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CONCURRENT SESSION

Caesars: Lessons Learned

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2017

_In re_ Caesars Entertainment Operating Co., Inc.
Panel Discussion Outline[1]
Subject: Parent Guarantee Litigation and Section 105 Litigation

Background

The Caesars debtors are the primary operating units of a larger group of companies described as "the Caesars Gaming Enterprise ("Caesars")." Caesars Entertainment Operating Company, Inc. ("CEOC") is the debtor in the lead case; the other debtors are all subsidiaries of CEOC. Caesars Entertainment Corp. ("CEC") is majority owner of CEOC. Caesars owns, operates or manages 50 casinos in five countries including the United States. It has 68,000 employees, million square feet of gaming space, and 39,000 hotel rooms. Debtors own, manage, or operate 38 of the casinos.

The Indentures and the LBO

In September 2005, CEOC and CEC entered into an indenture with U.S. Bank N.A. as indenture trustee (the "2005 Indenture"). Pursuant to the 2005 Indenture, CEOC issued $750 million in notes due in 2017 with an interest rate of 5.75% (the "2017 notes"). In June 2006, CEOC entered into a second indenture with U.S. Bank as indenture trustee (the "2006 Indenture") pursuant to which CEOC issued another $750 million in notes due in 2016 (the "2016 notes") with 6.5% interest. The 2016 and 2017 notes (jointly the "Senior Unsecured Notes") were unsecured, but CEC guaranteed CEOC's obligations under the Indentures and notes.

[1] This outline draws heavily on the opinion attached hereto at Appendix A, Caesars Entertainment Operating Co., Inc., et al. v. BOKF, N.A., et al. (_In re_ Caesars Entertainment Operating Co., Inc.), No. 15C6504, Adv. No. 15-100149 (N.D. Ill. Oct. 6, 2015), and the Disclosure Statement of Caesars Entertainment Operating Company, Inc., Docket No. 4220, filed on June 28, 2016, _In re_ Caesars Entertainment Operating Co., Inc.), No. 15-01148 (Bankr. N.D. Ill.).

In 2008, affiliates of Apollo Global Management, LLC ("Apollo") and TPG Capital LP ("TPG") and other investors acquired CEC (and all of its subsidiaries) in a $30.7 billion leverage buyout. The investors paid $6.1 billion in cash with the remainder funded through the issuance of approximately $24 billion in debt. Of the $24 billion, $19.7 billion was secured by liens on substantially all of Debtors' assets. In 2009, CEOC and CEC entered into a third indenture with U.S. Bank as indenture trustee (the "2009 Indenture") under which CEOC issued $3.71 billion in notes due in 2018 with interest at 10%. The notes were secured by second priority liens on, among other things, substantially all of CEOC's assets. In 2010 CEOC and CEC entered into a fourth indenture with U.S. Bank as trustee under which CEOC issued $750 million due in 2018 with interest at 12.75%. CEOC's obligations under the notes were secured in part by second priority liens on substantially all of its assets. CEC guaranteed CEOC's obligations under the 2009 and 2010 Indenture and under the 2018 Notes (jointly the "Second Lien Notes").

The Disputed Transactions

Around 2009, as a result of the 2008 financial crisis, Caesars sought to "restructure and manage" CEOC's debt. Caesars engaged in a series of over 45 "capital market transactions, including "assets sales, exchange and tender offers, debt repurchases and refinances." (The "Disputed Transactions"). Two of the Disputed Transactions are particularly relevant to the guarantees under the indentures.

The first such transaction, referred to as the B-7 Refinancing, occurred in May 2014 when CEC and CEOC had CEOC amend its first lien credit agreement and obtain an additional $1.75 billion in new term loans. As part of that transaction, CEC sold 68.1 shares, or 5%, of CEOC common stock for $6.15 million to institutional investors not affiliated with CEC. Based on this sale, CEC took the position that because CEOC was no longer a wholly-owned

subsidiary, CEC's guarantees of CEOC's obligations under the First and Second Lien Notes were terminated under the terms of the various indentures.

The second Disputed Transaction, referred to as the "Senior Unsecured Notes Transaction," occurred on August 12, 2014, when CEC and CEOC consummated a deal with certain holders of more than 51% of CEOC's outstanding Senior Unsecured Notes. CEC and CEOC repurchased $155.4 million of the Notes, with each paying $77.7 million plus accrued and unpaid interest. The selling noteholders agreed to support any future restructuring that had consent of at least 10% of outstanding noteholders. They also entered into a supplemental indenture that, among other things, removed CEC's guarantee of the Senior Unsecured Notes.

The Guarantee Litigation

CEC's attempts to extinguish its guarantees of CEOC's obligations under both the Second Lien Notes and the Senior Unsecured Notes led to lawsuits in the Delaware Court of Chancery and the U.S. District Court for the Southern District of New York. In each of those actions, the noteholders (or their indenture trustee) sought, among other things: (1) a declaration that CEC's efforts to effect a release of its guarantee is void; and (2) to enforce the respective guarantee.

First, on August 4, 2014, a second lien indenture trustee sued CEC, CEOC and others in the Delaware Court of Chancery, claiming, among other things, that the B-7 Refinancing breached the 2009 Indenture, and seeking a declaration that CEC's guarantee of the notes subject to the Indenture had not been released. Next, on September 3, 2014, MeehanCombs and certain other holders of the Senior Unsecured Notes sued CEC and CEOC in the Southern District of New York raising eight claims based on the Senior Unsecured Notes Transaction. The suit sought a declaration that CEC's guarantees of the 2005 and 2006 Indentures are still in effect,

damages under the Trust Indenture Act, 15 U.S.C. §§ 77aaa-bbb, and damages for breach of the Indentures and guarantees. Finally, in March 2015, another second lien indenture trustee sued CEC in the Southern District of New York claiming that CEC breached the guarantee and 2010 Indenture, and that the release of the guarantee in the B-7 Refinancing is void. These lawsuits are collectively the "Parent Guarantee Litigation."

The Special Governance Committee

In June 2014, just before the first suit was filed, CEOC appointed two independent directors as a Special Governance Committee ("SGC") tasked with investigating the Disputed Transactions to determine whether Debtors or their creditors or both have claims against CEC. The SGC investigation has taken thousands of hours. The SGC has apparently found that CEOC has substantial claims against CEC arising out of the Disputed Transactions, including claims for avoidable preferences and fraudulent transfers.

The Section 105 Litigation

On March 11, 2015, the Debtors commenced an adversary proceeding in the Bankruptcy Court to enjoin the continuation of the "Parent Guarantee Litigation" against CEC pursuant to section 105(a) of the Bankruptcy Code (the "105 Adversary Proceeding"). The Debtors contended that continuation of the Parent Guarantee Litigation outside of the chapter 11 cases would imperil their ability to reorganize. Specifically, the Debtors believed that their reorganization required a substantial contribution from CEC, whether through settlement or litigation, to fund recoveries for the Debtors' creditors. Any consideration that CEC would pay on account of its purported guarantees of the Debtors' funded debt obligations would reduce CEC's ability to make a contribution to the Debtors under the Plan (or through litigation to the extent that the settlement encompassed in the Plan fails). The Debtors also contended that an

adverse ruling in any of the actions in the Parent Guarantee Litigation may very well cause CEC to seek protection under the Bankruptcy Code, which would allegedly upset the Debtors' reorganization process given the Debtors' own claims against CEC.

Following an evidentiary trial and briefing by the parties, the Bankruptcy Court issued an opinion [Adv. Case. No. 15-00149 (ABG), Docket Nos. 158] (the "Original 105 Opinion") and order [Adversary Case No.-15-00149 (ABG), Docket No. 159] on July 22, 2015, denying the Debtors' request in the 105 Adversary Proceeding. The Bankruptcy Court held that controlling precedent required that "[u]nless the debtor's estate has a claim against the non-debtor, and unless that claim is based on the same acts and would be paid from the same assets as the third party's claim against the non-debtor, no relief is possible" from a bankruptcy court to enjoin that non-debtor third party litigation pursuant to section 105. See Original 105 Opinion at 28.

On July 24, 2015, the Debtors appealed this ruling (the "105 Appeal"). In the 105 Appeal, the Debtors argued that the Bankruptcy Court's "same acts" requirement is a misapplication of precedent from United States Court of Appeals for the Seventh Circuit (the "Seventh Circuit"), and requested that the District Court enter the requested section 105 injunction to protect the Debtors' interests in CEC's contributions to the Debtors pursuant to the Plan, or remand to the Bankruptcy Court to enter such an order or further consider the requested injunction. The District Court held oral argument in the 105 Appeal on September 29, 2015. On October 8, 2015, the District Court entered an order, and memorandum opinion and order, affirming the Bankruptcy Court's ruling. The Debtors appealed.

On December 23, 2015, the Seventh Circuit vacated the denial of the injunction and remanded to the Bankruptcy Court on the grounds that the "same acts" requirement was a misapplication of controlling Seventh Circuit case law.

On remand, the Bankruptcy Court took judicial notice of certain additional facts from the chapter 11 and the Parent Guarantee Litigation, including a pending trial date in the BOKF SDNY Action set for March 14, 2016, and a pending trial date in the Unsecured Notes SDNY Actions set for May 9, 2016. Based on the factual findings from the trial in the 105 Adversary Proceeding and judicial notice of these additional facts, on February 26, 2016, the Bankruptcy Court issued a ruling (the "105 Order"), which enjoined the BOKF SDNY Action until the earlier of (a) 60 days after the Examiner files his final (redacted) report and May 9, 2016. On May 9, 2016, the injunction expired.

Each of the SDNY Actions was subject to a summary judgment schedule culminating on June 24, 2016, with oral argument, and a "global" trial starting on August 22, 2016, if necessary. Similarly, the Delaware action was subject to a summary judgment schedule culminating in oral argument on June 16, 2016. On June 6, 2016, the Debtors filed an emergency motion (the "Renewed 105 Motion") seeking a temporary restraining order and preliminary injunction enjoining the plaintiffs in the Parent Guarantee Litigation from further prosecuting their guaranty lawsuits because the Debtors asserted such an injunction was necessary to protect the Debtors' ability to reorganize in the Chapter 11 Cases. An evidentiary hearing on the Renewed 105 Motion was held on June 8, 9, and 13, 2016. On June 15, 2016, the Bankruptcy Court granted the Renewed 105 Motion, enjoining the plaintiffs in the Parent Guarantee Litigation from further prosecuting their guaranty lawsuits until August 29, 2016.

After a further trial in late August, the Bankruptcy Court declined to further extend the injunction of the Parent Guarantee Litigation. The Southern District of New York was scheduled to go forward with oral argument in the SDNY Actions for August 30, 2016. However, the District Court in Chicago chose to extend the injunction while it heard the Debtors' emergency

appeal. On September 27, 2016, the Debtors and CEC announced they had reached an agreement in principle with essentially all of the Debtors' creditor groups. The Senior Unsecured Noteholders reached a settlement with the Debtors and CEC by mid-October.

Appendix A

[Caesars Entertainment Operating Co., Inc., et al. v. BOKF, N.A., et al. (*In re* Caesars Entertainment Operating Co., Inc.), No. 15C6504, Adv. No. 15-100149 (N.D. Ill. Oct. 6, 2015).]

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

IN RE: CAESARS ENTERTAINMENT OPERATING COMPANY, INC., ET AL., Debtors.	
CAESARS ENTERTAINMENT OPERATING COMPANY, INC. et al., Plaintiffs-Appellants, v. BOKF, N.A., WILMINGTON SAVINGS FUND SOCIETY, FSB, MEEHANCOMBS GLOBAL CREDIT OPPORTUNITIES MASTER FUND, LP, RELATIVE VALUE-LONG/SHORT DEBT PORTFOLIO, a Series of Underlying Funds Trust, SB 4 CF LLC, CFIP ULTRA MASTER FUND, LTD., TRILOGY PORTFOLIO COMPANY, LLC, and FREDRICK BARTON DANNER, Defendants-Appellees.	No. 15 C 6504 Judge Robert W. Gettleman Chapter 11 Case No. 15-01145 Adversary Proceeding No. 15-100149

MEMORANDUM OPINION AND ORDER

Caesars Entertainment Operating Company, Inc. ("CEOC") and approximately 170 of its subsidiaries ("Debtors") appeal from the decision of the bankruptcy court in Adversary Action 15 A 149, In re Caesars Entertainment Operating Co, Inc., 533 B.R. 714 (B.K. N.D. Ill. 2015). In that decision, the court denied Debtors' request for a preliminary injunction under § 105(a) of the Bankruptcy Code, 11 U.S.C. § 105(a), by which Debtors sought to enjoin defendants BOKF, N.A., Wilmington Savings Fund Society, FSB ("Wilmington"), MeehanCombs Global Credit Opportunities Master Fund, LP, Relative Value-Long/Short Debt Portfolio, a Series of Underlying Funds Trust, SB 4 CF LLC, CFIP Ultra Masters Fund, Ltd., Trilogy Portfolio

Company, LLC, ("MeehanCombs"), and Fredrick Barton Danner ("Danner"), from pursuing civil actions against CEOC's non-debtor parent, Caesars Entertainment Corp. ("CEC") pending in the Delaware Court of Chancery and the Souther District of New York. For the reasons described below, the decision of the bankruptcy court is affirmed.

BACKGROUND[1]

Debtors are the primary operating units of a larger groups of companies described as "the Caesars Gaming Enterprise ("Caesars")." CEOC is the debtor in the lead case[2], the other debtors are all subsidiaries of CEOC. CEC is majority owner of CEOC. Caesars owns, operates or manages 50 casinos in five countries including the United States. It has 68,000 employees, 3 million square feet of gaming space, and 39,000 hotel rooms. Debtors own, manage, or operate 38 of the casinos. In its most recent fiscal year Caesars had revenues in excess of $8 billions, of which Debtors contributed over $5 billion.

In September 2005, CEOC and CEC entered into an indenture with U.S. Bank N.A. as indenture trustee (the "2005 Indenture"). Pursuant to the 2005 Indenture, CEOC issued $750 million in notes due in 2017 with an interest rate of 5.75% (the "2017 notes"). In June 2006, CEOC entered into a second indenture with US Bank as indenture trustee (the "2006 Indenture") pursuant to which CEOC issued another $750 million in notes due in 2016 (the "2016 notes") with 6.5% interest. The 2016 and 2017 notes (jointly the "Senior Unsecured Notes") were unsecured, but CEC guaranteed CEOC's obligations under the Indentures and notes. Defendant

[1]The background facts are taken from sections of the bankruptcy court's findings of facts and conclusions of law to which neither party has objected.

[2]The underlying bankruptcy proceeding, 15 B 1145, is a set of jointly administered Chapter 11 actions.

MeehanCombs holds $15,318,000 of the 2016 notes and $5,623,000 of the 2017 notes. Defendant Danner holds $104,000,000 of the 2016 notes.

In 2008, affiliates of Apollo Global Management, LLC ("Apollo") and TPG Capital LP ("TPG") and other investors acquired CEC (and all of its subsidiaries) in a $30.7 billion leverage buyout. The investors paid $6.1 billion in cash with the remainder funded through the issuance of approximately $24 billion in debt. Of the $24 billion, $19.7 billion was secured by liens on substantially all of Debtors' assets.

In 2009, CEOC and CEC entered into a third indenture with U.S. Bank as indenture trustee (the "2009 Indenture") under which CEOC issued $3.71 billion in notes due in 2018 with interest at 10%. The notes were secured by second priority liens on, among other things, substantially all of CEOC's assets. In 2010 CEOC and CEC entered into a fourth indenture with U.S. Bank as trustee under which CEOC issued $750 million due in 2018 with interest at 12.75%. CEOC's obligations under the notes were secured in part by second priority liens on substantially all of its assets. CEC guaranteed CEOC's obligations under the 2009 and 2010 Indenture and under the 2018 Notes (jointly the "Second Lien Notes"). Defendant Wilmington succeeded U.S. Bank as Indenture Trustee under the 2009 Indenture. Defendant BOKF succeeded U.S. Bank under the 2010 Indenture.

Around 2009, as a result of the 2008 financial crisis, Caesars sought to "restructure and manage" CEOC's debt. Caesars engaged in a series of over 45 "capital market transactions, including "assets sales, exchange and tender offers, debt repurchases and refinances." (The "Disputed Transactions"). Debtors describe these transactions as designed to "extend debt

maturities, meet interest obligations, monetize assets and transfer debt in capital expenditure obligations at properties CEOC could not afford to invest in."

Prior to the Disputed Transactions, CEC was a holding company with its sole asset consisting of 100% of CEOC. At the time it guaranteed both the Senior Unsecured Notes and the

Second Lien Notes it possessed nothing but the equity in CEOC. It is only as a result of the Disputed Transactions that CEC obtained assets beyond its ownership interest in CEOC.

CEOC's creditors understandably take a dim view of the Disputed Transactions, considering them to be part of a "carefully orchestrated plan to strip CEOC of valuable assets," moving them beyond the creditors' reach. According to the creditors, the plan created a "Good Caesars" consisting of CEC and its affiliates holding prime assets that once belonged to CEOC, and "Bad Caesars," consisting of CEOC left with barely profitable or unprofitable properties and burdened with debt left from the 2008 leveraged buyout.

Two of the Disputed Transactions are particularly relevant to the instant dispute, because they led to the lawsuits that Debtors seek to enjoin. The first such transaction, referred to by the parties as the B-7 Refinancing, occurred in May 2014 when CEC and CEOC had CEOC amended its first lien credit agreement and obtain an additional $1.75 billion in new term loans. As part of that transaction, CEC sold 68.1 shares, or 5%, of CEOC common stock for $6.15 million to institutional investors not affiliated with CEC. Based on this sale, CEC took the position that because CEOC was no longer a wholly-owned subsidiary, CEC's guarantees of CEOC's obligations under the First and Second Lien Notes were terminated.

The second Disputed Transaction, referred to as the "Senior Unsecured Notes Transaction," occurred on August 12, 2014, when CEC and CEOC consummated a deal with certain holders of more than 51% of CEOC's outstanding Senior Unsecured Notes. CEC and CEOC repurchased $155.4 million of the Notes, with each paying $77.7 million plus accrued and unpaid interest. The selling noteholders agreed to support any future restructuring that had consent of at least 10% of outstanding noteholders. They also entered into a supplemental indenture that, among other things, removed CEC's guarantee of the Senior Unsecured Notes.

CEC's attempts to extinguish its guarantees of CEOC's obligations under both the Second Lien Notes and the Senior Unsecured Notes led to the four actions Debtors seek to enjoin. In each of those four actions, the plaintiff (defendants in the instant case) sought, among other things: (1) a declaration that CEC's efforts to effect a release of its guarantee is void; and (2) to enforce the respective guarantee. First, on August 4, 2014, Wilmington sued CEC, CEOC and others in the Delaware Court of Chancery, claiming, among other things, that the B-7 Refinancing breached the 2009 Indenture, and seeking a declaration that CEC's guarantee of the notes subject to the Indenture had not been released. Next, on September 3, 2014, MeehanCombs sued CEC and CEOC in the Southern District of New York raising eight claims based on the Senior Unsecured Notes Transaction. The suit seeks a declaration that CEC's guarantees of the 2005 and 2006 Indentures are still in effect, damages under the Trust Indenture Act, 15 U.S.C. §§ 77aaa-bbb, and damages for breach of the Indentures and guarantees.

One month later, on October 2, 2014, Danner filed a five count class action complaint against CEC and CEOC in the Southern District of New York. All counts contest the Senior Unsecured Notes Transaction. Danner seeks a declaration that the original 2006 Indenture

remains in effect and that the supplemental indenture and its release of the guarantee is void, and damages for breach of the 2006 Indenture. Finally, in March 2015, BOKF sued CEC in the Southern District of New York claiming that CEC breached the guarantee and 2010 Indenture, and that the release of the guarantee in the B-7 Refinancing is void.

In June 2014, just before Wilmington filed the first suit, CEOC appointed two independent directors as a Special Governance Committee ("SGC") tasked with investigating the Disputed Transactions to determine whether Debtors or their creditors or both have claims against CEC. The SGC investigation has taken thousands of hours. Although still ongoing, the SGC has apparently found that CEOC has substantial claims against CEC arising out of the Disputed Transactions, including claims for avoidable preferences and fraudulent transfers. It has not identified any specific claims or the transactions out of which they arise.

At the same time the SGC began its investigation, Debtors began negotiating with CEOC's first lien creditors and CEC over terms of a possible restructuring. On December 19, 2014, Debtors, CEC and some of the CEOC first lien note holders entered into a "Restructuring Support and Foreclosure Agreement" ("RSA"). In the RSA, CEC agreed to make a financial contribution to Debtors' restructuring. In exchange, CEOC agreed that the plan of reorganization would provide for a release of all claims the estates had against CEC, its affiliates, shareholders, officers, directors and others. The RSA would release CEC from more than $12 billion in note holder guarantee claims.

On January 12, 2015, three second lien noteholders filed an involuntary petition against CEOC in the District of Delaware. Three days later, January 15, 2015, Debtors filed voluntary Chapter 11 petitions in this district. The Delaware court transferred the involuntary case to this

district. On March 11, 2015, one week after BOKF filed the last of the four actions against CEC, Debtors filed the instant adversary action seeking, among other things, an injunction against defendants from prosecuting their guarantee claims against the "non-debtor affiliates." After an evidentiary hearing, the bankruptcy court denied Debtors' request for an injunction, concluding that "debtors have not demonstrated that the claims the estates have against CEC arise out of the same acts as the guaranty claims the defendants are pursuing against CEC in Delaware and New York." Caesars, 533 B.R. at 727.

DISCUSSION

This court has jurisdiction to hear appeals from final orders of the bankruptcy court. 28 U.S.C. § 158(a)(1). The court reviews the denial of an injunction for an abuse of discretion. See In re Rimsat, Ltd., 212 F.3d 1039, 1049 (7th Cir. 2000); In re Brittwood Creek, LLC, 450 B.R. 769, 744 (N.D. Ill. 2011). A trial court abuses its discretion when "it commits an error of law or makes a clearly erroneous finding of fact." Kress v. CCA of Tenn., LLC, 694 F.3d 890, 892 (7th Cir. 2012). Under this standard, this court should reverse "only where no reasonable person could take the view adopted by the [bankruptcy] court." Bedrossian v. Northwestern Memorial Hospital, 409 F.3d 840, 845 (7th Cir. 2005).

Debtors seek an injunction under § 105(a) of the Bankruptcy Code, which provides that "[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions this Title." 11 U.S.C. § 105(a). The statute permits a bankruptcy court to protect its jurisdiction by enjoining the prosecution of a third party's action against a non-debtor pending in another court. In re Teknek, LLC, 563 F.3d 639, 648 (7th Cir. 2009); Fisher v. Apostolou, 155 F.3d 876, 882 (7th Cir. 1998). This power to enjoin third party proceedings is

not limited to actions in which the third party seeks to prosecute claims that belong to the estate. "The jurisdiction of the bankruptcy court to stay actions in other courts extends beyond claims by and against the debtor, to include suits to which the debtor need not be a party but which may affect the amount of property in the bankrupt estate, or the allocation of property among creditors." Teknek, 563 F.3d at 648 (internal quotations omitted). The bankruptcy court's authority to enjoin actions under § 105(a) is not absolute, however, and when, as in the instant case, the third parties are asserting individual personal claims (as opposed to general claims that belong to the corporate debtor,) the court may enjoin prosecution only of claims that are sufficiently "related to" claims brought on behalf of the estate in the bankruptcy case. Id. (citing Fisher, 155 F.3d at 882).

In the instant case, the bankruptcy court determined that defendants' guarantee claims against CEOC are not sufficiently related to CEOC's potential (and as yet unidentified) claims against CEC to authorize an injunction. The court analyzed the Seventh Circuit's decisions in Fisher and Teknek, and concluded that individually and together they stand for the proposition that to be enjoined, the third parties' claims must arise out of the same acts as the estates' claims. Concluding that the third parties' breach of guarantee claims against CEC do not arise out of the same acts as CEOC's potential claims against CEC, it denied the requested injunction.

Debtors' argue that the Seventh Circuit precedent does not require the claims to arise from the "same acts," and that bankruptcy courts have the authority to enjoin any third party action that threatens the bankrupt estate. Next, they argue that even if the "same acts" requirement is the law in the Seventh Circuit, defendants' guarantee claims and CEOC's claims

against CEC all "arise from the same capital market transactions involving debtors and their debt."

It is not difficult to understand why the bankruptcy court held as it did. Although different factually, the Seventh Circuit's decisions in Fisher and Teknek focused on whether the third party claims against the non-debtor depended on the non-debtor's misconduct with respect to the corporate debtor. Teknek, 563 F.3d at 649. In Fisher, a Chapter 7 case, the corporate debtor was a commodities business that the individual debtor and his accomplices used as a "bucket shop" similar to a Ponzi scheme. After the fraud was discovered both the individual and the corporation were forced into bankruptcy. The corporate trustee brought claims against the non-debtor accomplices to recover on behalf of the estate, and a group of corporate investors sought to bring separate (outside the bankruptcy) securities, commodities and common law fraud claims against those same accomplices. The trustee filed an adversary action seeking to enjoin prosecution of the investors' claims because the estate had its own fraud claims against the investors. The bankruptcy court granted the injunction, but the district court reversed, concluding that the investors' claims were not the property of the estate. Fisher, 155 F.3d at 878-79.

The Seventh Circuit agreed with the district court that the investors' individual fraud claims (as opposed to claims that arose out of the investors' transactions with the corporation) were not property of the estate, id. at 881, but nonetheless upheld the bankruptcy court's injunction because the fraud claims were sufficiently related to the estate's claims. Id. at 882. In reaching this decision the court stated that "it is difficult to imagine how those claims could be more closely 'related to' it. They are claims to the same limited pool of money, in possession of

the same defendants, as a result of the same acts, performed by the same individuals, as part of the same conspiracy." Id. Thus, the court could "think of no hypothetical change to this case which would bring it closer to a 'property of' without converting it into one." Id.

In Teknek, another Chapter 7 case, Systems Divisions, Inc., ("SDI") obtained a judgment for patent infringement against Teknek, LLC ("Teknek") and a related corporation, Teknek Electronics ("Electronics"). While the infringement action was pending, Teknek's and Electronic's shareholders looted those two corporations, transferring their assets to Teknek Holdings ("Holdings"). The infringement court then added Holdings and the shareholders as alter egos and entered judgment against them directly. Teknek, 563 F.3d at 642.

Teknek filed for bankruptcy, but Electronics did not. The trustee brought an adversary action against the shareholders, seeking to hold them liable to the estate for the SDI judgment. At the same time, SDI was seeking to enforce its judgment against the same shareholders and Holdings. The bankruptcy court preliminarily enjoined SDI from collecting its judgment outside of the bankruptcy, concluding that SDI's claims against the alter egos were "property of the estate," giving the trustee exclusive right to bring the claims. The district court disagreed, finding that SDI's claims against the alter egos were neither property of the estate nor sufficiently related to the bankruptcy proceeding to warrant an injunction under § 105(a). The court vacated the preliminary injunction. Teknek, 563 F.3d at 641-2.

The Seventh Circuit affirmed the district court. After first concluding that SDI's claims against the alter egos were not property of the estate, the court turned to whether SDI's claims were sufficiently "related to" the estate's claims to warrant an injunction. In holding that they were not, the court distinguished both Fisher and Koch Ref. v. Farmers Union Cent. Exch., Inc.,

831 F.2d 1339 (7th Cir. 1987), a case which discusses the differences between general claims of the estate, and individual or personal claims of creditors:

> In both of these cases, the creditors' claims against the non-debtor fiduciaries depended on the non-debtors' misconduct with respect to the corporate debtor . . .. In this regard general claims and claims that are 'related to' the bankruptcy seemingly always involve transfers from the debtor to a non-debtor control person or entity.

Teknek, 563 F.3d at 649 (emphasis in original).

After acknowledging that the case involved such facts, the court then noted that Electronics was a separate non-debtor that was directly liable to SDI without regard to the debtors' liability. "SDI's claim against the alter egos does not depend on the alter egos' misconduct with respect to the debtor [Teknek]. SDI has equal recourse against the alter egos because of the injuries suffered by Electronics." Id. Thus, even though SDI's claims against the alter egos had the potential to affect the amount of property in the bankruptcy estate and the allocation of property among creditors, the court refused to enjoin them, stating, id.:

> Here, though SDI's claims involve the same pool of money as the trustee's claims, and that money is in the possession of the same defendants (the alter egos), the claims are not based on the same acts. The alter ego's looted both Teknek and Electronics. Those are separate acts, which cause separate injuries to two separate companies, only one of which is in bankruptcy.

In the instant case, defendants' claims against CEC do not in any way depend on CEC's misconduct with respect to CEOC. Defendants' claims arise out of CEC's failure to honor guarantee agreements entered by CEC well before any of the alleged Disputed Transactions. To be sure, the issue of whether the B 7 Refinancing and the Senior Unsecured Notes Transaction effectively released CEC's guarantee obligations will be litigated in the Delaware and Southern District of New York actions, and may also be litigated in the bankruptcy court. But it is the

defendants' claims that must relate to the debtors' potential claims, not just the issues or defenses involved in the litigation of those claims. See In re Pierport Dev. & Realty, Inc., 502 B.R. 819, 826 (B.K. N.D. Ill. 2013) (It is the conduct that cause the alleged injury, not the particular cause of action or legal theory that determines whether the bankruptcy trustee has standing.").

Here, defendants were allegedly injured by CEC's failure to honor its guarantees. The validity of the two transactions will be raised in the Delaware and New York actions, but the conduct causing defendants' injury is CEC's alleged breach of its contracts. And, in any event, Debtors have admitted at trial that they have no claim against CEC based on either the B 7 Refinancing or the Senior Unsecured Notes Transaction. Their argument that defendants' claims against CEC "arise from the same capital market transactions involving debtors and their debt," is simply wrong.

Thus, under any reading of Fisher and Teknek, it is obvious that whether a third-party's claims against a non-debtor arise out of the same acts as the estate's claims is a key component of the determination of whether a § 105(a) injunction is permitted. Whether it is a requirement for injunctive relief, as the bankruptcy court held, or whether it is simply a key factor that may tip the scale when no other factors mandate an injunction, is an issue that need not be resolved here. In the instant case, as in Teknek, defendants' claims involve the same pool of money as Debtors' claims, and that money is in the possession of the same defendant. The claims are not, however, based on the same acts. No other factors compel, or even support the issuance of an injunction.

Despite the obvious import of Teknek, Debtors continue to argue that § 105 is the "bankruptcy code's equivalent of the All Writs Act," providing the bankruptcy court with broad

authority to grant injunctive relief to protect the "integrity of the bankruptcy estate." The flaw in their position crystalized at oral argument when Debtors' counsel indicated that the size of the estate's claim is determinative. "And so if you're talking about something that would be a very small claim of the estate, I'm not sure that the bankruptcy court would necessarily have authority in those circumstances. But certainly it's got to be the case that a bankruptcy court would have the authority when the claim is the only asset of the estate." But, as defendants' counsel pointed out, if that were the test, the Seventh Circuit would have affirmed the injunction in Teknek, in which the estate's claims against the alter egos were it largest, if not only asset. Debtors' response was only to argue that Teknek did not address the propriety of temporarily enjoining lawsuits against a debtor's guarantors by a bankruptcy court, but instead addressed only situations where non-debtors and debtors disagreed over which entity owns a claim.

Debtors' reading of Teknek is incorrect. The Teknek bankruptcy court did hold that SDI's claims against the alter egos were property of the estate and therefore enjoined SDI from collecting its judgment outside the bankruptcy, but, as the Seventh Circuit made clear, the district court disagreed and held that SDI's claims were not property of the estate and not related to the bankruptcy proceeding. "It therefore ruled that SDI's claims were not subject to the automatic stay under § 362, nor to an injunction under § 105 of the Bankruptcy Code." Teknek, 563 F.3d at 642. The Seventh Circuit affirmed the district court on both points, holding that it had properly vacated the bankruptcy court's injunction. Thus, Teknek squarely addresses the propriety of an injunction under § 105, and demonstrates that something more than the claims simply involving the same pool of assets (even if very large) is needed to authorize the injunction. It is that something more that is missing in the instant case.

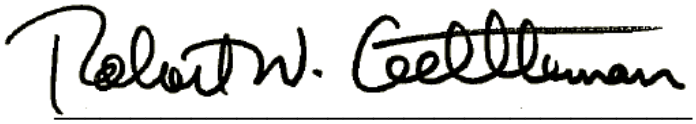
Without that something more, the instant case, like Teknek, is more akin to the "common case" where a creditor of a bankrupt corporation files a suit against the bankrupt's insurer or guarantor. Such suits are allowed to proceed because they are "only nominally against the debtor because the only relief sought is against [its] insurer, guarantor, or other similarly situated party." Teknek, 563 F.3d at 649 (quoting Fisher, 155 F.3d at 882-83).

Thus, for the same reason that a suit against a bankrupt's guarantor is not discharged under 11 U.S.C. § 524(e), because a discharge "does not affect the liability of any other entity on the debtor's debt," In re Hendrix, 986 F.2d 195, 197 (7th Cir. 1993), a third party action against a debtor's guarantor is not typically stayed under § 105(a). Consequently, the bankruptcy court's conclusion that Debtors are not entitled to an injunction is not erroneous as a matter of law and is not an abuse of discretion. The decision is affirmed.

CONCLUSION

For the reasons described above, the decision of the bankruptcy court is affirmed.

ENTER: October 6, 2015



Robert W. Gettleman
United States District Judge

KIRKLAND & ELLIS

March 9, 2017

Caesars' Chapter 11: Analyzing a Debtor's Ability to Enjoin Non-Debtor Third-Party Litigation

I. INTRODUCTION

This article analyzes one of the key issues in the Caesars Entertainment Operating Company, Inc. ("CEOC") chapter 11 cases: the ability to enjoin third party claims against non-debtors. Under established case law, bankruptcy courts may issue injunctions pursuant to section 105 of title 11 of the United States Code, 11 U.S.C. §§ 101–1532 (the "Bankruptcy Code"), which provides that a bankruptcy court "may issue any order, process or judgment that is necessary or appropriate to carry out the provisions" of the Bankruptcy Code. 11 U.S.C. § 105. *See, e.g.*, *In re Otero Mills, Inc.*, 21 B.R. 777, 779 (Bankr. D.N.M. 1982) (finding power to issue injunction under section 105 where (1) without the injunction there would be irreparable harm to the estate, (2) there was a likelihood for a successful reorganization, and (3) there was minimal or no harm to the enjoined party); *In re Monroe Well Service, Inc.*, 67 B.R. 746, 752 (Bankr. E.D. Pa. 1986) ("[T]he bankruptcy court, as a court of equity, has the power to issue injunctions under section 105 to prevent significant harm to the estate in appropriate circumstances.").

In CEOC's chapter 11 cases, CEOC had claims against its ultimate parent, Caesars Entertainment Corporation ("CEC"), and certain other non-debtors related to certain capital markets and sale transactions that CEOC asserted gave rise to, among other things, fraudulent conveyance and breach of fiduciary duty claims (the "Challenged Transactions"). CEOC ultimately asserted that these claims were worth between $3.2 and $5.8 billion, and were key estate assets for CEOC's reorganization. Prior to CEOC's bankruptcy filing, CEC took steps resulting in the release of its guaranty of approximately $13 billion of CEOC's bond debt. Certain of CEOC's creditors brought claims against CEC, CEOC, and others related to the Challenged Transactions and the release of CEC's guarantees of CEOC's debt. Once CEOC filed for bankruptcy, derivative creditor claims related to the Challenged Transactions (the "CEOC Claims") were stayed by the imposition of the automatic stay because such claims were property of the bankruptcy estate. But creditors continued to pursue, and other creditors commenced, direct actions against CEC, asserting, among other things, that the release of the guarantees was a violation of the Trust Indenture Act of 1939 and a breach of contract (the "Creditor Claims").

Shortly after CEOC's bankruptcy filing, CEOC moved to stay the Creditor Claims under section 105 of the Bankruptcy Code. CEOC's creditors opposed CEOC's requests for an injunction, ultimately resulting in four separate trials and three appeals of the underlying decisions. The first of these appeals eventually reached the Seventh Circuit Court of Appeals, which set out a broad standard for when it is appropriate for a bankruptcy court to issue an injunction of a dispute between two non-debtors.

This article focuses on Seventh Circuit precedent prior to CEOC's bankruptcy cases, lower court decisions grappling with that precedent, and the Seventh Circuit's decision in CEOC's chapter 11 cases.

II. SEVENTH CIRCUIT PRECEDENT PRIOR TO 2015

In 1994, the Seventh Circuit noted that if a bankruptcy court had at least "related to" jurisdiction over a claim or non-debtor litigation pursuant to 28 U.S.C. § 1334(b), then the court had the authority to stay such suits pursuant to section 105 of the Bankruptcy Code. *See Zerand-Bernal Grp., Inc. v. Cox* 23 F.3d 159, 161–62 (7th Cir. 1994) ("Once [an action is] shoehorned into the bankruptcy court on the authority of section 1334(b), such suits can then be stayed by authority of section 105 of the Bankruptcy Code."). After that decision, the Seventh Circuit was asked to examine the scope of a section 105 injunction in two cases that reached seemingly contradictory conclusions. *See Fisher v. Apostolou*, 155 F.3d 876 (7th Cir. 1998); *Levey v. Sys. Div., Inc. (In re Teknek, LLC)*, 563 F.3d 639 (7th Cir. 2009). As discussed below, in one case (*Fisher*), the Seventh Circuit held that an injunction was appropriate, but in the other (*Teknek*), the Seventh Circuit held that an injunction should not be issued. Each of these cases is examined in turn.

A. *Fisher*

Fisher involved a Chapter 7 debtor corporation which illegally traded investor funds. During the bankruptcy proceedings, a group of defrauded investors (the "Apostolou Plaintiffs") sought to file claims (the "Apostolou Claims") against certain third parties, a clearinghouse and sellers of commodities, affiliated with the debtor (the "Apostolou Defendants"). *Fisher*, 155 F.3d at 878. The bankruptcy trustee sought to enjoin the claims of the Apostolou Plaintiffs against the Apostolou Defendants under section 105 because the trustee was also pursuing claims against the Apostolou Defendants. The bankruptcy court granted this injunction on the basis that both the trustee and the Apostolou Plaintiffs were "pursuing the same dollars from the same defendants to redress the same harms" done to the debtor. *Id.* at 879. The district court disagreed with the bankruptcy court, stating that the Apostolou Claims were not property of the bankrupt estates due to the fact that the debtor was a party to the fraud, not a victim of it. *Id.* In such a circumstance, the district court held that the bankruptcy court could not enjoin the third-party litigation against a non-debtor.

On appeal, the Seventh Circuit reversed the district court's decision. *Id.* at 883. In doing so, the Seventh Circuit reiterated the standard that a bankruptcy court may use section 105 to enjoin the adjudication of claims that are not property of the estate so long as the claims in question are sufficiently "related to" the trustee's (or debtor's) work on behalf of the estate. *Id.* at 882. The Seventh Circuit held that because the Apostolou Plaintiffs asserted claims "to the same limited pool of money, in the possession of the same defendants, as a result of the *same acts*, performed by the same individuals," the Apostolou Claims were sufficiently related to the estate's claims and thus were appropriately stayed. *Id.* (emphasis added). Despite this somewhat limiting language on the basis for the particular injunction in *Fisher*, the Seventh Circuit had seemingly reaffirmed the core of *Zerand-Bernal* by reaffirming that an injunction was appropriate when the non-debtor third party litigation was "related to" the bankruptcy case.

B. *In re Teknek*

The Seventh Circuit was asked again to consider the scope of a section 105 injunction in 2009 in *In re Teknek*. 563 F.3d 639. Prior to the commencement of Teknek's chapter 7 case, one of Teknek's competitors ("SDI") obtained a judgment for patent infringement against each of the debtor and its affiliate company ("Electronic"). *Id.* at 641. While the patent suit was pending, the shareholders of the debtor transferred the debtor's and Electronic's assets into a new entity, leaving the debtor and Electronic both insolvent. *Id.* In addition, SDI sought and obtained a finding that Electronic's and the debtor's shareholders were jointly and severally (and directly) liable to SDI on an alter ego theory. After entry of the patent infringement judgment against it, Teknek filed for bankruptcy protection under chapter 7. Following the debtor's filing, SDI sought to collect the amounts owed to it under the judgment lien from the debtor's shareholders. *Id.* at 642. The bank-

ruptcy trustee also filed an adversary proceeding against the debtor's shareholders, asserting claims of fraudulent transfer and breach of fiduciary duty and also seeking to hold them personally liable for the debtor's obligation on the SDI judgment lien based on an alter ego theory. *Id.* at 643. The debtor in *Teknek* had no material creditors other than SDI.

The bankruptcy court entered the injunction, holding that it was necessary because SDI's proceedings were negatively affecting the trustee's attempts to settle the case for the benefit of the debtor's estate. *Id*. The district court reversed and vacated the injunction. In reversing the bankruptcy court's injunction, the district court found that SDI's judgment lien claim was joint and several against the debtor, Electronic, and the debtor's shareholders in their capacity as alter egos of Electronic. *Id.* The district court concluded that SDI's claims against non-debtors should not be enjoined because the claim was "personal to [SDI] and independent of any claim a hypothetical general creditor could have brought against" the debtor. *Id*. at 644. The district court further elaborated, stating that what made the claim unrelated to the chapter 7 proceedings was the fact that it was a claim against an "independent non-debtor" who was independently liable for the full amount owed under the claim. *Id.*

The Seventh Circuit upheld the district court's reversal of the injunction. In comparing the *Teknek* facts to *Fisher*, the Seventh Circuit held that the injunction in *Fisher* was appropriate because the claims to be enjoined in *Fisher* "against the non-debtor fiduciaries depended on the non-debtor's misconduct *with respect to the corporate debtor*." *Id.* at 649. In *Teknek*, however, the creditor claims "were not based on the same acts" but rather "separate acts, which caused separate injuries to separate companies, only one of which is in bankruptcy." *Id.* In this instance, the fact that there were similar shareholders of both Teknek and Electronic was "not sufficient to bring SDI's claim against Electronics under the umbrella of the bankruptcy proceeding." *Id.*

III. THE CEOC BANKRUPTCY AND DISTRICT COURT DECISIONS

CEOC sought an injunction of the Guaranty Actions in March 2015. The basis for that injunction request was that CEOC had claims against CEC on account of the Challenged Transactions that CEOC would either settle or litigate, but which were vital to CEOC's ability to deliver significant recoveries to all creditors. CEOC's argument was that the creditors pursuing the Guaranty Actions sought to "jump the line" and drain CEC of its resources ahead of other creditor recoveries, thus harming other creditors in the process of asserting the guarantees against CEC.

The trial on CEOC's initial injunction request was held in early June 2015, and the bankruptcy court issued its ruling in July. The bankruptcy court began by analyzing the facts underlying the CEOC Claims against CEC and the Creditor Claims against CEC. As noted above, the CEOC Claims were based on a series of capital market and sale transactions that harmed CEOC by improperly removing assets from CEOC to other non-debtor affiliates. Conversely, the Creditor Claims were based on other transactions that resulted in the alleged improper release of CEC's guaranty of CEOC's debt. *In re Caesars Entm't Operating Co., Inc.*, 533 B.R. 714, 722 (Bankr. N.D. Ill. 2015).

The bankruptcy court ultimately determined that the CEOC Claims and the Creditor Claims were not based on the "same acts." The bankruptcy court held that the CEOC Claims were based on a series of potentially fraudulent transactions, whereas the Creditor Claims were based on the alleged release of CEC's separate contractual guaranty of CEOC's debt. The bankruptcy court held that although facts underlying both sets of claims may overlap, the facts were nonetheless separate and distinct. *See id.* at 731 (finding that the allegations underlying the CEOC Claims "are not essential ... to the [Creditor C]laims"). The bankruptcy court also found that CEOC had not identified any estate claims against CEC on account of the release of the CEC debt guarantees. *Id.*; *id.* at n.15.

The bankruptcy court held that under *Fisher* and *Teknek*, the standard of "sufficiently related to" could only be satisfied when the claims of the estate and the claims of a third-party were "claims to the same assets in possession of the same defendants, and both sets of claims arise out of the *same acts*." *Id*. at 730 (emphasis added). Under the bankruptcy court's formulation, an injunction could only be issued when "the debtor's estate has a claim against the non-debtor" and the "claim is based on the same acts and would be paid from the same assets as the third party's claim against the non-debtor." *Id.* at 732. As a result, the bankruptcy court refused to enjoin the Creditor Claims.

On appeal, the District Court in the Northern District of Illinois affirmed. *In re Caesars Entm't Operating Co., Inc.*, 2015 WL 5920882, at *1 (N.D. Ill. Oct. 6, 2015). The district court held that the creditors' injuries stemmed from CEC's alleged failure to honor its guarantees, and noted that the bankruptcy court had found that CEOC had no direct claims against CEC based on the release of those guarantees. *Id.* at *5. The district court held that without "something more," there was no basis to enjoin the Creditor Claims no matter how large CEOC's claims may be and no matter that they may seek a recovery from the very same pool of assets from which the creditors' claims sought a recovery. *Id.* at *6.

IV. THE SEVENTH CIRCUIT RULING

On further appeal, the Seventh Circuit reversed the district court. *In re Caesars Entm't Operating Co., Inc.*, 808 F.3d 1186 (7th Cir. 2015). The Seventh Circuit held that there is no "same acts" requirement to issue an injunction. Although section 105 does not give the court "carte blanche" because it does not let a court override other provisions of the bankruptcy code, "it grants the extensive equitable powers that bankruptcy courts need in order to be able to perform their statutory duties." *Id.* at 1188. Once a bankruptcy court has jurisdiction over the matter (and there is "related to" jurisdiction over issues relating to the guaranty of a debtor's debts), the question that the court must ask is whether "the injunction sought . . . is likely to enhance the prospects for a successful resolution of the disputes attending [the] bankruptcy," and whether the denial of the injunction could endanger successful reorganization efforts by a debtor. *Id.* at 1188–89.

The Court then went on to explain that its decision was consistent with its prior holdings in *Fisher* and *Teknek*. *Fisher* involved a "more clear-cut case" for relief involving parties pursuing the same dollars from the same defendants to address the same harm. *Id.* at 1190. But the fact that *Fisher* was more clear-cut did not mean that CEOC was not entitled to the section 105 injunction it sought. *Id.* Rather, in both *Fisher* and CEOC's case, injunctive relief "could well facilitate a prompt and orderly wind-up of the bankruptcy." *Id. Teknek*, on the other hand, was different because there was only one major creditor and it could collect its claims (based on separate acts) entirely from the non-debtor without need for recourse against the debtor. *Id.* Thus, allowing the creditor in *Teknek* to pursue its claim against Electronic would have not affected the recoveries to the broader group of the debtor's creditors. *Id*. In CEOC's case, however, the potential injuries to CEOC's creditors and to the creditors pursuing the Creditor Claims were "not readily separable," because, for instance, "some of the same creditors have claims against both CEOC and CEC for repayment of the same loans, and their ability to recover from CEC (the guarantor) may depend on the amount they can recover directly from CEOC, their borrower. And were guarantor liability to be imposed on CEC, CEC's ability to satisfy CEOC's fraudulent-conveyance claims against it — and thus pay other creditors — would be impaired." *Id.* at 1190–91. The Seventh Circuit remanded to the bankruptcy court for further proceedings.

On remand, the bankruptcy court entered a temporary injunction. *In re Caesars Entm't Operating Co., Inc.*, 561 B.R. 441 (Bankr. N.D. Ill. 2016). The bankruptcy court held that an injunction was appropriate because it would enhance CEOC's prospects for a successful reorganization, serve the public interest, and ensure the balance of equities in CEOC's favor.[1] *Id.* at 450.

V. CONCLUSION

At core, the Seventh Circuit's opinion serves as an affirmation of a bankruptcy court's extensive equitable powers to protect its jurisdiction. The Seventh Circuit held that it is appropriate to issue an injunction when it will "enhance the prospects for a successful resolution" and "its denial will thus endanger the success of the bankruptcy proceedings." *Caesars*, 808 F.3d at 1189. This power makes sense given one of the primary purposes of the bankruptcy code: channeling all claims against a debtor and debtor assets into the bankruptcy estate for the equitable distribution to all creditors. *See, e.g.*, *Constitution Bank v. Tubbs*, 68 F.3d 685, 691 (3d Cir. 1995); *SEC v. Brennan*, 230 F.3d 65, 71 (2d Cir. 2000).

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[1] CEOC sought to obtain additional section 105 injunctions related to the same Creditor Claims over the course of its bankruptcy cases, certain of which the bankruptcy court granted and one of which was denied (though the Creditor Claims were stayed by the district court pending appeal). Those proceedings were fact-specific and go beyond the scope of this article.

If you have any questions about the matters addressed in this publication, please contact the Kirkland author or your regular Kirkland contact.

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