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EHYA Flash Forum

THE REALOGY DECISION

Thursday, 22 January 2009

The Realogy Decision

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Realogy Corporation, Harrah's Entertainment, Inc. Exchange Offers



Realogy Corporation Exchange Offers

Background



- **Realogy Corporation's capital structure includes:**
 - a \$3.17 billion term loan facility and \$750 million revolving loan and letter of credit facility under a secured Credit Agreement;
 - \$1.7 billion 10.50% unsecured Senior Notes due 2014;
 - \$875 million 12.375% unsecured Senior Subordinated Notes due 2015; and
 - \$550 million 11.00%/11.75% unsecured Senior Toggle Notes.
- On November 13, 2008 Realogy invited the noteholders to exchange their notes for \$500 million of new second lien term loans to be incurred by Realogy under the accordion feature of the Credit Agreement (the "Second Lien Term Loans").
- The primary objectives for the Company in designing the transaction were to:
 - reduce cash interest expense obligations; and
 - capture discounts in the Company's debt issues.

Background, cont'd.

- The proposed exchange offer was open to (in order of priority):
 - the Senior Subordinated Noteholders (some of the Senior Subordinated Notes were owned by Apollo Management);
 - the Senior Noteholders; and
 - the Senior Toggle Noteholders.
- The Senior Subordinated Noteholders would have been permitted to leapfrog senior debt (*i.e.*, the Senior Toggle Notes) in Realogy's capital structure (new security/ shorter maturity).

Realogy Offer Table

<u>Existing Notes</u>	<u>Outstanding Principal Amount</u>	<u>Tranche of New Term Loans</u>	<u>(Early Commitment) Price</u>	<u>Acceptance Priority Level</u>
12.375% Senior Subordinated Notes due 2015	\$875m	Term C	0.36	1
10.50% Senior Notes due 2014	\$1,700m	Term C	0.503	2
11.00%/11.75 % Senior Toggle Notes due 2014	\$582.2m	Term D	0.472	3

Litigation

- On November 24, 2008, Realogy received a letter from a law firm purporting to represent various institutions holding a majority in principal amount of the Senior Toggle Notes asserting, amongst other things, that the invitations to take part in the exchange offer are not permitted by the Credit Agreement or the indentures.
- On November 26, 2008, the early commitment period expired and Realogy had received approximately \$237 million of commitments.
- On the same day, the Senior Toggle Notes trustee and an entity controlled by Carl Icahn sued Realogy in the Delaware Chancery Court seeking declaratory relief that the invitations and the incurrence of the Second Lien Term Loans constituted a breach of the Senior Toggle Notes Indenture.
- In addition, Icahn sought declaratory and injunctive relief that the completion of the transaction would constitute a fraudulent conveyance by Realogy.

Litigation, cont'd.

- The parties agreed to expedite the contract claim and to put the fraudulent conveyance claim on hold pending resolution of the contract claim.
- Realogy agreed to extend the termination date until a date after which a decision on the contract claim was expected.
- On December 9, 2008, the parties submitted opening briefs on their cross-motions for summary judgment.
- On December 14, the parties submitted answering briefs on their cross-motions for summary judgment.
- A hearing was held on December 15, 2008.

Claims

- The Senior Toggle Noteholders' claims boiled down to the same proposition: that the proposed Second Lien Term Loans violated the Senior Toggle Notes Indenture because they violated the Credit Agreement (note that lenders under the Credit Agreement were not a party to the lawsuit).
- The Senior Toggle Notes Indenture allows a Permitted Lien for liens securing new debt under the Credit Agreement.
- If the Second Lien Term Loans violated the Credit Agreement, then the second-ranking liens securing them would not qualify as Permitted Liens under the Senior Toggle Notes Indenture.

Claims, cont'd.

- The Senior Toggle Noteholders argued that the proposed Second Lien Term Loans violated the Credit Agreement on two grounds:
 - the Second Lien Term Loans would not be loans “under the Credit Agreement” because they would not be funded in cash; and
 - the refinancing of the Senior Subordinated Notes with Second Lien Term Loans does not constitute Permitted Refinancing Indebtedness under the Credit Agreement.

Claims, cont'd.

- Loans must be funded in cash.
 - Senior Toggle Noteholders argued that the Credit Agreement speaks to loans in currency terms.
 - Senior Toggle Noteholders pointed to certain procedural and administrative provisions of the Credit Agreement as evidence that only cash-funded loans are permitted.
- The Court rejected both arguments.

Claims, cont'd.

- The proposed Second Lien Term Loans would violate the negative covenant in the credit agreement restricting Realogy's ability to make payments on the Subordinated Notes, Senior Notes and Senior Toggle Notes.
- Realogy argued that the Second Lien Term Loans would qualify under the "Permitted Refinancing Indebtedness" exception and therefore would be permitted under the Credit Agreement.

Claims, cont'd.

- The definition of “Permitted Refinancing Indebtedness” has a provision that states that the new debt cannot have “different obligors, or greater guarantees or security.”
- Under a proviso to this particular definition, however, “security may be added to the extent then permitted under Article VI [negative covenants].”

Claims, cont'd.

- Issue is whether the new Second Lien Term Loans meet the definition of “Permitted Refinancing Indebtedness”.
 - Realogy argued that:
 - the proviso means that if a lien is permitted by Article VI, it may be added to the refinancing indebtedness; and
 - since Article VI permits liens securing loans under the Credit Agreement, the new refinancing debt is allowed to be secured.
 - The Senior Toggle Noteholders argued that:
 - Realogy’s interpretation was too broad and would render the general restriction meaningless; and
 - the proviso means that if the indebtedness being refinanced could itself be secured, then the refinancing indebtedness can also be secured.

New York Contract Law Points

- “In interpreting contract language, New York contract law instructs courts ordinarily to give the words and phrases employed their plain and commonly accepted meanings.” *Law Debenture Trust Co. v. Petrohawk Energy Corp.*, 2007 WL 2248150, at *6 (Del. Ch.).
- “In its efforts to preserve the parties’ rights and the status quo, the court must be careful not to alter the terms of the agreement. The parties, having agreed upon their own terms and conditions, “the courts cannot change them and must not permit them to be violated or disregarded.”” *Metro. Life Ins. Co. v. RJR Nabisco, Inc.*, 906 F.2d 844, 899 (2d Cir. 1990) (some internal citations and quotations omitted) (quoting *Whiteside v. North American Accident Ins. Co.*, 93 N.E. 948, 950 (N.Y., 1911)).
- Interpretations of an unambiguous contract that render provisions meaningless are disfavored under the law. See, e.g., *Whitebox Convertible Arbitrage Partners, L.P. v. IVAX Corp.*, 482 F.3d 1018, 1021-22 (8th Cir. 2007) (applying New York law to a trust indenture).

Delaware Chancery Court's Holding

- The Court held that the Senior Toggle Noteholders' reading of the definition of Permitted Refinancing Indebtedness was the better reading.
- The Court agreed that Realogy's interpretation of the proviso would make it "the exception that swallows the rule". *Realogy* Opinion at 27
- "[Realogy's] interpretation would allow a mere proviso clause to entirely sap the vitality of what would otherwise be a significant restriction." *Realogy* Opinion at 28



Harrah's Entertainment, Inc. Exchange Offers

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- **On November 14, 2008, Harrah's announced private exchange offers to exchange the following outstanding unsecured notes for up to \$2.1 billion aggregate amount of New Second Lien Notes:**
 - 10.0% Second Lien Senior Secured Notes due 2015 for Old Notes maturing between 2010 and 2013; and
 - 10.0% Second Lien Senior Secured Notes due 2018 for Old Notes maturing between 2015 and 2018.
 - The amount of New Second Lien Notes to be issued in the exchange offers would not exceed the lesser of (a) \$2.1 billion and (b) any amount that would cause cancellation of debt income to exceed \$1.8 billion.
 - Four different acceptance priority levels across 10 series of notes with priority levels 2 and 3 subject to additional caps.
 - Approximately \$6.0 billion of notes was tendered, representing over 55% of the total outstanding notes.
 - An aggregate of approximately \$2.2 billion in existing notes was accepted.
 - \$1.050 billion in new second lien debt was issued.

Harrah's Offer Table

<u>Existing Notes</u>	<u>New Second Lien Notes due</u>	(Early Tender) <u>Price</u>	<u>Acceptance Priority Level</u>
5.50% Senior Notes due 2010	2015	1.00	1
7.875% Senior Subordinated Notes due 2010	2015	1.00	1
8.0% Senior Notes due 2011	2015	0.80	1
8.125% Senior Subordinated Notes due 2011	2015	0.80	1
5.375% Senior Notes due 2013	2015	0.50	1
5.625% Senior Notes due 2015	2018	0.40	2
6.5% Senior Notes due 2016	2018	0.40	2
5.75% Senior Notes due 2017	2018	0.40	2
10.75%/11.5% Senior Toggle Notes due 2018	2018	0.5725	3
10.75% Senior Notes due 2016	2018	0.70	4

Claims against Harrah's Entertainment, Inc.



- **On January 9, 2009, noteholders that had been excluded from the Exchange Offers brought suit in Delaware District Court against Harrah's Entertainment, Inc., Harrah's Operating Company, Inc. and the Board of Directors alleging that:**
 - the Exchange Offers breached the noteholders' indentures by, *inter alia*, not securing the New Notes equally and ratably with the Old Notes;
 - the Exchange Offers breached Sec. 14(d)(7) of the Securities Exchange Act of 1934 which prohibits unfair, arbitrary and discriminatory tender offers for similarly-situated securities holders;
 - the Exchange Offers breached the Trust Indenture Act by impairing the rights of the plaintiffs without proper consent due for the subordination of their Old Notes to the New Notes, thereby likely rendering their claim worthless "as the specter of Harrah's insolvency approaches";
 - the Company unilaterally and arbitrarily determined who and which entities were eligible as QIBs and certain non-U.S. investors located outside the United States (as the Exchange Offers were, however, limited to "QIBs" and "certain non-U.S. investors located outside the United States."), thereby excluding the plaintiffs, who believed they were eligible noteholders, from the Exchange Offers; and
 - the Board of Directors, in creating, ratifying, executing, negotiating and consummating the Exchange Offers, are themselves liable for the harm allegedly caused to the plaintiffs.

THANK YOU



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