

Client Alert

Financial Restructuring Practice Group

June 1, 2015

Recent Unitranche Issues in the RadioShack Bankruptcy Case

As the market for so-called “unitranche” credit facilities continues to increase, the Delaware Bankruptcy Court had an opportunity recently to answer positively the question of whether bankruptcy courts will enforce the Agreement Among Lenders (“AAL”) (a form of intercreditor agreement) used in such structures. Unitranche facilities (sometimes also referred to as “First Out/Last Out” credit facilities) typically use one credit agreement secured by a single lien on the borrower’s assets, but also have a separate AAL that divides the lenders into two or more groups with different payment, voting, and other intercreditor rights and priorities. Commonly, the borrower is not a party to or even aware of the terms of the AAL. Unitranche transactions differ in important respects from traditional first/second lien credit facilities and thus create noteworthy challenges for secured lenders.

An important question in unitranche financing is whether a bankruptcy court will exercise its jurisdiction to enforce and construe an AAL in a borrower’s bankruptcy case where the borrower is not a party to the AAL. In a recent oral ruling in the *RadioShack* bankruptcy case, the Delaware Bankruptcy Court implicitly recognized the court’s ability to construe and enforce the AALs at issue.¹

Background

When it filed for bankruptcy, RadioShack Corporation (the “Debtor”) was financed, in part, by two separate unitranche facilities. The Debtor had a \$585,000,000 syndicated ABL facility (the “ABL Loan”), which was secured by: (1) a first-priority lien on the Debtor’s inventory and receivables; and (2) a second-priority lien on the Debtor’s other assets. Pursuant to the AAL governing the ABL Loan (the “ABL Loan AAL”), a group of various funds were the “first out” lenders (the “First Out ABL Lenders”) and an affiliate of Standard General LP was the “last out” lender (“Standard General”).²

In addition to the ABL Loan, the Debtor had a syndicated term loan in the amount of \$250,000,000 (the “Term Loan”), which was secured by: (1) a second-priority lien on the Debtor’s inventory and receivables; and (2) a first-priority lien on the Debtor’s other assets. Pursuant to the AAL governing the Term Loan (the “Term Loan AAL”), an affiliate of Cerberus Capital Management was the “first out” lender (“Cerberus”) and an affiliate of Salus Capital Partners was the “last out” lender (“Salus”).³

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After filing its chapter 11 case, the Debtor sought approval of an asset sale to Standard General pursuant to which Standard General would credit bid its portion of the ABL Loan. Several creditors objected to the proposed sale, and two objections implicated unitranche issues.

First, Salus objected to the sale arguing, among other things, that the process was fundamentally flawed and unfair.⁴ Cerberus supported the sale and argued that the Term Loan AAL prohibited Salus from opposing and objecting to any sale that Cerberus supported. Specifically, Section 14(c) of the Term Loan AAL provided that “no Last Out Lender [*i.e.*, Salus] shall object to or oppose any such sale on any grounds that only may be asserted by [a secured lender] if [Cerberus] has consented to such sale.”⁵

Second, the First Out ABL Lenders objected to the sale and argued that, pursuant to the terms of the ABL Loan AAL, Standard General could only proceed with a credit bid if *all* claims of the First Out ABL Lenders were satisfied. Although the First Out ABL Lenders were to receive 100% of their outstanding principal and interest at the closing of the sale, the First Out ABL Lenders argued that their claims included contingent indemnification claims and that additional sale proceeds should be withheld to satisfy contingent claims that may arise from pending litigation brought by the Official Committee of Unsecured Creditors against the First Out ABL Lenders.⁶

Sale Hearing and Rulings

On March 31, 2015, after a four-day, very contentious sale hearing, the Bankruptcy Court approved the sale to Standard General.⁷ Importantly, in its oral comments and findings, the Bankruptcy Court construed and enforced the Term Loan AAL and the ABL Loan AAL.⁸ The court did not issue a precedential ruling on this point, but this should give secured lenders some comfort that AALs will be enforced in bankruptcy proceedings.

With respect to Salus’s objection, the court held that, pursuant to the Term Loan AAL, Salus could not oppose the sale on grounds that only can be asserted by a secured lender but could assert objections that are otherwise available to a general unsecured creditor.⁹ Salus’s permitted objections, however, were overruled by the court.¹⁰

The First Out ABL Lender’s objection was not ruled on by the court. Instead, the parties reached a consensual arrangement to withhold approximately \$12,000,000 to satisfy the First Out ABL Lenders’ potential indemnification claims.¹¹ However, before this agreement was reached, the court made comments suggesting that although the potential indemnification claims were part of the First Out ABL Lenders’ valid claims, it would be unreasonable to withhold the full amount of the sale proceeds to secure these contingent claims.¹²

Conclusion

The RadioShack sale hearing provides secured lenders with comfort that bankruptcy courts will enforce AALs in unitranche facilities. This underscores the need to carefully draft such agreements in order to ensure the protections afforded by an AAL are not circumvented in a bankruptcy proceeding.

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¹*In re RadioShack Corp.*, Case No. 15-10197 (Bankr. D. Del.).

²*Declaration of Carlin Adrianopoli in Support of First Day Pleadings (In re RadioShack Corp.)*, Case No. 15-10197, Docket No. 17, at 6–8 (Bankr. D. Del. Feb. 5, 2015).

³*Id.* at 9.

⁴*Obj. of Salus Capital Partners, LLC to Debtors' Sale Motion (In re RadioShack Corp.)*, Case No. 15-10197, Docket No. 1503, at 1 (Bankr. D. Del. Mar. 25, 2015).

⁵*Statement of Cerberus Lenders in Support of Sale to General Wireless, Inc. (In re RadioShack Corp.)*, Case No. 15-10197, Docket No. 1551, at 2–3 (Bankr. D. Del. Mar. 26, 2015).

⁶*Obj. of The First Out ABL Lenders*, Case No. 15-10197, Docket No. 1549, at 8–10 (Bankr. D. Del. Mar. 26, 2015).

⁷*Order Authorizing Sale*, Case No. 15-10197, Docket No. 1672 (Bankr. D. Del. Apr. 1, 2015).

⁸Hr'g Tr. 19–20, Mar. 30, 2015 (Afternoon Session). It does not appear that any party raised a subject matter jurisdiction objection to the Bankruptcy Court's consideration of the AALs.

⁹Hr'g Tr. 64, Mar. 31, 2015 (Afternoon Session) (noting that the Term Loan AAL restricts Salus's authority to raise certain objections).

¹⁰*Id.* at 63–64.

¹¹*Order Authorizing Sale*, Case No. 15-10197, Docket No. 1672, at 33 (Bankr. D. Del. Apr. 1, 2015); Hr'g Tr. 17, Mar. 31, 2015 (Afternoon Session).

¹²Hr'g Tr. 19–20, Mar. 30, 2015 (Afternoon Session).