UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

TRILOGY PORTFOLIO COMPANY, LLC, *et al.*, Plaintiffs, v. CAESARS ENTERTAINMENT CORPORATION, *et al.*, Defendants.	Case No. 1:14-cv-07091 (JSR)
FREDERICK BARTON DANNER, Individually and On Behalf of All Others Similarly Situated, Plaintiff, v. CAESARS ENTERTAINMENT CORPORATION, *et al.*, Defendants.	Case No. 1:14-cv-07973 (JSR) [Rel. Case No. 1:14-cv-07091 (JSR)]

REPLY MEMORANDUM OF LAW IN FURTHER SUPPORT OF PLAINTIFFS' JOINT MOTION FOR PARTIAL SUMMARY JUDGMENT

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Plaintiffs Trilogy Portfolio Company, LLC and Relative Value-Long/Short Debt, A Series of Underlying Funds Trust (the "Trilogy Plaintiffs"), together with Plaintiff Frederick Barton Danner ("Danner," and with the Trilogy Plaintiffs, "Plaintiffs"), respectfully submit this reply memorandum of law in further support of their joint motion for partial summary judgment.

PRELIMINARY STATEMENT

After multiple rounds of summary judgment briefing, the defects in CEC's case are now more apparent than ever.[1] In order to avoid liability based on its removal of the Guarantee from Plaintiffs' Indenture as part of the August Transaction, CEC must convince the Court that:

1. its Guarantee is not an "indenture security" under the TIA, even though the Securities Act, the TIA, the SEC, and CEC's own documents say that it is;
2. the Guarantee is not a "core term" of the Indenture, despite contrary holdings in *Federated*, *Marblegate*, *BOKF*, and this case; and
3. the Guarantee is not a "Security" for the purposes of the Indenture, despite the Indenture's specific inclusion of the Guarantee in the definition of that term.

If CEC loses on any of the above three issues, Plaintiffs are entitled to judgment under Section 316(b) of the TIA or, alternatively, Section 508 of the Indenture.

The prospects for CEC's guarantee release defense are equally grim. If the Guarantee was really released as a result of the May Transactions, then why did CEC and CEOC pay [redacted] to the Favored Noteholders to have it removed from the Indenture three months later? CEC does not address that question, but the answer is obvious: under the plain language of Regulation S-X and guidance from the SEC Staff and FASB, CEC continues to own

[1] Capitalized terms not defined herein have the same meaning as set forth in the Memorandum of Law in Support of Plaintiffs' Joint Motion for Partial Summary Judgment [*Trilogy* ECF No. 145; *Danner* ECF No. 123] ("Pls.' Br.").

"substantially all" of CEOC's voting shares. Although CEC argues at length that the Court should ignore applicable guidance from the SEC Staff and FASB on this issue, CEC offers no alternative basis for the Court's analysis of the regulation. Nor, as CEC urges, should the Court delay ruling on this issue based on purported factual disputes. The undisputed material facts confirm that at all relevant times CEC exercised complete and unchecked control over CEOC and its assets. Accordingly, CEC's defense fails as a matter of law.

For the reasons set forth below and in Plaintiffs' original moving papers and papers in opposition to CEC's motion for summary judgment, Plaintiffs are entitled to summary judgment.

ARGUMENT

I. PLAINTIFFS ARE ENTITLED TO SUMMARY JUDGMENT ON THEIR CLAIMS THAT THE AUGUST TRANSACTION VIOLATED SECTION 316(b) OF THE TIA AND SECTION 508 OF THE INDENTURE

A. The Guarantee is an "Indenture Security" Under the TIA

CEC's argument that the Guarantee is not an "indenture security" under Section 316(b) of the TIA is contrary to the express language of the applicable statutes and regulations. Although CEC argues that the Securities Act "states that a 'security' *can* include a 'guarantee' of a 'note'" depending on "a fact-specific analysis of its economic features,"[2] the statute says nothing of the kind. Rather, the Securities Act unambiguously states that a "guarantee" of any instrument it otherwise defines as a "security" is a "security" in and of itself. *See* 15 U.S.C. §77b(a)(1) (defining the term "security" to "mean[] any note, . . . bond, debenture, evidence of indebtedness . . . or . . . guarantee of . . . any of the foregoing.") (emphasis added). CEC fails to address the additional provisions of the TIA and applicable SEC guidance confirming that the Guarantee is a "security" under the Securities Act and an "indenture security" under the TIA.

[2] Mem. of Law of Caesars Entm't Corp. in Opp'n to Pls.' Mot. for Summ. J. [*Trilogy* ECF No. 153; *Danner* ECF No. 134] ("CEC Opp'n Br.") at 17.

See 15 U.S.C. § 77ddd(a)(1) (TIA Section 304) ("The provisions of [the TIA] shall not apply to any of the following securities: (1) any security other than (A) a note, bond, debenture, or evidence of indebtedness, whether or not secured. . . or (C) a temporary certificate for, or guarantee of, any such note, bond, debenture, evidence of indebtedness, or certificate . . . ." (emphasis added)); 15 U.S.C. § 77ccc(12) (TIA Section 303(12)) (including "guarantor" in the definition of "obligor"); Financial Statements and Periodic Reports for Related Issuers and Guarantors, SEC Release No. 33-7878 (effective Sept. 30, 2000), https://www.sec.gov/rules/final/33-7878.htm ("Guarantees of Securities are securities themselves for purposes of the Securities Act of 1933.").

Relying on the foregoing authorities, CEC's own lawyers have publicly advised that "Guarantees of securities are securities themselves for the purposes of the [Securities Act]." Supplemental Decl. of Clay J. Pierce in Supp. of Pls.' Joint Mot. for Partial Summ. J. ("Suppl. Pierce Decl."), Ex. C; Supplemental Decl. of Gordon Z. Novod in Supp. of Pls.' Joint Mot. for Partial Summ. J. ("Suppl. Novod Decl."), Ex. C. CEC admits that, consistent with this advice, it registered the Guarantee[3] with the SEC and represented that it was among "a class of securities to be registered." *See* CEC Opp'n Br. at 18. Regardless of whether CEC's admissions in its SEC filings are "binding,"[4] the Court can and should consider them when evaluating the merits

[3] CEC argues that, if the Guarantee is an indenture security, "'the SEC should have issued stop orders whenever'" it was confronted with indentures including guarantee release provisions. CEC Opp'n Br. at 20-21 (quoting Ben H. Logan, *The Trust Indenture Act, Debt Restructuring & Reorganization Tourism (Part I)*, 36 Bank. L. Letter No. 3 (March 2016) at 15). CEC is comparing apples and oranges. Plaintiffs' argument is not premised on a release of the Guarantee pursuant to the terms of the Indenture (*i.e.*, Section 1503), but rather on CEC's wholesale removal of the Guarantee from the Indenture.

[4] CEC cites *Great Rivers Co-Op. of Se. Iowa v. Farmland Indus., Inc.*, 198 F.3d 685, 699 (8th Cir. 1999) in support of its position, CEC Opp'n Br. at 18, but in that case the court affirmed dismissal of plaintiffs' fraud claims under the federal securities laws because the underlying instrument (capital credits in an agricultural cooperative) "lack[ed] the essential characteristics of

and credibility of CEC's argument. The Court also should consider CEC's internal memorandum stating that, in regard to CEC and CEOC's reporting obligations following the May Transactions, "[u]nder the US Securities laws, a guarantee of a security is considered to be a security separate and apart from the security it guarantees."[5] Regardless of whether the memorandum was a draft or considered by counsel, *see* CEC Opp'n Br. at 20, CEC's actions were entirely consistent with the memo: because the Guarantee is a "security," CEC registered the Guarantee with the SEC.[6]

CEC's argument that the Guarantee is not an indenture security also finds no support in the case law. As confirmed by the Supreme Court cases CEC cites, because it is undisputed that the Notes were issued for "investment purposes," CEC's Guarantee of the Notes constitutes a "security" as defined by the plain language of the Securities Act. *See Reves v. Ernst & Young*, 494 U.S. 56, 61-62 (1990); *see also United Hous. Found. v. Forman*, 421 U.S. 837, 847-48 (1975).

None of CEC's cases say that a guarantee cannot be a "security" in the context of a TIA claim. CEC Opp'n Br. at 18-19; Mem. of Law of Caesars Entm't Corp. in Supp. of its Mot. for Summ. J. [*Trilogy* ECF No. 138; *Danner* ECF No. 119] ("CEC Br.") at 16-17. Instead, CEC's cases hold that plaintiffs may not prosecute securities fraud actions based on the guarantee of a

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securities" (*e.g.*, they could only be exercised as a "right[] to purchase stock" if the holder qualified for membership in the cooperative). *Great Rivers*, like other cases CEC cites in support of its argument that its Guarantee should not be considered a "security," is entirely distinguishable from the context of Plaintiffs' claims, which are based on the Guarantee of an instrument (CEOC's Notes) that is indisputably a security under the statute.

[5] Statement of Undisputed Material Facts Pursuant to Local Civil Rule 56.1 in Supp. of Pls.' Joint Mot. for Partial Summ. J. [*Trilogy* ECF No. 143; *Danner* ECF No. 124] ("Pls.' SUMF") ¶ 17.

[6] *See* Pls.' Joint Resp. to Caesars Entm't Corp.'s Local Civil Rule 56.1 Statement of Undisputed Statement of Material Facts and Counter-Statement of Material Facts [*Trilogy* ECF No. 149; *Danner* ECF No. 131], Counter-SUMF ¶ 3.

financial instrument that itself did not constitute a "security" under the Securities Act.[7] *See Coan*, 813 F. Supp. at 935-40 (dismissing plaintiff's security fraud claims after concluding that a sale/leaseback arrangement with a single investor was not a "security"); *Woods v. Homes and Structures of Pittsburgh, Kansas, Inc.*, 489 F. Supp. 1270, 1293-94 (D. Kan. 1980) (holding that guarantees of municipal bonds that were otherwise exempt from the Securities Act should not be separately treated as securities subject to registration and antifraud requirements); *Haberman v. Wash. Public Power Supply Sys.*, 744 P.2d 1032, 1047-48 (Wash. 1987) (holding that guarantees of public bonds were not separate securities for purposes of plaintiffs' fraud claims based on the federal securities laws). Although the court in *Woods* noted that the guarantee in that case was not sold separately from the underlying bonds, it also found there was "no statutory requirement or public policy reason for treating [the guarantee] differently than the exempt bond issue." 489 F. Supp. at 1294. More to the point, *Woods* found that a "guarantee can be a security" and restricted its holding to the "particular circumstances of [the] case . . . ." *Id.* at 1294. Similarly, while the court in *Haberman* noted that the subject guarantee was not sold or marketed separately from the underlying instrument, the court held that "[t]he Participants 'guaranteed' only that they would purchase their share of [the project capability of two nuclear power plants whose construction was financed through the sale of revenue bonds] whether or not power was

[7] CEC is wrong when it states that the courts in these cases "all . . . reviewed the substantive nature of the guarantee [at issue in the case] and determined it was not a separate security, irrespective of the nature of the underlying obligation." CEC Opp'n Br. at 18. In *Coan*, for example, the court made clear that it evaluated the transaction as a whole (and did not independently consider the nature of the guarantee in isolation) in reaching its conclusion that "the sale/leaseback arrangement ha[d] no 'securities' implications." *Coan v. Bell Atl. Sys. Leasing Int'l, Inc.*, 813 F. Supp. 929, 940 (D. Conn. 1990); *see also id.* at 935 ("Other courts . . . do not view the guaranty in isolation but rather survey 'the entire transaction, including the guarantee,' to see whether it 'falls within the statutory definition of a security.' . . . As [plaintiff's] complaint seeks to attack the transaction as a package, it is appropriate for this Court to analyze the entire sale/leaseback arrangement in this context.") (citation omitted) (emphasis added).

produced. This obligation was an indirect guaranty of the bonds . . . [t]he Participants did not guarantee payment on the bonds directly." 744 P.2d at 1047-48 (emphasis added). These cases—all decades old and from outside of this jurisdiction—provide no support for CEC. In contrast, in *Banco de La Republica de Colombia v. Bank of New York Mellon*, No. 10 Civ. 536(AKH), 2013 WL 3871419, at *6 (S.D.N.Y. July 26, 2013), Judge Hellerstein found that a guarantor constitutes an "issuer" because a guarantee can be a "security" under the Securities Act.

Finally, neither the *Marblegate* decision nor Judge Scheindlin's rulings here and in *BOKF* support CEC's argument. *See* CEC Opp'n Br. at 19-20. None of the parties in *Marblegate* raised the issue of whether a guarantee can constitute an "indenture security" under the TIA, so the Court had no reason to consider that issue when discussing whether the removal of a guarantee by majority vote would violate Section 316(b). *See Marblegate Asset Mgmt. v. Educ. Mgmt. Corp.*, 75 F. Supp. 3d 592, 603, 610 (S.D.N.Y. 2014).[8] Likewise, this Court has never considered whether a Guarantee constitutes an indenture security, in this case or the related *BOKF* action.[9] For all of the above reasons, this Court should find that the Guarantee constitutes an indenture security for the purposes of TIA Section 316(b).

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[8] Although the defendants in *Marblegate* noted that "as a matter of 'belt and suspenders' the [p]arent [g]uarantee would also be released by a majority vote of the [n]oteholders pursuant to [the] indenture . . .," *id.* at 601 n.6, plaintiffs challenged the release of the guarantee pursuant to terms already included in the indenture, and this was the focus of the court's analysis. *See id.* at 601 ("In the Intercompany Sale, a number of steps would occur with near simultaneity: (i) the secured lenders would release [defendant's] parent guarantee of their loans . . . thus triggering the release of [defendant's] parent guarantee of the [n]otes . . . ."), 603 ("Pressed at oral argument, [p]laintiffs identified [d]efendants' active participation in the Intercompany Sale—nominally a process of the secured creditors exercising their rights to foreclose against [d]efendants—as the element of the Intercompany Sale that would offend [the TIA].").

[9] *See* CEC Br. at 15 (acknowledging the Court did not previously decide this issue in this action); *see generally MeehanCombs Global Credit Opportunities Mater Fund, LP v. Caesars Entm't Corp.*, Nos. 14-cv-7091(SAS), 14-cv-7973(SAS), 2015 WL 9478240, at *5-7 (S.D.N.Y.

B. The Guarantee is a "Core Term" of the Indenture for Purposes of TIA Section 316(b)

CEC says it is unaware of any court having "deem[ed] a guarantee a 'core term' of a debt instrument under the TIA such that the guarantee cannot be amended or removed without unanimous noteholder consent." CEC Opp'n Br. at 22. What CEC fails to mention is that no court has ever held a guarantee not to be a core term.[10] Rather, courts in this district have held that an indenture provision is a "core term" under the TIA when it "affect[s] a securityholder's right to receive payment of the principal of or interest on the indenture security on the due dates of such payments . . . ." *UPIC & Co. v. Kinder-Care Learning Ctrs., Inc.*, 793 F. Supp. 448, 452 (S.D.N.Y. 1992).[11] CEC does not dispute that the removal of its Guarantee "affected" Plaintiffs' ability to receive payment of principal and interest when those amounts became due (*i.e.*, when CEOC filed for bankruptcy) and impaired Plaintiffs' ability to institute suit against CEC as guarantor. *See generally* CEC Opp'n Br. at 22-25. This should be the end of the analysis.

Neither *Federated* nor *Marblegate* help CEC on its core term argument. In *Federated*, Judge Baer specifically cited the removal of a guarantee in finding that the proposed exchange offer violated the TIA. *Federated Strategic Income Fund v. Mechala Grp. Jamaica Ltd.*, No. 99

Dec. 29, 2015); *BOKF, N.A. v. Caesars Entm't Corp.*, Nos. 15-cv-1561 (SAS), 15-cv-4634 (SAS), 2015 WL 5076785, at *8-10 (S.D.N.Y. Aug. 27, 2015).

[10] CEC's arguments regarding the opinions of "bond market experts" and market practice are without merit. CEC Opp'n Br. at 22. Where the language of the Indenture is clear and unambiguous, the court need not look to evidence of market practices. *See BOKF*, 2015 WL 5076785 at *8. The several law journal articles CEC cites state only that TIA Section 316(b) protects the right to interest, principal, and maturity. *See* CEC Br. at 11, 14; CEC Opp'n Br. at 22. None of the articles address whether a guarantee is a core term and, as such, they offer no support for CEC's position.

[11] CEC again misrepresents the relevant case law when it argues that courts have "consistently limited 'core terms' of bond indentures to the principal owed to the noteholder, the calculation of interest to be paid, and the dates on which payments are due." CEC Opp'n Br. at 22 (citing CEC Br. at 11-12). None of the decisions cited by CEC adopt this narrow interpretation of "core term." *See* Plaintiffs' Mem. of Law in Opp'n to Caesars Entm't Corp.'s Mot. for Summ. J. [*Trilogy* ECF No. 151; *Danner* ECF No. 130] ("Pls.' Opp'n Br."), at 10-11.

CIV 10517 HB, 1999 WL 993648, at *7 (S.D.N.Y. Nov. 2, 1999). Although CEC suggests otherwise, the fact that the *Federated* court also noted that the transaction at issue would have effected a "simultaneous disposition of all meaningful assets," *id.*, does not mean that the court held that the guarantee was not a core term in and of itself, or that stripping the guarantee would not constitute a violation of the TIA.[12] Similarly, in *Marblegate*, Judge Failla found the TIA to have been violated based in significant part on the fact that, after the release of the parent guarantee, the plaintiffs would have no recourse against any company capable of paying a judgment. *See Marblegate*, 75 F. Supp. 3d at 616-17. Although CEC cites a passage of *Marblegate* discussing the possible removal of a parent guarantee from an indenture, *see* CEC Opp'n Br. at 23, that portion of the decision is mere dicta. *See Marblegate*, 75 F. Supp. 3d at 615. And again, *Marblegate* found that a guarantee release could violate the TIA—directly contradicting CEC's argument that a guarantee cannot be a "core term." *See id.* at 616-17.[13]

CEC also cannot avoid summary judgment based on supposed "issues of fact" regarding whether the Guarantee was an investment consideration for noteholders. *See* CEC Opp'n Br. at 24-25. Irrespective of what the Prospectus stated regarding the possible release of the Guarantee, it said nothing about CEC's wholesale removal of Plaintiffs' Guarantee rights regardless of whether the Guarantee release provisions had been satisfied. As for the Gadsden declaration, the

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[12] And besides, CEC did strip assets from CEOC, and the August Transaction purported to amend the Indenture to make asset-stripping easier. Pls.' SUMF ¶¶ 60, 80.

[13] CEC is also wrong that the Court's prior decisions in this action and *BOKF* do not support treatment of the Guarantee as a "core term." *See* CEC Opp'n Br. at 23-24. The impact of CEC's removal of the Guarantee from the Indenture is what drove the Court's opinion denying CEC's prior motion to dismiss. *MeehanCombs Global Credit Opportunities Funds, LP v. Caesars Entm't Corp.*, 80 F. Supp. 3d 507, 516 (S.D.N.Y. 2015). And, in *BOKF*, the Court found that the Guarantee "unambiguously" provided credit support for noteholders. *BOKF*, 2015 WL 5076785, at *7-8. Although the Court found in *BOKF* that the release of the guarantee in accordance with the terms of the indenture did not automatically violate plaintiffs' rights under the TIA, that holding does not apply to CEC's wholesale removal of holders' Guarantee rights from the Indenture without Plaintiffs' consent. *Id.* at *8-10.

Court has already found that the Guarantee unequivocally provides credit support to the noteholders based on the unambiguous language of the Indenture.[14] *BOKF*, 2015 WL 5076785 at *8 ("[T]here are no specialized terms used in the [g]uarantee provision that would necessitate looking to extrinsic evidence of custom and usage . . . CEC appears to argue that, while the language of the [i]ndenture unambiguously spells out a guarantee of credit support, the parties all understood that the [g]uarantee was essentially meaningless. This is exactly the type of extrinsic evidence of subjective intent that is inadmissible under New York law . . . ."). As such, CEC has no basis for the introduction of expert testimony, and the Gadsden declaration should be disregarded.

C. The Guarantee is a "Security" Under the Indenture

Lastly, CEC's argument that the Guarantee is not a "Security" under the Indenture, such that the August Transaction did not violate Sections 508 or 902 of the Indenture,[15] fails under the plain language of the Indenture.[16] CEC Opp'n Br. at 21.[17] CEC offers no explanation for why

[14] Plaintiffs are not required, as CEC suggests, to "present . . . evidence that they purchased their notes in reliance on the Guarantee." CEC Opp'n Br. at 25. Neither the TIA nor the relevant cases require reliance as an element of Plaintiffs' claims. The relevant analysis here (if the Court even engages in an analysis of whether the Guarantee is a "core term," *see supra* Argument, § I.A) is whether the Guarantee was a core term when the Indenture was entered into and the Notes were issued. *See, e.g.*, *Federated*, 1999 WL 993648 at *7 (describing guarantee as a "safety net" that "was obviously an investment consideration from the outset.").

[15] Section 508 of the Indenture expressly prohibits CEC from "impair[ing] or affect[ing]" Plaintiffs' rights to principal and interest on any "Security," or to institute suit for the enforcement of such payment, without their consent. Pls.' SUMF ¶ 24. Section 902 of the Indenture bars CEC from amending the Indenture to remove Plaintiffs' rights to principal and interest on any "Security" without Plaintiffs' consent. *Id.* ¶ 29.

[16] The Indenture defines the term "Securities" in two places. In the Recitals section, the Indenture states that CEOC and CEC "have duly authorized the execution and delivery of this Indenture to provide for the issuance from time to time of unsecured debentures, notes or other evidences of indebtedness (together with the related guarantees provided by the Guarantor, the "Securities"), to be issued in one or more series as provided for in this Indenture." *Id.* ¶ 15 (emphasis added). Similarly, in Section 101, the Indenture states that "'Securities' has the

the Recitals in the Indenture include the word "Guarantee" in the definition of "Security"—if not to make clear that the Guarantee is a "Security." Moreover, the Court can read the Indenture to define the Guarantee as a "Security" while still giving effect to Sections 902 and 1503, as Plaintiffs' claims are not premised on a release of the Guarantee pursuant to a release provision (Section 1503) that existed when the Notes were issued, but rather on CEC's wholesale removal of the Guarantee from the Indenture without Plaintiffs' consent, in violation of Sections 508 and 902.[18]

D. CEC Has Not Satisfied Its Burden on Its Affirmative Defense that the May Transactions Released the Guarantee

Although CEC suggests otherwise, the parties' dispute on the "wholly owned subsidiary" issue turns not on disputed questions of fact, but rather on the applicable legal standard. CEC disputes the plain meaning of Regulation S-X, and also urges the Court to ignore applicable SEC guidance. CEC's arguments are without merit, for the reasons set forth below.

1. The Undisputed Facts Show that CEC Holds "Substantially All" of CEOC's Voting Shares

Under Regulation S-X, CEOC is a "wholly owned subsidiary" of CEC so long as CEC holds "substantially all" of CEOC's voting shares. 17 C.F.R. § 210.1-02(aa). CEC incorrectly argues that "the meaning of 'substantially all' is not clearly ascertainable . . . ." CEC Opp'n Br. at 12. But courts routinely interpret the meaning of federal regulations, and the parties' decision

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meaning stated in the first recital of this Indenture and more particularly means any Securities authenticated and delivered under this Indenture." *Id.* ¶ 16 (emphasis added).

[17] CEC's argument based on the Recitals' use of the phrase "together with" is without merit. The decisions CEC cites on this point (*see* CEC Br. at 22), *Gibson v. City of Kirkland*, 433 F. App'x 539, 541 (9th Cir. 2011) and *Hinshaw v. M-C-M Props., LLC*, 450 S.W.3d 823, 827 (Mo. Ct. App. 2014), do not address contractual definitions at all, and hold only that the use of "together with" shows that the connected terms are related rather than independent. Because there is no dispute that the Guarantee is "related" to the Notes, these cases are inapposite.

[18] CEC acknowledges that "Section 902's authorization to amend the Indenture expressly carves out the very same rights protected by Section 508." CEC Br. at 21.

to incorporate Regulation S-X into the Indenture means the Court can and should apply the "substantially all" standard to the undisputed facts. *See, e.g., TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 448-49 (1976).

CEC does not dispute that "substantially" has been defined to mean "to a great or significant extent" or "for the most part; essentially."[19] *See* CEC Opp'n Br. at 10. Nor can CEC dispute that, owning 89% of CEOC's stock, CEC "to a great or significant extent" or "for the most part" holds all the voting shares of CEOC—*i.e.*, not just "most." CEC tries to get around these facts by asking the Court to adopt a narrower definition of "substantially all"—*e.g.*, "essentially or really the same" or "without material qualification." *Id.* But CEC offers no principled basis for why the Court should adopt the narrowest possible meaning of the term. Other available dictionary definitions show that CEC's suggested interpretation ("essentially or really the same") is unduly restrictive when compared with the range of meanings normally associated with "substantially all."[20]

In tax matters, the federal courts have found that "substantially all" means 85% or more. *See Cont'l Can Co., Inc. v. Chicago Truck Drivers, Helpers & Warehouse Workers Unions Pension Fund*, 916 F.2d 1154, 1158 (7th Cir. 1990) ("'Substantially all' is one of those phrases with a special legal meaning. Congress uses it all time in tax statutes, and the Internal Revenue Service decodes it as meaning 85%."). Here, where the SEC declined to adopt a specific numeric threshold in defining "wholly owned subsidiary," CEC has no basis to argue that "substantially all" necessarily means more than 89%, or otherwise fails to meet a "high

[19] *See* Oxford Dictionary, *available online* http://www.oxforddictionaries.com/us/definition/american_english/substantially.

[20] *See, e.g.*, Webster's New World Dictionary of the American Language, *available online* https://archive.org/stream/webstersnewworld001775mbp#page/n1493/mode/2up ("1. in a substantial manner; solidly; firmly; with strength; 2. to a substantial degree; specifically, a) truly; really; actually, b) largely; essentially; in the main").

threshold" standard. *Cf.* 15 U.S.C. § 80a-2(43) (the Investment Company Act of 1940) (defining "[w]holly-owned subsidiary" to mean "a company 95 per centum or more of the outstanding voting securities of which are owned by" the parent and its other wholly owned subsidiaries); 17 C.F.R. § 210.3-10(h)(1) (defining "100% owned" to describe situations where the parent owns, directly or indirectly, "*all* of [the subsidiary's] outstanding voting shares . . . .") (emphasis added). CEC fails to address any of the above authorities in its opposition papers.

Although CEC argues otherwise, *see* CEC Opp'n Br. at 12-13, the best guidance available to the Court concerning the meaning of "substantially all" is found in publications from the FASB and SEC Staff regarding push down accounting. As conceded by CEC's expert at deposition, the push down accounting guidance is the only guidance issued on Regulation S-X's definition of "wholly owned subsidiary." Suppl. Pierce Decl., Ex. CC, 93:2-25; Suppl. Novod Decl., Ex. CC, 93:2-25. Moreover, the fact that the SEC recently adopted another standard for push down accounting is irrelevant. Regardless of what the rule may be today, the SEC's prior guidance was undisputedly based on the same definition of "wholly owned subsidiary" that the parties incorporated into the Indenture. And, that guidance undisputedly was in place at the time the Indenture was signed. *See* SAB No. 54; EITF D-97.

The SEC Staff and FASB have stated that a subsidiary is "wholly owned" when the parent's holdings in the subsidiary are sufficient for the parent to "control the form of ownership" of the subsidiary and its assets.[21] Here, the undisputed facts show that CEC at all relevant times exercised complete and unchecked control over CEOC and its assets. Although

[21] *See* SAB No. 54; EITF D-97. Based on this standard, the SEC Staff has advised that companies may use push down accounting when they own at least 80% of the subsidiary, but not when the ownership level is below 80%. In advocating for a 95% threshold, CEC's expert ignores this fact, as well as the SEC's decision not to include a fixed numeric ownership threshold in its definition of "substantially all."

CEC touts its appointment of new directors to the CEOC board and new executives to CEOC's management following the May Transactions, those facts are irrelevant.[22] This is because the key distinction under Regulation S-X between a subsidiary that is "wholly owned" and one that is not is whether there is a "significant minority interest" that "impairs the parent's ability to control the form of ownership." SAB No. 54. No part of the push down accounting guidance states that appointment of independent directors is relevant for the "wholly owned subsidiary" analysis. Here, CEC concedes that all of the new appointments to CEOC's board and management (including CEOC's "independent" directors) were made by CEC and its equity sponsor Apollo—not CEOC's minority shareholders. Pls.' SUMF ¶ 217, 220. [redacted] *Id.* ¶¶ 220-26. CEC ensured this by: (i) amending CEOC's Certificate of Incorporation immediately prior to the May Transactions to give CEC the exclusive and unilateral right to take any and all actions it wished via written consent, without a shareholder vote, and without any advance notice to CEOC's minority shareholders; and (ii) excluding from the 5% Stock Sale and the PIP any grant of rights —*e.g.*, the right to call a special meeting of shareholders, the right to elect directors, and veto and/or approval rights over extraordinary actions—that would have diminished CEC's control over CEOC. *Id.* ¶¶ 219, 220-26.

[22] Although CEC contends that its appointment of a new CEO, CFO, and General Counsel to CEOC following the May Transactions is an additional reason why CEOC should not be considered a wholly owned subsidiary, CEC has offered no evidence that those officers (all of whom were chosen by Apollo) did anything other than take direction from CEC, Apollo and TPG. Notably, the terms of the August Transaction were negotiated entirely by David Sambur, without the involvement of any officer from CEOC. Suppl. Pierce Decl., Ex. AA, 90:16-91:14, Ex. BB, 321:15-322:7; Suppl. Novod Decl., Ex. AA, 90:16-91:14, Ex. BB, 321:15-322:7. Much of those negotiations took place before CEOC's new officers had even been hired, and before CEOC had independent counsel. Suppl. Pierce Decl., Ex. BB, 315:12-317:9; Suppl. Novod Decl., Ex. BB, 315:12-317:9.

CEC's argument that CEOC is not a "wholly owned subsidiary" because of CEOC's outstanding debt is also without merit. *See* CEC Opp'n Br. at 14. Although certain of CEOC's indentures included restrictions on its ability to issue preferred stock, engage in merger transactions, and engage in transactions with its affiliates, those restrictions (which neither CEC nor its expert explains) were immaterial. For example, CEOC could engage in transactions with its affiliates so long as the terms of the deal were "not materially less advantageous" than CEOC could negotiate with an unaffiliated party. *See* Suppl. Pierce Decl., Ex. Z § 4.07; Suppl. Novod Decl., Ex. Z § 4.07. Similarly, CEOC could issue stock and merge assets so long as its operating income was sufficiently in excess of its monthly charge for interest and preferred equity dividends. Suppl. Pierce Decl., Ex. Z § 4.03; Suppl. Novod Decl., Ex. Z § 4.03. CEC admits that it orchestrated literally dozens of capital market transactions for CEOC prior to its bankruptcy, including numerous sales of valuable property to CEC affiliates, and the issuance of multiple rounds of new indebtedness (which were subject to the same restrictions as the issuance of new preferred stock). Suppl. Pierce Decl., Ex. BB, 58:12-61:10; Suppl. Novod Decl., Ex. BB, 58:12-61:10. Nor does CEC contend that it lacked control over when and with whom to engage in these transactions. On these facts, CEC cannot reasonably argue that CEOC's debt covenants impaired CEC's ability to "control the form of ownership" of CEOC.[23]

2. The Undisputed Facts Show that Shares Held by CEOC's Minority Stockholders Should be Aggregated with Those Held by CEC

The SEC has advised that different shareholders' interests should be aggregated when determining whether a subsidiary is wholly owned under Regulation S-X where, in the context of

[23] CEC's reliance on cases finding that the determination of whether a corporation has conveyed "substantially all" of its assets are inapposite. *See* CEC Opp'n Br. at 11-12. Unlike corporate assets, all shares of CEOC stock are identical to one another. Thus, there is no need for any analysis of whether the assets retained by the seller are material to the company's business—the core issue in whether an asset purchase sale involves "substantially all" of a business's assets.

an acquisition, those shareholders act as a collaborative group. *See* EITF D-97 at 2. The concerns underlying the SEC's guidance warrant aggregation here based on the undisputed facts. CEC admits that, in the 5% Stock Sale, [redacted] Pls.' SUMF ¶ 90, 106-13. Similarly, in the PIP, CEC gifted CEOC shares to Caesars executives and employees, all of whom are by definition beholden to CEC and its financial success, and none of whom "invested" anything in the shares they held. *Id.* ¶ 131. [redacted] *Id.* ¶¶ 139-40, 142. [redacted] *Id.* ¶¶ 153-56.

In arguing against aggregation, CEC relies almost entirely on the proposed rebuttal expert testimony of Dr. Jerry L. Arnold.[24] Dr. Arnold's core contentions— that the SEC's guidance regarding collaborative groups is irrelevant, and that the guidance raises fact questions that cannot be resolved on summary judgment—are without merit. Although Dr. Arnold is correct that the SEC's guidance on collaborative groups was geared towards acquisitions, not divestitures, that fact does not matter. In both scenarios, different shareholders may effectively function as one in the control of a subsidiary, and the factors laid out by the SEC Staff are on

[24] *See* CEC Opp'n Br. at 16-17. CEC's reliance on Dr. Arnold's testimony is improper. CEC designated Dr. Arnold as an expert for the sole purpose of rebutting Plaintiffs' Regulation S-X rebuttal experts, Roberta Karmel (a former SEC commissioner) and Michael W. Phillips (an accounting expert at Floyd Advisory LLC). Because Plaintiffs do not rely on their Regulation S-X experts on this motion, there is no testimony for Dr. Arnold to rebut on summary judgment. *See NIC Holding Corp. v. Lukoil Pan Ams.*, No. 05-CV-09372(MEA), 2009 WL 996408, at *4 (S.D.N.Y. Apr. 14, 2009) (excluding rebuttal witness's testimony where affirmative expert testimony was not offered).

their face relevant to determining when such coordination may be presumed. By way of example, the SEC Staff has advised that investors may be presumed to be "independent" where "the investor is independent of and unaffiliated with all other investors," and where "the investor does not have other relationships with any other investor that are material to either investor." *See* EITF D-97 at 3. Here, CEC does not dispute that [redacted].[25] [redacted] Pls.' SUMF ¶ 135. On these facts, CEC's argument that the minority shareholders may be deemed "independent" of CEC (because of the size of their respective asset portfolios, or the possibility that they did not "know" one another) is disingenuous.

Regarding risks of ownership, there is no dispute that the PIP participants invested none of their personal funds in CEOC stock. The stock was given to them, along with extra funds to compensate them for any resulting tax liability. *Id.* ¶¶ 131, 153. CEC's argument that the employees may nonetheless be deemed to have incurred economic "risk" (CEC Opp'n Br. at 16)—[redacted]—is not credible.

The other factors lead to the same result. CEC admits that [redacted] *Id.* ¶¶ 91, 127. This clearly runs contrary to the SEC's guidance on Promotion (*i.e.*, that investors may be deemed not to have "promoted" the sale of

[25] Pls.' SUMF ¶¶ 106-13. [redacted] *Id.*

shares to other investors so long as they did not "solicit" the subject investments). *See* EITF D-97 at 4. In addition, CEC admits that its amendment of CEOC's Certificate of Incorporation effectively did away with shareholder votes, thereby giving CEC the power to act unilaterally via written consent. Pls.' SUMF ¶ 215. [redacted] *Id.* ¶¶ 139-40. Because of these undisputed facts, CEC's ability to control CEOC was essentially unchecked—a state of affairs that CEOC's minority shareholders had no incentive to change.

II. PLAINTIFFS ARE ENTITLED TO SUMMARY JUDGMENT ON THEIR CLAIMS THAT THE AUGUST TRANSACTION VIOLATED SECTION 316(a) OF THE TIA AND SECTION 902 OF THE INDENTURE

CEC concedes that the Favored Noteholders' consents were ineffective when made, and that the "Proposed Consents" did not become effective until the "consummation of the Closing" of the August Transaction, at which point the subject Notes had been transferred to CEOC and CEC (and to the Trustee for cancellation) and the Supplemental Indenture had been executed. *See* CEC Opp'n Br. at 26. Given these admissions, CEC has no defense to Plaintiffs' claims that the August Transaction violated Indenture Section 902 and TIA Section 316(a). *See* Pls.' Br. at 25-28.

First, CEC did not have the required majority consent required under Section 902 of the Indenture because the Notes were not "Outstanding Securities" (as that term is defined in the Indenture) at the time the Proposed Consents became "effective." Pls.' SUMF ¶ 29 (emphasis added). The Closing Memo (which CEC cites in its opposition)[26] confirms this fact. At the point when the Proposed Consents became effective: (i) CEC and CEOC had paid the Favored Noteholders for their Notes; (ii) the Favored Noteholders submitted withdrawals so their Notes

[26] CEC Opp'n Br. at 25.

could be cancelled; and (iii) the Trustee and CEOC released their signatures to the Supplemental Indentures. *See* Supplemental Decl. of Philippe Adler in Opp'n to Pls.' Mot. for Partial Summ. J. [*Trilogy* ECF No. 155; *Danner* ECF No. 136], Ex. 67 (the "Closing Memo") § C.[27]

CEC's argument that the ineffective Proposed Consents were delivered to CEC prior to the Closing is beside the point. As discussed more fully in Plaintiffs' opposition to CEC's motion for summary judgment, the structure of the August Transaction was inconsistent with standard industry practice because, among other reasons, at the point when the Supplemental Indenture was deemed executed, the Notes had been transferred to CEC and CEOC. *See* Pls.' Opp'n Br. at 26-27 (citing Nicholas P. Saggese, Gregg A. Noel, Michael E. Mohr, *A Practitioner's Guide To Exchange Offers And Consent Solicitations*, 24 Loy. L.A. L. Rev. 527, 590 (1991)).

With respect to Section 316(a) of the TIA, CEC argues that it never "controlled" the Favored Noteholders. CEC Opp'n Br. at 26. Plaintiffs do not argue that it did. Rather, Plaintiffs contend that CEC and CEOC had both actual and beneficial ownership (as well as possession) of the Favored Noteholders' Notes at the point when the Proposed Consents became effective. *See* Pls.' Br. at 25-27.[28] Prior to the Proposed Consents becoming effective, the terms of the NPSA barred the Favored Noteholders from selling the Notes (or the Notes' voting rights) and the Noteholders were obliged to take all commercially reasonable steps to effectuate the proposed amendments to the Indenture. *See* Pierce Decl., Ex. D § 5.1. CEC's argument that the SEC's guidance for determining when a security is beneficially owned is "irrelevant" for purposes of

[27] Indeed, step transactions are integrated transactions that occur simultaneously. *See, e.g.*, *Orr v. Kinderhill Corp.*, 991 F.2d 31, 36 (2d Cir. 1993).

[28] There is no dispute that, without the consents from the Favored Noteholders, CEC lacked the majority necessary for the amendment of the Indenture. Pls.' SUMF ¶¶ 29, 46, 52.

determining whether CEC had beneficial ownership of the Notes (*i.e.*, securities), *see* CEC Opp'n Br. at 27, makes no sense and should be disregarded. *See* 17 C.F.R. § 240.13d-3(a).

III. PLAINTIFFS ARE ENTITLED TO SUMMARY JUDGMENT ON THEIR CLAIMS THAT CEC BREACHED ITS DUTY OF GOOD FAITH AND FAIR DEALING

CEC concedes in its opposition that Plaintiffs may prosecute their good faith and fair dealing claims when the claims are: (i) "not redundant of, or in tension with, any terms in the indenture," and (ii) "so interwoven into the contract as to be necessary for effectuation of the purposes of the contract." CEC Opp'n Br. at 28 (internal quotation marks and citations omitted). Plaintiffs satisfy both elements of that test based on the undisputed facts.

As detailed in Plaintiffs' opposition to CEC's motion for summary judgment, the factual predicates for Plaintiffs' good faith claims and their contract claims are distinct. *See* Pls.' Opp'n Br. at 27-30. Plaintiffs' good faith claims are based on CEC's failure to offer the terms of the August Transaction to all noteholders, not just the Favored Noteholders. Although the Indenture allows majority amendments in certain circumstances, it does not address situations where CEOC or CEC offer financial incentives for consents. For that reason, the claim is not "redundant" of "any terms in the indenture."

Nor is the claim inconsistent or otherwise "in tension with" the Indenture. To the contrary, Plaintiffs' claims are in accord with Indenture provisions stating that "no one or more of such Holders shall have any right . . . to obtain or to seek to obtain priority or preference over any other of such Holders . . . ," *see* Pls.' SUMF ¶ 23 (Indenture § 507), and "[i]f less than all the Securities of any series are to be redeemed . . . the particular Securities to be redeemed shall be selected . . . by such method as the Trustee shall deem fair and appropriate . . . ," *see id.* ¶ 31 (Indenture § 1103). Because Plaintiffs' claims are consistent with the Indenture, the cases cited by CEC regarding the reluctance of courts to infer duties inconsistent with the indenture are

inapposite. *See Hartford Fire Ins. Co. v. Federated Dep't Stores, Inc.*, 723 F. Supp. 976, 992 (S.D.N.Y. 1989) (dismissing good faith claim that "contravene[d]" express contractual provisions); *In re Solutia, Inc.*, No. 03-17949, 2007 WL 1302609, at *10-13 (Bankr. S.D.N.Y. May 1, 2007) (refusing to imply terms where the debtor had the right under the indenture to structure its financing to avoid triggering the indenture's Equal and Ratable Clause).

CEC attempts to distinguish *Whitebox, Kass*, and *Katz* by claiming that none of these cases recognize an obligation for exit consents to be offered to all noteholders. *See* CEC Opp'n Br. at 30. This is wishful thinking on CEC's part. *Whitebox* involved a transaction substantially identical to the August Transaction (with a nearly identical equal treatment covenant) that the court characterized as a "partial redemption." *Whitebox Convertible Arbitrage Partners, L.P. v. World Airways, Inc.*, No. Civ.A. 1:04-cv-1350, 2006 WL 358270, at *3 (N.D. Ga. Feb. 15, 2006). The court stated, "[i]t appears that World Airways provided a special incentive to certain bondholders in an effort to obtain their approval of a bond exchange while not making the same offer to other bondholders . . . . It is such manipulation that section 1104 and the principles of good faith and fair dealing are designed to avoid." *Id.* (emphasis added). Likewise, although *Kass* and *Katz* ultimately rejected the plaintiffs' good faith and fair dealing claims based on the specific facts of those cases, the courts nevertheless recognized that in a situation such as the one here—*i.e.*, where a defendant had not made its offer to all bondholders on the same terms but had privately paid for the consent of only some of the bondholders—the duty of good faith and fair dealing would be breached. *See Kass v. E. Air Lines*, 1986 WL 13008, *5 (Del. Ch. Nov. 14, 1986); *Katz v. Oak Indus. Inc.*, 508 A.2d 873, 881 (Del. Ch. 1986).

CONCLUSION

For all of the reasons set forth above and in Plaintiffs' original moving papers and papers in opposition to CEC's motion for summary judgment, the Court should grant summary judgment against CEC on Counts One, Two, Three, Four, Eight, and Nine of the Trilogy Plaintiffs' Amended Complaint, and Counts One, Two, Three, and Six of the Danner Amended Complaint.

Dated: New York, New York
June 14, 2016

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CONCLUSION

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