CLIENT UPDATE

BANKRUPTCY COURT AUTHORIZES AMERICAN AIRLINES TO REPAY $1.3 BILLION DEBT WITHOUT MAKE-WHOLE

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On January 17, 2013, in a lengthy and closely reasoned opinion,[1] Judge Sean Lane of the Bankruptcy Court for the Southern District of New York authorized American Airlines, Inc. ("American") to repay $1.3 billion in debt without payment of a make-whole premium over the objection of U.S. Bank Trust National Association as trustee.[2] Judge Lane's decision is a useful reminder that the parties to a financing must carefully draft their agreements to clearly express their intentions with respect to whether a make-whole premium is payable upon the repayment of accelerated debt.

BACKGROUND

On November 29, 2011, AMR Corp. and a number of its subsidiaries, including American, filed voluntary petitions for relief under chapter 11 of the Bankruptcy Code. At the time of the filing, American was party to three separate financing transactions, each of which is secured by a different pool of aircraft.

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1 *In re AMR Corp., et al*, No. 11-15463 (American Airlines) (SHL) (Bankr. S.D.N.Y. Jan. 17, 2013) (ECF No. 6265). A copy of the decision can be found at http://www.debevoise.com/publications/pdf/case_no_11_15463.pdf.

2 Debevoise & Plimpton LLP is counsel to American Airlines, Inc. in this matter.

On October 9, 2012, American filed a motion seeking court approval to repay these financings and to obtain new secured financing in an amount of up to $1.5 billion. American sought permission to repay the existing financings without any make-whole premium. A make-whole premium, sometimes referred to as a yield maintenance premium, is a fee intended to compensate lenders for any damages resulting from payment of a loan prior to its stated maturity. Damages are often estimated by comparing the rate of interest payable on the loan to a reference rate, such as a treasury rate, at which the proceeds of the repayment are hypothetically reinvested.

In seeking authorization to repay the existing financings without any make-whole premium, American relied on the language of the indentures governing the existing financings, which provided for the automatic acceleration of the debt upon a bankruptcy filing and stated that in the event of acceleration, automatic or otherwise, "the unpaid principal of the [Notes] then outstanding, together with accrued but unpaid interest thereon and all other amounts due thereunder (but for the avoidance of doubt, without Make-Whole Amount)" would become immediately due and owing. The indentures also provided that "[n]o Make-Whole Amount shall be payable on the [Notes] as a consequence of or in connection with any Event of Default or the acceleration of the [Notes]."

U.S. Bank opposed American's motion on a variety of grounds. However, the principal argument advanced by U.S. Bank was that the indentures' voluntary redemption provisions, which contemplate the payment of a make-whole premium, governed the repayment.

MAKE-WHOLES ARE MATTERS OF CONTRACT, NOT POLICY

As Judge Lane noted, "There is no dispute that make whole amounts are permissible. The entitlement to such payments, however, is a matter of contract, not policy."[3] The Court ruled in favor of American, finding that the indentures provided for the automatic acceleration of the debt upon a bankruptcy filing, in which case the indentures were clear that no make-whole premium was due. The Court explained, "If the parties wished for the Make-Whole Amount to be due in these circumstances, they could have bargained for such a provision. Instead, the parties bargained for the exact opposite result, with the Indentures stating clearly, explicitly and unambiguously that the Make-Whole Amount is not due in the event of payment following acceleration."[4]

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3 *In re AMR Corp., et al*, at 33.

4 *Id.* at 34.

The Court further found the indentures' voluntary redemption provisions inapplicable because the automatic acceleration of the debt resulting from American's chapter 11 filing moved the maturity date forward and thus American's repayment of the debt is "'a post-maturity debt repayment'" governed by the acceleration provisions rather than a prepayment governed by the voluntary redemption provisions.[5]

SOUTHERN DISTRICT PRECEDENT

Judge Lane's decision is in line with prior precedent in the Southern District of New York which holds that where the parties intend that the lenders should receive damages in the event of repayment following acceleration they must explicitly so provide in their agreements.

In *In re Solutia Inc.*,[6] the Bankruptcy Court for the Southern District of New York refused to grant expectation damages to holders of notes that were repaid in violation of a "no call" provision after being automatically accelerated upon the filing of a chapter 11 petition. The notes in that case did not provide for payment of any make-whole amount in connection with acceleration and the Court declined to "read[ ] into agreements between sophisticated parties provisions that are not there."[7] In *HSBC Bank USA, N.A. v. Calpine Corp. (Calpine II),*[8] the District Court for the Southern District of New York reached a similar conclusion, stating that while the notes were silent on the issue, they could "have provided for the payment of premiums in the event of payment pursuant to acceleration."[9]

IMPLICATIONS

Judge Lane's decision in *American Airlines* makes clear that if parties to a financing wish to provide for the payment of a make-whole premium upon the repayment of accelerated debt, they should ensure that their agreements are drafted to explicitly and unambiguously provide for it.

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Please do not hesitate to contact us with any questions.

January 29, 2013

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5 *Id.* at 26 (citation omitted).

6 379 B.R. 473 (Bankr. S.D.N.Y. 2007).

7 *Id.* at 485 n.7.

8 No. 07-3088 (GBD), 2010 U.S. Dist. LEXIS 96792, 2010 WL 3835200 (S.D.N.Y. Sept. 15, 2010).

9 *Id.* at *4.