AMERICAN BANKRUPTCY INSTITUTE

Central States Bankruptcy Workshop

CONCURRENT SESSION

Liability-Management Exercises and Implications

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2025

Liability Management Exercises: Where are We Now?

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Definition

- Out-of-court restructuring of borrower's debt by subordinating certain debt and dividing lenders or bondholders into two classes: participating lenders/bondholders (the haves) and non-participating lenders/bondholders (the have nots).
- Transaction increases borrower's liquidity and extends maturity date – borrower may be facing a liquidity crunch and have no unencumbered assets.
- Oftentimes sponsor-owned portfolio company.
- Transactions may result in litigation and, in some instances, fail to stave off bankruptcy.
- Language in credit agreement/indenture controls (e.g., pro rata sharing, sacred rights, open market purchase, purchase, LME definition).

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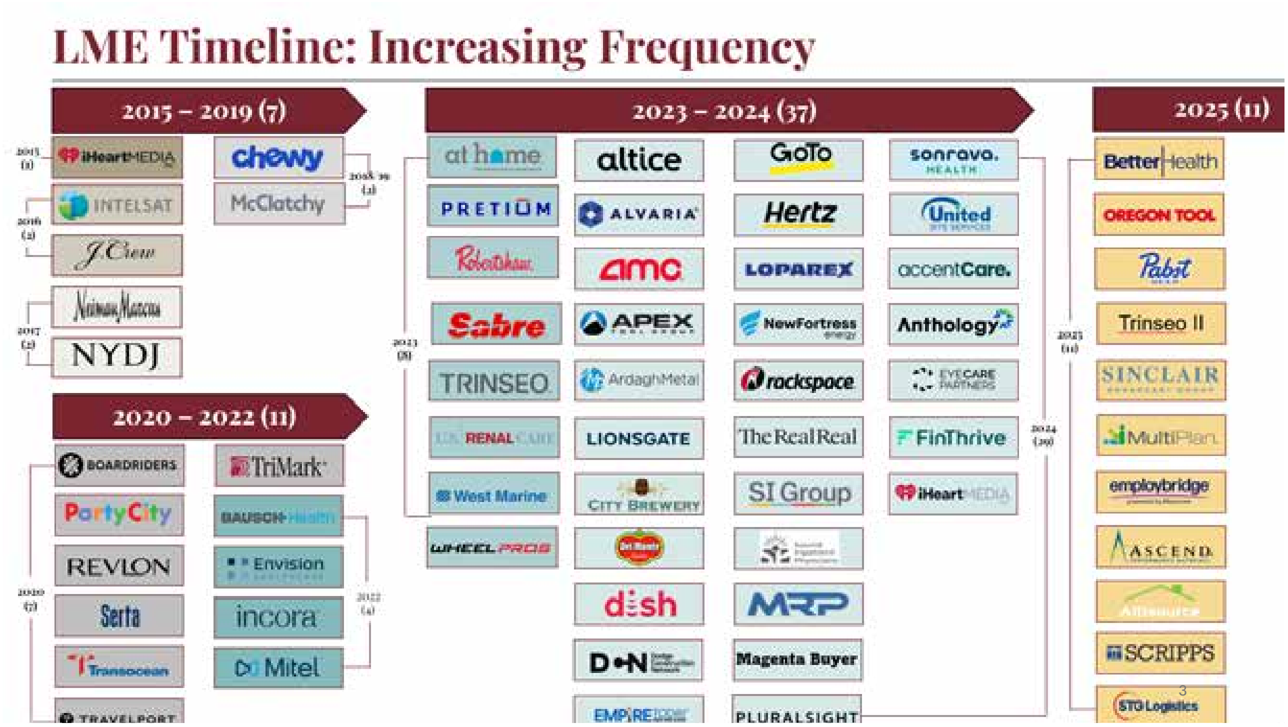

Parties & Goals

- Sponsor
  - Avoid borrower bankruptcy
- Lenders
  - Maximize returns
  - Market protections
- Borrowers
  - Best terms
  - Extend maturities

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Which Actors Can Catalyze A Transaction?

- Unilateral Borrower Action
- Some LMEs can be consummated by a Borrower without any lender consent under the existing loan documents.
- Majority Lender Action
- To consummate other LMEs, a Borrower needs the consent of Required Lenders (typically a simple majority of lenders or two-thirds of bondholders) to subordinate or release liens and to modify the existing covenants contained in the loan documents. Typically, loan documents do not require lenders to be given advance notice of amendments.

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Illustrative Transaction Overview

Assumptions	
Transaction Date	
Close Date	1/31/23
Assumed Participation Rates (Scenario 2)	
Existing Other Collateral Loans	88.0%
Existing Term Loans	66.7%
Existing Notes	66.7%
Existing Term Loan Exchange Allocation	
Existing Term Loan to New Other Collateral Loans	40.0%
Existing Term Loan to New Company Loans	60.0%
LTM Financials as of 9/30/22 ($ in Mns)	
Reported EBITDA	$ 145.5
Unrestricted Cash & Cash Equivalents	115.8
Restricted Cash	1.7

Sources & Uses *($ in Mns)*	
Sources	
New Other Collateral Loans	$ 179.0
New Company Loans	59.5
New Notes	187.3
Total Sources	$ 425.8
Uses	
Existing Other Coll. Loans (Principal)	$ 88.0
Existing Other Coll. Loans (Exit Fee)	1.8
Existing Loans	187.3
Existing Term Loans	148.8
Total Uses	$ 425.8

Pro-Forma Capitalization

		Pre-Transaction (9/30/22)			Trans.	Post-Transaction (1/31/23)		
($ in Mns)	Rate	Maturity	Amount	Leverage	Adj.[1]	Maturity	Amount	Leverage
ABL	B+3.00%	Feb-27	$ 55.0		$ -	Feb-27	$ 55.0	
Existing Other Collateral Loans	S+7.50%	Dec-23	100.0		(88.0)	Dec-23	12.0	
Existing Notes	10.00%	Aug-24	281.0		(187.3)	Aug-24	93.7	
Existing Term Loans[2]	L+8.00%	Feb-25	221.6		(147.2)	Feb-25	74.4	
New Other Collateral Loans	S+8.00%	n/a	-		179.0	Dec-27	179.0	
New Company Loans	S+8.00%	n/a	-		59.5	Dec-27	59.5	
New Notes	8.50%	n/a	-		187.3	Dec-27	187.3	
Total Secured Debt			$ 657.6	4.5x	$ 3.3		$ 660.9	4.5x
Foreign Notes Payable to Banks	Various	Various	548.5		-	Various	548.5	
Other Debt	n/a	n/a	0.6		-	n/a	0.6	
Total Debt			$ 1,206.7	8.3x	$ 3.3		$ 1,210.0	8.3x
(–) Cash & Cash Equivalents			(114.1)		-		(114.1)	
Net Debt			$ 1,092.6	7.5x	$ 3.3		$ 1,095.9	7.5x
Share Price as of 12/4/22 (in $)			$ 0.32				$ 0.32	
Total Shares Outstanding (in Mns)			25.0				25.0	
Market Capitalization			$ 8.0				$ 8.0	
(+) Net Debt			1,092.6				1,095.9	
Total Enterprise Value			$ 1,100.6				$ 1,103.9	

See slide 10 for additional detail behind the exchange calculations

Notes:

1. *Includes accrued PIK Interest on the Existing Term Loans from 9/30/22 to the assumed close date of 1/31/23 ($1.5M) plus the 2% exit fee on the exchanged Existing Other Collateral Loans ($1.8M, assuming 88% convert)*
2. *Existing Term Loans have a rate of L + 8.00% (1.50% LIBO Floor)+ PIK interest (1% starting 8/24/21 and increasing by 1% annually on 8/24 through maturity)*

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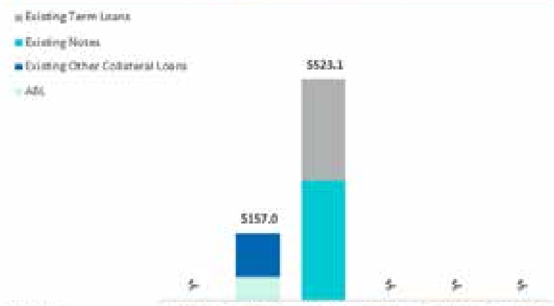
Maturity Wall[1]

The transaction significantly extends the Company's maturity wall, as the majority of the post-transaction debt matures at the end of 2027 (assuming the participation rates set forth on slide 9)

Pre-Transaction



($ in Mns)	FY2023	FY2024	FY2025	FY2026	FY2027	FY2028
ABL	$ -	$ 55.0	$ -	$ -	$ -	$ -
Existing Other Coll. TL[1]	-	102.0	-	-	-	-
Existing Notes	-	-	281.0	-	-	-
Existing TL	-	-	242.1	-	-	-
Total	$ -	$ 157.0	$ 523.1	$ -	$ -	$ -

Post-Transaction

($ in Mns)	FY2023	FY2024	FY2025	FY2026	FY2027	FY2028
ABL	$ -	$ -	$ -	$ -	$ 55.0	$ -
Existing Other Coll. TL[2]	-	12.2	-	-	-	-
Existing Notes	-	-	93.7	-	-	-
Existing TL	-	-	80.7	-	-	-
New Other Collateral TL	-	-	-	-	-	179.0
New Company TL	-	-	-	-	-	59.5
New Notes	-	-	-	-	-	187.3
Total	$ -	$ 12.2	$ 174.4	$ -	$ 55.0	$ 425.8

Notes:

1. *Does not include maturities of foreign lines of credit; assumes the springing maturity under the ABL is waived in the post-transaction chart*
2. *Assumes a 2% exit fee is paid at the maturity of the Existing Other Collateral Term Loan*

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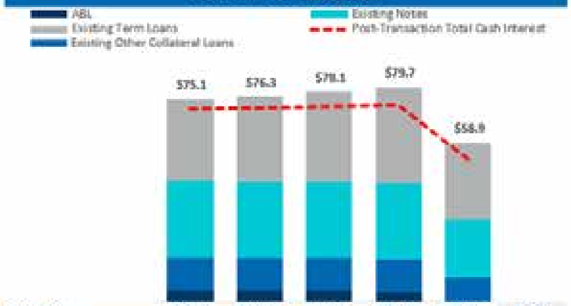
Pro-Forma Cash Interest Payments by Year[1]

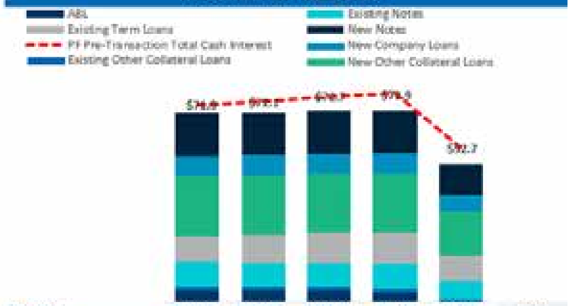
The pro-forma post-transaction cash interest from FY2024 – FY2028, assuming the participation rates set forth on slide 9, is ~$26M lower than the pro-forma cash interest due under the Company's current capital structure

Pro-Forma Pre-Transaction[2]



($ in Mns)	FY2024	FY2025	FY2026	FY2027	FY2028	Total
ABL	$ 4.2	$ 4.2	$ 4.2	$ 3.6	$ -	$ 16.4
Existing Other Coll. TL	12.1	12.1	12.1	12.1	9.1	57.6
Existing Notes	28.6	28.5	28.5	28.5	21.5	135.5
Existing TL	30.1	31.5	33.2	35.5	28.3	158.6
Total	$ 75.1	$ 76.3	$ 78.1	$ 79.7	$ 58.9	$ 368.0
Post-Txn Cash Interest	*$ 71.9*	*$ 72.1*	*$ 72.7*	*$ 72.9*	*$ 52.7*	*$ 342.4*
Variance to Post-Txn	*3.2*	*4.1*	*5.3*	*6.8*	*6.2*	*25.7*

Pro-Forma Post-Transaction[2]



($ in Mns)	FY2024	FY2025	FY2026	FY2027	FY2028	Total
ABL	$ 4.2	$ 4.2	$ 4.2	$ 3.6	$ -	$ 16.4
Existing Other Coll. TL	1.5	1.5	1.5	1.5	1.1	6.9
Existing Notes	9.5	9.5	9.5	9.5	7.2	45.2
Existing TL	10.0	10.5	11.1	11.8	9.4	52.9
New Other Collateral TL	22.8	22.8	22.8	22.8	17.2	108.3
New Company TL	7.6	7.6	7.6	7.6	5.7	36.0
New Notes	16.2	16.1	16.1	16.1	12.2	76.8
Total	$ 71.9	$ 72.1	$ 72.7	$ 72.9	$ 52.7	$ 342.4
PF Pre-Txn Cash Interest	*$ 75.1*	*$ 76.3*	*$ 78.1*	*$ 79.7*	*$ 58.9*	*$ 368.0*
Variance to PF Pre-Txn	*(3.2)*	*(4.1)*	*(5.3)*	*(6.8)*	*(6.2)*	*(25.7)*

Notes:

1. *Does not include cash interest due on foreign lines of credit*
2. *The pro-forma pre- and post-transaction cash interest analyses assume December 2027 maturities for all debt except the ABL which remains at its stated of maturity February 2027*

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Liability Management Exercise Options

- Uptier
- Drop-Down
- Double-Dip
- Pari-Plus
- Inside Out

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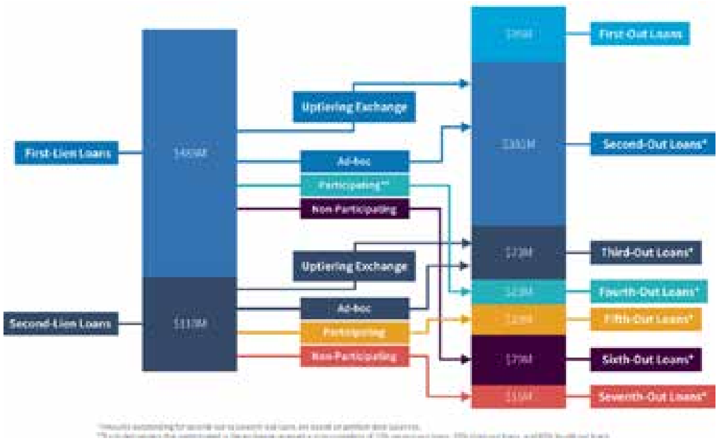
Uptier Transaction

- Subset of lenders provide new money financing and exchange existing debt for new debt with a higher priority, or alternatively, non-participating creditors lose the collateral support that underpinned their holdings.
- Robertshaw:



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Deep Dive – Serta (Uptier)

- In 2016, issued $1.95 billion in first-lien syndicated loans and $450 million in second-lien syndicated loans.
- The credit agreement for the first-lien loans contained a pro rata sharing provision requiring ratable repayment with an exception that permitted non-pro rata loan repurchases by a Serta affiliate in an "open market purchase," which was not defined, and for Dutch Auctions open to all lenders on a pro rata basis.
- In 2020, participating lenders who held a slim majority of first-lien debt and provided $200 million of new money financing were given the opportunity to exchange $1.2 billion of their existing loans for super-priority debt. The excluded lenders did not have the opportunity to participate on the same terms.
- In 2023, Serta filed for bankruptcy – the bankruptcy court sided with the participating lenders regarding their post-uptier super-priority debt and approved Serta's plan, which respected the uptier transaction.

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Deep Dive – Serta (Uptier) *(cont'd)*

- Serta and the participating lenders argued as follows:
  - No express requirement that "open market purchases" must be "open to all Lenders"
  - Excluded lenders made their own non-pro rata proposal to Serta and should be estopped from complaining
  - Market usage of "open market purchases" supports a broad reading
- Fifth Circuit reversed, holding that exchange of new super-priority loans for old loans in the uptier was not a permissible "open market purchase" of the old loans within the meaning of the credit agreement – Dutch Auction exception provision would be meaningless and violate doctrine of the rule of surplusage.
- But see New York Supreme Court's First Appellate Division: Mitel Networks "purchase" exception to the prohibitions on non-pro rata transactions.

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Drop-Down Transaction

- Borrower utilizes basket capacity under existing investment and restricted payment covenants to transfer collateral away from the restricted entities to an "unrestricted subsidiary."
- Being unrestricted, the subsidiary is typically not required to be a guarantor (and, accordingly, does not pledge its assets as collateral), nor is it subject to the covenants in the financing agreements.
- As a result, the unrestricted subsidiary is often free to issue new debt, which is then secured by the newly transferred assets.
- Transaction wherein assets are moved from a guarantor restricted sub into a non-guarantor subsidiary to allow the company to raise debt specifically secured by these assets/businesses.
- Unlike uptier transactions, drop-downs do not necessarily require the consent of the majority creditors, although subsequent ratification of the transaction is often sought and obtained from participating majority creditors to avoid litigation.

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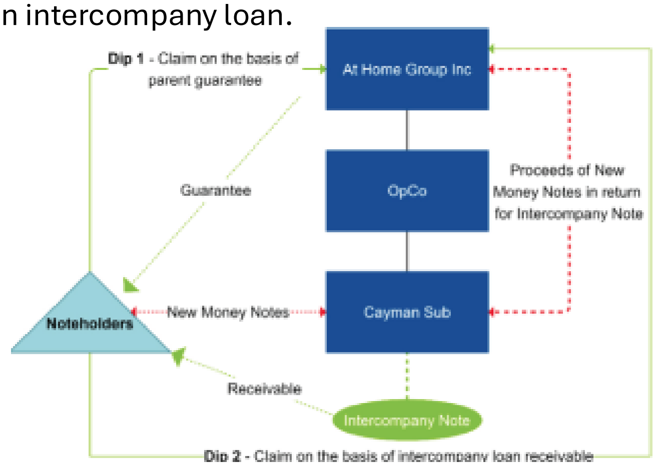
Double-Dip Transaction

- A "true" double-dip is a loan to an SPV which then on-lends the funds to a guarantor under an intercompany loan.



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Pari-Plus Transaction

- A subset of the double-dip genre, where the first dip is enhanced by having entities that are outside the existing credit group incur or guarantee the new-money secured facility.
- As a result, the double-dip lender in this transaction is "pari" regarding the intercompany claims provided through the second dip (i.e., intercompany receivable pledge), "plus" benefits from structurally senior claims on any assets of the obligors that are outside of the borrower's existing credit group.

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Inside Out Transaction

- **Goal**: Third-party or minority lender group dethrones majority lender group and acquires requisite lender status by funding a refinancing loan on a pro rata basis, normally prompted by companies wanting to engineer a new majority, borrower-friendly constituency.
- Happens where the majority lender group "refuses" to come close enough to the company's demands for a transaction to be executed.
- **Example**: Company with $100 million term loan, $55 million held by a majority lender group, potentially with an effective cooperation agreement, and $45 million held by various minority lenders. A third-party funds a $51 million refinancing loan, the proceeds of which are used to prepay the company's term loans at par on a pro rata basis.
  - Result: Third-party becomes the new majority lender, owning $51 million of the refinancing loans, former majority lender owns $26.95 million, and the former minority lenders owns $22.05 million.

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Clarifying Potential Misconceptions

- Disfavored by courts?
- Solely a bankruptcy fixture?
- Always impermissible?
- Is it ever a non-zero sum game?
- Bondholder vs. BSL lender expectations?

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Can we draw any macro conclusions?

- Non-Pro Rata Uptiers vs. Other Transactions Types

  Notwithstanding the headlines regarding non-pro rata uptier transactions, drop-down transactions still outnumber them.

- Catalysts matter in transaction structures

  While all transaction types have been used to address liquidity, companies seeking to address maturities have favored drop downs. This trend may continue, due to the presence of anti-Serta provisions that are now common in credit documentation, as well as the availability of third-party providers of capital to either address upcoming maturities when using a drop-down structure or to provide the company with negotiating leverage against incumbent creditor groups.

- Diversity of Actors

  LMEs are no longer a domain of the few. Many financial sponsors and an increasing amount of public companies have participated in LME transactions, especially within the last few years, to address challenges to their capital structures, which has resulted in an increased "normalization" of LME transactions in the credit markets.

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Repercussions

- Monetary damages for excluded lenders or undoing LME to restore liens (Robertshaw, Wesco/Incora)
- Co-operation agreements
- Omni-block and/or preemptive debt rights sophistication
- Industry fatigue by participants
- Prepetition leveraging by lenders or insolvency avoidance by borrower/sponsor
- Arbitrage opportunities for lenders

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"Omni-Blocker": Spirit Airlines

- Define "**Liability Management Transaction**" with a high-level definition followed by a non-exhaustive list of specific transactions to capture not only a list of LME structures but also the spirit of an LME transaction. Needs to provide borrower with latitude to conduct business.
  - "'Liability Management Transaction' shall mean, other than a transaction undertaken for a bona fide expansion of the Loan Parties' business pursuant to a business plan conducted in good faith, any transaction or series of related transactions that is designed primarily to (x) raise liquidity for Holdings and its Subsidiaries at a time when the Borrower's near-term liquidity prospects is constrained or diminishing, (y) preserve any portion of a valuable asset for the benefit of an Affiliate of the Loan Parties, or (z) restructure or otherwise impact the Loan Parties' capital structure in a manner that improves the prospects of a class or subset of stakeholders (including the Sponsor and its affiliates, any other equityholder, and any debt financing providers (including any class or subset of Lenders)) that is pari passu with or junior to the Lenders by elevating such stakeholder's priority (whether effectively, structurally or contractually) or ability to direct actions under the Loan Documents, including any of the following: …"
- Addressing non-pro rata risk.
- Addressing exclusive opportunity uptier, drop-down, double-dip, pari-plus risk.
- Addressing vote-rigging.

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Faculty

Kyle F. Arendsen is a member of Squire Patton Boggs US LLP's Restructuring & Insolvency Practice Group in Cincinnati. He focuses his practice on companies and creditors in all aspects of corporate restructurings, including in chapter 11 cases, out-of-court restructurings, cross-border insolvencies and supply chain matters. Mr. Arendsen's restructuring matters encompass a wide variety of industries, including mining, real estate, aviation, manufacturing, oil and natural gas, health care and pharmaceutical. He is a member of ABI and the Turnaround Management Association. Mr. Arendsen received his B.S. in 2013 from Cornell University and his J.D. in 2016 from the University of Virginia School of Law.

Victoria C. Hotchkiss is a director at Ducera Partners LLC in New York and has worked on a broad range of restructuring transactions, including Aeromexico, Bumble Bee Foods, CBL & Associates, Puerto Rico and Spirit Airlines. Previously, she worked at Miller Buckfire & Co. and Brookfield Asset Management. Ms. Hotchkiss received her B.A. from Georgetown University.

Hon. Marvin P. Isgur is a U.S. Bankruptcy Judge for the Southern District of Texas in Houston, appointed on Feb. 1, 2004, and reappointed on Feb. 1, 2018. He also served as Chief Judge from 2009-2012. Judge Isgur serves as adjunct faculty at the University of Houston Law Center. Between 1978 and 1990, he was an executive with a large real estate development company in Houston. From 1990 until 2004, he represented trustees and debtors in chapter 11 and chapter 7 cases, as well as various parties in 14 separate chapter 9 bankruptcy cases. Judge Isgur has written over 500 memorandum opinions. He was one of the first judges to issue opinions interpreting the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act. Judge Isgur is a volunteer with the Houston Urban Debate League, a nonprofit organization that works in partnership with the Houston Independent School District to bring policy debate to high school students. He is one of the principal organizers of the annual University of Texas Consumer Bankruptcy Conference and is a frequent speaker at continuing education programs. Judge Isgur received his bachelor's degree from the University of Houston in 1974, his M.B.A. with honors from Stanford University in 1978, and his J.D. with high honors from the University of Houston in 1990.

Joseph Richman is a senior director with FTI Consulting, Inc. in Denver and has worked with troubled and insolvent companies both in and out of the bankruptcy process, as well as unsecured creditors and secured lenders. He has experience in matters related to the financial advisory of distressed clients, including cash-flow projections, business plan analysis, liquidation analyses, claims reconciliations and fraudulent conveyance investigations (including expert report preparation). His recent sector experience includes retail, energy, minerals & mining, professional services and government contracting. Mr. Richman has worked as a turnaround and restructuring consultant for over a decade. Prior to joining FTI Consulting, he worked for a boutique debtor-side advisory practice based in Denver. Prior to moving to Denver, he worked in a similar role for a New York-based accounting firm. Mr. Richman has experience in securities trading and spent time working for a foreign exchange broker trading oil, precious metals and various foreign currencies. He also traded exchange-listed equity securities. Mr. Richman previously was a manager with BDO USA, LLP and a senior consultant with Gavin/Solmonese LLC. He received his Bachelor's degree in psychology, political science and government in 2010 from Georgetown University, and his M.Sc. in political science and government from The London School of Economics and Political Science in 2011.

Matthew L. Warren is a partner in the Financial Restructuring group at Paul Hastings, LLP and is based in the firm's Chicago and Houston offices. He advises clients on restructuring matters with a particular emphasis on distressed debt and insolvency issues. Mr. Warren represents lenders and bondholders, as well as companies and asset-buyers, in connection with restructuring and insolvency-related matters. He is a member of ABI's 2019 class of "40 Under 40" emerging leaders. He also was recognized for his work in Bankruptcy and Restructuring by *Chambers USA* 2019, and *Turnarounds & Workouts* named him a 2018 Outstanding Young Restructuring Lawyer. Mr. Warren is an ABI member, teaches as an adjunct professor of bankruptcy law at the DePaul College of Law, and regularly speaks and writes on bankruptcy topics. He received his B.S. *summa cum laude* from Southern Illinois University Edwardsville and his J.D. *summa cum laude* from the University of Arizona.