




## Lyondell Case Shows Bankruptcy Loans Are Available for a Price

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By Tiffany Kary



Feb. 4 (Bloomberg) -- **Lyondell Chemical Co.** obtained the biggest bankruptcy loan in history last month, the product of an eight-hour hearing running past midnight in a darkened Manhattan courthouse where hedge funds and banks fought to join the deal.

Though dozens of lenders sought to fund the \$8 billion "debtor in possession" loan, allowing the chemical maker to stay in business, the scrum by no means spells the end of the credit crisis. **Chris Taggart**, a senior loan strategist at CreditSights Inc., said only firms willing to pay higher fees and interest can

get loans.

"The DIP market has opened up, but at a price," said Lyondell lawyer **Deryck Palmer**. The loan "shows the pricing and incentives that have to be put into DIP financing to encourage lenders to participate."

The increasing frequency of DIP loans that "roll up" old loans with the new lending, giving the combined debt priority over other company obligations, is a sign that bankrupt companies are still having a tough time getting loans, lawyers said.

"DIPs are still hard to come by as the cost of capital is extremely high," Taggart said, noting that Lyondell's loan came with 13 percent interest and 7 percent in fees. Some of its lenders may end up getting 20 percent on their one-year **investment** in the loan, which matures Dec. 15, according to a report from Standard & Poor's.

'Creative Thinking'

"We will see more creative thinking on DIPs to get people involved," said attorney Rick Hyman, a partner at Mayer Brown.

Lyondell, based in Houston, listed assets of \$27.1 billion, debt of more than \$19.4 billion and 25,000 creditors in a Jan. 6 bankruptcy petition filed in U.S. Bankruptcy Court in Manhattan. Lyondell cited a "dramatic softening in demand" and volatility in raw materials costs, and needed a \$100 million "super-emergency" loan to keep running while it sought a DIP loan that could fund it through reorganization, according to court papers.

Without a DIP loan, bankrupt companies have two options: liquidation or an out-of-court restructuring, the second of which doesn't protect the debtor from lawsuits.

Both options are bad for lenders who fronted money to the company before it sought court protection. So bad, in fact, that most DIP loans where existing lenders take part are called "defensive DIPs," as they seek to protect outstanding debt by lending even more money.

Lenders who take part in a DIP loan get a "priming lien," a legal claim to a bankrupt company's assets

that supersedes claims by pre-bankruptcy lenders who don't take part.

#### Largest Participants

The largest participants in Lyondell's loan were UBS AG, with \$770 million; Apollo Management LP with \$710 million; Cerberus Capital Management LP with \$237.5 million; and ABN Amro Holding NV with \$230 million. Silver Point Capital LP, Angelo Gordon & Co. and Appaloosa each contributed \$200 million.

In Lyondell's DIP arrangement, for every new dollar extended as part of the DIP financing, a parallel dollar of a lender's pre-bankruptcy loans would gain the same level of protection.

Fourteen lenders advanced \$3.25 billion in new money to Lyondell, giving them greater protection on the same amount of old debt.

The value at which those different types of Lyondell debt are trading in the secondary market may be a strong indication that lenders who contributed new money can expect much greater recoveries.

After the Jan. 7 court hearing where the DIP financing was arranged, the new money in Lyondell's loan traded at around 96 to 98 cents on the dollar; the rolled-up pre-bankruptcy debt traded at 65 to 75 cents; and the non-rolled up pre-bankruptcy debt traded at around 31 to 36 cents, according to Standard & Poor's.

#### Primary Incentive

The primary incentive for lenders who are wandering back into the DIP financing market is the potential for profit.

"The best reason to consider a DIP is because of the fees," said attorney Brian Trust, also of Mayer Brown.

**David Ying**, a senior managing director at investment bank Evercore Partners Inc. who testified at Lyondell's hearing, said his phone was "ringing off the hook" from prospective lenders.

The Lyondell DIP loan was expensive relative to a year ago, but similarly priced to other recent DIPs, according to **Mohsin Meghji**, founder of restructuring adviser Loughlin Meghji.

Bankrupt Tronox Inc.'s \$125 million, 12-month revolving DIP loan was priced at Libor, or the London interbank offered rate, plus 950 basis points. VeraSun Energy Corp.'s \$20 million loan was at Libor plus 1000 basis points. Libor is the rate at which banks borrow from each other.

Over the past five months, the mean price of a DIP loan has been around Libor plus 640 basis points.

#### 'Last 5 Months'

"Even in the last 5 months, rates have gone through the roof," said Meghji. "Compared to a year ago, it's a sea change."

DIP fees are also rising. Tronox, an Oklahoma City-based maker of the whitening pigment titanium dioxide, disclosed that lead arranger Credit Suisse Group AG will get a 3 percent fee for syndicating the loan, according to court papers.

According to Loughlin Meghji, the mean for fees has been 306 basis points over the last five months. Lyondell's loan was 350 basis points and Lenox Group Inc., a bankrupt maker of fine china and gifts, had a fee of 450 basis points. Several loans also contain extra requirements. For example, Tronox's loan, at 300 basis points, also had a \$175,000 up-front fee plus another \$175,000 annual fee to Credit Suisse.

Lenders are seeking other unusual protections as well, including holding a property deed in lieu of foreclosure, said lawyer Heidi Sorvino, head of the bankruptcy practice at Smith Gambrell & Russell.

#### 'Almost Impossible'

"It's almost impossible to get a DIP. If you can, lenders are asking for everything under the sun," Sorvino said. DIP loans are particularly critical in real estate investments, as they're needed to finance

construction, she said.

DIP loans were once considered the safest type of loan because the lenders are first in line to be repaid when a company exits bankruptcy. The declining value of receivables in a down economy, however, is making DIPs riskier.

"The perceived risks associated with DIP lending have increased materially as business failure rates have increased," said **David Pauker**, a restructuring adviser at Goldin Associates.

Pauker said lenders, once willing to advance as much as 90 percent of receivables' estimated value, have in some cases reduced rates to 75-80 percent.

#### More Demanding

As lenders become more demanding, some companies are saying the covenants of their DIP loans may cause them to default, defeating the purpose of the loan -- to allow the company to continue operating until it emerges from bankruptcy.

Lenox Group fought with Bank of New York Mellon Corp., an agent to the company's pre-bankruptcy lenders, over its right to use money from an \$85 million DIP loan. Bank of New York argued that the financing, which came at a cost of \$2.55 million, was "illusory" and had unreasonable repayment deadlines that may push it into default.

"Some types of DIPs are riskier than others. That is a product of the business a company is in," Hyman said, citing quickly depreciating collateral at retailers as an example.

DIP lenders who expect to be paid back when a company exits bankruptcy may also come up short when exit financing fails.

Delphi Corp., the bankrupt auto-parts maker, battled with lenders over forbearance on its DIP loan last year. Portions of Delphi's \$4.35 billion loan trade at around 16 cents on the dollar, according to Markit.

"The ability to exit the lending packages is suspect," Taggert said.

The case is *In re Lyondell Chemical Co.*, 09-10023, U.S. Bankruptcy Court, Southern District of New York (Manhattan).

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