

Case No. 09-31169

IN THE
United States Court of Appeals
FOR THE FIFTH CIRCUIT

JOHN HANCOCK LIFE INSURANCE COMPANY,
Plaintiff-Appellant,
—v.—

UNITED STATES OF AMERICA,
Defendant-Appellee.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF LOUISIANA, NO. 2:08-CV-3911
BEFORE THE HONORABLE JAY C. ZAINEY

**BRIEF OF AMICI CURIAE THE CLEARING HOUSE ASSOCIATION L.L.C.,
THE FINANCIAL SERVICES ROUNDTABLE, AND THE SECURITIES
INDUSTRY AND FINANCIAL MARKETS ASSOCIATION
IN SUPPORT OF PLAINTIFF-APPELLANT**

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March 10, 2010

CERTIFICATE OF INTERESTED PERSONS

1) The number and style of this appeal is No. 09-31169, *John Hancock Life Insurance Company v. United States of America*.

2) The Clearing House Association L.L.C. (“The Clearing House”) is a limited liability company and as such has no shareholders. Rather, each member of The Clearing House holds a proportionate limited liability interest in The Clearing House. The Clearing House, The Financial Services Roundtable, and The Securities Industry and Financial Markets Association (collectively, the “*amici*”), are not subsidiaries of other corporations, and no publicly held corporation owns 10% or more of their stock. *Amici* are unaware of persons with an interest, as set forth in Fifth Circuit Rule 28.2.1, in the outcome of this case, other than the parties to this appeal, and those interested persons listed in their briefs. These representations are made in order that the judges of this court may evaluate possible disqualification or recusal.

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INTRODUCTION

Pursuant to Fed. R. App. P. 29(a), The Clearing House Association L.L.C. (“The Clearing House”), The Financial Services Roundtable (the “Roundtable”), and the Securities Industry and Financial Markets Association (“SIFMA”) (collectively, “*amici*”), respectfully submit this brief of *amici curiae*, with the consent of both parties, in support of the appeal of Plaintiff-Appellant John Hancock Life Insurance Company (“Hancock”) from an Order (the “Order”) entered by the United States District Court for the Eastern District of Louisiana (Zainey, J.) on October 14, 2009, granting the motion of the Defendant-Appellee United States of America for summary judgment and denying the cross-motion of Hancock for the same relief. The Order granted summary judgment dismissing Hancock’s claim that the U.S. Internal Revenue Service (“IRS”) wrongfully levied on certain monies held in an account at Capital One, N.A. (“Capital One”). The district court held that Hancock, as the lender, did not hold a security interest entitled to protection against subsequent government tax liens because Capital One, the “indenture trustee” which administered the loan on behalf of Hancock, was the sole holder of a security interest with respect to the borrower.

The *amici* submit that the decision below was in error because the court ignored clear statutory guidance and incorrectly treated Hancock and the trustee as though they were legally distinct and separate parties for these purposes.

26 U.S.C. § 6323(e)(2) provides that priority over a subsequent tax lien extends to the charges of an indenture trustee “holding the security interest for the benefit of the *holder* of the security interest.” (Emphasis added.) Contrary to the district court’s holding, therefore, that holder of the security interest in this case is Hancock. The court below never mentioned Section 6323(e)(2). Moreover, the trustee is the holder’s agent and only represents the holder’s rights with respect to the obligor. The court also ignored binding authority concerning this issue.

As a policy matter, correcting this error is necessary to avoid widespread ramifications. As shown below, the indenture provisions on which the court – having separated Hancock from the trustee – determined that Hancock was not a holder of a security interest are standard provisions established in accordance with federal law. These provisions appear in innumerable indentures affecting probably hundreds of billions of dollars worth of collateralized bonds outstanding across the nation. Similar provisions in indentures have been used to administer bond offerings for over 170 years and, since 1939, the federal securities laws have *required* the use of indenture trustees in virtually all publicly traded debt transactions. In addition, as here, indentures and indenture trustees are also employed voluntarily in countless non-publicly traded debt transactions.

If not reversed, the district court’s erroneous construction of federal law will expose the collateral underlying all these bonds to the risk of later-arising

government tax liens, thereby undermining the continued viability of indenture trustee arrangements in the bond markets. That outcome will significantly increase the burdens and risks facing parties currently involved in the bond markets and inevitably increase the costs of borrowing. And any uncertainty created by the decision below is magnified because of the uniformity of the provisions at issue:

[U]niformity in interpretation is important to the efficiency of capital markets. . . . [T]he creation of enduring uncertainties as to the meaning of boilerplate provisions would decrease the value of all debenture issues and greatly impair the efficient working of capital markets. Such uncertainties would vastly increase the risks and, therefore, the costs of borrowing with no offsetting benefits either in the capital market or in the administration of justice.

Sharon Steel Corp. v. Chase Manhattan Bank, N.A., 691 F.2d 1039, 1048 (2d Cir. 1982); see *Broad v. Rockwell Int’l Corp.*, 642 F.2d 929, 943 (5th Cir. 1981) (*en banc*) (“A large degree of uniformity in the language of debenture indentures is essential to the effective functioning of the financial markets.”).

Obligors who fail to make payments on secured debt often fail to pay taxes too, and the court’s decision has altered impermissibly the statutory priorities between secured lenders and the IRS, with potentially devastating effects. This Court should reverse.

STATEMENT OF THE IDENTITY AND INTERESTS OF *AMICI CURIAE*

The Clearing House is an association of leading commercial banks which, through an affiliate, provides payment, clearing and settlement services to its member banks and other financial institutions.¹ The Clearing House regularly appears as *amicus curiae* in cases that raise significant legal issues relating to banking, and in particular in cases like this one that raise important questions concerning the framework for virtually all publicly traded debt offerings.

The Roundtable represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. Roundtable members account directly for \$74.7 trillion in managed assets, \$1.1 trillion in revenue, and 2.3 million jobs.

SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with

¹ The members of The Clearing House are: Bank of America, N.A.; The Bank of New York Mellon; Capital One, N.A.; Citibank, N.A.; Deutsche Bank Trust Company Americas; HSBC Bank USA, N.A.; JPMorgan Chase Bank, N.A.; The Royal Bank of Scotland, N.V.; UBS AG; U.S. Bank N.A.; and Wells Fargo Bank, N.A. Capital One, N.A., is the indenture trustee in the debt offering at issue here.

offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association.

As leading associations of banks and other financial services companies, the *amici* have a substantial interest in protecting purchasers of secured debt, which have contracted for what were heretofore universally understood as secured interests, against being treated effectively as *unsecured* creditors under federal law. Banks and other financial institutions frequently serve as indenture trustees, as underwriters for secured debt offerings, and as buyers of secured debt issued pursuant to security agreements involving indenture trustees. The indenture provisions used in this case and, as required by the federal securities laws, in virtually all publicly traded debt offerings, are essential to maintaining the uniformity and predictability, and thus the value and marketability, of secured debt issued under indentures. If not reversed, the district court's misreading of Section 6323 would leave banks and other bondholders unprotected against the risk of later-arising tax liens, increasing the costs of borrowing and damaging the interests of issuers, investors and the general public.

BACKGROUND

1. Background Regarding Indenture Trustees

The use of indenture trustees in connection with secured debt offerings dates to the early nineteenth century, when railroads issuing debt secured by mortgages concluded that it had become “impractical to name all of the original bondholders as mortgagees.”² Martin D. Sklar, *The Corporate Indenture Trustee: Genuine Fiduciary or Mere Stakeholder?*, 106 Banking L.J. 42, 43 (1989). Their solution was to formulate a security arrangement that would permit mortgagees to purchase and obtain security against a debt, while also providing for the efficient “change of ownership through trading in the bonds.” American Bar Foundation (“ABF”), *Commentaries on Indentures* 5 (1971) (“*Commentaries*”);³ see also Talcott M. Banks, Jr., *Indenture Securities and the Barkley Bill*, 48 Yale L.J. 533,

² Secured debt issued under indentures typically involves “bonds,” which are long-term secured obligations. For convenience, hereinafter, we will use the term “bonds” to refer to any secured obligations involving indenture trustee agreements, and the holders of those obligations, such as Hancock, will be identified as “bondholders.” The terms “issuer” or “borrower” will be used interchangeably to refer to the entity, such as the Schwegmann Trust here, which has issued the debt and retains the obligation to repay it. We will use the term “trustee” to refer to indenture trustees, such as Capital One.

³ The *Commentaries on Indentures* are included in the American Bar Foundation, *Commentaries on Model Debenture Indenture Provisions 1965 - Model Debenture Indenture Provisions All Registered Issues 1967 and Certain Negotiable Provisions Which May Be Included in a Particular Incorporating Indenture* 1 (1971). See *Broad v. Rockwell Int’l Corp.*, 642 F.2d 929, 932 (5th Cir. 1981) (*en banc*) (discussing the *Commentaries on Indentures* in connection with the court’s observation that indenture agreements usually include “boiler-plate” provisions that are “virtually the same for all indentures”).

534 (1939) (“[A] mortgage split among a number of mortgagees involved undesirable technical difficulties in transfer and foreclosure, and it lacked the inducement of negotiability.”). Under the indenture trustee structure, all mortgageable assets were to be transferred to a single trustee, which would hold them as agents for the benefit of all bondholders. *Id.*

Indenture trustees soon became the preferred means of administering secured debt offerings. Employing an indenture trustee allowed the efficient creation and transfer of debt in a manner best suited to “establish contact between the money needs of the business world on the one hand and the multitude of investors on the other.” Louis S. Posner, *Liability of the Trustee Under the Corporate Indenture*, 42 Harv. L. Rev. 198, 198 (1928) (“The annual investment of hundreds of millions of dollars in securities issued under such indentures is proof of the necessity no less than of the popularity of the device.”). Seventy-one years ago, in response to certain perceived abuses in the capital markets, Congress enacted the Trust Indenture Act of 1939 (the “TIA”), Pub. L. No. 76-253, 53 Stat. 1149 (codified as amended at 15 U.S.C. §§ 77aaa-77bbbb). The TIA mandated that virtually all public debt offerings adopt a particular form of indenture, one that emphasized the trustee’s role in protecting the interests of bondholders. *See, e.g.*, 15 U.S.C. § 77bbb(a)(2). The TIA made clear that the presence of indenture trustees as intermediaries was not intended to dilute the interests or control of

bondholders but for the purpose of ensuring the “protection and enforcement” of their rights as investors. See Efrat Lev, *The Indenture Trustee: Does It Really Protect Bondholders?*, 8 U. Miami Bus. L. Rev. 47, 73 (1999) (“[T]he [Trust Indenture Act] itself was supposed to be the investor’s silent representative in the drafting process of the indenture.”).

Over the last several decades, the role of the indenture trustee has been acknowledged as a “practical necessity whenever there are any substantial number of holders of the debt securities,” even where its use is not prescribed by the TIA.⁴ See *Commentaries* at 8. The modern indenture trustee’s role includes “pure trustee functions,” such as pursuing litigation on behalf of the bondholders in the event of default, as well as its more ministerial functions as a “transfer agent and paying agent” in administering the sale of debt. *Id.* As this Court has observed, the presence of the trustee is essential to ensuring the marketability of secured debt and the administration of debt offerings in the bond markets:

It would be wholly impractical to have the security run to the group of bondholders directly or to have a separate security instrument for each bondholder. Such action

⁴ By its terms, the TIA only “applies to securities sold to the public by use of the mails or in interstate commerce.” *E.F. Hutton Southwest Prop. II v. Union Planters Nat’l Bank*, 953 F.2d 963, 968 (5th Cir. 1992). However, even secured debt offerings exempt from the TIA typically employ indenture trustees that, as in the instant case, have the same rights and responsibilities as those governed by the TIA. This is because, regardless of whether the TIA applies, indenture agreements typically adhere to the provisions reflected in the model indentures.

would cause crippling complexity in the execution and enforcement of the security and in cases of transfers of the bonds. To make the transaction feasible *the security interest must be centered in a single entity which is to act for the bondholders* who purchase their bonds from time to time and for their successors in interest.

E.F. Hutton Southwest Prop. II v. Union Planters Nat'l Bank, 953 F.2d 963, 967 (5th Cir. 1992) (emphasis added) (quotation marks and citation omitted). Because the uniformity of indenture provisions supports the consistent application of their terms and allows lower costs, they are used whether there is one bondholder or multiple bondholders. Moreover, even when a transaction starts with one bondholder like Hancock, these provisions support that bondholder's ability to sell its position, including to more than one potential bondholder. Thus, the district court's ruling will affect the *entire* secured bond market.

Virtually all modern indentures, including the one at issue here, adhere to the model indenture provisions drafted by the American Bar Foundation ("ABF") and the American Bar Association ("ABA"). 3 A.A. Summer, Jr., *Securities Law Techniques* § 27.03[2] (2009). Given the length and complexity of indenture trust agreements, this Court has noted the importance of these models and their "boiler-plate" provisions:

A large degree of uniformity in the language of debenture indentures is essential to the effective functioning of the financial markets: uniformity of the indentures that govern competing debenture issues is what makes it possible meaningfully to compare one debenture issue

with another, focusing only on the business provisions of the issue (such as the interest rate, the maturity date, the redemption and sinking fund provisions and the conversion rate) and the economic conditions of the issuer, without being misled by peculiarities in the underlying instruments.

Broad v. Rockwell Intern. Corp., 642 F.2d 929, 943 (5th Cir. 1981); *see, e.g., Leverso v. Lieberman*, 18 F.3d 1527, 1531 (11th Cir. 1994) (“[T]rust indenture boilerplate provisions . . . were developed in order to standardize debenture indenture contractual rights and provide uniformity to the financial market. It is therefore imperative that the terms of the indenture govern the parties’ contractual rights as determined by the judiciary.”) (citing the *Commentaries* 1-3).

The most closely applicable form indentures in this case are the ABF’s *Mortgage Bond Indenture Form* (1981) (the “ABF Form”) and the ABA’s *Revised Model Simplified Indenture*, 55 Bus. Law. 1115 (May 2000) (the “ABA Model”).⁵ These model indentures, and the analogous provisions in the TIA, make clear that virtually all modern indenture agreements, including those under which there may initially be only one bondholder, typically share the following features:

- Indenture agreements are executed only by the issuer and the trustee. *See* ABF Form at 1, 188; ABA Model at 1118. The agreement typically does *not* identify specific bondholders nor is it executed by any individual bondholders, given that the principal purpose of the indenture mechanism is to avoid the “crippling complexity” and “impracticality” of having the “security run to the group of bondholders directly or to have a

⁵ These documents are attached as addenda to Hancock’s principal brief.

separate security instrument for each bondholder.” G. Bogert, *The Law of Trusts and Trustees* § 250 (2009).

- The trustee is granted the security interest in the underlying collateral, for the benefit of the bondholders. See ABF Form at 1, 6-7. As a practical matter, the grant of the security interest to the trustee is what makes the indenture agreement such an effective device for maintaining the value and marketability of secured debt. See 15 U.S.C. § 77bbb(a)(1) (stating that “the national public interest and the interest of investors . . . are adversely affected . . . when the obligor [or, borrower] fails to provide a trustee to protect and enforce the rights and to represent the interests of such investors”).
- In the event of the borrower’s default, a specified number of bondholders may issue a binding directive to the trustee to pursue legal remedies against the borrower. See ABF Form at 120; ABA Model at 1137; see also 15 U.S.C. § 77ppp(a)(1). As noted in the *Commentaries*, the “major purpose” of this feature of indenture agreements is to deter a multitude of suits by individual bondholders for “unworthy or unjustifiable reasons.” *Commentaries* at 232. This is purely a contractual limitation on bondholders’ suits and does not divest them of any portion of their respective security interests in the collateral securing the debt.
- In the event that the trustee fails to take action as directed by the bondholders within a specified period of time, the bondholders themselves may pursue legal remedies directly against the borrower. See ABF Form at 119; ABA Model at 1137-38; see also 15 U.S.C. § 77ppp(b).
- The trustee may be removed at any time by a majority of the bondholders, without cause and without notice to the borrower. ABF Form at 135; ABA Model at 1143.
- The trustee is the party responsible for enforcing and monitoring the bondholders’ rights in connection with the indenture. See 15 U.S.C. § 77bbb (providing that trustees must “have adequate rights and powers, or adequate duties and responsibilities, in connection with matters relating to the

protection and enforcement of the rights of such investors [*i.e.*, bondholders]” and that “the trustee is under an affirmative duty to take action for the protection and enforcement of their rights”).

The indenture in this case includes all of the features of the typical indenture outlined above. These are the same features prescribed by Congress in the TIA, which have heretofore been construed as applying to secured interests for all purposes, including protection against subsequent federal tax liens. Put simply, there is absolutely nothing in the security arrangement in this case that distinguishes it from the typical indenture trustee agreement, or that limits or narrows the security interests normally possessed by a bondholder in such an agreement. That is why the district court’s ruling that these provisions mean the lender is not the holder of a security interest, *see* R.707-08, is not only erroneous as a matter of law, but contrary to sound policy as implemented by both Congress and the market.

2. The Proceeding Below

In May 1994, the Schwegmann Family Trust No. 2 (the “Schwegmann Trust”) borrowed in excess of \$9 million from Hancock and executed several promissory notes, a mortgage of commercial property, an assignment of leases and rents, and an indenture with the predecessor of Capital One (collectively, the “Agreements”), all for the benefit of Hancock. Thirteen years later, on December 10, 2007, the IRS issued a notice of levy to Capital One,

the indenture trustee for the promissory notes held by Hancock. The IRS sought to levy on \$397,041.85 from accounts (the “Accounts”) held by the Schwegmann Trust at Capital One that, pursuant to the Agreements, secured the loans and contained funds for servicing of the loans. R.20-21.

On July 11, 2008, Hancock initiated this action pursuant to 26 U.S.C. § 7426(a)(1), claiming that the IRS wrongfully levied on the funds held in the Accounts. On October 14, 2009, following argument on the parties’ cross-motions for summary judgment, the district court issued the Order granting the government’s motion for summary judgment. The Order framed the question below as follows:

[I]f Hancock can establish that it falls within the narrow class of stakeholders enumerated in § 6323(a) with respect to the funds held in the Capital One accounts, *i.e.*, if it is the holder of a security interest, then its interest in the funds will prime the IRS’s lien and the levy will have been improper.

R.701. In resolving this question, the district court stated that it was unable to identify any guidance in federal or state law as to the definition of the term “holder” of a security interest under Section 6323(a). R.703. As discussed herein, the court inexplicably failed to take note of direct guidance in both. The district court concluded that “a security interest could be granted in *favor* of one party but for the *benefit* of another,” but treated the trustee and the lender as separate parties rather than as agent and principal. R.703 (emphasis in original). The district court

listed a number of the provisions described above and found in the parties' Agreements and, based on those provisions, the court ultimately concluded that Hancock was not a "holder" of a security interest under Section 6323.

The district court reached this conclusion without, it appears, having considered the remaining provisions of Section 6323, including Section 6323(e)(2) (which would have yielded a clear answer to the question), or controlling state law authority concerning the unitary interests of lenders and their indenture trustees. The district court determined that "Capital One was the 'holder' of the security interest, not Hancock," R.708, but that Capital One was not the "holder" of the security interest for the purposes of Section 6323 because it had lent no money. R.710. The court deemed this an "unfortunate result . . . when a security interest is held by a fiduciary for the benefit of another party." *Id.*

The only discernible focus of the district court's inquiry appeared to be that the lender, Hancock, was not specifically named in the indenture or mortgage agreements or related documents, which only referenced Capital One and unnamed "Note Holders." R.707-09. In the district court's view, this "compel[led] the conclusion that the security interest was created directly in favor of Capital One as opposed to Hancock or any other note holder," although the court cited no case law in support. R.707. Despite the fact that Capital One possessed its rights under the indenture only for the benefit of Hancock, the court

said that Hancock had been confined to a “limited and passive role with respect to the security,” although the court did not attempt to explain why this made a difference, and held that Hancock therefore was not a “holder of a security interest” within the meaning of Section 6323(a).

SUMMARY OF ARGUMENT

Section 6323(a) protects secured creditors' collateral in the event that the borrower becomes subject to a later-arising federal tax lien. In concluding that Capital One but not Hancock was the "holder of a security interest" within the meaning of the statute, the court ignored the clear guidance in the very statute it was considering and incorrectly treated Hancock, the bondholder, and Capital One, the indenture trustee, as though they were unrelated parties. In doing so, the court overlooked or ignored settled law concerning the identity of interest between the bondholder and the indenture trustee.

Contrary to the court's conclusion that Hancock was not a "holder" of a security interest, the plain text of Section 6323(e)(2) clearly indicates that bondholders like Hancock – who purchased debt subject to a security arrangement employing an indenture trustee – are protected by the statute: "the priority of a [pre-existing] lien or security interest shall extend to . . . (2) the reasonable charges and expenses of an indenture trustee or agent holding the security interest for the benefit of the holder of the security interest;" That holder can only be the bondholder – here, Hancock.

The court's reasoning calls into question the viability of countless indentures which, as required by the federal securities law, underpin virtually every publicly traded bond in the United States. By holding that Hancock is not

protected by Section 6323(a), the district court has effectively concluded that *no* bondholder with an indenture trustee is protected by Section 6323(a) against later-arising tax liens. Congress plainly did not intend that its far-reaching requirements for the use of indenture trustees would be critically undercut by the risk that bondholders' collateral would be exposed to later-arising government tax liens.

If not reversed, the district court's holding will inflict costs on the bond market far beyond this case. Undermining the priority of secured debt involving indenture trustees would almost certainly result in the loss of the advantages indenture trustees provide to the bond market – namely, enabling bondholders to overcome the collective action problem in monitoring their investments and maintaining the efficient transferability of secured debt. At a minimum, the court's reasoning, if not rejected in this appeal, poses a serious threat to the uniformity of indenture provisions employed in secured debt offerings within the Fifth Circuit. The mere creation of uncertainty concerning the substance and form of indenture provisions imposes substantial, entirely unnecessary additional costs for conducting transactions in the bond markets.

ARGUMENT

I. SECURED CREDITORS WHO ARE PARTIES TO TRUST INDENTURE AGREEMENTS ARE HOLDERS OF SECURITY INTERESTS PURSUANT TO SECTION 6323(a)

Section 6323(a) provides that a federal tax lien “shall not be valid” as against a “holder of a security interest” that was established prior to the filing of notice of the lien. 26 U.S.C. § 6323(a); *see, e.g., Matter of Sills*, 82 F.3d 111, 112-13 (5th Cir. 1996). The provision is designed to ensure that secured creditors are protected against losing their collateral in the event that the borrower becomes subject to a later-arising federal tax lien. *See, e.g., Air Power, Inc. v. United States*, 741 F.2d 53, 55 (4th Cir. 1984) (“Congress’ purpose in imposing the notice requirement on the government was to protect the perfected interests of innocent third parties from ‘secret tax liens.’”).

The application of Section 6323(a) should have been straightforward in this case. Section 6323(h)(1) defines a “security interest” as being composed of the following five elements: (1) “any interest” in property; (2) “acquired by contract”; (3) “for the purpose of securing payment of an obligation”; (4) that is “protected under local law against a subsequent judgment lien arising out of an unsecured obligation”; and (5) for which “the holder has parted with money.” 26 U.S.C. § 6323(h)(1). It is clear that all five of these elements are satisfied in connection with the rights and interests conferred on Hancock by the indenture in

this case. The *amici* agree with and join in the arguments advanced by Hancock on this issue.

However, the district court failed to address *any* of the elements of the statutory definition of a “security interest” under Section 6323(h)(1), including whether Hancock, having satisfied the other elements and “parted with [its] money,” logically had to be the holder of any security interest. The district court instead found no legal guidance to assist the inquiry as to whether Hancock was a “holder” of a security interest under Section 6323(a), R.703, and, in the supposed absence of such guidance, somehow concluded that Hancock was not a “holder” of a security interest.

But it is clear that the guidance sought by the district court is found in Section 6323 itself, which guidance, astonishingly, the opinion below does not even mention. Section 6323(e)(2) provides that the value of a security interest protected by the statute should include “the reasonable charges and expenses of an *indenture trustee or agent* holding the security interest *for the benefit of the holder of the security interest.*” 26 U.S.C. § 6323(e)(2) (emphasis added). This provision plainly indicates that the holder of the security interest for the purposes of Section 6323 is the bondholder. Section 6323(e)(2) states that the priority includes the expenses and charges of the indenture trustee, which holds the security interest in a representative capacity on behalf of the actual holder, the bondholder. Any

argument that the presence of an indenture trustee somehow diminishes the bondholder's status as a "holder of a security interest" within the meaning of Section 6323(a) is precluded by Section 6323(e). *Id.*; *see also* 15 U.S.C. § 77ppp(b) (TIA) ("[T]he right of any holder of any indenture security to receive payment of the principal of and interest on such indenture security, on or after the respective due dates expressed in such indenture security . . . shall not be impaired."). Given the unambiguous language in Section 6323(e)(2) that bondholders who employ indenture trustees are considered "holders of a security interest," it is simply not plausible that the same word, "holder," would have the opposite meaning in Section 6323(a).⁶

The court also erred in treating Hancock, the bondholder, and Capital One, the trustee, as though they were unrelated parties to conclude that Capital One but not its principal, Hancock, was the "holder" of a security interest. It is settled

⁶ Based on the date that Congress enacted part (e)(2) of Section 6323, it is clear that the "indenture trustee" mechanism referenced in that provision describes precisely the same indenture trustee mechanism involved in this case. The "indenture trustee" provision was added as part (e)(2) of Section 6323 in 1966, *after* the enactment of the TIA in 1939 and the publication of the ABF's first model indenture in 1965. *See* Federal Tax Lien Act of 1966, Pub. L. No. 89-719, 80 Stat. 1125; *see also Commentaries* at ix. Thus, each of the indenture provisions highlighted by the district court that, in its view, indicated Hancock was not a "holder" of a security interest would have been present in substantially the same form in the TIA and the ABF's model indenture provisions prior to the addition of Section 6323(e)(2) to the tax code.

law that the indenture trustee serves as the bondholder's agent and only represents the bondholder's rights with respect to the obligor. *See In re Plankinton Bldg. Co.*, 135 F.2d 273, 275 (7th Cir. 1943) ("Certainly at the time that this bargain, embodied in the trust indenture, was made between the debtor and the indenture trustee *as agent for the bondholders*, the contracting parties contemplated that the indenture trustee should represent all the bondholders.") (emphasis added); *In re FSC Corp.*, 64 B.R. 770, 772 (Bankr. W.D. Pa. 1986) ("[T]he Indenture Trustee acted as an agent for its principals, the debenture holders.").

The Agreements here are governed by and specifically incorporate provisions of Louisiana law, which also provides that an indenture trustee acts as the bondholder's agent, and that, to the extent the trustee holds any security interest with respect to the borrower, it is also held by the bondholder. In Louisiana, an indenture trustee serves as the "fiduciary for the holders of the obligations" where, as here, the underlying contract names the trustee as the "mortgagee in trust for the benefit of the creditors."⁷ La. Rev. Stat. § 9:5302. The trustee is thereby established as the "special attorney-in-fact" for the bondholder, La. Rev. Stat. § 9:5302, or, in other words, the bondholder's agent. *See Ross v. Ross*, 857 So.2d

⁷ As summarized in Hancock's principal brief, the Agreements in this case expressly provide that Capital One assumes the role of "indenture trustee," serving as the "special attorney-in-fact" for Hancock and retaining powers only "on behalf of the Note Holders." Hancock here is the sole "Note Holder." R.77.

384, 397 n.9 (La. 2003) (“An agent is one who acts for or in place of another by authority from the latter.”). Given these authorities, any “security interest” held by Capital One as trustee here was necessarily held by Hancock, the bondholder, as well. See La. Civ. Code art. 3022 (“A third person with whom a mandatary [*i.e.*, “agent”] contracts in the name of the principal, or in his own name as mandatary, is bound to the principal for the performance of the contract.”).

As acknowledged by the district court, a trustee may hold a “security interest as a fiduciary for the protection and benefit of another party.” R.707-08. Applying this principle, the court concluded that Hancock indeed held an “interest in the secured property” that was “not divest[ed]” by “Capital One’s agency status.” R.707-08. These observations make clear that, even in the view of the district court, Hancock held an “interest in the secured property,” R.708, – *i.e.*, a security interest – through its agent Capital One that was valid under Louisiana law. In the court’s view, however, Hancock’s “interest in the secured property” somehow did not merit protection under Section 6323(a). R.708.

Contrary to the court’s erroneous construction of applicable law, there is no question that Louisiana law and the Uniform Commercial Code (“UCC”) provide that indentures, like the agreement at issue here, establish a security interest in favor of the bondholder, which is also held in a representative capacity by the trustee. Nothing in federal law is to the contrary. Article 9 of the UCC,

which has been enacted in Louisiana, expressly provides that the term, the “Secured Party,” in a security agreement includes *both* the “person in whose favor a security interest is created or provided for” *and* the “indenture trustee, agent, collateral agent, or other representative in whose favor a security interest . . . is created or provided for.” See La. Rev. Stat. §§ 10:9-102(72)(A), (E). Indeed, as the provisions of the UCC make clear, security interests are *routinely* held by trustees or agents in representative capacities on behalf of the holders of the security interest themselves. For instance, Section 9-503(d) of the UCC, which concerns the technical requirements for financing statements, expressly permits the secured party’s representative to file a financing statement on the secured party’s behalf, and deems such a filing “sufficien[t]” even where the statement omits the name of the secured party itself: “Failure to indicate the representative capacity of a secured party or representative of a secured party does not affect the sufficiency of a financing statement.” La. Rev. Stat. § 10:9-503(d).

By holding that Hancock is not protected by Section 6323(a), the district court effectively found that *no* secured creditor protected by a trust indenture agreement could be covered by the statute. In the TIA, Congress formulated a detailed framework that required the use of indenture trustees in a broad category of secured debt transactions – in fact, even five years before the TIA’s passage, “approximately \$40 billion in corporate debt securities were issued

under trust indenture agreements.” Steven L. Schwarcz, *Intermediary Risk in a Global Economy*, 50 Duke L.J. 1541, 1543 (2001) (citing Joel Seligman, *The Transformation of Wall Street: A History of the Securities and Exchange Commission and Modern Corporate Finance* 194 (rev. ed. 1995)). Congress plainly did not intend to institute such a far-reaching requirement only to undercut the indenture trustee mechanism by excluding bondholders from protection against later-arising government tax liens. Even if Congress had intended to adopt such a sweeping limitation – one that would significantly diminish the value and marketability of any debt subject to an indenture – surely it would not have done so *sub silentio*, without a clear legislative directive.

The clear language of Section 6323(e), the requirements of the TIA, the practices of the bond market applying these provisions of federal law, and the consistent legislation enacted by the State of Louisiana all demonstrate that bondholders such as Hancock are to be protected. Hancock is a “holder of a security interest” entitled to protection under Section 6323(a) against later-arising tax liens.

II. THE DISTRICT COURT'S HOLDING UNDERMINES THE WELL-SETTLED FRAMEWORK FOR ADMINISTERING SECURED DEBT OFFERINGS IN THE BOND MARKET

The district court's holding that Hancock, as a secured creditor subject to an indenture agreement, is excluded from the protection of Section 6323(a), threatens repercussions throughout the financial markets. The indenture provisions found in this case are also found in some form in virtually all publicly traded debt offerings. Therefore, unless reversed, the Order will significantly increase the burdens and risks for parties involved in the bond market or other secured debt transactions.

The district court's erroneous reasoning exposes bondholders to the risk of being treated as *unsecured* creditors in the event of a later tax delinquency by the issuer, which is likely to occur in the too typical situation when an issuer struggling to meet its debt obligations is also then unable to satisfy its tax burden. The result of the district court's holding is that the express purpose of Section 6323 – to protect secured creditors against later-arising government tax liens – would be subverted in connection with the statute's application to the bond markets. The impact of this change could be staggering.

For bondholders, the potential exposure of their secured collateral to government tax liens would significantly diminish the value and transferability of their debt investments, especially given the increased potential for borrowers to

default on both their debt and tax obligations in difficult economic times. Bondholders involved in security arrangements covered by the TIA would be caught – they would be required by the federal securities laws to continue using the indenture trustee structure but, as a result, would also be forced to accept the potential of a substantially lower value for their investments. The flow of capital into the bond market would be reduced, and issuers would be unable to expand and create jobs, as potential purchasers of debt evaluate the previously unheard-of risk that their security interests would be subject to later-arising government tax liens against issuers. The costs of borrowing inevitably would increase.

If the district court's decision is not reversed, parties looking to purchase secured debt outside of the mandates of the TIA may simply refuse to tolerate the risk involved in signing trust indenture agreements unprotected against subsequent federal tax liens, and may not continue to use the same form of indentures and provisions as mandated under the TIA. This threat to the uniformity of indenture trustee agreements would raise the price of entering into and completing transactions in the capital markets. "Such uncertainties would vastly increase the risks and, therefore, the costs of borrowing with no offsetting benefits either in the capital market or in the administration of justice." *Sharon Steel Corp.*, 691 F.2d at 1048; see *Broad*, 642 F.2d at 943 ("A large degree of

uniformity in the language of debenture indentures is essential to the effective functioning of the financial markets.”).

Only a clear legal mandate should move a court to undercut the indenture trustee component of secured debt offerings, given that it has, in some form or another, guided the administration of debt issues for nearly two centuries and has been adopted by the federal securities laws as the central component of security arrangements in the bond markets. The district court failed to identify any reason in law or fact to create such a counter-productive and market-disruptive result.

CONCLUSION

For the foregoing reasons, the *amici* respectfully request that this Court reverse the judgment of the district court.

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CERTIFICATE OF COMPLIANCE WITH RULE 32(a)

This brief complies with the type-volume limitation of Fed. R. App. P. 29(d) because the brief contains 6,354 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii). This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft Word 2007 in 14-point Times New Roman font.

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