SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART 48

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EMBARQ, L.L.C.,

Plaintiff,

- v -

THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A., CAPITAL RESEARCH AND MANAGEMENT COMPANY, and DISCOVERY CAPITAL MANAGEMENT, LLC,

Defendant.

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INDEX NO. 651404/2023

MOTION DATE _____

MOTION SEQ. NO. 006 007

DECISION + ORDER ON MOTION

HON. ANDREA MASLEY:

The following e-filed documents, listed by NYSCEF document number (Motion 006) 64, 65, 66, 67, 68, 69, 70, 71, 72, 73, 74, 75, 76, 91, 96, 100, 101, 102
were read on this motion to/for JUDGMENT - SUMMARY.

The following e-filed documents, listed by NYSCEF document number (Motion 007) 77, 78, 79, 80, 81, 82, 83, 84, 92, 94, 97, 98, 99, 103
were read on this motion to/for JUDGMENT - SUMMARY.

Upon the foregoing documents, it is

Plaintiff Embarq, L.L.C. (Embarq) brings this declaratory judgment action against defendants Capital Research and Management Company and Discovery Capital Management, LLC (together, the Noteholders), seeking a declaration that the recent issuance of liens and guarantees by certain Embarq subsidiaries does not constitute a breach of the indenture (Indenture) governing the unsecured notes that Embarq issued to the Noteholders in 2006. (NYSCEF Doc. No. [NYSCEF] 2, Complaint at ¶19.) Defendant The Bank of New York Mellon Trust Company, N.A. is the successor trustee under the Indenture. (NYSCEF 46, Joint Statement of Undisputed Material Fact [JS], ¶

3.)[1]

In their answer, the Noteholders contend that Embarq has breached the Indenture and counterclaim for declaratory judgment, breach of contract and breach of the implied covenant of good faith and fair dealing. (NYSCEF 11, Answer with Counter-claim(s), ¶¶ 41-78.)

Embarq and the Noteholders move for summary judgment. (NYSCEF 64 and 77, Notices of Motion [Motion #006 and Motion #007 respectively].)

I. Background

In May 2006, Embarq issued $1.485 billion in unsecured 7.995% notes due in 2036 (the Embarq Notes), which are governed by the Indenture. (NYSCEF 46, JS ¶¶ 1, 2; *see also* NYSCEF 47, Indenture; NYSCEF 48, Global Note.) Embarq, which has no capital assets, is the sole obligor under the Indenture. (NYSCEF 46, JS ¶¶ 7, 8.)

Section 1008 of the Indenture titled "Limitation Upon Mortgages and Liens of the Company," provides that:

> "The Company will not, and will not permit any Restricted Subsidiary to, directly or indirectly, create or suffer to be created or to exist, any Lien (other than Permitted Liens) upon any of its Property, unless it has made or will make effective provision whereby the Outstanding Securities will be secured by such Lien equally and ratably with (or prior to) all other indebtedness of the Company or such Restricted Subsidiary secured by such Lien for so long as any such other indebtedness of the Company or such Restricted Subsidiary shall be so secured. Notwithstanding the foregoing, the Company may, and may permit any Restricted Subsidiary to, issue, assume, guarantee, create or suffer to be created or to exist indebtedness secured by Liens on Property that are not Permitted Liens without equally and

[1] The Indenture, dated May 17, 2006, was originally between Embarq and J.P. Morgan Trust Company, National Association, as indenture trustee. (NYSCEF 46, JS ¶ 2; *see also* NYSCEF 47, Indenture at 1).

> ratably securing the Outstanding Securities, so long as the sum of all such indebtedness then being issued or assumed together with all remaining outstanding indebtedness secured by a Lien that is not a Permitted Lien together with the Attributable Debt in respect of any Sale and Leaseback Transaction does not exceed 15% of the Consolidated Net Tangible Assets."[2] (NYSCEF 47, Indenture § 1008.)

The Indenture defines the terms "Lien" and "Property" as follows:

> "'Lien' means, with respect to any Property of any Person, any mortgage or deed of trust, pledge, hypothecation, assignment, deposit arrangement, security interest, lien, charge, easement or zoning restriction, encumbrance, preference, priority or other security agreement or preferential arrangement of any kind or nature whatsoever on or with respect to such Property including any Capital Lease Obligation, conditional sale or other title retention agreement having substantially the same economic effect as any of the foregoing or any Sale and Leaseback Transaction.
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> "'Property' means any asset or property of a Person, whether now owned or hereafter acquired, or any interest therein or any income or profits therefrom, including capital stock and indebtedness of Subsidiaries."[3] (*Id.*, § 101.)

Under the Indenture, whether a subsidiary of Embarq is a "Restricted Subsidiary" depends on whether "such Subsidiary has substantially all of its Property in the United States" and whether its value exceeds the specified threshold at the end of a fiscal quarter. (*See id.*) At all times relevant to this dispute, Embarq allegedly had only one Restricted Subsidiary, Brightspeed of Eastern North Carolina, LLC (f/k/a Carolina

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[2] "Outstanding Securities" includes the Embarq Notes. (NYSCEF 47, Indenture § 101 [defining "Outstanding"].)

[3] "'Person' means any individual, Corporation, partnership, limited liability company, joint venture, trust, unincorporated organization or government or any agency or political subdivision thereof." (*Id.*)

Telephone and Telegraph Company LLC). (*See* NYSCEF 107, tr 11;[4] NYSCEF 71, Affidavit of Russ Mincey in Support of Embarq, L.L.C.'s Motion for Summary Judgment, ¶ 5.)

The Indenture defines "Permitted Lien" as, among other things, "(iv) Liens on Property of any entity, or on the stock, indebtedness or other obligations of such entity, existing at the time (a) such entity becomes a Restricted Subsidiary." (NYSCEF 47, Indenture § 101.)

In connection with the issuance of the Embarq Notes, Embarq filed a prospectus, dated May 12, 2006 (the Prospectus), with the United States Securities and Exchange Commission. (NYSCEF 46, JS ¶ 6.) The cover page of the Prospectus advises that "the notes will effectively rank junior to all indebtedness and other liabilities of [Embarq's] subsidiaries." (NYSCEF 49, Prospectus, at 2.) The Prospectus also discloses the following "**Risk Factors Relating to the Notes**":

> "**We may be unable to pay interest on or repay the notes. We will be a holding company and our subsidiaries will have no obligations to the holders of the notes. The debt of our subsidiaries will be effectively senior to the notes.**
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> ". . . Following the spin-off, we will conduct substantially all of our business through our subsidiaries. Our cash flow and, consequently, our ability to pay interest in cash and to service our debt, including the notes, will be dependent upon the cash flow of our subsidiaries and the payment of funds to us by those subsidiaries in the form of loans, dividends or otherwise. . . . Our subsidiaries will be separate and distinct legal entities and will have no obligation, contingent or otherwise, to pay any amounts due on the notes or to make cash available for that purpose. These subsidiaries may use the earnings they generate, as well as their existing assets, to fulfill their own direct debt

[4] Transcript has no line numbers. Parties are reminded to insist on transcripts with line numbers and to cite those line numbers.

> service requirements. . . . Our subsidiaries may incur additional debt. The debt of our subsidiaries will be effectively senior to the notes.
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> "**There are limited restrictive covenants in the indenture governing the notes relating to our ability to incur future indebtedness, pay dividends or engage in other activities, which could adversely affect our ability to pay our obligations under the notes.**
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> "The indenture governing the notes does not contain any financial covenants and contains only limited restrictive covenants. The indenture will not limit our or our subsidiaries' ability to incur additional indebtedness, issue or repurchase securities, pay dividends or engage in transactions with affiliates. We, therefore, may pay dividends and incur additional debt, including secured indebtedness in certain circumstances or indebtedness by, or other obligations of, our subsidiaries to which the notes would be structurally subordinate. Our ability to incur additional indebtedness and use our funds for numerous purposes may limit the funds available to pay our obligations under the notes." (*Id.* at 24-25/166.)[5]

On August 3, 2021, Connect Holding LLC (Connect Holding), an affiliate of funds managed Apollo Global Management, Inc., entered into a purchase agreement with Lumen Technologies, Inc. (Lumen) for the purchase of certain Lumen subsidiaries, including Embarq. (*See* NYSCEF 46, JS ¶¶ 11, 12.) The sale was structured as a leveraged buyout (LBO). (*Id.* ¶18.) Ultimately, Connect Holding's subsidiary, Connect Holdings II LLC (d/b/a Brightspeed) (Brightspeed) acquired Lumen's assets. (*Id.* ¶¶ 11, 12.)

A September 16, 2022 press release described the transaction, in pertinent part, as follows:

> "Brightspeed expects the debt financing to be comprised of approximately $5.465 billion of secured debt, including a

[5] NYSCEF pagination.

> $600 million revolving credit facility, which is expected to be (i) guaranteed by all of Brightspeed's subsidiaries, including Embarq Corporation ('Embarq') and its transferred subsidiaries, and (ii) secured by substantially all of the assets of Brightspeed and its subsidiary guarantors, other than the assets of Embarq and certain subsidiaries of Embarq that are 'restricted subsidiaries' under the indenture governing Embarq's 7.995% senior notes due 2036 (the 'Embarq Notes').
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> "In connection with the Acquisition, Embarq will be acquired by Brightspeed and the Embarq Notes are expected to remain outstanding as obligations of Embarq. The Embarq Notes are not expected to be guaranteed by any of Embarq's subsidiaries (or by Brightspeed or other subsidiaries of Brightspeed) or secured by any assets of Embarq or its subsidiaries (or assets of Brightspeed or other subsidiaries of Brightspeed)." (*Id.*, ¶¶ 13, 14; *see also* NYSCEF 50, September 16, 2022 Press Release at 2.)

On September 21, 2022, the Noteholders' counsel sent a letter to Embarq, addressing the proposed LBO. (NYSCEF 46, JS ¶ 15; NYSCEF 51, September 21, 2022 Letter.) The letter informed Embarq, in pertinent part, that:

> "In exchange for the Embarq Noteholders loaning to the Company approximately $1,485,000,000, with a 30-year tenor, the Company agreed to maintain the Embarq Notes' rank and priority with respect to any other indebtedness of the Company or its Restricted Subsidiaries (as defined in the Indenture). It did so by covenanting and agreeing not to grant any liens, priorities or other preferential rights on any of its or its Restricted Subsidiaries' assets without granting equal and ratable liens and preferential rights to the Embarq Noteholders (the 'Equal and Ratable Covenant').
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> "The Proposed Financing Terms contemplate granting preferential arrangements covered by the Equal and Ratable Covenant. In particular, the lenders and/or noteholders under Credit Facilities, the Revolving Credit Facilities and the New Notes would receive guarantees (the 'Proposed Embarq Guarantees') from all of the Company's subsidiaries, including any Restricted Subsidiaries (the

> 'Proposed Embarq Guarantors'). Granting such guarantees would insert up to $5,465,000,000 of Proposed Acquisition Debt Financing between the Company and the value of its and its Restricted Subsidiaries' assets, and, therefore, the Company's equity in those asset-owning subsidiaries would be massively devalued. As a result, the Embarq Noteholders would go from being first in line to receive payment on the residual equity value of the Proposed Embarq Guarantors, to being second in line to such value behind up to $5,465,000,000 of newly-incurred debt. The Proposed Embarq Guarantees, thus, would make the Proposed Acquisition Debt Financing structurally senior to the Embarq Notes, in that the lenders and/or noteholders under the Proposed Acquisition Debt Financing would be entitled to collect from the ultimate Company assets ahead of the Embarq Noteholders. Accordingly, the Proposed Embarq Guarantees give the lenders and/or noteholders under the Proposed Acquisition Debt Financing 'preference' and 'priority' over the Embarq Notes and the Proposed Embarq Guarantees constitute a 'preferential arrangement' vis-à-vis the Embarq Notes. The Proposed Embarq Guarantees thus fall squarely within the definition of Lien in the Indenture and trigger the protections promised in the Equal and Ratable Covenant.
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> "**Unless the Proposed Embarq Guarantees are issued to the Embarq Notes on an equal and ratable basis, proceeding with the Proposed Financing Terms means that the Company will be in default in its performance under the Indenture and in breach of its covenants.**" (*Id.* at 2-4.)

The letter also states that the Noteholders were still conducting diligence on the proposed liens on Embarq's assets and the assets of certain of its subsidiaries to determine if these violated the Equal and Ratable Covenant. (*Id.* at 3 n 1.)

Embarq asserts that the terms of the LBO's loan documents were altered to provide that the guarantees issued by Restricted Subsidiaries did not exceed the Allowed Basket Amount. (NYSCEF 98, Embarq's Memo of Law in Opposition to

Noteholder's Motion for Summary Judgment at 19/28; *See* NYSCEF 47, Indenture, §1008, at 64.75[6].)

On October 3, 2022, the LBO closed and Brightspeed, Embarq's new parent company, incurred $5.465 billion in secured debt (LBO Debt). (NYSCEF 46, JS ¶¶ 12, 18). Embarq and its subsidiaries did not retain any of the proceeds from the LBO Debt, all of which were paid to the seller. (See NYSCEF 79, Complaint ¶¶ 30-33; NYSCEF 52 First Lien Credit Agreement at 1; NYSCEF 54, Senior Secured Interim Credit Agreement at 1.)

Certain subsidiaries of Brightspeed provided guarantees and granted liens to secure the LBO Debt. (NYSCEF 46, JS ¶ 19.) Specifically, Embarq's Restricted Subsidiary guaranteed the LBO Debt up to the Allowed Basket Amount and Embarq provided an uncapped guarantee for the LBO Debt. (NYSCEF 66, Frederick G. Van Zijl, May 12, 2023 aff ¶27.) Neither granted any liens. (*Id.*) Embarq's remaining subsidiaries provided uncapped guarantees and granted liens on their property to secure the LBO Debt. (*See* NYSCEF 46, JS ¶ 19; *see also* NYSCEF 56 Collateral Agreement (First Lien) §§ 2.01, 3.01; NYSCF 57, Subsidiary Guarantee Agreement (First Lien) § 2; NYSCEF 58, Subsidiary Guarantee Agreement (Bridge) § 2; NYSCEF 56, Collateral Agreement (First Lien) § 5.16, Schedule I [provides that "no Subsidiary that is Embarq or an Embarq Restricted Subsidiary shall be required to become a Pledgor" while the Embarq Notes remain outstanding and does not include Embarq or its Restricted Subsidiary among the list of "Pledgors" securing the LBO Debt]; NYSCEF 57, Subsidiary Guarantee Agreement (First Lien) and NYSCEF 58, Subsidiary

[6] NYSCEF pagination.

Guarantee Agreement (Bridge), § 2(h) [cap "the aggregate amount of the Obligations that are guaranteed by . . . Embarq Restricted Subsidiaries at any time . . . at an amount equal to the Allocated Basket Amount at such time"].) Neither Embarq nor its subsidiaries granted or issued any guarantees or security interests in favor of the Embarq Notes in connection with the LBO Debt. (NYSCEF 46, JS ¶ 20.) However, concerning the guarantee provided by Embarq, the Noteholders admit that it "[does] not implicate the Equal and Ratable Lein Covenant because . . . the Note obligations are already equal and ratable with the Embarq guarantee." (NYSCEF 11, Answer at 20 n 5, response to ¶ 39.)

The Collateral Agreement, which grants the liens to secure the LBO Debt, provides that each "Pledgor" grants a security interest in substantially all its assets, with the exception of "Excluded Property." (NYSCEF 56, Collateral Agreement (First Lien) § 2.01.) "Excluded Property" is defined as, among other things, "(xvi) for so long as the Embarq Notes remain outstanding, any asset or property of Embarq or an Embarq Restricted Subsidiary . . . or any asset or property that would otherwise require the Embarq Notes to be ratably secured by Liens on such assets or property at any time." (*Id.*, § 1.02 [defining "Excluded Property"].)

The Subsidiary Guarantee Agreement (First Lien) and the Subsidiary Guarantee Agreement (Bridge) (together, the "Guarantee Agreements") provide the guarantees for the LBO Debt (*see* NYSCEF 46, JS ¶¶ 18, 21.) Section 2 (h), found in both agreements, provides:

> ". . . no guarantee or other credit support from Embarq or any Embarq Restricted Subsidiary in favor of the Obligations shall be effective hereunder or under any other Loan Document to the extent the effectiveness of such guarantee

> or other credit support would cause a default or event of default under the terms of the Embarq Notes, and any rights and remedies of the Administrative Agent and the other Secured Parties hereunder or under any other Loan Document shall be limited accordingly to give effect to this Section 2(h)." (NYSCEF 57, Subsidiary Guarantee Agreement (1st Lien); NYSCEF 58, Subsidiary Guarantee Agreement (Bridge) § 2 [h].)

On February 6, 2023, the Noteholder Defendants issued to Embarq a notice of default (the Notice of Default) (NYSCEF 46, JS ¶ 22.) It states as follows:

> "The Purchaser financed a portion of the LBO purchase price by borrowing funds (the 'LBO Debt') from certain financial institutions (the 'LBO Lenders'). The undersigned understand that, as credit support for the LBO Debt, the Company and its Subsidiaries granted to the LBO Lenders certain security interests (the 'Embarq Security Interests') and guarantees (the 'Embarq Guarantees').
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> "The undersigned understand that the direct Subsidiaries of the Company issued Embarq Security Interests and Embarq Guarantees in favor of the LBO Lenders. The equity value in each of the Company's direct Subsidiaries constitutes Property of the Company. Any security interest or guarantee issued by the Company's direct Subsidiaries in favor of the LBO Lenders provides the LBO Lenders with a 'preference,' 'priority' and 'preferential arrangement' with respect to such equity value – as well as with respect to the capital stock of such Subsidiaries owned by the Company – and, accordingly, constitutes a Lien. The Company's failure to deliver such a Lien, on an equal and ratable basis, to the Embarq Noteholders is a violation of the Equal and Ratable Covenant.
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> "[T]he undersigned understand that the LBO Lenders have agreed to limit the Embarq Guarantees by the Restricted Subsidiaries as is necessary to cause the Company to be in compliance with the Equal and Ratable Covenant. Premised and contingent upon this understanding and assuming that such agreement by the LBO Lenders is valid and

> enforceable, the undersigned are not, at this time, asserting a default with respect to the Lien granted to the LBO Lenders via the Embarq Guarantees issued by the Restricted Subsidiaries." (NYSCEF 59, Notice of Default at 2-3.)

The parties agreed that Embarq would commence an action "seeking only a declaratory judgment that Embarq is in compliance with the terms of, and has not breached or defaulted under, the Indenture by the issuance of the Embarq Guarantees or the Embarq Security Interests." (NYSCEF 60, March 14, 2023 Agreement between Embarq and Discovery at 1-2.) The Noteholders also agreed to rescind the Notice of Default, provided that, should the court find against Embarq, the Notice of Default would be deemed automatically delivered to Embarq. (*See id.* at 3.) Upon delivery, Embarq would have a 30-day cure period before default under the Indenture. (*See id.* at 4.)

Embarq then commenced this action, seeking declaratory judgment pursuant to CPLR 3001, declaring that:

> "(i) the liens and guarantees provided by Embarq's subsidiaries that are not Restricted Subsidiaries (the "Unrestricted Subsidiaries") are not Liens upon the Property of Embarq or its Restricted Subsidiaries under the Indenture; (ii) a guarantee is not a 'Lien' as that term is defined in the Indenture; (iii) the liens and guarantees from Embarq's Unrestricted Subsidiaries are not subject to the Equal and Ratable Lien Covenant and do not constitute a default under the Indenture; (iv) no liens or guarantees provided under the [LBO] Debt documents constitute a default or Event of Default under the Indenture; and (v) the [LBO] Debt does not trigger a default or Event of Default under any other provision of the Indenture." (NYSCEF 2, Complaint, ¶ 55.)

The Noteholders counterclaimed for: (1) declaratory judgment, seeking a declaration that Embarq breached the Indenture by permitting the direct, wholly-owned subsidiaries of Embarq and its Restricted Subsidiary (the "Direct Subsidiaries") to issue

liens and guarantees in connection with the LBO Debt, thereby giving the LBO Lenders a priority with respect to the Direct Subsidiaries' equity value; (2) breach of contract, seeking damages for breach of the Equal and Ratable Covenant; (3) declaratory judgment, seeking a declaration that, absent a cure of Embarq's default under the Indenture, it must redeem the Embarq Notes; (4) breach of contract, seeking specific performance (i.e. the issuance of adequate guarantees and security interests such that the Embarq Notes become situated and/or secured equally and ratably with the LBO Debt); and (5) breach of the implied covenant of good faith and fair dealing, as an alternative to the breach of contract claims. (*See* NYSCEF 11, Answer at ¶¶34, 44-54.)

II. Analysis

Pursuant to CPLR 3212 (b), "[t]o obtain summary judgment, the movant 'must make a prima facie showing of entitlement to judgment as a matter of law, tendering sufficient evidence to demonstrate the absence of any material issues of fact.'" (*Madeline D'Anthony Enters., Inc. v Sokolowsky*, 101 AD3d 606, 607 [1st Dept 2012], quoting *Alvarez v Prospect Hosp.*, 68 NY2d 320, 324 [1986].) "Failure to make such prima facie showing requires a denial of the motion, regardless of the sufficiency of the opposing papers." (*Alvarez,* 68 NY2d at 324.) Once the movant satisfies its burden, the opposing party must "'produce evidentiary proof in admissible form sufficient to establish the existence of material issues of fact which require a trial of the action.'" (*Madeline D'Anthony Enters., Inc.*, 101 AD3d at 607, quoting *Alvarez*, 68 NY2d at 324.)

A. Declaratory Judgment Cause of Action/Counterclaims and Breach of Contract Counterclaims

Embarq contends that the plain language of the Indenture provides that the Equal and Ratable Covenant unambiguously applies to Liens on the Property of

Embarq and its Restricted Subsidiaries only. It argues that to apply the covenant to Unrestricted Subsidiaries would render the term "Restricted Subsidiaries" superfluous. Embarq also offers the Prospectus and evidence of industry custom and practice as further proof that the Unrestricted Subsidiaries are free to place liens on their property and to issue guarantees. In addition, Embarq argues that guarantees are not "Liens" under the Indenture and, as such, do not breach the Equal and Ratable Covenant. Lastly, Embarq points out that the Collateral Agreement and Guarantee Agreements contain provisions that ensure that no liens or guarantees could be granted in violation of the Indenture.

The Noteholders respond that Embarq's motion should be denied, as its reliance on parol evidence (the Prospectus and an expert opinion on industry custom and practice) undercuts its argument that there are no issues of fact. They also contend that they are entitled to summary judgment on their counterclaims, because: (1) the equity value that Embarq and its Restricted Subsidiary hold in their Direct Subsidiaries constitutes "Property" under the Indenture's expansive definitions of that term; and (2) the Direct Subsidiaries' guarantees and liens granted the LBO Lender priority with respect to the Direct Subsidiaries' equity value, thereby creating Liens on Embarq and the Restricted Subsidiary's Property. In other words, the Noteholders argue, not only does the Equal and Ratable Covenant prohibit Embarq and its Restricted Subsidiary from encumbering the capital stock they hold in their Direct Subsidiaries, it also prohibits them from obtaining the same result indirectly by diverting the equity value of such stock, here, through liens on their property and guarantees securing the LBO Debt. As concerns the savings clauses, the Noteholders argue that these cannot, after the fact,

erase Embarq's breach of the Equal and Ratable Covenant and that, in any event, they do not correct public records.

The parties also dispute whether redemption of the Notes and specific performance are remedies available to the Noteholders under the Indenture.

The interpretation of an unambiguous contract is a question of law for the court (*Ruttenberg v Davidge Data Sys. Corp.*, 215 AD2d 191, 192 [1st Dept 1995]), as is the determination of whether a contract is ambiguous. (*W.W.W. Assoc. v Giancontieri*, 77 NY2d 157, 162 [Ct App 1990].) "[L]anguage in a contract is unambiguous if it has a definite and precise meaning, unattended by danger of misconception in the purport of the [agreement] itself, and concerning which there is no reasonable basis for a difference of opinion." (*Wachter v Kim*, 82 AD3d 658, 662 [1st Dept 2011] [internal quotation marks and citations omitted].) "Where the terms of a contract are clear and unambiguous, the intent of the parties must be found within the four corners of the contract, giving a practical interpretation to the language employed and reading the contract as a whole." (*Georgia Malone & Co., Inc. v E&M Assoc.*, 163 AD3d 176, 185 [1st Dept 2018] [internal quotation marks and citations omitted].) "It is also important to read the document as a whole to ensure that excessive emphasis is not placed upon particular words or phrases" (*South Rd. Assoc., LLC v International Bus. Machs. Corp.*, 4 NY3d 272, 277 [Ct App 2005] [internal citation omitted]) and to "give effect to each and every part, so as not to render any provision meaningless or without force or effect." (*Western & S. Life Ins. Co. v U.S. Bank N.A.*, 209 AD3d 6, 13 [1st Dept 2022] [internal quotation marks and citations omitted].) Lastly, "[a] contract should not be interpreted to produce a result that is absurd, commercially unreasonable or contrary to the

reasonable expectations of the parties." (*Matter of Lipper Holdings v Trident Holdings*, 1 AD3d 170, 171 [1st Dept 2003] [internal citations omitted], *appeal denied*, 2004 N.Y. App. Div. LEXIS 1625 [1st Dept 2004].)

Here, the Equal and Ratable Covenant unambiguously applies to Embarq and its Restricted Subsidiaries only. The Noteholders' attempt to expand its reach to Unrestricted Subsidiaries, through an overbroad reading of "Property" and "Lien," is unpersuasive.

First, contrary to the Noteholders' contentions, the definition of "Property" does not encompass the equity value of Embarq and its Restricted Subsidiary's interests in their Direct Subsidiaries. The Indenture defines "Property" to include "*any* asset or property. . . , whether now owned or hereafter acquired, or *any interest therein* or any income or profits therefrom, *including* capital stock and indebtedness of Subsidiaries." (NYSCEF 47, § 101 [emphasis added].) While "the word 'include' is generally a term of enlargement and not of limitation," it also "connot[es] an illustrative application of a general principle." (*Empire Mut. Ins. Co. v Applied Sys. Dev. Corp.*, 121 AD2d 956, 960 [1st Dept 1986].) Here, the illustrative examples (capital stock and a subsidiary's loan obligations to the parent) have some tangible aspect. In other words, they are things that can be encumbered or conveyed. Similarly, "income or profits" share this trait. This reading is supported by the use of "Property" in other parts of the Indenture. In defining "Lien," "Permitted Liens," "Restricted Subsidiary" and "Sale and Leaseback Transaction," it is clear that the Indenture is concerned with "Property" that can be "pledge[d]," "encumber[ed]," "acqui[red]," "attach[ed]" located "in the United States" and "sold or transferred." (*See* NYSCEF 47, Indenture at 5, 7-8, 9.) Equity value, which is

"the difference in value between a business entity's assets and its liabilities" (Black's Law Dictionary [11th ed 2019], owners' equity), does not fit within this definition of Property. Thus, viewing the definition of "Property" "in the light of the obligation as a whole and the intention of the parties as manifested thereby," (*Georgia Malone & Co., Inc.*, 163 AD3d at 185 [internal quotation makes and citations omitted]), without undue emphasis on any single word or phrase (*South Rd. Assoc., LLC*, 4 NY3d 272 at 277), the Indenture clearly and consistently uses the term "Property" to refer to various types of assets and not the equity value of those assets. (*See Giray*, 212 AD3d 439 at 440-441 [stating that "when . . . the parties us(e) a certain word or expression in different parts of (the instrument), it is reasonable to suppose that it was always used in the same sense," and " [a]lthough the words might seem to admit of a larger sense, . . . they should be restrained to the particular occasion and to the particular object which the parties had in view" [internal quotation marks and citations omitted].) In *Giray*, the court rejected an interpretation of a word that was contrary to the parties' reasonable expectations, made clear by the repeated use of the word in the document. (*Id.*)

Second, the Noteholders' reading of "Lien" would "produce a result that is absurd, commercially unreasonable or contrary to the reasonable expectations of the parties." (*Matter of Lipper Holdings*, 1 AD3d 170 at 171 [internal citations omitted].) As a preliminary matter, the Indenture defines "Lien" as something "with respect to any Property of any Person." (NYSCEF 47, Indenture § 101.) As discussed above, equity value is not "Property" under the Indenture. Therefore, a preferential arrangement with respect to equity value is, by definition, not a "Lien." Additionally, the Noteholders readily admit that they take issue with this transaction only because none of the

subsidiaries retained any of the proceeds from the LBO Debt, which negatively impacted the equity value that Embarq and its Restricted Subsidiary hold in their Direct Subsidiaries. (*See* NYSCEF 107, tr at 47, 55-56.) Thus, the Noteholders would treat the same lien granted by a subsidiary on its property differently depending on its impact on the equity value of Embarq's interest in that subsidiary. Nothing in the language of the Equal and Ratable Covenant, or the Indenture generally, supports this outcome-based approach to determining whether a lien is a "Lien." Additionally, the definition of "Permitted Liens" indicates that the parties intended for subsidiaries to be able to encumber their Property with Liens prior to becoming Restricted Subsidiaries. (*See* NYSCEF 47, Indenture § 101 [defining "Permitted Liens" to include "Liens on Property of any entity, or on the stock, indebtedness or other obligations of such entity, existing at the time (a) such entity becomes a Restricted Subsidiary"].) Finally, the Noteholders' approach disregards "[a] basic tenet of American corporate law . . . that the corporation and its shareholders are distinct entities. . . . A corporate parent which owns the shares of a subsidiary does not, for that reason alone, own or have legal title to the assets of the subsidiary . . ." (*Dole Food Co. v Patrickson*, 538 US 468, 474-475 [2003] [internal citations omitted].) The Noteholders would obliterate this distinction anytime a subsidiary's disposition of its property had a negative impact on the value of its stock. Accordingly, the court must reject the Noteholder's interpretation of "Lien." (*See Matter of Lipper Holdings*, 1 AD3d at 171; *see Giray*, 212 AD3d at 440.)

Ultimately, the Noteholder's interpretation of the Equal and Ratable Covenant is problematic because, at its core, it disregards that the covenant expressly limits its scope to "[t]he Company" and "any Restricted Subsidiary." (NYSCEF 47, Indenture

§1008.) In seeking to control the conduct of the Direct Subsidiaries, the Noteholder would render this limitation superfluous, an outcome that must be avoided in contract construction. (*See Western & S. Life Ins. Co. v U.S. Bank N.A.*, 209 AD3d at 13.)

To the extent that Embarq seeks a declaration that a guarantee is not a "Lien," as that term is defined in the Indenture, the motion is denied. "The general purpose of the declaratory judgment is to serve some practical end in quieting or stabilizing an uncertain or disputed jural relation either as to present or prospective obligations." (*Thome v Alexander & Louisa Calder Found.*, 70 AD3d 88, 99 [1st Dept 2009], *leave to appeal denied by* 2010 N.Y. LEXIS 1383 [Ct App 2010] [internal quotation marks and citations omitted].) Here, the above determination fully resolves all disputes as to the guarantees issued by the Unrestricted Subsidiaries, and the Noteholders do not challenge the guarantees issued by Embarq or its Restricted Subsidiary. (*See* NYSCEF 11, Answer at 20 n 5, response to ¶ 39; NYSCEF 59, Notice of Default at 2.)

In light of the foregoing, the court does not address the parties' remaining contentions.

Accordingly, Embarq's motion for summary judgment is granted to the extent the claim for declaratory judgment seeks a declaration that the liens and guarantees provided by Embarq's Unrestricted Subsidiaries are not Liens upon the Property of Embarq or its Restricted Subsidiaries under the Indenture, are not subject to the Equal and Ratable Covenant and do not constitute a default under the Indenture. The Noteholders' motion for summary judgment on their declaratory judgment counterclaims is, accordingly, denied. Summary judgment is also denied with respect to their breach of contract counterclaims, which allege breach of the Equal and Ratable Covenant. As

there is no basis to sustain these counterclaims, summary judgment is granted in favor of Embarq, dismissing counterclaims one through four. (CPLR 3212 [b].)

B. Breach of the Implied Covenant of Good Faith and Fair Dealing Counterclaim

The Noteholders contend that because Embarq is the sole obligor on the Notes and has no capital assets of its own, a "reasonable person would understand the Indenture to include a covenant that Embarq would not interfere with or attempt to undermine the Embarq Notes' rank and priority with respect to equity value in the Direct Subsidiaries held by Embarq." (NYSCEF 83, Embarq's Memo of Law at 19.) Embarq responds that the claim is duplicative of the breach of contract counterclaims.

"In New York, all contracts imply a covenant of good faith and fair dealing in the course of performance," meaning 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." (*511 W. 232nd Owners Corp. v Jennifer Realty Co.*, 98 NY2d 144, 153 [Ct App 2002] [internal quotation marks and citations omitted].)

> "[The Court of Appeals] has consistently observed that the covenant requires the parties to perform under the contract in a reasonable way. In discerning what is 'reasonable,' the Court looks to what the parties would have expected under the contract: the Court will infer that contracts include any promises which a reasonable person in the position of the promisee would be justified in understanding were included at the time the contract[s] [were] made. No obligation can be implied, however, which would be inconsistent with other terms of the contractual relationship." (*Cordero v Transamerica Annuity Serv. Corp.*, 39 NY3d 399, 409-410 [Ct App 2023] [internal quotation marks and citations omitted].)

Here, as explained above, the Equal and Ratable Covenant expressly limits its reach to Embarq and its Restricted Subsidiaries. (NYSCEF 47, Indenture §1008.) It

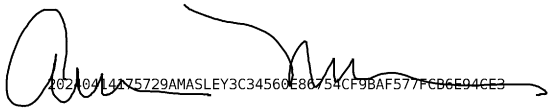
does not limit the Unrestricted Subsidiaries' ability to encumber or dispose of *their* property. As such, there can be no reasonable expectation that this right is implied when it was expressly omitted from the Indenture. (*See Cordero*, 39 NY3d at 410.) The Prospectus expressly advises that Embarq's subsidiaries have no obligation to repay the Embarq Notes and are free to grant liens on their property, which may result in the subordination of the Notes. (*See* NYSCEF 49, Prospectus at 21-22.) Contrary to the Noteholders' contentions, nothing in the Prospectus indicates that these disclosures relate to "ordinary course lending transactions, i.e., where the entity that incurs the indebtedness receives the borrowed proceeds." (NYSCEF 100, Embarq Noteholders' Memo of Law in Opposition to Embarq LLC's summary Judgment Motion at 13.) The Prospectus is silent on this subject. As the Noteholders cannot demonstrate a justified belief that the Equal and Ratable Covenant would limit the ability of Unrestricted Subsidiaries to issue liens on their property, the Noteholders' motion for summary judgment on the fifth counterclaim must be denied and the counterclaim dismissed. (*See Alvarez,* 68 NY2d at 324; CPLR 3212 [b].)

Accordingly, it is

ORDERED that plaintiff Embarq, L.L.C.'s motion for summary judgment on its first cause of action and a declaratory judgment with respect to the subject matter of that cause of action is granted; and it is further

ADJUDGED and DECLARED that the liens and guarantees provided by Embarq, LLC's Unrestricted Subsidiaries: are not Liens upon the Property of Embarq, LLC or its Restricted Subsidiaries under the Indenture; are not subject to the Equal and Ratable Covenant; and do not constitute a default under the Indenture; and it is further

ORDERED that defendants Capital Research and Management Company and Discovery Capital Management, LLC's motion for summary judgment is denied and their counterclaims are dismissed in their entirety.



4/14/2024
DATE

ANDREA MASLEY, J.S.C.

CHECK ONE:	X	CASE DISPOSED			NON-FINAL DISPOSITION		
		GRANTED		DENIED	X	GRANTED IN PART	OTHER
APPLICATION:		SETTLE ORDER				SUBMIT ORDER	
CHECK IF APPROPRIATE:		INCLUDES TRANSFER/REASSIGN				FIDUCIARY APPOINTMENT	REFERENCE