

Lessons from the Bankruptcies of Donald Trump

By James V. Irving



Among other things, Donald Trump's presidential campaign has moved bankruptcy law from the financial page to the front page. On four occasions, Trump, who has characterized bankruptcy as part of the cost of doing business, has sought to use the provisions of Chapter 11 of the Bankruptcy Code to his advantage. Within the reams of filings and paperwork lie some important distinctions and universal lessons.

Donald Trump had an ownership interest in four companies that filed for bankruptcy protection between 1991 and 2009. Three of the bankruptcies were largely related to his casino operations in Atlantic City, New Jersey. One of the bankruptcies involved the Plaza Hotel that Trump acquired in 1988. Each of the bankruptcies forced Trump into difficult reorganizations that cost him equity in his companies. The Plaza bankruptcy and the final casino bankruptcy resulted in him ceding his influence over day-to-day operations of the companies.

Bankruptcy No. 1 – Trump Taj Mahal Hotel –1991

Trump's first bankruptcy appears to have hit him the hardest. It was the only one of the four to place his personal finances at risk. This Chapter 11 reorganization was filed in the Camden Division of the District of New Jersey Bankruptcy Court, where Trump faced a tough battle developing a reorganization plan acceptable to the creditors' committee. The result was painful.

His critical error may have arisen from overconfidence. To acquire the Taj Mahal from Merv Griffin, Trump ceded control over his Atlantic City hotel and casino company, Resorts International, Inc., and personally guaranteed some of the junk bond loans used to finance the acquisition. After lower-than-expected returns, the casino couldn't

pay back the interest rates on the junk bonds that ran as high as 14%. In the ensuing bankruptcy, he leveraged business debt to protect his personal assets, but it cost him his yacht, the Trump Princess, the Trump Shuttle airline and much of his equity stake in the hotel. He was also forced to accept humiliating limits on his personal spending. Perhaps a more seasoned dealmaker – or one with better options – wouldn't have placed his personal assets at risk in the first place.

Mr. Trump came away with one positive: he retained some of the equity in his casinos. However, the bankruptcy was very damaging financially, no matter how you spin it.

Bankruptcy No. 2 – Plaza Hotel –1992

Within a year, Trump again found himself under water. This time, the asset was the Plaza Hotel, which he acquired after winning a bidding war at an auction in 1988. Thrilled to secure this New York landmark, he promised to make it "the most luxurious hotel in the world." Within four years of the purchase, the hotel was unable to make its debt service payments, and Trump found himself in a Chapter 11 proceeding in the U.S. Bankruptcy Court for the Southern District of New York.

Did the overconfidence or arrogance, which led Trump to guarantee junk bonds to finance the Taj Mahal, result in overpayment for an asset that his acquisitive ambition demanded? This is a legitimate question without a definitive answer. However, Trump defended the acquisition by relying on non-economic justifications for the purchase, such as calling the Plaza a "work of art." He also stated that his wife, Ivana, would be the President of the hotel for a salary of "\$1 a year plus all the dresses she can

buy.” Hardly the words of a calculating business mogul.

In the reorganization, Trump gave up day-to-day operational influence in the short term, his CEO salary, and a substantial ownership stake. Citibank – and other lenders – gained a 49% interest in the hotel. Three years later, Trump sold even more of his equity to CDL Hotels and Saudi Prince Walid bin Talal, but he retained a minority interest.

Bankruptcy No. 3 – Trump Hotel and Casino Resorts – 2004

By 2004, Trump’s holding company Trump Hotels and Casinos Resorts controlled the Trump Taj Mahal, Trump Plaza Hotel, Trump Marina Hotel and Casino in Atlantic City, Trump 29 Casino in California, and Trump Riverboat Casino operating out of Gary Indiana in Indiana. Facing stiff competition from other casinos and carrying 1.8 billion in debt, Trump was forced to place the holding company in Chapter 11. Minimizing the process as “just a technical thing,” he negotiated lower interest rates and a \$500 million line of credit in return for a reduction in his stake from 47% to 27%. He also was forced to pump \$72 million of his personal wealth into the deal to keep the restructuring afloat. But, at the end of the process Trump boasted that the Trump brand was “bigger than Pepsi.”

Bankruptcy No. 4 – Trump Entertainment Resorts – 2009

In 2009, Trump bankrupted Trump Entertainment Resorts, the company that was the successor to the original Trump Hotel and Casino Resorts company that went bankrupt in 2004 (see Bankruptcy No. 3 above). In some ways, this 4th bankruptcy may have polished his reputation more than it harmed it. He was able to fend off an attempted take-over by rival tycoon Carl Icahn, who wanted the Trump brand, while providing positive tabloid fodder for himself.

The proceeding was not without pain. Trump was forced to give up his seat on the board of directors – technically, he resigned from the board just before the company filed for bankruptcy – and influence in day-to-day operations of the company. Trump’s ownership stake was reduced to 10% in a deal with the bondholders, who became the new owners under the approved plan, but, significantly, he didn’t have to risk his own assets. Perhaps most importantly, in rebuffing Icahn, the bankruptcy judge noted that the Trump brand was “very valuable” in the casino industry. Today, the Trump brand may still be his most valuable asset.

Donald Trump’s bankruptcy travails have revealed a resilient man who learns from his mistakes. In particular, he learned not to expose his personal wealth. The man who imprudently overvalued and overpaid for a hotel in the early 90s later battled head-to-head with rival titan Carl Icahn. The man who guaranteed junk bonds in the acquisition of his first hotel used the bankruptcy forum as a vehicle to burnish his mark fifteen years later. After each bankruptcy, Trump managed to land on his feet. As Trump himself has said, the bankruptcy laws exist to be used by debtors to their advantage, and he has certainly done so.

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