

STATE OF NORTH CAROLINA
COUNTY OF MECKLENBURG

IN THE GENERAL COURT OF JUSTICE
SUPERIOR COURT DIVISION
C.A. No. 07 CVS 5097

WACHOVIA BANK, NATIONAL)
ASSOCIATION and WACHOVIA CAPITAL)
MARKETS, LLC,)

Plaintiffs)

v.)

HARBINGER CAPITAL PARTNERS)
MASTER FUND I, LTD. et al.,)

Defendants)

DEFENDANTS' MEMORANDUM IN SUPPORT OF MOTION TO DISSOLVE
PRELIMINARY INJUNCTION AND STAY ACTION

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PRELIMINARY STATEMENT

On November 1, 2006, after news broke of its massive fraud, Le Nature's, Inc. was placed into involuntary bankruptcy by several of its creditors. Le Nature's' long-term advisor and investment banker, Wachovia Capital Markets, LLC ("Wachovia"), together with its affiliate Wachovia Bank, National Association ("Wachovia Bank"), fully expected that they would be sued for enabling, assisting, and effectuating the fraud. Knowing that they would be sued by, among others, the purchasers of Le Nature's debt on the secondary market, the Wachovia entities filed this action in a preemptive attempt to block those claims by several such purchasers (the "Secondary Lenders"). They sought a judicial declaration that any such claims would be champertous, and obtained the preliminary injunction that is now in place. The injunction prevents Defendants from asserting certain tort claims against Plaintiffs in any forum other than this Court.

In issuing the injunction, Judge Ervin stated that he was not adjudicating Plaintiffs' underlying claims of champerty; rather, he was issuing the injunction solely to prevent a multiplicity of cases being filed in numerous courts raising similar claims. Judge Ervin expressed the concern that absent an injunction there might be inconsistent resolutions in different courts. Pursuant to the injunction, Judge Ervin required that Defendants assert any state law personal tort claims in this Court.

On September 17, 2007, Defendants herein, joined by several of the initial lenders to Le Nature's who are not parties to this action (the "Initial Lenders"), filed a complaint (Exhibit A hereto) in the United States District Court for the Southern District of New York, asserting federal and state law claims against Wachovia, BDO Seidman, LLP ("BDO"), and two of Le Nature's' executives (the "New York Action"). The filing of the New York Action did not contravene this Court's order, in part because the Defendants herein do not, in that action, assert against Wachovia any of the state law tort claims covered by the order.

The filing of the New York Action by holders of Le Nature's debt (both the Initial Lenders and the Secondary Lenders) demonstrates that the preliminary injunction entered in this case is unnecessary and should be dissolved. As a result of the joinder of so many lenders in a single, comprehensive case against most potentially responsible parties, the risk Judge Ervin identified – a multiplicity of cases in numerous courts – will not materialize. To the extent they own interests in the Le Nature's debt, all the Defendants in this case have joined in a single action in a single jurisdiction. That action is the most efficient vehicle for resolving these disputes because the Defendants here are asserting their claims side-by-side with several Initial Lenders which are not, and could not be, defendants in this case. In addition, the New York Action includes claims against the accountants and Le Nature's executives that are not covered by this Court's preliminary injunction. Accordingly, an injunction to avoid a multiplicity of suits is no longer necessary or appropriate.

If the preliminary injunction were to remain in effect, the only result would be the multiple suits this Court sought to avoid. The federal claims against Wachovia, Defendants' state law claims against BDO and the Le Nature's executives, and all the Initial Lenders' claims would proceed in New York. And, in adjudicating those claims, the federal court would necessarily address Wachovia's champerty defense. Thus, if the preliminary injunction requires Defendants to pursue their state law tort claims against Wachovia in this Court, two suits will go forward. For this reason, the injunction should be dissolved.

Separately, but equally important, Defendants respectfully submit that the Court erred in issuing the preliminary injunction by attempting to bar the assertion of state law claims in federal court. In *Donovan v. City of Dallas*, 377 U.S. 408 (1964), the United States Supreme court ruled that state courts lack the power to enjoin parties from asserting claims in federal court. Thus, the

preliminary injunction should be dissolved even if it could achieve its stated purpose of preventing multiple suits – which it cannot.

In addition to dissolving the preliminary injunction, this Court should stay this action. The affirmative claims that Plaintiffs attempt to bar in this action will now be litigated, with additional claims and additional parties, in a single, plenary action in New York. As shown below, all the factors to be considered in assessing such a stay – including the nature of the case and the availability of evidence and witnesses – favor staying this case pending resolution of the New York Action. The New York Action is a far more complete proceeding. In that case, the plaintiffs assert affirmative claims for relief (as opposed to the defensive claims asserted here) on behalf of more plaintiffs and against more defendants.

This Court should permit the efficient prosecution of all claims by dissolving the preliminary injunction and staying this case pending resolution of the New York Action.

STATEMENT OF FACTS

Background to the Parties' Dispute. On or about September 1, 2006, Le Nature's, Inc. borrowed \$285,000,000 in a loan arranged and underwritten by Wachovia, which then “syndicated” the loan by selling virtually all the indebtedness to numerous banks and investors. Through the syndication process, those banks and investors became lenders to Le Nature's. As a result of the syndication, Wachovia generated massive fees for itself and reduced Wachovia Bank's share of the debt – and concomitant risk – to less than \$10,000,000.

Later, less than 60 days after Wachovia and its affiliates laid off almost all their exposure, it was publicly revealed that Le Nature's was a massive fraud. Among many false statements, the Company had reported sales bearing no relation to its actual results. In 2005, for example, Le Nature's reported net sales of over \$275,000,000, when its true revenues (as determined by a court-appointed custodian) were as low as \$32,000,000. Accordingly, on November 1, 2006, a

group of Le Nature's' creditors placed the Company in involuntary bankruptcy. Le Nature's ceased operations shortly thereafter.

For many years preceding Le Nature's' demise, Wachovia was Le Nature's trusted advisor and confidant, and earned tens of millions of dollars in fees by structuring, underwriting, syndicating, and managing Le Nature's' bank facilities and securities issuances, including the September 1, 2006 loan (the "Credit Facility"). As the result of this close relationship, Wachovia obtained substantial information regarding the financial improprieties and fraudulent conduct that threatened the Company's viability. Rather than disclose the materially damaging information to lenders, however, Wachovia concealed that Le Nature's (i) had repeatedly been unable to make timely interest payments, a fact that Wachovia Bank hid by fronting interest payments; (ii) was reporting sales that could not possibly be accurate; (iii) improperly recorded more than \$200,000,000 in capital leases as operating leases, thereby removing those massive liabilities from its balance sheets and facilitating false assertions of compliance with financial covenants in the loan documents; (iv) had been investigated by a special committee of its board of directors that identified serious financial reporting and managerial integrity issues; (v) disregarded specific mandates to improve accounting, inventory, and other financial safeguards; and (vi) had suffered the removal of its products from retailers' shelves. While concealing these crucial facts, Wachovia published false information that portrayed Le Nature's as a strong, growing company capable of assuming more debt.

Wachovia was not alone in assisting Le Nature's in carrying out its fraud. BDO, as the outside auditor for Le Nature's, also contributed to the deception by issuing clean audit opinions to accompany Le Nature's' financial statements for several years leading up to the Company's bankruptcy, including the year ended December 31, 2005, in which Le Nature's overstated revenues by a factor of ten. BDO was also instrumental in fraudulently misclassifying Le

Nature's massive capital lease obligations as operating leases. Without such assistance, the Credit Facility never could have been consummated.

Following Le Nature's involuntary bankruptcy, the value of interests in the Credit Facility plummeted. Consequently, various initial lenders – i.e., lenders that purchased interests in the Credit Facility directly from Wachovia Bank – sold all or portions of their Le Nature's interests on the secondary market to Secondary Lenders. This secondary market activity was specifically contemplated by the Credit Facility, which allowed lenders to sell their interests in the Credit Facility to other lenders.

The Distressed Debt Market. Many participants in the syndicated loan market, including Wachovia Bank, are members of the Loan Syndications and Trading Association (“LSTA”), a Manhattan-based trade association dedicated to the promotion and orderly development of a fair, efficient, liquid, and professional trading market for commercial loans.¹ Members of the LSTA can, among other things, sell impaired loans, known as “distressed debt.”

The U.S. distressed debt market has grown dramatically since the early 1990s when it was a small, specialty inter-bank market. In 1991, approximately \$4.4 billion of distressed debt was traded. By 2006, that amount increased nearly tenfold, to \$39.89 billion.² As has been noted, the “impressive” growth of the distressed loan trading market in the United States has been achieved “with the support of bodies such as the LSTA, [which] have revised their strategies and practices . . . to help foster a liquid and efficient marketplace. The volume of

¹ Barry Bobrow, a managing director of Wachovia Bank, is a member of the LSTA's 20-member board of directors. See Affidavit of Elliot Ganz, filed herewith (“Ganz Aff.”), ¶ 3.

² Reuters Loan Pricing Comparison, *U.S. Secondary Loan Market Volume*, available at http://www.loanpricing.com/analytics/pricing_service_volume1.htm. See also Ganz Aff. ¶¶ 4-5.

trades successfully concluded in the distressed loan trading market is a testament to the results of relentless efforts to standardize the trade process and provide uniform guidelines.”³

The LSTA has developed, and the market has adopted for use, standard documentation for the sale of interests in syndicated loans, including so-called distressed debt. The LSTA Standard Terms and Conditions (“Standard Terms”) make clear that when interests in a distressed credit facility are sold, *all* the seller’s interests are conveyed, including any rights to assert legal claims against third-parties related to the debt at issue. (Ganz Aff. ¶¶ 6, 10, and Exh. C.)

The Standard Terms also require that parties to LSTA Purchase Agreements submit any claims arising out of such debt transfers to a court in New York County applying New York law. Thus, the parties to a distressed debt sale are contractually obligated to resolve any issues related to such sale in the New York courts under New York law. (*Id.* ¶ 6.) Participants in the market benefit from the uniform application of New York law, which increases liquidity, transparency, and predictability in the market. (*Id.* ¶ 7.)

The Preliminary Injunction. Anticipating that Le Nature’s’ fraud and bankruptcy would result in claims being brought against them by Credit Facility lenders, Plaintiffs filed this preemptive action on March 14, 2007 against only a subset of the secondary lenders. In this suit, Plaintiffs seek declaratory relief, including a declaration that the LSTA Standard Terms are champertous under North Carolina law to the extent they assign tort claims as part of the sale of debt, and a declaration that such claims have not been and cannot be assigned. The suit also seeks indemnification for a proportionate share of expenses allegedly owed under the Credit

³ Beatty B. Page and Federico A. Goudie, *The Distressed Loan Trading Market In The United States*, presented at the International Bar Association Conference on “*Insolvency Is Changing Globally – How and Why*” in Seville, Spain, April 17-20, 2004.

Facility. Tellingly, none of the Initial Lenders is party to the suit, nor is BDO or any of Le Nature's' executives.

Simultaneous with the filing of their complaint, Plaintiffs obtained a broad *ex parte* temporary restraining order (replete with six pages of pre-written findings of fact and conclusions of law) enjoining the Defendants from asserting various tort claims against them anywhere at any time. The TRO was based on the assertion that Plaintiffs had heard the Secondary Lenders planned to assert claims against them. On April 12, 2007, Judge Ervin revisited the TRO and entered an order granting a much narrower injunction (the "Order") that superseded the findings of the TRO. Judge Ervin granted the injunction for the limited purpose of preventing "a multiplicity of suits in a number of jurisdictions." (Order at 6.) Judge Ervin found that if multiple suits were filed, it would be "impractical" for Plaintiffs "to obtain the determination they seek in a reasonable and orderly manner consistent with the ends of justice." *Id.* With that in mind, Judge Ervin concluded that preliminary injunctive relief was warranted until the Court resolved the personal jurisdiction issue (Order at 7, Conclusion of Law No. 1), noting that it was unclear whether the Court could even assert personal jurisdiction over the Secondary Lenders (Order at 2).

The Order is limited in a number of key respects. First, Judge Ervin made no findings whether the Court possesses personal jurisdiction over the Defendants. Second, he made no findings on champerty, including whether it applies at all to Defendants' claims, whether North Carolina law governs, or whether North Carolina's champerty rule should be modified. Third, Judge Ervin noted that "claims for breach of contract, against the Plaintiffs or others" could lawfully be assigned, and therefore ruled that the Defendants "should not be enjoined from asserting such breach of contract claims" in other jurisdictions. (Order at 8, Conclusion of Law No. 8.) Fourth, no Defendant "need be restrained from asserting unassigned Personal Tort

Claims (*i.e.*, any Personal Tort Claims not being asserted pursuant to an assignment and alleging wrongful conduct after the date on which such [Secondary Lender] first became a Lender pursuant to the Credit [Facility]).” *Id.* Finally, Judge Ervin limited the category of Personal Tort Claims subject to the injunction to claims “arising under the law of North Carolina or of any other state.” (Order at 10, ¶ 2.) Thus, the Order did not limit assertion of claims arising under federal law.

The New York Action. On September 17, 2007, various Initial Lenders (including the Missouri State Employee’s Retirement System; BlackRock Global Floating Rate Income Trust; BlackRock Limited Duration Income Trust; BlackRock Senior Income Series; BlackRock Senior Income Series II; BlackRock Senior Income Series III, PLC; Magnetite V CLO Limited; BlackRock Senior Loan Portfolio; Harch CLO II, Ltd.; and RZB Finance LLC), joined by the Defendants in this action, filed suit against Wachovia, BDO, and several of Le Nature’s executives in the United States District Court for the Southern District of New York (the “New York Action”). The plaintiffs in the New York Action own more than \$165,000,000 of the Credit Facility debt. Each of the plaintiffs in the New York Action asserted federal claims against Wachovia, BDO, and the Le Nature’s executives, including claims for violations of the RICO Act. Additionally, the plaintiffs asserted claims for fraud, aiding and abetting fraud, negligent misrepresentation, and civil conspiracy. A copy of the complaint in the New York Action is attached.

In light of, and in deference to, the preliminary injunction issued by this Court, the Defendants herein refrained from asserting state law tort claims against Wachovia in the New York Action. The Secondary Lenders did assert such claims against the other defendants, and the Initial Lenders asserted such claims directly against Wachovia. As a result, state law tort

claims against Wachovia will be addressed in the New York Action, in addition to the numerous other claims against Wachovia and the other defendants.

The Parties' Presence in New York. All parties to this action (as well as other tortfeasors and Lenders) are present in New York or are otherwise amenable to jurisdiction there. For example, the Wachovia Securities website discloses that it has \$760 billion in retail client assets and maintains offices in at least seven different locations in Manhattan. (“Wachovia Securities” is the trade name used by Wachovia.) Additionally, Wachovia, a Delaware limited liability company, boasts of its memberships in several Manhattan-based securities organizations. And Wachovia Bank identified New York as one of its principal places of business in a complaint it filed in New York in August 2007.⁴

BDO is a New York limited liability partnership that maintains several offices in New York. The Le Nature’s executives and board members named as defendants in the New York Action are Pennsylvania residents who traveled to New York to participate in meetings in furtherance of Le Nature’s fraud, including specifically meetings to promote syndication of Le Nature’s’ bank debt.

Finally, the Secondary Lenders who, joined by many of the Initial Lenders, have filed suit in New York have submitted themselves to jurisdiction there by virtue of filing the New York Action. Thus, all parties necessary to a complete resolution of the disputes raised in this action are already present and subject to personal jurisdiction in New York.

⁴ See Exhibit B hereto, Complaint in *Wachovia Bank, N.A. v. Thornburg Mortgage, Inc.*, 07-CV-7486 (S.D.N.Y. Aug. 23, 2007) ¶ 2 (“Plaintiff Wachovia is a national banking association with principal places of business at 301 South College Street, Charlotte, North Carolina and 375 Park Avenue, New York, New York.”).

ARGUMENT

I. THIS COURT SHOULD DISSOLVE THE PRELIMINARY INJUNCTION

As the North Carolina Supreme Court has explained, injunctions may be modified upon a clear showing of changed conditions meriting relief. *McGuinn v. City of High Point*, 219 N.C. 56, 62, 13 S.E.2d 48, 52 (1941) (concerning modification of permanent injunction).⁵ Here, the preliminary injunction is now causing the very harm it was intended to prevent and should be dissolved for that reason alone. Moreover, the preliminary injunction must be dissolved because it violates a fundamental principle articulated by the United States Supreme Court: “state courts are completely without power to restrain federal-court proceedings in *in personam* actions,” even if the restraint is only as to the assertion of state law claims. *Donovan*, 377 U.S. at 412-13.

A. The Preliminary Injunction Now Creates the Very Harm It Was Intended to Prevent

Ironically, Defendants’ deference to the preliminary injunction is causing the very harm – a multiplicity of actions – that Judge Ervin sought to prevent. All parties bound by the preliminary injunction are parties to the New York Action,⁶ as are numerous other interested parties. Solely as a consequence of this Court’s injunction, the Secondary Lenders have not at this time asserted their state law tort claims against Wachovia in the New York Action.

⁵ The standard for modifying a preliminary injunction is, unsurprisingly, more lenient; modification is generally left to the discretion of the court. *Conservation Council of N.C. v. Costanzo*, 528 F.2d 250, 251-52 (4th Cir. 1975) (holding that trial court’s decision to dissolve temporary injunction and deny preliminary injunction request did not constitute abuse of discretion); *Barr-Mullin, Inc. v. Browning*, 108 N.C. App. 590, 598, 424 S.E.2d 226, 231 (1993) (citing *Conservation Council* for proposition that it is in trial court’s discretion to dissolve, modify or deny requests relating to preliminary injunctions).

⁶ All of the Defendants labeled “Fund Defendants” by the Plaintiffs in this action are parties to the New York Action. The so-called “Agent Defendants,” which do not own any of the Le Nature’s bank debt, are not plaintiffs in the New York Action because they do not possess claims based on interests in the Credit Facility. As previously noted by Defendants, the “Agent Defendants” have no place in this action, given their lack of relevant interests and rights.

During oral argument concerning the preliminary injunction, Judge Ervin attempted to identify the problems that might ensue if Defendants (the only parties subject to the preliminary injunction) were free to file separate actions asserting assigned state-law tort claims:

[O]ne case might get filed in New York, one might get filed in the Caymans, one might get filed in Delaware, and you might also have the New York [court] rule no problem with the assignment, or a court would conclude the assignment is champertous, the court in the Grand Caymans rules God-knows-what under the law of the Grand Caymans, and so the parties are inflicted with multiple lawsuits of the same issue. And second, the likelihood of different outcomes, when in some courts the court rules that you can bring a claim and then it recovers. The other court rules that you cannot bring the claim, so you've got inconsistent results on essentially the same core set of facts.

March 29, 2007 Hearing Transcript (“Tr.”) at 48:15-49:5. Judge Ervin repeated those concerns in the text of his Order: “Should the Fund Defendants be allowed to assign such Personal Tort Claims against Plaintiffs while this action is pending, without restriction, a multiplicity of suits in a number of jurisdictions will likely result.” (Order at 6, ¶ 17.) He further noted that in the event of a multiplicity of suits, it would be “impractical for the Plaintiffs to obtain the determination they seek in a reasonable and orderly manner consistent with the ends of justice.” *Id.*

The basis for Judge Ervin’s concerns in issuing the Order no longer exists. The Initial and Secondary Lenders have not brought a “multiplicity” of actions rendering it “impractical” for Plaintiffs “to obtain the determination [of their defenses] in a reasonable and orderly manner.” Rather, they have joined as plaintiffs in a *single lawsuit* against Wachovia and other defendants to prosecute their claims efficiently and effectively. The New York Action is the single action Judge Ervin sought, and the preliminary injunction is, accordingly, unnecessary to achieve the Court’s stated goal of avoiding multiple suits.

The New York Action constitutes not only the single proceeding envisioned by Judge Ervin, but a proceeding that is more comprehensive than the pending North Carolina action, both in terms of the claims and parties included. And New York courts unquestionably have personal jurisdiction over the defendants named in that matter: BDO is a New York limited liability partnership with multiple offices there, Wachovia has extensive operations in New York, and the Le Nature's executives (Gregory Podlucky and Robert Lynn) traveled to New York on several occasions to market Le Nature's various offerings. Thus, the federal court in New York can resolve all disputes among all parties, a result entirely consistent with North Carolina's "history of promoting judicial economy." *Rhyne v. K-Mart Corp.*, 358 N.C. 160, 189, 594 S.E.2d 1, 20 (2004). To the extent it dissuades Defendants from asserting state law claims outside North Carolina, the preliminary injunction now frustrates judicial economy, and should be dissolved to permit all claims to be heard by a single court.

B. The Preliminary Injunction Improperly Attempts to Enjoin the Assertion of State Claims in Federal Court

The preliminary injunction herein is also at odds with well-established, unambiguous federal law. In *Donovan v. City of Dallas*, 377 U.S. 408 (1964), the United States Supreme Court held that state courts are prohibited from issuing injunctions that even indirectly restrain federal court proceedings in *in personam* actions. *Donovan* involved an injunction issued by a Texas state court that barred the defendants from bringing federal or state claims in any other court. Despite the order, the defendants sued in federal court on both federal and state grounds and were consequently found guilty of contempt by the Texas state court. The Supreme Court reversed because state courts cannot infringe upon the jurisdiction of federal courts, and thus cannot prevent parties from asserting claims in federal court:

While Congress has seen fit to authorize courts of the United States to restrain state-court proceedings in some special circumstances, it has in no way relaxed the old and well-

established judicially declared rule that state courts are completely without power to restrain federal-court proceedings in *in personam* actions And it does not matter that the prohibition here was addressed to the parties rather than to the federal court itself.

Id. at 412-13 (footnotes omitted); *see also Gross v. Weingarten*, 217 F.3d 208, 221 (4th Cir. 2000) (rejecting idea that state may oust federal courts of jurisdiction by creating exclusive forum for certain claims: “An attempt to restrain the exercise of federal jurisdiction is no more effective when made by a court in the form of an injunction.”).

To comply with *Donovan*, this Court should have excepted from the preliminary injunction not only federal claims, unassigned tort claims, and contract claims, but rather *all* claims brought in federal court, including state law claims subject to pendent or diversity jurisdiction. (Although the scope of the preliminary injunction exceeds the extent of the Court’s jurisdiction in this important respect, Defendants have not at this time asserted state law tort claims against Wachovia so as to comply with the terms of the Order as written.) Because the Order is not appropriately limited, it is facially invalid and must be dissolved.⁷

II. THIS ACTION SHOULD BE STAYED TO PREVENT A SUBSTANTIAL INJUSTICE

Because the New York Action presents an efficient proceeding in which to resolve claims relating to the Le Nature’s bank debt, Defendants further seek to stay this action pending adjudication of the claims in New York. N.C. Gen. Stat. § 1-75.12 provides:

⁷ The Order should be dissolved for the additional reason that it issued based on a misapprehension of the law. Judge Ervin understandably wanted to avoid a multiplicity of lawsuits. However, a prohibitory preliminary injunction may be granted *only* when irreparable injury “is real and immediate.” *DaimlerChrysler Corp. v. Kirkhart*, 148 N.C. App. 572, 586, 561 S.E.2d 276, 286 (2002). Here, there is no possibility of irreparable injury. It is well established that “the possibility that [a p]laintiff may have to defend itself in a lawsuit, or multiple lawsuits, is not a sufficiently substantial injury to support [a] preliminary injunction.” *Id.* at 586, 561 S.E.2d at 287.

(a) When Stay May be Granted

If, in any action pending in any court of this State, the judge shall find that it would work substantial injustice for the action to be tried in a court of this State, the judge on motion of any party may enter an order to stay further proceedings in the action in this State. A moving party under this subsection must stipulate his consent to suit in another jurisdiction found by the judge to provide a convenient, reasonable and fair place of trial.

The decision to grant or deny a stay ““is a matter within the sound discretion of the trial judge and will not be disturbed on appeal absent an abuse of that discretion.”” *Wachovia Bank, N.A. v. Deutsche Bank Trust Co. Americas*, 2006 NCBC 8, at ¶ 31 (N.C. Super. Ct. June 2, 2006) (unpublished) (quoting *Lawyers Mut. Liab. Ins. Co. of N.C. v. Nexsen Pruet Jacobs & Pollard*, 112 N.C. App. 353, 356, 435 S.E.2d 571, 573 (1993)) (Exhibit C hereto).

A. All Factors of North Carolina’s Ten-Factor Test Favor a Stay

In determining whether to grant a stay, “the trial court may consider the following factors: (1) the nature of the case, (2) the convenience of the witnesses, (3) the availability of compulsory process to produce witnesses, (4) the relative ease of access to sources of proof, (5) the applicable law, (6) the burden of litigating matters not of local concern, (7) the desirability of litigating matters of local concern in local courts, (8) convenience and access to another forum, (9) choice of forum by the plaintiff, and (10) all other practical considerations.” *Wachovia Bank*, 2006 NCBC 8, at ¶ 32 (citing *Lawyers Mut. Liab. Ins. Co.*, 112 N.C. App. at 356, 435 S.E.2d at 573). Here, *every one* of these factors favors a stay.

Nature of the Case. The first factor militates in favor of a stay because this action is a preemptive strike intended to secure a perceived advantage in litigation that Plaintiffs anticipated the Defendants might commence. The complaint itself concedes this action was filed *because* Plaintiffs feared Defendants would sue them. (Compl. ¶¶ 2-3.)

Preemptive declaratory relief actions are entitled to little deference. In *Coca-Cola Bottling Co. Consol. v. Durham Coca-Cola Bottling Co.*, 141 N.C. App. 569, 541 S.E.2d 157 (2000), a purported purchaser brought an action seeking declaratory judgment and specific performance by a vendor. The trial court denied the vendor's motion seeking to dismiss the declaratory judgment claim. The Court of Appeals reversed, holding that the declaratory judgment action should have been dismissed in favor of the later-filed action by the party asserting substantive claims. The Court of Appeals explained that:

[I]n situations in which two suits involving overlapping issues are pending in separate jurisdictions, priority should not necessarily be given to a declaratory suit simply because it was filed earlier. Rather, ***if the plaintiff in the declaratory suit was on notice at the time of filing that the defendant was planning to file suit, a court should look beyond the filing dates to determine whether the declaratory suit is merely a strategic maneuver to achieve a preferable forum.*** See [*Centennial Life Ins. Co. v. Poston*, 88 F.3d 255, 258 (4th Cir. 1996)] (“[A]lthough the federal action was filed first, we decline to place undue significance on the race to the courthouse door, particularly in this instance where [the plaintiff] had constructive notice of [the defendant’s] intent to sue.”); [*Mission Ins. Co. v. Puritan Fashions Corp.*, 706 F.2d 599, 602 (5th Cir. 1983)] (holding that plaintiff should not be permitted to gain precedence in time and forum by filing a declaratory action which is merely anticipatory of a parallel state action).

Coca Cola Bottling Co., 141 N.C. App. at 579, 541 S.E.2d at 164 (emphasis added).

There can be no dispute that, in filing this declaratory relief action, Plaintiffs were racing to the courthouse door. Their application for injunctive relief, for example, was supported by the Affidavit of Katherine A. Harkness dated March 14, 2007 (“Harkness Aff.”), in which Ms. Harkness declared:

I have listened to a number of hearings in the [Le Nature’s] bankruptcy proceedings. The Fund Defendants and Agent Defendants . . . participate through counsel in those proceedings as members of an “Ad Hoc Committee of Secured Creditors” (the “Ad Hoc Group”). During hearings in open court, counsel for the Ad Hoc Group has informed the Bankruptcy Judge that the

members of that Group intend to assert claims against “Wachovia”

. . . .

(Harkness Aff. ¶ 16.)

Ms. Harkness expressed further concern that members of the Ad Hoc Group were attempting to obtain copies of Wachovia documents and were “attempting to use the discovery processes available in Bankruptcy Court for the ‘prosecution of their individual causes of action against third parties.’” *Id.* ¶ 17. Further, Ms. Harkness averred that “Defendants’ plans to sue Wachovia . . . have been the subject of news coverage.” *Id.* ¶ 19. Based on the foregoing, Ms. Harkness declared that there was a justiciable controversy because “it is apparent that the Defendants intend to assert claims that they believe have been assigned to them directly (or indirectly through intermediate assignments) by prior members of the syndicate for the replacement Facility pursuant to the Supplements attached as Exhibit C.” *Id.* ¶ 20.

In other words, Wachovia anticipated it would be sued, so it sued first, seeking declaratory relief in a forum it believed would be favorable to it. Favoring such defensive proceedings would, in the words of the Court of Appeals, “encourage a race to the courthouse in situations in which a potential defendant anticipates litigation by the natural plaintiff in a controversy.” *Coca Cola Bottling Co.*, 141 N.C. App. at 581, 541 S.E.2d at 165. Accordingly, the nature of this case favors a stay.

Convenience of the Witnesses. It is certainly more convenient for a witness to testify in one proceeding than it is to testify in two proceedings at different times and in different places. Given the number and scope of parties and array of claims in the New York Action, that case will move forward and require testimony from all witnesses with relevant information. The only question is whether witnesses will also be required to testify in North Carolina, in a case that concerns only a subset of the issues now before the New York court. This factor thus clearly

favors a stay of this action. Indeed, further testimony in this Court will likely prove unnecessary once the New York Action is resolved.

Availability of Compulsory Process to Require the Appearance of Witnesses. The third factor weighs in favor of a stay because third-party witnesses beyond this Court's subpoena power are largely located in New York and surrounding areas. These witnesses include:

- Employees of Defendants in this action that may be dismissed based on the lack of *in personam* jurisdiction;
- Employees of the Initial Lender plaintiffs in the New York Action;
- Employees of BDO, a party in the New York Action but absent here, who were responsible for conducting the Le Nature's audits;
- Key Le Nature's executives, parties to the New York Action but absent here, who played a central role in the Company's fraud;
- Employees of Kroll Zolfo Cooper, Le Nature's court-appointed custodian, which has its principal place of business in New York;
- Counterparties to the assignments of Le Nature's bank debt, many of which are located in New York or within the 100-mile federal subpoena radius; and
- Witnesses knowledgeable about the LSTA standard terms and conditions, including the effect of debt assignments.

Even this simple list, which is not comprehensive, indicates the concentration of New York area witnesses who will be outside the subpoena power of a North Carolina court.

Relative Ease of Access to Sources of Proof. Like the relevant non-party witnesses, important documents possessed by non-parties are more likely obtainable in a federal action in New York than by the parties to a North Carolina state court action. Among others, documents concerning Le Nature's audits, key Le Nature's executives' misconduct, the transfer of Credit Facility interests, and the procedures and findings of the court-appointed custodian will all be readily accessible in New York, and far more difficult to obtain in North Carolina. Accordingly, the fourth factor favors a stay.

Applicable Law. This factor favors a stay because the central issue in this action is whether the LSTA Standard Terms are enforceable. Those terms provide that any rights to tort or other legal claims against third-parties related to the debt at issue are conveyed with the sale of the debt. Billions of dollars per year are traded pursuant to the LSTA Standard Terms. Those Standard Terms mandate that the parties submit to the exclusive jurisdiction and venue of courts in New York County for all actions arising out of or related to transfers effected under the LSTA Purchase Agreement and further provide that any such actions be decided *pursuant to New York law*.

Against this backdrop, Wachovia will likely point to language in the Credit Facility requiring application of North Carolina law to claims under that agreement. As Judge Ervin noted, however, the choice of law provision in the Credit Facility is not applicable here: “I don’t think the original contract that says North Carolina law is determinative” (Tr. at 55:10-11). Rather, the claims against Wachovia arise largely in tort, and thus are subject to choice of law principles applicable to tort claims. As Judge Ervin explained, “[Y]ou’ve got to figure out what the tort claim is. Once the tort claim is defined, then you can figure out what’s basically the last act for that tort claim. That’s going to tell you which state’s tort law applies, and it would seem to me the tort law of that state would tell you whether you can transfer [the] assignment or not.” (Tr. at 67:15-23.) Judge Ervin concluded, “It seems to me that . . . there is an issue as to a choice of law...” (Tr. at 85:24-25.) Accordingly, North Carolina law may well not govern Wachovia’s champerty defense.⁸

⁸ Notably, even if North Carolina law were applicable, there is no basis for applying the doctrine to the sale of distressed debt, which is accompanied by an assignment of *all* tort claims related thereto:

“Champerty” is a form of maintenance whereby a stranger makes a
“bargain with a plaintiff or defendant to divide the land or other

(footnote continued)

Burden of Litigating Matters Not of Local Concern. The sixth factor clearly weighs in favor of a stay because the issues herein, including the interpretation and application of LSTA requirements, are of national concern and, for the reasons noted above, can more easily be litigated in New York.

Desirability of Litigating Matters of Local Concern in Local Courts. The seventh factor also favors a stay because this action does not raise matters of local concern. To begin with, the transactions at issue concern the debt of a company located in Pennsylvania, which was traded in various locations (including, primarily, New York), pursuant to documents expressly governed by New York law.

Moreover, Wachovia's ability to deter claims against it can hardly be termed a local issue. Wachovia (a Delaware limited liability company) transacts business internationally, it syndicates loans to banks and investors everywhere, and it has billions of dollars in assets throughout the United States. Its bank affiliate, Wachovia Bank (a national association) lists New York as one of its principal places of business, is a member of the board of the New York-

matter sued for between them if they prevail at law, whereupon the champertor is to carry on the party's suit at his own expense."

DaimlerChrysler Corp. v. Kirkhart, 148 N.C. App. 572, 580, 561 S.E.2d 276, 283 (2002) (quoting *Wright v. Commercial Union Ins. Co.*, 63 N.C. App. 465, 469, 305 S.E.2d 190, 192 (1983)). Under the LSTA Purchase Agreement, the debt purchaser is vested with all claims arising from the debt and pursues those claims for its own account alone. Moreover, North Carolina has an interest in insuring that its champerty rules do not conflict with modern commercial realities. As the appellate court stated in *DaimlerChrysler*,

[O]ur Supreme Court in *Smith* noted that many exceptions to the principles of champerty and maintenance have been recognized, "so that they may be adapted to the new order of things in the present highly progressive and commercial age."

DaimlerChrysler Corp., 148 N.C. App. at 580, 561 S.E.2d at 283 (quoting *Smith v. Hartsell*, 150 N.C. 71, 77, 63 S.E. 172, 174 (1908)); cf. *Osprey, Inc. v. Cabana Ltd. P'ship*, 340 S.C. 367, 384, 532 S.E.2d 269, 279 (2000) (abolishing defense of champerty in South Carolina "because we believe it no longer is required to prevent the evils traditionally associated with the doctrine as it developed in medieval times").

based LSTA, and is represented on the subcommittees that drafted the LSTA forms used to convey the debt at issue.⁹ Wachovia is, quite simply, not a local business. North Carolina has no overpowering interest in determining the rights of a multi-billion dollar, multinational company with respect to transactions centered in the New York market.

Convenience and Access to Another Forum. The eighth factor favors a stay because Plaintiffs have substantial resources to expend on litigation and already transact substantial business in New York. Additionally, as demonstrated by the existence of the New York Action, New York is a viable – indeed, more efficient – forum for resolution of the parties’ disputes. Litigating a single action in New York that resolves all issues will be less burdensome than litigating separate actions in North Carolina and New York involving overlapping claims.

Choice of Forum by the Plaintiff. Plaintiffs’ strategic assertion of their claims in North Carolina is not entitled to great weight. To begin with, North Carolina discounts a plaintiff’s choice of forum when a defendant has made a sufficiently strong showing as to other relevant factors. *Wachovia Bank*, 2006 NCBC 8, at ¶ 53 (citing *Lawyers Mut. Liab. Ins. Co.*, 112 N.C. App. 353, 435 S.E.2d 571). Moreover, when the plaintiff brings a preemptive declaratory relief action to secure a perceived strategic advantage, the plaintiff’s choice of forum deserves little weight. *Coca-Cola Bottling Co. Consol. v. Durham Coca-Cola Bottling Co.*, 141 N.C. App. 569, 541 S.E.2d 157 (2000). Because that is exactly what plaintiffs have done, their filing here does not favor retention of the action.

All Other Practical Considerations. Finally, given that it is inherently easier to try one case in one state than two cases in two states, and given further that the trial of separate actions could lead to inconsistent results, the tenth factor also favors a stay of this action.

⁹ See *Ganz Aff.* ¶¶ 3, 9.

B. All Factors of North Carolina’s Alternative Test Also Favor a Stay

The trial court is not obligated to consider each factor of the ten-factor test, nor is it obligated to consider every factor that supports a stay. Instead, a court “acts within its discretion if it considers whether ‘(1) a substantial injustice would result if the trial court denied the stay, (2) the stay is warranted by those factors present, and (3) the alternative forum is convenient, reasonable, and fair.’” *Wachovia Bank*, 2006 NCBC 8, at ¶33 (quoting *Lawyers Mut. Liab. Ins. Co.*, 112 N.C. App. at 357, 435 S.E.2d at 574). Here, all three of these prongs would be satisfied if the Court were to issue the requested stay.

Substantial Injustice Would Result if the Trial Court Denies the Stay. The New York court is uniquely positioned to accord full relief to all parties. It will address claims by both Initial and Secondary Lenders against a broad spectrum of defendants. New York has jurisdiction over all parties, can compel the production of key documents and the appearance of important witnesses, and is capable of adjudicating all claims, whichever state’s law may apply. Allowing the New York court to resolve all the parties’ disputes will avoid the very problem that Plaintiffs identified in seeking a preliminary injunction in the first instance – a multiplicity of actions – and will promote both judicial economy and prevent inconsistent results. Moreover, given the number of parties and claims in the New York Action, that case will proceed whether or not this case is stayed. The only way to avoid overlapping litigations, accordingly, is to stay this case pending the outcome of that proceeding.

New York also has a substantial interest in the outcome of the litigation. All plaintiffs and defendants in the New York Action (except Le Nature’s’ executives) are either headquartered in New York or routinely conduct business there. Additionally, Wachovia is seeking a declaration that the assignment of tort claims in connection with the sale of distressed debt to the Secondary Lenders was champertous. Those sales – many of which were completed

in New York – were all made pursuant to the LSTA Standard Terms, which require that New York courts, applying New York law, resolve any disputes concerning such transfers.

All told, the New York Action – unlike this action – can address all claims and, if warranted, provide complete relief against several significant defendants. As an LSTA board member, Wachovia can hardly be surprised or claim prejudice because purchasers of Le Nature’s debt brought claims in New York. By preventing efficient litigation of the action in New York, and by creating the very multiplicity of actions that this Court sought to avoid, denial of the requested stay would result in “a substantial injustice.” *Wachovia Bank*, 2006 NCBC 8, at ¶33.

The Stay Is Warranted by Those Factors Present. As shown above, all factors of the ten-factor analysis point to New York as both an appropriate forum for trial of the claims herein and as the only forum where complete relief could be accorded to all parties. Thus, a stay is warranted by the ten-factor test.

The Alternative Forum Is Convenient, Reasonable and Fair. Although the North Carolina Business Court clearly has the expertise for complex business disputes of the sort presented by this preemptive action and the New York Action, so, too, do the New York courts, including the federal district court in Manhattan. Courts in New York routinely address complex banking and financial disputes in a reasonable and fair manner. Also, given Wachovia’s substantial New York City presence, there is no question as to the convenience of the forum. Accordingly, the final factor of the alternative test also favors a stay.

For these reasons, this action, which involves a limited set of parties and a few, primarily defensive claims, should be stayed to allow the parties to resolve their disputes in a court that can resolve all issues among all parties.

CONCLUSION

For the reasons set forth above, this Court should dissolve the preliminary injunction and stay this action pending the outcome of the New York Action.

Respectfully submitted this the 17th day of September, 2007.

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RULE 15.8 CERTIFICATION

I certify that this brief complies with BCR 15.8.

This the 17th day of September, 2007.

/s/ James B. Gatehouse