

ENGLISH HIGH COURT, APPLYING NEW YORK LAW, DETERMINES THAT ORION SECURITY AGREEMENT DOES NOT GIVE SENIOR CREDITORS THE RIGHT TO SPECIFY THE TIME, PLACE AND MANNER OF SALE OF SIV COLLATERAL

The English High Court of Justice, applying New York law, has decided that, in the absence of provisions in a security agreement providing for an express right of senior creditors to direct the security trustee with respect to the time, manner and place of a disposal of the assets of a structured investment vehicle, such a right shall not be read into such security agreement, and the security trustee shall be required to determine how such assets should be disposed of in accordance with the terms of the security agreement and the rights and obligations of a security trustee under New York law.

In *The Bank of New York v Montana Board of Investments and others* ([2008] EWHC 1594 (Ch)), the Chancery Division of the English High Court of Justice applied New York law regarding the interpretation of written contracts and the rights and obligations of a security trustee. The Bank of New York, as security trustee, sought a determination with respect to various issues that were the subject of a dispute between the holders of senior notes issued by Orion Finance Corporation, a structured investment vehicle incorporated in the Cayman Islands, and the holders of Orion's subordinated notes. Following the occurrence of certain defaults, the holders of the senior notes had directed the security trustee to commence the liquidation of the assets of Orion serving as collateral for Orion's notes, and the holders of the subordinated notes responded by directing the security trustee to refrain from doing so.

The security trustee requested that the court provide a decision regarding the construction of Orion's security agreement with respect to, *inter alia*, (1) whether the security agreement provided the senior creditors with the right to direct the security trustee regarding the time, place and manner of the sale of Orion's assets and (2) whether the security agreement mandated any specific timing for the liquidation of the collateral securing the notes upon the occurrence of a "Mandatory Acceleration Event" – in this case, an "Insolvency Event" arising from Orion's failure generally to pay its debts as they became due.

In the absence of an express right of the senior creditors to so direct the security trustee, and making reference to New York principles of law that "[a] contract is to be interpreted so as to give effect to the intention of the parties as expressed in the words of the written agreement" and that a security trustee "is not the mere agent of the creditors, but is required to exercise a discretion," the court ruled that the security agreement did not give the senior creditors the right to specify the time, place and manner of the sale of collateral.

With respect to whether the security agreement set forth any specific timing for the disposal of the collateral in the absence of any ability of the senior creditors to provide such direction, the court ruled that in the absence of any express provision in the security agreement in relation to the timing of liquidation upon a Mandatory Acceleration Event, the security trustee should conduct any sale of the collateral in accordance with the provisions of the security agreement regarding a sale of collateral upon the occurrence of an "Enforcement Date," noting that a Mandatory Acceleration Event can only occur

when an Enforcement Date has occurred. These provisions indicated that the security trustee “shall have the exclusive right to exercise any and all rights with respect to the Collateral,” “shall sell, assign and deliver ... the Collateral at such place or places as the Security Trustee deems best,” and that “[a]ny sale shall be conducted in a commercially reasonable manner.”

In rejecting the senior creditors’ claim that a sale should proceed as soon as reasonably practicable, the court relied upon Article 9-610(b) of the New York Uniform Commercial Code, to the effect that “[e]very aspect of a disposition of collateral, including the method, manner, time, place and other terms, must be commercially reasonable” The court also noted, in its description of the duties of a security trustee under New York law, the official comment to Article 9-610 that the article does not specify a particular time frame for the disposal of collateral, further noting (in the context of the lack of liquidity in the structured products markets) the example set forth in the official comment that it may be prudent not to dispose of goods when the market for such goods has collapsed.

At the same time, the court stated that the security trustee “does not enjoy anything approaching an unfettered discretion” in enforcing upon the collateral. It emphasized the full subordination of the senior subordinated notes, that the purpose of the security interest was to ensure prompt payment of the notes when due, and that all the senior creditors had resolved that the security trustee should enforce the security.

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