

Momentive Ruling Highlights Risks to Senior Creditors Under Intercreditor Agreements

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In the wake of the recent Momentive ruling on cramdown plan confirmation ([discussed in our recent client memorandum](#)), on September 30, 2014, the bankruptcy court also rejected the senior lien creditors' efforts to make up their losses by obtaining a recovery from the second lien noteholders pursuant to the applicable intercreditor agreement. Although the intercreditor agreement prohibited the second lien noteholders from receiving proceeds of the "common collateral" before payment of the senior lien notes in full in cash, the court held that the equity distributed to second lien noteholders did not constitute proceeds of common collateral, and that other actions taken in support of the plan by the junior lienholders did not violate the intercreditor agreement. This holding highlights the limited protection offered by lien subordination, as compared to payment subordination, unless the relevant agreement is carefully drafted to protect the senior creditor, which the market often does not permit. Furthermore, the decision shows that the carefully crafted prohibitions an intercreditor agreement places on second lien creditors can be swallowed by overbroad language preserving those creditors' rights to participate in the bankruptcy proceedings as unsecured creditors.

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