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Five Notable Arguments Worth Paying Attention to in STG Logistics' LMT Litigation

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The Bottom Line™:

- STG Logistics engaged in a liability management transaction in October 2024 which included drop-down, uptiering, and double dip components.
- Certain holdout lenders commenced litigation against the company in January 2025, with a motion to dismiss filed in March 2025, and oral arguments held in August 2025.
- The case has caught the attention of the market at large as it touches on a number of issues relevant to liability management practice.
- In advance of an expected decision on the motion to dismiss in the near term, we discuss five arguments raised in the course of the litigation and their potential implications on LMTs going forward.

Overview

STG Logistics (the "Company" or "STG") and its ongoing litigation with certain creditors has caught the attention of the broader market in recent months, unsurprisingly so given that the case addresses a liability management transaction—the boogeyman of investors everywhere.

STG's transaction (the "LMT")—which closed in October 2024—was a complex mélange of J. Crew-style asset drop-downs, unrestricted subsidiary debt issuances, multiple tiers within the new debt, coercive exchange mechanics, and even a double dip component. Though the LMT was supported by a wide range of creditors, two holdouts—Siemens and Axos (the "Plaintiffs")—did not participate and sued the Company, the administrative agent (Antares Capital) and majority participating lenders (the "Defendants") in the Supreme Court of the State of New York, New York County (the "Court")[1] on January 30, 2025 via an amended complaint (the "Amended Complaint").[2]

The Amended Complaint asserted a number of causes of action, including breach of contract, breach of the implied covenant of good faith and fair dealing, and fraudulent transfer. The Company filed for a motion to dismiss (the "Motion to Dismiss") on March 31, 2025, supported by separate motions filed by the agent

[1] Despite its lofty name, the "Supreme Court" in New York State is the trial level of courts in the state (though anyone who has a passing familiarity with any of the various Law & Order series probably already knew that).
[2] The Amended Complaint can be accessed here. Other filings from the case can be accessed on the New York State Unified Court System website.

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and participating lenders, and oral arguments were held this past summer (the transcript for the oral arguments as filed in the case docket is referred to in this report as the "Oral Arguments Transcript").[3]

With Judge Anar Patel's decision expected in the coming months, the market should clearly understand the mechanics behind the LMT as well as salient arguments raised in the course of the litigation. How Judge Patel will rule on these, and other, points could have significant impact on liability management practice going forward. For purposes of this report, we do not discuss the causes of action relating to fraudulent transfer under New York's Uniform Voidable Transactions Act or related jurisdictional arguments.

A Review of STG's 2024 LMT

STG's LMT was a complicated transaction with multiple components. The story begins with the Company's acquisition of the intermodal division of XPO Logistics in March 2022, which was financed by the broadly syndicated loan market under a Credit Agreement, dated March 24, 2022 (the "Credit Agreement"). At closing, the facilities consisted of a $725 million first lien term loan and $150 million of pari passu first lien revolving commitments.

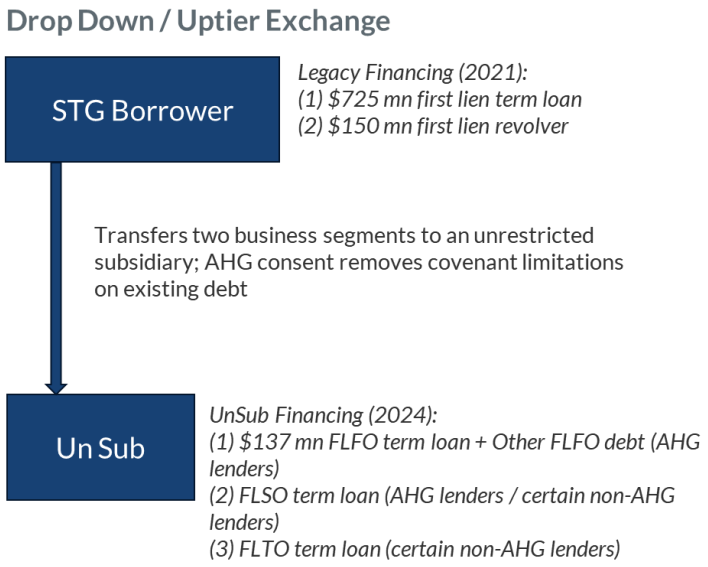
The Company enjoyed positive performance in the first year after the financing, driven primarily by post-COVID demand for freight services. However, fortunes began to falter thereafter due to a number of macro-economic factors, including shifting market trends as well as "strikes, labor shortages, and increased regulatory pressures."[4] By May 2024, liquidity constraints forced the Company to enter into a stop-gap amendment to the Credit Agreement (the "Fifth Amendment"). The Fifth Amendment afforded the Company with a seven-quarter holiday with respect to the revolving facility's financial covenant (through Q3 2025), while imposing additional protections for lenders designed to inhibit non-pro rata transactions and transfers to unrestricted subsidiaries. Concurrently, the sponsors injected another $30 million of equity. Plaintiffs were not part of the May 2024 negotiations but did not object to the Fifth Amendment.

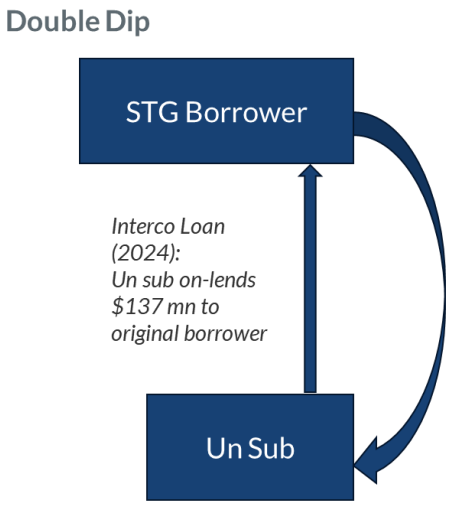
By August 2024, it was clear that the liquidity injection had only delayed the inevitable. At this point, the same group of lenders (the "ad hoc group" or "AHG") who had steered the Fifth Amendment quietly negotiated with the Company an extensive liability management transaction in hopes of establishing a more permanent solution to the Company's woes. The LMT generally consisted of the following:

1. Another amendment to the Credit Agreement (the "Sixth Amendment") consented to by "Required Lenders"[5] which not only stripped away the added protections imposed in the Fifth Amendment, but most of the covenants and EoDs from the existing Credit Agreement as well.
2. The creation of a new subsidiary not subject to the Credit Agreement (the "Unrestricted Subsidiary").
3. The transfer of the "less-than truckload" (LTL) segment and the "STG Distribution" (STGD) segment to the Unrestricted Subsidiary. Plaintiffs have claimed that these two segments constituted "substantially all"[6] of Company's assets.

[3] See coverage by LevFinInsights on STG Logistics for additional background.
[4] See 71 of the Amended Complaint.
[5] Generally requiring a majority of all outstanding Term Loans and Revolver borrowings and commitments. The AHG lenders are understood to have accounted for Required Lenders.
[6] See 186 of the Amended Complaint.

4. The Unrestricted Subsidiary's incurrence of $137 million of new money "first lien first out" ("FLFO") debt provided by AHG lenders.
5. Repayment in full of AHG lenders' holdings under the Credit Agreement "at a premium to their trading price—at or near the face value of the Loans"[7] in exchange for additional FLFO debt as well as first lien second out ("FLSO") debt at the Unrestricted Subsidiary. The prepayments of AHG lenders relied on the Company's ability to repurchase Term Loans at a discount on a non-pro rata basis under Section 2.7(d) of the Credit Agreement.
6. On-lending of the $137 million new money from the Unrestricted Subsidiary to the borrower under the Credit Agreement, with existing loan parties providing a first lien guarantee of the new Unrestricted Subsidiary debt (thereby creating a "double dip" structure on behalf of the AHG lenders and diluting the Plaintiff's liens on whatever residual collateral under the Credit Agreement still remained).
7. Following the initial exchanges, the Company offered lenders outside of the AHG group an opportunity to exchange into a mix of FLSO and first lien third out ("FLTO") term loan debt issued by the Unrestricted Subsidiary debt on "less-favorable" terms.[8]
8. The Company also offered an opportunity to other lenders (including Plaintiffs) to exchange into Unrestricted Subsidiary debt at 40 cents of FLSO debt and 30 cents of FLTO for every dollar of legacy Term Loans repaid.





Source: Covenant Review

Unleash the Litigators

While the vast majority of the Company's existing creditors participated in the LMT, there were holdouts—the Plaintiffs. Licking their wounds, the Plaintiffs engaged counsel Selendy & Gay, commencing litigation in January 2025. The Motion to Dismiss followed in March. The following discussion addresses five notable

[7] See 11(c) of the Amended Complaint.
[8] See 11(d) of the Amended Complaint.

arguments raised by both sides. We consider each argument as well as speculate about implications on the broader practice of liability management transactions.

1. Technical Reads vs Common Sense Interpretations—Why People Hate Lawyers

STG's LMT ultimately relied on a mix of carrots and sticks to accomplish its goals. With respect to sticks, one of the bigger ones (let's call it a branch) was the removal of regular cash interest payments under the existing Credit Agreement per the Sixth Amendment. The Sixth Amendment did this by modifying the "grace period" for an interest payment default so that the Company had the option to extend it to the maturity date (from a three-business day grace period originally).[9] We have previously discussed the implications of such changes, but the bottom line is that any cash interest payments under the existing debt is effectively "shut off."[10]

Plaintiffs claim this is in violation of their sacred rights—i.e., those provisions in the Credit Agreement's amendments section that require affected lender consent (or other heightened threshold)—which in relevant part *does* prohibit amendments that "postpone or delay" interest payment dates.[11] The Defendants claim that the change here does *not* modify *when* a payment date is scheduled to occur but rather only modifies the grace period before a failure to pay interest ripens into an event of default (which is never mentioned in in the sacred rights).[12] The Defendants' argument stems from the recent *Mitel* decision, which they claim stands for the proposition that if an amendment to the grace period for an interest payment default was intended to be a sacred right, the principals would have explicitly made it so.[13] However, it is clear that the *result* of a change in the grace period can be functionally the same as a delaying the payment date—in both instances, the date the interest is paid occurs later than originally scheduled.

While prior liability management exercises have utilized similar tactics, the Defendants' argument does not pass the "gut" test—it *feels* wrong to make a technically permitted change that has the exact same effect as a prohibited change. As long-time market observers, we also have a realistic viewpoint on how credit agreements are actually drafted and negotiated—that is, too quickly and with limited input from actual syndicate members. This militates against taking too technical a read of documentation. On the other hand,

[9] See 90 of the Amended Complaint.

[10] See Diebold Nixdorf: Can the Company Extend the Grace Period for Interest Payment Defaults Under the 2024s Without Unanimous Consent? See also Sacrilege? Turning Off Cash Interest Payments in Credit Agreements with Only Majority Consent.

[11] 105 of the Amended Complaint notes that the existing Credit Agreement generally requires affected lender consent for any changes that "postpone or delay any date fixed for, or reduce or waive, any scheduled installment of principal or any payment of interest, fees or other amounts (other than principal) due to the Lenders."

[12] See page 12 of the Motion to Dismiss, where the Defendants argue that the Plaintiffs failed to allege a breach of a sacred right regarding delay in interest payment dates because:

> "Plaintiffs assert that the Sixth Amendment had the 'effect' of postponing interest payment dates and 'purported ***effectively*** to eliminate STG's duty to make scheduled interest payments[.]' *See* Ex. 1 146 (emphasis added). This fails to state a claim under the plain terms of the Credit Agreement, which addresses only an actual waiver, reduction, or delay."

[13] See Oral Arguments Transcript pages 17-18 ("As the court knows, *Mitel* held that quote 'had the parties wanted an effective or functional amendment to be covered, they could have used language to that effect' close quote.")

from a purely legal viewpoint, we as lawyers have sympathy for Defendants' reliance on the "words on the page" position, as it avoids relying on the vagaries of market practice or other extrinsic evidence.

While the provision at issue here is esoteric and fairly specific, the underlying debate is a fundamental one, not just in LMT practice but in contractual interpretation generally: how much deference should one pay to the explicit words on the page and how much should the spirit of the language dictate the interpretation of the agreement?

2. Don't Stand So Close to Me (When There's a No Action Clause Around)

A core component of the Motion to Dismiss is procedural—i.e., that the Plaintiffs lack "standing" to sue (in layman's terms, they do not have the right to sue the Defendants). Lack of standing can arise from absence of harm or, in this case, a contractual limitation. Defendants reason that Plaintiffs lack standing here because of the Credit Agreement's "no-action" clause in Section 9.3(c),[14] which vests the *exclusive* authority to enforce rights and remedies under the Credit Agreement and other loan documentation to Antares as the administrative agent. Relatedly, all actions and proceedings at law connected with such enforcement must be instituted and maintained exclusively by the agent for the benefit of the lenders. According to the Defendants, because Antares is not engaging in any enforcement action on behalf of the Plaintiffs (and, indeed, is one of the Defendants), Judge Patel should dismiss the Amended Compliant.

The Defendants also cite *Beal Savings Bank v. Sommer* (2007)—a New York Court of Appeals[15] decision which generally held that an individual lender could not sue a defendant because the debt documentation lacked explicit references to such individual rights—or, more specifically—*Beal* stands for the proposition that if an agreement includes "an unequivocal collective design," then individual lenders will lack standing to engage in individual enforcement, even if "no action clauses" are absent.[16] The Defendants argue that like in *Beal*, the Credit Agreement also contemplated a "collective enforcement scheme" because it broadly provides the agent with the ability to exercise rights and remedies throughout the document.

Plaintiff's counterarguments rely primarily on futility (i.e., it is futile to expect the agent to exercise remedies on the Plaintiffs' behalf when the agent itself is a defendant in the lawsuit).[17]

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[14] This provision, as set forth in the Motion to Dismiss, reads as follows:

> "[T]he authority to enforce rights and remedies hereunder and under the other Loan Documents against the Credit Parties or any of them shall be vested exclusively in, and all actions and proceedings at law in connection with such enforcement shall be instituted and maintained exclusively by, Agent in accordance with the Loan Documents for the benefit of all the Secured Parties."

[15] The highest court in the State of New York. Like the Supreme Court…of New York, except not (see footnote 1 above).

[16] See pages 9-10 of the Motion to Dismiss.

[17] See page 59-60 of the Oral Arguments Transcript (as argued by counsel for the company:

> "The no action clause does not bar plaintiffs' claims because it would be futile to demand that Antares bring the claims not only against itself as trustee, it would also be futile to expect Antares to sue STG for a scheme in which it is alleged to have colluded to have been part of the same actions and the same breaches that STG and the other lenders participated in."

Discussing the full panoply of legal arguments for and against the application of "no action" clauses is beyond the scope of this report. However, the Court's determination[18] on this issue could have wide ranging effects on liability management transactions, as a holding in favor of the Defendants could impose significant hurdles for future plaintiffs in similar cases. This is particularly true for the BSL market where no action / collective action provisions are prevalent.[19]

3. Fifty Shades of Subordination

Is a Serta blocker that does no blocking still a Serta blocker? Plaintiffs argue that the Company's LMT violated the existing Credit Agreement's Serta blocker in Section 10.1(a)(iv)(A), which requires that affected lenders consent to an amendment that:

> "could change or have the effect of changing the priority or pro rata treatment of any payments (including voluntary and mandatory prepayments), Liens, proceeds of Collateral or reductions in Commitments (including as a result in whole or in part of allowing the issuance or incurrence, pursuant to this Agreement or otherwise, of new loans or other Indebtedness having any priority over any of the Obligations in respect of payments, Liens, Collateral or proceeds of Collateral, in exchange for any Obligations or otherwise)."[20]

Defendants counter these claims on a number of fronts but mainly rely on the idea that "no amendment[s]" were made to the pro rata sharing and payments waterfall provisions.[21] This seems to skip over the part about how Section 10.1(a)(iv)(A) is not specifically relating to changes to pro rata sharing provisions but instead a broader prohibition against certain amendments that can affect *priority* or pro rata sharing treatment.

Separately, there is also *another* Serta blocker in the Credit Agreement under Section 10.1(a)(viii) which requires affected lender consent to "subordinate the Liens securing the Obligations to Liens securing Indebtedness for borrowed money or subordinate all or any portion of the Obligations to any Indebtedness for borrowed money."[22] Defendants counterargue that the LMT did not subordinate the Plaintiffs' claims against collateral (which is true). While this seems to read out the latter part of the blocker that extends to amendments that "subordinate all or any portion of the Obligations to any Indebtedness for borrowed money," this is likely due to the fact that the Motion to Dismiss is responding explicitly to the Amended Complaint, which Defendants claim describes lien subordination as the end result.[23]

In both Section 10.1(a)(iv)(A) and 10.1(a)(viii), the Plaintiffs could be arguing for a broader interpretation of the term "subordination." After all, Defendants have the factual upper hand in that there was indeed neither payment nor lien subordination in the October 2024 LMT. Instead, the Company's "uptier" was via

[18] See page 14 of the Oral Arguments Transcript, where Judge Patel did appear to sympathize with the Plaintiffs, noting that it would indeed be futile for the Plaintiffs to rely on Antares to "exercise remedies" on their behalf given the lawsuit.
[19] See Market Alert: Not So "Sacred Rights"? for an analysis of no action clauses, collective action clauses, and the *Beal* decision.
[20] See 111 of the Amended Complaint (emphasis removed).
[21] See page 14 of the Motion to Dismiss.
[22] See 116 – 117 of the Amended Complaint.
[23] See page 15 of the Motion to Dismiss.

structural subordination and debt issued at the Unrestricted Subsidiary. While the term "subordinate" (when used by itself) is *usually* interpreted as limited to payment or contractual subordination, the absence of a defined term in the Credit Agreement for "subordination" arguably opens the door that it could be interpreted as also encompassing *structural* subordination.

Thus, in contrast to the grace period / delayed interest payment point, Plaintiffs have the more technical (if not also more reasonable) read of the Credit Agreement when it comes to violation of the blockers. While many Serta blockers lack the "effect of" language, the presence of such language in Section 10.1(a)(iv)(A) technically expands the scope of the blocker beyond just payment / lien priority and into the realm of other potentially senior debt (including structurally senior debt at a non-loan party subsidiary). Similarly, one could interpret the generic "subordination" language in Section 10.1(a)(viii) as prohibiting structural (as well as payment and collateral) subordination. On this latter point, however, it is true that the Plaintiffs do not *explicitly* argue that "subordination" should be interpreted to include "structural subordination," though that may be more of a flaw of the argumentation and not the argument.[24]

4. Implied Covenants—Last Ditch Hail Mary Do or Die?

The Plaintiffs' penultimate cause of action in the Amendment Complaint deals with the implied covenant of good faith and fair dealing under New York law.[25] This implied covenant is intended to apply to all contracts and (in theory) keeps the parties "from doing anything that will have the effect of destroying or injuring the right of the other parties to receive the fruits of the contract."[26]

Plaintiffs argue that the LMT was a breach of the implied covenant of good faith and fair dealing because it resulted in the Plaintiffs no longer receiving "equal and fair treatment as compared to all other holders of the Loans."[27] Moreover, in the case of Defendant lenders, the entry of the Sixth Amendment demonstrated bad faith as they "would not have agreed to" had they remained party to the Credit Agreement.

Defendants' responses are procedural in nature. Causes of action based on breaches of implied covenant of good faith and fair dealing cannot be made at the same time as claims based on breach of contract; with New York courts "routinely" dismissing the former in the presence of the latter—to the extent both claims arise from the same facts and circumstances.[28]

While other lawsuits arising from liability management transactions have raised similar claims, the results have been patchy at best.[29] It certainly does not help that actions tied to the implied covenant of good faith lean heavily on eliciting an emotional response (this doesn't *feel* fair), rather than upon an objective understanding of *what* exactly constitutes the "fruits of the contract." It is little wonder then that judges seem to shirk from utilizing the implied covenant as a hammer against aggressive transactions.

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[24] See page 17 of the Memorandum of Law in Support of Defendant Lenders' Motion to Dismiss ("Moreover, Plaintiffs do not allege that the Fifth Amended Agreement prohibits *structural* subordination—*i.e.*, that Lenders cannot directly access the value of a subsidiary's assets to satisfy their Loans until that subsidiary's creditors are fully paid.")
[25] See 241-249 of the Amended Complaint.
[26] See 243 of the Amended Complaint.
[27] See 243 of the Amended Complaint.
[28] See page 20 of the Motion to Dismiss.
[29] See, e.g., *Serta*, *Mitel*, and *Trimark*.

On the other hand, a successful implied covenant claim in a liability management case could upend the distressed debt world or at least transactions that rely on "creditor-on-creditor" violence, which usually rely on there being winners *and* losers. Any reasonable expectation of success from an implied covenant claim could therefore give just enough support for lenders on the fence to hold out in a coercive exchange offer, FOMO be damned.

5. Wait, "Internally Generated Funds" Means *What*?

We end our list with an exercise in contractual interpretation. As noted above, a core component of the LMT involved the Company repurchasing the AHG lenders' existing debt[30] under Section 2.7 of the Credit Agreement. This section allows non-pro rata "discounted buybacks" subject to meeting certain conditions (notably—and like in Mitel's debt documentation—the Credit Agreement does not use the term "open market purchase," thereby sidestepping any limitations to that term imposed by the Fifth Circuit's *Serta* decision last year). Section 2.7 (at least under the Fifth Amendment) required that the Company fund any discounted buyback with internally generated funds. Plaintiffs argue that Defendants did not comply with this language since the prepayments were largely funded by intercompany loans received from the Unrestricted Subsidiary and not from internally generated funds "from operations."[31] Defendants, on the other hand, have staked a curious position claiming that intercompany loans are "by their nature, internally generated because the funds come from within the company,"[32] irrespective of the fact that the source of funds was debt issued out of the Unrestricted Subsidiary. Relying again on *Mitel*, the Company's counsel argued that if "internally generated" means "internally generated *from operations*," then the Credit Agreement *would have said so*.[33]

We tend to agree with the Plaintiffs on this point—taking the Defendants' position reads "internally generated funds" into non-existence. If intercompany loans (which are, themselves, sourced externally) are "internally" generated because they "come from within the company," then a borrower can artificially designate *any* cash (external, internal, or otherwise) as "internally generated" via funneling the proceeds through an intermediary subsidiary. Even under *Mitel*, this seems like a bridge too far from the reasonable expectation of the parties.

Separately, the Defendants also argue that the argument is ultimately irrelevant since the Sixth Amendment also added "or otherwise"[34] after "internally generated cash," though Plaintiffs largely ignore this argument, as much (if not all) of their case is predicated on the claim that the Sixth Amendment is not validly executed.[35] For purposes of this report, we will not go into detail on the "or otherwise" argument.

Conclusion

Rare is the lawsuit that manages to touch on so many issues pertinent to the practice of liability management.

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[30] See Item 5 in the description of the LMT on page 3 above.
[31] See page 55 of the Oral Arguments Transcript.
[32] See page 18 of the Motion to Dismiss.
[33] See page 102 of the Oral Arguments Transcript.
[34] See page 18 of the Motion to Dismiss.
[35] That said, "or otherwise" has also demonstrated a capacity for controversial interpretations; see Incora: "Or Otherwise" Now Means "Or Similarly".

How (or even whether) Judge Patel will address the specific arguments noted in the foregoing discussion remains to be seen. As we have discussed, however, the consequences of his decision could be significant to market practitioners and observers alike.

In short, watch this space. Things are liable to get (more) exciting for LMTs in the coming months.

— *Covenant Review*

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