

Court Looks to Obscure Law: Trust Indenture Act of 1939

By Erika K. Solanki, J.D. Candidate 2017 | January 24, 2015

When some bondholders purchased debt in casinos operated by [Caesars Entertainment](#), they felt comfort in the guarantees of the parent company that it would stand behind the debt payments, even if something were to go awry. When Caesars found itself in financial distress, the company abruptly eliminated its guarantees, leaving bondholders to turn to an obscure Depression-era law: the Trust Indenture Act of 1939 (The Act). The Act was originally devised to protect bondholders from abusive tactics, such as back-room deals that stripped bondholders of their rights.

On December 30, 2014, the U.S. District Court for the Southern District of New York issued an opinion in *Marblegate Asset Management v. Education Management Corp.*, interpreting broadly the protections granted to bondholders under the Trust Indenture Act of 1939. *Marblegate Asset Management v. Education Management Corp.*, No. 14 CIV. 8584 KPF, 2014 WL 7399041 (S.D.N.Y. Dec. 30, 2014). A substantial portion of the opinion analyzes Section 316(b) of the Act: “The questions presented on the merits essentially boil down to a dispute over the scope of the protections afforded by the Trust Indenture Act: Is it a broad protection against nonconsensual debt restructurings, or a narrow protection against majority amendment of certain ‘core terms’? ... the Court finds the former interpretation more persuasive.” *Id.* at *15. The Court turned to legislative history and confirmed the Act was intended to prohibit companies from restructuring debt out-of-court as a means to eliminate certain material rights of non-consenting bondholders. See Latham & Watkins Client Alert Commentary: [A New Tool for Holdout Bondholders: The Trust Indenture Act](#).

Companies in trouble usually ask their debt holders to restructure the terms of the obligations they hold. Reducing the interest rate on the debt or retiring its full value can assist financially distressed companies return to good health. Naturally, while debt holders often object to such changes, many companies ultimately win these battles in favor of the changes as bondholders want to avoid a bankruptcy filing, a definitively worse outcome. After the release of this opinion, however, [other disgruntled bondholders have quickly followed suit](#), championing the Act for their own legal protection. Now that the Trust Indenture Act is gaining traction, it will be interesting to follow the ensuing litigation.