RX INTERVIEWS

DOUBLE-DIP GUIDE

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INTRODUCTION

In the world of restructuring, no matter where you go, and no matter who you talk to, you'll eventually end up talking about drop-downs and non-pro rata uptiers in some capacity. I think it's inarguable that they've been the two dominate developments in the industry over the past five years – not so much because of their direct impact, since they're still done relatively rarely, but because of their indirect impact.

In the case of both drop-downs (e.g., J. Crew, PetSmart, Neiman Marcus, Revlon, Envision, etc.) and non-pro rata uptiers (e.g., Serta, Boardriders, TriMark, Incora, Envision, etc.) this indirect impact comes through ushering in a reimagining of how permissible debt docs can *really* be, and how much the boundaries can *really* be bent before courts begin pushing back (this latter point still mostly being an unknown vis-à-vis non-pro rata uptiers and suddenly much more uncertain with the unfortunate downfall of our old friend Judge Jones who I spent so much time talking about in relation to Serta).

In all of my writing on Serta, Incora, etc. this is something that I've tried to get across: that these two types of solutions have caused a meaningful shift in the Overton window. Today, you're invariably going to pay more attention to if pro-rata sharing provisions can be amended by a simple majority, how much value can be shifted to an unrestricted subsidiary, etc. in assessing the potential solutions available to a company – and, importantly if you're on the buy-side, if you could be caught on the wrong end of a solution.

The new normal is thinking about these solutions in the back of your mind, and this leads to their impact being felt in situations where there's just the *possibility* that they could be effectuated (e.g., leading to more cooperation agreements being signed as creditors eschew undergoing an arms race to offer companies the best non-pro rata solution in favor of working together on more vanilla out-of-court solutions, leading to companies more easily getting amend and extends done through being able to offer lenders valuable non-monetary consideration in the form of tightening up credit agreements to preclude drop-downs or uptiers from occurring in the future, etc.).

Additionally, it's inarguable that the rise of drop-downs and non-pro rata uptiers has inspired the search for other creative solutions – ideally some that, at least superficially, look a little less abrasive to non-participating creditors and thus results in companies incurring less immediate litigation costs. And this search has only been accelerated by the current rates backdrop that has led to a proliferation of stressed companies that need an infusion of liquidity or the ability to refi existing debt coming due but also need to find ways to keep down their cash interest expense – since S + 800 feels a bit different when SOFR is north of 5% as opposed to south of 1%.

Anyway, a new solution has been found – one that, over the past few quarters, has been reproduced with a few tweaks multiple times just as Serta's non-pro rata uptier was reproduced with a few tweaks by Boardriders and TriMark shortly after it was announced.

However, unlike drop-downs or non-pro rata uptiers the solution found isn't *really* that novel. Rather, it's a retrofitting of an old concept – initially popularized a few decades ago by distressed funds – that has been given a new lease on life and will join drop-downs and non-pro rata uptiers as being yet another tool in the toolbox (assuming that it holds up in court once tested, something that only time will tell but that most are bullish on as this "new" solution doesn't hinge on a creative reading of the debt docs or harm non-participating creditors quite as much – at least initially).

NOTE BEFORE BEGINNING

There's a certain level of complexity that's unavoidable in discussing double-dips. I've tried my best (hopefully successfully!) to thread the needle, build up concepts over time through multiple examples, and not make this all *too* confusing or overwhelming.

However, if you're currently preparing for interviews it's important to keep in mind the essentials: the accounting questions, the waterfall questions, the structural subordination questions, the bond math questions, etc. Those are the kinds of questions that will dominate your interviews.

It's certainly impressive to be able to explain (roughly) what drop-downs, non-pro rata uptiers, or double-dips are in an interview *if* the opportunity arises. However, as I stressed in the Serta Postmortem Guide, knowing the granular specifics is well beyond any interviewer's expectations.

It's incredibly unlikely that you're going to be preemptively asked about double-dips – they're the kind of thing that would only come up if *you* initially brought them up (e.g., if you brought them up in response to being asked about a trend you're following, the kinds of solutions available to a stressed company, etc.).

So, knowing the rough mechanics of double-dips is a fantastic way to stand out in interviews and hopefully you find this all interesting. However, if you begin to feel a bit lost in the sauce reading about Trinseo's combined drop-down and double-dip, or about how to determine basket capacity, don't worry about it at all. Please don't think that understanding everything in here is a prerequisite for interview purposes because that couldn't be further from the truth. Read through this if you have the time and just focus on the bigger picture of how double-dips arose, how they're (roughly) structured, and how they make sense for the new-money lenders participating in them.

THE TRADITIONAL DOUBLE-DIP

In the real world, thanks to George Constanza's chip dipping proclivities, the term double-dip has taken on a negative connotation. However, in the world of restructuring the term has anything but a negative connotation. In fact, it has been used for decades to refer to something that, at first blush, seems a little bit like alchemy.

The term "double-dip" refers to a situation where a creditor holding debt that's been issued by a non-guarantor restricted subsidiary or unrestricted subsidiary can end up having a recovery upon the company filing that's around double (or more) that of pari debt issued by some other entity (although the total recovery, in dollar terms, of a creditor benefiting from a double-dip is capped at payment in full – typically just meaning par although there could be a make whole, accrued interest, etc. nudging the total recovery above par).

Functionally, the way this potential doubling of recovery occurs is through the subsidiary-issued debt holders establishing *two* independent allowed claims against the company (ergo, the term double-dip). The first dip arising from an entity, or a series of entities, where value resides providing a guarantee of the subsidiary-issued debt. The second dip arising from the subsidiary upstreaming the proceeds from the subsidiary-issued debt, in the form of an intercompany loan, to an entity where value resides and often where some or all of the company's existing debt has been issued out of in return for an intercompany loan receivable that's then pledged to the double-dip creditors as security for their debt.

So, upon filing, there are two independent allowed claims that redound to the benefit of the subsidiary-issued debt holders: the *direct* claim arising from the guarantee(s) provided and the *indirect* claim arising from the subsidiary separately being able to enforce the intercompany loan against the debtor with any recovery then flowing to the subsidiary-issued debt holders.

Note: The above description is trying to retain as much generality as possible – something that's impossible to do perfectly since double-dips have many permutations as we'll soon discuss. If things seem a bit murky now, it'll all (hopefully!) be cleared up as we move forward. For now, just keep in mind the basic principles: you could find yourself getting a recovery that's around double that of pari creditors upon filing – although the dollar amount of your recovery will be capped at payment in full – and this arises through establishing two independent allowed claims against the debtor (each one of these allowed claims being a "dip", ergo the double-dip name).

Anyway, to avoid ourselves getting too lost in caveats before we even get going, let's put a bit of meat on the bones through a little example. Imagine that we have an entity called ParentCo. It holds all of the company's assets and is the issuer of the company's only debt: a $200mm 1L TL. Because of regulatory reasons or tax reasons or *some reasons* the company created a non-guarantor restricted subsidiary that we'll call SubCo. SubCo then issued $200mm of Senior Secured Notes to some creditors and, as you might expect, the creditors demanded a secured (first-lien) guarantee from ParentCo to make the subsidiary-issued Senior Secured Notes pari with the ParentCo-issued 1L TL.

Now, SubCo was just a shell that was created for *some reason*, and it had no use for the $200mm raised there. In fact, the debt docs governing this $200mm in debt specifically precluded SubCo from engaging in any business activities other than more-or-less servicing its debt.

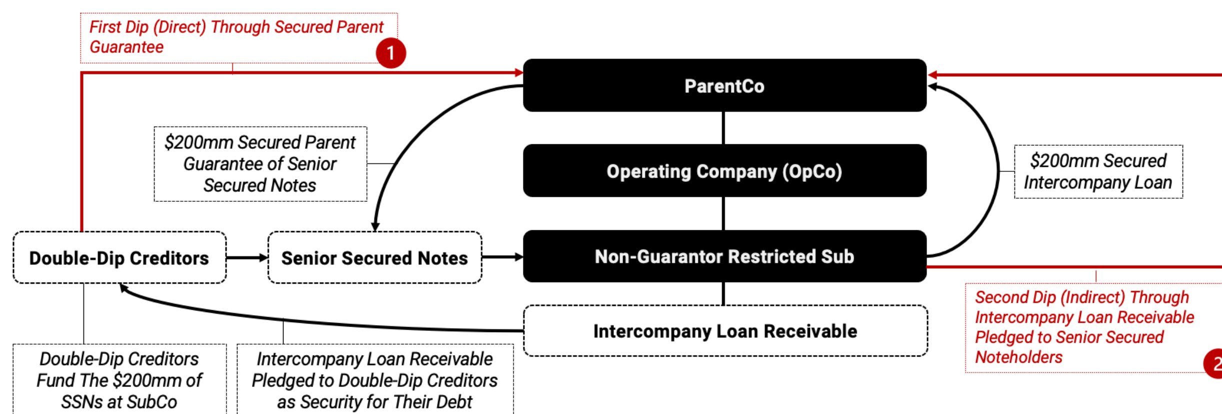
Therefore, SubCo immediately upstreamed the proceeds from its debt issuance to ParentCo through an intercompany loan that was also secured on a first-lien basis and thus resides pari with ParentCo's 1L TL. In return, SubCo received an intercompany loan receivable to the tune of $200mm and this receivable was pledged to the Senior Secured Noteholders as security for their debt. Therefore, SubCo, the erstwhile shell company, now has $200mm in assets (the intercompany loan receivable) and $200mm in liabilities (the Senior Secured Notes).

So, to be clear, before filing ParentCo – the entity in this example that's the issuer of the company's pre-existing debt, has all of the company's assets exclusive of the intercompany loan receivable, etc. – will be regularly paying the intercompany loan and those proceeds will be used by SubCo to pay the Senior Secured Notes. It all just flows through and the rate on the intercompany loan will be exactly the same as the rate on the Senior Secured Notes. (Remember: the only real reason this debt was incurred at SubCo to begin with was for *some* reason that precluded it being incurred as secured debt at ParentCo.)

However, if filing occurs down the road then things get a bit interesting because all of a sudden we're looking at a double-dip situation…

Think about it from the Senior Secured Noteholders' perspective: if filing occurs then the Senior Secured Notes, that have a secured guarantee from ParentCo, will reside pari to the 1L TL at ParentCo. However, the SubCo can separately enforce the intercompany loan against ParentCo that's also been made pari to the 1L TL residing there and the recovery stemming from this will, obviously, flow to the creditors of the SubCo – and the only creditors residing there are the Senior Secured Noteholders.

Therefore, we have two independent allowed claims here that both redound to the benefit of Senior Secured Noteholders but one being direct and one being indirect. First, the direct claim arising from the secured guarantee of the Senior Secured Notes. Second, the indirect claim arising from SubCo's intercompany loan receivable that's been pledged to the Senior Secured Notes. So, effectively, the Senior Secured Noteholders have two bites at the ParentCo apple.



Put another way, if we were to do a little waterfall there would be $600mm of claims that are all residing pari to each other arising from the $200mm 1L TL, the $200mm Senior Secured Notes, and the $200mm Intercompany Loan. It just so happens that $400mm of these claims, in the end, benefit one group of creditors: the Senior Secured Noteholders.

Now, to turn this into more of an interview question, although it would never be asked, let's imagine that the company files and that we apply a 6x multiple to their LTM Adj. EBITDA of $40mm (don't worry about deficiency claim stuff). In other words, let's pretend there's $240mm in distributable value for waterfall purposes. If there weren't a double-dip, and instead the Senior Secured Notes had *only* the secured guarantee, then you'd say there are $400mm in total first-lien claims. So, there'd be a 60% recovery ($240mm / $400mm) for both the 1L TL and the Senior Secured Notes (in other words, $120mm of recovery for each).

However, as mentioned, with the double-dip there are really $600mm in first-lien claims. So, the 1L TL would receive a 40% ($240mm / $600mm) recovery or $80mm. However, the Senior Secured Noteholders would benefit from a 40% recovery on the Senior Secured Notes residing pari to the 1L TL *and* a 40% recovery on the Intercompany Loan residing pari to the 1L TL that'll flow to them through SubCo. Since both of these are $200mm claims, the recovery from each will be $80mm and the total recovery, in the end, for the Senior Secured Noteholders will be $160mm or 80% of the amount initially lent. Therefore, even though the ParentCo-issued 1L TL and SubCo-issued Senior Secured Notes have identical face values and reside pari to each other, the Senior Secured Notes are getting double the recovery due to their multiple (two) allowed claims. Magic.

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In the preamble I alluded to there really being two phases to the history of double-dips. The first phase, encompassing the better part of two decades, is one where the only double-dips that arose did so organically – they were merely a natural consequence of certain companies having cavernous capital structures borne, usually, out of a need to issue debt out of foreign subsidiaries for tax or regulatory reasons (e.g., Lehman, General Motors, etc.).

In other words, it wasn't *really* the intention of these companies to create a double-dip when they were raising debt at some SubCo and most of the holders at the subsidiary level were entirely unaware that there was even the possibility of being able to multiply their allowed claims if the company were to file.

Given this, in the past twenty years many of the old guard of the distressed world (e.g., Appaloosa, Elliott, Redwood, etc.) have tried to find these relatively rare double-dip opportunities out in the wild and take advantage of them.

And there's an obvious reason for doing so: if no one else recognizes that the debt issued by some SubCo could have around double the amount of claims and, by extension, could have around double the potential recovery it otherwise would have then the market is probably pricing the debt as if it has only a single-dip (e.g., pricing based on the assumption of a thirty-cent on the dollar recovery, not up to a sixty-cent on the dollar recovery, etc.). It's been a good trade if you can find it and execute it in size – neither being easy to do.

Anyway, I've talked a bit before about how the announcement of Serta's non-pro rata uptier, to the surprise of many within the industry, caused incredulous indignation outside the industry. It struck many outsiders as fundamentally unfair, on its face, that a simple majority could radically reorientate the priority of those in the minority. It was tantamount to bullying – even if those being bullied weren't the most sympathetic cast of characters.

I can imagine that some reading this may look at double-dips the same way and are wondering how this has all stood up in court over the years. What were the arguments in favor? What were the arguments against? What are the rules of the road, the boundaries that can't be broken? Surely, if there's been a number double-dip situations over the past two decades, *someone* has litigated all of this and *some* precedence has been set. It's not like these are benign situations where no one loses – we just saw in our little waterfall example that the gains in recovery of one party in-court (SubCo's Senior Secured Notes) are per se the losses in recovery of another (ParentCo's 1L TL). This is claim dilution and, just like with all kinds of dilution, if you're the one being diluted you won't be happy! Especially if you didn't realize you would be diluted!

However, I've talked a lot before about how many issues in restructuring that are controversial, contentious, and continually litigated tend to languish in a legal limbo – coming close to the brink of being ruled on, but never being so. And this is because, just as occurred with Apollo's complaint surrounding Serta's use and abuse of their DQ list we talked about in the Serta Postmortem Guide, the issue gets settled before a court has the opportunity to weigh in one way or the other.

This has more-or-less been the case with direct double-dips litigation. There's been a few decisions from courts around the margins but, in the end, settlements usually end up occurring at the eleventh hour. For example, the most famous double-dip involved Lehman Brothers. To reduce a mountain to a molehill here, Lehman Brothers Treasury Co. (LBT), a subsidiary domiciled in the Netherlands, issued around $35bn of Notes that were guaranteed by Lehman Brothers Holdings Inc. (LBHI). Immediately upon issuance, LBT upstreamed the proceeds to LBHI.

Upon filing the LBT Noteholders claimed they had a double-dip with a direct claim arising from the guarantee of the LBT Notes by LBHI and an indirect claim arising from the intercompany loan that was the result of LBT upstreaming the debt issuance proceeds to LBHI. This set off a fire storm and led to LBHI holders advocating for substantive consolidation to, in part, void the double-dip and it looked like this mess was going to be decided by the court.

However, before the final reckoning a settlement was reached. There would be no full double-dip, and there would be no substantive consolidation. Instead, both LBT claims were allowed in the POR *but* a portion of the LBT Noteholders' double-dip recovery would be allocated to LBHI holders.

So, when it was all said and done, those who timed their entry into LBT prior to the double-dip becoming well known, and those who timed their entry into LBHI before they regained leverage in the case through the substantive consolidation push, made historic windfalls (although in Lehman the biggest winners were arguably the advisors who risked nothing and gained nine figures – not bad work if you can get it).

Anyway, it's unfair to say that these organically arising double-dips are entirely untested. There may be a paucity of precedence but there is a kind of tactic approval from bankruptcy courts stemming from PORs getting confirmed that contemplate certain creditors getting the benefit of a double-dip (even if, as in Lehman's case, those creditors don't get *quite* as much recovery as they were initially jockeying for due to a settlement occurring vis-à-vis the double-dip).

For example, in LatAm, a pandemic-era case, a number of distressed funds (e.g., Redwood) successfully argued that they had a double-dip that boosted the recovery of their holdings above pari creditors holding debt that didn't benefit from a double-dip. It's perhaps not surprising then that it would be Redwood that spearheaded the evolution of double-dips this year – sparking an onslaught of transactions with many of the big names in distressed rushing in to participate…

THE EVOLUTION OF DOUBLE-DIPS

In Northern Italy finding white truffles is done the old-fashioned way: you get a hound with a good nose, go marching through the forest for days on end, and, after many false positives, end up finding a few hunks that are worth their weight in gold. It's laborious, inefficient work.

In the last few decades, finding double-dip opportunities has been roughly similar – just swap out the hound with a good nose for a distressed analyst with a masochistic relationship to their work, the old-growth forest of Northern Italy for a stressed company's corporate structure, etc.

Given the relative rarity of double-dip opportunities and how tricky identifying them can be it seems natural to think that if the concept of double-dips has been at least tacitly supported by courts then why go through the rigmarole of finding them out in the wild to begin with? Why should it matter if they arose organically or not? Why not just, like, create them out of thin air?

This can seem to be an obvious thought in light of the drop-downs and non-pro rata uptiers that have occurred in recent years. But this is the rationale behind me going through my whole song and dance about the Overton window in the preamble. There is no reason the evolution of double-dips that we're about to discuss couldn't have happened earlier. It's just that there's been, for lack of a better turn of phrase, an attitudinal shift that's allowed this evolution to occur now -- and, as with all things in finance, once one person does something then everyone piles on.

So, as you've guessed, the evolution of double-dips that began this summer involves companies manufacturing double-dips as part of a new-money transaction – something that participating creditors, obviously, love as it provides better downside protection if the company files in the future (through benefiting from a total claim size that's around double, depending on the transaction structure, the face value of the debt that has the benefit of the double-dip).

The transaction that spurred this evolution was At Home, a sponsor-backed retailer of hokey home décor. They were acquired by Hellman & Friedman a few years ago and pre-transaction their capital structure consisted of a $425mm ABL with $321mm drawn, a $600mm 1L TL with $593mm outstanding, $300mm in Senior Secured Notes, and $500mm in Senior Notes (the 1L TL and SSNs were pari).

Sadly, it appears that the inflatable pumpkin, etc. market has seen better days. This year At Home had modestly negative EBITDA and, through the magic of addbacks, slightly positive Adj. EBITDA. But that's a far cry from the $300mm of both that they did two years ago (although they're expecting that both will rebound next year to over $100mm as freight-disruptions abate, cost reduction initiatives take hold, etc.).

Anyway, they needed some fresh liquidity and to dream up some ideas for doing so they brought in Kirkland & Ellis and PJT. In the end, they settled on a transaction that involved manufacturing a double-dip on a $200mm new-money investment – and it's somewhat natural that they did considering that one of those providing the new liquidity, Redwood, was more than familiar with taking advantage of double-dip opportunities in the wild.

Similar to the first drop-downs and uptiers that occurred, this first manufactured double-dip was relatively straight-forward – not having the bells and whistles that double-dips that have come in the wake of At Home's transaction (e.g., Tinseo and Wheel Pros) have had.

So, let's work through the steps that At Home took to effectuate the transaction. As you go through these steps, keep in mind that we're literally just trying to re-create a "traditional" double-dip that you'd find in the wild – therefore, we're really just working backwards from the end goal of providing creditors participating in the transaction multiple allowed claims if filing occurs.

1 CREATING THE SUBSIDIARY

First, a subsidiary needs to be created. In At Home's transaction, a non-guarantor restricted subsidiary was created, based in Cayman, that we'll call SubCo. To be clear, it was a shell – having no assets and no liabilities. The "restricted" descriptor means that SubCo had to comply with the negative covenants underpinning At Home's existing debt docs, whereas the "non-guarantor" descriptor means that SubCo wasn't a guarantor of any of At Home's existing debt.

You'll recall that I've talked about unrestricted subsidiaries many times before – especially in relation to Serta's transaction and the drop-down that was unsuccessfully pitched. Unlike a non-guarantor restricted subsidiary, an unrestricted subsidiary doesn't need to comply with the negative covenants underpinning a company's existing debt docs *and* doesn't have to guarantee any of a company's existing debt – it's fully outside the restricted group thus the name.

Ideally, you'd rather be spinning up an unrestricted subsidiary to do one of these transactions instead of a non-guarantor restricted subsidiary – and in some cases like Sabre and Trinseo that's been the case. However, the reason you'll see non-guarantor restricted subsidiaries used is due to the underlying debt docs: more specifically, some debt docs precluding restricted group entities from guaranteeing the debt of an unrestricted subsidiary or, more generally, allowing unrestricted subsidiaries to incur debt that is recourse to assets residing within the restricted group (in most situations the restricted group entities are those that have issued most, or all, of the company's existing debt and contain most, or all, of the company's existing assets – so, if you're looking to do a double-dip, you want access to those assets!).

2 ISSUING THE SUBSIDIARY DEBT

Second, with the subsidiary created it now needs to actually issue the debt. In At Home's transaction this was $200mm of 11.5% Secured Private Placement Notes maturing in 2028. Redwood led the way in providing the funding along with a cohort of others that, like Redwood, were pre-existing Noteholders (we'll circle back to this point in a few minutes).

Now, backing up for a second, all debt docs are heavily negotiated and *try* to strike a balance between restricting the company from taking actions that could diminish recoveries for holders while ensuring that the company has the flexibility to manage its affairs. This can most clearly be seen in the capacity that debt docs provide for a company to incur additional debt (e.g., the *priority* it can be incurred at, the *purposes* it can be incurred for, the *type* of entity that can incur it, etc.).

Therefore, to effectuate a double-dip, the company's existing debt docs must allow it to incur the new debt at the subsidiary level *and* guarantee that new debt at the subsidiary level (thereby providing the first dip) *and* permit the intercompany loan from the subsidiary to the operating company that'll be using the funds (thereby providing the second dip). In other words, the existing docs must permit all *three* of these things to manufacture a double-dip.

So, getting back to our second step, we know there needs to be existing capacity under the existing debt docs to incur debt at the subsidiary level. If the subsidiary is an unrestricted subsidiary, then there's no issue with *this* step as the subsidiary isn't subject to the negative covenants of the existing debt docs. Practically this means you can raise as much debt at an unrestricted subsidiary as folks are willing to give you – the trick is figuring out how to provide sufficient value at the unrestricted subsidiary level such that people will actually *want* to put money there. (It's not too enticing to lend to an empty shell that has no recourse to any value!).

This is how many drop-downs fail at the planning stage because the existing docs don't allow enough value to be transferred down to an unrestricted subsidiary to make it worthwhile to pursue. Not to get too off track but this is, in the end, how Apollo, et al. got our maneuvered in Serta: there was only around $675mm in value that could be transferred to an unrestricted subsidiary, so there was a natural binding constraint on how much new-money could reasonably be lent to an unrestricted subsidiary and the amount of debt it'd make sense to exchange over.

Anyway, in At Home's transaction the SubCo was a non-guarantor restricted sub. This means, as discussed, it *is* subject to the negative covenants under the existing debt docs. Therefore, to incur debt at the subsidiary there must be sufficient debt *and* lien capacity, and this capacity must be able to be tapped specifically for the purpose of incurring debt at a non-guarantor restricted subsidiary. The most common baskets that can be tapped are the general debt and lien baskets along with foreign or non-guarantor debt and lien baskets (although others can be available).

This is a huge rabbit hole that I'll try to not go down too far. But think of baskets as being like little carveouts in the debt docs that allow additional debt to be incurred at *some* priority, at *some* type of entity, for *some* purpose. Some baskets will be a flat amount, some will expand or shrink as total assets or EBITDA or some other metric expands or shrinks, some will permit an amount of debt up until some ratio such as leverage or FCCR. The point is that in assessing the viability of most out-of-court solutions, you need to turn to the debt docs and figure out if there's the capacity to do what you want. Some of the baskets won't be applicable to the specific thing you're trying to do, and some of baskets can be added together to get to the capacity desired.

So, if someone is asking, "How much additional debt can a company incur?" it's far too general of a question to really answer. Is the debt going to be secured? Is it going to be structurally senior? Is it going to be used to repay existing debt? Depending on the answer, how much capacity the company has can be wildly different.

Knowing the ins and outs of tallying up capacity, or specific baskets that should be looked to in certain situations, is, to put it mildly, well beyond the scope of what you need to know in interviews. It's just important to bring this all up to reinforce the point that most out-of-court solutions are going to be constrained by the debt docs, and this is true of double-dips too. Although, it should be noted that eventually you'll learn the ins and outs and be putting together slides breaking down the capacity in the docs – albeit with "subject to review by counsel" emblazoned on them since it's counsel that will have the final say, perhaps with some creative interpretation à la Envision.

Note: To maintain the integrity of the double-dip that's being put in place, the debt docs governing the subsidiary-issued debt should ideally be heavily restrictive – precluding additional borrowing at the subsidiary, transferring its sole asset of the intercompany loan receivable, or otherwise doing any business beyond servicing the debt that resides there. The double-dip is predicated, obviously, on diluting the claims of *other* creditors through establishing multiple allowed claims – but double-dip creditors need to be mindful of the tables being turned on them and having value leak from their own subsidiary. You can't just play offense; you need to play a little defense too.

3 GUARANTEEING THE SUBSIDIARY DEBT

In order to create the first "dip" a subsidiary's newly issued debt needs to be guaranteed by entities where (obviously!) some actual value resides. In most situations this will mean a guarantee coming from one entity (or many entities) within the restricted group.

So, for example, in At Home the newly issued Private Placement Notes were guaranteed on a first-lien basis by the At Home ParentCo (At Home Group) and some of its domestic restricted operating subsidiaries thereby making them pari to the pre-existing 1L TL and SSNs.

Philosophically, if we think about what a guarantee *really* is, it's functionally similar to regular-way debt being incurred by the entity providing the guarantee. This is the rationale behind nearly all debt docs treating guarantees as the assumption of additional debt – and, as we discussed above, when you're trying to determine if debt can be incurred at *some* priority, at *some* type of entity, and for *some* purpose you need to turn to the debt docs and look for capacity.

The debt and lien capacity relied on can stem from the general debt and general lien baskets, guarantee-specific baskets (only if the guarantee is to the benefit of a restricted group entity, such as a non-guarantor restricted subsidiary), and the incremental debt basket (although, to be clear, all debt docs are unique snowflakes with a mix of baskets – these are just commonly used here).

Importantly, to create a *secured* guarantee you need both debt *and* lien capacity. The lien capacity being necessary to make the guarantee secured and, as you can imagine, in a double-dip transaction where the company is per se stressed you're going to want a secured guarantee to make sure your new-money is pari to the company's existing secured debt.

(Alternatively, double-dip creditors can have secured guarantees from non-guarantor restricted subsidiaries, thereby giving themselves structurally senior claims on the value residing there relative to the company's existing secured debt, as we'll talk about later with Sabre and Trinseo).

4 CREATING THE INTERCOMPANY LOAN

In order to create the second "dip" the funds raised at the subsidiary-level need to be upstreamed, in the form of an intercompany loan, to some entity (usually that has issued the company's pre-existing secured debt) with the subsidiary then receiving an intercompany loan receivable that, in turn, is pledged to the subsidiary's creditors as security for their debt.

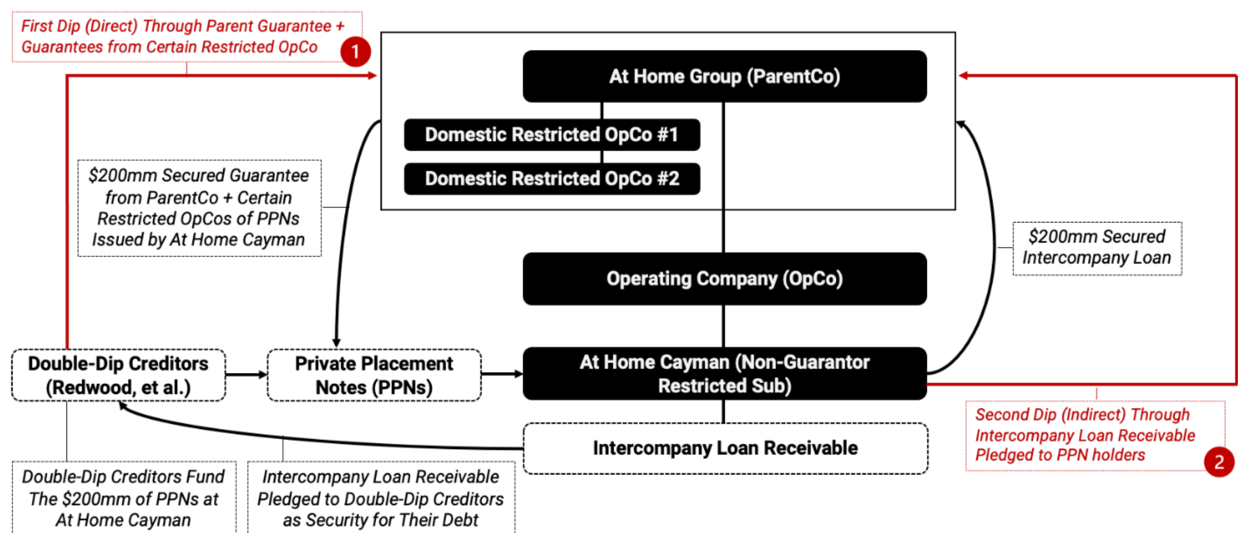
Once again, this requires debt *and* lien capacity under the debt docs with the lien capacity being necessary insofar as you want the intercompany loan to be secured and thereby residing pari to the company's existing secured debt (e.g., in At Home the Intercompany Loan was from At Home Cayman to At Home Group and was made pari to At Home Group's existing first-lien debt).

Therefore, in determining if capacity exists, you'll go back to the same well: looking at general debt and lien baskets, the incremental (secured) debt basket, etc. if there's remaining capacity there. However, in many double-dip transactions (e.g., Sabre and Trinseo) the intercompany loan proceeds are used specifically to repay existing debt – and, in this case, permitted refinancing baskets can be used that, to simplify, allow debt to be refinanced by similar debt (e.g., secured debt being refinanced by a secured intercompany loan à la Trinseo).

In the end, the lynchpin of making one of these Double-Dip 2.0 transactions work is making sure that the intercompany loan resides pari to the company's pre-existing secured debt. Technically, if you wanted, both the double-dip debt guarantee and intercompany loan could be unsecured and in that case you wouldn't need the existing docs to provide lien capacity (they'd just need to provide debt capacity, and this is invariably more ample). But if you're looking at a stressed company that's desperate for liquidity or can't do a regular-way refi of its existing debt then you're not liable to get much recovery if your claims are behind a wall of pre-existing secured debt!

5 WRAPPING UP AT HOME

So, we've briefly covered the mechanics of manufacturing double-dips and how, in the case of At Home, Redwood, et al. have turned a $200mm new-money investment at SubCo into $400mm of first-lien claims if filing occurs (although remember that the maximum recovery of the PPNs is capped at payment in full). Here's how you can visualize things…

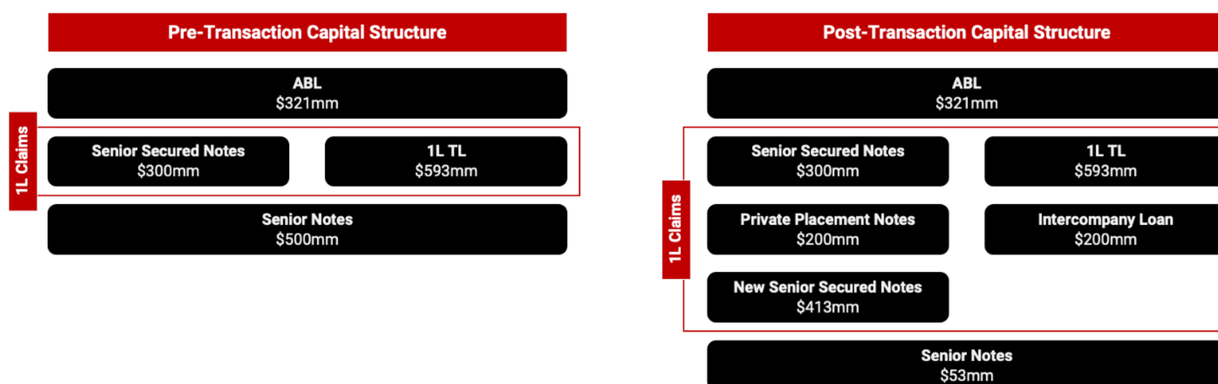


But let's take a wider lens here and bring things full circle. You'll recall that I mentioned some of the new-money participants were pre-existing Senior Noteholders – residing pre-transaction behind a wall consisting of the $321m ABL, $593mm 1L TL, and $300mm Senior Secured Notes. Now, if you're providing new money to a struggling company, and you also happen to hold some lower part of the capital structure that's inline for a de minimums recovery, then you'll want to try to salvage some value – and one way you can do that is through trying to roll up your holdings as part of the transaction to a higher position in the capital structure.

So, that's exactly what was done here. In conjunction with the $200mm new-money financing, $447mm of the pre-existing Senior Notes were exchanged into $413mm of new Senior Secured Notes that reside pari to the other At Home first-lien claims. The rate on the Senior Notes and these new Senior Secured Notes is the same (7.125%) but there is the ability to toggle the new Senior Secured Notes to PIK at 8.625%. Therefore, this little exchange created a bit of discount capture, since the exchange happened below par, and in the future At Home will be able to conserve some cash if they want to utilize the PIK toggle.

So, if we're thinking about the waterfall, there's the $321mm ABL; the pre-existing $300mm Senior Secured Notes, the $593mm 1L TL, the $200mm Private Placement Notes, the $200mm Intercompany Loan, and the new $413mm Senior Secured Notes that are all pari; and then there's the lowly $53mm of left-behind Senior Notes that weren't allowed to participate in the exchange.

Put another way: pre-transaction there were $893mm of first-lien claims and now there are $1,706mm – not something that the pre-existing 1L TL and SSNs are too happy about, even if the reason for the claim dilution is, in part, the new-money investment that was desperately needed.



THE BENEFITS OF DOUBLE-DIPS

Similar to drop-downs and non-pro rata uptiers, double-dips won't be able to be done by every company under stress. It all comes down to the docs: if there's not sufficient basket capacity to incur the debt at the subsidiary *and* guarantee that debt on a secured basis *and* put in place the secured intercompany loan then the double-dip will be a non-starter (unless the transaction is being done by a majority of *existing* lenders, so the docs can just be amended to effectively add in the capacity as was done in Wheel Pros…).

Regardless, many will be able to do a double-dip, and there's been a narrative develop over the summer that they'll somehow replace drop-downs and non-pro rata uptiers. However, this is overstating the case for them. There will be times when a double-dip makes the most sense, and

there will be times when a drop-down or non-pro rata uptier makes the most sense. Additionally, there will be times when a combination of these three solutions makes the most sense (e.g., Tinseo's combined drop-down and double-dip, Envision's combined drop-down and uptier, etc.).

But, to be clear, there are undoubtably benefits to double-dips, so let's talk about a few of them…

First, there's a certain innocuous quality to double-dips. Unlike in drop-downs or non-pro rata uptiers where the full weight of the transaction is immediately felt by non-participating creditors, in double-dips the impact is primarily felt by those "harmed" only upon filing – when suddenly they find themselves diluted down by the multiplicative claims arising from the double-dip.

The natural extension of double-dips appearing to be more innocuous when they're executed is that there's less immediate litigation costs. This stands in sharp contrast to drop-downs and non-pro rata uptiers where – as we've discussed ad nauseam in relation to Incora, Serta, etc. – there's nearly always going to be some level of immediate litigation coming from those creditors who've been left out in the cold (although this isn't always the case, Envision was a masterclass in doing follow-on transactions to diminish the amount of litigation that would eventuate).

Additionally, since most (not all!) doing these more "creative" transactions are sponsor-backed, this lack of litigation is valued not just from a cost-savings perspective but from a reputational perspective. This isn't because sponsors are benevolent but because many creditors in one PortCo's capital structure are going to be in other, or future, PortCo capital structures. So, all else equal, sponsors would rather not make creditors too mad as that could result in a slightly higher cost of debt in future buyouts (e.g., the so-called Apollo premium). Personally, I think this is all heavily overstated as a rationale for doing a double-dip as opposed to a more aggressive alternative but this is a narrative you'll often hear, so now you've heard it too.

Second, in theory there's no need for a new-money lender in a double-dip to be an existing creditor. The new-money at the subsidiary level could be funded by anyone so long as they liked the terms of the debt and felt comfortable with their enhanced downside protection (in other words, the enhanced level of recovery they'd get upon filing through having the double-dip).

This stands in contrast to non-pro rata uptiers where, by definition, you need a simple majority of the relevant *existing* creditors in order to amend the docs to effectuate the transaction. So, there's not *that* much leverage for the company as the only ones who can do the uptier are some combination of existing creditors that can form a simple majority. In fact, the only real leverage of the company comes through threatening to try to do another type of transaction, instead of the uptier, if those pitching the non-pro rata uptier don't agree to a lower exchange rate or better terms (from the company's perspective) on the new super priority debt.

Third, the pricing of the double-dip debt (e.g., the subsidiary-issued debt that benefits from the double-dip upon filing) is usually pretty favorable considering the stressed nature of the company. For example, At Home's Private Placement Notes have an interest rate of 11.5% and ended up pricing at around a 13% yield. Not exactly cheap. But considering that the pre-existing Senior Secured Notes had a yield well into the 20s pre-transaction (remember: they have a first-lien claim too) the pricing was about as good as could be hoped for from the company's perspective.

The rationale behind the double-dip debt being relatively cheap for the company is pretty straight-forward: the downside risk to holders of this debt is significantly diminished due to having around double, give or take, the allowable claims relative to the amount lent if the company files.

Think about it this way: imagine you're looking at a piece of debt and think the company could file in the next two or three years. Now let's imagine that through your genius analysis you think the recovery you'll get upon filing is around 30-40%. In this case, the size of the coupons you're clipping over these two or three years pre-filing better be large or, alternatively, the entry point you're getting into the debt at better be pretty low in order to make a reasonable return. But if there's a double-dip then the recovery you're assuming that you'll get if filling occurs will be significantly higher (by virtue of the multiplicative claims) than it otherwise would be so you don't need the coupons you're clipping to be quite as large, or the entry point into the debt to be quite as low, to arrive at the same level of return or better.

Therefore, for a company struggling in the current rates environment, the double-dip is a valuable *non-monetary* form of compensation to give holders. In other words, the company doesn't need to provide holders the same upside pre-filing (through high coupons or a low entry point) because the company is manufacturing a better downside for holders through a higher recovery than pari creditors post-filing.

Fourth, in the same way that drop-downs and non-pro rata uptiers can result in significant discount capture through having existing holders exchange their debt below par, so too can double-dips as part of the broader transaction (or as a direct part of it, à la Wheel Pros). In At Home this occurred, as we've already discussed, through $447mm of the Senior Notes rolling up into $413mm of the new Senior Secured Notes – thereby netting a nice little discount capture.

Additionally, it's important to keep in mind that a company may look toward a more creative transaction not only to bring in new liquidity but to effectively refi or otherwise reconstitute debt through an exchange. For example, in Trinseo the blended double-dip and drop-down transaction was used to take out its remaining $660mm TLB due in 2024 and over three-quarters of its Senior Unsecured Notes due in 2025. Thereby pushing back maturity walls and giving itself some much needed breathing room (although it'll still have to deal with those Unsecured Notes left behind).

In At Home the challenge was less about maturity walls and more about the need to bring in liquidity and, if possible, keep cash interest expenses as low as possible. To this end, the Senior Notes exchanged into Senior Secured Notes had an identical cash rate. However, unlike the Senior Notes, the SSNs included a PIK toggle thereby providing more cash interest breathing room if needed in the future. So, this effective reconstituting of the Senior Notes into a PIK instrument as part of the broader transaction provides the company a bit more optionality moving forward.

THE EXPANSION OF DOUBLE-DIPS

Whenever a new type of solution comes along a familiar script occurs: the first transaction is relatively vanilla and then, as the transaction is digested, a slew of similar transactions occur that are expanded and enlarged in increasingly novel (read: aggressive and/or complicated) ways.

If you've read all my writing on non-pro rata uptiers over the years, then this script will be familiar. Serta's PTL Lenders exchanged their existing holdings well below par, thereby creating a huge discount capture for the company. But then, just three months later, Boardriders decided to push the envelope a bit more through announcing their own transaction that was similar in style but with participating holders exchanging their existing debt at par (a better deal for participating holders and causing much more indignation among non-participating holders given that the debt being exchanged was trading well below par).

More recently, if you've read my posts on Incora, you'll recall that things were taken a step further with the Unsecured Notes rolling up above pre-transaction Senior Secured Notes at par – despite the Unsecured Notes trading *way* below par – to the direct benefit of the sponsor that had been buying up some Unsecured Notes themselves. Now *that's* aggressive.

Anyway, the same script has played out vis-à-vis double-dips. Something that shouldn't be too surprising given that double-dips, unlike drop-downs or non-pro rata uptiers, are a bit more flexible and can be more easily combined with other types of solutions.

1 SABRE

Immediately following At Home, we had Sabre that involved a larger new-money component and a bit more complicated of a structure (there was another proposal from existing lenders on the table, but the company opted to go the double-dip route after the double-dip proponents lowered the interest rate on the new-money and upped its size). PWP advised Sabre.

The transaction involved a group led by Centerbridge – with Oaktree, Oak Hill, and JPM tagging along in much smaller size – providing a $700mm Term Loan to an unrestricted subsidiary that the company had spun up. The first dip is effectuated through a secured guarantee of the Centerbridge, et al. Term Loan being provided by a few different entities: the UnSub's direct parent and a host of non-guarantor restricted subsidiaries (e.g., the UK, Australian, etc. foreign subsidiaries of Sabre). However, due to capacity constraints in the pre-existing debt docs the foreign sub guarantees are capped at $400mm.

The second dip is effectuated through the intercompany loan – arising from the proceeds of the issuance at the UnSub being upstreamed to Sabre GLBL – being secured on a first-lien basis. Sabre GLBL is the entity that issued the company's pre-existing secured debt, so the intercompany loan resides pari to that debt. The intercompany loan proceeds were then utilized to repay, at par, $670mm of the company's outstanding 9.250% Senior Secured Notes maturing in 2025 (leaving behind around $105mm to deal with another day).

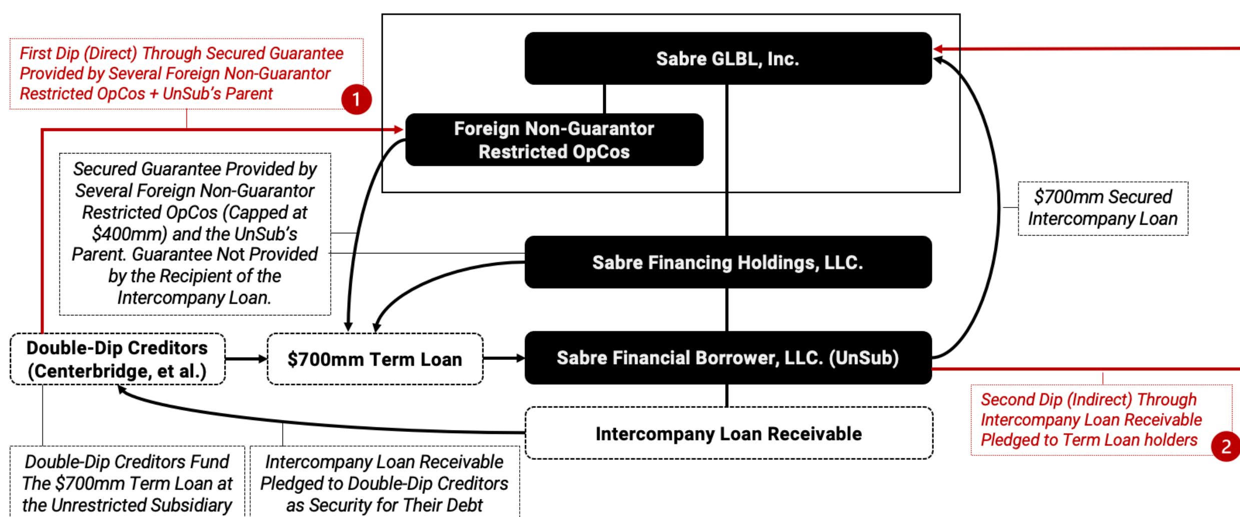
So, in Sabre we still have a recognizable double-dip (e.g., the new-money creditors are going to have two independent allowed claims if the company files in the future). However, there are some things that make it distinct from At Home's transaction…

- First, we see the use of an unrestricted subsidiary to issue the double-dip debt as opposed to a non-guarantor restricted subsidiary as in At Home.
- Second, we see that the guarantees provided to the benefit of the Centerbridge, et al. Term Loan are *not* coming from the same restricted group entities that benefited from the intercompany loan proceeds – instead, as illustrated in the graphic below, the guarantees come from a hodgepodge of foreign subs at a capped amount due to the debt docs not providing the capacity to provide secured guarantees equivalent to the Term Loan size. This stands in contrast to At Home where there was a circular flow with At Home Group providing a secured guarantee of the PPNs *and* At Home Group being the recipient of the secured intercompany loan, thus making the PPNs and intercompany loan reside pari to the company's existing first-lien debt (e.g., the pre-existing SSNs and 1L TL).
- Third, the double-dip in Sabre had a fundamentally different purpose than in At Home. In Sabre, we see the double-dip being used as a creative way to take out existing debt. Whereas in At Home we see the double-dip being used to obtain fresh liquidity.

- Fourth, the terms of the Centerbridge, et al. Term Loan and the resulting intercompany loan are identical, so the cash just flows through. However, the terms of both are, uh, aggressive. The rate is determined retrospectively, every three months, based on the highest YTM of the company's other secured debt *plus* 25bps if the company elects to pay cash interest or 175bps if the company elects to do PIK. The interest rate floors (e.g., the minimum amount of interest, even if the company's pre-existing secured debt suddenly has much lower yields due to the company turning things around) are 11.50% for cash interest and 13.00% for PIK interest. The interest rate ceilings (e.g., the maximum amount of interest, irrespective of the yields on pre-existing secured debt) are 17.50% for cash interest and 19.00% for PIK interest. Both the TL and intercompany loan mature in Dec '28.

Note: The terms of the new-money are a classic Centerbridge concoction and are predicated on extracting as much as possible – in either cash or, if PIK is elected, additional claims – before the company files. Because even though this transaction helps in the short-term there are other looming maturity walls to deal with and the terms of this debt aren't exactly charitable. So, Centerbridge structured the transaction such that if the company manages to get through the next few years without filing then, like, that's fantastic – they'll still be clipping a *minimum* of 11.50% and likely more. But the transaction's real intent is to make sure that if filing occurs the recovery, in conjunction with the pre-filing coupons clipped, still nets out a healthy return.

Note: Centerbridge provided $542mm of the new-money with Oaktree making up the majority of the remainder through providing $84mm. So, this is why I'm saying this is a classic Centerbridge concoction (which, to be clear, isn't a derisive remark but rather a high compliment!).



2 TRINSEO

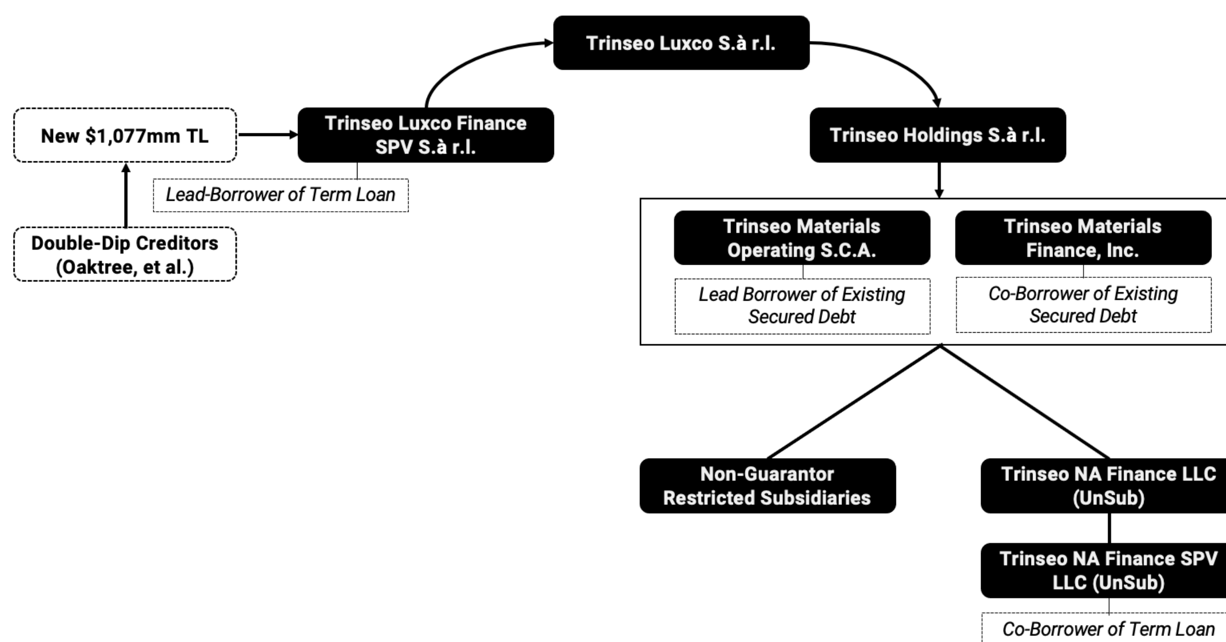
In Trinseo the new-money became even bigger, and the transaction structure a bit more complicated. Centerview had the debtor-side mandate, Evercore had a creditor-side mandate working with an ad hoc group of lenders, and PWP had a creditor-side mandate working with an ad hoc group of noteholders.

The impetus for needing to do something was that the company had a ~$660mm TLB coming up in September of 2024 and $500mm of Senior Unsecured Notes coming up in September of 2025.

Plus, even though their $375mm Revolver was undrawn and maturing in May of 2026, it had a springer: meaning that if the TLB was still outstanding three months prior to its maturity, June of 2024, then the Revolver maturity would spring forward to that date. So, the aim here was to craft a transaction that'd push these maturity walls back – but given around $170mm of LTM Adj. EBITDA and around ~$2,200mm of net debt, some creativity would have to be used. (As illustrated in the cap table to follow, Trinseo is anticipating a huge rebound in Adj. EBITDA next year that would put it on a much more stable footing, so we'll see if that really materializes or not…).

Ultimately, the transaction crafted was a blended double-dip and drop-down with a new lender group – consisting of Oaktree, Apollo, and Angelo Gordon – providing a $1,077mm Term Loan maturing in May of 2028 to two newly created subsidiaries (Trinseo Luxco Finance SPV S.à r.l. as Lead Borrower and Trinseo NA Finance SPV LLC as Co-Borrower).

Note: Trinseo Luxco Finance SPV S.à r.l. *isn't* an unrestricted subsidiary. However, it's a subsidiary of Trinseo Luxco S.à r.l., the Trinseo ParentCo, not a subsidiary of the operating entities that have actually issued the company's pre-existing debt *or* a subsidiary of the parent entity that's a guarantor of the company's pre-existing debt (Trinseo Holdings S.à r.l). Therefore, Trinseo ParentCo can be thought of as residing above the existing restricted group and thus its subsidiaries are not restricted by the negative covenants of the company's pre-existing debt docs. Trinseo NA Finance SPV *is* an unrestricted subsidiary so, as we've discussed before, it's also not restricted by the negative covenants in the debt docs governing the company's existing debt. So, this is a long-winded way of saying that the entities borrowing the Term Loan both have the ability to incur this debt without using the basket capacity found in the company's existing debt docs.



So, moving on to the transaction itself, the drop-down element comes into play because the company transferred its Americas Styrenics LLC business (more specifically, its 50% stake in the business since it's a joint-venture with Chevron) that's worth around $500mm down from the restricted group to one of the new subsidiaries (Trinseo NA Finance SPV) that this new lender group will now have a first-lien claim on. (The Styrenics business is currently undergoing a sale process and all proceeds from the sale must be used to repay the Oaktree, et al. Term Loan).

The double-dip element comes into play because the new lender group benefits from i) various guarantees from non-guarantor restricted subsidiaries, likely capped at around $352mm for similar reasons as Sabre's guarantees were capped, along with guarantees from the parent entities of the subsidiaries created to facilitate the transaction and ii) the pledge of intercompany loan receivables arising from the intercompany loans we'll talk about more in a second.

I don't want to get too off track, but let's talk briefly about how the company only has the ability to provide $352mm of secured guarantees assuming that they're coming from non-guarantor restricted subsidiaries (the details of the secured guarantees and their cap aren't public yet). Remember: to provide a *secured* guarantee you need debt *and* lien capacity, and to find that you need to look at the underlying debt docs. As mentioned, the first thing you'll look to are the general debt basket and general lien basket. The former had about $176mm in capacity and the latter had around $67mm, so if we're only looking at these two baskets in isolation there was only the ability to provide $67mm worth of *secured* guarantees (as the lien capacity is the binding constraint here on providing a *secured* guarantee or incurring any other form of *secured* indebtedness).

However, there's also a specific non-guarantor debt basket and non-guarantor lien basket, with the former being $176mm and the latter allowing lien capacity up to the amount of applicable debt capacity the company has so long as the liens are against *non-guarantor* assets (e.g., assets residing within non-guarantor restricted subsidiaries, practically meaning not the entities that have issued or guaranteed the company's existing debt). Therefore, the total debt capacity available to provide a secured guarantee to debt issued out of a non-guarantor restricted subsidiary in this case was the $176mm from the general debt basket *and* the $176mm from the non-guarantor debt basket, with the lien capacity coming exclusively from the non-guarantor lien basket. This is how we get to the roughly $352mm cap on the level of secured guarantees.

Note: The general debt basket was the greater of $140mm and 5.25% of total assets, the general lien basket was the greater of $60mm and 2.00% of total assets, and the non-guarantor debt basket was the greater of $125mm and 5.25% of total assets. Given that the total assets on the company's balance sheet in the quarter prior to the transaction were $3,355.00, this is how we arrive at $176mm, $67mm, and $176mm, respectively. (Non-Loan Party = Non-Guarantor).

(r) Indebtedness of a Non-Loan Party which, when aggregated with the principal amount of all other Indebtedness incurred pursuant to this clause (r) and then outstanding, does not exceed an aggregate principal amount equal to the greater of (x) $125,000,000 and (y) 5.25% of Total Assets, in each case determined at the time of incurrence, and any Permitted Refinancing thereof;

(s) Indebtedness which, when aggregated with the principal amount of all other Indebtedness incurred pursuant to this clause (s) and then outstanding, does not exceed the greater of $140,000,000 and 5.25% of Total Assets, in each case determined at the time of incurrence, and any Permitted Refinancing thereof;

(ff) other Liens with respect to property or assets of the Lead Borrower or any of its Restricted Subsidiaries securing obligations in an aggregate principal amount outstanding at any time not to exceed the greater of $60,000,000 and 2.0% of Total Assets, in each case determined as of the date of incurrence; and

(w) Liens on property of any Non-Loan Party, which Liens secure Indebtedness of the applicable Non-Loan Party permitted under Section 7.03 or other obligations of any Non-Loan Party not constituting Indebtedness;

Anyway, as you can tell the Trinseo transaction is a bit of a grab bag because, given the size of the Term Loan, the company didn't have the capacity to do a "clean" double-dip (e.g., just have a non-guarantor restricted subsidiary or unrestricted subsidiary issue a $1,077mm term loan, have that debt guaranteed on a secured basis by restricted group entities, and then put in place a secured intercompany loan that would also reside pari to the company's secured debt).

So, this is the rationale behind blending in the drop-down component -- basically saying to participating lenders, "We can't give you regular-way secured guarantees on the *entire* billion-dollar Term Loan but we *can* put this valuable business, worth around $500mm, down at the UnSub level for you *and* give you $352mm of secured guarantees from a smattering of non-guarantor restricted subs. It's a bit of a hodgepodge of stuff but the outcome is close to the same!

In other words, these two things, in conjunction with the secured intercompany loans, will still result in you having a much better recovery (double-ish?) relative to existing secured creditors!”

However, an initial hiccup in the planning stage of the transaction was that, well, the debt docs didn’t just not provide the capacity to provide secured guarantees of the entire Term Loan provided by Oaktree, et al. but the debt docs also didn’t provide the capacity to transfer the entire Americas Styrenics business to the unrestricted sub! In other words, even if the Term Loan could be incurred, and the secured intercompany loan made, the second leg of the double-dip – that involved providing value through regular-way guarantees and the drop-down that, when taken together, come close to the size of the face value of money lent – wasn’t looking possible.

Note: In figuring out the amount of value that can be transferred down to an unrestricted sub the most common baskets you’ll look to in the debt docs are the general investments basket, investments in unrestricted subsidiaries basket, investments in similar businesses basket, and general restricted payments basket (although not all of these are per se present in any given credit agreement, and there can be additional baskets that can be used, or reconstituted, to effectuate a drop-down like the general prepayments basket, etc.).

Note: In Trinseo’s case the baskets that could be tapped to do the drop-down were the general restricted payments basket, general investments basket, and investments in similar businesses basket. These were the greater of $125mm and 4.25% of total assets, the greater of $120mm and 5.0% of total assets, and the greater of $50mm and 2.0% of total assets, respectively, in both the credit agreement and indentures. Therefore, since the total assets in the quarter prior to the transaction were $3,355.00, we arrive at $377mm of total transfer capacity – a value around $125mm less than the drop-down of Americas Styrenics would require. Below are the credit agreement excerpts, followed by the matching 2025 Senior Notes indenture excerpts…

(g) the Lead Borrower and its Restricted Subsidiaries may make Restricted Payments in an aggregate amount not to exceed (x) the greater of $125,000,000 and 4.25% of Total Assets, as determined at the time of such Restricted Payment (*less* the amount of any prepayments, redemptions, purchases, defeasances and other payments in respect of Junior Financings in reliance on the dollar amount set forth in Section 7.13(a)(vi)) plus (y) the Cumulative Credit at such time (provided that with respect to any Restricted Payment (other than a Restricted Investment) made out of amounts under clause (a) of the definition of “Cumulative Credit” pursuant to this clause (y), no Event of Default has occurred and is continuing or would result therefrom and the Borrowers, immediately after giving effect to such Restricted Payment on a Pro Forma Basis, could incur $1.00 of additional Permitted Ratio Debt);

(u) additional Investments having an aggregate fair market value, taken together with all other Investments made pursuant to this clause (u) that are at that time outstanding, not to exceed the greater of $120,000,000 and 5.0% of Total Assets (with the amount of Total Assets being measured at the time such Investment is made); provided that if such Investment is in Equity Interests of a Person that subsequently becomes a Restricted Subsidiary, such Investment shall thereafter be deemed permitted under clause (a) or (b) above and shall not be included as having been made pursuant to this clause (u);

(b) Investments in (i) a Similar Business taken together with all other Investments made pursuant to this clause (b)(i) that are at that time outstanding, not to exceed the greater of (x) $50,000,000 and (y) 2.0% of Total Assets (with the amount of Total Assets being measured at the time such Investment is made) and (ii) a Person if such Person is engaged in a Similar Business and will, upon the making of such Investment be merged, consolidated or, otherwise combined with or into, or transfers or conveys substantially all of its assets to the Lead Borrower or a Restricted Subsidiary; provided that any Investment pursuant to this clause (b)(ii) made by the Loan Parties in Persons that do not merge, consolidate or otherwise combine with or into, or transfer or convey substantially all of their assets to, the Loan Parties contemporaneously with such Investment shall not exceed (when added to the aggregate amount of Investments made by any Loan Parties in Persons that are not Loan Parties (or that will not contemporaneously with such Investment become Loan Parties) pursuant to clause (a) above) an aggregate amount outstanding at any time equal to the greater of (1) $100,000,000 and (2) 4.25% of Total Assets (with the amount of Total Assets being measured at the time such Investment is made);

(16) so long as no Event of Default has occurred and is continuing (or would result therefrom), Restricted Payments (including loans or advances) in an aggregate amount outstanding at the time made not to exceed the greater of $125.0 million and 4.25% of Total Assets (with the amount of Total Assets being measured at the time such Investment is made);

(21) additional Investments having an aggregate fair market value, taken together with all other Investments made pursuant to this clause (21) that are at that time outstanding, not to exceed the greater of $120.0 million and 5.0% of Total Assets (with the amount of Total Assets being measured at the time

(2) (a) any Investment in a Similar Business taken together with all other Investments made pursuant to this clause (2) not to exceed the greater of (i) $50.0 million and (ii) 2.0% of Total Assets (with the amount of Total Assets being measured at the time such Investment is made) and (b) Investments in another Person if such Person is engaged in any Similar Business and as a result of such Investment such other Person is merged, consolidated or otherwise combined with or into, or transfers or conveys all or substantially all its assets to, the Company or a Restricted Subsidiary;

So, to be able to do the drop-down some new capacity had to be found – or manufactured – and the intercompany loan resulting from the new Term Loan provided by Oaktree, et al. did just that by being structured into two tranches: Tranche A of $129mm and Tranche B of $948mm.

The Tranche A Term Loan of $129mm flowed from Trinseo Luxco Finance SPV (the Lead Borrower referenced earlier) to its parent (Trinseo Luxco S.à r.l.). This parent entity wholly-owns Trinseo Holdings S.à r.l., the parent guarantor of the company’s existing secured debt. So, upon Trinseo Luxco S.à r.l. receiving the funds, it turned around and made an *equity* contribution to

Trinseo Holdings S.à r.l. to the tune of $125mm that was then passed on to the Trinseo Lead Borrower (meaning, the entity that actually has issued the company's existing secured debt, Trinseo Materials Operating S.C.A.).

> (k) Equity Contribution. The Administrative Agent and the Lenders shall have received a certificate duly executed by a Responsible Officer of the Parent certifying that with the proceeds of the Tranche A Term Loans, the Lead Borrower will immediately make the Intercompany Parent Loan to Parent, and immediately thereafter, Parent will make an equity contribution in an amount not less than $125,000,000 to Trinseo Holdings, and Trinseo Holdings will immediately thereafter contribute the same to Trinseo Lead Borrower, which equity contribution shall be designated as an "Excluded Contribution" (as such term is defined in the 2025 Senior Indenture and the 2029 Senior Indenture) for purposes of the 2025 Senior Indenture and the 2029 Senior Indenture (the "Equity Contribution").

So, basically, the $129mm Tranche A Term Loan goes up the ladder to the parent, and the parent then uses the funds received, after adjusting for some fees, to make a $125mm equity contribution that flows down until hitting the entity that actually has issued the company's existing debt. The purpose behind this structuring is that the $125mm equity contribution led to a one-to-one increase in restricted payments capacity that was sufficient to provide the total capacity necessary to be able to transfer the Americas Styrenics LLC business down to the UnSub (as detailed above, previously there was around $377mm of transfer capacity, so the $125mm increase got it to the ~$500mm that was needed as the business was independently assessed as being worth ~$500mm). Put another way, the intercompany loan contribution to one entity was transformed into an equity contribution to another so that the drop-down could now proceed.

Now the lenders (Oaktree, et al.) still get an intercompany loan receivable here – but, unlike in past transactions, the intercompany loan is not residing pari to the company's pre-existing secured debt. Because remember the intercompany loan was to Trinseo Luxco S.à r.l., the *parent* entity of the *parent* guarantor of the company's existing debt, not to the pre-existing Trinseo Lead Borrower and Trinseo Co-Borrower that issued the company's pre-existing secured debt. Functionally, this is much less valuable than having a secured claim residing pari to the company's pre-existing secured debt. However, this structuring enabled the drop-down (that provides lots of value to Oaktree, et al.) and the much larger Tranche B Term Loan we're about to discuss is a normal secured intercompany loan residing pari to the company's pre-existing secured debt. Plus, there are all the guarantees from non-guarantor restricted subs and the parent entities of the Lead Borrower and Co-Borrower backing the Term Loan provided by Oaktree, et al. so it's well protected even if the intercompany loan receivable stemming from the Tranche A Term Loan that's been pledged to them isn't likely to be too valuable upon filing.

The $948mm Tranche B Term Loan is much less complicated. Just like Tranche A, it was issued out of Trinseo Luxco Finance SPV S.à r.l. However, it immediately flowed to the existing restricted group entities that issued the company's existing secured debt (e.g., the Trinseo Lead Borrower, Trinseo Materials Operating S.C.A., and the Trinseo Co-Borrower, Trinseo Materials Finance, Inc.). This intercompany loan tranche was structured as $268mm in Incremental Term Loans, utilizing a portion of the $385mm in incremental debt capacity under the debt docs, and $680mm in Refinancing Term Loans, utilizing the permitted refinancing capacity under the debt docs. Therefore, this intercompany loan tranche was secured (e.g., residing pari with the company's existing secured debt) and the resulting intercompany loan receivable was pledged to the Term Loan lenders (Oaktree, et al.) as security.

> (B) together with the Incremental Term Loans made and Incremental Revolving Credit Commitments established under such Incremental Amendment, the aggregate principal amount of Incremental Term Loans made and Incremental Revolving Credit Commitments established under this clause (B) (plus Incremental Equivalent Debt incurred in reliance on clause (i)(B) of the proviso of Section 2.16(h)) does not exceed the sum of (i) $385,000,000 plus (ii) the principal amount of any voluntary prepayments of Term Loans (limited, in the case of Incremental Term Loans, to the principal amount of voluntary prepayments of Incremental Term Loans incurred pursuant to the preceding clause (i)) (other than to the extent made with the proceeds of Indebtedness (other than the incurrence of Revolving Credit Loans or extensions of credit under any other revolving credit or similar facility)); provided that it is understood that (1) Incremental Term Loans and Incremental Revolving Credit Commitments may be incurred under either clause (A) or clause (B) as selected by the Lead Borrower in its sole discretion, including by designating any portion of Incremental Commitments in excess of an amount permitted to be incurred under clause (A) at the time of such incurrence as incurred under clause (B); and

So, in the end, we still have $1,077mm worth of intercompany loans here it's just that they were broken into two tranches that followed two different paths: $948mm sent immediately to restricted group entities that's secured on a pari basis with the existing secured debt of the company, and $129mm sent to a parent entity that turned it into an equity contribution that meandered its way down to the restricted group to open up the requisite basket capacity to complete the drop-down of the Americas Styrenics business into an unrestricted sub (keep in mind, the unrestricted sub the Americas Syrenics business is dropped into is Co-Borrower of the Oaktree, et al. term loan).

Anyway, I know this is a lot of entity names and terms flying around, and rest assured this is all *lightyears* beyond what you need to know. But the *real* point of going through all of this is merely to illustrate that Trinseo represents a bit more of a grab bag than prior transactions, and this was strictly required to get the transaction done in the size that it was done at. It's not a "clean" double-dip, because one couldn't be manufactured due to the restrictions of the debt docs.

So, to recap, a group of lenders (Oaktree, et al.) provided a $1,077mm Term Loan at SOFR + 8.5% (with the ability to do SOFR + 4.25% cash interest plus 5.25% PIK interest in the first two years). This Term Loan had two borrowers, neither being restricted by the existing debt docs: the Lead Borrower, Trinseo Luxco Finance SPV S.à r.l., and the Co-Borrower, Trinseo NA Finance SPV LLC.

This former entity, Trinseo Luxco Finance SPV, used the proceeds to issue two intercompany loans that both, eventually, ended up benefiting the Trinseo Lead Borrower and Trinseo Co-Borrower (Trinseo Materials Operating S.C.A. and Trinseo Materials Finance, Inc., respectively) These are the two entities that issued Trinseo's existing secured debt and actually, like, have most of the company's assets and stuff (although, remember, some of the assets reside in non-guarantor restricted subs and this is where the capped secured guarantees come into play).

Now, the first intercompany term loan, the $129mm Tranche A Term Loan, through a series of twists and turns discussed above, ended up becoming a $125mm equity contribution (excluded contribution) at Trinseo Materials Operating S.C.A. This was strictly necessary to boost up the capacity to allow for the transfer of the Americas Syrenics business – which, as you'll recall, was transferred (dropped down) to the Co-Borrower of the Oaktree, et al. Term Loan, Trinseo NA Finance SPV LLC. The resulting intercompany loan receivable was still pledged to lenders (Oaktree, et al.) but since this intercompany loan isn't residing pari to the company's existing secured debt the receivable is less valuable – but you gotta crack a few eggs to make an omelet.

The second intercompany term loan, the $948mm Tranche B Term Loan, didn't take any twists and turns: the proceeds were sent directly to the Trinseo Lead Borrower and Trinseo Co-Borrower. It has a rate of SOFR + 9.66%, is secured pari (first-lien) to the company's existing secured debt, and the resulting intercompany loan receivable was pledged to lenders (Oaktree, et al.) as security for their debt.

Now, the point of all this mess was to deal with the company's looming maturity walls – and, to that end, the transaction is a home run. The proceeds of the $1,077 Term Loan, net of fees, was about $1,045mm. This was able to take out the entire $660mm TLB coming due in September of 2024 (done at par) and $385mm of the Senior Unsecured Notes coming due in September of 2025 (also done at par).

I hate to keep circling back to more and more minute points, but now is as good a time as any to talk about the structure of the $948mm (intercompany) Tranche B Term Loan. Because, as you'll

recall, I mentioned it was broken into Incremental Term Loans and Refinancing Term Loans – and as you've already guessed the rationale behind this has *something* to do with the debt docs.

The $680mm Refinancing Term Loans were specifically earmarked to fully take out the $660mm TLB plus accrued interest, etc. This is because permitted refinancing capacity in almost all credit agreements will stipulate that it can only be tapped to refinance debt with similar debt (e.g., secured debt being refinanced with secured debt of a similar priority, just as is happening here since the Refinancing Term Loans will reside pari in priority to the TLB being taken out).

The remaining Tranche B Term Loan, comprising the Incremental Term Loans totaling $268mm, relied on the incremental secured debt basket – of which there was more than enough capacity as I highlighted above – to ensure that it was also secured pari to the company's existing secured debt issued out of the Trinseo Lead Borrower and Trinseo Co-Borrower. Then, the combination of proceeds arising from the Incremental Term Loans, along with the cash from the equity contribution provided through the Tranche A Term Loan that meandered on down to the Trinseo Lead Borrower and Trinseo Co-Borrower level, provided sufficient funds to take out $385mm of Senior Unsecured Notes at par. So, to be clear, the permitted refinancing capacity couldn't be used to take out the Senior Unsecured Notes because that would be refinancing unsecured debt with secured debt (in other words, not like-for-like).

Anyway, the transaction allowed for the maturities walls to be effectively pushed back: leaving a much smaller slug of 2025 Senior Unsecured Notes ($115mm) to deal with another day, along with the $375mm ABL maturing in May of 2026. But this all came at a cost: even if the PIK toggle is elected for the new term loan debt, we're talking about an annual cash interest expense increase of just over $30mm and PIK interest of just under $60mm.

Trinseo Pro-Forma Capital Structure

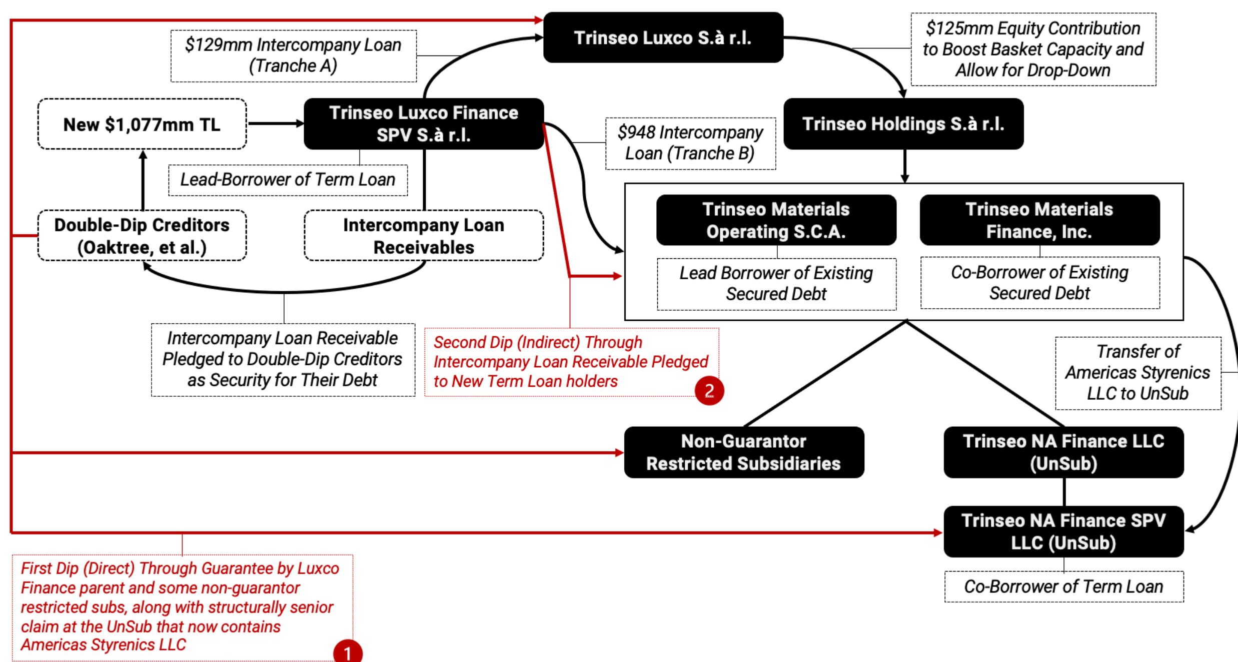
				Coupon		Maturity		Cash Interest			Total Leverage	
	Pre	Adj	Post	Pre	Post	Pre	Post	Pre	Post Cash	Post PIK	Pre-Trans.	Post-Trans.
Cash	$270	-	$270									
Secured Debt												
SubCo $1,077mm Term Loan	-	$1,077	$1,077	-	S + 8.5%	-	May-28	-	$100	$57		
Total Priority Secured Debt	**-**	**$1,077**	**$1,077**					**-**	**$100**	**$57**	**0.0x**	**2.6x**
$375mm Senior Secured Revolver	-	-	-	L + 2.0%	L + 2.0%	May-26	May-26	-	-	-		
$700mm Senior Secured TLB	660	(660)	-	L + 2.0%	-	Sep-24	-	46	-	-		
$750mm Senior Secured TLB	734	-	734	L + 2.5%	L + 2.5%	May-28	May-28	55	55	-		
Intercompany Loan (Tranche B)	-	948	948	-	S + 9.66%	-	May-30					
Total Secured Debt (Excl. Intercompany Loan)	**$1,394**	**$417**	**$1,811**					**$101**	**$155**	**$57**	**3.4x**	**4.4x**
Unsecured Debt												
5.375% Senior Unsecured Notes	$500	(385)	$115	5.38%	5.38%	Sep-25	Sep-25	$27	$6	-		
5.125% Senior Unsecured Notes	447	-	447	5.13%	5.13%	Apr-29	Apr-29	23	23	-		
Other	8	-	8					-	-	-		
Total Debt (Excl. Intercompany Loan)	**$2,349**	**$32**	**$2,381**					**$151**	**$184**	**$57**	**5.7x**	**5.7x**
Net Debt (Excl. Intercompany Loan)	*2,080*	*32*	*2,112*								*5.0x*	*5.1x*
Memo:												
Estimated 2024 Adj. EBITDA	$415											

Note: The SubCo TL is broken out from the other secured debt in the cap table above because it benefits from *structurally senior* claims. Think about it this way: the SubCo TL has a higher priority than the pre-existing secured debt on the value within the non-guarantor restricted subs that have provided the (capped) secured guarantees and the unrestricted sub where the Americas Styrenics business was dropped into *plus* is pari, through the Tranche B Term Loan, to the pre-existing secured debt on the value that's backing the pre-existing secured debt. Therefore, we're breaking the SubCo TL out to reflect the fact that it has primed the pre-existing secured debt on the value residing within the non-guarantor restricted subs and the unsub where Americas Styrenics was dropped into. This is a similar situation to Sabre but is distinct from At Home or Wheel Pros; these latter two involved the secured guarantees coming from the same restricted group entities as the intercompany loans benefited, so the double-dip claims in each are pari to the pre-existing secured debt claims and thus we'd place the SubCo debt alongside the existing secured debt.

Finally, there's one last point we should discuss since this will also be a feature of some double-dips in the future. I mentioned earlier that the debt docs governing the new-money placed at the subsidiary level should be more-or-less like a straight-jacket to avoid value leakage: precluding the subsidiary from doing pretty much anything other than paying the subsidiary-issued debt.

However, in the credit agreement governing the Term Loan provided by Oaktree, et al. we see that it *does* allow the subsidiary to issue more debt. Specifically, it created a $115mm incremental debt basket that can only be tapped, "…solely to exchange, redeem or refinance in full the 2025 Senior Notes that remain outstanding after the Closing Date". But there's a catch: this $115mm must be subordinate to the existing Term Loan – similar to the Wheel Pros' transaction where there are 1L *and* 2L double-dip creditors created through the exchange of pre-existing debt.

There are some smaller details of the Trinseo transaction I'll glaze over (e.g., the economics for lenders with the make-whole) but the main thing, once again, is that a company facing imminent maturity walls, that couldn't complete a regular-way refi, was able to leverage a double-dip, with the help of a drop-down, to meaningfully increase its runway.



So, if I haven't gone down too many rabbit holes here and haven't inadvertently caused too much confusion, now you should be able to read the transaction summary provided by Trinseo and have a rough feel for how this all occurred, and why the transaction was structured in such a seemingly schizophrenic way…

"Transactions" means, collectively, (a) the funding of the Tranche A Term Loans on the Closing Date, (b) the issuance by Parent of the Intercompany Parent Note and the concurrent contribution of the proceeds thereof by Parent to Trinseo Holdings and by Trinseo Holdings to Trinseo Lead Borrower on the Closing Date, (c) contribution by Trinseo LLC of the JV Interests to the Co-Borrower, (d) the funding of the Tranche B Term Loans on the Closing Date, (e) entry into 2023 Incremental and Refinancing Amendment, (f) the refinancing in full of the 2018 Refinancing Term Loans (as defined in the Trinseo Credit Agreement) with the proceeds of the 2023 Refinancing Term Loans together with cash on hand on the Closing Date, (g) the redemption of not less than $385,000,000 of the principal amount of the 2025 Senior Notes with the proceeds of the 2023 Incremental Term Loans and cash on hand and (h) the payment of Transaction Expenses.

3 WHEEL PROS

Finally, we have Wheel Pros that was relatively unique for a few different reasons…

- First, it involved an exchange in which all existing 1L TL lenders and three-quarters of the Senior Notes were permitted to participate (these two pieces of debt comprised the entire capital structure excluding the $200mm ABL facility).
- Second, the new money element ($235mm) doesn't itself directly benefit from the double-dip, rather it's the debt that's been exchanged as part of the transaction that does.
- Third, because the transaction involved the full participation of the existing 1L TLs (well, 99.7% technically), along with all the Senior Notes that were *permitted* to participate, it was more defensive in nature (e.g., involving existing creditors putting in the new-money to prevent a third-party from swooping in to do so and thereby diluting pre-existing holder's claims à la Sabre).
- Fourth, because the transaction involved (almost) full participation of the existing 1L TLs and three-quarters of the Senior Notes, the debt docs were able to be amended pre-transaction to open up the basket capacity to effectuate the transaction as the debt docs would have otherwise precluded the transaction.
- Fifth, the transaction involved the creation of first-lien and second-lien double-dip debt for participating creditors – something not seen in prior transactions.

So, with all of that out of the way, Wheel Pros hired HL earlier this year with an ad hoc group of lenders bringing in PJT. The transaction arrived at involved creating a $235mm first-in-last-out (FILO) Facility that was open to all existing 1L TL lenders to contribute to (although it was backstopped by 70% of the existing 1L TL lenders, and they took a hefty fee for doing so).

This S + 8.875% FILO Facility was issued by Wheel Pros Inc., the issuer of the company's pre-existing secured debt, and has a first-lien on ABL collateral but is in a second-out position (e.g., behind the ABL in payment priority). Otherwise, the FILO Facility resides pari to the pre-existing 1L TL and all other 1L claims that arose from the exchange component of the transaction (although the FILO Facility was structured such that upon filing it needs to be paid in full before the 1L claims created through the exchange get any recovery – so it's exceptionally well covered).

As mentioned, the double-dip isn't to the benefit of the new-money component of the transaction (the FILO facility). Rather, the double-dip is to the benefit of those participating in the exchange component of the transaction – something that was open to all $1,154mm of 1L TL lenders and three-quarters, or $272mm, of Senior Noteholders to participate in.

To complete the exchange and effectuate the double-dip on the exchanged debt, a new non-guarantor restricted subsidiary was spun up and a new $1,014mm 1L TL was created alongside a $272mm 2L TL. The first dip arises from these new term loans benefiting from secured guarantees from Wheel Pros Inc., the borrower of the company's pre-existing secured debt, and all its wholly-owned subsidiaries. The second dip arises from the term loan proceeds, totaling $1,286mm, being sent, through an intercompany loan, up to Wheel Pros Inc. and being secured and guaranteed by Wheel Pros Inc. and all its wholly-owned subsidiaries. So, similar to At Home, the secured guarantees of the new-money are originating from the same entities that the intercompany loan is benefiting and being secured by (whereas in Sabre and Trinseo the guarantees are originating from different entities than the intercompany loan is benefiting).

Finally, the proceeds of the $1,286mm intercompany loan were used by Wheel Pros Inc. to execute open-market purchases on the participating holders' existing 1L TL and Senior Notes positions (at 85% and 100% exchange rates, respectively). So, this just amounts to an exchange (at a discount) of the existing 1L TL at the ParentCo into a 1L TL at the SubCo with the benefit of a double-dip, and an exchange of the existing Senior Notes at the ParentCo into a 2L TL at the SubCo with the benefit of a double-dip.

Wheel Pros Pro-Forma Capital Structure

				Coupon		Maturity		Total Leverage	
	Pre	Adj.	Post	Pre	Post	Pre	Post	Pre-Trans.	Post-Trans.
Cash	$10	-	$10						
Secured Debt									
$200mm ABL Facility	$176	(160)	$16	-	-	-	-		
$235mm FILO Facility	-	235	235	S + 8.875%	-	-	-		
Total ABL Priority Debt	**$176**	**$75**	**$251**					**1.3x**	**1.8x**
Pre-Existing 1L TL	$1,154	(1,151)	3	L + 4.5%	-	May-28	-		
SubCo 1L TL	-	1,014	1,014	-	S + 4.5%	-	May-28		
Intercompany Loan	-	1,286	1,286	-	-	-	-		
Total 1L Debt (Excl. Intercompany Loan)	**$1,330**	**(62)**	**$1,268**					**9.5x**	**9.1x**
SubCo 2L TL	-	$272	$272	-	6.50%	-	May-28		
Total Secured Debt (Excl. Intercompany Loan)	**$1,330**	**$210**	**$1,540**					**9.5x**	**11.0x**
Unsecured Debt									
6.500% Senior Notes	$365	(272)	$93	6.50%	6.50%	May-29	May-29		
Total Debt (Excl. Intercompany Loan)	**$1,695**	**(62)**	**$1,633**					**12.1x**	**11.7x**
Net Debt (Excl. Intercompany Loan)	*1,685*	*(62)*	*1,623*					*12.0x*	*11.6x*
Memo:									
Pro-Forma Estimated 2023 Adj. EBITDA	$140								
LTM Adj. EBITDA	$80								

Note: In case you're wondering about the rationale behind only 75% of Senior Notes being allowed to participate, those spearheading (read: backstopping) the transaction were significant cross-holders of the 1L TL (~70%) and Senior Notes (~75%). So, the transaction was designed specifically to get their Senior Notes into a structurally superior position (the 2L TL at SubCo) relative to the other 25% of Senior Notes.

Note: The FILO Facility was open to all 1L TL holders to participate in (read: contribute to). However, if someone decided not to participate in funding it, then they were only allowed to exchange their 1L TL into the SubCo 1L TL at sixty cents on the dollar not eight-five cents.

So, this is a transaction that, at first blush, may seem to be a bit nonsensical since it's open to all 1L TL holders and nearly all Senior Noteholders to participate in – and, as I mentioned above, virtually everyone that could participate *did* participate. So, isn't this all a bit like rearranging the deck chairs on the Titanic? Who's really winning here?

The short answer is there's definitely a point to the transaction, but it doesn't move the needle the same way that other double-dips or drop-downs or non-pro rata uptiers we've talked about have.

From the company's perspective, they do get *much* needed liquidity as they were running on fumes with only around $15mm of liquidity pre-transaction (roughly $10mm in cash, $5mm in ABL availability due to constraints on drawing it in full). And, in the end, the $235mm FILO Facility led to a liquidity increase of around $160mm. This is likely a liquidity increase that's lower than you'd expect, but there were around $35mm is backstop-related fees, $20mm in advisory fees, and $20mm in accrued interest that needed to be paid since the transaction was done inter-quarter. (The cost of capital for those who need it most is invariably the most expensive!).

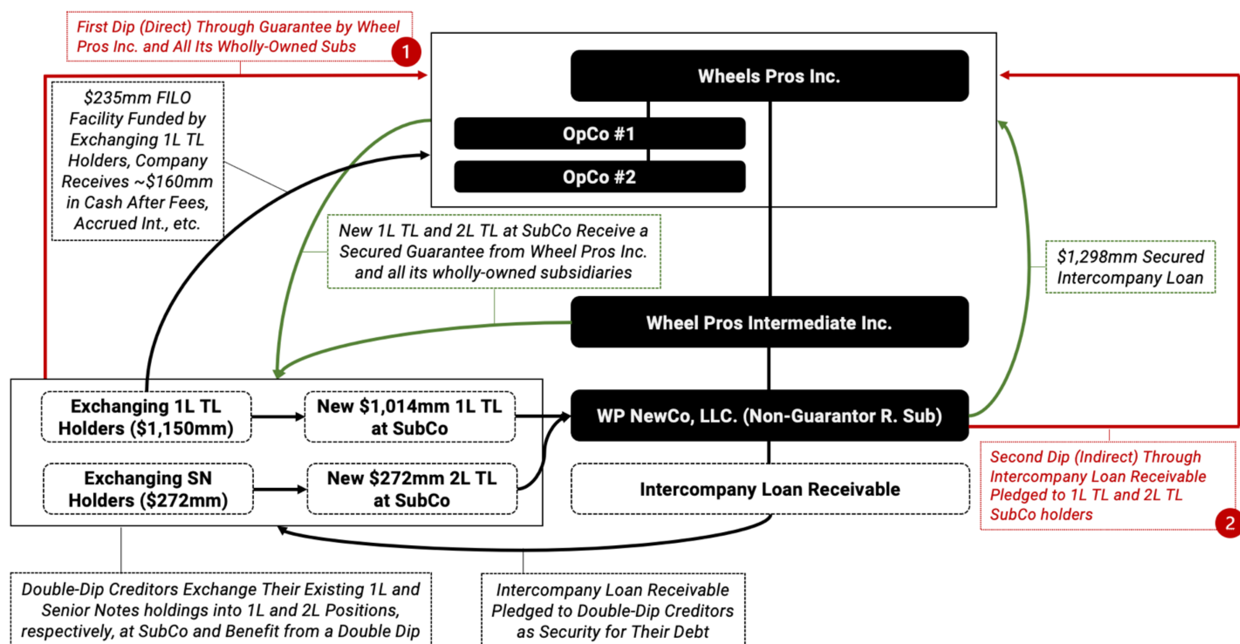
From the commitment parties' perspective (those spearheading the transaction) they're providing new money, sure, but they're also immediately recouping some of that through backstop fees coming back to them and the new-money FILO Facility is extremely well covered (never say never, but there's really no scenario in which it'd end up not getting a full recovery).

Additionally, as we've just discussed, they're rolling-up their Senior Notes to a structurally better position and are doing so at par (remember the commitment parties held the 75% of Senior Notes that are being rolled-up). Finally, if existing lenders decided not to participate in funding the FILO Facility, they could exchange only at sixty-cents on the dollar into the SubCo 1L TL (so, effectively, this would give those that exchanged and funded the FILO Facility an even greater share of the first-lien claims pool than they otherwise would have had).

So, we aren't talking about there being a windfall for those participating in the transaction, or even for the commitment parties backstopping it. The 1L TL was liable to be where value would break pre-transaction, and now it's the SubCo 1L TL.

But, as you'd guess, there is a method to the madness going on here: no one is under the illusion that there's a big "winner" like in Serta or Incora or even At Home but the transaction did get Wheel Pros some much-needed runway since filing would've been imminent without it.

In the end, Wheel Pros really demonstrates how existing creditors – staring down the barrel of a stressed company they don't *really* want to put new money into – can structure a transaction to buy a company more breathing room to implement a turnaround without it to being too risky *and* make sure that no third-party comes in to do a transaction that suddenly strips value from them (drop-down) or dilutes their existing claims (double-dip). So, of all the double-dips that have occurred, this is the most defensive-minded transaction.



So, as discussed above, it's not fair to say that this transaction doesn't move the needle on the company's prospects: it *has* bought them time, and they *could* turn things around. But it's not a huge liquidity injection and it's fair to say this transaction was *mostly* done to preserve value for existing holders through precluding some third-party coming in and mucking up the capital structure – therefore, this transaction is almost assuredly the last straw and it's sink or swim time for Wheel Pros (unless the sponsor, Clearlake, wants to start injecting new-money into it but don't count on that – they have a few dozen other distressed PortCos to worry about).

Given this, let's walk through a little waterfall of how the recoveries would flesh out assuming the company continues on its current trajectory and Clearlake eventually throws up their hands and decides to hand over the keys to creditors and be done with it.

So, as we discussed in the Case Study Guide, the first thing we need to think about is *when* they'd file. Because there are no near term maturities *and* they've just brought in a non-trivial amount of cash through the FILO Facility.

For the sake of argument, let's say that post-transaction they have $175mm in liquidity: the $15mm in pre-transaction liquidity, stemming from cash on the balance sheet and remaining ABL availability, and the $160mm of fresh cash brought in through the FILO Facility net of all fees, etc. But to determine the company's runway we need to look at both the company's liquidity *and* its cash burn – in other words, do a little liquidity roll-forward as I detailed in the Case Study Guide.

Since Wheel Pros is sponsor-backed, I'm going to need to keep things a little bit generalized. So, instead of doing a full liquidity roll-forward, let's do a little back of the envelope math here and focus on the bigger picture…

Recently, Wheel Pros has been burning around $20mm in cash per quarter. So, let's assume as our base case that this level of cash burn continues (in other words, let's assume the touted turnaround doesn't actually turn things around – because if it were easy the company wouldn't have found itself on the brink of filing pre-transaction).

However, one thing we *do* know is that the company will have higher annual cash interest expenses post-transaction, so we *can* make an adjustment to the $20mm in quarterly cash burn for that.

Since the pre-existing 1L TL was exchanged at 85%, and the SubCo 1L TL has the exact same rate, there's around $14mm of cash interest savings here arising from the roughly $140mm in discount capture. However, these savings are more than eaten up by the new FILO Facility, with its very healthy S + 8.875% terms, that adds $34mm in annual cash interest expense. Therefore, the company's annual cash interest expense, excluding the ABL, has gone up around $20mm.

Pre-Transaction Cash Interest				
	Outstanding	SOFR / LIBOR	Rate	Cash Interest
Pre-Existing 1L TL	1,154.0	5.5%	4.5%	115.4
Senior Notes	365.0	0.0%	6.5%	23.7
Total Cash Interest	**$1,519.0**			**$139.1**

Post-Transaction Cash Interest				
	Outstanding	SOFR / LIBOR	Rate	Cash Interest
$235 FILO Facility	235.0	5.5%	8.9%	33.8
Pre-Existing 1L TL	3.5	5.5%	4.5%	0.3
New 1L TL	1,014.0	5.5%	4.5%	101.4
New 2L TL	271.9	0.0%	6.5%	17.7
Senior Notes	93.1	0.0%	6.5%	6.0
Total	**$1,617.4**			**$159.2**
Cash Interest Increase (Decrease)				*$20.1*

Now, the proceeds from the new-money FILO Facility went toward paying down the ABL Facility that had $176mm outstanding and was nearly tapped out pre-transaction. Functionally, this amounts to swapping one type of liquidity (cash) for another type of liquidity (ABL availability) but it'll reduce down the cash interest paid on the ABL outstanding. Also, the proceeds being used to heavily paydown the ABL was used, in part, as leverage to cajole the ABL lenders into extending out the ABL maturity to 2028 – never miss an opportunity to push out maturity walls!

Anyway, since this is private we'll use some general numbers here: let's assume that the company used *all* of its $160mm in fresh cash to paydown the ABL bringing the amount outstanding to a paltry $16mm. If we assume the ABL is at L + 2.5% then this $160mm paydown would lead to an annual cash interest savings of $13mm. So, taken together, this leads to the post-transaction capital structure, at time zero, increasing annual cash interest expense by $20mm - $13mm = $7mm. (Needless to say, if the level of cash burn we're anticipating occurs then the level of cash interest will slowly grind up as the company draws its ABL but we'll leave this consideration to the side moving forward).

So, to recap, pre-transaction the company had $15mm in liquidity: roughly $10mm in cash on the balance sheet and roughly $5mm in ABL availability (it's not important, but ABL covenants precluded being able to draw the full $24mm of the ABL that should've been available pre-transaction).

Now, to keep the numbers simple, we're assuming that the company brought in exactly $160mm of cash net of all fees, etc. through the new FILO Facility, and that all of the proceeds went toward paying down the ABL (leaving $16mm drawn and cash on the balance sheet unchanged). However, even with the cost savings from the discount capture on the 1L TL exchange *and* the paydown of the ABL, the annual cash interest expense will still be roughly $7mm higher post-transaction due to the FILO Facility's aggressive terms.

Therefore, since we're assuming that the status-quo of $20mm in quarterly cash burn will continue unabated, our revised cash burn, taking into account the heightened interest expense, will be roughly $27mm per quarter – and the total liquidity at time zero, once again, is $175mm: arising from $10mm of cash on the balance sheet, and now $165mm in ABL availability assuming that the pre-existing maximum that can be drawn out of the ABL Facility is ~$181mm as it was pre-transaction.

So, theoretically, if the cash burn is $27mm per quarter and we have $175mm in liquidity then the transaction has bought the company around five or six quarters of runway. However, the most likely outcome is that within the next few quarters the future of Wheel Pros will become self-evident: either the turnaround they're touting will show signs of success with the company's runway extending even further as FCF improves or the company will go up in a rubberized plume of smoke with filing occurring sometime next year.

Since the entire rationale behind this section is to illustrate a double-dip waterfall, let's assume the worst for Wheel Pros. We'll assume that quarterly cash burn continues at a $27mm clip, and that, mercifully, after three quarters they throw in the towel and file.

Note: In the post-transaction cleansing docs, Wheel Pros itself stated that they're anticipating liquidity to fall from around $173mm post-transaction to $136mm in Q1 '24 (representing around $18.5mm in quarterly cash burn). This is a lesser cash burn than we're anticipating here but, as you'd expect, the post-transaction projections of companies are almost invariably too rosy (although, to be fair, it's not like their cash burn projections here are *too* rosy!).

In the Case Study Guide waterfall I went a little overboard with the pre-petition, post-petition, and return structure discussion (as mentioned in that Guide, it's all beyond what you need to know for interview purposes). Here we're going to forget about the small stuff and keep things pretty straight-forward since this is all about illustrating the waterfall mechanics with a double-dip.

So, we'll assume the company filed with $10mm of cash on its balance sheet and $97mm of its ABL drawn (this increase over the $16mm post-transaction amount being due to the $27mm in cash burn over three consecutive quarters). We'll also assume an EV of $1,120mm, utilizing the company's Estimated 2023 Adj. EBITDA of $140mm with a multiple of 8.0x. This EV, that we're assuming here is identical to the distributable value, isn't drawn entirely out of thin air: it roughly matches the current market value of Wheel Pros' debt (e.g., the face value of all tranches multiplied by the current trading price).

So, with those assumptions made, let's (finally!) start walking through the waterfall…

First, the ABL is, obviously, very well covered and receives full recovery. Second, there's the FILO Facility. As we discussed earlier, it has a bit of a unique structure. It's in a second-out position vis-à-vis the ABL collateral and otherwise resides pari to the company's first-lien claims. However, it must be paid in full before the SubCo 1L TL arising from the exchange receives any recovery – so, functionally, it's very well covered too. Basically unless the distributable value is less than the ABL amount outstanding *and* the FILO Facility amount, the FILO Facility will get back par.

Third, we have the regular-way first-lien claims (in other words, the first-lien claims *after* dealing with the FILO Facility). Since we began with $1,120mm of distributable value, by the time we're done with the ABL and FILO Facility there's $788mm in value left to go around. So, there are three kinds of pari first-lien claims here: $3.5mm arising from the 0.3% of Pre-Existing 1L TL holders that didn't participate in the exchange; $1,014mm arising from the 99.7% of Pre-Existing 1L TL holders that did participate in the exchange at an 85% exchange rate, inclusive of the $36mm in SubCo 1L TL that was paid as a backstop fee; and $1,286mm arising from the Intercompany Loan. If we tally up these claims, we arrive at $2,303.5mm and if we divide that by the amount of distributable value left for them, $788mm, we arrive at a recovery rate of 34.2%.

The recovery for the $3.5mm of Pre-Existing 1L TLs is straight-forward: it's 34.2% of their $3.5mm claim value or $1.2mm. Moving to the SubCo 1L TL we arrive at the double-dip consideration: holders are benefiting from a 34.2% recovery, no different from the Pre-Existing 1L TL, but on both the SubCo 1L TL claim amount *and* the Intercompany Loan claim amount. Thus, how their $787mm in recovery is arrived at: $347mm from the SubCo 1L TL claim, $440mm from the Intercompany Loan claim.

But, to be clear, the SubCo 1L TL recovery – ignoring accrued interest, etc. considerations – is capped at par ($1,014mm). In other words, if there were any value remaining after they received full recovery then that value would flow to those next in priority (the SubCo 2L TL).

Anyway, the reason for doing this little waterfall is to illustrate the real benefit of the double-dip: the SubCo 1L TL holders are getting recovery directly from the secured guarantee of their debt by Wheel Pros Inc., et al. *and* indirectly through the secured Intercompany Loan. And this combination vaults their recovery to *over* double that of the Pre-Existing 1L TL holders that didn't exchange (remember that the reason the Intercompany Loan is larger than the SubCo 1L TL is because of the SubCo 2L TL contribution – but the SubCo 2L TL only benefits from the Intercompany Loan after the SubCo 1L TL has received full recovery as I'll illustrate in a second).

Assumptions	
Estimated Adj. EBITDA	$140.0
EBITDA Multiple	8.0x
Estate Fees	10.0
Cash Build Post-Filing	10.0
Shares Outstanding	100.0
Cash Balance Pre-Filing	10.0
Cash Build Post-Filing	-
Pre-Existing 1L TL	1,154.0
$200mm ABL Facility Drawn	97.0
Pre-Existing Senior Notes	365.0
SubCo 1L TL Participation Rate	99.7%
SubCo 1L TL Exchange Rate	85.0%
SubCo 1L TL (Incl. Backstop Fee)	1,014.0
SubCo 2L TL Participation	74.5%
SubCo 2L TL Exchange Rate	100.0%
SubCo 2L TL	271.9

Illustrative Waterfall Analysis	
Estimated Adj. EBITDA	$140.0
EBITDA Multiple	8.0x
Enterprise Value	**$1,120.0**
Cash Balance Pre-Filing	$10.0
Plus: Cash Build Post-Filing	-
Less: Estate Fees	(10.0)
Distributable Value	**$1,120.0**
Value for ABL Creditors	**$1,120.0**
$200mm ABL	$97.0
Total ABL Priority Claims	**$97.0**
Recovery of Claim Value (%)	*100.0%*
Value for First-Lien Creditors	**$1,023.0**
$235mm FILO Facility	$235.0
Pre-Existing 1L Term Loan	3.5
SubCo 1L Term Loan	1,014.0
Intercompany Loan	1,285.9
Total First-Lien Claims	**$2,538.3**
Recovery of FILO Facility Claim Value (%)	*100.0%*
Recovery of Remaining 1L Claim Value (%)	*34.2%*
Value for Second-Lien Creditors	**-**
SubCo 2L Term Loan	271.9
Total Second-Lien Claims	**$271.9**
Recovery of Claim Value (%)	*0.0%*
Value for Senior Noteholders	**-**
Senior Notes	93.1
Total Unsecured Claims	**$93.1**
Recovery of Claim Value (%)	*0.0%*

Exchange Economics	
Pre-Existing 1L TL	$1,154.0
SubCo 1L TL Participation Rate	99.7%
SubCo 1L TL Exchange Rate	85.0%
SubCo 1L TL (Incl. Backstop Fee)	**$1,014.0**
Pre-Existing Senior Notes	$365.0
SubCo 2L TL Participation	74.5%
SubCo 2L TL Exchange Rate	100.0%
SubCo 2L TL	**$271.9**

Recovery Rates	
ABL Recovery (%)	100.0%
ABL Claim Value	97.0
ABL Recovery ($)	**$97.0**
FILO Facility Recovery	100.0%
FILO Facility Claim Value	235.0
FILO Facility Recovery ($)	**$235.0**
Pre-Existing 1L TL Recovery (%)	34.2%
Pre-Existing 1L TL Claim Value	3.5
Pre-Existing 1L TL Recovery ($)	**$1.2**
SubCo 1L TL Term Loan Recovery (%)	34.2%
SubCo 1L TL Claim Value	1,014.0
Intercompany Loan Recovery (%)	34.2%
Intercompany Loan Claim Value	1,285.9
SubCo 1L TL Recovery ($)	**$786.8**
SubCo 1L TL Recovery (%)	*77.6%*
SubCo 2L TL Recovery (%)	0.0%
SubCo 2L TL Claim Value	271.9
SubCo 2L TL Recovery ($)	**-**
Senior Notes Recovery (%)	0.0%
Senior Notes Claim Value	93.1
Senior Notes Recovery ($)	**-**

Note: Remember that although the SubCo 1L TL holders are technically getting recoveries in the waterfall that are more than double Pre-Existing 1L TL holders, the SubCo 1L TL holders initially exchanged their Pre-Existing 1L TL holdings into SubCo 1L TL holdings at eight-five cents on the dollar. So, to do a real apples-to-apples comparison you would need to make an adjustment here. In this example, if you held $1mm of the Pre-Existing 1L TL you're receiving a 34.2% recovery or $0.342mm. But if you held $1mm of the Pre-Existing 1L TL and were a member of the commitment party, then you now hold, after making an adjustment for your share of the backstop fee, $0.895 of SubCo 1L TL and are receiving a 77.6% recovery on *that* amount or $0.694.

To see how value flows to the 2L TL holders, imagine that the amount of distributable value we're starting our waterfall with is a bit higher. In the below example, we'll assume there's $1,440mm of distributable value – something that's seems *pretty* unlikely to eventuate, but perhaps the company's turnaround plan is successful insofar as it does raise Adj. EBITDA but their quarterly cash burns remains the same as in our last example due to maintenance capex rising a commensurate amount or something (thus the amount of ABL drawn at filing in the below example is the same at $97mm). Needless to say, the distributable value could be higher for *whatever* reason and the ABL could be drawn *whatever* amount – the specifics don't matter for our purposes here, we just care about the fact that for *whatever* reason there's enough value to hit the SubCo 2L TL.

Anyway, in this case the ABL and FILO Facility receive full recovery – no different than in the scenario above. This leaves $1,108mm in value for the remaining first-lien claims: the Pre-Existing 1L TL, the SubCo 1L TL, and the Intercompany Loan. These total claims when added together are $2,303.5mm, so the recovery ($1,108mm / $2,303.5mm) is around 48.1%.

So, the Pre-Existing 1L TL holders receive $1.7mm *but* the SubCo 1L TL holders receive full recovery because 48.1% of their $1,014mm 1L TL claim is around $488mm and 48.1% of the Intercompany Loan claim, that SubCo 1L TL holders have first priority on, is around $618mm. However, this amount of implied SubCo 1L TL recovery ($1,106mm) is in excess of the actual SubCo 1L TL amount outstanding ($1,014mm) and, as mentioned many times before, double-dip creditors are capped at payment in full which we're assuming here means getting back par.

Therefore, the way to think about the value that flows to the SubCo 2L TL is that it's the amount of Intercompany Loan recovery that's in excess of the amount needed to make the SubCo 1L TL receive payment in full.

So, the SubCo 1L TL has a claim of $1,014mm and receives a direct recovery of $488mm ($1,014 * 48.1%) thereby leaving a hole of $526mm. Now, the recovery on the Intercompany Loan, as mentioned, is around $618mm and SubCo 1L TL holders have first dibs on it. So, the "excess value" remaining for the SubCo 2L TL, after topping up the SubCo 1L TL until they've received full recovery, is the spread between $618mm and $526mm or $92mm – and since the SubCo 2L TL has a claim of $272mm they're in for a 34% recovery.

Here's another way to think about it: the Intercompany Loan recovery of $618mm belongs to the SubCo – the entity that issued the Intercompany Loan to ParentCo – and the SubCo issued two pieces of debt to fund this Intercompany Loan: the SubCo 1L TL and the SubCo 2L TL. So, think about the waterfall at SubCo if there's $618mm in value to distribute. First, there's the SubCo 1L TL that already received partial recovery of $488mm, so there's only $526mm that needs to flow to them. Second, there's the SubCo 2L TL and there's $92mm in value from the Intercompany Loan recovery that's left for them thereby giving them a 34% recovery ($92mm / $272mm).

Assumptions	
Estimated Adj. EBITDA	$160.0
EBITDA Multiple	9.0x
Estate Fees	10.0
Cash Build Post-Filing	10.0
Shares Outstanding	100.0
Cash Balance Pre-Filing	10.0
Cash Build Post-Filing	-
Pre-Existing 1L TL	1,154.0
$200mm ABL Facility Drawn	97.0
Pre-Existing Senior Notes	365.0
SubCo 1L TL Participation Rate	99.7%
SubCo 1L TL Exchange Rate	85.0%
SubCo 1L TL (Incl. Backstop Fee)	1,014.0
SubCo 2L TL Participation	74.5%
SubCo 2L TL Exchange Rate	100.0%
SubCo 2L TL	271.9

Illustrative Waterfall Analysis	
Estimated Adj. EBITDA	$160.0
EBITDA Multiple	9.0x
Enterprise Value	**$1,440.0**
Cash Balance Pre-Filing	$10.0
Plus: Cash Build Post-Filing	-
Less: Estate Fees	(10.0)
Distributable Value	**$1,440.0**
Value for ABL Creditors	**$1,440.0**
$200mm ABL	$97.0
Total ABL Priority Claims	**$97.0**
Recovery of Claim Value (%)	*100.0%*
Value for First-Lien Creditors	**$1,343.0**
$235mm FILO Facility	$235.0
Pre-Existing 1L Term Loan	3.5
SubCo 1L Term Loan	1,014.0
Intercompany Loan	1,285.9
Total First-Lien Claims	**$2,538.3**
Recovery of FILO Facility Claim Value (%)	*100.0%*
Recovery of Remaining 1L Claim Value (%)	*48.1%*
Value for Second-Lien Creditors	**$92.4**
SubCo 2L Term Loan	271.9
Total Second-Lien Claims	**$271.9**
Recovery of Claim Value (%)	*34.0%*
Value for Senior Noteholders	**-**
Senior Notes	93.1
Total Unsecured Claims	**$93.1**
Recovery of Claim Value (%)	*0.0%*

Exchange Economics	
Pre-Existing 1L TL	$1,154.0
SubCo 1L TL Participation Rate	99.7%
SubCo 1L TL Exchange Rate	85.0%
SubCo 1L TL (Incl. Backstop Fee)	**$1,014.0**
Pre-Existing Senior Notes	$365.0
SubCo 2L TL Participation	74.5%
SubCo 2L TL Exchange Rate	100.0%
SubCo 2L TL	**$271.9**

Recovery Rates	
ABL Recovery (%)	100.0%
ABL Claim Value	97.0
ABL Recovery ($)	**$97.0**
FILO Facility Recovery	100.0%
FILO Facility Claim Value	235.0
FILO Facility Recovery ($)	**$235.0**
Pre-Existing 1L TL Recovery (%)	48.1%
Pre-Existing 1L TL Claim Value	3.5
Pre-Existing 1L TL Recovery ($)	**$1.7**
SubCo 1L TL Term Loan Recovery (%)	48.1%
SubCo 1L TL Claim Value	1,014.0
Intercompany Loan Recovery (%)	48.1%
Intercompany Loan Claim Value	1,285.9
SubCo 1L TL Recovery ($)	**$1,014.0**
SubCo 1L TL Recovery (%)	*100.0%*
SubCo 2L TL Recovery (%)	34.0%
SubCo 2L TL Claim Value	271.9
SubCo 2L TL Recovery ($)	**$92.4**
Senior Notes Recovery (%)	0.0%
Senior Notes Claim Value	93.1
Senior Notes Recovery ($)	**-**

POSTSCRIPT #1: SOME NITPICKY NUANCE

I've been more deliberate than normal in how I've explained all of this and have tried my best to venture down rabbit-holes on an as-needed basis. Therefore, there are some nitpicky things that I've avoided discussing because even if they matter in a *strict* sense they matter much less in a *practical* sense – and, if I brought them up above, it would likely serve to confuse more than clarify.

But, for the sake of completeness, there are two little nitpicky things that I think are worth briefly mentioning (also since I've already written 17,000 words on double-dips then I might as well write a few hundred more).

First, if you're dreaming up a double-dip transaction and are thinking about using an unsub then you'll need to turn to the debt docs (surprise, surprise) to see how the company can designate unrestricted subsidiaries. In practice, the act of designation itself isn't the main issue with using an unrestricted sub in a double-dip transaction as the unsub used will *initially* be an empty shell. So, for example, in Trinseo the credit agreement in part states that it could designate unrestricted subsidiaries as long as it didn't make the FCCR worse at the time of designation – but since the unsub used as part of the broader transaction was initially an empty shell there was no issue as it per se didn't make the FCCR worse (there was no initial value in the sub!).

However, as I discussed earlier, the *main* issue with using an unsub – and the issue that could preclude one being used as the issuer of the double-dip debt and the originator of the intercompany loan – is that the debt docs *could* prohibit restricted group entities from guaranteeing the unsub-issued debt and prohibit the unsub from making intercompany loans to restricted group entities after designation. In other words, sure, the debt docs could allow you to designate an empty shell as an unsub but then you might not be able to use it to actually effectuate a double-dip thereafter.

So, in thinking about designation provisions, it's helpful to think about what the restrictions are at the time of designation *and* thereafter. In some debt docs strict restrictions around designation apply at time zero but not on an on-going basis thereby providing a little loophole (e.g., Trinseo's indenture saying that an unsub can't hold any debt, or have any lien, that's recourse to the restricted subs, but this only applies at the time of designation *not* thereafter). However, in other debt docs these kinds of strict restrictions apply both at the time of designation *and* thereafter – thereby precluding the ability to spin up an empty shell, designate it as an unsub, and *then* effectuate the double-dip. So, in these cases, the double-dip debt issuer would need to be a non-guarantor restricted sub unless the lawyers found some clever workaround due to some sloppy wording in the debt docs. (I'm talking about Trinseo here as an example but remember that the intercompany loans were issued out of a Trinseo ParentCo sub that wasn't an unsub).

Note: In Envision there was a bit of controversy because Envision redesignated the existing AmSurg restricted subsidiaries (where value *already* resided) into unrestricted subsidiaries in order to do a drop-down, and this was allowed through a creative interpretation of the sloppily-worded "specified disposition" language in the credit agreement. Envision is a whole 'nother story but it's important to keep in mind that debt docs are all unique snowflakes and this holds true for even seemingly minor elements of them like unrestricted subsidiary designation provisions.

Second, in practice the secured guarantees of the subsidiary-issued debt and the secured intercompany loan will require debt, lien, *and* (often) investment capacity. The reason that the investment capacity side of the equation wasn't brought up earlier is that (often) the debt docs will provide, as a matter of course, investment capacity insofar as there's sufficient debt and lien capacity that can be tapped.

In other words, there will often be an investment basket that allows investments that also constitute debt if that debt is otherwise permitted under the debt and lien covenants. So, the investment capacity isn't usually a binding constraint and usually takes care of itself if there's sufficient debt and lien capacity (remember that both the new-money guarantees and the intercompany loan require debt and lien capacity in double-dips since you want them secured).

POSTSCRIPT #2: JUDGE JONES JETTISONED (11/01/2023)

Finally, we need to talk about Judge Jones because, as mentioned in the preamble, he's resigned due to, uh, an undisclosed living situation that *really* should've been disclosed. I've written about Judge Jones a fair amount (see: the Serta Postmortem Guide) because he's had a truly outsized impact: turning the Southern District of Texas into the hottest venue in bankruptcy both literally and figuratively and tackling some of the most contentious cases. This includes current cases with far-reaching implications, like Incora, where the battle is still in full heat and that will now be reassigned. In fact, Judge Jones was actually hearing summary judgement arguments in Incora's case *after* his living situation became public but resigned shortly thereafter – causing more than a few heart palpitations over at Platinum, I'm sure.

In my writing on Serta I think I made it pretty clear that Judge Jones is a divisive character – with the more uncharitable thinking that he's an unserious self-promoter who is deferential to debtors to the detriment of case outcomes because to be known as debtor-friendly is to ensure that the largest and most controversial (read: consequential) cases continue coming to his court (and, like, he *has* handled over 10% of all cases with over $100mm in liabilities since 2016 and around 17% of all cases with over $1,000mm in liabilities since 2020 for a reason).

Top 10 Most active bankruptcy judges: cases with liabilities greater than USD 1bn (Jan 2020 - present)			
Judge	**Court**	**No. of cases**	**% of total cases**
David R. Jones	Texas Southern	29	17%
Marvin Isgur	Texas Southern	23	14%
Michael E. Wiles	New York Southern	16	9%
Mary F. Walrath	Delaware	10	6%
Martin Glenn	New York Southern	8	5%
John T. Dorsey	Delaware	6	4%
Shelley C. Chapman	New York Southern	6	4%
Christopher M. Lopez	Texas Southern	5	3%
Craig Todd Goldblatt	Delaware	5	3%
James L. Garrity	New York Southern	5	3%

Source: Debtwire's Restructuring Database

However, there are some – not just those at Kirkland! – who would defend Judge Jones as being someone whose eccentricities belied a seriousness of purpose, and who stood athwart those who would rather see cases shrouded in uncertainty because that may bear out organic compromises even if it prolongs the debtor's time in-court. Judge Jones believed that in the most controversial and contentious cases, expediency *is* a form of equity, that cases must be dealt with as delivered, and that preserving business value should be sacrosanct even if this requires *sometimes* rubberstamping some dubious debtor behavior.

In the end, this is where much of the resentment toward Judge Jones comes from. For example, everyone knows that his *real* reason for upholding Serta's non-pro rata uptier boils down to him more-or-less thinking, "If I unwind this transaction it'll unleash chaos. There's no doubt that it'll be value destructive for Serta itself, since it'll languish in-court longer, but it'll also be value destructive for all the other companies that have done a non-pro rata uptier over the last three years. It's not my issue that this wasn't all decided by an Article III court in the *three years* prior to coming to me. So, it's plausible to me that this transaction is permissible. Plus, it's not like every credit agreement in the aftermath of Serta blocked these kinds of transactions from occurring. In other words, it's not like Apollo, et al. are the unlucky few here who've been blindsided by this in a way that no one else ever will be. Therefore, on balance, it's better to try not to put the toothpaste back in the tube – it would unquestionably be a negative for these businesses and their employees and could even end up being a Pyrrhic victory for non-participating creditors if unwinding these destroys enough business value."

Note: I think it's fair to say that I view Judge Jones in a more sympathetic light than many although, I mean, that's *really* not saying much. However, there's no doubt in my mind, or in Apollo's, that he would have readily rubberstamped the DQ list issue we talked about in the Serta Postmortem Guide (likely making a few remarks along the way about how he doesn't see what the issue even is) and I would have vehemently disagreed with that.

Anyway, there's no defense of the actions of Judge Jones that led to his resignation – it was as clear of a failure to disclose as there could be, and he knew it. However, the announcement of his living situation and his subsequent resignation was met with a certain level of triumphalism that, well, I don't know if it was per se surprising but it was a bit much.

Remember that most in the industry are not in favor of these more creative transactions – and non-pro rata uptiers are especially loathed. So, the jubilation here is, in part, a reflection of the belief that non-pro rata uptiers now rest on a much shakier foundation with Incora still in-court and Serta's issue at the Fifth Circuit on appeal – and there's no getting around that this is true.

Rest assured, Apollo and Angelo Gordon have continued making their arguments that non-pro rata uptiers are an afront to all that is decent in this world at the Fifth Circuit. Immediately following Judge Jones' resignation they filed a reply brief stating that their appeal should be reversed, remanded, and *moved* to the Southern District of New York.

> When the dust settles, appellees are left defending the extreme position that almost any exchange of value—including a complete recapitalization and restructuring of Serta's balance sheet—is an open market purchase that can nullify the pro rata right. There might be transactions that present close questions on the open-market-purchase issue. This is not one of them. The bankruptcy court's order granting partial summary judgment should be reversed and the case remanded for further proceedings on damages. Because the bankruptcy judge who presided over the proceedings below has resigned, the Court should remand the case to the district court with instructions either to transfer the case to the Southern District of New York or to proceed with the case itself.

Meanwhile, both Apollo and Angelo Gordon a few months ago led the combined drop-down and double-dip in Trinseo that saw them manufacture the ability to allow one of the most valuable parts of the business to be stripped away from existing creditors *and* simultaneously diluted down the first-lien claim pool at RemainCo (although, to be fair, the trading levels of Trinseo's secured and unsecured debt were slightly higher post-transaction, so it wasn't like the transaction had the *immediate* negative impact that Serta's transaction had on Apollo and AG's positions).

Now, Serta and Trinseo are two different kinds of transactions, etc. and it's fine, or at least not inconsistent, to argue that non-pro rata uptiers are a blight on the industry and that drop-downs and double-dips are as wholesome as apple pie. But it's important to remember that the moralizations in these briefs aren't a reflection of what anyone at Apollo or Angelo Gordon *truly* believes – and Judge Jones, in his classily curt and cantankerous way, made it known that he at least understood this much.

However, don't be so sure that other judges will – especially if this does ends up back in the Southern District of New York. In the end, *someone* needs to decide what "open-market purchase" means (we can't just have judges say it's "ambiguous" forever!) and that decision *will* be one informed by the perceived fairness of the transaction even if it's wrapped up in a much longer dissertation on these six syllables than Judge Jones provided.

Note: In much of the financial press, as you can read in the above links, there's very much a court-thrown-into-disarray narrative surrounding Judge Jones' departure. But that's all heavily overstated. It'll all be fine. The current cases will be reassigned and the prior cases won't be opened up unless there's a clear and compelling reason for doing so. This is all a mess but it's not *that* bad – well, I'll reserve final judgement on that until we see how Serta and Incora do.