XAIA INVESTMENT
Perspectives

June 10, 2025

"Secured Twice, Nice?" – Value Transfers Through Double Dips

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In our last two editions, we explored how value transfers – strategic shifts of economic value within a capital structure – have become a defining feature of modern liability management exercises (LMEs). These tools often favor a select group of creditors, challenging traditional notions of pari passu treatment and introducing new risks for investors.

This month, we focus on double dips – a once-niche liability management strategy that has now become a headline tactic in modern credit restructurings. A double dip gives a lender two enforceable, often secured, claims against the same underlying collateral: one directly through a parent guarantee, and another indirectly through a pledged intercompany loan. While no additional capital is provided, the lender's structural position is dramatically improved – often to the detriment of legacy creditors.

What Is A Double Dip?

To borrow the well-worn metaphor: imagine dipping a nacho chip into guacamole, taking a bite, and dipping again. The guacamole is the collateral pool – and a double dip gives certain creditors two bites at it.

A double dip transaction is a capital structure arrangement designed to allow a creditor to have two enforceable claims tied to a single economic exposure. In essence, it transforms one loan into two paths for recovery – typically by structuring a new loan through an intercompany funding chain. It is primarily used in distressed or opportunistic capital raises to attract new money by offering enhanced recovery scenarios, without triggering formal subordination.

The mechanics follow four distinct steps:

1. **Creating the Subsidiary:** A non-guarantor restricted subsidiary is formed. It may or may not be part of the existing credit group, depending on the company's debt document flexibility. This subsidiary is a shell, with no operations (HoldCo). Its only purpose is to facilitate the transaction.

2. **Issuing the Subsidiary Debt:** The subsidiary borrows money (New Debt).

3. **Guaranteeing the Subsidiary Debt:** The ParentCo formally guarantees the New Debt, and the guarantee is secured by the same first-lien collateral package that supports the group's existing first-lien obligations. The new money provider now holds a **direct senior claim against the ParentCo.**

4. **Creating the Intercompany Loan:** The issuing HoldCo on-lends the funds to the ParentCo, typically under an intercompany loan agreement to the parent or another OpCo. The subsidiary then pledges the intercompany loan receivable it received, giving creditors a second, **indirect claim on the same assets**.

In this structure, the HoldCo holds a single asset – the intercompany loan receivable – and a single liability – the New Debt. Because both the guarantee and the pledged receivable are backed by the same collateral, lenders benefit from dual avenues to enforce repayment.

To illustrate: a lender providing $500 million in new financing ends up with two $500 million claims – one from the guarantee, one from the pledged intercompany loan. While recovery remains capped at $500 million, the dual claims improve positioning in a restructuring.

Economically, the lender has not increased its risk exposure or extended more capital. Instead, the structure enhances their recovery prospects by positioning them more favorably in the event of a restructuring, often at the expense of legacy creditors who only hold a single claim.

In a restructuring or insolvency, the lender can assert **a claim against HoldCo's estate** (intercompany loan receivable) and a **claim through the HoldCo's rights as a pari-passu creditor of ParentCo**. Thus, the lender has effectively "dipped" twice into the group's asset base.

Why Are Double Dips Possible?

For a double dip to work, each leg of the transaction must be allowed under the issuer's existing debt documents. The feasibility hinges on the interplay of several key covenants, such as debt covenants.

Double dips only works if all of the four steps are simultaneously permissible under the documents. What makes the double dip viable is not only creativity, but careful reading of the language – and the presence of just enough flexibility to allow it.

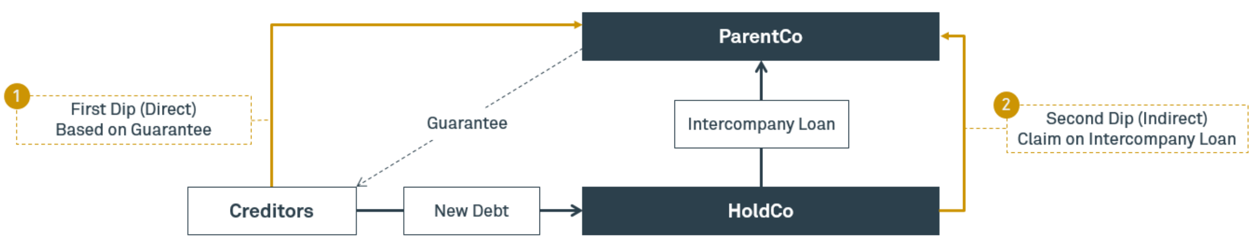
One high-profile example that illustrates the constraints of creative restructurings is the Serta Simmons transaction, we discussed in our last letter. In that case, Apollo was outmaneuvered during negotiations because only $675 million in asset value could be transferred to an unrestricted subsidiary (HoldCo). This limitation imposed a natural cap on how much new-money could reasonably be lent to the unrestricted entity and, by extension, constrained the amount of existing debt that could be restructured or exchanged as part of the drop-down. The narrow transfer capacity ultimately curtailed Apollo's competing proposal and cleared the way for Serta's now-infamous uptiering deal.

Why It's Gaining Traction?

Double dip structures have grown increasingly popular in recent restructuring and financing scenarios, primarily because they offer enhanced economic incentives for new money providers. By creating two recovery paths on the same underlying value, these structures can significantly improve the likelihood and scale of recovery for fresh capital, especially in distressed situations where traditional security packages may not suffice to justify the risk.

From the perspective of the issuer, double dip transactions serve as a powerful tool to attract liquidity without having to formally subordinate existing creditors. By routing the new loan through a holding entity and on-lending to the parent company, borrowers can offer better structural positioning to new lenders – sometimes without breaching existing documentation.

FIGURE 1: DOUBLE DIP LEADS TO DILUTION OF EXISTING CREDITORS
Pre- and post-transaction capital structure comparison



Source: Company reports, XAIA Investment GmbH

What further adds to the appeal is the legal flexibility of the structure. If carefully documented, the intercompany lending arrangement and the dual claim structure can be designed to avoid triggering negative covenants or intercreditor restrictions, making it especially attractive for sponsors seeking to execute a liability management exercise without provoking immediate creditor resistance.

Risks and Market Concerns

However, while the structure may look clean on paper, it can introduce significant risk for legacy creditors. The most immediate concern is economic dilution. The new lender's claim, backed by both the assets of the ParentCo and the pledged intercompany receivable, effectively reduces the value available for recovery by the original creditors. What was once a single claim on the group's asset base becomes a two-tiered claim structure, skewing the recovery waterfall.

The complexity of these arrangements can also disrupt the existing intercreditor balance. Because double dip lenders may sit structurally senior to other creditors – or hold claims through multiple levels of the group – intercreditor negotiations become more complicated and often contentious.

However, the enforceability of these arrangements is not guaranteed. Whether the second layer of recovery – the intercompany receivable – is honored in insolvency proceedings depends heavily on jurisdiction, documentation, and the recognition of upstream guarantees or internal loans. In multi-jurisdictional groups, this becomes especially murky, adding an extra layer of legal uncertainty.

European Developments

Originally a U.S. innovation, double dip transactions are gaining momentum in Europe, with regional variations in structure and legal complexity. Recent cases involving companies like Adler Group, Intrum, and Ardagh highlight growing interest in these features as part of liability management strategies.

A major enabler is the use of flexible holding company structures in jurisdictions like Luxembourg and the Netherlands, which offer favorable rules on intercompany lending and insolvency ring-fencing. These allow sponsors to replicate the economic effect of U.S.-style double dips within European legal constraints.

New restructuring regimes – such as the UK's Restructuring Plan, Germany's StaRUG, and the Dutch WHOA – also support these strategies by enabling companies to bind dissenting creditors and implement layered recovery structures. Additionally, the growing use of New York law–governed (NYL) bond documentation in European capital structures – illustrated in deals like Hunkemöller – provides the covenant flexibility and creditor hierarchy mechanics needed to implement double dip features more effectively.

However, investor pushback is growing. Creditors are demanding tighter controls on intercompany transfers and more transparency around the impact on existing security and priority rights. While still legally viable and structurally appealing, double dip transactions in Europe are likely to attract increased scrutiny going forward.

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Philipp Graxenberger and Josef Pschorn oversee Alternative Credit Strategies at XAIA Investment, specializing in identifying inefficiencies in the credit market, particularly within complex capital structures and special situations. Their expertise spans credit arbitrage, relative value, special situations, and restructurings.