reluctance to reference some extrinsic manifestations of intent in interpreting corporate financing instruments.

In sum, because these contractual rights are designed to be traded, courts seek to enhance the certainty of contractual interpretation. In addition, this context has fostered a decreased reference to extrinsic manifestations of intent, even though these transactions produce some evidence of this that is not typically available in other contracts.

\section*{C. Statutory Overlay}

Interpretation of these corporate financing instruments is also influenced by separate statutory provisions. The Trust Indenture Act of 1939 \(^54\) directly

\(^{50}\) See Plaintiff’s Exhibit 103, Direct Testimony of Stephen L. Burns, Chesapeake Energy Corp. v. Bank of N.Y. Mellon Trust Co. at 14, ¶ 26, 13 Civ. 1582 (PAE), 2013 WL 1890278 (S.D.N.Y. Apr. 21, 2013) (“Associates who work for me are under standing instructions in such situations to conform, closely if not exactly, the draft indenture to the applicable provision in the description of notes of the prospectus supplement.”).

\(^{51}\) See Direct Testimony Declaration of James A. Mullin, Chesapeake Energy Corp. v. Bank of N.Y. Mellon Trust Co. at p.5, ¶¶ 12-14; p.9, ¶ 26, p. 11, ¶ 30, 13 Civ. 1582 (PAE), 2013 WL 1890278 (S.D.N.Y. Apr. 21, 2013) (referencing internal memorandum in providing an opinion as to the terms of securities).

\(^{52}\) See infra note 69 and accompanying text.

\(^{53}\) See, e.g., JOSEPH M. PERILLO, CALAMARI AND PERILLO ON CONTRACTS § 3.10 (6th ed. 2009).

regulates the terms of some of these agreements. Under that act, publicly sold debt securities are generally required to be issued under an indenture appointing a trustee.\textsuperscript{55} The act provides that certain terms are automatically incorporated by reference into the indenture, some of which can be changed by agreement.\textsuperscript{56} Thus, interpretation of these provisions inherently involves statutory interpretation.\textsuperscript{57}

Statutory provisions can have a more indirect impact on the contours of the rights created by corporate financing instruments. An issuer may structure a transaction of potential concern to securityholders in a form that is regulated by state corporation law. For example, an issuer having outstanding convertible stock may have promised to make adjustments in the convertible stock if the underlying securities are reclassified. An issuer may alter the underlying stock in a merger, giving rise to interpretive questions concerning whether promises triggered by reclassifications of underlying stock are implicated by a merger.

Delaware and some other jurisdictions follow the Doctrine of Independent Legal Significance,\textsuperscript{58} under which “action taken in accordance with different sections of that law are acts of independent legal significance even


\textsuperscript{57} See generally Emmet & Co. v. Catholic Health E., 951 N.Y.S.2d 846, 850-51 (Sup. Ct. 2012) (involving claims alleging issuer's tender offer for bonds to be followed by redemption of bonds not tendered constituted a partial redemption not following partial redemption procedures; exception in no-action provision to payments of principal and interest does not apply because the exception is limited to past-due principal and interest).

\textsuperscript{58} Statutory provisions include GA. CODE ANN., § 14-2-103 (Westlaw through June 15, 2013); KY. REV. STAT. ANN. § 271B.1-430 (Westlaw through 2012 First Extraordinary Sess.); MO. REV STAT. § 351.017 (Westlaw through May 15, 2013). See also William J. Carney & George B. Shepherd, The Mystery of Delaware Law's Continuing Success, 2009 U. ILL. L. REV. 1, 13-14, 13 n.70 (also citing case law in the State of Kansas and the State of Rhode Island using the signal “See, e.g.,” although there does not appear to be significant supporting case law in other jurisdictions. See Westlaw search: “independent legal significance” /200 corporation, all state and federal cases (identifying 126 cases providing limited additional authority on-point) (July 1, 2013).
Though the end result may be the same under different sections. This principle of statutory interpretation has been extended to construction of corporate financing contracts in Delaware. In a variety of contexts, this principle has been the basis for allowing an issuer to avoid prohibitions or limitations on certain transactions by achieving the same result through another extraordinary action. For example, voting rights applicable to adverse amendments in terms of securities may be avoided by achieving the same result through a transaction structured as a merger.

As another illustration of inconsistency, although Delaware courts frequently apply the principle (although not always), there is older U.S. Supreme Court authority taking the opposite approach—treating an action as permitted because a similar result could have been achieved in a different way that was not prohibited.

Other statutes regulate various types of corporate transactions, such as tax law. Interpretive principles developed to restrain avoidance of statutory restrictions, such as those applied in tax law, may be carried over to fortify interpretation of corporate financing instruments. The analogy is easier because

60 See, e.g., D. Gordon Smith, Independent Legal Significance, Good Faith, and the Interpretation of Venture Capital Contracts, 40 WILLAMETTE L. REV. 825, 837 (2004) (“In a modern twist, the Delaware Supreme Court has changed the doctrine of independent legal significance from a rule of statutory interpretation into a rule of contract interpretation.”); C. Stephen Bigler & Blake Rohrbacher, Form or Substance? The Past, Present, and Future of the Doctrine of Independent Legal Significance, 63 BUS. LAW. 1 (2007) (discussing the doctrine and how recent court decisions may impact the doctrine).
61 See, e.g., Elliott Assocs., L.P. v. Avatex Corp., 715 A.2d 843, 853, 855 (Del. 1998) (holding based on the certificate of designation that holders of preferred stock had a right to a class vote on a merger of the issuer into its newly-formed subsidiary in which the preferred stock would be converted into common stock of the survivor; noting voting rights under section 242 of the Delaware General Corporation Law were not implicated because the transaction was a merger).
63 Otis & Co. v. SEC, 323 U.S. 624, 637-38 (1945) (“Enforcement of an overriding public policy should not have its effect visited on one class with a corresponding windfall to another class of security holders. Nor should common stock values be made to depend on whether the Commission, in enforcing compliance with the Act, resorts to dissolution of a particular company in the holding company system, or resorts instead to the devices of merger or consolidation, which would not run afoul of a charter provision formulated years before adoption of the Act in question. The Commission in its enforcement of the policies of the Act should not be hampered in its determination of the proper type of holding company structure by considerations of avoidance of harsh effects on various stock interests which might result from enforcement of charter provisions of doubtful applicability to the procedures undertaken.”).
the same kinds of moves available to corporations to avoid proscriptions in tax or other statutory law may be used to evade promises in corporate financing instruments. For example, reference to a “step transaction” or a “sham,” interpretive principles familiar in tax law,\(^{64}\) may be applied analogously in interpreting corporate financing instruments. In corporation law, the common corporate principle concerning respect to the corporate form, or disregarding it under principles of piercing the corporate veil, have analogues in interpretation of corporate financing instruments where issuers have sought with some success to avoid proscriptions by acting through subsidiaries.\(^{65}\)

Additionally, a number of statutory provisions may reference terms or acts regulated by contract. State corporation law will, for example, regulate declarations of dividends. Of course, covenants in a corporate financing instrument also may reference dividends by restricting them. Interpretive gloss applied in construing the term in the statutory context may carry over to interpretation of the term as used in corporate financing agreements.

In sum, statutory provisions directly adjust the interpretation of corporate financing instruments. In addition, interpretive principles governing statutory language, which may be at odds with how corporate financing instruments otherwise would be interpreted, may be imported into interpretation of corporate financing instruments in derogation of the norm of literalism.

D. Nature of the Transactions; Creation of Potentially Relevant Evidence of Intent

The dollar amounts at issue in these transactions are large. The transactions also create relationships that can last decades, sometimes occasionally longer.\(^{66}\) Consequently, the documents governing these relationships are lengthy, detailed and complex. That complexity results in more interpretive issues being raised.

\(^{64}\) See, e.g. William H. Byrnes & Jason A. Fiske, Mertens Law of Federal Income Taxation § 26:11 (Westlaw through July 2013) (providing section titled, “Sham Transactions and Transactions Lacking Economic Substance”); James S. Eustice & Thomas Brantley, Federal Income Taxation of Corporations and Shareholders ¶ 1.05[2][d] (Westlaw through 2013) (“In viewing a dynamic whole, the courts often say that an integrated transaction must not be broken into independent steps or conversely that the separate steps must be taken together in attaching tax consequences. The so-called step transaction doctrine is encountered most often in the taxation of corporations and shareholders, but its scope is much broader.”).

\(^{65}\) See infra notes 143-150 and accompanying text.

Modernly, reference often is made to the parties’ evident purposes in contract interpretation.\(^67\) The complexity of the transactions may make the purposes less patent. It appears that, when the evident purposes cannot be ascertained, a court interpreting a contract is more likely to retreat into reliance on literalism and obscure rules of syntax. Thus, that kind of retreat is more likely in construction of these instruments.

A large dollar amount also provides a greater incentive to try to evade these contractual promises. In a transaction involving small dollar amounts, transaction costs may make it infeasible for a promisor to engage in complicated transactions designed to evade contractual promises. However, where the dollar amount is large, as in corporate financing contracts, the transaction costs may be relatively small, in comparison to the benefits to be realized. Hence, the large dollar amount can increase the likelihood that creative actions to evade contractual promises are proposed and ultimately litigated.

As discussed above,\(^68\) the process of consummating these transactions often involves the creation of documents, such as prospectuses or offering memoranda, that describe the negotiated contracts. There also may be press releases as well as documents prepared by investment banks for internal distribution that describe the terms of the transaction so that investment bank personnel can prepare for marketing efforts or communications with ratings agencies.\(^69\) This atypical creation of documents memorializing contemporaneously the understanding of the instruments, only some of which are available to the ultimate parties to the instruments, presents issues as to the scope of material to be considered in interpreting the instruments. As will be seen, a number of cases seem to evince an idiosyncratic bias against reference to this type of extrinsic evidence in subsequent litigation.\(^70\)

### III. Consistency and Deviation from Norms in Interpretative Approaches to Construction of Corporate Financing Instruments

One can identify competing paradigms of contract interpretation that emphasize the language used: one that emphasizes literalism and another that

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\(^67\) See, e.g., infra 80 and accompanying text.

\(^68\) See supra note 50-51 and accompanying text.


\(^70\) See infra notes 183-189 and accompanying text.
seeks to give effect to the parties’ evident intent, as expressed in the language of the agreement, even if doing so does not result in the best literal interpretation (understanding, of course, courts can stray farther from the literal language by emphasizing other factors, such as trade practice). As this Part shows, although the extent to which one or the other is referenced may be different in interpreting corporate financing instruments, this variation is not accompanied by predictability. There remains great inconsistency and unpredictability as to which will be applied in interpreting corporate financing instruments.

Much of the language of nineteenth century authority emphasizes literalism in interpretation of contracts. For example:

- “Courts have power to enforce contracts, not to make them.”

- “This court is powerless to make a new contract, but its province is to construe and enforce the agreement made by the parties themselves.”

- “[T]o give [a contract] the construction claimed by the appellant, we must interpolate into the body of the contract words which the parties to it did not deem fit to incorporate. In other words, we must make a new contract for them. This clearly is not the province of a court. To construe contracts, not make new ones, is our duty.”

- “The intention of the parties is the pole-star of construction; but their intention must be found expressed in the contract and be consistent with rules of law. The courts will not make a new contract for the parties, nor will words be forced from their real signification.”

- “This court cannot interpolate what the contract does not contain.”

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71 Burbank v. Wood, 12 Haw. 591, 598 (1862).
73 Cheney v. Barber, 1 Colo. 256 260 (1871).
74 I John Bouvier, Law Dictionary 357 (1871).
75 Sheets v. Selden, 74 U.S. 416, 424 (1868).
This nineteenth century reasoning is echoed later in the twentieth century, such as in *Smith v. Stowell*,\(^76\) which, in interpreting option rights in stock quotes Corpus Juris Secundum to the following effect:

This from 17A C.J.S. Contracts § 296(3), pages 89-98 (1963), is also quite applicable here: “It is not within the province, function, duty, or power of the court to alter, revise, modify, extend, rewrite, or remake a contract by construction, or to make a new, or different, contract for the parties, whether in the guise of construction or otherwise; its duty is confined to the construction or interpretation of the one which they have made for themselves.

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The court may not rewrite the contract for the purpose of accomplishing that which, in its opinion, may appear proper, or, on general principles of abstract justice, or under the rule of liberal construction, make for the parties a contract which they did not make for themselves, or make for them a better contract than they chose, or saw fit, to make for themselves, or remake a contract, under the guise of construction, because it later appears that a different agreement should have been consummated in the first instance, or in order to meet special circumstances or contingencies against which the parties have not protected themselves.

Likewise, the court may not alter a contract for the benefit of one party and to the detriment of the other or others, or make a new contract at the instance of one of the parties, or, by a process of interpretation, relieve one of the parties from the terms to which he voluntarily consented, or, because of equitable considerations, obviate objections which might have been foreseen and guarded against, . . .”\(^77\)

One may describe continued adherence to this interpretative approach as *vestigial literalism*. That approach may be contrasted with more modern statements such as the following from the Restatement (Second) of Contracts: “Words and other conduct are interpreted in the light of all the circumstances, and if the

\(^76\) 125 N.W.2d 795 (Iowa 1964).

\(^77\) *Id.* at 799 n.4.
principal purpose of the parties is ascertainable it is given great weight.\textsuperscript{78} \textit{American General Corp. v. Continental Airlines Corp.}\textsuperscript{79} provides a more detailed articulation of a modern approach emphasizing the purposes manifested by the language used. In a case construing anti-dilution and anti-destruction provisions in warrants, the Delaware Chancery Court noted that:

Despite the existence of separate parts, a contract is to be considered as a whole and its meaning gathered from the entire context, and not from particular words, phrases or clauses, or from detached or isolated portions of the contract. In order to determine the meaning of each part, the entire agreement must be considered. Thus, a “meaning which arises from a particular portion of an agreement cannot control the meaning of the entire agreement where such inference runs counter to the agreement’s overall scheme or plan.”\textsuperscript{80}

Thus, in some contexts, courts apply the more modern principles in interpreting corporate financing agreements. However, vestigial literalism at times prevails as the method of interpretation,\textsuperscript{81} sometimes by virtue of enhanced deference to precedents, and at other times apparently because the evident purposes underlying the pertinent contractual provisions are sufficiently complex that they cannot be recognized, resulting in retreat to literalism. In addition, as Part IV shows, certain technical interpretive principles are applied idiosyncratically to corporate financing instruments.

\textsuperscript{78} \textit{Restatement (Second) of Contracts} § 202(1) (1981).


\textsuperscript{80} \textit{Id.} at *4 (citations omitted) (quoting \textit{E.I. duPont de Nemours & Co., Inc. v. Shell Oil Co.}, 498 A.2d 1108, 1113 (Del. 1985)). \textit{Accord Empire Props. Corp. v. Mfrs. Trust Co.}, 43 N.E.2d 25, 28 (N.Y. 1942) (“The meaning of a writing may be distorted where undue force is given to single words or phrases. We read the writing as a whole. We seek to give to each clause its intended purpose in the promotion of the primary and dominant purpose of the contract.”).

\textsuperscript{81} \textit{See generally} \textit{Speiser v. Baker}, 525 A.2d 1001, 1008 n. 5 (Del. Ch. 1987) (“Some commentators have thought some of the case law of this state unduly literal. For example, Professor Buxbaum has referred to \textit{Providence & Worcester Co. v. Baker}, Del.Supr., 378 A.2d 121 (1977) as: “an opinion startling in its literalness even for Delaware.” Buxbaum, \textit{The Internal Division of Powers in Corporate Governance}, 73 Calif.L.Rev. 1671, 1694 (1985).”)}
A. Conventional Statement in Construction of Corporate Financing Instruments of Good Faith or Conventional Focus on Purpose

The modern doctrine of contract interpretation may give effect to an agreement’s evident purposes, and thus deemphasizes literalism, by express reference to purposes or by reference to the implied covenant of good faith and fair dealing, which builds on the parties’ evident purposes. Although modern authority construing the implied covenant of good faith in the context of corporate financing transactions sometimes applies the principles in ways inconsistent with contemporary approaches, the statements of the principles themselves are often consistent with contemporary doctrine. For example, one of the better-known cases construing the implied covenant of good faith as applied to corporate financing instruments, *Metropolitan Life Insurance Co. v. RJR Nabisco, Inc.*, 82 restates the pertinent principles in at least four separate ways, albeit each generally consistent with contemporary statements in other areas:

1. “A plaintiff always can allege a violation of an express covenant. If there has been such a violation, of course, the court need not reach the question of whether or not an implied covenant has been violated. That inquiry surfaces where, while the express terms may not have been technically breached, one party has nonetheless effectively deprived the other of those express, explicitly bargained-for benefits. In such a case, a court will read an implied covenant of good faith and fair dealing into a contract to ensure that neither party deprives the other of ‘the fruits of the agreement.’”83

2. “[T]he implied covenant will only aid and further the explicit terms of the agreement and will never impose an obligation ‘which would be inconsistent with other terms of the contractual relationship.’”84

3. “Viewed another way, the implied covenant of good faith is breached only when one party seeks to prevent the contract’s performance or to withhold its benefits. As a result, it thus

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83 *Id.* at 1516-17 (emphasis in original).
84 *Id.* at 1517 (quoting Sabetay v. Sterling Drug, Inc., 506 N.E.2d 919, 922 (N.Y. 1987)).
ensures that parties to a contract perform the substantive, bargained-for terms of their agreement."

4. “[A] promise by the defendant should be implied only if the court may rightfully assume that the parties would have included it in their written agreement had their attention been called to it . . . .”

The articulation of the principles governing the implied covenant of good faith and fair dealing in a number of other cases construing corporate financing instruments is similarly conventional.

Although some authority relied upon by Metropolitan Life involves corporate transactions, other authority the court relies upon addresses contracts or contexts not implicating the law of corporate finance or corporate law, e.g., construction of a sublease, an employment relationship, and covenants

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85 Id. at 1517 (citation omitted).

86 Id. at 1521 (quoting Neuman v. Pike, 591 F.2d 191, 195 (2d Cir. 1979)).

87 E.g., Hartford Fire Ins. Co. v. Federated Dept. Stores, Inc., 723 F. Supp. 976, 991 (S.D.N.Y. 1989) (“This implied covenant means that ‘neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract.’” (quoting Van Gemert v. Boeing Co., 520 F.2d 1373, 1383-85 (2d Cir. 1975)); In re Sunstates Corp. S’holder Litig., 788 A.2d 530, 535 (Del. Ch. 2001) (“[T]he duty [arising from the implied covenant] arises only where it is clear from what the parties expressly agreed, that they would have proscribed the challenged conduct as a breach of contract . . . had they thought to negotiate with respect to the matter.” (quoting Dave Greytak Enters., Inc. v. Mazda Motors of Am., Inc., 622 A.2d 14, 22-23 (Del. Ch.), aff’d, 609 A.2d 668 (Del. 1992)) (emphasis added in Sunstates)); Lohnes v. Level 3 Commc’ns, Inc., 272 F.3d 49, 61 (1st Cir. 2001) (“This implied covenant forbids a party from doing ‘anything which will have the effect of destroying or injuring the rights of the other party to receive the fruits of the contract.’” (quoting Druker v. Roland Wm. Jutras Assoc., 348 N.E.2d 763, 765 (Mass. 1976))). See generally Tauke, supra note 4, at 131 (“In refusing to create substantive protections for bondholders under the implied covenant of good faith the courts certainly seem to be justified.”).

88 See Neuman v. Pike, 591 F.2d 191 (2d Cir. 1979) (agreement governing management of close corporation) (statement (4)).


governing real estate development. So, in articulating standards, the opinion is not constrained to authority construing corporate financing instruments.

1. Outcome in *Metropolitan Life* consistent with modern principles

The actual outcome in *Metropolitan Life* does not seem idiosyncratic in applying principles of good faith. Peculiar facts militated against the creation of an implied duty under any standard. The case included a claim that an issuer’s incurrence of additional debt, as part of a leveraged buy-out, violated the implied covenant of good faith. The court held a prohibition on incurring additional indebtedness was not implied.

The claims involved six classes of debt securities. Two of the classes had originally “restricted the company’s ability to incur precisely the sort of debt involved in the recent LBO.” The limits on indebtedness were eliminated in exchange for various changes the holder then thought desirable, in one case receipt of a parent guaranty and in the other providing an indenture that would facilitate public resale of the debt.

The court rightly noted that the incongruity of finding an implied limit on the issuer’s incurrence of indebtedness “where, as here, that very term—a limitation on the incurrence of additional debt—has in other past contexts been expressly bargained for. . . .” And the opinion, in language that is easily elided, indicated this peculiar context may be outcome-determinative:

> It is not necessary to decide that indentures like those at issue could never support a finding of additional benefits, under different circumstances with different parties. Rather, for present purposes, it is sufficient to conclude what obligation is *not* covered, either explicitly or

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93 Metro. Life Ins., 716 F. Supp. at 1510.

94 Id.

95 Id.

96 Id. at 1519.
implicitly, by these contracts held by these plaintiffs.\footnote{Id. (emphasis in original). Some dissonance is created by this part of the opinion. The court elsewhere quoted with approval, \textit{Sharon Steel Corp. v. Chase Manhattan Bank}, 691 F.2d 1039, 1048 (2d Cir. 1982), as supporting the proposition that indenture covenants “do not depend upon particularized intentions of the parties to an indenture” and there are “no adjudicative facts relating to the parties.” \textit{Metrop. Life Ins.}, 716 F. Supp. at 1515. The quoted language would indicate particularized intentions are relevant.}

It bears mention that the outcome modernly often is referenced without limiting its application to circumstances where the bonds being interpreted had previously been amended to eliminate covenants inhibiting refinancing.\footnote{\textit{See In re Loral Space & Commc’ns Inc. Consol. Litig.}, Nos. 2808-VCS, 3022-VCS, 2008 WL 4293781, at *36 n.190 (Del. Ch. Sept. 19, 2008). \textit{Loral} quoted a textbook to the following effect: “Metropolitan sued [RJR] arguing that [its pre-LBO] bonds contained an \textit{implied} covenant preventing major financing changes that would undercut existing bondholders. However, Metropolitan lost: The courts held that \textit{only the written covenants count.}” \textit{Id.} (quoting \textit{RICHARD A. BREALEY \& STEWART C. MYERS, PRINCIPLES OF CORPORATE FINANCE} 713 (7th ed. 2003)) (first and second emphases in \textit{Loral}; first emphasis in textbook). \textit{Loral} further noted, “Although that conclusion may be too simplified from a legal perspective, its general point is useful for understanding the view on implied covenants in the financial community.” 2008 WL 4293781, at *36 n.190. There are additional illustrations of discussions attributing to \textit{Metropolitan Life} a holding lacking nuance. \textit{E.g.}, Jonathan Friedland et al., \textit{The Dealmaker’s Guide to Buying Distressed Assets—Section 363 Sales and the Alternatives}, in \textit{NORTON’S ANNUAL SURVEY OF BANKRUPTCY LAW}, 183 n.15 (2008) (“\textit{Metropolitan Life Ins. Co. v. RJR Nabisco, Inc.}, 716 F. Supp. 1504 (S.D. N.Y. 1989) (explaining that corporation was entitled to incur new debt in order to complete LBO, and bondholders had no basis for recovery absent a term in the indenture limiting such action)’’); Thomas O. McGimpsey \& Darren R. Hensley, \textit{Successor Obligor Clauses: Transferring “All or Substantially All” Corporate Assets in Spin-Off Transactions}, \textit{COLO. L. REV.}, 45, 48 (Feb. 2001) (discussing the case without emphasizing this aspect of the circumstances); F. John Stark, III, et al., \textit{Marriott Risk}: \textit{A New Model Covenant to Restrict Transfers of Wealth from Bondholders to Stockholders}, 1994 \textit{COLUM. BUS. L. REV.} 503, 515 (“\textit{[T]he [Metropolitan Life] court sent a message to the investment world—bondholders must negotiate sound restrictive covenants, because courts will not imply covenants that are not bargained for.”).}

We shall see other illustrations of “abstraction,” where courts treat interpretation of corporate financing instruments as involving principles to be applied divorced from the language or context giving rise to the initial authority.\footnote{\textit{See infra} Part IV.B.}

The context of the dispute in \textit{Metropolitan Life} is compelling for excluding an implied duty. The case thus does not present an opportunity for illuminating any difference in application of the standard in corporate financing transactions.
A number of cases apply modern interpretive principles in construction of corporate financing instruments, although they do not consistently do so. The circumstances where courts apply these modern interpretive principles to corporate financing agreements seem typically to include: (i) cases where the interpretive question was not previously addressed (i.e., not addressed when courts were generally more inclined to follow literalism); and (ii) circumstances not involving some selected recognized and disapproved forms of evasion of contractual rights. We may first turn to cases applying modern interpretive principles.

2. Sale of participation

Empresas Cablevisión, S.A.B. de C.V. v. JPMorgan Chase Bank involved a loan agreement, ninety percent of which the lender, JPMorgan, sought to assign to a firm, Inbursa, which was controlled by the borrower’s competitor. The loan agreement required the borrower’s, Cablevisión, consent for any assignment, which the borrower did not provide. The lender sought to evade the consent requirement by merely selling that firm a participation in the loan, with terms granting the buyer of the participation atypical access to information. The court, on a motion for preliminary injunction, found a likelihood of success on the merits on a claim that the acts would violate the implied covenant of good faith, noting:

> [E]very contract “embraces a pledge that ‘neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract.’” The facts presently before the Court make out a very strong showing that JPMorgan, after failing to obtain Cablevisión’s consent to an assignment of

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101 680 F. Supp. 2d 625 (S.D.N.Y. 2010), modified, 381 F. App’x 117 (2d Cir. 2010).

102 Francis D. Logan et al., The Securitization of U.S. Bank Activities in the Eurodollar Market—Issues for U.S. Counsel, 11 N.C. J. INT’L L. & COM. REG. 539, 544-45 (1986), describes a loan participation as follows: “In a loan participation the lender originates the loan, then ‘sells’ a share to another entity without recourse. . . By acquiring a participation, the participant becomes entitled to receive a specified portion of the borrower’s principal and interest payments on the participated loan, but only if and when the seller qua lender receives the payments from the borrower.”
90% of the loan to Inbursa, negotiated an agreement with Inbursa that, while it took the form of a participation, gave Inbursa much of the substance of the forbidden assignment and purposely undercut what JPMorgan knew the assignment veto was designed to prevent. Such an end-run, if not a downright sham, is not permissible if, as here, it does away with the “fruits” of the contract.  

3. Subordination

Modern judicial interpretation of subordination provisions de-emphasize literalism. A subordination provision is one in which certain creditors agree that they will be paid only after another class of creditors is paid. These provisions can be very complicated, because they may address not only distributions in liquidation but also complicated distributions in connection with reorganizations.

In re Envirodyne Industries, Inc., involves one of those complicated circumstances, where a plan of reorganization for an issuer provided for distribution of stock evidently in cancelation of certain existing senior and subordinated indebtedness. The business deal underlying subordination is that, if the senior indebtedness is not to be paid in full, e.g. in liquidation, junior indebtedness is to receive nothing. However, holders of the subordinated indebtedness in this case claimed, based on a literal reading of the subordination provisions, that they were entitled to a proportionate share of the distribution of stock.

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104 29 F.3d 301, 303 (7th Cir. 1994). The opinion describes the payment as “partial.” Review of the lower court opinion confirms “partial” was not used to mean the senior creditors retained their claims (unaltered) for senior debt and received these distributions in lieu of some of the payments then due on them. Rather, the senior claims were extinguished in exchange for receipt of the common stock. See In re Envirodyne Indus., Inc., 161 B.R. 440, 443-44 (Bankr. N.D. Ill. 1993), aff’d, 29 F.3d 301.

105 In re Envirodyne, 29 F.3d at 303, 306. The opinion further recites:

That indenture provided that in the event of a default, “all Superior Indebtedness” . . . “shall first be paid in full before the Noteholders, or the
The court rejected the claim and implemented the basic purpose of the subordination—not allowing the appellant junior creditors to receive distributions pro rata—although noting the junior creditors perhaps had the better of the argument as to the literal reading of the provisions: “On balance the appellants have the better of the purely semantic argument. But their interpretation makes no sense once the context of the terminology being interpreted is restored.”

These subordination provisions are complicated to draft. The Envirodyne approach is followed in In re Dura Automotive Systems, Inc., where the court settles on a similar outcome, albeit one where the court has to interpret similarly unclear language. That is not to say that all interpretations of subordination provisions are thoughtful and give effect to the evident intent of the parties.

Trustee, shall be entitled to retain any assets (other than shares of stock of the Company, as reorganized or readjusted or securities of the Company or any other corporation provided for by a plan of reorganization or readjustment, the payment of which is subordinated, at least to the same extent as the Notes, to the payment of all Superior Indebtedness which may at the time be outstanding).”

Id. at 303.

106 Id. at 305.

107 379 B.R. 257, 268 (Bankr. D. Del. 2007) (“Despite an invitation extended by this Court at oral argument, neither [party] would acknowledge that the X-Clause at issue here was poorly drafted. However, like the x-clause in Envirodyne, the X-Clause here, while not legally ambiguous, lacks the utter clarity that BNY and the Debtor would now surely prefer. But, like the Envirodyne courts, in interpreting the contract language before me, I will: ‘read the contract as a whole and consider all parts of the whole and not give undue force to certain words or phrases that would distort or confuse the primary and dominant purpose of the contract.’” (emphasis in original)).

This case also is one of the most express in stating that idiosyncratic principles govern interpretation of corporate financing instruments, in stretching the meaning of “unambiguous” to retain interpretation of the contract as a function for the court. See, e.g., id. at 270 (“[T]he Metromedia court called the x-clause before it ‘not self-reading; the applicability of the clause in a specific case is not readily apparent . . . .’ The only thing missing here is actual use of the word ‘ambiguous.’”). Treating the language as ambiguous, and allowing a jury to interpret it, is understood as undesirable. See supra text accompanying note 29. See also Bratton, supra note 4, at 402 (“Jury participation makes the interpretation process less certain.”).

108 JPMorgan Chase Bank v. Baupost Grp., LLC (In re Enron Creditors Recovery Corp.), 380 B.R. 307, 315-16, 319 (S.D.N.Y. 2008), interpreted a definition of senior debt, which included the phrase “all indebtedness of [Enron] . . . evidenced by notes, debentures, bonds or other securities sold by [Enron] for money borrowed . . . .” The court, referencing the “rule of the last antecedent,” held that the qualifier “sold . . . for money borrowed” does not limit the reference to “notes, debentures, [or] bonds.” Id. This approach is simply foolish. The reason the definition of senior debt references obligations for“money borrowed” is that only creditors of the type that provide a better business deal by virtue of being senior are to be given senior status.
4. No-action and no-recourse provisions

Indentures often contain so-called no-action provisions and no-recourse provisions. There are a number of purpose-focused interpretations of no-action and no-recourse provisions, and provisions granting a trustee the power to pursue claims on behalf of bondholders.

Under a no-action provision, individual bondholders cannot initiate certain lawsuits. For publicly issued bonds, the provision cannot limit lawsuits for scheduled principal or, with exceptions not normally present, interest. But the provisions will address, for example, breach of a financial covenant. They will require that if bondholders wish to pursue a covered claim, they must hold a specified amount of the bonds and first unsuccessfully request that the trustee bring suit. The point is to have such claims brought on behalf of all bondholders to avoid inconsistent judicial determinations, strike suits and the like.

An indenture will also have a complementary provision granting the trustee the right to maintain claims on behalf of the bondholders. These two provisions need to be construed in harmony with each other. It is obviously problematic if the bondholders cannot directly bring a claim and the trustee also has not been given the authority to bring the claim on behalf of bondholders. Such a gap would indirectly eliminate liability for certain causes of action.

A no-recourse provision limits the extent to which claims may be brought against persons other than the primary obligor, i.e., the issuer. The precise details vary among contracts, including the extent to which they purport to bar pursuit of claims other than breach of contract.

In interpreting these provisions, a thoughtful court will consider the interaction between the two and will conform its interpretation to avoid the implicit elimination of liability, i.e., reference the evident purpose. *U.S. Bank National Ass’n v. U.S. Timberlands Klamath Falls, L.L.C.* presents another illustration of a court giving effect to evident purposes, in this case also expressly declining to follow precedent.

109 See generally Kahan, supra note 34, at 1050-51 (discussing scope of these provisions).


The court noted no-action provisions substantially the same as those included in the indenture in question had been construed in Delaware as barring noteholders from bringing non-contractual claims without satisfying the demand requirement of the no-action clause.\textsuperscript{113} The court identified a preference for deference to prior interpretations of corporate financing instruments from other jurisdictions. It concluded, however, that it could not, because that would produce “absurd” results.\textsuperscript{114}

A number of other courts also avoided literal construction of no-action provisions, allowing securityholders to bring claims literally barred by the contract provisions where the trustee had a conflict of interest\textsuperscript{115} or otherwise unreasonably refused to bring a claim,\textsuperscript{116} although there is some other, curiously putatively literal, construction of these provisions.\textsuperscript{117}

\textsuperscript{113} Id. at 940.

\textsuperscript{114} Id. at 942 (“While this court is reluctant to interpret the provisions of a trust indenture differently from another court interpreting substantially the same provision, to do otherwise would require the court either to drastically restrict the scope of the no-action clause, as interpreted in prior decisions of this court, or render the operation of that clause absurd.”). The absurd outcome the court rejects is one Kahan references as potentially present and problematic. Kahan, supra note 34, at 1074. Of course, that this well-known commentator identifies this as a problem, suggesting it will not be adequately addressed in interpretation, evidences the lack of predictability of the law in this area.


\textsuperscript{116} Birn v. Childs Co., 37 N.Y.S.2d 689, 697 (Sup. Ct. 1942) (holding that an unreasonable refusal of trustee to sue excused compliance with no-action provision, where the plaintiff held bearer bonds, making it difficult to locate the required percentage of bonds). See also Ettlinger v. Schumacher., 36 N.E. 1055 (N.Y. 1894) (allowing lawsuit where the trustee was absent from the country and probably insane). There have long been provisions limiting direct action by bondholders. See Seibert v. Minneapolis & St. Louis Ry. Co., 53 N.W. 1134, 1136 (Minn. 1893) (discussing such a provision).


\begin{quote}
[N]o Holder of any Note shall have any right by virtue of or by availing of any provision of this Indenture to institute any suit, action or proceeding in equity or at law upon or under or with respect to this Indenture, or for the appointment of a receiver, . . . or for any other remedy hereunder, unless [certain pre-suit requirements are met].
\end{quote}
Id. at *5. The court held those claims were barred, an outcome that it described as consistent with prior authority, Noble v. European Mortg. & Inv. Corp., 165 A. 157 (Del. Ch. 1933), which held a no-action clause did not preclude a receivership action because the contract provided:

Nothing in this Section or elsewhere in this indenture . . . shall affect or impair the obligation of the Company, which is unconditional and absolute, to pay the principal and interest of the bonds . . . nor affect or impair the right of action, which is also absolute and unconditional, of such holders to enforce such payment.

Id. at 158. Tang Capital Partners indicated that the Noble indenture “reserved to plaintiffs the right to commence actions relating broadly to payment of amounts owed,” and, as to the indenture in Tang Capital Partners, “[n]either does the Indenture here contain such a reservation.” 2012 WL 3072347 at *7. The following language was incorporated by reference into the Tang Capital Partners indenture:

[T]he right of any holder of any indenture security to receive payment of the principal of and interest on such indenture security, on or after the respective due dates expressed in such indenture security, or to institute suit for the enforcement of any such payment on or after such respective dates, shall not be impaired or affected without the consent of such holder . . . .

15 U.S.C. § 77ppp; see also Savient Pharmaceuticals, Prospectus re. $200,000,000 4.75% Convertible Senior Notes due 2018, at 49 (Feb. 1, 2011) (referencing incorporation of terms set forth in the Trust Indenture Act of 1939). When one has to compare dense language like this, the way to proceed is to reduce the language into its components. Simplifying the language from Tang Capital Partners results in the following:

[T]he right of any holder to receive payment of the principal of and interest, or to institute suit for the enforcement of any such payment on or after such respective dates, shall not be impaired . . . .

Further simplification yields:

[T]he right of any holder … to institute suit for the enforcement of any such payment [of principal or interest] on or after such respective dates, shall not be impaired . . . .

It is not clear to this author how that language differs materially from language in the Noble indenture, which the court found a basis for a different conclusion:

Nothing in … this indenture … shall affect or impair … the right of action, which is also absolute and unconditional, of such holders to enforce such payment.

165 A. at 158. Is “the right to institute suit for the enforcement of any such payment” different in meaning from “the right of action to enforce such payment?”

The Tang Capital Partners court also referenced the unhelpful bromide supporting avoidance of constructions resulting in surplusage. 2012 WL 3072347, at *8.
Feldbaum v. McCrory Corp.\textsuperscript{118} also provides an interpretation of a no-action provision that de-emphasizes literalism. The agreement limited the ability of a securityholder to “pursue any remedy with respect to this Indenture or the Securities.”\textsuperscript{119} The court held this prohibition extended, inter alia, to limit claims alleging (i) fraudulent conveyance of assets (generally addressing claims a creditor transferred assets without having received equivalent value in exchange)\textsuperscript{120} and (ii) fraud arising from an allegedly false statement made by the issuer and its affiliates after the bonds had been issued, allegedly causing bondholders not to sell their bonds and not to sue to enjoin certain allegedly improper transactions.\textsuperscript{121}

It is not clear that either of these claims was “with respect to” the indenture or the securities. Each arose out of prohibitions outside the promises made in the indenture and the securities—fraudulent conveyance law or common law fraud. The court reached the conclusion that the no-action provision limited initiation of these claims by securityholders based on the court’s perception as to the purposes of the provision—limiting bondholders bringing claims individually when the “trustee is capable of satisfying its obligations” and the trustee can enforce the claim “on behalf of all bonds.”\textsuperscript{122}

The court further referenced a “policy favoring the channeling of bondholder suits through trustees” as a basis for concluding that the no-action provisions extended to limit claims brought against persons not parties to the indenture, stating, “So long as the suits to be dismissed seek to enforce rights shared ratably by all bondholders, they should be prosecuted by the trustee.”\textsuperscript{123}

\begin{footnotes}
\item[118] Nos. 11866, 11920, 12006, 1992 WL 119095 (Del. Ch. June 1, 1992).
\item[119] Id. at *5.
\item[120] See generally, e.g., Jonathan C. Lipson, First Principles and Fair Consideration: The Developing Clash Between the First Amendment and the Constructive Fraudulent Conveyance Laws, 52 U. MIAMI L. REV. 247 (1997) (discussing the principles).
\item[121] Id. at 251.
\item[122] Feldbaum, 1992 WL 119095 at *6 (“Given the purposes for which no-action clauses are designed, I cannot accept plaintiffs’ position. No principled reason or factual particularity of this case is advanced that would justify this view. In my opinion, no matter what legal theory a plaintiff advances, if the trustee is capable of satisfying its obligations, then any claim that can be enforced by the trustee on behalf of all bonds, other than a claim for the recovery of past due interest or principle [sic], is subject to the terms of a no-action clause of this type.”).
\item[123] Id. at *6 (also claiming literal support from the language of the provision, asserting “Moreover, like other no-action clauses, the clauses at issue here explicitly make their scope depend on the nature of the claims brought, not on the identity of the defendant.”).
\end{footnotes}
Very similar contract language is construed inconsistently—not requiring channeling of claims through the trustee—in *LaSalle National Bank v. Perelman*. The court described the contract as including “no recourse provisions [that] exempt directors, officers and stockholders from liability ‘for any obligations of the Company or the Trustee under the Securities or the Indenture or for any claim based on, in respect of or by reason of such obligation or their creation.’” The court held that this provision did not bar assertion of claims of veil piercing and that dividends constituted wrongful transfers, among other claims. It somewhat directly eschewed seeking to tie the outcome to the language of the provision. Instead, the court cited other authority for the proposition “that the Geyer [v. Ingersoll Publications Co.] court did not rely on the word ‘hereunder’ or any specific language of the provision in limiting the provision to contract claims. Instead, the Chancery Court generally held that no recourse provisions are limited to contract claims . . . .”

So, for some purposes, claims that allege actions defraud creditors pursue remedies “with respect to” an indenture or the securities (Feldbaum), but, in other circumstances, claims that allege actions defrauding creditors do not pursue remedies “under the Securities or the Indenture or for any claim based on, in respect of or by reason of such obligation” (LaSalle). We shall see other circumstances in which courts treat contractual provisions in corporate financing instruments as concepts merely suggested by, and not controlled by, the actual language of the provisions.

5. Recognized schemes for evasion of contractual obligations

Courts have identified certain categories of prohibited acts issuers can take to avoid promises in corporate financing instruments. So, if the issuer’s acts can be placed in one of these categories, there is a significantly greater likelihood that actions allegedly literally permitted will be treated as violating the pertinent

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125 Id. at 459.
126 Id. at 457, 462-63.
127 Id. at 461 (citing Geyer v. Ingersoll Pub’ns Co., 621 A.2d 784 (Del. Ch. 1992)). *See also* Howe v. Bank of N.Y. Mellon, 783 F. Supp. 2d 466, 473-74 (S.D.N.Y. 2011) (noting that indenture provision limiting lawsuits “with respect to this Indenture, or for any other remedy hereunder” does not limit claim brought against trustee alleging breach of fiduciary duty or taking “extra-contractual action”).
128 *See infra* Part IV.B.
agreement, although this categorization is not necessarily sufficient. The primary categories include an invasion of contractual provisions by dividing an act into multiple steps (step-transaction) and acting through a subsidiary.\(^{129}\) In addition, if the acts are amenable to characterization as a “sham,” the acts may be found to be prohibited.

These principles are primarily used in connection with other circumstances, such as ascertaining compliance with tax law (step transaction)\(^{130}\) or determining whether the corporate veil should be pierced for creditors generally (not respecting the corporate form, which is at the heart of extending promises to bind subsidiaries of a promisor). It may be the fact that deviation from literalism has been recognized in contexts outside interpretation of contracts gives additional, necessary impetus to a desire to extend non-literal contractual interpretation to various aspects of corporate financing contracts.

**Step transaction.** A number of cases have addressed dividing acts into multiple steps in connection with reviewing consideration receivable upon exercise of warrants following an issuer’s merger. *Noddings Investment Group, Inc. v. Capstar Communications, Inc.*\(^{131}\) involved an issuer of stock purchase warrants that spun-off shares of a subsidiary followed by a cash-out merger. The warrants did not contain express adjustment provisions for a spin-off,\(^{132}\) though they did for a merger.\(^{133}\) The court concluded, as a matter of law, that the two steps were to be integrated (not respected as separate transactions), so that warrants, following the merger, were to be exercisable for both the spun-off shares and the cash consideration delivered in the merger.\(^{134}\) There is other, similar authority in one case that concerned a cash dividend paid before a merger,\(^{135}\) and in another case

\(^{129}\) Buxbaum’s 1954 article notes the problem. Richard M. Buxbaum, *Preferred Stock—Law and Draftsmanship*, 42 CALIF. L. REV. 243, 257 (1954) (“As to all these clauses, it is vital that all payments, distributions, acquisitions, etc., include those of subsidiaries; otherwise the provisions can be totally avoided.”).

\(^{130}\) See supra note 64.

\(^{131}\) No. 16538, 1999 WL 182568 (Del. Ch. Mar. 24, 1999).

\(^{132}\) Id. at *1.

\(^{133}\) Id. at *3 n.12.

\(^{134}\) Id. at *6-7 (referencing principles of the “step transaction doctrine” principles followed in tax law).

that involved certain supplemental rights given to employee stockholders in connection with a merger.\textsuperscript{136}

\textit{In re Associated Gas \& Elec. Co.}\textsuperscript{137} followed a similar approach in construing a successor liability provision. The court, reviewing a special master’s report, opined as to a covenant requiring a firm that acquires all the issuer’s assets assume the issuer’s debt obligations “that a trial court would be justified in viewing these separate transactions as parts of a single scheme.”\textsuperscript{138}

\textit{Alleco, Inc. v. IBJ Schroder Bank \& Trust Co.}\textsuperscript{139} similarly recharacterized multiple steps, in that case in connection with interpreting a covenant restricting dividends, as well as redemptions or repurchases of stock. The court held that a leveraged buy-out of an issuer, effected by a tender-offer, resulting in ownership of ninety-four percent of the issuer,\textsuperscript{140} followed by a merger, constitutes a dividend as restricted by a covenant in the target’s outstanding debt securities.\textsuperscript{141} In reaching this conclusion, the court focused on the economic substance of the transaction and the purpose of the covenant restricting dividends: “If sections like [this covenant] are to have any meaning, courts must consider the substance of the disputed transaction.”\textsuperscript{142}

\textit{Acting through a subsidiary.} An issuer may seek to avoid compliance with covenants by acting through a subsidiary. Authority is inconsistent as to whether

\begin{footnotesize}
\begin{enumerate}
\item 61 F. Supp. 11, 28 (S.D.N.Y. 1944), aff’d, 149 F.2d 996 (2d Cir. 1945).
\item Id. See also U.S. Bank N.A. v. Angeion Corp., 615 N.W.2d 425 (Minn. Ct. App. 2000) (discussing multiple transactions in reversing trial court’s grant of summary judgment in favor of issuer; plaintiff claimed that the transactions constituted sale of substantially all the issuer’s assets, triggering a repurchase option). Whether the transactions can be collapsed may depend on whether they were part of an overall plan or “discrete, context-based decisions.” \textit{But cf.} Bank of N.Y. Mellon Trust Co. v. Liberty Media Corp., 29 A.3d 225, 243-44 (Del. 2011) (affirming Chancery Court’s determination that multiple transactions were not sufficiently “connected” to warrant aggregating them in construing a successor obligor provision in an indenture; reserving determination whether New York would follow the step-transaction doctrine in construing successor obligor provisions). See generally Bank of N.Y. v. Tyco Int’l Grp., S.A., 545 F. Supp. 2d 312 (S.D.N.Y. 2008) (examining spin-off and successor clause). The analysis is something at odds with the principles underlying the Doctrine of Independent Legal Significance. See generally supra notes 59-63 and accompanying text.
\item 745 F. Supp. 1467 (D. Minn. 1989).
\item \textit{Alleco}, 745 F. Supp. at 1474-75.
\item Id. at 1475.
\end{enumerate}
\end{footnotesize}
acts of a subsidiary are treated as acts of the parent/issuer for purposes of corporate financing instruments.

The Delaware Chancery Court held in In re Sunstates Corp. Shareholder Litigation\(^{143}\) that a charter provision preventing an issuer’s purchasing stock does not prohibit purchases made by the issuer’s subsidiaries. The court expressly rejected finding that this violates the implied covenant of good faith and fair dealing.

Roeston OL, LLC \(v\). Dynegy Holdings Inc.\(^{144}\) addressed whether a limit on a corporation’s transfer of assets restricted asset transfers by subsidiaries. Roeston indicated “No.” The court found that a creditor was unlikely to succeed—and denied a temporary restraining order\(^{145}\)—in a claim that a covenant restricting transfer of a guarantor’s assets\(^{146}\) restricted transfers of assets by the guarantor’s subsidiaries. The plan involved contributing assets to newly-formed entities designed to be bankruptcy-remote and that could separately borrow,\(^{147}\) which would effectively (structurally)\(^{148}\) subordinate claims against the guarantor to those future creditors.

Yet courts are not consistent in treating acts of a subsidiary as acts of the parent for purposes of covenants. So, there is authority to the opposite effect of Roeston.\(^{149}\) And the court in Shenandoah Life Insurance Co. \(v\). Valero Energy Corp. indicated (in dicta) that an issuer would violate a restriction on refinancing with lower-rate debt by distributing assets to a subsidiary that borrowed money and distributed the funds to the parent/issuer.\(^{150}\)

\(^{143}\) 788 A.2d 530, 535 (Del. Ch. 2001).


\(^{145}\) Id. at *1.

\(^{146}\) The pertinent language is, “The Guarantor shall not consolidate with or merge into any other Person, or convey, transfer or lease its properties and assets substantially as an entirety to any Person in one or a series of transactions ….” Id. at *3.

\(^{147}\) See id. at *6.

\(^{148}\) Structural subordination refers to the fact that creditors of a parent corporation are, by virtue of the corporate structure, effectively subordinated to creditors of a subsidiary (to the extent of assets in the subsidiary). See Stark et al., supra note 98, at 517 n.52 (discussing structural subordination).


\(^{150}\) Shenandoah Life Ins. Co. \(v\). Valero Energy Corp., No. 9032, 1988 WL 63491, at *20-22 (Del. Ch. June 21, 1988). The court states that act would “likely be found to violate such an implied duty even if there were no ‘indirectly’ language in the restriction.” Id. at *8.
Sham. We have already encountered one case, Empresas Cablevisión, S.A.B. de C.V. v. JPMorgan Chase Bank,\textsuperscript{151} referencing categorization of a transaction as a “sham” as a basis for extending a promise beyond its literal terms.\textsuperscript{152} In addition, Birn v. Childs Co.\textsuperscript{153} supports the notion that effect will not be given to a sham designed to avoid promises in an indenture. It is common for an indenture to provide that an issuer can satisfy an obligation to redeem a portion of outstanding bonds (called a “sinking fund”) by purchasing the securities in the market and delivering the repurchased securities to the trustee for cancelation. The Birn court held that delivering to a trustee securities that had been authenticated but never issued could not be used to satisfy a sinking fund obligation.\textsuperscript{154}

6. Corresponding statutory language

These classes of transactions—transactions divided into multiple steps, actions taken by a subsidiary, and sham transactions—do not exhaust the circumstances where courts may take a non-literal approach in interpreting corporate financing instruments. Courts also exhibit greater flexibility in interpreting these provisions where the language in question is also used in a statute. For example, state corporation law will regulate a corporation’s payment of dividends (prohibiting their payment if resulting in the firm’s insolvency or the like).\textsuperscript{155} Repurchases of stock will also be regulated under state corporation law.\textsuperscript{156}

One gets the sense that the desire to retain discretion in construing the terms in the statutory context carries-over to interpreting the same terms when used in corporate financing agreements. Whether that is the reason, or whether there is some other, in corporate financing instruments these terms are construed less literally than other language. Dividends restricted by corporate financing instruments may be found to have been effected by:

\textsuperscript{151} 680 F. Supp. 2d 625 (S.D.N.Y.), modified, 381 F. App’x 117 (2d Cir. 2010). See supra notes 101-103 and accompanying text.

\textsuperscript{152} See supra notes 101-103 and accompanying text.

\textsuperscript{153} 37 N.Y.S.2d 689 (Sup. Ct. 1942).

\textsuperscript{154} Id. at 695.

\textsuperscript{155} See JAMES D. COX & THOMAS LEE HAZEN, 3 TREATISE ON THE LAW OF CORPORATIONS § 20:12 (Westlaw through Dec. 2012) (“Every state statutorily restricts the directors’ authority to make dividend distributions based on the corporation’s financial condition.”).

\textsuperscript{156} Id. at § 21:4 (discussing statutory restrictions on repurchases).
• A corporation’s cancelation of a tax-sharing agreement with its parent, thereby eliminating an obligation of the parent;\textsuperscript{157}

• A two-step leveraged buy-out taking the form of a tender offer followed by a merger;\textsuperscript{158}

• A corporation’s discharge of its parent’s obligation;\textsuperscript{159} and

• An extension of credit to a control person, used to acquire the issuer’s stock.\textsuperscript{160}

B. Inconsistency in Reference to Purposes

1. Anti-dilution and anti-destruction

Although some authority applies modern interpretive principles to corporate financing instruments in ways that are comparable to their application to other agreements, that is not universal. As discussed above, a number of cases treat corporate financing contracts and other agreements differently in determining whether an adjustment arising from a split or a reverse split of stock should be implied. \textit{Reiss v. Financial Performance Corp.},\textsuperscript{161} among other cases,\textsuperscript{162} held an adjustment should not be implied in a corporate financing instrument, whereas other authority not addressing corporate financing instruments found an

\textsuperscript{157} See FDIC v. First Heights Bank, 229 F.3d 528, 539 (6th Cir. 2000).


\textsuperscript{160} Pereira v. Cogan, 294 B.R. 449, 542 n.89 (S.D.N.Y. 2003) (holding that an extension of credit constituted a redemption for purposes of Delaware General Corporation Law § 160 and “likely” constituted a repurchase under a charter provision), \textit{vacated}, Pereira v. Farace, 413 F.3d 330 (2d Cir. 2005).


\textsuperscript{162} See Lohnes v. Level 3 Comm’cns, Inc., 272 F.3d 49, 55-61 (1st Cir. 2001) (no adjustment in warrant held by landlord for split effected as a stock dividend; warrant expressly provided for adjustments for “capital reorganization” or a “reclassification”); Smith v. Stowell, 125 N.W.2d 795, 798 (Iowa 1964) (no adjustment to options implied where the issuer effected a 4:1 split through a stock dividend).
adjustment implied, with *Cofman v. Acton Corp.* express expressly stating authority construing similar language in corporate financing instruments is inapposite.

Not all aspects of anti-dilution and anti-destruction provisions in corporate financing contracts are construed literally. *Fluor Corp. v. Citadel Equity Fund, Ltd.* provides an illustration in which a court addressed a defect in drafting, where a referenced security price was not properly defined. The case held, as a matter of law, that an indenture’s reference to the “closing sale price per share of the Common Stock,” in provisions addressing property deliverable on conversion of bonds, was to be adjusted for a 2:1 split, where the referenced price per share was after the common stock traded with a “due bill” for the additional

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163 958 F.2d 494 (1st Cir. 1992). A number of other cases not involving construction of corporation financing instruments reach an outcome similar to that in *Cofman*. The court in *In re Tamaron Investments, Inc.*, 637 N.Y.S.2d 637 (Sup. Ct. 1996), adjusted the terms of an arbitration award of shares of a corporation’s stock where the corporation effected a reverse split between the time of the arbitration hearing and the issuance of the award. *Id.* at 638-39 (“The only construction of the term ‘shares’ is one that conforms with what the parties and the arbitrator understood it to mean as of the close of evidence in March 1995. Since the arbitrator did not make a conscious, substantive decision to award 2000 shares of post-reverse split stock, any ambiguity engendered by the subsequent change in circumstances may be clarified or corrected by the court.”). *Smith v. Hilliard*, 408 S.W.2d 440, 442-43 (Ky. 1966), involved a customer’s agreement to sell 100 shares of NYSE-listed stock, made after a 2:1 split had been declared and before the stock was trading on the exchange ex-dividend. The exchange had issued a directive requiring persons selling stock would, when delivering their old certificates, need to deliver a “due bill” for the new shares (thereby conveying to the buyer the shares issued in the split). The customer had received a check reflecting the pre-split price, and under separate cover, a confirmation requiring delivery of the due bill. However, the customer had not delivered the due bill. Although the requirement that the customer send the due bill had not been discussed when she entered her sale order, the court found principles of unjust enrichment required her to do so, and affirmed summary judgment for the brokerage firm. *Watson v. Santalucia*, 427 S.E.2d 466, 470 (W. Va. 1993), involved construction of legacies of specified numbers of shares of stock, which the court adjusted where the issuer had declared a split a few months after the instrument had been executed and a month before the testator’s death. One can contrast *Watson* with authority from half a century earlier, *In re Fosdick’s Trust*, 152 N.E.2d 228 (N.Y. 1958) (applying a more formalistic approach).

164 760 F. Supp. 2d 685, 691-93 (N.D. Tex. 2010), *aff’d in part and vacated in part*, 413 F. App’x 756 (5th Cir. 2011).

165 *Fluor* provides an illustration that is grasped with relative ease. *See also In re Envirodyne Indus., Inc.*, 29 F.3d 301, 305 (7th Cir. 1994) (construing somewhat complex subordination provisions and stating, “On balance the appellants have the better of the purely semantic argument. But their interpretation makes no sense once the context of the terminology being interpreted is restored.”).

166 *Fluor Corp.*, 760 F. Supp. 2d at 688.
In reaching this conclusion, the *Fluor* court cited a conventional modern interpretative principle to subordinate a literal interpretation where appropriate to promote the evident purposes of the contract.\(^{168}\)

This outcome, although clearly reflecting the hypothetical bargain, creates substantial uncertainty where courts in other circumstances apply vestigial literalism. When the issue involves anti-dilution protection, not all corporate financing contracts will be construed literally. Even when the issue is restricted to the consequences of a split, in some cases the contract will be construed literally, and in others it will not, leaving an ill-defined dividing line.

2. **Notice**

An additional illustration of inconsistency involves notice requirements. The court in *Van Gemert v. Boeing Co.*\(^{169}\) held that an issuer cannot simply give the notice specified by contract, but is required to give additional notice where reasonably necessary to alert a securityholder.\(^{170}\) However, *Lorenz v. CSX Corp.* affirmed dismissal of a claim that an issuer was under an implied obligation to give notice of a spin-off, distinguishing *Van Gemert* on the basis that the earlier case involved merely making express notice more effective, whereas creation of a notice obligation was at-issue in *Lorenz*.\(^{171}\)

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\(^{167}\) Id.

\(^{168}\) *Id.* at 689 (citations omitted) (“A court must fairly and reasonably interpret the contract consistently with its intended purpose. However, what the parties intended is only relevant to the extent that such intentions are evidenced by the language of the contract.”). So far as this author is aware, the earliest case presenting this type of issue in stark detail is *Harcourt Brace Jovanovich, Inc. v. Sun Bank*, No. CI 87-3985 (Fla. Cir. Ct. Orange County June 25, 1987).

\(^{169}\) 520 F.2d 1373, 1383 (2d Cir. 1975).

\(^{170}\) *Id.*

\(^{171}\) *Lorenz v. CSX Corp.*, 1 F.3d 1406, 1416-17 (3d Cir. 1993) (affirming the trial court’s dismissal of debentureholder claims an issuer was under an implied obligation to give the debentureholders advance notice of a spin-off). In *Lorenz*, the issuer had transferred some assets to a subsidiary and, on the same day, declared a dividend spinning-off the subsidiary, to inhibit issuance of stock to debentureholders. The issuer sought to avoid issuance of stock to debentureholders, because it thought too many holders would impose additional burdens in connection with compliance with the registration requirements of the Securities Act of 1933. *Id.* at 1409. The court distinguished *Van Gemert* on the basis that finding a violation in *Lorenz* would require creating a new term (an obligation to provide notice), as opposed to merely making the expressly required notice effective. *Id.* at 1416-17. *See also* Lohnes v. Level 3 Commc’ns, Inc., 272 F.3d 49, 50-51, 55-62 (1st Cir. 2001) (holding an issuer was neither required to adjust a warrant for a 2:1 split effected as a stock dividend nor even to provide the warrantholder advance notice).
That distinction creates interpretative questions with unpredictable resolutions. For example, if notice is required for a reclassification of underlying stock, must it be given for a merger in which the underlying stock is converted? Would that be a question of creating a new notice (evidently not implied under *Lorenz*) or simply giving effect to the purposes of the express notice (perhaps implied under *Van Gemert*)? If notice is required of a merger, would it extend to the first step of a two-step recapitalization comprised of a very large dividend followed by a merger? The distinction created by *Lorenz* shifts the dividing line between implied duties and no implied duties, but it does not eliminate uncertainty as to the dividing line’s location.

3. Release of collateral

In *Rievman v. Burlington Northern Railroad Co.*, which involved two series of long-term, secured bonds, the court found that the bondholders had made an adequate showing of a likelihood of success on the merits to warrant issuance of a preliminary injunction restraining consummation of collateral substitution, even though the court referenced the bondholders as seeking merely to “hold-up” the transaction, reflecting what one might categorize as “bad faith.” The court seemed to ground its decision on a need to follow on-point precedent, and an increased need for certainty in interpreting corporate financing instruments. This result may be contrasted both with the Restatement (Third) of Property (Mortgages), which would treat the debtor more favorably—providing an opportunity to substitute collateral (albeit not precisely the collateral at issue in *Rievman*), and *Littlejohn v. Parrish*, holding the implied covenant of good faith


173 *Id.* at 602 (“Though not absolutely certain that plaintiffs would prevail on the merits at trial, the court is persuaded that plaintiffs have made a sufficient showing of the likelihood of success on the merits to warrant preliminary relief.”).

174 *Id.* at 594. Moreover, the railroad’s expert explained he could not issue a fairness opinion as to the terms of the offer, because he could not value the “hold-up” right. *Id.* at 597.

175 *Id.* at 601 (“In addition, at least one of the key cases relied on by plaintiffs cannot be effectively distinguished by the Railroad, and appears to govern this case. . . . The New York Court of Appeals seemed to be laying down a *per se* rule: because of the ‘vast sums invested in railroad bonds’ and the need to insure investor confidence, railroad mortgage trustees may not ‘sell, change, or in any manner compromise the security except as authorized in express terms or by necessary implication’—even where the sale or change would not harm the bondholders’ interests.”).

176 Restatement (Third) of Property (Mortgages) § 6.2 (1997).
limited an issuer’s actions when presented with a borrower’s offer to repay a secured loan.  

4. Impairing right to payment

The Trust Indenture Act provides that the

Right of any holder . . . to receive payment of the principal of and interest on such indenture security, on or after the respective due dates . . . or to institute suit for the enforcement of any such payment . . . shall not be impaired or affected without the consent of such holder.

Whether actions that decrease the likelihood of repayment are limited by this provision has received inconsistent treatment by courts.

Federated Strategic Income Fund v. Mechala Group Jamaica Ltd. addressed a distressed issuer’s work-out involving downstreaming assets and release of subsidiary guarantees, leaving the issuer as a company with nominal assets. The court found that the bondholders adequately established, for purposes of a motion seeking a preliminary injunction, that these acts would eliminate bondholders’ ability to recover. Although not expressly referencing the “purposes” of the provisions being impaired were these acts to be consummated, the court found a likelihood of success on the merits of a claim that the proposed acts violated the Trust Indenture Act and the indenture provisions implementing this statute.

Yet In re Northwestern Corp. followed an inconsistent approach. Securityholders formerly looked to payment from assets of a subsidiary. The court held that upstreaming the assets (described as “going flat,” a description of collapsing a hierarchical corporate structure), resulting in the reversal of structural subordination of parent obligations, did not violate this provision of the Trust Indenture Act. The court’s language rejected giving effect to language in a way that would further the securityholder’s “practical rights;” it stated this

181. Id. at 598.
provision “applies to the holder’s legal rights and not the holder’s practical rights to the principal and interest itself.”

C. Decreased Reference to the Parties’ Intent

Subpart A collects authority where courts emphasized purposes in construction of corporate financing instruments. Subpart B collects cases that reached inconsistent conclusions as to particular issues. Some other authority impedes reference to evidence of intended purposes underlying corporate financing instruments were a court inclined to give effect to those purpose.

As discussed above, certain aspects of the process by which corporate financing instruments are negotiated makes it more likely there will be available contemporaneous evidence of the parties’ intent. Some of that information is publicly available (prospectuses and news reporting), and other will be available to investors (a private placement memorandum and the like). Insofar as that information is available to subsequent investors, it would appear referencing that material would enhance predictability of interpretation. However, notwithstanding this increased availability of information potentially documenting the parties’ intent, case law diminishes reference to the parties’ intent in interpretation of corporate financing instruments, relative to reference to information relevant to that intent in other contexts.

The Sharon Steel court states:

Boilerplate provisions are thus not the consequence of the relationship of particular borrowers and lenders and do not depend upon particularized intentions of the parties to an indenture. There are no adjudicative facts relating to the parties to the litigation for a jury to find and the meaning of boilerplate provisions is, therefore, a matter of law rather than fact.

182 Id. at 600 (emphasis in original).

183 See supra note 50 and accompanying text.

184 See generally Tauke, supra note 4, at 115-16 (“Far more often, however, courts have been willing to consider evidence of market understanding, even when they otherwise have been following fairly traditional contract interpretation principles.”).

185 Sharon Steel Corp. v. Chase Manhattan Bank, 691 F.2d 1039, 1048 (2d Cir. 1982). See generally Marcel Kahan & Michael Klausner, Standardization and Innovation in Corporate Contracting (or “The Economics of Boilerplate”), 83 VA. L. REV. 713, 765 (1997) (“[T]here should be no inquiry into the
Another court states, “[I]n interpreting boilerplate indenture provisions, ‘courts will not look to the intent of the parties, but rather the accepted common purpose of such provisions.’” Reflecting the decreased reference to this extrinsic evidence in interpretation, interpretation of these instruments is much more likely to be done by the court, as opposed to a jury acting as fact-finder, although in recent times there seems to be some retrenchment as to that approach. This preference for judicial interpretation seems to play some role in making a court less likely to find an agreement ambiguous in this context and, hence, elide reference to extrinsic evidence in its interpretation.

subjective intent of a firm that has adopted a standard term. Interpretation of standard terms should be treated like the interpretation of laws: Judges, not juries, should interpret them, and their interpretations should have precedential value.”).


187 See Chase Manhattan Bank v. Traffic Stream (BVI) Infrastructure Ltd., 52 F. App’x 528, 530 (2d Cir. 2002) (stating, as to construction of definition of event of default and whether government action excuses an event of default, “This section is a boilerplate provision, and must therefore be interpreted as a matter of law.”); Leverso v. SouthTrust Bank of Ala., 18 F.3d 1527, 1534 (11th Cir. 1994) (stating, in addressing a distribution plan allocating proceeds in accordance with bondholders’ cost basis, “The meaning of boilerplate provisions is a matter of law and must be given a consistent, uniform interpretation, ‘whether it be correct or not as an initial proposition . . . ’” (citation omitted) (quoting Sharon Steel, 691 F.2d at 1048)); Bank of N.Y. v. Tyco Int’l Grp., S.A., 545 F. Supp. 2d 312, 319 (S.D.N.Y. 2008) (“Because of the importance of uniformity to the efficient functioning of capital markets, the Second Circuit held that the interpretation of boilerplate provisions is a matter of law and should not be submitted to a jury.”); Drage v. Santa Fe Pac. Corp., No. 67966, 1995 WL 396370, at *5 (Ohio Ct. App. July 3, 1995) (noting that “when a court is confronted with boilerplate provisions . . . the court is to construe such boilerplate provisions as a matter of law rather than fact.”).

188 See, e.g., Okla. Police Pension & Ret. Sys. v. U.S. Bank Nat’l Ass’n, 291 F.R.D. 47, 68 (S.D.N.Y. 2013) (“Where the contract language is subject to more than one reasonable meaning and where extrinsic evidence of the parties’ intent exists, the question of the proper interpretation should be submitted to the trier of fact, unless the extrinsic evidence is so one-sided that no reasonable jury could find in favor of the non-moving party.”); Whitebox Convertible Arbitrage Partners, L.P. v. World Airways, Inc., No. Civ. A. 1:04-CV-1350, 2006 WL 358270, at *4 n.5 (N.D. Ga. Feb. 15, 2006) (stating it is a jury question to determine whether an issuer violated indenture provision requiring securities to be redeemed in a partial redemption to be selected for redemption by lot or pro rata or other fair and appropriate means, where the issuer separately negotiated to exchange some debentures and redeemed all debentures not so exchanged).

189 See Shiftan v. Morgan Joseph Holdings, Inc., 57 A.3d 928, 935 (Del. Ch. 2012) (“In the case of documents like certificates of incorporation or designation, the kinds of parol evidence
However, as is the common theme, this principle is not consistently followed. Thus, some authority references offering documents in construction of the terms of the corporate finance instruments.\footnote{Vanderbilt Income & Growth Assocs. v. Arvida/JMB Managers, Inc., No. 15238, 1996 WL 652773, at *2 (Del. Ch. Nov. 7, 1996) (considering the prospectus), rev'd sub nom., 691 A.2d 609 (Del. 1996) (holding consideration of the prospectus converted the motion to dismiss to one for summary judgment, requiring the Court of Chancery to afford a party an opportunity for some discovery before ruling); Birn v. Childs Co., 37 N.Y.S.2d 689, 693 (Sup. Ct. 1942).} Other authority references language considered in negotiations but not ultimately included\footnote{See In re Avon Sec. Litig., No. 91 Civ. 2287(LMM), 2004 WL 3761563, at *8 (S.D.N.Y. Mar. 29, 2004) (referencing parties’ understandings in construction, but stating that they were “not of much assistance” because they were not communicated).} and what the parties communicated extrinsic to the writing, at least where the pertinent language is not categorized as “boilerplate”.\footnote{In re Payless Cashways, Inc., 215 B.R. 409, 415-16 (Bankr. W.D. Mo. 1997) (stating the negotiations leading-up to an agreement on an indenture can be considered in interpreting an ambiguous agreement, unless the pertinent language is “boilerplate”).} Frequently available in the case of warmly negotiated bilateral agreements are rarely available. Investors usually do not have access to any of the drafting history of such documents, and must rely on what is publicly available to them to understand their rights as investors. Thus, the subjective, unexpressed views of entity managers and the drafters who work for them about what a certificate means has traditionally been of no legal consequence, as it is not proper parol evidence as understood in our contract law.” (internal citations omitted)). See also supra note 107; Harris v. Union Elec. Co., 622 S.W.2d 239, 251 (Mo. Ct. App. 1981) (“We emphasize that our determination of the redemption features under the bond contract has not taken into consideration the Prospectus applicable to the Series 2005 Bonds.”), appeal on remand, 685 S.W.2d 607 (Mo. Ct. App. 1985); Hassett v. S.F. Iszard Co., 61 N.Y.S.2d 451, 455 (Sup. Ct. 1945) (“The prospectus and advertisements used in the promotion of the sale of the preferred stock were offered in evidence by the plaintiff and excluded on objection by the defendant. This evidence might be competent in an action in fraud by a purchaser of stock to recover damages or rescind the sale, but this is not such an action. This is an action to enforce rights based on contract, in which the stock certificate constitutes the contract between the parties. The written contract is complete, definite and void of ambiguity. The evidence offered is incompetent and irrelevant on any issue involved in this case.”).
D. Tedious Literalism

A number of factors described above result in courts relying to a lesser extent on the evident purposes of contractual provisions in interpreting corporate financing instruments. Some of this comes from enhanced deference to older precedent, decided at a time when courts were more likely to emphasize literalism in interpretation. Some is a consequence of courts decreasingly referencing extrinsic evidence, which may bear on the evident purposes. In addition, the complexity of the transactions causes the documents to contain detailed provisions whose purposes are less likely to be apparent to the uninitiated who may include judges who need not have practiced corporate financing law before ascending to the bench. One consequence is tedious literalism—hyper-literalism—may reign in interpreting corporate financing instruments.

1. Meaning of *in lieu of*

For example, *Wood v. Coastal States Gas Corp.*\(^{193}\) follows a literal approach in interpreting anti-dilution and anti-destruction provisions, basing the determination on construction of the phrase *in lieu of*. The conversion rights of convertible preferred stock were subject to an adjustment upon a recapitalization. The pertinent term provided:

(5) In the event that the Corporation shall be recapitalized, consolidated with or merged into any other corporation, or shall sell or convey to any other corporation all or substantially all of its property as an entirety, provision shall be made as part of the terms of such recapitalization, consolidation, merger, sale or conveyance so that any holder of . . . Preferred Stock may thereafter receive in lieu of the Common Stock otherwise issuable to him upon conversion of his . . . Preferred Stock, but at the conversion ratio stated in this Article . . . which would otherwise be applicable at the time of conversion, the same kind and amount of securities or assets as may be distributable upon such recapitalization, consolidation, merger, sale or conveyance with respect to the Common Stock of the Corporation.\(^{194}\)

The court, considering an appeal following a trial on the merits, stated, “The Vice Chancellor reasoned that a key phrase, ‘in lieu of,’ in the Certificate implies that the existing shares of Coastal common must be exchanged for

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\(^{193}\) 401 A.2d 932 (Del. 1979).

\(^{194}\) Id. at 937.
something else before there is a ‘recapitalization’ which creates rights in the preferred.”  The court affirmed, apparently relying, as did the Vice Chancellor, on the inclusion of “in lieu of” in the anti-dilution provisions.

Understanding such prolix language often requires creation of a redacted version, such as: “[After a . . . recapitalization], . . . any holder of . . . Preferred Stock may thereafter receive in lieu of the Common Stock otherwise issuable . . . upon conversion . . . the same . . . securities . . . as may be distributable upon such recapitalization, . . . with respect to the Common Stock of the Corporation.”

Put more simply, “after a recapitalization, a holder converting preferred stock may receive in lieu of the common stock otherwise issuable on conversion the same securities as may be distributable upon such recapitalization with respect to the common stock.”

The better way to express this type of adjustment—one provided in the Commentaries—is to provide that after an event triggering an adjustment, the securities will be convertible into the property that the holder would have had after the event had the securities been converted immediately prior to the triggering event. That standard language does not suffer from potential ambiguity.

Some authority construes all boilerplate provisions as having a similar import, disregarding the implications of any deviation in the literal language. Illustrating the lack of predictability of interpretation, the Wood court did not follow that approach. It referenced a literal interpretation that created a relationship that, frankly, makes no sense.

There is, unsurprisingly, authority construing the phrase “in lieu of.” State v. Smith references “the ordinary meaning of the phrase ‘in lieu of,’ which is ‘in the place of: instead of.’” To say that, after a recapitalization, preferred stock is “instead” convertible into whatever a holder would have possessed had the preferred stock been converted immediately before the recapitalization would have allowed treatment of the event in question as a recapitalization. The actual

195 Id. at 936.
196 Id. at 939-40.
197 See id. at 937
198 AM. BAR FOUND., supra note 111, at 552.
199 See infra note 288 and accompanying text.
200 779 P.2d 1097, 1098 (Or. Ct. App. 1989) (quoting WEBSTER’S THIRD NEW INTERNATIONAL DICTIONARY 1306 (1976)).
problem is the language in Wood referenced conversion into securities that were “distributable” in the triggering event, and it should also have included whatever was retained by common stockholders.201

2. Definition of final maturity

Wilmington Trust Co. v. Aames Financial Corp.202 also expressed excessive literalism. This case involved an issuer bound by a limit on refinancing subordinated debt with new indebtedness having a maturity earlier than that of the senior debt. The court approved this evasion of the purposes of this limit by allowing the issuer to exchange existing subordinated debt for new indebtedness, 30% of the new indebtedness to be mandatorily redeemed almost immediately. This allowed the subordinated debt to receive some payment before maturity of senior debt, evidently with a view to allowing the subordinated debt to receive more than it would have received had it been paid only subsequent to payment of the senior debt.

The court reached this conclusion based on a literal interpretation of the term “final maturity”:

\[\text{[S]ince debenture holders may not trade the portion of their debenture that is to be redeemed on December 15, 2002 separately from the rest of the debenture, it follows that under the Exchange Offer there is only one set of securities with a maturity date of June 15, 2012, of which a prorated 30% is scheduled to be redeemed on December 15, 2002.}\]

Lastly, the court rejected characterizing as a sham the issuer’s right to redeem the remaining 70% of the bonds at any time after the mandatory redemption at 5% of

201 It bears mention that this language has another patent defect. It provides for an adjustment where the issuer is merged “into” another firm, but not where it is merged “with” another firm. Because the stock of the survivor can be converted in a merger (as in a customary acquisition effected through reverse triangular merger), the failure to make an adjustment where there is a merger in which the issuer is the survivor is, simply, a mistake. That there is a patent mistake as to part of the anti-destruction provisions would not seem to justify extending the error to another circumstance—concerning the definition of recapitalization—where the language does not clearly require it.


203 Id. at 4.
their principal amount, although redemption of the remainder required consent of the senior indebtedness.\footnote{Id.} Understanding the bonds issued in exchange bore interest at over 5%, the arrangement is very difficult to distinguish, economically, from a prohibited early distribution to subordinated bondholders.\footnote{See Br. For Pl.-Appellant at 3, Wilmington Trust Co. v. Aames Fin. Corp., No. 780, 2002 WL 34246543 (N.Y. App. Div. Dec. 30, 2002).} It is very difficult to imagine parties expressly bargaining for subordination provisions allowing this.

3. Surrender of securities altering payments on senior securities

As the terms of corporate financing arrangements become more arcane, identification of the underlying purposes becomes more difficult. It is, of course, possible that the transaction is so complex that, as to a particular issue, the structure of the transaction does not yield a clear implication as to an issue being litigated.\footnote{See Howe v. Bank of N.Y. Mellon, 783 F. Supp. 2d 466, 479-80 (S.D.N.Y. 2011) (holding that a trustee’s ability to sell “defaulted” underlying collateral did not allow for the sale of securities allegedly “immanently about to default.”)} Where an informed assessment of the context does not yield an evident purpose, it is, of course, appropriate to rely on literalism.

However, at other times, familiarity with the context may yield an evident purpose as to the issue in question, although the complexity of the transaction may make it less likely that it will be evident to a court. Perhaps the complexity of the transaction allows litigants seeking to avoid purposes more opportunity to hide their purpose. In any case, it would appear courts are more likely to retreat to literalism when identification of evident purpose is more difficult.

\textit{Concord Real Estate CDO 2006-1, Ltd. v. Bank of America}\footnote{996 A.2d 324 (Del. Ch. 2010).} is one such case. It involved issuance of collateralized debt obligations—various securities issued by a special purpose entity holding a pool of debt obligations,\footnote{Id. at 327.} which can have very complex financial terms. Various tranches (levels) of securities had been issued.\footnote{Id. at 326.} If certain financial ratios based on the amount of securities outstanding were not met, more senior tranches would be redeemed.\footnote{Id. at 328.} In anticipation of the
test being failed, an affiliate of the issuer surrendered for cancelation—surrendered without consideration—certain junior securities, with a view to altering the ratio and thereby not having some of the senior securities redeemed.\textsuperscript{211} The trustee declined to accept them for cancelation.\textsuperscript{212} The court granted summary judgment to the issuer who sought a declaration that the securities were properly surrendered for cancelation.\textsuperscript{213}

The court did in fact reference seeking an interpretation consistent with the “‘plain purpose and object’ of the agreement.”\textsuperscript{214} However, the analysis does not seem to conform fully with that approach. The opinion noted that the common law generally gave effect to a creditor’s surrender of an obligation without consideration (the “delivery rule”).\textsuperscript{215} The court then concluded that, absent a contrary provision in the indenture, the delivery rule remained in effect.\textsuperscript{216}

Although modern indentures for securities issued by firms that are not special purpose entities make express provision for cancelation of securities acquired by the issuer and delivered to the trustee for cancelation,\textsuperscript{217} this indenture did not so provide,\textsuperscript{218}—an omission that would appear to be highly probative as to whether the parties anticipated allowing surrender of securities that would influence payments due on senior securities. However, the court reached the opposite conclusion:

\begin{quote}
Unlike the model provisions, Section 2.9[concerning cancelation of securities,] does not contain the language about an issuer’s right to tender securities for cancellation. Because the history of the model provision shows that language was intended to confirm the common
\end{quote}

\textsuperscript{211} Id. at 326.

\textsuperscript{212} Id. at 329.

\textsuperscript{213} Id. at 339.

\textsuperscript{214} Id. at 330 (quoting Kass v. Kass, 696 N.E.2d 174, 181 (N.Y. 1998)).

\textsuperscript{215} Id. at 332.

\textsuperscript{216} Id. at 333.


\textsuperscript{218} Concord, 996 A.2d at 335.
law right, the omission of the language from Section 2.9 does not alter the Delivery Rule.\textsuperscript{219}

It seems that the correct answer is that the author of the indenture simply did not expect the securities to be surrendered and also likely was not focused on any need to negate this arcane common law doctrine. In an ordinary case, an issuer may buy back bonds because it may be in the issuer’s interest to do so. It may satisfy a sinking-fund obligation less expensively by purchasing the bonds in the market, or the issuer may be able to repurchase them at below face value and decrease its obligations. The terms of these transactions will be based on market prices.

On the other hand, a securityholder, even an affiliate of an issuer, that initially holds securities as an investment (not as part of a plan to repurchase and retire securities) would not ordinarily be expected simply to relinquish a bond. Had surrender of bonds been anticipated by the author of the indenture, one would not expect the draftsman to have omitted from the form of indenture a provision that is common in model indentures allowing for cancelation of surrendered securities.

Where the result of the court’s interpretation is evidently to limit the extent to which payments are made to more senior securityholders and there is not a specific provision in the indenture allowing the issuer to avoid the payments (redemptions) to senior securities, this author would think that the senior securityholders would have the better of the argument as to what was the evident purpose of the provision.

4. Poison put and board approval of multiple slates of directors

Determining whether Concord Real Estate implements the purposes evidenced by the agreement is a question of judgment. This author’s view is it does not, though one supposes that might be a matter of debate. \textit{San Antonio Fire & Police Pension Fund v. Amylin Pharmaceuticals, Inc.},\textsuperscript{220} on the other hand, reached an interpretation where subsequent events indicate the judicial outcome likely did not represent the parties’ evident purposes.

The court referenced one general nature of covenants in public debt, that they are less intrusive covenants than covenants in credit agreements, when

\textsuperscript{219} \textit{Id.} at 336.

\textsuperscript{220} 983 A.2d 304 (Del. Ch. 2009).
construing the public debt. The reason, as the court noted, is that a lender’s rights under a credit agreement can more easily be released.\textsuperscript{221} The court referenced this relationship in construing a covenant (a poison put) in the public debt in a fashion unfavorable to the public bondholders.

Although the court’s reference to this evident purpose is helpful, it would appear that another perspective on the evident purpose would have been appropriate. The pertinent provision granted the holders the right to have their securities redeemed if there were a change in control. The pertinent contractual provisions involved the definition of a “Fundamental Change”:

A “Fundamental Change” is defined in Section 1.01 of the Indenture to have occurred if, \textit{inter alia}, “at any time the Continuing Directors do not constitute a majority of the Company’s Board of Directors . . . .” The Indenture defines “Continuing Directors” as:

(i) individuals who on the Issue Date constituted the Board of Directors and (ii) any new directors whose election to the Board of Directors or whose nomination for election by the stockholders of the Company was approved by at least a majority of the directors then still in office (or a duly constituted committee thereof) either who were directors on the Issue Date or whose election or nomination for election was previously so approved.\textsuperscript{222}

The question addressed was whether the board could “approve” someone who was not a board nominee, so that even if a board nominee lost, the winning candidate would still be a “continuing director.”\textsuperscript{223} To put it another way, could the board “approve” more than one person for a board position?

It is certainly possible to view these redemption provisions as not really benefitting the noteholders but, rather, simply providing tools to fend-off hostile takeovers. But, insofar as they are in fact designed to benefit noteholders, it would seem that the idea is the noteholders believe their likelihood of being repaid is enhanced where the current management continues to control the firm.

\begin{footnotes}
\item\textsuperscript{221} Id. at 315 n.30.
\item\textsuperscript{222} Id. at 307-08 (footnotes omitted).
\item\textsuperscript{223} Id. at 306.
\end{footnotes}
In that case, a person viewed by the incumbent board as inferior should not be satisfactory—should not be a “continuing director.”

Subsequent events would seem to show that the results of this interpretative approach are on-the-mark. The terms of debt securities in four subsequent offerings involving Sullivan & Cromwell LLP, a prominent law firm involved in the issuance of notes at issue in the case, were reviewed. The term “continuing director” is defined in each so that it clearly would no longer allow a person who was competing for a position with someone nominated by the board to be a “continuing director.”

> See Indenture Among DISH DBS Corp., Guarantors & Wells Fargo Bank, Nat’l Ass’n, (Dec. 27, 2012), in DISH DBS Corp., Current Report on Form 8-K (Dec. 27, 2012) (“‘Continuing Director’ means, as of any date of determination, any member of the Board of Directors of DISH Network Corporation who: (a) was a member of such Board of Directors on the date of this Indenture; or (b) was nominated for election or elected to such Board of Directors with the affirmative vote of a majority of the Continuing Directors who were members of such Board at the time of such nomination or election or was nominated for election or elected by the Principal and his Related Parties.”); AMC Networks, Inc., Prospectus Supplement (Dec. 10, 2012) (“‘Continuing Directors’ means, as of any date of determination, any member of the Board of Directors of the Company who: (1) was a member of such Board of Directors on the date of initial issuance of the debt securities of the applicable series; or (2) was nominated for election or elected to such Board of Directors with the approval of a majority of the Continuing Directors who were members of such Board of Directors at the time of such nomination or election.”); First Supplemental Indenture Between Dunn & Bradstreet Corp. & Bank of N.Y. Mellon (Dec. 3, 2012), in Dun & Bradstreet Corp., Current Report on Form 8-K (Nov. 25, 2012) (“‘Continuing Director’ means, as of any date of determination, any member of the board of directors of the Company who: (1) was a member of such board of directors on the date of the issuance of the securities; or (2) was nominated for election or elected to such board of directors with the approval of a majority of the Continuing Directors who were members of such board of directors at the time of such nomination or election.”); Aetna, Inc., Form of Security (n.d.), in Aetna, Inc., Current Report on Form 8-K (Nov. 2, 2012) (“‘Continuing Directors’ means, as of any date of determination, any member of the Board of Directors of the Company who (1) was a member of the Board of Directors of the Company on the date of the issuance of the Notes; or (2) was nominated for election or elected to the Board of Directors of the Company with the approval of a majority of the Continuing Directors who were members of such Board of Directors of the Company at the time of such nomination or election (either by specific vote or by approval of the Company’s proxy statement in which such member was named as a nominee for election as a director).”.

Note that a failure of the market to change language after a judicial interpretation does not necessarily mean the interpretation is consistent with the market’s expectation as to the meaning of the term. In this case, it is relatively straight-forward to revise the language to clarify its meaning. However, in other cases, it may not be, and a failure to change may reflect difficulty in adequately specifying an alternative treatment. See generally Mitu Gulati & Robert E. Scott, The Three and a Half Minute Transaction 10-11 (2013) (stating in examining a pari passu
5. Rejection of gray matter grinding argument

The tedious literal argument does not always win the day. In one of then-Chancellor (now Chief Justice) Strine’s many memorable observations,225 Law Debenture Trust Co. of New York v. Petrohawk Energy Corp., the Chancellor described an argument for a literal interpretation of a covenant triggering redemption on a change in control as a “confusing and gray matter grinding argument.”226 Illustrative of the tedious arguments that the bondholders made was that a voluntary transaction triggered a poison put, requiring that the issuer offer to redeem notes where a majority of its board did not constitute continuing directors (as defined).227 The court rejected an argument that the precise method of seating the directors resulted in some literal deficiency, noting that the purpose of the provision was to allow redemption where a non-consensual transaction occurred yet this one was consensual.228

clause in sovereign debt, “Boilerplate clauses—standardized clauses that have been used by rote over long periods of time—often remain unchanged, even when a court decision has created uncertainty regarding the clauses’ meaning. In short, boilerplate clauses are sticky: They seem resistant to amendment even when amendment seems desirable.”); Kahan, supra note 34, at 1078 (“Once a contractual term is widely employed, parties rationally may believe that others have studied the term and concluded that it operates well. This may lead them to set aside their own view that the term is deficient and could be improved.”); Kahan & Klausner, supra note 185, at 720-21 (making a similar point).

Provisions concerning refinancing with lower interest rate debt are an example. The original language at issue in, for example, Franklin Life Insurance Co. v. Commonwealth Edison Co., 451 F. Supp. 602 (S.D. Ill. 1978), aff’d, 598 F.2d 1109 (7th Cir. 1979), involved prohibitions on direct or indirect refunding. See infra notes 255-264 and accompanying text. The drafting problem is that it is difficult in advance to specify all the indirect ways a security can be refinanced with lower-interest-rate debt.

225 See, e.g., In re Synthes, Inc. S’holder Litig., 50 A.3d 1022, 1036 (Del. Ch. 2012) (“The world is diverse enough that it is conceivable that a mogul who needed to address an urgent debt situation at one of his coolest companies (say a sports team or entertainment or fashion business), would sell a smaller, less sexy, but fully solvent and healthy company in a finger snap (say two months) at 75% of what could be achieved if the company sought out a wider variety of possible buyers, gave them time to digest non-public information, and put together financing. In that circumstance, the controller’s personal need for immediate cash to salvage control over the financial tool that allows him to hang with stud athletes, supermodels, hip hop gods, and other pop culture icons, would have been allowed to drive corporate policy at the healthy, boring company and to have it be sold at a price less than fair market value, subjecting the minority to unfairness.”).


227 Id.

228 Id.
This collection of authority illustrates the lack of predictability in the courts’ interpretation of corporate financing instruments. Some authority subordinates a better literal reading to the evident purposes manifested by the language as a whole. That is more likely to happen within certain classes of circumstances: (i) where a comparable interpretative issue was not litigated long ago (e.g., modern subordination provisions); (ii) where the actions can be categorized as a common scheme of evasion, such as a step-transaction or a sham; or (iii) where the language is also used in a statute. However, reference to purposes is inconsistent, so that they may be given effect in construction of such terms as anti-dilution and anti-destruction provisions, notice provisions, provisions for release of collateral, and limits on impairing rights to payment. In addition, it would appear that the complexity of the transactions often causes courts to retreat to literalism in their construction.

Predictability is also inhibited by the failure to reference contemporaneous documents memorializing parties’ intended meanings. Courts construing corporate financing instruments further compound this unpredictability by not consistently omitting their reference to this material. Lastly, that the instruments are complex appears sometimes to cause courts to retreat into tedious literalism, but not always. In sum, predictability and consistency are not hallmarks of the collection of cases.

IV. DIFFERENCES IN INTERPRETATIVE APPROACHES

Interpreting contractual agreements involves both reference to literal terms and reference to evident purposes, even if not the best literal reading. In connection with all contractual interpretation, a balance is struck with literalism governing in some areas and purpose-based interpretations governing elsewhere. At some point, an attempt to implement claimed purposes will be so at odds with the directly pertinent literal language that a court will be unwilling to stray from the literal interpretation. The preceding Part shows that where that balance is struck—the dividing line between interpretation based on the evident purposes and interpretation reflecting literalism—is different in connection with construing corporate financing instruments, as compared to other agreements, although that difference is not accompanied by increased certainty.

However, this literalism issue is not the sole difference in interpretive approach applicable to corporate financing instruments. This Part turns to two additional differences: the extent to which the contractual relationships are
construed against a particular party and what might be described as “abstraction” of contractual interpretation beyond the language initially construed—a somewhat complicated process described in more detail below.

A. Contra Proferentem and the Like; Pro-Issuer Construction

In a variety of contexts, interpretive principles are adjusted depending on the type of instrument involved. For example, it is said that a guaranty is narrowly construed,229 and a deed is construed against the grantor.230

Contra proferentem (construction of an ambiguous contractual provision against its draftsman) is a familiar principle of contract construction that applies interpretive principles based on the process by which a contract has been negotiated and documented.231 As the court in Kaiser Aluminum Corp. v. Matheson noted, courts disagree over whether this principle applies to corporate financing agreements, stating “This reflects, in part, contrasting views regarding the respective roles played by underwriters and issuers.”232 In considering the application of this principle, courts express disagreement concerning the extent to which the participating investment banks represent investors during negotiation of the terms of the instruments.233 The Kaiser Aluminum court concluded, “[W]hen faced with an ambiguous provision in a document such as the Certificate, the Court must construe the document to adhere to the reasonable expectations of the investors who purchased the security and thereby subjected themselves to the terms of the contract.”234 On the other hand, other authority in Delaware provided, “Indentures are to be read strictly and to the extent they do

229 PERILLO, supra note 53, § 3.13, at 138.
230 Id.
232 681 A.2d 392, 398 (Del. 1996). See generally Bratton, supra note 4, at 381 (noting that underwriters’ counsel typically drafts the indenture, and noting the problem with construing an indenture adverse to the underwriters).
234 Id. at 399 (citing Rhone-Poulene Basic Chem. Co. v. Am. Motorists Ins. Co., 616 A.2d 1192, 1196 (Del. 1992)). See also Kelly v. Cent. Hanover Bank & Trust Co., 11 F. Supp. 497, 503 (S.D.N.Y. 1935) (“While, too, an instrument such as this, created and issued by [the issuer] is to be construed against it in case of doubt or ambiguity, nevertheless, it is to be fairly construed in the light of its context and of all of the surrounding circumstances.”), remanded, 85 F.2d 61 (2d Cir. 1936); Bank of N.Y. Mellon v. Commerzbank Capital Funding Trust II, 65 A.3d 539, 552 (Del. 2013) (“[T]hat principle is properly applied as a ‘last resort,’ because the Defendants could have easily drafted the “hopelessly ambiguous” Parity Securities definition in the LLC Agreement in a straightforward manner. Yet they did not.” (footnote omitted)).
not expressly restrict the rights of the issuer, the issuer is left with the freedom to act, subject only to the boundaries of other positive law.”

One might hazard that the distinction involves the type of corporate financing instrument: that the principle of construction in favor of reasonable expectations of investors is limited to stock. However, Kaiser Aluminum, a case that involved construction of preferred stock, rejected that distinction, referencing application of the principle to “bond contracts.” So, even within a single jurisdiction, there is inconsistency in application of this interpretative principle.

Moreover, additional inconsistencies in the doctrine arise because some authority states that the principle of contra proferentem is inapplicable to construction of a corporate financing instrument, although other authority

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236 Kaiser Aluminum, 681 A.2d at 398-99 (quoting Tauke, supra note 4, at 89).

237 See Broad v. Rockwell Int’l Corp., 642 F.2d 929, 947 n.20 (5th Cir. 1981) (“While as a matter of abstract contract law it is proper to construe ambiguities against the drafter of a contract, that tenet of contract law has only limited practical significance in the context of construing an indenture. To the extent the rule is practicable at all, it can only be readily applied to those terms that were actually discussed and thought about by the parties—which is almost never the case with boilerplate provisions such as the ones at issue here.”); Morgan Stanley & Co. v. Archer Daniels Midland Co., 570 F. Supp. 1529, 1541 (S.D.N.Y. 1983) (“Finally, we view this as a most inappropriate case to construe ambiguous contract language against the drafter. The Indenture was negotiated by sophisticated bond counsel on both sides of the bargaining table. There is no suggestion of disparate bargaining power in the drafting of the Indenture, nor could there be. Moreover, even if we were to adopt this rule, it is not at all clear that ADM would be considered the drafter of the Indenture, given the active participation of the managing underwriter. Indeed, it is arguable that the ambiguous language should be construed in favor of ADM.”).

The oft-cited Sharon Steel opinion provides a different interpretative approach:

Where contractual language seems designed to protect the interests of both parties and where conflicting interpretations are argued, the contract should be construed to sacrifice the principal interests of each party as little as possible. An interpretation which sacrifices a major interest of one of the parties while furthering only a marginal interest of the other should be rejected in favor of an interpretation which sacrifices marginal interests of both parties in order to protect their major concerns.

Sharon Steel Corp. v. Chase Manhattan Bank, 691 F.2d 1039, 1051 (2d Cir. 1982).
holds to the contrary.\textsuperscript{238} Certainly, a part of that conclusion derives from the difficulty in describing authorship of components of provisions, because there may be back-and-forth over individual drafts and a court may generally be reluctant to apply this principle to a contract drafted in that fashion, regardless of the type of contract. In addition, there are difficulties in applying this principle to construction of corporate financing instruments, because securityholders often are not participants in the original drafting.\textsuperscript{239}

In counterpoint to the approach reflected in \textit{Kaiser Aluminum}, other authority seems simply to reflect a bias against those providing the financing. \textit{Beal Savings Bank v. Sommer}\textsuperscript{240} exhibited a curious proissuer bent. The court ultimately concluded that the holder of a syndication interest in a bank loan was not permitted to pursue remedies directly, where the remaining thirty-six syndicate members were of a different view.\textsuperscript{241} It is frankly surprising for a court to find an implied limit on a party’s right to maintain a claim—to impose a limit on the party that the action be approved by a majority of similarly situated persons. By way of contrast, the Trust Indenture Act would render unenforceable an \textit{express} attempt to limit direct action as to principal or interest (with minor exceptions) if the claimant holds registered debt securities.\textsuperscript{242} So, it is surprising for a court to have found some implied limit on the exercise of a remedy when in other circumstances, an express attempt to bargain for that result has been prohibited. Perhaps the best that can be said of this opinion is that the court is seeking to rescue the promisor from the improvident consequences of failing to have bargained expressly for protection from hold-outs.

\textit{Chesapeake Energy Corp. v. Bank of New York Mellon Trust Co.} provided a more recent illustration.\textsuperscript{243} Issuer’s counsel stumbled in seeking to implement

\begin{itemize}
\item \textsuperscript{239} See generally Stark et al., supra note 98, at 559-61 (noting underwriter conflict of interests in criticizing construction in favor of the issuer).
\item \textsuperscript{240} 865 N.E.2d 1210 (N.Y. 2007).
\item \textsuperscript{241} Id. at 1211.
\item \textsuperscript{242} See supra note 110 and accompanying text.
\item \textsuperscript{243} No. 13 Civ. 1582 (PAE), 2013 WL 1890278 (S.D.N.Y. May 8, 2013).
\end{itemize}
changes from ordinary redemption provisions. Paragraph (b) of section 1.7 of a supplemental indenture provided:

(b) At any time from and including November 15, 2012 to and including March 15, 2013 (the “Special Early Redemption Period”), the Company, at its option, may redeem the Notes . . . . The Company shall be permitted to exercise its option to redeem the Notes pursuant to this Section 1.7 so long as it gives the notice of redemption pursuant to Section 3.04 of the Base Indenture during the Special Early Redemption Period. Any redemption pursuant to this Section 1.7(b) shall be conducted, to the extent applicable, pursuant to the provisions of Sections 3.02 through 3.07 of the Base Indenture.\textsuperscript{244}

Section 3.04 of the base indenture required the issuer to provide bondholders at least thirty-day’s advance notice of any redemption.\textsuperscript{245} The issuer sought a declaratory judgment that it was permitted to effect a redemption as long as the notice was issued on or before March 15, 2013.\textsuperscript{246}

The drafting was simply a mistake. A typical way to draft redemption provisions contemplates that the draftsman identify the time-period in which the securities are redeemable in a first provision, and then provide whatever advance notice is required in a second provision. For idiosyncratic reasons, this issuer sought to change this standard approach by identifying whether the securities were redeemable based on the time that the notice was issued, as opposed to the date of the redemption.\textsuperscript{247} To draft this alternative scheme properly, the first sentence needs to be revised so that reference to the redeemability is based not on the dates of redemption but, instead, allows redemption as long as the notice of redemption is given by a particular time.

Interestingly, press reports quoted a senior person affiliated with the bank leading the offering to the effect that the offering had an “8-percent-plus IRR

\begin{footnotesize}
\begin{itemize}
\item\textsuperscript{244} Id. at *2.
\item\textsuperscript{245} Indenture among Chesapeake Energy Corp., Subsidiary Guarantors & Bank of N.Y. Mellon Trust Co. 24, in Chesapeake Energy Corp., Registration Statement on Form S-3 (Aug. 2, 2010) (“At least 30 days but not more than 60 days before a redemption date, the Company shall mail a notice of redemption by first-class mail to each Holder of Securities to be redeemed at such Holder’s registered address.”).
\item\textsuperscript{246} Chesapeake Energy, 2013 WL 1890278, at *1.
\item\textsuperscript{247} Id.
\end{itemize}
\end{footnotesize}
internal rate of return],” though an expert computed securities bearing that rate of return required redemption (not notice of redemption, but redemption itself) not later than May 15, 2013.248

The court simply rescued the issuer from its drafting mistake.

In addition to this informal interpretative bias against investors, two formal interpretative principles create uncertainty, typically weighing against the investors. One, mentioned above,249 is the Doctrine of Independent Legal Significance. The second is that, where the corporate financing instrument is preferred stock, Delaware authority requires the preferences be “expressly and clearly stated” and “not be presumed or implied.”250 As the Court of Chancery recently noted, there is tension between this interpretive principle and the Delaware approach, which requires construction in favor of the reasonable expectations of the investors.251 Illustrating the indeterminacy of the law, there has been some change over time concerning the standard for assessing the clarity of expression of differences. In 1990, the Delaware Supreme Court indicated putative differences were to be “strictly construed” as in derogation of the common law default that all stock is equal,252 a test the Delaware Supreme Court softened only eight years later.253

B. Abstraction of Interpretation: Interpretation Divorced from Language or Context

Another anomaly in the construction of corporate financing agreements involves what may be termed “abstraction”—a process in which interpretations are based on considering precedent or the contract language in the abstract and disregarding facts or contractual language that would seem relevant. A series of


249 See supra notes 59-61 and accompanying text.

250 Elliott Assocs., L.P. v. Avatex Corp., 715 A.2d 843, 852-53 (Del. 1998) (“Any rights, preferences and limitations of preferred stock that distinguish that stock from common stock must be expressly and clearly stated, as provided by statute. Therefore, these rights, preferences and limitations will not be presumed or implied.” (footnote omitted)).


252 See Waggoner v. Laster, 581 A.2d 1127, 1134-35 (Del. 1990) (citing numerous cases holding that stock preferences are to be strictly construed).

253 See Elliott Assocs., 715 A.2d at 853 n.46 (continuing to approve Waggoner but determining that the use of “strict construction” was problematic).
cases extended the precedent to contexts that the initial authority would seem to indicate would be distinguishable.  

1. Covenants limiting refinancing with lower-cost funds

*Franklin Life* involved a claim that an issuer in 1972 violated restrictions on redemption of preferred stock issued in 1970. The terms of the preferred stock stated that none of the stock “may be redeemed through refunding, directly or indirectly, by or in anticipation of the incurring of any debt [having a lower interest rate].” The prospectus for the preferred stock declared a need for approximately $1 billion of capital to fund planned construction that was expected to be raised through further securities sales. Consistent with that plan, in 1971, the issuer incurred over $1 billion of debt. It was all, however, below the triggering interest rate. In March 1972, the issuer redeemed the preferred stock, applying segregated proceeds from the sale of common stock and warrants. The court found, after a bench trial, the issuer did not breach the contractual terms of the preferred stock.  

The court’s analysis distinguished between the following prohibitions: (1) preferred stock cannot be redeemed “in anticipation of debt,” and (2) preferred stock cannot be redeemed “through refunding in anticipation of debt.” The opinion stated version (1) would have been breached. However, the actual terms, corresponding to version (2), were not breached, because common stock “cannot be refunded.” It would appear that the analysis was that any low-interest debt

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256 Id. at 613.  

257 Id. at 605.  

258 Id.  

259 Id. at 606.  

260 Id. at 606.  

261 Id. at 604.  

262 Id. at 616.  

263 Id. at 614.  

264 Id. at 614 (“Were it not for ‘refunding’, plaintiffs’ argument would be persuasive.”).
cannot “refund” the common stock whose proceeds were directly used to redeem the preferred stock. This distinction is important because, as will be seen, this crucial justification for the outcome is later disregarded.265

In reaching its conclusion, the court considered expert testimony from a former director of underwriting at a well-known investment bank.266 The expert stated this type of provision was originally used in issuance of bonds in the 1930s and 1940s, and that such a provision “was designed to prevent this type of redemption, but not to prevent the redemption out of an issue of common stock.”267 The court ultimately disregarded the evidence, finding trade understandings in the bond market unpersuasive in construing preferred stock terms.268

The opinion noted that the securityholders “believed redemption could not be accomplished so long as defendant was a ‘net borrower’, that is, had borrowed more money per year than it repaid.”269 However, the court also noted that the issuer must have intended to retain some right of redemption.270 It further found that any redemption would have been highly unlikely under the plaintiffs’ interpretation.271 The court concluded, “Thus, plaintiffs’ interpretation in effect would render the stock uncancellable prior to August 1, 1980. If this were [the issuer’s] intent it could have been achieved with a great deal less words.”272

The court’s analysis in Franklin Life does not seem to reflect the proper interpretative approach. Instead of focusing on the burden arising from the express provision, the focus should be on what benefit the provision was designed to provide. Recall that the implied covenant of good faith is often phrased in terms of assuring that “neither party deprives the other of ‘the fruits of the agreement’” or providing a remedy where a party “seeks . . . to withhold [the contract’s] benefits.”273

265 See infra notes 275-278 and accompanying text.
266 Franklin Life, 451 F. Supp. at 609.
267 Id.
268 Id. at 615-16.
269 Id. at 608.
270 Id. at 615.
271 Id.
272 Id.
273 See supra notes 83, 85 and accompanying text.
Franklin Life referenced a different method of interpretation depending on whether the provision was found in preferred stock or bonds. Subsequent authority produced results inconsistent with the basis of the original decision. Morgan Stanley & Co. v. Archer Daniels Midland Co. involved a covenant with the following prohibition: “[T]he Company may not redeem any of the Debentures pursuant to such option from the proceeds, or in anticipation, of the issuance of any indebtedness for money borrowed [at specified interest rates].”

Recall from above that Franklin Life indicated two factors were important in determining whether the redemption was permitted: (1) that the redeemed securities were not bonds (for which there was a relevant trade practice), and (2) that the pertinent covenant did not prohibit redemption merely “in anticipation of debt,” but, rather, prohibited redemption “through refunding … by or in anticipation of the incurring of any debt [having a lower interest rate].” These factors were not present in Archer Daniels. Nevertheless, the Archer Daniels court held the plaintiffs failed to show a sufficient likelihood of success to grant preliminary injunctive relief.

Franklin and Archer Daniels illustrate a pattern of contract interpretation, in which: (1) a court first interprets some provision, relying on the precise language or the context to support the conclusion; and (2) another court in another case elides the basis for that initial decision and extends the interpretative outcome to a case where the significant context or particulars in language are not present. Though the Archer Daniels court justified its outcome as necessary to avoid

\[\text{See Franklin Life, 451 F. Supp. at 616 ("[W]ere the redemption provisions contained in a corporate bond, the expert testimony would be more relevant and more persuasive. But the issue here is preferred stock.").}\]

\[\text{570 F. Supp. 1529, 1531 n.1 (S.D.N.Y. 1983).}\]

\[\text{451 F. Supp. at 611, 613 616.}\]

\[\text{See generally William A. Klein et al., The Call Provision of Corporate Bonds: A Standard Form in Need of Change, 18 J. Corp. L. 653, at 686-87 (1993) ("[T]he typical nonrefunding provision that has been used in the past is largely ineffective for the simple and obvious reason that money is fungible and that, consequently, a borrower that is willing to incur some transaction costs can avoid the nonrefunding stricture.").}\]
“intolerable uncertainty in the capital markets,” extending a call provision’s authority beyond its express contours does not achieve that result.

One cannot simply conclude, however, that corporate financing terms limiting refinancing are interpreted with tedious literalism. Other case law over eighty years old seems to emphasize the evident purposes in allowing a refinancing.

2. Parkinson and anti-destruction protection

In addition to these and other cases that followed Metropolitan Life Insurance Co. v. RJR Nabisco, Inc., one can identify three similar circumstances where courts have extended a provision’s authority beyond its original, well-circumscribed contours. In Parkinson v. West End St. Ry. Co., the court held that an issuer’s

370 F. Supp. at 1542 (“Given the paramount interest in uniformly construing boilerplate provisions, and for all the other reasons stated above and in our prior Opinion, we chose to follow the holding in Franklin.”).

Kelly v. Cent. Hanover Bank & Trust Co., 11 F. Supp. 497 (S.D.N.Y. 1935), remanded, 85 F.2d 61 (2d Cir. 1936), elsewhere described as “[t]he great pathological decision of the depression era,” Bratton, supra note 4, at 391 n.67, examines a covenant restricting incurrence of “additional indebtedness.” 11 F. Supp. at 502 n.3. The District Court for the Southern District of New York, as the U.S. Court of Appeals for the Second Circuit noted, dismissed claims that an issuer violated a negative pledge and violated a provision limiting the incurrence of indebtedness. 85 F.2d at 62. The finding on the latter point is of interest.

As to renewals of short-term debt upon its maturity, at times at a higher interest rate, see Kelly, 11 F. Supp. at 504-05, the district court found, “No ‘additional indebtedness’ is ‘created’ or ‘assumed’ by the renewal of a loan; those phrases, taken together, connote extension in amount, not extension in time. The obvious purpose of the covenant was to prevent an increase in [the issuer’s] total liabilities, not to prevent postponement of the payment of an old liability . . . . That the interest rates were increased in consideration of the renewals is immaterial; the covenant relates to the creation and not to the cost of carrying the principal of the indebtedness.”

This outcome makes the word “additional” carry a lot of water, particularly where the court makes express reference to construing ambiguous debt provisions against the issuer. See supra note 234. If one wishes to exclude renewals on maturity from the scope of a covenant limiting incurrence of indebtedness, it is certainly easy so to provide expressly. See Kelly, 11 F. Supp. at 503. And a bondholder is certainly not indifferent where the new indebtedness is at a higher interest rate. Notwithstanding the ease of clarifying the right to renew, the court found that the agreement had the meaning that could have been easily clarified, id. (and one that one would have expected to have been so clarified had the matter been considered).

In remanding, the Second Circuit directed the district court to make findings on a matter relevant to another clause (a negative pledge) and to determine whether subsequent lenders had knowledge of the covenants. 85 F.2d at 63. No further opinions are reported. The remand, therefore, seemingly did not call into question the district court’s determination as to renewals.

53 N.E. 891, 892-93 (Mass. 1899).
successor by consolidation was not in breach for failure to deliver preferred stock on maturity of bonds, even though the predecessor issuer had undertaken to do so. The court stated:

A consolidation which makes no arrangement for furnishing stock in the new company, and which ends the existence of the old ones, as a general rule may be presumed to put an end to the right of bondholders to call for stock, not because the law has not machinery for keeping such a right alive, but because, not being bound to do so, it has made dispositions which manifestly take no account of the right.\(^{282}\)

Earlier authority from the same court, *John Hancock Mut. Life Ins. Co. v. Worcester, N. & R. R. Co.* relied on statutory language to affirm a determination that convertible bonds, following what the opinion described as a “consolidation,” remained convertible.\(^{283}\) In the *Parkinson* court’s view, the

\(^{282}\) Id. *Parkinson* now appears long-settled law. *See Buxbaum, supra* note 129, at 287. It is interesting to note that, three decades after it was decided, Berle references an approach at odds with the case:

Many covenants in support of conversion or stock purchase warrants explicitly state this rule[, adjusting conversion rights where the authorized capital is changed,] at present. Particularly where the privilege may be exercised in respect of stock without nominal or par value . . . it is frequently provided that the conversion privilege may be exercised in respect of a greater number of shares in the event of any splitting of units. It is believed that these specific covenants merely state the rule which a court of equity would enforce in any event. The fact that the conversion privilege uses a name which is applicable to the shares both before and after the splitting-up process, can hardly be construed to give the obligor corporation liberty to evade its promise by completely altering the unit value of the share.

A. A. Berle, Jr., *Convertible Bonds and Stock Purchase Warrants*, 36 YALE L.J. 649, 655 (1927) (footnote omitted) (citing John Hancock Mutual Life Ins. Co. v. Worcester R.R., 21 N. E. 364, 364-65 (Mass. 1889) (statute providing successor in consolidation of two railroads subject to all duties, debts, obligations, etc. of either caused convertible bondholder of successor not to lose conversion right upon consolidation; expressly limiting the analysis to this particular consolidation)); Gay v. Burgess Mills, 74 A. 714 (R.I. 1909)). But see Broad v. Rockwell Int’l Corp., 642 F.2d 929, 943 (5th Cir. 1981) (“Justice Holmes’ decision in *Parkinson* was aptly cited by the authors of the Commentaries for the proposition that antidilution protection must be provided by contract if it is to be provided at all, for *Parkinson* holds that there is no such protection at common law.”). Buxbaum’s 1954 article indicates that, as of that time, Berle’s view had been rejected. *See Buxbaum, supra* note 129, at 282 (indicating an adjustment for a split will not be implied).

\(^{283}\) 21 N.E. 364, 364-65 (Mass. 1889).
different outcomes in these two cases resulted from different levels of “intimacy” between the pairs of constituent corporations.\textsuperscript{284} On the basis of the curious authority of Parkinson, modern courts continue to interpret typical corporate financing instruments as not having implied anti-destruction protection.\textsuperscript{285} However, balancing the “intimacy” of the constituent corporations appears no longer in vogue.\textsuperscript{286}

3. No-recourse provisions: \textit{LaSalle}

Another illustration is provided by \textit{LaSalle National Bank v. Perelman}.\textsuperscript{287} The court made reference to the construction of no-recourse provisions based on the general purposes of such provisions as opposed to the actual agreed-upon language of the no-recourse provision being litigated.\textsuperscript{288} Language in \textit{Bank of New York Mellon Trust Co. v. Liberty Media Corp.} is to a similar effect.\textsuperscript{289}

4. Successor liability: \textit{Liberty Media}

\textit{Bank of New York Mellon Trust Co. v. Liberty Media Corp.}\textsuperscript{290} involved an odd illustration of abstraction of the analysis presented in \textit{Sharon Steel Corp. v. Chase

\textsuperscript{284} 53 N.E. 891, 892.

\textsuperscript{285} \textit{See, e.g.}, Lorenz v. CSX Corp., 1 F.3d 1406, 1417 (3d Cir. 1993) (citations omitted) (“[A] corporation is under no duty to act for the benefit of its debentureholders, or to refrain from action which dilutes their interest, except as provided in the indenture.”).

\textsuperscript{286} No other pertinent case was found in the following Westlaw search: Parkinson & (merge! or consolidat!) & intimacy (Westlaw, ALLCASES database) (Feb. 10, 2013). The search revealed six other cases, which involved criminal or anti-trust or other matters not relevant to this subject.

\textsuperscript{287} 141 F. Supp. 2d 451 (D. Del. 2001).

\textsuperscript{288} As noted above, \textit{see supra} note 122 and accompanying text, in rejecting a claim that language construed in a prior case was materially different (based on whether the term “hereunder” was included), the \textit{LaSalle} opinion stated:

\begin{quote}
[T]he \textit{Geyer v. Ingersoll Publications Co.}, 621 A.2d 784, 793 n. 6 (Del. Ch. 1992), court did not rely on the word ‘hereunder’ or any specific language of the provision in limiting the provision to contract claims. Instead, the Chancery Court generally held that no recourse provisions are limited to contract claims . . .
\end{quote}

141 F. Supp. 2d at 461.

\textsuperscript{289} 29 A.3d 225, 241 (Del. 2011) (“[I]n interpreting boilerplate indenture provisions, ‘courts will not look to the intent of the parties, but rather the accepted common purposes of such provisions.’”); \textit{see supra} note 186.

\textsuperscript{290} 29 A.3d at 237-39.
Manhattan Bank. Sharon Steel involved a firm whose shareholders approved a plan of liquidation. An initial step in that liquidation was the sale of one of its three lines of business. Later that year, the issuer entered into agreements to dispose of its remaining assets in separate transactions. The opinion noted that various indentures contained “a ‘successor obligor’ provision allowing [the issuer] to assign its debt to a corporate successor which purchases ‘all or substantially all’ of [the company]’s assets. If the debt is not assigned to such a purchaser, [the company] must pay off the debt.” The issuer sought to substitute the last buyer as a successor obligor. Judgment was rendered in favor of the bondholders, holding that the final sale was not a sale of substantially all the issuer’s assets, but was simply one part of a multi-step transaction. The U.S. Court of Appeals for the Second Circuit affirmed.

Liberty Media, however, abstracted the outcome of Sharon Steel to control the construction of an indenture having materially different language. The Liberty Media indenture made express reference in the successor obligor provision to application to a “series of transactions”—language not included in the Sharon

291 691 F.2d 1039, 1048 (2d Cir. 1982).
292 Id. at 1045.
293 Id. at 1046.
294 Id. at 1046-47.
295 Id. at 1044-45.
296 Id. at 1046-47.
297 Id. at 1051.
298 Id. at 1053.
299 The relevant language in question was somewhat anomalous:

[Liberty Sub] shall not consolidate with or merge into, or sell, assign, transfer, lease, convey or other[wise] dispose of all or substantially all of its assets and the properties and the assets and properties of its Subsidiaries (taken as a whole) to, any entity or entities (including limited liability companies) unless:

(1) the successor entity or entities . . . shall expressly assume, by an indenture (or indentures, if at such time there is more than one Trustee) supplemental hereto executed by the successor Person and delivered to the Trustee, the due and punctual payment of the principal of, any premium and interest on and any Additional Amounts with respect to all the Securities and the performance of every obligation in this Indenture and the Outstanding Securities on the part of [Liberty Sub] to be performed or observed . . . ;
Steel indenture. Nevertheless, the court concluded that as to the question of whether multiple transactions should be integrated for purposes of interpreting successor obligor provisions, the two indentures should be construed as having the same meaning. The language referring to a “series of transactions” in the Liberty Media indenture was essentially read out because the language in the Liberty Media indenture was, in the court’s view, not sufficiently different from the language in the Sharon Steel indentures:

Liberty’s Indenture was executed many years after the Second Circuit’s decision in Sharon Steel. There is no evidence in the record that the “series” language was included for any reason other than to clarify that the Successor Obligor Provision should be interpreted in the same manner as the one at issue in Sharon Steel. The trial testimony established—and the Trustee admits—that the Successor Obligor Provision was never a subject of negotiations between the parties in the case. Had the parties to the Indenture intended to create an asset disposition covenant with a broader scope than the standard, boilerplate successor obligor covenant, it was incumbent upon them to include it in a separate, negotiated covenant. As two commentators have noted:

Sharon Steel illustrates the narrow construction of indenture provisions and the underlying concerns that inform the interpretation of indenture provisions by the courts. It is therefore important

(2) immediately after giving effect to such transaction or series of transactions, no Event of Default or event which, after notice or lapse of time, or both, would become an Event of Default, shall have occurred and be continuing; and

(3) either [Liberty Sub] or the successor Person shall have delivered to the Trustee an Officers’ Certificate and an Opinion of Counsel [containing certain statements required by Section 801].


The anomaly was that the reference to a “series of transactions” is in clause (2). It is not clear why the language did not include “in one transaction or a series of transactions” immediately before “unless” (the last word before clause (1)). The Liberty Media court did not seem to find this oddity relevant; rather, it focused on whether the reference to a “series” of transactions meant something other than the kind of series at issue in Sharon Steel. See id. at 235-36 (“The parties dispute whether Liberty will breach the Successor Obligor Provision by disposing of substantially all its assets in a series of transactions. It is undisputed, however, that the Capital Splitoff, standing alone, does not constitute “substantially all” of Liberty’s assets. The threshold question is, therefore, whether the Capital Splitoff should be aggregated with the prior spinoffs of LMI and Discovery and the splitoff of LEI.”).
that negotiated provisions in an indenture be not only explicit but also distinct from boilerplate provisions. Modifications to common indenture provisions will unlikely yield additional rights as courts will not look to the intent of the parties, but rather the accepted common purpose of such provisions.

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We conclude that the principles articulated in Sharon Steel are the proper basis for determining, under New York law, the nature and degree of interrelationship that will warrant aggregation of otherwise separate and individual transactions as a part of a “series.” In Sharon Steel, the Second Circuit determined that aggregation is appropriate only when a series of transactions are part of a “plan of piecemeal liquidation” and “an overall scheme to liquidate” and not where each transaction stands on its own merits without reference to the others.300

Note that Sharon Steel itself did not actually address the issue presented by Liberty Media.301 Sharon Steel found that multiple transactions pursuant to an approved plan of liquidation, occurring within one year, were to be integrated.302 It did not speak to the issue in Liberty Media of whether multiple transactions occurring over more than half a decade, not pursuant to a determination to liquidate, were to be integrated.303

There are now multiple sources of form language. They include the Commentaries,304 the Model Simplified Indenture,305 the Revised Model Simplified Indenture306 and the Model Negotiated Covenants and Related Definitions.307

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300 Id. at 242-43 (quoting Dennis Connolly & William Hao, X Marks the Spot: Contractual Interpretation of Indenture Provisions, 17 J. BANKR. L. & PRAC. 6, Art. 1, 12 (2008) (emphasis added by the court)) (footnote omitted).

301 See Sharon Steel Corp. v. Chase Manhattan Bank, 691 F.2d 1039 (2d Cir. 1982).

302 Id. at 1051.

303 29 A.3d at 227, 235 (final transaction announced in 2010, referenced as the “fourth major distribution of assets since March 2004”).

304 AM. BAR FOUND., supra note 111.


306 Ad Hoc Comm. for Revision of the 1983 Model Simplified Indenture, supra note 211.
Under the Liberty Media approach, language that is similar to that contained in one of these models will be construed as if the language from the model were included, ignoring any differences as long as the language is similar.308

These cases reflect unrealistic expectations concerning the drafting of these types of agreements.309 In this author's experience, one drafts agreements focusing on the pertinent language, which may be taken from a source of form documentation such as the Commentaries, but is often simply taken from some previous deal, a process which does not indicate whether the language is based on something from a form. One drafts such agreements starting with language used in a prior transaction and modifying it for the deal at hand. It was not this author's experience that the drafting of each individual covenant was the subject of research to determine whether the language initially was set forth in some model such as the Commentaries. Under the Liberty Media approach, such a drafting method might significantly influence a judicial interpretation of the covenant. Given the proliferation of forms, such extensive research is likely to be prohibitively expensive.

Even if one were aware of the origin of the language used in an agreement, the editorial changes required by the Liberty Media court to change the meaning of the language are unreasonable.310 It is not clear what constitutes a "separate" covenant. Must it be a separate sentence or a separate section? Why must one create a "separate" covenant to alter the meaning from language in a form, regardless of whether a separate sentence or a separate section is required? Why must it be "negotiated"? Why must it be ineffective if it is included in an initial draft and never objected to by the parties? And how can the question of whether it was "negotiated" be harmonized with the common view that these types of documents are construed based on the language used, eschewing reference to the negotiations that cannot be observed by subsequent traders in the securities?311 This approach to contract interpretation substantially impedes

308 See Liberty Media, 29 A.3d at 242 ("Modification to common indenture provisions will unlikely yield additional rights as courts will not look to the intent of the parties, but rather the accepted common purpose of such provisions." (emphasis in original)).
309 See generally Kahan & Klausner, supra note 185, at 765 ("Ambiguity in the customized term should be resolved to give the term a meaning distinct from that of its standard counterpart." (emphasis added)).
310 See 29 A.3d at 242 ("[I]t was incumbent upon them to include it in a separate, negotiated covenant.").
311 See supra Part III.C.
the ability of those negotiating to draft language that can be interpreted as the draftsman intends.

C. Conclusion

This Part collects a few additional idiosyncrasies in the interpretation of corporate financing instruments. Courts are inconsistent in determining whether the instruments should be construed against a particular party and, if so, against which party. Such inconsistencies provide a source of great uncertainty. This Part also illustrates a curious abstraction that is at times applied in the construction of corporate financing instruments. The language used is sometimes construed as an abstract contract, divorced from the actual, negotiated language. Such an interpretative approach impedes the ability of draftsmen to document transactions in language that a court will give the intended effect. This is particularly curious when one considers that these instruments are often drafted by highly sophisticated counsel with substantial expertise in the field; the approach certainly cannot be considered as enhancing the ex-ante predictability of the negotiated terms.

V. Conclusion: Failure to Achieve Objective of Enhanced Predictability; Deference Inhibiting Diversification

Assorted authority provides for an anomalous, enhanced literalism in the interpretation of corporate financing instruments, putatively to assure needed predictability in the interpretation of these agreements. As these principles are implemented in fact, they do not yield predictability. Courts more frequently settle with vestigial literalism when dealing with agreements that involve corporate financing transactions. But they do not do so consistently. In the end, predictability is not achieved, and draftsmen are left with the additional disadvantage of the persistence of interpretative norms that in other contexts have been discarded as undesirable.

Some modern authority interpreting corporate financing instruments conventionally applies modern interpretative principles, such as a recent case restraining a lender that sought to evade limits on assignment of the loan by conveying a participation.312 Part III.A also collects modern interpretative approaches in the construction of subordination provisions, as well as no-action and no-recourse provisions. It also identifies authority implementing modern interpretations where a court categorizes challenged acts as a sham or a prohibited

312 See supra notes 101-103 and accompanying text.
step transaction. Vestigial literalism may also be rejected in construction of contract language paralleling statutory provisions that also may be construed. However, as shown in the remainder of Part III, implementation of modern interpretative principles emphasizing the evident purposes is intermittent and unpredictable.

Accompanying this enhanced literalism is an increased deference to precedent, including precedent from other jurisdictions, often justified for the same reasons. Somewhat ironically given the literalism applied in some contexts, terms of corporate financing agreements are at times abstracted in the course of interpretation. An atypically enhanced specificity, of an inadequately identified scope, may be required to draft provisions that will be interpreted by courts as effecting an election to create terms different from those that were the subject of prior construction, whether by a court or by the authors of model forms. Because it is often not practicable during the negotiation of corporate financing transactions to trace the precise origins of language, and compare it to all these other sources, this approach decreases the ability of draftsmen to reflect the intended bargain in the terms of corporate financing contracts. Any increase in ex post certainty is at the expense of decreased ex ante certainty. This anomalous interpretative approach, which increasingly relies on vestigial literalism that depends on interpretations from long ago, coupled with the path-dependence of current interpretative doctrine applied to corporate financing instruments, creates a framework that often makes it impracticable for a draftsmen to assure contemplated contract language will achieve the intended results.

Consider the following example: An issuer proposes to take an action that a majority of bondholders believes to be unpermitted—an allegedly improper dividend. A no-action clause allows holders of some percentage of securities to bring a lawsuit after some period of time following an unsuccessful demand that the trustee sue. The issuer gives little advance notice of the dividend. Under the literal terms of the no-action clause, if the trustee declines to sue, the bondholders’ right to sue will only mature after the dividend has been made.

Is this a circumstance where a court will emphasize the evident purposes of the provision (avoidance of inconsistent enforcement and action brought as a mere strike-suit by one without a real interest—concerns that are likely ill-founded when it is a majority of bondholders who wish to sue)? Will construction in light of evident purposes be applied to these provisions, avoiding the possibility that the ability to litigate a bona fide claim will be lost, as in U.S. Bank? Or will the court retreat to literalism? Akanthos Capital Management, LLC v.
CompuCredit Holdings Corp. provided the latter answer.\textsuperscript{313} In that case, a lawsuit was initiated and sought to enjoin an allegedly improper dividend from being effected before the bondholders could sue directly.\textsuperscript{314} The outcome of such a case, at least in that circuit, is now clear. However, the outcome was not predictable, at least to this author, with any amount of confidence.\textsuperscript{315}

The framework for interpreting these instruments does not yield a process that provides predictable outcomes. As each new dispute arises, a student of these interpretative principles cannot confidently predict the outcome a court will reach. The problems are even greater for those tasked with documenting these types of transactions. The current process ultimately results in outcomes that are less likely to be correct and limits the ability of bondholders to diversify their risk. This author would commend enhanced reference to the evident purposes manifested by the instruments taken as a whole, a method articulated by some courts.\textsuperscript{316} Where one cannot identify a plausible reason why parties would have bargained for the outcome dictated by a literal parsing of individual provisions, giving effect to the evident purposes manifested by the agreement as a whole is well-justified. This author further commends the budding retrenchment from enhanced deference to precedent in construction of these instruments.

\textsuperscript{313} 677 F.3d 1286 (11th Cir. 2012).
\textsuperscript{314} Id. at 1297.
\textsuperscript{315} Another example is Law Debenture Trust Co. v. Maverick Tube Corp., 595 F.3d 458, 471-72 (2d Cir. 2010) (American Depositary Shares not treated as common stock for purposes of covenant triggered by change in control; hypothetical bargain rationale for this treatment of American Depositary Shares not provided).
\textsuperscript{316} See, e.g., supra note 80 and accompanying text.