Lead Left Interview – Wayne McKinzie

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This week we chat with Wayne McKinzie, a partner at Moore & Van Allen PLLC. Named in *Best Lawyers in America for Banking and Finance Law*, Wayne represents investors in various senior and mezzanine financing transactions and investments. Moore & Van Allen, based in Charlotte, is one of the largest law firms in the Southeast, employing nearly 300 attorneys, with approximately 80 attorneys on the Financial Services team.

The Lead Left: Wayne, from your perspective representing the buy-side, how do you see terms evolving for leveraged loans?

Wayne McKinzie: Clearly 2015 has continued the trend with financial sponsors having lots of negotiating leverage, given the strong demand for leveraged paper. What everyone says about structures weakening – or becoming more flexible, depending on your viewpoint – is accurate. We focus mostly on the middle market.

TLL: What are some trends in the middle market?

WM: I would say the big theme is what has moved down from the larger middle market in terms of structures. The tension for our investor clients is financing companies that are not as large, often with unproven management and business plans. Some of these firms have had a bumpy ride.

TLL: What terms are coming down market from larger issuers?

WM: Investors are being asked to build in all sorts of flexibility, which may not be appropriate at the front end. If the borrower wants lots of room on covenants or baskets, investors may prefer to accommodate them down the road when a specific transaction or situation is at hand. Right now we're helping clients pick their battles.

TLL: Could you share with our readers some of the big issues you're wrestling with?

WM: It's about overall structures. We have clients pitching multiple options – first lien/second lien, first lien/mezzanine – often with ancillary revolving credits. I know you had a column on RCs. We spend a lot of time on RC needs and draw conditions. No question our clients need to offer that capacity in the current market.

TLL: It seems to be the price arrangers pay for leading transactions.

WM: You don't want the RC to end up as additional long-term debt. It's often important to build in an incurrence or other incremental long-term debt test. You can borrow but you have to show you're in covenant compliance. For example, leverage at draw needs to be no greater than starting leverage. We also sometimes see a 45-day clean-down of the RC to ensure it's a true working capital facility.

TLL: How about inter-creditor issues?

WM: They come up in a number of middle market deals. We've seen them when dealing with seller notes, usually structured as hold co securities. Also, when sponsors fund acquisitions they sometimes structure a portion of their investment as hold co debt. One big issue relates to structuring for future incremental debt and having the note holder agree to be subordinate to these new facilities.

TLL: What about second liens?

WM: Not all players have the same conception of what it means to be a second lien. Some are expecting second lien with no payment blocks as part of the inter-creditor agreement, just lien subordination. But some first lien lenders expect the second lien to accept a payment block as well.

TLL: And you represent both first and second lien holders.

WM: One tricky situation is when you have the same arranger and agent for both first and second lien facilities. When you're representing a second lien lender, one key is negotiating when the second lien can be released by the first lien lenders. Ideally that happens only when the first lien lenders are exercising remedies and proceeds go to pay down the first lien, or in any transaction permitted by the second lien documents.

TLL: Where are the pain points for you representing second lien holders?

WM: We push back on forced lien releases in connection with an asset sale approved by the first lien lenders when the borrower wants to keep the proceeds for "liquidity." The downside is when there's a problem and the sponsor is not compelled to fix the problem.

TLL: Wayne, could you help clear up the confusion on debt baskets? How do you think about incremental debt from the lender's perspective?

WM: There certainly are a variety of debt baskets in documentation – builder, starter, and "free-and-clear (FAC)". Let me first take the incremental baskets. These typically have ratio-based components. One question is, can you use a leverage based component first, and then add debt using a FAC basket?

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