Recovery Finance Corp.

The extended shutdown of major parts of our economy threatens the financial ruin for countless businesses. Letting businesses simply go under would endanger the economy’s ability to recover quickly once we come out on the other side of this. The Federal government is preparing measures to support a few select companies, and it will face pressure to do the same for others down the line. Our society already has tools and principles for managing financial problems like this: bankruptcy and financial reorganization or restructuring. Unfortunately, the current disaster makes normal bankruptcy inadequate to the scale of the problem at hand. We need Federal monies and we need to act on a scale that the bankruptcy courts will not be able to manage. However, we should not simply toss aside all of the principles and tools employed in a normal bankruptcy process and substitute new and untested subsidy channels. We should apply those principles and tools to whatever new Federal support channel we create. Here’s how.

1) Create a Federal Recovery Finance Corp (RFC) as the vehicle through which Federal dollars go to businesses.
2) Businesses can apply for RFC-financing. To do so, they must accept or fulfill certain conditions.
   • Agree to submit themselves to a bankruptcy-like process. This will not involve bankruptcy courts, but be entirely separate. It will, however, be governed by similar principles and processes. Call it the bankruptcy-19 process, after COVID-19.
   • All creditors must agree to participation in the bankruptcy-19 process as well. This includes a temporary stay on all debt payments, except for pension liabilities.
3) RFC financing comes only in the form of DIP-like financing. Call it DIP-19 financing.
   • DIP stands for Debtor-in-Possession. DIP-19 financing becomes senior to all existing liabilities, so that any business receiving DIP-19 financing pays the government back before paying other creditors and before current equity holders.
4) The bankruptcy-19 process foresees a restructuring of the existing debt and equity just as does a traditional bankruptcy process, except for pension liabilities.
   • The restructuring probably cannot be completed anytime soon, until the length of the current economic shutdown becomes clearer and the future prospects of the business become clearer.
5) Through the bankruptcy-19 process the RFC must evaluate and approve the ongoing business plan of the company just as happens in any Chapter 11 or Chapter 13 bankruptcy process. What lines of business should be maintained? What not?
   • The RFC can simultaneously consider applications from related businesses. For example, it can consider applications from the airlines, but also from the many contract businesses supplying services to the airlines.
6) Any business or creditors that do not like the terms of the bankruptcy-19 process and so do not want RFC financing are always free to take their insolvency to the traditional bankruptcy courts instead.

- However, these courts are likely to be swamped. The bankruptcy-19 process is a vehicle for faster action.
- Moreover, the DIP-19 financing is only available via the bankruptcy-19 process, which makes it attractive.
- But, in the end, companies and creditors either choose the process, or not.

The RFC and its associated bankruptcy-19 process and DIP-19 financing is just the vehicle for Federal monies to certain businesses. It operates alongside other programs, such as direct cash payments to individuals, funding to states and localities, as wells as other federal programs for health care and so on. It is not a substitute for any of those.

Alternative vehicles for channeling federal money to businesses are ill-suited to the nature of the crisis we face. This is not a typical recession where responding with some injections of money encourages helpful investments. This is a giant financial hit to a wide range of businesses, and it creates a giant insolvency problem. A bankruptcy-like vehicle is best suited to addressing this. There is a large array of expertise that understands how to do bankruptcy proceedings and the attendant financial restructurings. We should benefit from that common understanding to help execute on this complex problem. If we try to substitute other vehicles, there will be lots of wasted money.

The scale of the insolvency problem facing businesses across the US is enormous, but not yet well appreciated. Moreover, we don’t yet know the full extent, even where we can see the initial figures. An RFC like vehicle is flexible. It can receive future installments of funding from Congress, and accept applications from businesses across the country and any industry.

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