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DIP Financing

Why Extend Credit to a Bankrupt Company?

It may seem counterintuitive that a lender would want to give significant amounts of money to a bankrupt company. Because Congress understood that lenders may have reservations about extending credit to a debtor, the Bankruptcy Code offers substantial protections to such lenders

The protections afforded to DIP lenders are set forth in section 364 of the Bankruptcy Code. This section sets forth a hierarchy of protections available based on the nature of financing options (e.g., secured vs. unsecured) available to the debtor

- If the debtor can demonstrate that financing could not be procured on any other basis, the court can, subject to certain limitations, authorize the debtor to grant the DIP lenders, among other protections:
  - a "priming" lien, or
  - a superpriority claim over administrative expenses (including post-petition vendor and employee claims) and other claims

Why Extend Credit to a Bankrupt Company?

Priming Liens

- Provide valuable protection – drive much of the DIP financing structure and documentation
- May be granted to the DIP lender if the debtor in possession cannot obtain credit without granting a priming lien, and either:
  - the "primed" prepetition secured creditors consent to priming; or
  - the debtor can prove that the interest of any primed secured creditor is "adequately protected"
- Due to the uncertainties of establishing "adequate protection," DIP lenders are often themselves the prepetition secured creditors or obtain consent of the secured creditors that are being primed
  - Why would anyone consent to being primed?
- Practice Point: The priming lien will only be granted on liens specifically indicated as being primed (e.g., the first lien loan and second lien notes). It is critically important to ensure that all liens that should be primed are identified, and any liens not being primed are specifically excepted from the liens being subordinated to the priming lien

Superpriority Claims

- A superpriority claim means that the debtors cannot emerge from chapter 11 without repaying the DIP facility in cash in full (absent consent of the DIP lenders)

Who Lends?

What types of institutions provide DIP loans?

- Commercial Banks
  - Commercial banks historically provided DIP loans, but are increasingly retreating from the DIP market due to (among other factors) hesitation to lend against declining asset values and stricter regulations
- Non-Traditional Lenders
  - Non-traditional DIP lenders, such as hedge funds, private equity firms, institutional lenders and CLOs have dramatically expanded their role in this market

What is the DIP lender's relationship to the debtor?

- Defensive DIPs
  - When the DIP loan is provided by the prepetition secured lenders
- Offensive/"New Money" DIPs
  - When a new third-party lender provides the DIP loan

Defensive DIPs

Defensive DIPs

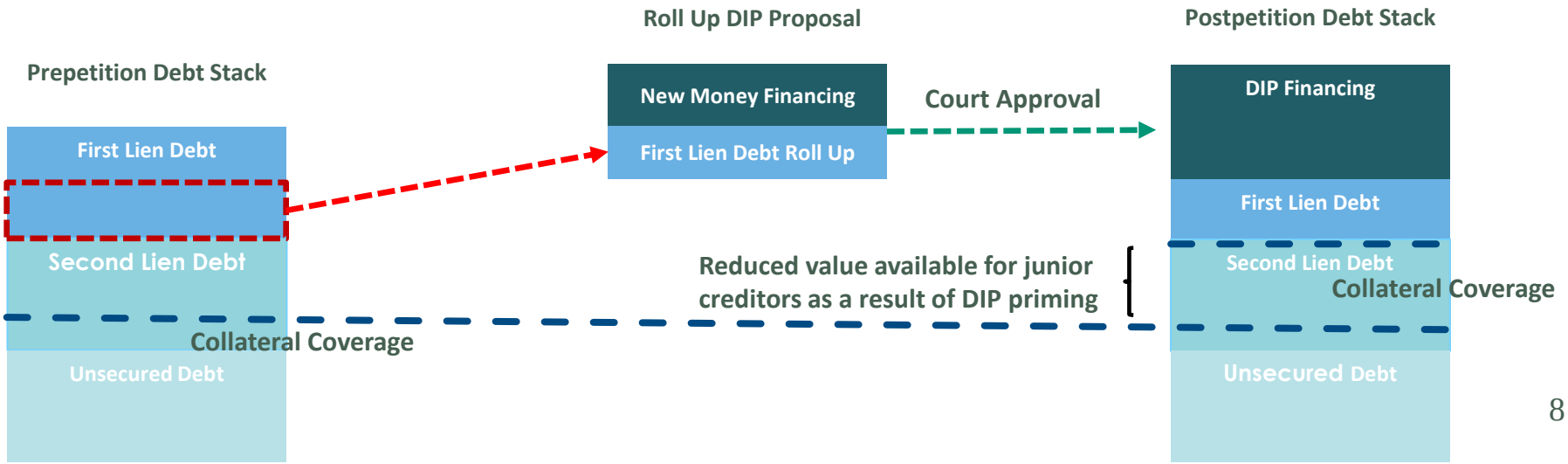
Prepetition secured lenders often provide DIP financing to protect their existing credit exposure and avoid the priming of their liens (with potentially insufficient adequate protection) by other providers of postpetition financing

- Prepetition senior secured lenders
  - Price/timing/knowledge advantage from preexisting relationship
  - May use postpetition lending to secure adequate protection for, or roll-up of, prepetition loans
  - Improve bargaining position in bankruptcy and gain additional control over the case (potentially through milestones, consent rights, and other covenants)
  - Prevent liens from being primed by other parties
  - Avoid adequate protection and valuation fights
  - Ensure that the debtor has sufficient liquidity to reorganize and maximize value
- Prepetition junior secured or unsecured lenders
  - Benefit from many of the same advantages as senior secured lenders in terms of pre-existing relationship
  - Usually want to participate to improve bargaining position and/or gain greater control of the case
  - A way to make a significant return on a position with respect to which their prepetition exposure might obtain a very low (or no) recovery
  - Less common than defensive DIP from prepetition senior secured lenders

Roll-Ups

- Roll ups refer to the conversion of prepetition debt into DIP financing, thereby entitling prepetition debt to receive administrative priority which must be paid in full in cash under a Chapter 11 plan

- Generally, secured claims, even those that are fully secured, are subject to "cram up" under section 1129(b) of the Bankruptcy Code and can be forced to accept takeback debt under a Chapter 11 plan, likely on unfavorable economic terms. By converting these claims to administrative expense claims, a debtor will be unable to cram up the claims.

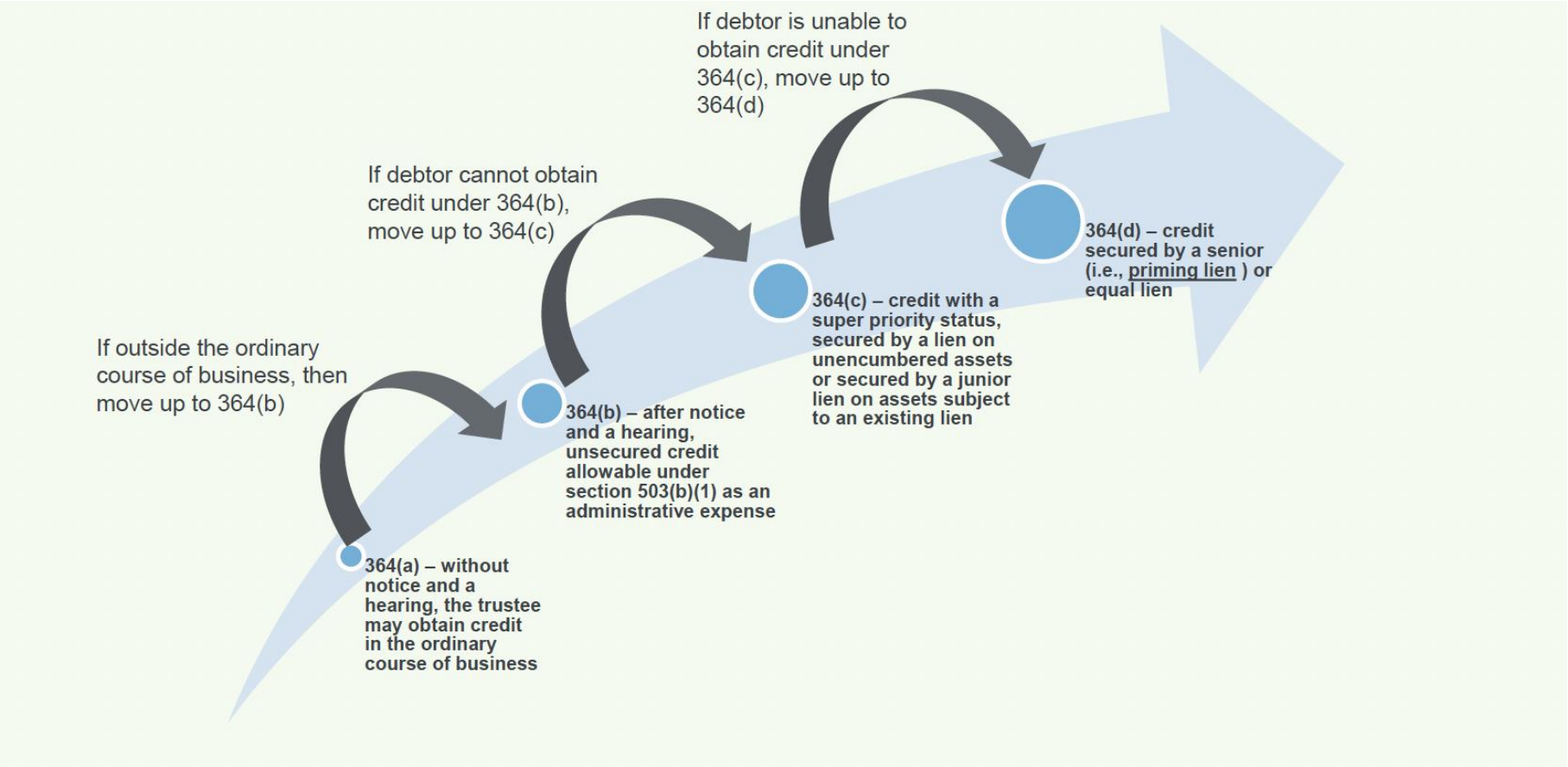


New Money DIPs

Other lenders may provide Offensive/New Money DIPs

- Significant returns on DIP financings can bring third parties to the table
- Third parties discouraged from lending where a priming fight is likely
- Typically only seen in cases of a bridge to an asset sale by the proposed purchaser

Section 364 Hierarchy



DIP-to-Exit Facilities

- At emergence, DIP facilities are often refinanced with exit facilities
- Alternatively, the DIP facility can roll into an exit facility with the consent of the DIP lender (could be structured this way at onset of the case, or agreed upon closer to the end of the case)
- Typical "exit conversion" conditions include:
  - Confirmation of an acceptable plan and entry of confirmation order
    - Lenders usually require that the confirmation order be final and non-appealable, with the DIP/Exit Lenders having the right to waive that condition.
  - Exit fee paid to Lenders
  - Compliance with leverage ratio and/or satisfaction of financial forecasts
- Relatively recent examples include: *iHeart, TCEH, Momentive*

DIP Financing Trends: Day One Roll-ups

- *Ascend Performance Materials*
  - About $2 billion of pre-petition secured debt, including a $1.1 billion term loan, a $348 million ABL, and a $150 bridge facility
  - $900 million DIP included (i) a $500 million ABL and (ii) a $400 million term loan
    - ABL included first day approval of the roll-up of bank product/LC obligations; fees, interest, and expenses; and a "creeping roll" on other ABL obligations, with a full roll-up to follow upon entry of the final DIP order
    - Term included first day rollup-up of the bridge facility
  - Total new cash is $400 million

- *DocuData Solutions/Exela*
  - About $1.4 billion of secured multi-tranche pre-petition debt, including bank debt and notes (plus $24 million of unsecured pre-petition notes)
  - DIP includes a $185 million facility, including a new money loan of $80 million, together with a first-day roll of $75 million in outstanding pre-petition secured notes, and a second day roll of $30 million

DIP Financing Trends: Equitizing DIPS

- Equitizing DIPs figured prominently in airline bankruptcies during the pandemic
  - Aeroméxico, Avianca, and LATAM each filed for US chapter 11 in 2020 to take advantage of various benefits of the Bankruptcy Code, including provisions relating to DIP financing
  - The greatest source of available value for the DIP lenders, as well as other stakeholders in these cases, was the equity of the reorganized company. As a result, the DIP facilities in these cases included equity conversion features that were heavily negotiated between the companies and their respective DIP lenders, as well as among the DIP lenders themselves

- Since 2020, DIPs with reorganized equity features have arisen in a number of other cases, suggesting a trend that may continue to have appeal in the market

- Equitization features can lead to objections from creditors and attract court scrutiny – approval can turn on whether the bankruptcy court believes the relevant DIP provisions improperly dictate the terms of an eventual plan
  - In LATAM, for example, the bankruptcy court denied approval of the DIP motion, agreeing with certain objecting creditors (including the UCC) that the proposed DIP facility constituted a sub rosa plan that "prematurely allocat[ed] reorganization value to LATAM's existing equity holders"
  - In Enviva, the court approved an equitizing DIP with a portion reserved for participation by existing shareholders over objection that it violated the absolute priority rule
  - The equitizing DIP facilities in Avianca, Aeroméxico, and Phoenix Services were uncontested and approved without issue

DIP Financing Trends: Equitizing DIPS

enviva	Court approved $250m equitizing DIP tranche (including 20% of tranche reserved for existing shareholders), with option of each holder to convert obligations into reorganized equity at the same value as any rights offering later approved in the case
LUMILEDS	Court approved a $175m DIP that reserved a portion of reorganized equity for payment of DIP lenders' fees
Avianca Airlines	Court approved uncontested $2bn DIP with a $722m tranche, convertible at the option of the debtor into a minimum of 72% of the reorganized equity at a discount to plan value of 8%
Grupo AEROMEXICO	Court approved uncontested $1bn DIP with an $800m tranche, convertible at the option of the DIP lender exclusively into equity at either the plan value or a discounted value reached during the confirmation process
LATAM	After significant litigation, court approved revised $2.45bn DIP with a $1.15bn tranche without a conversion feature
SAS	Court approved uncontested $700m DIP, convertible at the option of the DIP lender into equity at a rate based on a $3.2bn fixed total enterprise value. This was accompanied by a right of the borrower to reject the DIP lender's exercise of conversion. DIP facility also included a tag-right package for lenders to subscribe for up to 30% of any new-money equity interests provided by a third party on the same terms and conditions
PHOENIX	Court approved contested $200m DIP, convertible at the option of the DIP lender exclusively if new investor makes an equity investment, and on the same terms as the new money equity investment
Diebold Nixdorf	Court approved uncontested $1.25bn DIP with backstop premium of 13.5% of reorganized equity, upfront premium of 6.5% of reorganized equity, an additional premium of 7.0% of reorganized equity and a participation premium of 10.0% of reorganized equity
PCHI	$150m DIP providing backstop parties with right to convert DIP term loans into reorganized equity contested by non-backstop party noteholder. Ultimately settled and approved

DIP Financing Trends: Stalking Horse DIPS

Synthego Corp.

- Pre-petition secured credit facility of about $73.5 million with Perceptive Credit Holdings III, LP
  - Loans included additional bridge financing of $3.5 million (March 2025) and $4.3 million (April 2025)
  - Company filed in Delaware on May 5 with a stalking horse bid APA with Perceptive in place, seeking stalking horse protections including a 1.5% break-up fee of and a $1 million expense reimbursement Perceptive also provided a $50 million DIP, including $12.5 million of new money and a $37.5 million roll-up, including a first day roll of $10 million
  - Bid of not less than $72.4 million plus up to $12,500,000 in respect of the DIP loans (so full amount of debt less $1 million)
- Sale process underway
  - Stalking Horse expenses of up to $1 million approved; request for break fee withdrawn
  - Bids due June 24

DIP Financing Trends: Refinancing DIPS

GWG Holdings

- Upon filing, sought approval of a facility with National Founders for a $65 million facility that included an option to refinance DLP IV's and DLP VI's existing facilities, effectively shifting the policy portfolio to a new SPE
- The Court approved the financing on an interim basis giving the Debtors access to $10 million, but raised concerns at the first-day hearing about the proposed refinancing in the DIP and the Debtors reopened the DIP marketing process, ultimately returning to court with a Blue Owl Capital-affiliated entity, Chapford, willing to lend on improved terms, and with an option that gave the Debtors an option to compel the replacement lender as a stalking horse bidder with a $610 million floor
- Bondholders committee had limited objections to terms but generally supported a deal that removed the lender's purchase option; National Founders objected to absolute language requiring DLP IV and DLP VI to become debtors; thereafter the provision was modified and the Court entered a final DIP order
- Thereafter, Debtors entered into negotiations with an affiliate of Obra Capital (then called Vida Capital), agreeing to an option to enter into a replacement DIP permitting the Debtors to refinance their existing DIP and prepetition facilities, and to secure exit financing of up to $630 million in lieu of a sale
- The Court approved the replacement DIP on an interim basis in October 2022, and, after the Debtors indicated their intent to elect the option with Vida, on a final basis in December 2022, resulting in the repayment of the prepetition debt

DIP Financing Trends: Refinancing DIPS

Core Scientific

- Filed with commitments for up to $57 million and support for the syndication of $75 million; half available on an interim basis
- 1:1 Roll Up and high fees led to objections
- Debtors came back with a replacement DIP of up to $70 million

DIP Financing Trends: Exclusive Roll-Ups

American Tire

- AT's proposed DIP financing included (i) a $1.123B superpriority DIP term loan facility and (ii) a $1.2B superpriority ABL facility, to be funded by certain priming lenders
  - The term loan included $250 million of new cash and a $750 million roll-up of the priming lenders pre-petition term loans, and a full roll-up of a $75 million FILO facility funded by the priming lenders
  - Court approved on an interim basis at the first day hearing
- An ad hoc group of non-participating pre-petition lenders objected to a roll-up of pre-petition obligations that applied only to debt of DIP participants, arguing that it violated the ratable payment requirement of their pre-petition credit agreement
- Priming lenders argued that the roll-up was not payment on account of pre-petition debt but consideration for the new loan
- Court did not take issue with priming DIP generally, but drew the line at a making a finding in favor of the roll-up aspects of the loan based on contract language and on "commercial rationality"
  - At the final DIP hearing, J. Goldblatt commented that the proposed exception to pro rata sharing would turn "every prepetition agreement into . . . a game of Russian roulette such that any time you find yourself standing when the music stops, you go to zero."
- Parties returned to the table with a consensual deal that removed the term loan roll-up, leaving only the FILO roll-up in place

Exit Financing

Rights Offerings

- A rights offering provides creditors or equity holders with the option (or right) to purchase new securities in a reorganized company at a set subscription price, often at a discount, during a set subscription period
- Rights offerings can benefit both debtors and creditors/equity holders
  - Debtor increases liquidity and fortifies the balance sheet
  - Reduces reorganized debtor's leverage
  - Liquidity supports plan feasibility to avoid subsequent bankruptcy filing
  - Creditor has investment opportunity usually on favorable terms
  - Enhanced recovery on claims
  - Potential to resolve valuation disputes among constituents
- Key Components of a Rights Offering:
  - Backstop: One or more parties commit to subscribe for a minimum amount, in return for a commitment/backstop fee and other consideration (e.g., break-up fee, expense reimbursement).
  - Price: Participants are offered the right to purchase securities, normally at discount to plan equity value. A larger discount increases the attractiveness, but it also increases the dilutive effect of the issuance on the parties unable or unwilling to participate.
  - Eligibility: Potential participants are typically a limited pool of creditors. Wide eligibility may increase support for the chapter 11 plan, but could also increase regulatory and administrative concerns.
  - Section 1145 Exemption: If the rights offering complies with § 1145 of the Bankruptcy Code, no SEC registration is required. Debtors may use other exemptions in conjunction with § 1145 to avoid registration.
  - Oversubscription Right: The right to subscribe for unsold rights remaining after subscription period.
  - Overallotment Right: The right to purchase an additional, predetermined amount of interests should offering be fully subscribed.
  - Transferability: Rights offerings are typically non-transferable (except together with the underlying claim) to avoid jeopardizing registration exemptions.

Rights Offerings

The following levers are frequently utilized to generate value for participating investors:

Discounted Equity Purchase	▪ Rights to purchase equity are granted at a discount to transaction value (or the transaction value can be set at a discount to market value) ▪ Allows participants in a RO to obtain a disproportionate share of ownership in exchange for their willingness to invest new capital
Backstop Fee	▪ Fee paid to certain specified investors (the "Backstop Parties") who agree to fund any shortfall due to other parties' failing to exercise their rights ▪ Backstop Parties are paid a fee in exchange for their commitment, which can be in the form of cash, equity or note
Allocation / Holdback	▪ Can be allocated entirely to one tranche of stakeholders or multiple tranches ▪ Certain investors in the rights offering are guaranteed a specific allocation of the new money investment, regardless of their pre-transaction positions
Backstop Waterfall Structure	▪ Structure in which Backstop Parties agree to the order in which they will fulfill their backstop commitments, such that certain investors are more likely to fund a shortfall than others ▪ Can be combined with a tiered backstop fee in which certain Backstop Parties get paid a larger fee in exchange for a greater probability of funding

Exit Financing Trends: Lender v. Lender Issues

- Rights Offerings
  - Holders of particular claims are given the right to purchase, in satisfaction of their claims, a prorated amount of securities as a discounted value
  - To guarantee the debtor sells the securities needed to meet funding expectations, debtors often negotiate with a subset of creditors, who agree in advance to backstop the offering, usually in exchange for a fee or premium (cash or additional securities paid in kind)
  - Creditors who are not invited to backstop often complain that they are receiving unequal treatment in violation of Bankruptcy Code section 1123(a)(4), which requires "the same treatment for each claim . . . of a particular class",
  - Courts routinely permit rights offerings, however, where debtors and the participating parties can show that the differing treatment is based on a separate right or contribution – i.e., the risk accompanying the agreement to be bound, as opposed to additional distributions on account of identical claims

- Historic Cases
  - *CHC* (2017, N.D. Texas)*:* Excluded secured creditors objected to confirmation after they were not permitted to participate in the backstop and thus not entitled to a put option premium; their view was not that it should necessarily have been open to all parties, but certainly to them
  - *Peabody* (2018, E.D. Mo.): $750 million private placement of preferred stock to "qualifying creditors" upheld by the Bankruptcy Court, the District Court, and the Eight Circuit following objections by a non-participating group of creditors whose alternative proposals were rejected

Exit Financing Trends: Lender v. Lender Issues

ConvergeOne

- ConvergeOne filed a prepack in April 2024 with the support of about holders of about 80% of its first and 100% in voting of its second lien debt
- Plan included takeback paper and an equity rights offering, with the supporting lenders (i) directly purchasing $85.75 of new equity at a discount and (ii) backstopping 35% of the $159.25 rights offering, subject to a 10% put option premium owed to the same parties, in exchange for a fee equal to 10% of the total equity raise
- Objecting lenders, who had not been part of the negotiation, and who had submitted proposals post-petition, objected on several grounds:
  - Plan did not satisfy section 1129(a)(3) good faith requirement (and was subject to review under Delaware's entire fairness standard)
  - Plan violated section 1123(a)(4) under *203 N. LaSalle* because participating parties would be receiving consideration on account of their claims that others would not, and that the absence of a market test rendered the plan unconfirmable
- The Bankruptcy Court overruled objections, finding that entire fairness did not apply, but even if it did, the Debtors satisfied it and had proposed the plan in good faith, and that *203 N. LaSalle* did not create an issue outside the cramdown context, and where the deal had not been "struck in the dark" between the debtor and equity, and also found the deal passed market test muster and the consideration was not on account of claims
- However, on September 25, 2025, the District Court for the Southern District of Texas (Judge Hanen) reversed the decision, specifically finding that because the backstop opportunity was neither offered to all class members nor subject to a market test, the "exclusive opportunity constituted unequal treatment of members of the same creditor class" under section 1123(a)(4).

Exit Financing Trends: Lender v. Lender Issues

LATAM (S.D.N.Y. 2022)

- LATAM's proposed plan included a $5.442 billion capital raise
  - $800 million of new common stock and three series of convertible notes (Class A, B, C), all pursuant to rights offerings
  - Commitment Creditors agreed to backstop $400 million of and $3.296 billion of the Class C notes in exchange for a cash payment fee of 20% of the backstop commitments ($734m) and a holdback of 50% of the Class C notes
  - Backstop shareholders backstopped $400m of common and $1,373B of Class B, with no fee, but with expense reimbursement and indemnity benefits
- Nonparticipating creditors objected to both backstop motion and confirmation
- J. Garrity overruled both backstop motion and confirmation objections (an appeal of the backstop was dismissed by the District Court)
- Confirmed a plan granting backstop parties a 20% fee ($734 million) on equity issuance and holdback of 50% of Class C convertible notes