American Bankruptcy Institute

New York City Bankruptcy Conference

Private Credit Restructuring

Michael O'Hara, Moderator
Jefferies

Rodi Blokh
AlixPartners, LLP

Michael R. Handler
King & Spalding LLP

Andrew Hede
Accordion Partners

Vincent Indelicato
Proskauer Rose LLP

Lauren Krueger
Kohlberg Kravis Roberts & Co.

Ryan A. Maupin
Deloitte

Morgan O'Neill
Capital Solutions Group

Hon. Michael E. Wiles
U.S. Bankruptcy Court (S.D.N.Y.)

CONCURRENT SESSION

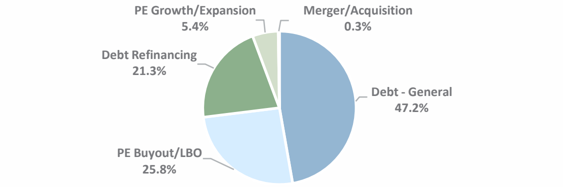
2024

Private Credit Overview

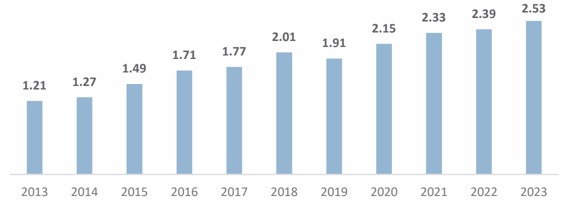
Characteristics

- **What is Private Credit?** Private Credit investments are debt-like, non-publicly traded instruments provided by non-bank entities, such as private credit funds or business development companies (BDCs), to fund private businesses. Private credit loans can include features uncommon to traditional bank loans, including a structured equity component, high prepayment penalties, or a role in oversight or management of the company[1]
- **Issuers:** Middle-market firms with annual revenues between $10 million and $1 billion, but the market has grown rapidly in recent years to fund larger companies that were traditionally funded by leveraged loans[1]
- **Distribution:** Private, small group, up to 15 creditors for larger financings[2]
- **Secondary Trading:** None
- **Credit Ratings:** Unrated

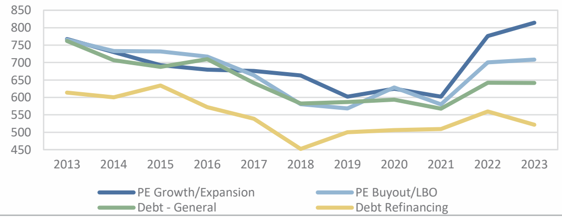
Private Credit Deal Types[1]



Average Number of Lenders Per Facility[1]



Average Loan Spread by Deal Type[1]



(1) Sourced from www.federalreserve.gov; *"Private Credit: Characteristics and Risks" by Fang Cai, and Sharjil Haque.*
(2) Sourced from DLD Private Data; *Maturity data is gleaned from the 2nd Edition of "Private Debt: Yield, Safety and the Emergence of Alternative Lending" by Stephen Nesbitt, founder of Cliffwater.*

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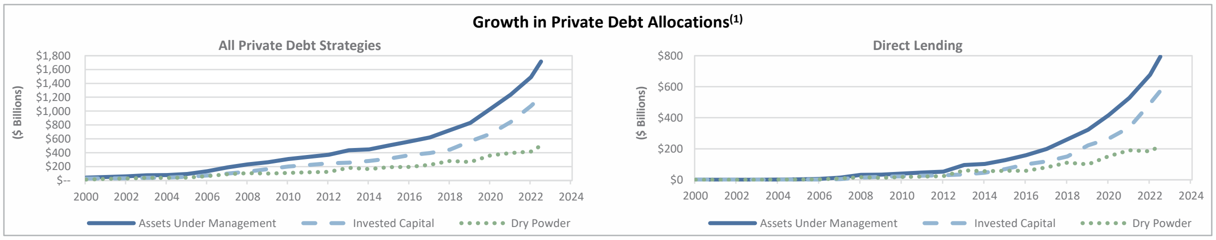
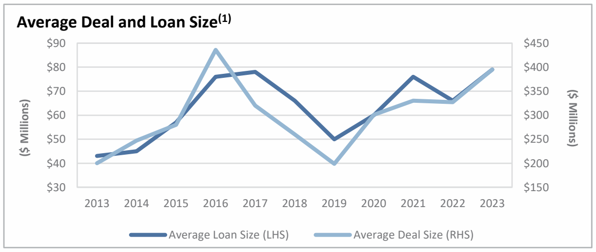
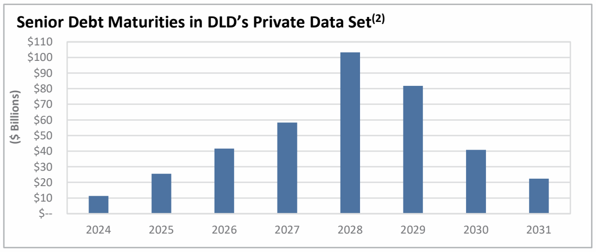
Size of the Private Credit Market







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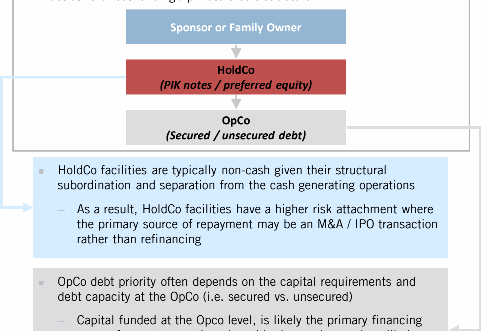
Typical Direct Lender / Private Creditor Stressed Credit Scenarios

Can either be HoldCo or OpCo lending structures with varying levels of collateral security and flexible structuring of economics

Common Private Credit / Direct Lender Structures

- *Illustrative direct lending / private credit structure:*



- HoldCo facilities are typically non-cash given their structural subordination and separation from the cash generating operations
  - As a result, HoldCo facilities have a higher risk attachment where the primary source of repayment may be an M&A / IPO transaction rather than refinancing
- OpCo debt priority often depends on the capital requirements and debt capacity at the OpCo (i.e. secured vs. unsecured)
  - Capital funded at the Opco level, is likely the primary financing source for any transaction alongside the revolver and ancillaries
  - Primary repayment sources for OpCo debt are disposals and / or refinancing

Typical Situations Jefferies Advises Direct Lenders / Private Credit

- Company underperformance, or sector dynamics lead to value erosion and / or declining LTV / covenant issues
- Inability or unwillingness of Sponsor or Family owners to inject new capital into the situation where it is required
- Impending debt maturities with no clear route to refinancing (or repayment via disposals); could be at HoldCo or OpCo level
- New money requirement at the OpCo with no obvious third party or equity (jr.) capital providers and / or sufficient mechanism to fund
- Loss of stakeholder confidence in the business or owners (e.g. other lenders, rating agencies, credit insurers, suppliers, customers, etc.)
- Governance issues – divergence in objectives between the business, lenders, or owners
- Breach of maintenance covenants, liquidity, fraud, or other direct triggers

Above scenarios often require lenders to take a proactive approach in order to limit collateral diminution and to protect their investment

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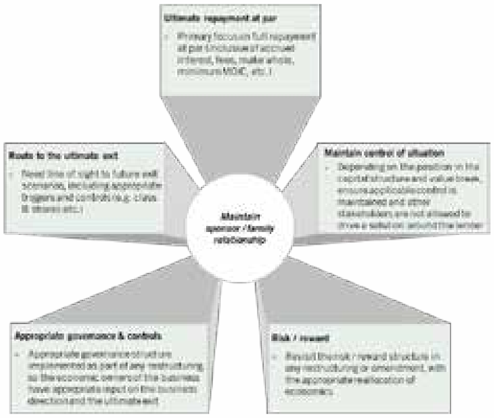
Core Objectives for Direct Lenders / Private Credit Lenders

Given stakeholder concentration, and the direct lender / private credit relationship focused ecosystem, when dealing with stressed credits there are a number of competing objectives that need to be balanced against the relationship with the sponsor or family owner

Key Objectives



Potential Conflicts vs. Relationship with Equity

- Given the private credit / direct lender ecosystem, maintenance of the relationship with the equity owners (i.e. sponsor / family) is typically the central objective
- Status of the corresponding other objectives and lender value of the central "relationship" will dictate which objectives take priority
- For example, in an effort to maintain the central "relationship" objective lenders may be hesitant to act quickly, leading to other creditors or stakeholders taking action and driving a resolution that may end in a sub-optimal outcome for the lender
- Sponsors / family owners may pressure the relationship importance in order to encourage the lender to drive a solution on a 'subsidized' basis for the sponsor / family
- There is often sensitivity around lenders insisting a new appropriate governance structure is put in place, given the wider relationship – this may include (among others):
  - Participation at a board level
  - Use of golden shares to drive an exit
- Hard wiring a route to exit is often very important, however, the risk is the exit triggers are watered down due to relationship pressure, which jeopardizes potentially achieving a full recovery / proper return

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Assessment of Situation

As well as understanding the credit, it is important to understand sponsor / lender relationship dynamics to work out the range of potential options available

Initial Credit Assessment

- Confirm core underperformance issues facing the company (liquidity, refinancing, litigation, fraud, etc.)
- Isolate areas of operational and / or financial performance concern impacting the business
- Assess achievability of the business plan
- Undertake valuation assessments to establish value break / fulcrum point and evolution over time
- Form internal view on range of solutions for the business
  - Assess new money investment required and debt capacity
  - Consider likely exit routes now and over time – M&A, Disposals, refinancing, etc.
  - Confidence in the management team?
- Identify triggers available to lenders and other stakeholders, including associated timing of such triggers
- Review credit documents for areas of weakness / risk and strength / leverage
- Assess positions and motivations of other stakeholders, including management and equity owners

Sponsor Relationship

- Assess internal sponsor / equity owner relationship and importance to lender's portfolio of existing credits and new credit origination capabilities
- Gauge importance of the business to the equity owner's portfolio and their realistic long term view on their equity value / position in the business
  - What returns / cash have the equity owner extracted from the business to date
  - Consider M&A environment and economics of a forced sale
- Are the equity owner's and / or management asleep at the wheel or actively developing a solution
  - Determine if management / equity owner are consistent in communication with the lenders regarding performance and issues (or are they doing the bare minimum)
  - If no action plan exists at all is sponsor walking away / in denial / being difficult?
- Develop an internal view on relationship importance with the equity owner and consider in conjunction with the owner's "current" view of their equity position
  - Is the equity owner realistic about the value of their equity in the context of the facts of the current situation or in 'denial'

- Ideal solution(s) vs. bare minimum solution
- Consider the ability to exit now, what an exit would provide for the lender(s) and owners, and therefore whether likely to get sufficient stakeholder buy in
  - Assess structured exit overtime, depending on comfort around floor value and growth potential
    - Gauge market sentiment and what is likely to happen to value over the short to medium term (multiples, buyer interest etc.)
  - Explore sale if the business is "broken" or continuing to deteriorate with limited growth prospects in the near to medium term – better to take a loss now instead of a greater loss in 3+ years
- Form view on most aggressive transaction the lender is willing to pursue, if needed
  - Take keys / own the business and implement new governance structure (likely to be ultimate backstop and provide strongest negotiating position)
    - Need a robust view on the ability to ultimately implement a successful exit
  - Requires diligence from an M&A perspective
- Consider protections required as a result of any transaction structure where the lender remains involved
  - Maintenance covenants, reporting covenants, tighter baskets, new money, governance, etc.
- Future exit milestones and ability to drive

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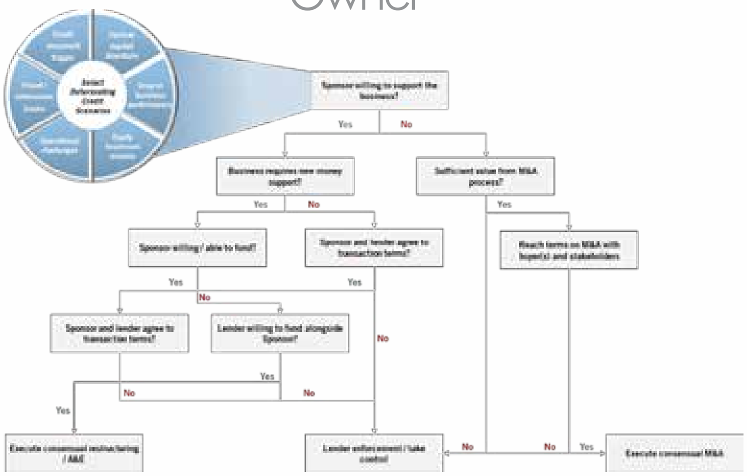
Lender Road Map to Engagement with Sponsor or Family Owner



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Spectrum of Transaction Structure Options

The usual spectrum of options typically available range from amend & extend to enforcement. We often see an M&A process as a compromise or the backstop to no agreement on alternative transactions or resolutions

Amend & Extend	M&A	Restructuring	Enforcement
• Work alongside management and the equity owner to develop a consensual resolution – May involve extension of maturity and gives/gets on economics and other key terms – Can be implemented consensually (out of court) or through a scheme or restructuring plan • Equity owners and lender(s) consensually agree on funding terms of any potential capital need • Assess the business plan to ensure the proposed transaction properly positions business to provide a successful exit and return for its stakeholders • A transaction may be implemented in steps, however, ensure no single transaction is executed in isolation without a comprehensive view toward how the lender will receive a successful exit	• Equity owners drive M&A process to exit and repay lenders – Set up regular cross-party update / progress meetings – Request dataroom / materials access as appropriate • Lender involvement will decrease/increase depending on where value of bids break – The lender should ensure equity owners understand paydown expectations (i.e. make whole, prepayment premiums, etc.) – Conduct M&A-type diligence concurrent to the 3rd party sale process to determine if the lender is willing to own the business or willing to sell if bids break in the debt • If equity owners move to abandon the sale process due to valuation concerns, the lender should communicate what they will require from the equity as return for more time / runway	• Work alongside management and equity to find a consensual resolution – May involve equitization of debt, recapitalization supported by lender and sponsor, structured return waterfall, etc. – Can be implemented via an out-of-court transaction, a scheme, a restructuring plan, or other court processes • Equity and lender consensually agree on funding terms of any potential capital need • Understand voting thresholds and requirements to ensure a transaction can be delivered • Develop appropriate go-forward governance structure to protect the lender • If the lender is to receive equity-like instruments, assess the business plan from an M&A / ownership perspective and ensure proper returns	• Equity and lender are unable to agree to the terms of a transaction or equity prefers to turn the keys over to the lender • Understand enforcement requirements and implementation to ensure a smooth transition of keys to the lender • Conduct accelerated M&A style due diligence to assess the state of the business, go-forward plan, and any issues awaiting the lender taking the keys • Determine if the lender wants to remain involved in the business to grow value or conduct an exit / sale process • Governance structure will need to be reworked • Ensure a communication plan in place for management, key customers, key vendors, etc.
• **Ensure the proposed transaction provides a clear path to an exit and proper return for the lender as opposed to a "band-aid" solution**	• **If value indications break in the debt, the lender may need to drive the sale process alongside the Company** • **If equity owner abandons the sale process, the lender should communicate their ability or inability to extend their debt and the associated cost**	• **A strong governance structure is imperative in any scenario where the lender takes equity risk** • **Ensure the transaction provides line of sight to a future exit**	• **Key to understand enforcement requirements and conduct detailed due diligence on an accelerated basis** • **Determine sooner than later if the lender wants to hold business or exit immediately**

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Key Areas of Focus for Lenders under Various Transaction Solutions

Amend & Extend

- Comfort with the trajectory of the business and management team capabilities
- Alignment with equity on respective longer term goals
- Diligence business plan
- Confirm proposed transaction structure aligns with the business plan to position the company to refinance its capital structure in the future
- Reset maintenance covenants in light of current and projected financial performance
- Tighten credit documentation to protect lender, while ensuring operations and success of business are not overly constrained
- Assess any required improvements in reporting standards
- Consider implementing milestones as appropriate (situation specific)
- Equity option value or other upside economics in return for agreeing to a delayed exit

M&A

- Equity and company advisors led process (input and engagement with lenders' advisors)
  - Lender participation is key to ensure buyers take the process seriously
- In the background, lenders should prepare for a downside scenario where they need to decide on owning the business vs. selling for a discount
- Conduct concurrent M&A "lite" due diligence on the business (i.e. receive access to sale process VDR, IM's, etc.)
- Prepare valuation to assess internal view on enterprise value
- Assess appetite to own business if bids come in below the debt
- Determine if there is a feasible plan B (i.e. A&E or restructuring transaction) if the sale process doesn't generate sufficient equity value and equity pushes to hold the business
- Conduct preliminary work on triggers available to lenders and enforcement actions to the extent alignment between the equity and the lender start to diverge

Restructuring

- Comfort with longer term prospects of the business
- Assess management team and determine if adjustments are needed
- Alignment with equity on respective longer-term goals
- Conduct M&A style diligence of the company and business plan given potential equity risk assumed via the restructuring
- Prepare valuation which will be required to finalize the transaction structure (i.e. debt sizing, equity splits, management incentives, etc.)
- Confirm proposed transaction structure aligns with business plan to position the lender for an eventual exit
- Implement strict governance structure due to resulting equity risk
- In the event equity owners remain involved, ensure incentives are aligned with the lender
- Ensure pathway for lender to take control or force exit as needed if business plan does not pan out

Enforcement

- Develop enforcement and communication action plan to limit disruption to the business
- Ensure current equity or other stakeholders who are going to be impaired are not imperative to the business's success (or are aligned with approach)
- Conduct accelerated M&A style due diligence to assess state of the business
- Prepare status quo valuation and future valuation to develop internal views on value break for the business
- Determine if lender wants to remain involved in the business to grow value or pivot to conducting an exit / sale process
- Assess management team and if adjustments are needed
- Prepare detailed and realistic business plan under an enforcement / ownership scenario and consider resulting exit considerations for the lender (i.e. does business plan indicate lender should exit immediately or in the future)
- Governance structure will need to be reworked

Faculty

Rodi Blokh is a partner and managing director at AlixPartners, LLP in New York and has significant restructuring, corporate strategy and transaction experience. He co-leads the firm's lender advisory service offering, and has advised lenders and other creditors across the capital structure on maximizing creditor recoveries in distressed situations. In addition, Mr. Blokh advises management teams and boards of directors when representing distressed companies. His expertise includes developing and implementing strategies to enhance enterprise value and recoveries, along with long-term business plan development, near-term liquidity analyses, transaction structuring and contingency planning. Mr. Blokh is a recognized expert in restructuring, and he has provided testimony in support of clients in a number of situations. Prior to joining AlixPartners, he covered energy and power at Bank of America Merrill Lynch, evaluating and executing financing for M&A, distressed debt and general liquidity purposes. Mr. Blokh received his B.S. in finance from Rutgers University and his M.B.A. from U.C. Berkeley's Haas School of Business.

Michael R. Handler is a partner in King & Spalding LLP's Financial Restructuring practice in New York. He focuses on representing lenders and bondholders across the capital structure and companies in all aspects of workout, restructuring, special-situation financing matters and distressed M&A transactions. He also has significant experience in connection with investment manager and broker-dealer liquidations and wind-downs. Mr. Handler is at the forefront of intercreditor litigation and related issues, having led significant matters concerning the protection of minority lender rights in the Ascena Retail Group, Inc. and 24 Hour Fitness chapter 11 cases and the ongoing Boardriders, Inc. litigation in New York Supreme Court. He is a noted authority on such issues, having appeared on panels and/or podcasts for Debtwire and Bloomberg's The Brink. Mr. Handler has been recognized by *Turnarounds & Workouts* as a 2023 Outstanding Young Restructuring Lawyer and by *The Best Lawyers in America*'s Ones to Watch for Bankruptcy and Creditor/Debtor Rights/Insolvency and Reorganization Law in 2021, 2022 and 2023. He also devotes significant time and resources in support of New York philanthropic initiatives, including as an active fundraiser for Tina's Wish and a member of the UJA Federation's NextGen Bankruptcy & Restructuring Committee. Mr. Handler received his B.A. and M.A. in history *summa cum laude* from Emory University, and his J.D. *cum laude* from Northwestern University School of Law, where he served as an executive articles editor of the *Journal of Criminal Law and Criminology*.

Andrew D. Hede is a senior managing director with Accordion Partners in New York and heads its Turnaround & Restructuring Practice. He has 30 years of financial and operational transformation and restructuring experience in both the U.S. and Australia, advising clients in numerous formal and out-of-court restructurings. Mr. Hede specializes in advising companies, creditors and equity sponsors in distressed and nondistressed situations, with a particular focus on financial and operational reviews, liquidity management, performance improvement, business and asset divestment, business plan preparation and review, recapitalization strategies, and negotiation of reorganization plans. His experience covers a broad range of sectors, with experience in consumer products and retail, real estate and construction, media and telecom, and transportation and distribution. In addition to his advisory experience, Mr. Hede has regularly served in an interim management capacity, including as CEO, president, CRO and chief transformation officer. Prior to joining Accordion, he was a partner and U.S. head of Restructuring at McKinsey & Company. Mr. Hede received his B.Com. in accounting and business law from the University of Melbourne and is a member of Chartered Accountants of Australia and New Zealand.

Vincent Indelicato is co-head of the Business Solutions, Governance, Restructuring & Bankruptcy Group and a member of the Private Credit Restructuring Group of Proskauer Rose LLP in New York. His practice focuses on corporate restructurings, with an emphasis on the representation of direct lenders, ad hoc groups, bondholders and creditors' committees both out of court and in chapter 11. Mr. Indelicato is frequently consulted by leading distressed hedge funds, BDCs, private credit lenders, private-equity investors and creditors on complex domestic and international insolvency and restructuring issues, including intercreditor and interlender matters, across a variety of industries. He also was part of the firm's cross-disciplinary, cross-jurisdictional Coronavirus Response Team, helping to shape the guidance and next steps for clients impacted by the pandemic. Mr. Indelicato was honored as one of ABI's 40 Under 40 and as an Outstanding Young Restructuring Lawyer by *Turnarounds & Workouts*. In addition, he has been named a "leading lawyer" in *The Legal 500* and listed in *The Best Lawyers in America*. Mr. Indelicato received his B.A. from Haverford College and his J.D. from the University of Michigan Law School, and he was a visiting student at the University of Oxford from 2001-02.

Lauren Krueger is a managing director in Kohlberg Kravis Roberts & Co.'s Credit business in New York, where she leads corporate governance and restructuring efforts. She is a member of the firm's Global Corporate Private Credit Investment Committee and co-chair of the firm's Private Credit Portfolio Monitoring Committee. Ms. Krueger currently sits on the boards of directors of several KKR portfolio companies, including JW Aluminum Inc., PRG Worldwide Entertainment, Constellis and One Call. Prior to joining the firm, she was an independent fiduciary for Drivetrain Advisors, where she worked with investors to maximize value for stressed and distressed companies. Previously, Ms. Krueger served in investing roles at Esopus Creek Advisors and the D.E. Shaw Group and in restructuring advisory at Lazard Freres. Ms. Krueger serves on the advisory board of Columbia Business School's Heilbrunn Center for Graham & Dodd Investing. In addition, she currently sits on the board of directors of Her Justice, a nonprofit organization that provides free legal help to women living in poverty in New York City, and the board of trustees of Horace Mann School. Ms. Krueger received her A.B. from Princeton University and her M.B.A. from Columbia Business School, where she served as an associate adjunct professor of finance and taught the course "Misunderstood Securities" for several years.

Ryan A. Maupin is the national practice leader of Deloitte's Turnaround & Restructuring practice for the US and the Americas in New York. He has more than 20 years of experience advising boards, domestic and international company executives, secured and unsecured creditors, hedge funds and private-equity funds in transitional situations both in court and out of court. Mr. Maupin is primarily focused on advising clients in complex financial turnarounds, § 363 sale processes, debt-restructurings and liquidations. He was selected as part of ABI's inaugural class of "40 Under 40" in 2017. Mr. Maupin is a member of ABI, the Association of Insolvency and Restructuring Advisors, and the Turnaround Management Association. He received his B.S. from Millikin University.

Michael O'Hara is co-head of the U.S. and a managing director in the Debt Advisory and Restructuring Group of Jefferies LLC in New York. He advises on a variety of restructuring and special-situation assignments for companies, creditors, corporate boards, and acquirers and sellers of distressed assets. Additionally, he has worked on several sovereign situations. Mr. O'Hara's notable company/debtor assignments include AbitibiBowater, Akorn Pharmaceuticals, American Axle & Manufacturing, AIG, Ascent Resources Marcellus, Brock Group, Energy Future Holdings, EXCO Resources, Fusion Connect, Mallinckrodt, MoneyGram, Mrs. Fields, Quad Graphics (re: Vertis), RockPile Energy Services, Samson Resources, Southland Royalty Co., Taro Pharmaceutical, Travelport, Triangle Petroleum and Washington Mutual, among others. His creditor assignments have included Chaparral Energy, Dana, Delphi, Eastman Kodak, EP Energy, Extraction, Gulfport, Hostess Brands, Intrawest, Jupiter Resources, Lehman, Preferred Sands, Quicksilver Resources, Ultra Petroleum and Vanguard Natural Resources, among others. Mr. O'Hara has been a guest lecturer at the University of Chicago Booth School, Columbia Business School and the Wharton School at the University of Pennsylvania, among others, and has participated in many restructuring industry conferences. Before joining Jefferies, Mr. O'Hara was a partner in the Restructuring and Special Situations Group of PJT Partners (formerly Blackstone). He also previously worked in the M&A groups at Wasserstein Perella & Co. and Stephens Inc. Mr. O'Hara received his B.S. in finance from Georgetown University and his M.B.A. from Columbia Business School.

Morgan O'Neill is currently a portfolio manager with Capital Solutions Group in New York, where she evaluates investment opportunities for the Capital Solutions Strategy in the private credit vertical. She previously was with Sound Point and worked at HPS Investment Partners on its Specialty Loan Fund, where she underwrote and executed new investment opportunities. Prior to HPS, she was an investment banking analyst in the leveraged finance group at Bank of America Merrill Lynch. Ms. O'Neill received her B.A. in economics and B.S. in business administration *cum laude* from the University of North Carolina at Chapel Hill.

Hon. Michael E. Wiles is a U.S. Bankruptcy Judge for the Southern District of New York in New York, sworn in on March 3, 2015. Previously, he was a partner with Debevoise & Plimpton LLP, where he focused on general commercial litigation and bankruptcy. Judge Wiles co-authored the *Collier Business Workout Guide* (Mathew Bender 2007) and has appeared on panels organized by the Association of the Bar of the City of New York, the American College of Investment Council and others to discuss current issues in bankruptcy litigation. He is a former member of the Committee on Bankruptcy and Reorganization of the Association of the Bar of the City of New York. His publications and written CLE materials include "May Parties Consent to Bankruptcy Court Adjudication of '*Stern* Claims'" (September 2014) (presented at a continuing legal education session at the Association of the Bar of the City of New York); "Ponzi Schemes and Avoidance Actions: 3 Issues," *Law360* (March 7, 2011); "The Good Faith Defense to Fraudulent Transfer Claims" (December 2010) (presented at a continuing legal education session at the Association of the Bar of the City of New York); and "At the Crossroads: The Intersection of the Federal Securities Laws and the Bankruptcy Code," *The Business Lawyer* (November 2007). Judge Wiles received his A.B. from Georgetown University in 1975 and his J.D. from Yale Law School in 1978.