

CLIENT UPDATE

CHESAPEAKE MOVES FORWARD WITH \$1.3B PAR NOTE REDEMPTION AFTER LOSING PRELIMINARY INJUNCTION HEARING

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Last Thursday, Chesapeake Energy Corporation (“Chesapeake”) failed to win a preliminary injunction permitting it to redeem \$1.3 billion in notes without paying a make-whole premium. One week ago, Chesapeake sued the note trustee, the Bank of New York Mellon Trust Company, N.A. (“BNY”), in the Southern District of New York seeking declaratory judgment to permit Chesapeake to redeem \$1.3 billion in notes at par. Alternatively, Chesapeake asked the court to rule that the notice of redemption would not be construed as a notice requiring redemption at the make-whole price if the court later determines that the notice was ineffective to initiate a redemption at par. The court denied the preliminary injunction on both grounds, but, in a detailed opinion from the bench, indicated its “overwhelming” belief that Chesapeake should be able to give an effective notice of redemption at par and not be bound to redeem at make-whole if it lost on the first question.

The indenture governing the notes provides Chesapeake the ability to redeem the notes at par, plus accrued and unpaid interest to the redemption date, during a “Special Early Redemption Period” that runs from November 15, 2012 to March 15, 2013. The parties’ dispute centered on whether March 15 is the final date on which the redemption must be completed, or whether the redemption at par may be completed after March 15 as long as the formal notice of early redemption is provided on or prior to March 15. BNY and certain noteholders contended that Chesapeake missed its opportunity to redeem the notes at par because of a separate provision in the indenture that requires Chesapeake to provide irrevocable notice to the noteholders at least 30 days prior to the proposed redemption date.

Certain language supports Chesapeake's position that the redemption would be timely as long as notice is given by March 15; the agreement purports to allow Chesapeake to redeem the notes "so long as it gives the notice of redemption ... during the Special Early Redemption Period." Conversely, BNY and the noteholders' position is supported by language that Chesapeake "may redeem" the notes at par only during the Special Early Redemption Period.

The disclosure to purchasers in the placement of the notes included the "so long as it gives notice" phrase, substantially identical to the provision in the supplemental indenture. Papers filed on behalf of BNY assert that a preliminary draft of the indenture supplement prepared by counsel for the issuer included the "so long as" phrase, as well as additional language clearly providing that the redemption could occur after the Special Early Redemption Period so long as the notice was given within it. That additional language was removed in the final version of the indenture supplement, possibly in order to conform the indenture provision exactly to the language in the disclosure document.

In his ruling from the bench, U.S. District Judge Paul Engelmayer determined that the relevant language in the supplemental indenture is ambiguous and that the parties "are in rough equipoise" based on their textual arguments regarding the disputed provision. It is likely that a final judgment will hinge on extrinsic evidence presented at trial. The judge also stated that it was "overwhelmingly likely" that Chesapeake would prevail on the legal merits of the question of whether an untimely notice of Special Early Redemption would require redemption at the make-whole price if Chesapeake lost on the first question. News reports today indicate that Chesapeake is moving forward with issuing its redemption notice, expressly indicating that any redemption would be at par, because the judge granted "comparable relief" to a preliminary injunction on that issue.

The case presents at least two practical lessons:

- Borrowers and their counsel must take special care to avoid ambiguities when drafting and negotiating the commercial terms of financing agreements, including redemption provisions.
- The description of material terms in note disclosure documents should be drafted and negotiated with a similar level of care as the indentures governing the notes.

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Please do not hesitate to contact us with any questions.

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