BONY v. Liberty Media: Delaware Supreme Court Finds that a "Disaggregation Strategy" Does Not Constitute a Sale of "Substantially All" of a Company's Assets for Indenture Covenant Purposes

On a matter of first impression, the Delaware Supreme Court applied New York law to affirm that a series of individual decisions, made over several years, to transfer a large portion of company assets did not constitute a disposition of "substantially all" of the company's assets, and thus did not violate the successor obligor provision contained in an issuer's debt indenture (the "Indenture"). The September 21, 2011 decision, *Bank of New York Mellon Trust Company, N.A. v. Liberty Media Corp.*, cleared the way for Liberty Media Corporation ("Liberty") to split off two of its businesses into a new, publicly traded company without triggering an event of default under the Indenture.[1]

I. Facts and Procedural History

Liberty grew out of efforts to deconsolidate the telecommunications industry. Tele-Communications, Inc. ("TCI") created Liberty in 1991, in response to the prospect of Congress regulating joint ownership of programming and cable systems. By 1998, AT&T acquired both TCI and Liberty, and Liberty was allowed to operate autonomously, as a wholly owned AT&T subsidiary. In 1999, Liberty entered into the Indenture under which it issued, over time, a total of about $13.7 billion in debt. Approximately $4.2 billion in debt remained outstanding under the Indenture when this case arose. The Indenture contained a rather standard "successor obligor covenant," which prohibited Liberty from disposing of "all or substantially all of its assets and [] properties and the assets and properties of its Subsidiaries (taken as a whole) to any entity or entities," unless the acquiring entity assumed Liberty's obligations under the Indenture. The Indenture was governed by New York law.

In 2001, AT&T split off Liberty completely, enabling it to trade as a public company. The company that emerged from AT&T held a range of minority equity positions. Given complete independence, Liberty management set out to acquire controlling stakes in synergistic businesses, and dispose of assets where they could not obtain control or envision substantial increases in value for the benefit of Liberty's shareholders (a "disaggregation strategy"). For example, Liberty acquired a major international cable operation, which it split off in 2004 into Liberty Media International, Inc. ("LMI"). The same year, Liberty sought, in the alternative, either a takeover or initial public offering for Discovery, the cable television channel company, based on Liberty's minority position in Discovery. When both of those efforts were rejected by Discovery's majority owners, Liberty dividended its Discovery shares to Liberty stockholders. In 2009, Liberty split off its interest in DirecTV into a new entity, Liberty Entertainment, Inc. ("LEI"). In public statements, Liberty's chairman explained that the company's motivating "philosophy" was to "disaggregate in order to consolidate."

Liberty continued this strategy through 2010, when it sought to split off many of its entertainment properties -- including the Atlanta Braves, Starz Media, Starz Entertainment, Liberty Sports Interactive, True Position and a stake in Sirius XM -- into a new public entity. After the proposed split-off of those businesses, Liberty would retain QVC, the home shopping channel, and several e-commerce businesses, which were organized within Liberty's Interactive Group. The parties in the case did not dispute that the proposal, like the LMI transaction, the Discovery dividend or the LEI transaction, would not in and of itself constitute a disposition of "substantially all" of Liberty's assets and properties under the Indenture. However, an anonymous bondholder threatened, through an attorney letter, to declare an event of default under the theory that when considered on a

[1] *Bank of New York Mellon Trust Company, N.A. v. Liberty Media Corp.,* 2011 WL 4376552 (Del. Sup. Ct. Sept. 21, 2011).

cumulative basis, the three split-off transactions since 2004 and the proposed split-off would constitute the disposition of substantially all company assets and properties for purposes of the Indenture's successor obligor covenant. Liberty responded by bringing an action against the Trustee under the Indenture, seeking injunctive relief and a declaratory judgment that the proposed split-off would not trigger the Indenture covenant.

After a trial, the Delaware Court of Chancery held that the four transactions should not be considered on a collective basis, since each resulted from "a distinct and independent business decision," separated from others by years, and without any "master plan to strip Liberty's assets out of the corporate vehicle subject to bondholder claims."[2] The Court also applied the "step-transaction doctrine" to reach its decision.[3]

The Trustee appealed. Both parties also requested a decision within one week of oral argument, which prevented the Delaware Supreme Court from following its usual practice of certifying questions of first impression under New York law to the New York Court of Appeals.

II. The Delaware Supreme Court's Decision

The Delaware Supreme Court affirmed the Court of Chancery's decision, and incorporated its application of the closest case on point, *Sharon Steel Corp. v. Chase Manhattan Bank, N.A.*[4] In that case, the Second Circuit analyzed a series of "piecemeal" transactions cumulatively for a "substantially all" determination, because they were part of a single, "overall scheme to liquidate."[5] The Second Circuit had noted that selling assets "in the regular course of business" to "strengthen the corporation," by contrast, would not trigger a cumulative analysis of whether "substantially all" assets are in play. Drawing on *Sharon Steel* and other cases, the Supreme Court stated the general rule that courts do not aggregate where transactions are "not piecemeal components of an otherwise integrated, pre-established plan to liquidate . . . nearly all assets," *and* each transaction "stands on its own merits without reference to another."[6]

The Supreme Court stated that the Court of Chancery was right to apply *Sharon Steel* by assessing whether Liberty had a master scheme to liquidate its assets or avoid claims from bondholders. The Supreme Court also agreed with the lower court's finding that no such scheme existed, since the series of transactions fit with Liberty's post-AT&T strategy of consolidating business ownership where a path to control existed, and exiting positions where no path or compelling upside was available.

The Supreme Court declined to endorse the Court of Chancery's additional analysis, however, which sought to provide a general standard for determining when a series of transactions *should* be aggregated applying the "step transaction doctrine".[7] The Supreme Court concluded that it was not necessary to determine whether the New York Court of Appeals would apply the step transaction doctrine generally in deciding cases of this type.[8]

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[2] *Bank of New York Mellon Trust Company, N.A. v. Liberty Media Corp.,* WL 1770298 (Del. Ch. April 29, 2011).

[3] The "step transaction doctrine" treats the "steps" in a series of formally separate but related transactions involving the transfer of property as a single transaction, if all the steps are substantially linked. In making such an analysis, courts will look to whether the series of transactions were pre-arranged; whether the steps were legally interdependent on one another; and whether at the time the first step was entered into, there was a binding commitment to undertake the later steps. Id. at 33-34.

[4] *Sharon Steel Corp. v. Chase Manhattan Bank, N.A.*, 691 F.2d (2nd Cir. 1982).

[5] Id. at 1050.

[6] Id. at 30.

[7] *Noddings Inv. Grp., Inc. v Capstar Commc'ns, Inc.*, 1999 WL 182568 (Del. Ch. Mar. 24, 1999), aff'd 741 A.2d 16 (Del. 1999) (applying the step-transaction doctrine to determine whether a spinoff and merger should be considered together

III. Boilerplate Provisions Require Uniform Interpretation

The Supreme Court also emphasized that "successor obligor provisions in bond indentures consist of market-facilitating boilerplate language," and courts aim to apply the plain terms of "such provisions in a uniform manner to promote market stability."[9] The Court noted that because boilerplate provisions are not the product of the relationship between particular borrowers and lenders, or their specific goals, courts look to the common purposes of such provisions and not the parties' intent.[10] In this case, the Supreme Court found that the Court of Chancery had properly recognized the boilerplate character of the Indenture's successor obligor provision, and correctly emphasized the importance of uniform interpretation.

IV. Motive Over Math

The Delaware Supreme Court's opinion did not use any quantitative analysis to measure whether Liberty's disposition transactions constituted "substantially all" of its assets or properties. Quantitative analyses of assets, earnings and other financial measures has been part of other courts' consideration in cases in which the scope of the term "substantially all" was considered.[11] The fact that the Supreme Court did not do so here may simply reflect the sequencing of its analysis; that is, having rejected the aggregation theory, the court did not find it necessary to analyze any financial quantitative measures to find the proposed transfer did not constitute "substantially all" of Liberty's assets or properties.

Thus, for companies surveying the landscape after *Liberty Media*, the case is a reminder that a "substantially all" analysis is remarkably fact-intensive, and in construing the facts of a particular case, courts may give greater weight to an issuer's business intentions than to quantitative measures.

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Helene Banks at 212.701.3439 or hbanks@cahill.com; Charles A. Gilman at 212.701.3403 or cgilman@cahill.com; Jon Mark at 212.701.3100 or jmark@cahill.com; or John Schuster at 212.701.3323 or jschuster@cahill.com.

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under an adjustment provision of a warrant governed by New York law).

[8]The Indenture covenant did contain language that in order to comply with the covenant there be no default or event of default following completion of the "transaction or series of transactions" being analyzed. However, the Supreme Court did not accept the argument that such language was meant to apply to the kind of separate transactions that Liberty effected. Rather, the Court held that clause was merely included to "underscore that a disposition of 'substantially all' assets may occur by way of a single transaction or an integrated series of transactions, as occurred in *Sharon Steel*." Id. at 37-38.

[9] Id. at 36 (citing *Wilmington Trust Co. v. Tropicana Entm't, LLC*, 2008 WL 555914 (Del Ch. Feb. 29, 2008).

[10] Id. at 36 and following.

[11] See, *Bank of New York v. Tyco International Group, S.A.* 545 F. Supp.2d 312 (S.D.N.Y.2008) and *B.S.F. Company v. Philadelphia National Bank*, 204 A2d 746 (Del. 1964).

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