IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

CYPRESS ASSOCIATES, LLC,	)	
	)	
Plaintiff,	)	
	)	
v.	)	C.A. No. 1607-N
	)	
SUNNYSIDE COGENERATION ASSOCIATES PROJECT, SUNNYSIDE HOLDINGS I, INC. and SUNNYSIDE II, L.P.,	)	
	)	
Defendants.	)	

MEMORANDUM OPINION

Date Submitted: November 7, 2006
Date Decided: January 17, 2007

William M. Lafferty, Esquire, Samuel T. Hirzel, Esquire, Lisa Whitaker, Esquire, MORRIS, NICHOLS, ARSHT & TUNNELL, LLP, Wilmington, Delaware, *Attorneys for Plaintiff.*

Donald J. Wolfe, Jr., Esquire, Michael A. Pittenger, Esquire, Berton W. Ashman, Jr., Esquire, POTTER ANDERSON & CORROON LLP, Wilmington, Delaware; David Clarke, Jr., Esquire, James D. Mathias, Esquire, DLA PIPER RUDNICK GRAY CARY US LLP, Baltimore, Maryland, *Attorneys for Defendants.*

STRINE, Vice Chancellor.

I. Introduction

The plaintiff in this case, Cypress Associates, LLC ("Cypress"), owns a large amount of Series B Bonds backed by the assets and profits of a business that runs a power plant in Utah. The defendants are the business, nominal defendant Sunnyside Cogeneration Associates Project, which I shall call the "Project," and the Project's controlling stockholders, defendants Sunnyside Holdings, I, Inc. and Sunnyside Holdings, II, L.P. (collectively, the "Controller").

There are two disputes between the Controller and Cypress. The first (the "Base Amount Dispute") involves the manner in which the interest on the Series B Bonds is calculated. The Series B Bonds are hybrid investment instruments with some very equity-like features. The interest due on them each year is a function of the income earned by the Project that year — the Series B are entitled to one-half of the Project's gross revenue after certain expenditures are deducted. Cypress claims that the Controller has been improperly duplicating certain deductions from its gross revenue. The result is that the Series B Bondholders have been denied interest to which Cypress claims the Series B Bondholders are rightfully entitled. Cypress has sued, asking this court to declare its interpretation of the contract provision governing the interest calculation correct and to award it the interest to which it is entitled for the years in question.

The second dispute (the "PPA Amendment Dispute") involves the Controller's attempt to amend one of the Project's material contracts, a Power Purchase Agreement between the Project and one of its customers (the "PPA"). Cypress has sued to prevent the Controller from implementing the Amendment. In my March 8, 2006 opinion in this case

denying the Controller's motion to dismiss, I concluded that pursuant to the unambiguous terms of a loan agreement, of which Cypress is a third-party beneficiary, the Controller could not implement the Amendment without the support of 80% of the Bondholders.[1] Because Cypress owns more than 20% of the Bonds, its refusal to consent denied the Amendment the level of support necessary for it to pass. But under the terms of the loan agreement, the Bondholders' consent must not be unreasonably withheld. The Controller now claims that Cypress has unreasonably withheld consent and, as a result, it should be permitted to implement the Amendment.

Cypress has moved for judgment on the pleadings under Court of Chancery Rule 12(c), asking this court to decide both the Base Amount Dispute and the PPA Amendment Dispute in its favor. The Controller has filed a cross motion for judgment on the pleadings with respect to the Base Amount Dispute but claims that a factual issue regarding the reasonableness of the Cypress's refusal to consent precludes the entry of judgment on the pleadings in the PPA Amendment Dispute.

As to the Base Amount Dispute, I find that the contract language governing the calculation of the Series B interest is ambiguous and that, as a practical commercial matter, neither of the disparate interpretations presented to me by the parties is the obviously correct reading. A fact issue remains regarding the original intent of the parties. I therefore deny both parties' motions for judgment on the pleadings.

[1] See *Cypress Associates, LLC v. Sunnyside Cogeneration Associates Project*, 2006 WL 668441, at *8 (Del. Ch. 2006).

As to the PPA Amendment Dispute, the Controller is correct that, ordinarily, a well-pled allegation that Cypress unreasonably withheld consent would raise a factual issue and preclude entry of judgment on the pleadings. But the argument that the Amendment should be deemed effective because Cypress's refusal to consent was unreasonable constitutes an affirmative defense that must be supported by pled facts and the Controller's answer does not plead facts sufficient to withstand a Rule 12(c) motion. The facts on which the Controller bases its unreasonably withheld contention — primarily that Cypress has unreasonably withheld consent solely to gain negotiating leverage in the Base Amount Dispute — appear for the first time in its briefing on this motion.

If the Controller's pleading defects were in a complaint instead of an answer, those defects, coupled with its decision to stand on its pleading in the face of a motion attacking the pleading's sufficiency, would be fatal to the Controller's case.[2] But Court of Chancery Rule 15(aaa) does not apply to this situation and the interests of justice require me to permit the Controller to amend its answer to include the facts it recited in its brief. That relief, however, is conditioned on the Controller's obligation to reimburse Cypress for the unnecessary costs, including attorneys' fees, that it incurred in bringing the PPA Amendment portion of its motion only to be faced by an unreasonably late request to amend.

[2] Court of Chancery Rule 15(aaa); *see also Griffin Corporate Services LLC v. Jacobs*, 2005 WL 2000775, at *4 & n.24 (Del. Ch. 2005) (dismissing the plaintiff's complaint and denying leave to amend under Rule 15(aaa) even though the plaintiff's briefs contained facts to support its claim).

II. The Procedural Framework And The Opinion's Structure Of Analysis

The Base Amount Dispute and PPA Amendment Dispute both come before me on a motion for judgment on the pleadings. Each Dispute therefore implicates the same procedural standard. Moreover, each Dispute involves the interpretation of a contract governed by Utah law. But the facts and legal analysis relevant to resolving the two Disputes are distinct and easier to follow if digested into two separate courses. Therefore, the decision is structured in that manner.

I begin with a description of the Bonds involved in these disputes. After I lay out that basic background, I turn to the Base Amount Dispute and then to the PPA Amendment Dispute.[3] But first, I will briefly set forth the procedural standards and principles of contract interpretation relevant to both Disputes.

In ruling on a Rule 12(c) motion, I am required to view the facts pled and the inferences to be drawn from them in the light most favorable to the non-moving party.[4] I am not, however, required to accept as true conclusory assertions unsupported by specific factual allegations.[5] In moving for judgment on the pleadings, a litigant impliedly admits the truth of its adversary's well-pled allegations and the falsity of its own assertions that have been denied by the adversary.[6] If, after these principles are applied, I conclude that

[3] The factual recitations are drawn from the pleadings and the exhibits to the pleadings, in accordance with Rule 12(c).
[4] *Desert Equities, Inc. v. Morgan Stanley Leveraged Equity Fund, II, L.P.*, 624 A.2d 1199, 1205 (Del. 1993).
[5] *H-M Wexford LLC v. Encorp, Inc.*, 832 A.2d 129, 139 (Del. Ch. 2003).
[6] 5C C. WRIGHT & A. MILLER, FEDERAL PRACTICE AND PROCEDURE § 1368 at 230 (3d ed. 2004).

there is no material question of fact and the movant is entitled to judgment as a matter of law, I must grant the motion.[7]

In resolving this motion, I am also forbidden from considering any facts other than those alleged in the pleadings, except that I may consider the unambiguous terms of exhibits attached to the pleadings and those incorporated into them by reference.[8]

These Disputes involve the various documents that set forth the rights and obligations of the parties. The parties agree that Utah contract law principles apply. Utah law instructs courts to look to the objectively demonstrated intent of the parties by interpreting unambiguous contracts according to the plain meaning of the language within the four corners of the contract.[9] But if that language is reasonably capable of being understood in more than one sense, it is ambiguous,[10] and the court must look to extrinsic evidence to determine the intentions of the parties.[11] In that instance, it is

---

[7] *Desert Equities*, 624 A.2d at 1205.

[8] *OSI Systems, Inc. v. Instrumentarium Corp.*, 892 A.2d 1086, 1090 (Del. Ch. 2006). In briefing these motions regarding the Base Amount Dispute, the parties have presented documents to the court that are not attached to, or incorporated by reference into, the pleadings. Ordinarily, in these circumstances, a trial court is instructed to treat the motion as one for summary judgment. *See* Court of Chancery Rule 12(b) ("If . . . matters outside the pleading are presented to and not excluded by the Court, the motion shall be treated as one for summary judgment and disposed of as provided in Rule 56 . . . ."). Before a motion for summary judgment is ripe for decision, however, the non-movant normally should have an opportunity for some discovery. *See In re Santa Fe Pac. Corp. S'holder Litig.*, 669 A.2d 59, 69 (Del. 1995); Court of Chancery Rule 12(b) ("[A]ll parties shall be given reasonable opportunity to present all material made pertinent to [a summary judgment motion] by Rule 56."). Because the parties have not had a full opportunity to conduct discovery in this case, it would be improper to convert these motions to summary judgment motions. Further, because the additional materials presented to me would not, outside the fuller context that a discovery record would afford, alter my conclusions, I simply ignore them in ruling on these Rule 12(c) motions.

[9] *Dixon v. Pro Image, Inc.*, 987 P.2d 48, 52 (Utah 1999).

[10] *Id*.

[11] *Central Florida Investments, Inc. v. Parkwest Associates*, 40 P.3d 599, 605 (Utah 2002);

generally improper to grant a motion for judgment on the pleadings because to do so would resolve the ambiguity on an incomplete record not shaped by discovery.[12]

III. The Bonds

The Bonds trace their origins to a 1987 municipal bond issuance by Carbon County, Utah (the "County") to finance the construction of a local solid waste disposal facility (the "Facility"). The County itself did not intend to build or operate the Facility. Rather, by issuance of the tax-exempt 1987 Bonds, it sought to obtain favorable financing terms to facilitate construction of the Facility by a private for-profit entity. The County loaned the bond proceeds to Sunnyside Power Corporation ("Sunnyside Power"), to build the Facility. The loan was accomplished through a loan agreement dated December 1, 1987 (the "Loan Agreement"). The County retained very limited rights and obligations with respect to the Bonds. Sunnyside Power took on most of those rights and responsibilities — it alone had a duty to repay the Bondholders. If Sunnyside Power defaulted, there was to be no recourse against the County.

The Bonds were refinanced a number of times between 1987 and 1999. At some point during that time, the Project, a Utah Joint Venture, took over the Facility and assumed Sunnyside Power's debt obligations. The Bonds at issue in this lawsuit arose

[12] I sidestep for now a debate about Utah's law of contract interpretation. Cypress argues that Utah law follows the traditional rule that if the language within the four corners of the contract is unambiguous, the parties' intentions are determined without resort to parol evidence. It cites for that proposition *Wagner v. Clifton*, 62 P.3d 440, 442 (Utah 2002). In contrast, the Controller argues that Utah requires the court to review the parol evidence before determining that a contract is unambiguous, citing *Ward v. Intermountain Farmers Ass'n.*, 907 P.2d 264, 268 (Utah 1995). Whether this is actually an unsettled debate in Utah is a question I do not answer because I need not. Because I ultimately find that the Indenture is ambiguous on its face, I must consider parol evidence to reach a final resolution, even under a more traditional approach to contract interpretation.

out of an August 1999 refinancing (the "Refinancing"), which became necessary because the Project was experiencing financial difficulties and had become unable to make the debt-service payments on the then-outstanding bonds. The Refinancing was an exchange offer in which the existing Bondholders exchanged their old bonds for new ones. Simultaneously with the Refinancing, Sunnyside I and Sunnyside II — who I have defined as the Controller — acquired all of the equity interests in the Project.

Thus, to recapitulate, as of the key time, the business entity that actually owned and operated the Facility was the Project. The Project's equity was owned by the Controller.

In the Refinancing, the Project issued $59 million in Series A Bonds and $18 million in Series B Bonds. According to the complaint, $48.7 million in Series A Bonds and all of the Series B Bonds remain outstanding.

The Series A and Series B Bonds have very different sets of rights. The Series A Bonds are typical debt securities that are entitled to fixed payments of principal and interest at a specified percentage rate. By contrast, the Series B Bonds are not guaranteed any interest as a percentage of the $18 million in principal. Instead, the Series B Bondholders are entitled to one-half of the annual revenue generated by the Project's operations after the payment of operating expenses, debt service on the Series A Bonds, capital expenditures, and certain other fees. In other words, the Series B Bonds derive much of their value from their right to share in the upside profits of the Project. To the extent that the Project is profitable, the Series B Bondholders share in those gains. But to the extent that the Project simply covers costs, the Series B Bondholders do not receive

any interest. The $18 million in principal on the Series B Bonds is payable in a lump sum on maturity, which does not occur until August 15, 2024.

The Series A and Series B Bonds were initially issued together as a package to the then-existing Bondholders in exchange for their old Bonds. The Controller argues that the Series B was essentially an "equity kicker" designed as an added incentive to convince the Bondholders to go along with the Refinancing. But although the Series A and Series B Bonds were issued to, and initially owned concurrently by, the same parties, both the Series A and Series B Bonds were fully negotiable and contained no transfer restrictions. That is, a Bondholder could sell its Series B Bonds but retain the Series A or vice versa. Indeed, shortly after the Refinancing, Cypress, bought up most (approximately 75%) of the Series B Bonds, which it continues to hold.

IV. The Base Amount Dispute

A. Factual Background

1. The Base Amount Definition And The S&M Fee

The Base Amount Dispute is a disagreement over the amount of interest to which the Series B Bondholders are entitled. The Series B interest calculation is governed by an Amended and Restated Trust Indenture (the "Indenture") that was executed in connection with the Refinancing. The Indenture provides that the Series B Bondholders are entitled to a single annual interest payment equal to one-half of the "Base Amount." The Base Amount is defined as follows (the "Base Amount Definition"):

> [F]or the twelve month period ending on December 31 of each year, the [Project's] gross revenues during such period less actual expenditures for items included in the applicable

> Annual Operating Budget not in excess of the amount budgeted, for such item in such Annual Operating Budget for such period, including, without limitation, (i) capital expenditures for maintenance of the Facility required or permitted to be made during such period in accordance with the provisions of the Loan Agreement, (ii) principal paid at maturity or scheduled redemption of the [Series A Bonds], together with interest paid thereon, during such period, (iii) any payment made during such period to replenish the Debt Service Reserve Fund or to reimburse the issuer of any Debt Service Reserve Fund Guarantee provided with respect to or for the benefit of the holders of the [Series A and Series B Bonds], (iv) the Administrative Fee payable to CP Sunnyside [i.e., the Controller] during such period, and (v) the Service and Maintenance Fee payable to the [Project] during such period, plus any unpaid Service and Maintenance Fees for any prior periods.[13]

The Base Amount Dispute centers on the meaning of the last clause of the Base Amount Definition regarding deductions from the Base Amount for the Service and Maintenance Fee (the "S&M Fee") payable to the Project. By payable to the Project, the language of the Indenture, in essence, means payable to the Controller.

The S&M fee is a fixed sum, (initially set at $1.5 million per year and adjusted annually for inflation) owed annually to the Project and paid before any payments are made to the Series B Bondholders. Contrary to its name, the S&M Fee, unlike a typical "fee," does not reimburse the Project for out-of-pocket expenses or for management services. Indeed, there is a separate fee, the "Administrative Fee," payable to an affiliate of the Controller, which serves that purpose. The S&M Fee instead functions as a

[13] Complaint, Ex. A at 4. For the sake of clarity, I have interpolated the term "Project" in all places where the Indenture refers to the actual entity that owns the Facility. The Project is the entity that borrowed money under the Indenture. As the owner of the only equity in the Project, the Controller tends to benefit from any payments to the Project itself, in distinction from payments made to the Series B Bondholders.

preferred return to the Project's equity holders — i.e., the Controller — that has priority over the Series B interest.

According to the Controller, the S&M Fee was a material inducement offered by the Bondholders to persuade the Controller to acquire the Project in 1999. The S&M Fee is "paid" only in the sense that it is transferred from the Indenture Trustee, who, as described below, controls all of the cash that moves through the Project to an account from which funds can be disbursed to the Controller. In other words, the S&M Fee is deducted from the Base Amount so that it can be retained in full by the Project (for the benefit of the Controller).

As the Controller views it, its right to an S&M Fee is superior to the Series B Bondholders' expectations of payment and the Base Amount Definition is designed to reflect that superiority by reducing the Base Amount by the extent of any unpaid S&M Fees.

Cypress has a contrasting view. According to it, the S&M Fee is simply a mechanism for effectuating the basic business deal between the parties, which it claims is that after all of the Project's expenses are paid, including the interest on the Series A Bonds and the Administrative Fee, the Controller would ultimately get the first $1.5 million (increased annually for inflation) of profit each year, and would split the residual annual profit 50%-50% with the Series B Bondholders.

2. The Waterfall

Proper analysis of the Base Amount Dispute requires an understanding of the way cash moves through this business. That requires an understanding of a separate provision

of the Indenture — § 4.03, which the parties refer to as the "Waterfall." Under the Indenture, all cash earned by the business is deposited into a "Revenue Fund" that is administered by the Indenture Trustee (the "Trustee"). The Trustee then doles out the cash in the strict order of priority set forth in the Waterfall.

The Project's ordinary business expenses, which include the Administrative Fee and interest on the Series A Bonds have first priority. Each month, under § 4.03(a), the Trustee pays (or sets aside funds for payment of) all of those expenses.

The S&M Fee takes second priority. Under § 4.03(b), the Trustee transfers the S&M Fee from the Revenue Fund to the Project (for the benefit of the Controller) semi-annually out of available cash on February 1 and August 1 of each year. To the extent that there is not sufficient cash in the Revenue Fund on those dates to make the S&M Fee payment, the liability carries over to the next payment date and is to be made on that date.

But S&M Fee payments cannot be made on any date other than February 1 or August 1. That is, if the Project lacks the cash to make an S&M Fee payment on February 1, no payment is made to the Controller even if cash sufficient to make the payment is expected to come in on February 2. Put simply, the key to whether the Controller receives its S&M Fee on time is the cash position of the Project on two specific dates (February 1 and August 1) every year.

If the cash to make an S&M Fee payment exists, the Trustee has no discretion other than to make the payment (in full or in part) on the specified date to the full extent that cash is available.

The third priority under the Waterfall involves payments to replenish a Debt Service Reserve Fund. The Indenture required the Controller initially to infuse that fund with $6 million. Section 4.03(c) of the Indenture contemplates keeping the Debt Service Reserve Fund at $6 million in order to ensure that the Project has an adequate safety net to continue to make the regular interest payments on the Series A Bonds.

Fourth comes the Series B interest. Under § 4.03(d), it is paid once per year, on February 20. Finally, fifth, under § 4.03(e) of the Waterfall, whatever cash remains in the Revenue Fund on February 20 after making the § 4.03(d) payment to the Series B Bondholders is paid to the Project for the benefit of the Controller.

Unavoidably, I must now add more complexity. To protect the Series B Bondholders, the Waterfall's normal operation is subject to a protective bypass provision (the "Series B Bypass"). To the extent that there is not sufficient cash in the Revenue Fund on February 20 to pay all of the Series B interest that is owed, the Series B Bypass kicks in and the shortfall is made up in monthly payments that take priority over certain expenses, including the S&M Fee and the Administrative Fee, that otherwise would have priority over the Series B interest. Under the Series B Bypass, whatever cash is left in the Revenue Fund each month, after the payment of ordinary operation and maintenance costs and the Series A interest, goes one-half to the Series B Bondholders and one-half to the Project until the Series B shortfall is made up. To be clear, even though the Series B Bypass appears in § 4.03(d), both the Series B Bondholders and the Project (i.e., the Controller) get paid under the Series B Bypass. That is, when the Bypass kicks in and until the shortfall is made up, the Controller loses its monthly Administrative Fee

permanently (because there is no provision for accrual of unpaid Administrative Fees) and must suffer deferral of its S&M Fee, but splits half of the residual Bypass amounts. Once the shortfall to the Series B Bondholders is caught up, the normal operation of the Waterfall is restored.

Another complexity lies in the inconsistency of the Indenture in tying various parties' rights to payments to either the actual cash position of the Project or the financial performance of the Project over time. For example, the S&M Fee is only payable by the Trustee if the cash position of the Project on February 1 and August 1 is sufficient to make the payment. By contrasting example, the calculation of the Base Amount (and thus of the Series B interest) does not turn on the cash position of the Project at any given time, but on the difference between the Project's revenues for each calendar year and certain defined "actual expenditures," whether or not that difference equals the Project's cash on hand as of the date that the Base Amount is calculated or the date the Series B interest is supposed to be paid (February 20). In this respect, although Cypress asserts that the parties intended a 50%-50% split of the residual profits, the Waterfall, and particularly § 4.03(e), does not precisely embody that as the contractual benchmark. Under the language of the Waterfall, if the *cash* remaining in the Revenue Fund after payment of all of the S&M Fees and the Series B interest is an amount greater than what was paid to the Series B Bondholders as its interest for the year, that extra cash value inures to the benefit of the Project and thus to the Controller because it is paid to the Project regardless of how the amount of the § 4.03(e) payment relates to the amount paid to the Series B Bondholders. In other words, if all expenses, including the S&M Fee, are

current and the amount calculated as the Base Amount (of which the Series B Bondholders get half) is less than the net cash on hand as of February 20 of the year, the Waterfall would not accomplish precisely what Cypress claims was the business deal between the parties. In that instance, the Project would get the other half of the Base Amount, plus whatever cash is left — meaning that the Project will get more than 50% of the residual profit, and the Series B Bondholders will get less. Conversely, if the amount of cash in the Revenue Fund is less than the Base Amount, the Project (and therefore the Controller) will get less in the way of residual profit than the Series B Bondholders.

3. The Controller's Calculation Of The Base Amount From 2001 To 2005

Now that the relevant contract language has been explained, it is time to dig into the core dispute about the calculation of the Base Amount by looking at what happened during the years in question.

Cypress's complaint cites fiscal year 2001, which was a very good year for the Project, as an example of the correct calculation of the Base Amount. In 2001, the Project realized approximately $42.5 million in income from operations and deducted from the Base Amount actual expenditures of approximately $14 million. Included in those deductions was about $1.55 million for the S&M Fees earned by and actually paid to the Project for the year. The excess profit of approximately $28.5 million was then divided equally between the Series B Bondholders and the Project. In other words, the Series B Bondholders got a one-half share of the residual income for the year. Indeed, the Base Amount calculation works out fairly easily when the Project stays in the black.

The issue in dispute is how the Base Amount is calculated when the Project lacks sufficient cash to make the S&M Fee payments on the contractually specified dates.

In 2002, the Project lost money. It generated only $7.9 million in revenue and incurred over $9 million in actual expenditures. On February 1 and August 1 of that year, the Project was able to pay itself only $0.8 million out of the $1.6 million in S&M Fees that were owed for the year. Nonetheless, in calculating the Base Amount, the Controller deducted the full $1.6 million, consisting of the $0.8 million in S&M Fees actually paid and $0.8 million in S&M Fees accrued but not paid. No interest was paid to the Series B Bondholders for the year.[14]

In 2003, the Project made a modest profit ($2.63 million before taking into account the S&M Fees), but, perhaps as a result of the poor performance in the prior year, was unable to pay itself any of the $1.6 million in S&M Fees attributable to 2003 or the $0.8 million left unpaid from the year before. The Controller took the position that under the plain language of the Base Amount Definition, it was entitled to deduct both the S&M Fee attributable to 2003 and "any unpaid [S&M Fees] for any prior periods." Thus, in calculating the 2003 Base Amount, the Controller deducted a total of $2.4 million in S&M Fees, reflecting both $1.6 million in S&M Fees accrued for the year 2003, plus the $0.8 million attributable to 2002 that remained unpaid. That resulted in a Base Amount calculation of only $181,060, of which the Series B got one-half, $90,530.

[14] That would have been the case regardless of what deductions were made for the S&M Fees because actual expenditures exceeded revenue for the year.

In 2004, the Project made a pre-S&M Fee profit of $4.77 million, but again was unable to pay itself any S&M Fees. Accordingly, in calculating the Base Amount, the Controller deducted approximately $4.1 million in S&M Fees, representing $1.7 million accrued for the year $2004, plus the $2.4 million from the prior two years that remained unpaid. In other words, the Controller deducted the same $0.8 million of unpaid S&M Fees attributable to 2002 in each of 2002, 2003, and 2004. The Controller deducted the $1.6 million in S&M Fees attributable to 2003 in both 2003 and 2004. The Base Amount for 2004 was calculated at $633,505, of which the Series B Bondholders were paid $316,752.

In February 2005, the Project finally paid most of the accrued S&M Fees. It remains unclear from the pleadings what deductions for S&M Fees were made from the 2005 Base Amount. But what is clear is that for the combined years 2003-04, the Controller should have "earned" an aggregate of $3.3 million in S&M Fees. During that time, the Controller deducted a combined total of $6.3 million in S&M Fees. For the years 2003 and 2004, before deduction of any S&M Fees, the Project earned an aggregate profit of $7.4 million. If the business deal was, as Cypress contends, that the equity owners of the Project would get the first $1.5 million (adjusted for inflation) in profits each year and would then split the rest 50%-50% with the Series B Bondholders, that would leave about $4.1 million to be divided equally between the two. The Series B Bondholders would have been entitled to just over $2 million in interest payments for those 2 years. Instead, the Series B were paid only about $400,000.

The value taken from the Series B Bondholders as a result of the double and triple deductions of the S&M Fees is lost to them forever. That value inures to the benefit of the Project and thus the Controller because the Project ultimately receives the cash free of any obligation to the Series B Bondholders. As discussed, the Base Amount turns on a contractual calculation of gross revenue minus certain actual expenditures. The receipt of cash at any time does not affect the Base Amount. It is unclear why the Revenue Fund lacked sufficient cash to make the S&M Fee payments for the years 2003-05, though, as stated, one can infer that it was a result of the Project's poor performance in 2002. It is further unclear what happened to the cash attributable to the undisputed profit earned by the Project from 2003-2005. But that cash ultimately must, under the terms of the Waterfall, make its way into the Revenue Fund, and will eventually all be paid to the Project under § 4.03(e) of the Indenture.

B. The Contending Positions Of The Parties

The parties have starkly different views of how the Base Amount calculation works in years when the Project is unable to pay all the S&M Fees that have accrued. Each justifies its position by two primary means: 1) an argument premised on the text of the Base Amount Definition; and 2) an argument premised on how its reading of the text most logically implements the "business deal" between the Bondholders and the Controller.

For its part, the Controller justifies the approach it took in these terms. As a linguistic matter, it stresses that the term "actual expenditures" as used in the Base Amount Definition expressly refers to the "Service and Maintenance Fee *payable* to the

[Project] during such period, plus any *unpaid* Service and Maintenance Fees for any prior periods." Given the use of the words payable and unpaid in the Base Amount Definition, the Controller argues that the Base Amount Definition clearly contemplated and required the deduction of the S&M Fee due for the current period and any amounts still due from prior periods. Otherwise, the Controller believes the words payable and unpaid are read out of the Base Amount Definition.

Furthermore, as a business matter, the Controller argues that its reading makes the most sense because the Waterfall clearly gives the S&M Fee priority over the Series B interest payment. It therefore makes sense that the Base Amount Definition would reflect that priority by denying the Series B Bondholders payments in years when the Controller has been deprived its greater-in-priority S&M Fees. Until the Controller has been made whole for its higher-priority S&M Fees, the amount of the total S&M arrearage is deducted precisely to ensure that the Project will be able to give the S&M Fees the priority they deserve when it is in a cash position to do so. Otherwise, by ignoring the inability of the Project to pay the S&M Fee, the Base Amount Definition would exacerbate that inability, by artificially inflating the Base Amount, increasing required payouts to the Series B, and thereby lengthening even further the period of delay until the Project would be able to pay the S&M Fees in full.

In contrast, Cypress has a very different take on the text and business purpose of the Base Amount Definition. In its view, both the text and business purpose preclude the Controller from deducting from the Base Amount S&M Fees that were not actually paid during the relevant period. That is, Cypress contends that the Controller is not entitled to

any deduction from the Base Amount for S&M Fees in years when the Project was unable to pay them. Cypress takes particular offense at the Controller's decision to deduct unpaid S&M Fees for prior periods in multiple years (e.g., by deducting the unpaid 2002 Fee in 2002, 2003, and 2004), which Cypress claims is an outrageous exercise in double-dipping and unfairly allows the Controller to reap an unconscionable and uncontemplated share of the Project's profits.

As to the textual basis for that contention, Cypress argues that the most important words are the core definition of what must be deducted before the Base Amount is determined — namely, "actual expenditures." By that phrase, the Base Amount Definition clearly intends only for deductions for funds in fact (i.e., actually) expended during the relevant period. Only the S&M Fees actually paid during a period are an example of a proper deduction (i.e., an actual expenditure) regardless of whether the Fees are for what is, by terms of the Indenture, payable during the current period or attributable to Fees that remain "unpaid" from prior periods. According to Cypress, the Controller has read the word "actual" out of the Base Amount Definition.

As a business matter, Cypress contends its position makes the most sense. It views the S&M Fee as a preferred return that ensures that the Controller will eventually get $1.5 million (on an inflation adjusted basis) per year in profit that the Series B does not. But it claims the Indenture is not written in a manner that starves the Series B Bondholders until that preferred return can be paid. Rather, if the Project cannot pay the S&M Fees on the appointed dates, the Controller just has to wait longer for its preferred return. If nothing is "actually expended" for S&M Fees during a year, the Base Amount

for that year is simply unaffected by that category, and the Controller and Series B Bondholders will split a greater amount. Because the Controller will get the other half the Base Amount, this is not a penalty to the Controller, just the equal splitting of the annual profits that Cypress says was contemplated. Eventually, the Controller will be made whole by deducting from the Base Amounts in later years the full amount of any S&M Fee make-up payments when the S&M Fees are brought current. And, assuming the Project ultimately performs well enough, the Controller will eventually get all of its S&M Fees, but it will only get them once, instead of multiple times, as happens under the Controller's interpretation. Cypress claims that to the extent the Controller is delayed in collecting its S&M Fee, or there is a risk that the fees will never be brought current, it is commercially reasonable that the Controller suffer that delay and bear that risk because it made an equity investment in the Project — an inherently lower-priority, riskier investment than the quasi-debt investment made by Cypress.

Having stated these contending positions, I now examine whether either is so clearly right that a ruling in either party's favor can be made based on the text of the Indenture.

C. The Language Used In The Base Amount Definition Is Ambiguous

To recap, the question is this: does the final clause of the Base Amount Definition directing the deduction of S&M Fees "payable . . . during such period, plus any unpaid [S&M Fees] for any prior periods" permit the Controller to deduct all accrued and unpaid S&M Fees in each period until the Fees are made current, or does it, as Cypress claims,

require the Controller to take no deduction for S&M Fees in the years when the Fees go unpaid and deduct those amounts only when the Fees are actually paid in later years?

Viewed in isolation, the final clause appears to allow the Controller to do precisely what it has done — deduct from the Base Amount the S&M Fee payable for the period (i.e., the S&M Fee attributable to or "earned by" the Controller in that year), plus any unpaid S&M Fees from prior periods (i.e., any accrued S&M Fees attributable to prior periods that remain unpaid). But interpreting this contract language is made difficult by the fact that each numbered clause in the Base Amount Definition purports to describe an "actual expenditure," and the Controller's interpretation of the final clause, which appears correct if the clause is read in isolation, actually describes the full amount of a liability owing to the Controller that will be paid at some time in the future — a balance sheet concept that hardly seems akin to an actual expenditure.[15]

---

[15] In an attempt to resolve this difficulty, the Controller points to § 1.02(c) of the Indenture, which provides that all accounting terms used in the Indenture, but not defined therein, shall be interpreted according to the meaning given them by the then-applicable generally accepted accounting principles ("GAAP"). The Controller contends that the accounting profession does not limit the meaning of the term "expenditure" to an actual outlay of cash. *E.g.*, KOHLER'S DICTIONARY FOR ACCOUNTANTS 203 (W. W. Cooper & Yuri Ijiri eds., 6th ed. 1983). Thus, the term "expenditures" includes incurred expenses, and the word actual is used simply to differentiate actual business expenses from the "amount[s] budgeted" referred to immediately thereafter. Defs. Rep. Br. at 3 n.2 (citing *id.*). But the Controller has cited no authority, and I am unaware of any, to support the contention that "actual expenditure" is a GAAP term. Rather, the use of a non-accounting word like "actual" as a qualifier suggests that the drafters of the Indenture were seeking to implement a more specific and narrower meaning of "expenditure" — one that was based on the actual payment of money. Moreover, the Controller's citation to GAAP for the proposition that the Base Amount Definition requires multiple deductions of unpaid S&M Fees for multiple periods is puzzling. Regardless of the precise meaning attributed to "actual expenditure," it would be a tad unusual for a contract to provide that the S&M Fee attributable to 2003 was an "actual expenditure" in 2004 when it was also an actual expenditure in 2003 and 2005. In the more ordinary business context, involving the preparation of financial statements, no rational system of accounting would treat a single item of expense as an

But just as the Controller's reading of the Base Amount Definition gives no meaning to the word "actual," so does Cypress's reading tend to slight words in the final clause. Cypress's reading is basically this: the Controller gets to deduct "actual expenditures *for* S&M Fees *paid* during the period." In the Controller's view, Cypress reads the language "*payable* to the [Project] during such period, plus any *unpaid* [amounts] for any prior periods" out of the Indenture entirely. Although the Base Amount Definition uses the term "actual expenditure," it more particularly requires the deduction of any S&M Fees "payable" for that period and any "unpaid" from prior periods. This, in the Controller's view, was designed to protect the greater priority given to the Controller's right to an S&M Fee in comparison to interest payments to the Series B Bondholders. It is rational, as will be noted later, that the Series B Bondholders would have their interest reduced every year by the full amount of an arrearage in higher-priority payments due to the Controller.

The Base Amount Definition therefore appears to be internally inconsistent. The ambiguity stems from the fact that the final clause purports to be describing a category of "actual expenditure," but what its more specific words plausibly describe is in fact different than an "actual expenditure" under an ordinary interpretation of that term.

"expenditure" more than once and in more than one period. GAAP would not condone accounting for an expenditure in 2004 if that expenditure was already accounted for in determining the Project's 2003 financial performance. *E.g.*, *In re Chambers Development Securities Litigation*, 848 F. Supp. 602, 620 (W.D. Pa. 1994) (stating that double counting expenses violates GAAP). Given that the drafters of the Indenture created an idiosyncratic formula designed for a particular business purpose, the Controller's resort to a GAAP definition of "expenditure" does little to convince me that its interpretation of the different, and non-standard, term "actual expenditure" is correct.

That internal tension, perhaps, can be minimized by an examination of the specific categories used in the Base Amount Definition as examples of actual expenditures. The first three — dealing with capital expenditures, interest or principal retirement payments made on the Series A Bonds, and replenishments made to the Debt Service Reserve Fund — clearly describe "actual expenditures" in the sense that the funds for those purposes would have in fact been spent during the year.

The latter two examples — the Administrative Fee and S&M Fee "payable" to the Controller — are phrased differently, for a reason that the Controller slights. It is logical that the Base Amount Definition would describe the S&M Fee and the Administrative Fee would in terms of what is payable. Under the Base Amount Definition, the Controller is only able to deduct "actual expenditures" in accordance with the "amount budgeted, for such item in [the] Annual Operating Budget for such period . . . ." But the amount of the S&M Fee and the Administrative Fee are not determined by an annual budgeting process. They are fixed by the terms of the Indenture. The use of the words "payable" and "unpaid" can thus be understood as a way of explaining that the Controller could deduct the amounts of those Fees that were "actually expended" during the period so long as those Fees were within the definitions of what was payable for that purpose in the Indenture.

Candidly, this explanation, which the parties themselves do not dilate upon, inclines me toward the view that Cypress has the better of the arguments from text. But this explanation does not convince me that Cypress's argument is the only plausible one. In coming to that conclusion, I am confessedly influenced by the practical implications

Cypress's argument has for the Controller's ability to receive, in a seasonable manner, what the Waterfall establishes as priority rights — the Administrative and S&M Fees. As I discuss below, by allowing no deduction for these categories in periods when they cannot be paid, the Base Amount Definition would inflate required payouts of cash to the Series B, and minimize the Project's ability to pay the Administrative and S&M Fees in a timely way in the future and to catch up on over-due S&M Fee payments.

D. As A Business Matter, Each Of The Parties' Interpretations Is Neither Clearly Correct nor Irrational

Perhaps because the parties recognize that the language of the Indenture is not a model of clarity, each argues that the Indenture is unambiguous in its particular direction because a contrary ruling would produce results that are absurd in a business sense.

The problem is that neither party's position leads to a patently irrational result as a commercial matter. In fact, the plausibility of each party's position indicates that the Indenture's drafters probably never contemplated that the temporal and qualitative differences in the Indenture's approach to paying the S&M and Administrative Fees under the Waterfall, on the one hand, and the Series B interest under the Base Amount Definition, on the other, would result in a dispute of this kind. Although each party has submitted some parol evidence indicating that the parties knew some issues could arise because of these differences, at this stage it is plausible that none of them thought the divergence in approach between the payment calculations for the Controller and the Series B Bondholders would produce a big dollar dispute. In other words, the drafters perhaps believed that the S&M Fee would tend to be paid, and the Series B interest

would tend to be high, in periods of profitability, and that the S&M Fee would tend not to be paid in whole or in part, and the Series B would tend to receive little or no interest, in periods when the Project was barely or not profitable.

Obviously, this dispute suggests that the differences in calculating the payouts to the Controller and the Series B have turned out to matter. Which of the parties' competing interpretations is chosen has a material impact, with millions of dollars at stake. Neither has persuaded me that the drafters intended the other party to be the loser in the scenario that has arisen.

The Controller's position — which is that the Base Amount Definition is not intended to generate a payment for the Series B without considering the total S&M Fees remaining due — is vulnerable primarily because both the Base Amount Definition and the Waterfall appear to contemplate that the Controller will earn only a single S&M Fee payment each year. Indeed, that is precisely what happens when the Project performs well enough to pay all of the S&M Fees when they are due. But when the Project falls behind on the S&M Fees, under the Controller's reading of the contract, the Controller becomes entitled to deduct, and (assuming the S&M Fees are eventually brought current), by operation of the Waterfall (specifically, § 4.03(e)), ultimately to keep for itself more than one S&M Fee for each year because it gets to deduct from the Base Amount each year's S&M Fee multiple times — in each successive year until the Fee is paid in cash.

Cypress's contention — that the Controller is inequitably "double dipping" in the S&M Fees — has some appeal because it is hard to imagine why the parties would have agreed that the Controller would be entitled to additional fees simply by reason of the

Project's inability to meet its cash obligations. Moreover, if, as Cypress argues, the S&M Fee is viewed as a preferred return for the Controller, there is nothing absurd about Cypress's approach. Although it requires the Controller to go without its S&M Fees for a potentially long period of time, the Controller will eventually be made whole for those Fees by deducting the full amount of all actual S&M Fee payments in the years they are made, and the Controller will still receive its § 4.03(e) share in the interim.

Cypress's interpretation is the only one that can effectuate what Cypress contends was the original business deal — a 50%-50% split of the Project's residual profit. To be concrete, Cypress argues that the Controller's interpretation produces a windfall for it for the years 2003 and 2004. Over those years, the Controller deducted approximately $6.3 million from the Base Amount for S&M fees by double counting the over-due Fees from several periods. Ultimately, the Controller got paid the $3.3 million in S&M Fees that it "earned" over that time. But it also stood to reap 100% of the cash left in the Project as a result of the additional $3 million in Fees that were deducted from the Base Amount. As a result, Cypress argues that the Controller got its S&M Fee plus a much-greater-than 50% split of the residual profit. Again, in concrete terms, Cypress claims that the Controller got at least a $1.5 million windfall that it was not entitled to (i.e., half of the additional $3 million in S&M Fees that were deducted from the Base Amount that Cypress claims should belong to it).[16]

[16] As stated, the 50%-50% deal that Cypress insists was intended by the parties is not written into the language of the Indenture with precision. But the parties to the Indenture may simply have assumed that the aggregate amount of cash ultimately paid out under § 4.03(e) will, over time, work out to be the same as the aggregate amount paid out to the Series B under § 4.03(d). The

That said, this does not mean that Cypress's reading is the only sensible one. In fact, Cypress's interpretation is questionable because it permits zero deduction from the Base Amount for years in which the S&M Fees are not paid. That is, the fact that cash was not available to pay the S&M Fees when due causes the Series B Bondholders to get more than they would have gotten in that year had the Project had sufficient cash to make the S&M Fee payment — an obligation that admittedly has a higher priority than the

---

reason that the Indenture doesn't just say that on February 20, the Series B Bondholders get half of the Base Amount and the Project gets the other half is that the amount of cash in the Revenue Fund on February 20 after payment of all other obligations will likely never exactly equal the Base Amount. One reason is that all of the cash attributable to the revenue accounted for in the Base Amount calculation for the prior year will likely not have been collected by February 20. Another is that in the regular course of business, cash accounts tend to fluctuate. Thus, when drafting the Indenture, reasonable parties focused on the issue at hand would likely have understood that it was unrealistic to assume that the amount of cash in the Revenue Fund on February 20 would exactly equal the Base Amount. Cypress's interpretation — that the Indenture does in fact contemplate a 50%-50% split of the residual profit — finds support in the Series B Bypass provision contained in § 4.03(d) of the Indenture. That provision provides:

> to the extent the Revenue Fund does not, on [February 20] contain an amount equal to the [interest owed to the Series B Bondholders] for the preceding Fiscal Year, the Trustee shall [pay the Series B Bondholders] one half of the moneys then available in the Revenue Fund for such purpose and shall on the first day of each month thereafter, following the [payment of ordinary business expenses and the Series A interest], transfer from the Revenue Fund to the [Series B Bondholders] one-half of any moneys then contained in the Revenue Fund until such time as the [Series B Bondholders have been paid in full] and shall, concurrently with such transfer, disburse from the Revenue Fund to the [Project] an equal amount.

Complaint, Ex. A at 30. If the Revenue Fund does not have enough cash to pay the Series B what they are owed, there is in fact an express 50%-50% split in both the initial § 4.03(d) payment and the monthly Bypass payments. The Series B get half of whatever cash is in the Revenue Fund and the Controller will get the other half under § 4.03(e). Then whenever the Series B get a Bypass payment, the Controller is entitled to an equal amount. Cypress's position finds further support in certain documents attached to its complaint. Documents entitled "Series B Bond Amount Reports," submitted annually to the Series B Bondholders refer to equal residual payments to the Series B Bondholders and the Controller under the heading "cash split." Complaint, Exs. D-G. The Project's "Projected Statement of Cash Flow," attached to the Loan Agreement, also refers to a "cash split: equity 50% debt 50%." Complaint, Ex. B.

Series B interest. It is an odd contention that, where the Series B interest is measured by the operational performance of the business, a cash deficiency (i.e., poor cash performance) results in an increase in its interest payment. Indeed, the increased interest payment would put further strain on the Project's cash position and make it more likely that the S&M Fees would continue to go unpaid. If Cypress's approach is adopted, it is possible that the Controller could endure a half-decade, or more, of delay before its S&M Fees are brought current. Although Cypress claims that even a delay of that length is reasonable because the S&M Fee is a component of the return on the Controller's equity investment, it turns the Waterfall's system of priority on its head because the S&M Fees are supposed to come before interest payments to the Series B Bondholders.

Further, it is arguably sensible, as the Controller contends, to view the Series B's right to interest as a claim on the surplus produced by the Project after meeting the higher priority items in the Waterfall. Until those higher priority items are paid and arrearages made current, there is no surplus from which to pay the Series B Bondholders, who are supposed to share in the Project's profits only to the extent the profits exceed the Controller's S&M Fees. That this could result in a higher ultimate share of the Project's profits for the Controller is not irrational, just a product of the Project's inability to seasonably pay what was due to the Controller.

Moreover, Cypress's description of the business deal as a simple 50%-50% split of the residual profit fails to account for how losses are to be allocated between the Controller and the Series B Bondholders. Presumably, under Cypress's interpretation, if the Project experiences a loss in a particular year (as it did in 2002) that loss falls only on

the Controller and not on the Series B Bondholders. If, in the following year, the Project has a profit again, the amount of cash in the Revenue Fund will likely be substantially less than the Base Amount because the Base Amount calculation for the year in which there was a profit will not be influenced by the fact that there was a loss in the prior year. Thus, over the aggregate two-year period, the Series B Bondholders would get more than 50% of the net profit for that combined period because the loss in year one was not accounted for in determining the Series B share of the year-two profit.[17] Thus, Cypress's interpretation does not accomplish a 50%-50% split of the Project's total residual profit as measured over multiple periods if the Project suffers even a single yearly loss. Or put less extremely, at the very least, the split of profits is more beneficial to the Series B because they do not bear any of the losses. That these results could obtain cuts against ignoring altogether the Project's inability to pay S&M Fees on the appointed dates in the calculation of the Base Amount. In other words, in contending that the Controller has reaped a windfall by double and triple deducting the S&M Fees that temporarily went unpaid, Cypress fails to take account of the Project's losses for the year 2002. If the loss in 2002 was substantial — say, one million dollars — that would substantially reduce the alleged windfall of at least $1.5 million that Cypress claims the Controller enjoyed and bring the split of net profits closer to 50%-50%.

[17] For example, if the Project loses $500,000 in year one and has a $2 million profit in year two, under Cypress's interpretation, the Series B would be entitled to nothing in year one and $1 million in year two. Over the two year period, there is a net profit of $1.5 million, of which the Series B would get $1 million (66.7%). Further, the fact that the Trustee will have to pay out the full $1 million in cash under § 4.03(d) would put the Project deeper into a cash crunch and make it more likely that the Project will not be able to pay future S&M Fees or the Controller's § 4.03(e) share.

The Controller's interpretation of the Base Amount Definition, under which it gets to deduct the full amount of the outstanding unpaid S&M Fees essentially forces the Series B Bondholders to bear some of the Project's losses by reducing the Series B Bondholders' share of the profits in subsequent years until the Controller's S&M Fees are brought current. That is arguably a rational business deal because, as stated, until the S&M Fees are brought current, there can be no surplus from which to pay the Series B Bondholders. But it also is not the clearly correct interpretation because it strikes me as an imprecise means of splitting the losses between the Controller and the Series B Bondholders — especially because the Project's ability to pay S&M Fees on time turns only on the cash position of the Project on two specific days out of the year (February 1 and August 1).

The existence of cash in the Revenue Fund on a given date is not perfectly related to the actual performance of the business during the periods in which those dates fall. Under the Controller's interpretation of the Base Amount Definition, it would get to take an extra S&M Fee deduction even if, despite a cash shortfall on August 1, there was a large influx of cash into the Revenue Fund on August 2 — and even if the business performed so well during the fourth quarter that it is clear there will be sufficient cash available in the following February to bring all of the S&M Fee payments current.

Following the Controller's interpretation to its logical end, the fact the large influx of cash came on August 2 instead of July 31 is a fact that would cost the Series B Bondholders about $400,000. If the cash had been received only three days earlier, the S&M fee would have been paid, and the Controller would have gotten only one

deduction for the approximately $800,000 Fee that is owed each August 1. Instead, the Controller now gets to take an additional deduction in the following year because that $800,000 Fee remained unpaid. The three-day differential in the timing of the cash receipt hardly seems a material consideration in determining the amount to which the Series B Bondholders are entitled.[18]

Put simply, and without belaboring the issue even further, I am not persuaded that the terms of the Indenture, when understood in a business context, are susceptible to only one reasonable interpretation. Teasing through the implications of the operations of the Base Amount Definition and the Waterfall based solely on the pleadings is a head-hurting exercise that cannot claim as its reward a reliable determination of the parties' intent. The ambiguities can only be resolved, if at all, after considering relevant parol evidence. Therefore, the cross-motions for judgment on the pleadings are denied.

[18] The possibility that such a result was not intended is buttressed by the fact that because the Controller was the party actually running the business, it was in a position to control, to some extent, the timing of the Project's receipt of cash. Indeed, Cypress contends that the Project had the wherewithal to pay accrued S&M Fees in 2003 but chose not to. That the Series B Bondholders would have agreed to give a Controller with power over the Project's billing practices and books the ability to cause unpaid S&M Fees to be deducted multiple times by manipulating the timing of cash receipts is questionable. Although the Controller contends that it would be self-defeating for it to defer S&M Fee payments to itself, that contention is not necessarily correct as an economic matter. An economically-rational opportunist might defer collection of an $800,000 S&M Fee for six months in order to take $400,000 of value to which it would otherwise not be entitled. In recognizing this, I do not suggest that the Controller in fact engaged in opportunistic behavior of this kind. I only point out that the Controller's reading of the contract gives it the opportunity to do this and, as a result, the indisputability of its reading is undermined.

V. The PPA Amendment Dispute

A. Factual Background

I now turn to the other discrete area of contention between these parties, the PPA Amendment Dispute. I begin with a recitation of the additional facts required to resolve it.

The Project earns much of its revenue by selling energy generated by the Facility to various power companies throughout the western portion of the United States. In November, 2004, the Project attempted to resolve a dispute with Utah Power and Light Company ("Utah Power") regarding the prices for energy delivered to Utah Power by amending the Power Purchase Agreement between them (the "PPA"). The Amendment would provide for a floor and ceiling on the prices Utah Power would pay for energy.

The PPA historically calculated energy prices without regard to a floor and ceiling. At various times, the pre-Amendment price was both above the ceiling and below the floor. The PPA Amendment would guarantee a minimum and maximum revenue stream from the operation of the Facility. It would also make it less likely that the Project fails and is forced into bankruptcy before the date on which the principal is due to be repaid on the Series A and Series B Bonds.

But the PPA Amendment also alters the economics underlying an investment in the Series B Bonds by capping the Project's upside potential, and thus the upside on the Series B interest payments. Cypress claims that the PPA Amendment will greatly reduce, if not altogether eliminate, the future interest payments on the Series B Bonds because the ceiling price under the Amendment may have the effect of reducing, by over 50%, the

price that Utah Power would otherwise pay. Cypress has not consented to the Amendment.

Section 9.4 of the Loan Agreement states:

> the [Project] agrees that it will not terminate or amend in any material respect or permit any termination or material amendment of any of the Facility Documents without the prior written consent of the Trustee and the Required Percentage of Bondholders, which consent shall not be unreasonably withheld or delayed.[19]

In my March 8, 2006 opinion in this case, I concluded that because the PPA Amendment was a material amendment to a Facility Document, and because the Project could not achieve the consent of the Required Percentage of Bondholders (80%) without Cypress's approval, § 9.4 effectively gave Cypress (who owns just over 20% of the Bonds) veto power over the Amendment.[20] But the Loan Agreement provides that Cypress cannot unreasonably withhold or delay consent. The Controller seeks to avoid judgment against it on the pleadings in the PPA Amendment Dispute by relying on the allegation in its answer that Cypress unreasonably withheld or delayed consent to the Amendment. For the sake of simplicity, I refer to that as the "Withheld Consent

[19] Complaint, Ex. B at 36.

[20] *See Cypress Associates, LLC v. Sunnyside Cogeneration Associates Project*, 2006 WL 668441, at *8 (Del. Ch. 2006). To be precise, that opinion resolved the Controller's motion to dismiss Cypress's claims with respect to the PPA Amendment Dispute. I concluded that Cypress's reading of the relevant contract provisions to give it veto power was clearly a colorable reading of the documents and thus that the Controller's motion to dismiss must be denied. Cypress's opening brief on this Rule 12(c) motion sought judgment to the effect that the Amendment had to be approved by 80% of the Bondholders under § 9.4. The Controller did not oppose that part of the motion, while purporting to reserve all appellate rights. Thus, I will enter an order granting Cypress's motion to the extent it seeks a determination that the Amendment required the Controller to seek Cypress's consent, which could not be unreasonably withheld.

Defense." As stated, the Controller alleges no facts in its answer to suggest why Cypress's failure to give consent was unreasonable.

B. The Controller's Belated Contentions

Despite the absence of facts in its pleading, the Controller suggests two potential factual arguments in its briefing on this motion.

First, the Controller contends that because the loan documents were drafted in a context where every Bondholder would be acquiring the same percentage of Series A and Series B Bonds, an economic judgment based solely on the return on the Series B Bonds, without taking into account the obvious benefits that the Amendment will confer on holders of the Series A Bonds, is per se unreasonable. By guaranteeing a minimum revenue stream, the PPA Amendment makes it more likely that the Project will continue to be able to make the Series A interest payments, that it will not default on the Series A Bonds, and that it will ultimately be able to repay those Bonds in full. The Controller claims that it would be unreasonable for any Bondholder to withhold consent to the PPA Amendment because the Amendment is beneficial to the Series A and Series B Bondholders collectively.

That argument is without any force and I reject it. The Bonds are freely transferable. Nothing in the text of the Loan Agreement or the Indenture prohibits a purchaser of the Series B Bonds from considering whether to consent from the perspective solely of a Series B Bondholder and the Controller has no rational argument for implying such a condition on Cypress's consent rights.

The second argument has more color. The Controller now contends that Cypress's refusal to consent to the Amendment is not based on the principled rationale that is recited above — i.e., that the Amendment fundamentally alters the economics of the Series B Bonds by capping the upside on the Series B interest payments. Rather, the Controller contends that that rationale is an entirely pretextual one that was never communicated by Cypress for the entire six-month period during which the Controller tried to obtain Cypress's consent. Instead, the Controller claims that its repeated requests for consent were met with no firm answer and that Cypress used the request for consent as an unreasonable attempt to gain leverage in then-ongoing negotiations over the Base Amount Dispute. That is, Cypress threatened to use its blocking position to hold up the Project's settlement with Utah Power unless the Controller agreed to accede to its interpretation of the Base Amount Definition. Thus, Cypress allegedly unreasonably delayed responding to the request, and unreasonably withheld (by not answering) consent, not because of the Amendment's own merits, but as a weapon in an unrelated dispute.

I confess that I am skeptical about the ultimate viability of this argument. Given the rather obvious economic effect that the Amendment has on the value of the Series B Bonds, it seems reasonable for Cypress to refuse to allow the Controller to implement it. If Cypress preferred the potential for gain that uncapped power prices presented to the Project even in light of the risk of greater losses in other periods, it had the right to vote its economic self-interest.

Moreover, that Cypress may have expressed a willingness to compromise on the PPA Amendment issue in order to resolve the ongoing Base Amount Dispute does not strike me as unreasonable at all. Settlements like that get done every day and the Controller will bear the burden of disproving this very likely scenario. That is, there would be nothing wrong if Cypress honestly preferred that the Amendment not be adopted but evinced a willingness to go along with it if the Base Amount Dispute was resolved in its favor. That sort of non-violent compromise is something informed citizens should recognize as a valuable attribute of a well-ordered polity. The law should not chill such a give and take, and thereby promote discord and costly litigation.

But the reality is that at this stage, one cannot safely rule out the possibility that, under relevant Utah law principles, Cypress would have unreasonably delayed or withheld consent to the Amendment if it: (1) actually believed the Amendment posed no harm to the Series B Bondholders; (2) would not have objected absent the Base Amount Dispute; and (3) simply used its blocking power to force the Controller to compromise on the Base Amount Dispute. In stating the Controller's argument in these terms, I do it the favor of articulating its position in a clearer and more compelling way than it did in its briefs or oral argument. And its advocacy of new factual arguments in a brief and at oral argument obviously compromised Cypress's ability to respond. Indeed, neither of the parties submitted any authority regarding how the Utah Supreme Court would analyze the reasonability of Cypress's response to the Controller's request for consent. Nor do the pleadings quantify the likely effects of the PPA Amendment on the Project's expected future financial performance. Viewing the facts articulated in the briefs and oral

argument in the light most favorably to the Controller, it is possible that Cypress didn't really care about the PPA Amendment at all and that it simply used its fortuitous position of being able to block the Amendment in order to get the Controller to accede to its demands in a completely unrelated dispute. It is also possible that under relevant authority, such a factual scenario might involve an unreasonable denial of consent.[21]

C. The Controller's Answer Is Defective

Cypress did not get the fair shake at responding to this factual argument that the Court of Chancery Rules contemplate. Cypress's motion in the PPA Amendment was based on a simple and forceful argument: the Controller's Withheld Consent Defense was not supported by facts pled in the Controller's answer, which simply contained the conclusory assertion that Cypress had unreasonably delayed or withheld its consent. Therefore, the key issue Cypress raised was whether the Controller's conclusory pleading was adequate to preserve this Defense.

That issue does not fall out in favor of the Controller. The burden of proving unreasonableness in failing to give consent on a matter rests on the party who challenges the reasonableness of the other's actions.[22] Thus, when a contract provision providing

[21] *See Commonwealth Associates v. Providence Health Care, Inc.*, 1993 WL 432779, at *7 (Del. Ch. 1993) (stating that a party may properly withhold consent to a transaction only when the decision is made for a legitimate business purpose) (citing *Bonady Apts. v. Columbia Banking Fed. Sav. & Loan Ass'n.*, 465 N.Y.S.2d 150, 154 (N.Y. Sup. Ct. 1983), *modified* 472 N.Y.S.2d 221 (N.Y. App. Div. 1984)); *Union Oil Co. of California v. Mobil Pipeline Co.*, 2006 WL 3770834, at *11 (Del. Ch. 2006) (same).

[22] *See, e.g., Jones v. Andy Griffin Products, Inc.*, 241 S.E.2d 140, 144 (N.C. App. 1978) (explaining that the burden of proving the unreasonableness of a landlord's failure to give consent to a sublease rests upon the tenant challenging the landlord's actions); A.L.R. 3d 679, at § 2(b) (same); *see also Safeway, Inc. v. CESC Plaza Ltd. Partnership*, 261 F. Supp. 2d 439, 463 n.30 (stating that the principle placing the burden of proving the unreasonableness of a landlord's

that consent shall not be unreasonably withheld is invoked defensively, as it is in this case, it takes the form of an affirmative defense, and the burden of proof is on the defendant.[23] As a result, because affirmative defenses must be supported by pled facts,[24] the Controller cannot survive a Rule 12(c) motion simply by denying the reasonableness of Cypress's refusal to consent.

In so holding, I reject the Controller's argument that its conclusory statement that Cypress unreasonably withheld consent would be sufficient to satisfy a plaintiff's burden to plead a claim. The Controller's argument supposedly draws support from *Desert Equities, Inc. v. Morgan Stanley Leveraged Equity Fund, II, L.P.*,[25] a case in which the Delaware Supreme Court reversed this court's ruling that the conclusory allegations of wrongdoing in a plaintiff's complaint were legally insufficient. In *Desert Equities*, the plaintiff had alleged that the general partner of the defendant, an investment fund, acted in bad faith and for retaliatory purposes in excluding the plaintiff from certain investment opportunities. The plaintiff's complaint specifically pled facts to suggest how the general partner's actions were wrongful — the plaintiff alleged that the defendant had refused to allow it to participate in the investment opportunities in retaliation for the plaintiff

---

failure to give consent to a sublease on the tenant challenging the landlord's actions persuasively applies to other contexts).

[23] *See In re Tjia*, 50 S.W. 3d 614, 617 (Tex. App. 2001) (stating that the defendant's contention that consent was unreasonably withheld is an affirmative defense, and the burden of proof lies on the defendant); *Rollins Properties, Inc. v. CRS Sirrine, Inc.*, 1989 WL 158471, at *1 (Del. Super. 1989) (referring to the contention that a party to a contract unreasonably withheld consent as an affirmative defense).

[24] *E.g.*, *Speiser v. Baker*, 525 A.2d 1001, 1006 (Del. Ch. 1987) (stating that in testing the sufficiency of an answer's pleading of affirmative defenses, "the task is to evaluate the sufficiency of the facts alleged *while ignoring wholly conclusory statements*") (emphasis added).

[25] 624 A.2d 1199 (Del. 1993).

previously having brought suit against an affiliate of the defendant.[26] In other words, the plaintiff at least suggested that the defendant's acts were the product of a specific improper motive in a manner that gave the defendant notice of the contentions it would make in the case. The Controller's answer here makes no attempt to provide that notice, and instead contains mere naked legal conclusions that do not plead facts supporting the viability of its affirmative defense.

D. I Conditionally Grant The Controller Leave To Amend Its Answer

I must now decide whether to enter judgment on the pleadings in favor of Cypress or whether to indulge the Controller's belated request at oral argument for leave to amend its answer to plead facts supporting its affirmative defense on the potentially viable theory I have earlier described. In answering this question, I note that Chancery Court Rule 15(aaa), which imposes a restrictive standard on certain motions for leave to amend, is not applicable to a motion by a plaintiff for judgment on the pleadings.[27] As a result, the Controller's right to amend its answer is governed by the permissive standard of Rule 15(a), which provides that "[a] party may amend the party's pleading . . . by leave of [the] Court . . . and leave shall be freely given where justice so requires." Rule 15(a) reflects the policy that, in absence of prejudice to the other party, disputes should be

[26] *Id.* at 1205-06.

[27] *Lillis*, 896 A.2d at 877-78 (noting that although it would seem true that some of the same concerns that prompted the court to adopt Rule 15(aaa) are present in a case where a defendant stands on its answer in response to a motion for judgment on the pleadings, the language of the rule makes clear that it does not apply to such a case); Chancery Court Rule 15(aaa) (a plaintiff who unsuccessfully contests a "*motion to dismiss under Rules 12(b)(6) or 23.1*" is ordinarily not given leave to amend its defective complaint) (emphasis added).

decided on their merits instead of on technical or procedural grounds.[28] This case is not so far advanced or so costly to Cypress that permitting an amendment could be seen as giving rise to an injustice. Because the facts suggested in the Controller's briefs and at oral argument plausibly support its Withheld Consent Defense, the interests of justice require me to grant the Controller leave to amend its answer.

But in deciding to grant leave to amend, I am mindful of the needless expense Cypress suffered as a result of the Controller's failure to craft a proper pleading in the first instance. Because the Controller clearly failed to plead facts supporting its Withheld Consent Defense, Cypress made a good faith decision that it was entitled to judgment on the pleadings in the PPA Amendment Dispute. Upon receiving Cypress's brief, the Controller chose not to seek leave to amend its answer and instead stood on its defective pleading, making a series of meritless arguments, only to beg for leave to amend at oral argument. As a result, Cypress incurred substantial expense in briefing and arguing its motion. That expense is wasted by my decision granting the Controller belated leave to amend.[29]

"A conditional allowance is within the court's discretion under Rule 15" for a reason.[30] That option permits the court to balance the interest in deciding a case on its merits with the costs incurred when parties do not timely comply with pleading requirements. Here, that balance is properly struck by requiring the Controller to bear the reasonable legal fees and costs incurred by Cypress in bringing the PPA Amendment

[28] *See Lillis*, 896 A.2d at 877.
[29] *See id.* at 879.
[30] *Id.* (citing *Brunswick Corp. v. Colt Realty, Inc.*, 253 A.2d 216, 220 (Del. Ch. 1969)).

portion of its Rule 12(c) motion.[31] Pending my receipt of notice of the Controller's decision to pay those expenses to Cypress, I will defer decision on the Rule 12(c) motion with respect to the PPA Amendment dispute.

Equally as important, I condition the Controller's right to amend on its ability to plead facts, in compliance with the obligations owed to the court under Rule 11, consistent with the one theory I have articulated above as potentially supporting a viable Withheld Consent Defense. Absent an ability on the Controller's part to do that in good faith, I shall enter judgment for Cypress and declare that the Amendment failed to gain approval from the required percentage of Bondholders and that, as a matter of law, the Controller has not pled facts supporting an inference that Cypress's denial of consent was unreasonably delayed or withheld.

VI. Conclusion

For the reasons stated, both motions for judgment on the pleadings in the Base Amount Dispute are denied. With respect to the PPA Amendment Dispute, I will enter an order granting Cypress's motion to the extent that it seeks a ruling that § 9.4 of the Loan Agreement required the Controller to seek Cypress's consent, which could not be unreasonably delayed or withheld. As to the Controller's Withheld Consent Defense, I provisionally deny Cypress's motion based on the Controller's request to amend its answer and subject to the Controller's compliance with the conditions I have set on its right to do so. Cypress shall submit an affidavit identifying with reasonable precision the expense it incurred in addressing the PPA Amendment Dispute in this motion practice.

[31] *Id.*

The Controller shall pay that expense within 15 days of receipt and amend its answer on that same date. If the Controller fails to pay that expense or fails to meet the conditions on the nature of its amended pleading articulated in this opinion, I shall enter judgment against the Controller on the entirety of the PPA Amendment Dispute upon Cypress's request. IT IS SO ORDERED.