United States Bankruptcy Court
Northern District of Illinois
Eastern Division

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Bankruptcy Caption: In re Caesars Entertainment Operating Co., Inc., *et al.*

Bankruptcy No.: 15 B 1145

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UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

In re:	)	Chapter 11
	)	
CAESARS ENTERTAINMENT	)	No. 15 B 1145
OPERATING CO., INC., *et al.*,	)	(Jointly administered)
	)	
Debtors.	)	Judge Goldgar

MEMORANDUM OPINION

Before the court for ruling is a motion of the Second Priority Noteholders Committee "the Committee") to compel production of documents from Caesars Entertainment Corp. ("CEC"), Apollo Global Management, TPG Capital, and the Paul Weiss law firm under the crime-fraud exception to the attorney-client privilege. The motion will be denied.

1. Background

Early on in these cases, an examiner was appointed to investigate, among other things, a series of transactions that the parties have generally called "the disputed transactions" for short. The disputed transactions were engineered by CEC, parent of lead debtor Caesars Entertainment Operating Co. ("CEOC"), and by Apollo and TPG, ultimate owners of the Caesars enterprise. Paul Weiss represented CEC and CEOC in the transactions. Both CEOC and the Committee have asserted that the transactions stripped CEOC of assets, and the bankruptcy estates have claims against CEC, Apollo, TPG, and others arising out of the transactions.

During the examiner's investigation enormous numbers of documents were produced to him from an enormous number of parties. These parties included CEC, Apollo, and TPG. Under an arrangement worked out with the parties, the examiner was given access not only to documents that were not privileged in any way but also documents that were subject to the

attorney-client privilege.

In March, the examiner issued an extensive report in which he concluded that the bankruptcy estates do indeed have claims against CEC, Apollo, and TPG. The claims include fraudulent transfer claims based on actual fraud and constructive fraud.

The debtors have proposed a plan of reorganization under which all of the estates' claims against these and other parties will be released. The Committee intends to object to confirmation at least in part because of the release. Confirmation will therefore be contested. The hearing on plan confirmation is set for January 17, 2017, and all parties are currently subject to a scheduling order that sets deadlines for discovery related to confirmation.

The Committee served subpoenas on CEC, Apollo, TPG, and Paul Weiss that sought documents relating to the alleged fraudulent transfers. Some of those documents were withheld as subject to the attorney-client privilege, and the Committee now moves to compel their production. The Committee argues that under the "crime-fraud" exception to the privilege, the documents must be produced. CEC, Apollo, TPG, and Paul Weiss oppose the motion.

2. Discussion

The Committee does not dispute that unless the "crime-fraud" exception applies, the documents in question are privileged and need not be produced. So the only question is whether the Committee has shown the exception does apply – or at least shown that an *in camera* inspection of the documents is warranted. The answer to the second question is no, and so the answer to the first must be no, as well.

The crime-fraud exception prevents parties from invoking the attorney-client privilege to protect communications made "for the purpose of getting advice for the commission of a fraud or crime." *United States v. Zolin*, 491 U.S. 554, 563 (1989) (internal quotation omitted). For the

exception to apply, two elements must be present: a crime or fraud must have been attempted or committed, and the communications must have been made in furtherance of the crime or fraud. *Mattenson v. Baxter Healthcare Corp.*, 438 F.3d 763, 769 (7th Cir. 2006); *see also* 3 Joseph M. McLaughlin, Jack B. Weinstein & Margaret A. Berger, *Weinstein's Federal Evidence* § 503.31[4][a] at 503-99 (2014) (describing the "two-part inquiry").

In this circuit, the party invoking the exception must present "'prima facie evidence'" of these elements, meaning evidence "'that gives color to the charge by showing some foundation in fact.'" *United States v. Boender*, 649 F.3d 650, 655 (7th Cir. 2011) (quoting *United States v. BDO Seidman, LLP*, 492 F.3d 806, 818 (7th Cir. 2007)). Despite the term "prima facie," the standard "'is not whether the evidence supports a verdict but whether it calls for inquiry.'" *United States v. Al-Shahin*, 474 F.3d 941, 946 (7th Cir. 2007) (quoting *In re Feldberg*, 862 F.2d 622, 625 (7th Cir. 1988)); *see also BDO Seidman*, 492 F.3d at 818.

If necessary, the court can also examine the communications themselves to determine whether they further a crime or fraud. *Boender*, 649 F.3d at 656. Because judicial review entails less of an intrusion into the attorney-client relationship, a "lesser evidentiary showing is needed to trigger *in camera* review than is required ultimately to overcome the privilege." *Zolin*, 491 U.S. at 572. To warrant an *in camera* inspection, there need only be a "showing of a factual basis adequate to support a good faith belief by a reasonable person that *in camera* review of the materials may reveal evidence to establish the claim that the crime-fraud exception applies." *Id.* (internal quotation omitted); *see also Boender*, 649 F.3d at 656.

Here, the Committee has not made even the showing necessary to justify *in camera* review of the documents. In support of its motion, the Committee relies on its motion from February 2015 requesting appointment of the examiner; the examiner's report itself; and the

debtors' recently-filed adversary complaint against CEC, Apollo, TPG, and others alleging claims arising out of the disputed transactions.

The Committee's motion established nothing, except perhaps grounds for appointment of an examiner under section 1104(a) of the Code – and such an appointment is appropriate for "cause," of which "fraud" is only one enumerated example. The motion mentioned "[t]he existence of potential avoidance claims and other actions against insiders and related parties" (Dkt. No. 367 at 4), but it did not suggest those claims involved fraud, let alone establish a factual basis sufficient to support a good faith belief that fraud had occurred. The word "fraud" barely appeared in the motion. (*See id.*).

The examiner's report, on the other hand, found the estates had fraudulent transfer claims, both actual and constructive, of varying strengths. But an examination of the report shows the "actual fraud" claims all involved an intent "to hinder or delay" creditors, not an intent to defraud them. Nowhere in his report does the examiner conclude the estate has any "actual fraud" claims dependent on fraudulent intent. The report itself declares up-front that of all the claims the examiner discovered, "[n]one . . . involve criminal or common law fraud." (Dkt. No. 3720 at 1).

As for the debtors' adversary complaint, the claims in it parallel the claims the examiner found. The debtors allege fraudulent transfer claims based on an intent to hinder or delay creditors; no intent to defraud creditors is alleged. (*See, e.g.*, Adv. No. 16 A 522, Dkt. No. 1, at ¶¶ 1, 334, 395, 437). The phrase "intent to defraud" shows up in the complaint's introduction (*see id.*, ¶ 17) and later in boilerplate conspiracy allegations repeated in various counts (*see, e.g.*, *id.*, ¶¶ 322, 428-29, 453-54, 501-02), but that is all. A complaint is in any event simply a set of allegations; it establishes no facts.

The Committee appears to take the position that a fraudulent transfer claim based on actual fraud necessarily involves fraud. As CEC correctly argues, however, "fraudulent transfer" is an umbrella term for a variety of claims, some of which involve fraud in the usual sense and some of which do not. Even so-called fraudulent transfer claims based on actual as opposed to constructive fraud may not involve fraud, since those claims can be premised on an intent to hinder or delay creditors. The examiner made this same observation in his report. (*See* Dkt. No. 3720, App'x. 5 at 20-21).

To support a broader interpretation of "actual fraud," the Committee cites the Supreme Court's recent decision in *Husky Int'l Elecs., Inc. v. Ritz*, ___ U.S. ___, 136 S. Ct. 1581 (2016). *Husky*, though, addressed a different issue: whether "actual fraud" in section 523(a)(2)(A) requires a misrepresentation. The Court held only that no misrepresentation was required, *id.* at 1588, taking the same view the Seventh Circuit had taken in *McClellan v. Cantrell*, 217 F.3d 890 (7th Cir. 2000). The Court pointedly did not "adopt a definition" of fraud "for all times and all circumstances." *Husky*, ___ U.S. at ___, 136 S. Ct. at 1587.

In reaching its conclusion, however, the Court in *Husky* did observe that "'fraud' connotes deception and trickery generally," *id.* at ___, 136 S. Ct. at 1586, and that fraudulent conduct for purposes of actual fraud consists of "the acts of concealment and hindrance," *id.* at 1587. The Court's use of the term "concealment" is noteworthy. Although actual fraud need not involve a misrepresentation, it still involves some "deceit, artifice, trick, or design . . . to circumvent and cheat another." *McClellan*, 217 F.3d at 893 (internal quotation omitted). Without some element of deceit, then, there is no fraud. And it is possible to hinder or delay creditors without deceiving them. Assuming the disputed transactions here were undertaken with that motivation, they appear to fit the bill: the Committee in its motion nowhere suggests

any deception.

Lastly, the Committee argues that the crime-fraud exception extends beyond crimes or frauds to other intentional torts. Some courts have said so. *See* Christopher B. Mueller & Laird C. Kirkpatrick, *Federal Evidence* § 5:27 at 629 (3d ed. 2007) (citing cases). Others have disagreed. *See, e.g.*, *Motley v. Marathon Oil Co.*, 71 F.3d 1547, 1551 (10th Cir. 1995); *Prudential Ins. Co. of Am. v. Massaro*, No. CIV. A. 97-2022, 2000 WL 1176541, at *10 (D.N.J. Aug. 11, 2000). The Seventh Circuit has not extended the exception but has continued to call it the "crime-fraud exception" and apply it only to crimes and frauds. *See, e.g.*, *Shaffer v. American Med. Ass'n*, 662 F.3d 439, 447 (7th Cir. 2011); *Boender*, 649 F.3d at 655; *BDO Seidman*, 492 F.3d at 818; *Al-Shahin*, 474 F.3d at 946; *Mattenson*, 438 F.3d at 769.[1/] Absent guidance from the court of appeals or some reason to believe there is a groundswell of opinion with which that court would likely go along, the exception should not be expanded beyond fraud in the *McClellan* sense.

In sum, the Committee has not provided "a factual basis adequate to support a good faith belief by a reasonable person" that an *in camera* inspection of the documents might show communications in furtherance of a fraud in the sense discussed. And since the lesser showing for an *in camera* inspection has not been made, necessarily the Committee has produced no *prima facie* evidence that would bring the crime-fraud exception into play.

Had the Committee made the lesser showing, finally, an *in camera* inspection would still be inappropriate. In *Zolin*, the Supreme Court took note of "the burdens *in camera* review places

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[1/] Only two trial courts in this circuit have extended the exception – and in both cases some form of concealment was involved. *See In re Application of Heraeus Kulzer, GmbH*, No. 3:09-CV-530 RM, 2012 WL 1493883, at *3 (N.D. Ind. Apr. 26, 2012); *1100 West, LLC v. Red Spot Paint & Varnish*, No. 1:05-cv-1670-LJM-JMS, 2009 WL 232060, at *4-5 (S.D. Ind. Jan. 30, 2009).

upon the district courts, which may well be required to evaluate large evidentiary records without open adversarial guidance by the parties." *Zolin*, 491 U.S. at 571. Even when the necessary factual showing has been made, consequently, the decision whether to conduct an *in camera* inspection rests with "the sound discretion of the district court." *Id.* at 572. In exercising that discretion, the court should consider

> the facts and circumstances of the particular case, including, among other things, the volume of materials the district court has been asked to review, the relative importance to the case of the alleged privileged information, and the likelihood that the evidence produced through *in camera* review, together with other available evidence then before the court, will establish that the crime-fraud exception does apply.

Id.

These factors counsel against an *in camera* inspection here. The volume of documents, first of all, is overwhelming. Apollo and TPG assert without contradiction that they have withheld as privileged more than 180,000 documents. CEC asserts it has withheld more than 50,000 documents. And these are documents, not pages. Assuming these 230,000 documents averaged three pages long, and assuming further that this court examined 30 pages an hour for 8 hours a day, 5 days a week, without interruption, it would take just over 11 years to perform the inspection. This for a hearing set to begin in four months.

The relative importance of the documents to the case is not nearly great enough to justify an effort of that kind. As Apollo and TPG also observe, again without contradiction, millions of documents have already been produced to the Committee, as well as 16,000 pages of 74 different interviews the examiner conducted. If, as all parties seem to agree, the release will rise or fall under the Rule 9019 standards for approving settlements, the confirmation hearing will only require canvassing the merits of the estate's claims. *See In re Commercial Loan Corp.*, 316 B.R.

690, 698 (Bankr. N.D. Ill. 2004). The claims themselves will not be tried. The Committee offers no reason to believe the privileged documents are critical to a canvassing of the merits and would add anything to the material the Committee already has.

For the reasons discussed, finally, there is no reason to believe that an *in camera* inspection may show the crime-fraud exception applies. In the course of his investigation, the examiner, a dispassionate third party, saw and considered all of the privileged documents the Committee wants to see. Those documents did not lead him to conclude that any fraud had been committed – other than "actual fraud" with no intent to defraud, which is not fraud for purposes of the crime-fraud exception.

3. Conclusion

The motion of the Second Priority Noteholders Committee to compel production of documents under the crime-fraud exception is denied.

Dated: September 21, 2016

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A. Benjamin Goldgar
United States Bankruptcy Judge