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Restructuring Support Agreements, Ad Hoc Committees And Non-Debtor Third-Party Releases Win by a Nose

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In Ben Hur, Judah Ben-Hur's team of white horses beat Messala's black horses in the climactic chariot race. In a similar battle to the death in In re Indianapolis Downs, LLC, the white horses won again when Delaware Bankruptcy Judge Brendan L. Shannon confirmed Indianapolis Downs' joint Chapter 11 plan of liquidation (the "Plan") over a series of hard-fought objections focusing on the implications of a Restructuring Support Agreement and the propriety of third-party releases. The Bankruptcy Court also denied a motion to designate the votes of certain creditors on the Plan, without which the Plan would have pulled up lame leaving Plan confirmation to another jockey and another race. The Bankruptcy Court's decision can be found HERE.

The Debtors operate a "racino" (combination horse track and casino) in Shelbyville, Indiana, within just a few furlongs of Indianapolis (and not to be confused with the Shelbyville of Civil War fame, which also happens to be the "American Saddlebred Capital of the World"). The Debtors declared as win, place and show three pieces of prepetition secured debt heading into the Chapter 11 race – a $98 million first lien, $375 million second lien and $78 million third lien – leaving the Debtors well short of the finish line from a financial perspective. Chapter 11 ensued. A year later, the Debtors pulled into the starting gate with a Restructuring Support Agreement that permitted the jockey to either push toward the rail for an internal recap or move outside for a third-party sale. A sale it was, and the Debtors proposed to cross the finish line holding the reins of a $500 million offer. Various insiders (known as the Oliver Parties) objected, forcing the Judge to choose the right horse for the course.

First, the Oliver Parties sought to disallow the votes of the creditors who had entered into the RSA, on the basis that it comprised an improper postpetition solicitation of votes on the Plan. This was not a lame attempt – there were cases that legitimately supported both sides. In the end, however, Judge Shannon rode with the Debtors, concluding that properly negotiated and pursued RSAs should be encouraged. The Judge started with the Secretariat of solicitation cases: the Third Circuit's decision in In re Century Glove, which applied a narrow construction of the type of conduct that would constitute "improper solicitation."

The Bankruptcy Court also relied heavily on a Texas bankruptcy case – In re Heritage Organization, L.L.C. – in reaching its decision not to disallow the votes. In the Heritage court's words, "if a creditor believes that it has sufficient information about the case and the available alternatives to jointly propose a Chapter 11 plan with another entity . . . it is absurd to think that the signing of a term sheet by those parties (that contains the material terms of their to-be-filed joint plan and states that the co-proponent creditor(s) will vote for their agreed upon joint plan) is an improper solicitation of votes in accordance with § 1125(b)." The Bankruptcy Court found the reasoning in Heritage dispositive, and held that signing the RSA postpetition helped to facilitate creditor negotiations, especially where the prepetition negotiations had broken down, and it was therefore not an improper solicitation warranting designation of voting rights.

The Oliver Parties also tried to make hay by challenging the Plan's fee payment provisions. First, they argued that the Plan's cap on professional fees violated the Bankruptcy Code's requirement that all administrative expenses must be paid in full. Second, they tried to trip up the Plan's proposal to pay the fees of an ad hoc committee. However, it was the lawyers who galloped to victory when the Judge hobbled both these arguments. As to administrative expenses, the Bankruptcy Court concluded that the Plan did not provide for capped payment of professional fees, it only provided that the RSA parties no longer needed to support the Plan if the caps were exceeded. For the ad hoc committee fees, the Court said you cannot expect the jockey to ride for free. The ad hoc committee's professionals trained and rode the winning horse and should be entitled to payment for their services.

Finally, the Oliver Parties rode double on the United States Trustee's mount, which reared up over third-party releases in the Plan. Of particular interest here was the Plan's provision that, if you do not vote on the Plan, you are deemed to have consented to the releases. This sounded to the US Trustee like losing a bet you never even place. However, the Court sent the US Trustee back to the stables, concluding that the non-voting creditors had been fully informed about the deemed release and therefore had a fair opportunity to escape before the barn door closed.

There are four important takeaways from Indianapolis Downs that will leave you four lengths ahead as a creditor in a race to confirm a Chapter 11 plan in Delaware. First, when you sign an appropriately drafted Restructuring Support Agreement postpetition, you have good odds that you will be permitted to spur it on towards victory. Second, you can condition your support on a fee cap, as long as you realize that, sooner or later, the lawyers need to be fed their oats. Third, if you are in an ad hoc group and you make a substantial contribution to the case, there is now a well-reasoned decision to keep you on track for reimbursement of your fees. And finally, third-party releases can be enforced in Delaware under certain circumstances, even as against creditors who cast no vote at all. And, of course, when dealing with a racino, expect a wild ride but don't get thrown by fences in your path.