

Strafford

presents

Commercial Real Estate Loan Workouts

Strategies for Developers, Owners and Lenders to Negotiate an Effective Workout Agreement

A Live 90-Minute Teleconference/Webinar with Interactive Q&A

Today's panel features:

Ren R. Hayhurst, Partner, **Bryan Cave**, Irvine, Calif.
Steven D. Collier, Counsel, **Alston & Bird**, Atlanta
David A. Barksdale, Partner, **Ballard Spahr**, Los Angeles

Tuesday, October 5, 2010

The conference begins at:

1 pm Eastern

12 pm Central

11 am Mountain

10 am Pacific

You can access the audio portion of the conference on the telephone or by using your computer's speakers.
Please refer to the dial in/ log in instructions emailed to registrants.

For CLE purposes, please let us know how many people are listening at your location by

- closing the notification box
- and typing in the chat box your company name and the number of attendees.
- Then click the blue icon beside the box to send.

For live event only.

- If you are listening via your computer speakers, please note that the quality of your sound will vary depending on the speed and quality of your internet connection.
- If the sound quality is not satisfactory and you are listening via your computer speakers, please dial **1-866-871-8924** and enter your PIN when prompted. Otherwise, please send us a chat or e-mail sound@straffordpub.com immediately so we can address the problem.
- If you dialed in and have any difficulties during the call, press *0 for assistance.



Developing and Implementing a Workout Strategy

Ren Hayhurst (Irvine,CA)
949-223-7125; rrhayhurst@bryancave.com



A Broader PerspectiveSM

Overview of Workouts/Restructures

- DEVELOP A STRATEGY
 - Restructures vs. Workouts
 - Immediate Action Steps
 - Limits on the Lender's Objectives/Borrower's Options
 - Know Your Enforcement Options
- TYPES OF WORKOUTS
 - Foreclosure And Alternatives to Contested Proceedings
 - Forbearance Agreements
 - Bankruptcy and Mitigation Techniques

Restructures vs. Workouts

- Key Distinctions - Goals Follow Desired Exit Strategy
 - Restructure Involves Changing The Terms Of A Currently Performing Loan, Or To A Loan That Can Become Performing After The Restructure
 - Workout Involves Taking A Non-Performing Loan And Working To An Agreed-upon Exit Strategy
- Initial Agreements Set Terms For Future Relationship
 - Purposes Include Giving Notice Of Defaults, Reserving Rights/Remedies, Requiring Performance Under The Loan, “Cleaning-up” Deal, Warning Of “Consequences”
 - Borrower’s Ability to Negotiate

Note on Restructures vs. Workouts

- Practice Tip
 - Banks with loans purchased from the FDIC may have a loss share agreement that limits their negotiating options
 - Loss share agreements require the lender to get FDIC approval for:
 - short sales,
 - loan payoff discounts, and
 - guaranty compromises
 - This can delay or inhibit a lender from being too aggressive on loan workouts

Immediate Actions

- Default/Acceleration Notices
 - Use Of Pre-Workout Letters
 - Establish Basis Of Disputes – Describe Disputes And Defaults
 - Sets Boundaries For Discussions – No Obligations On Lender, No Waiver Or Estoppel, Confidentiality, Right To Terminate And Pursue Remedies, Ease Path To Remedies - i.e., Receivership
- Enforceability of Pre-Workout Letters
 - Extent of Confidentiality/Evidentiary Protections
 - Specific Remedies/Attorneys' Fees Provisions

Note on Immediate Actions

- Practice Tip
 - Very little litigation on the enforceability of Pre-Workout Letters
 - Try to take full advantage of existing state and federal law on settlement discussions
 - Err on the side of more detail and more explanation of the terms and boundaries

Immediate Actions (Part II)

- Obligations of the Property Manager
 - Terminate Or Continue
 - Insider vs. 3rd Party Managers
- Lockboxes
 - Change Application Of Funds; Hold Excess Proceeds
 - Springing Lockboxes;
 - “ARD” Situations for Securitized Loans

Immediate Actions (Part III)

- Staged Response
 - First, Default/Notice Letter – this document puts the game in motion and often is required in syndicated or participated loans
 - Practice tip: Beware of the need for co-lender approvals
 - Next, Pre-Workout Letter – this document sets the ground rules and establishes the protections for the lender to have open discussions
 - These are more negotiable when the lender is not a loan servicer
 - Finally, Forbearance Agreement or Modification Agreement

Limits on the Lender's Objectives

- Value Of Collateral
 - Oversecured vs. Undersecured
- Priority of Security Interest
 - Intercreditor Issues
 - Perfection Issues
- Recourse v. Non-Recourse Liability
 - One-Action and Anti-Deficiency Issues
- Securitized Loans And PSA Requirements
- Loss Share Agreements

Forbearance Agreements

- Basic Elements

- Acknowledge Defaults
- Allow Notice and Cure Periods to Expire
- Initiate and Then Postpone Remedies
- Obtain Key Waivers Not Available In Other Contexts (i.e., One-Action, Anti-deficiency and Bankruptcy)
- Maintain Maximum Leverage Over Borrower
- Restructure the Business Terms

- Reasons for Using This Agreement

- Maintain Relationship as Part of Exit Strategy

Enforcement Options

- Receivership
 - Ex Parte vs. Motion for Appointment
 - Practical Considerations
- Writs of Attachment
 - Tool To Use On Guarantors
- Remedies Against Personal Property Collateral
- Judicial vs. Non-Judicial Foreclosure
 - One Action and Anti-Deficiency Considerations
 - Optional Use of Either Remedy; “Dual Tracking”
 - Timing Considerations

Enforcement Options (Part II)

- Bad Boy Carve-Out Guaranties
 - Enforced by Courts for Damages or Full Recourse
 - Not Prohibited as Liquidated Damages or Penalty Provisions
 - Specificity of Provisions Affects Enforceability
- Springing Recourse Guaranties
 - BK Filing, SPE Violations, Additional Debt and Unpermitted Transfers Can Be Recourse Triggers
 - Practice Tip: Misapplication of Funds Can Apply to Transfers of Rents, Proceeds, Accounts and Receivables

Enforcement Options (Part III)

- Expansion Of Waste Remedies
 - Failure to Maintain or Repair Property with Rents or Other Revenues
 - Failure to Pay Taxes or Insurance Premiums
- Material Adverse Change (or MAC) Provisions
 - Limited Case Law in the Loan Context (most cases come out of the insurance context)
 - Subjective vs. Objective Standards
 - Practice Tip: Enforceability is often tied to objective criteria for triggering a MAC provision
 - Trigger Default vs. Trigger Additional Lender Rights

Types of Workouts

- Alternatives to Foreclosure
 - Deed in Lieu of Foreclosure
 - Title Subject to Competing Liens and Other Defects
- Consensual Foreclosure
 - Permits a Lender to “Clean Up” Title, And Can Speed Up the Process
- Consensual Bankruptcy
 - Risk Of Trustee Or Judicial Interference

Types of Workouts (Part II)

- Note Sales
 - Previously Limited Market; Uncertain Pricing
 - Loss share agreement issues
 - More sophisticated investors in the market now, so more note sales
 - Practice Tip – If the borrower is in bankruptcy, then:
 - Note sale is possible without court approval
 - Property sale requires court approval
 - Note that a competing property sale offer can be the basis for a lender's competing plan and can lead to a 363 sale

Conclusion

- Understand the Advantages of Approaches and Use Them As Required to Stay On Top Of the Borrower and the Project
- A Little Advance Warning to Third Parties Is Invaluable to Identify Problems Or Possible Claims
- Remind Borrower of The Extent of Your Remedies, and take Action To Factually and Legally Preserve All Rights and Remedies



COMMERCIAL REAL ESTATE LOAN WORKOUTS
New Restructuring Opportunities

Teleconference Sponsored by
Legal Publishing Group of Strafford Publications
October 5, 2010

The Threat of Bankruptcy
Forbearance Agreements
&
Bankruptcy Mitigation Techniques

Presented by:
Steven D. Collier
ALSTON & BIRD LLP
One Atlantic Center
1201 West Peachtree Street
Atlanta, Georgia 30309-3424
(o) 404/881-7638
(f) 404/253-8552
steve.collier@alston.com



The Threat of Bankruptcy

- Measure workouts against bankruptcy
- Is there equity in the property?
- Are there junior creditors?
- What to do with cash collateral?



Till v SCS Credit Corp, 541 U.S. 465 (2004)

- Cram down interest rate for Chapter 13
- Prime rate plus 1-3%
- Footnote 10 says *Till* may apply to Chapter 11
- Footnote 14 points to DIP financing rates for Chapter 11
 - GGP case: DIP financing at LIBOR plus 12%
- *In Re American Homepatient Inc.*, 420 F3d 559 (6th Cir 2005)
 - Applies *Till* to Chapter 11
 - Treasury rate plus 3.5%
 - What is the appropriate spread?



SPE Bankruptcy Remoteness & Independent Directors

- Most CMBS/securitized loans contain SPE provisions
 - Designed to limit creditors and insulate the property
 - Avoid entanglement with parent bankruptcy
- Didn't work in the GGP bankruptcy
 - Performing properties were placed in bankruptcy
 - Independent directors apparently voted yes
 - Cases settled and so issue was not litigated
- Generally RE bankruptcies are not as common as 90s
 - Death of the new value exception
 - Single asset real estate provisions
 - Springing recourse

Alternatives to Foreclosure

Commercial Real Estate Loan Workouts:
New Restructuring Opportunities

October 5, 2010

David A. Barksdale

Partner

barksdaled@ballardspahr.com

424.204.4322

Alternatives to Foreclosure

- Threshold Question - Should the owner be replaced?
 - Identify the cause of the default
 - Relationship between borrower and lender
 - Does the lender trust the borrower?
 - Does lender have confidence in the borrower?

Alternatives to Foreclosure

- Evaluate Conduct of Borrower
 - Did borrower disclose problems to the lender
 - Has borrower preformed under loan documents and other agreements affecting the project?
 - How has borrower responded to the problems?
 - What is the status of
 - other projects of borrower?
 - similar projects in the market?

Alternatives to Foreclosure

- Leaving Borrower in Control
 - Tighten operational and/or financial controls and reporting requirements
 - Modify loan terms
 - extend the term
 - reduce interest rate and/or principal
 - forbearance
 - obtain additional collateral
 - “split” the loan – performing and deferred components
 - Taking equity interest in project

Alternatives to Foreclosure

- Removing Borrower
 - Foreclosure
 - Disadvantages
 - length of process and potential delay
 - expense
 - continued decline in value
 - no assurance of positive result
 - may trigger bankruptcy

Alternatives to Foreclosure

- Deed in Lieu of Foreclosure
 - Relatively inexpensive and expeditious
 - Consideration
 - Title insurance
 - Junior liens and encumbrances
 - Discharge and merger of mortgage
 - Documentation
 - settlement agreement
 - representations and warranties
 - conveyance documents

Alternatives to Foreclosure

- Consensual Foreclosure
 - May be preferable if subordinate liens and encumbrances exist
 - Length of process
 - Judicial vs. non-judicial
 - Bidding considerations

Alternatives to Foreclosure

- Additional Considerations Where Borrower Surrenders the Project
 - Release of borrower and guarantors
 - Project management
 - Share in sales proceeds
 - Right of first refusal/brokerage commissions

Alternatives to Foreclosure

- Risks to Lenders Taking Ownership
 - Environmental considerations
 - Premises liability
 - Bankruptcy considerations
 - Due diligence is critical

Alternatives to Foreclosure

- Consensual Bankruptcy
 - Advantages
 - preservation of assets
 - conveyance of title by court order
 - appointment of trustee vs. receiver under state law
 - Modify voting requirements for syndicated loans
 - Disadvantages
 - expense and length of time
 - potential loss of control

Alternatives to Foreclosure

- Bankruptcy Considerations
 - Automatic stay
 - SARE – single asset real estate
 - Adequate protection
 - Cash collateral and post-petition financing
 - Executory contracts and unexpired leases
 - Plan confirmation

Alternatives to Foreclosure

- Sale of the Project or Loan
 - Project
 - Short sale
 - Three party negotiation
 - Borrower/seller, buyer and lender
 - Terms – cash or lender financing
 - May involve modification of existing loan
 - Evaluate loan to value and effect of debt service
 - Documentation
 - Due diligence

Alternatives to Foreclosure

- Sale of the Project or Loan
 - Loan/Note
 - Due diligence considerations
 - Limited opportunity will probably result in lower price
 - Capital structure
 - Receivership
 - Allows REMICs to provide seller financing
 - May increase recovery



Forbearance Agreements

- *Hope springs eternal*
- Short term forbearance agreements designed to lead to near term payoff of the loan
- Reinstatement agreements designed to lead to near term restoration of the loan to non-delinquent status
- “One bite at the apple” forbearance structures designed to achieve finality.



Classic mortgage loan workouts

- What's in it for the Lender? Lender "wish list" includes:
 - -paydown of the loan or other cash infusion
 - -additional collateral
 - -increase the interest rate or amortization, shorten the period to maturity or retrade other business terms such as payoff provisions
 - -add guarantors or recourse to a non-recourse loan
 - -establish escrows (tax, insurance, capital reserves, tenant work)
 - -activate or establish a lockbox to control cash flow
 - -obtain/require supplemental property information or reports
 - -reduce/eliminate Borrower rights such as partial releases of collateral
 - -increase/enhance lender rights such as approval over budget or leasing
 - -correct any legal weaknesses/deficiencies in the existing documents
 - -waive existing offsets, defenses or lender liability claims
 - -change in property management/leasing agent



“One bite at the apple”

- Forbearance Agreements with finality
- Waivers, acknowledgements, and factual stipulations re: foreclosure
- Springing recourse liability for any opposition to Lender’s remedies
- Releases of guaranties conditioned upon the Borrower’s compliance
- Discounted payoff rights which expire after the forbearance period
- Deed in lieu of foreclosure held in escrow
- Consent judgment of foreclosure held in escrow
- Consent order incorporating the forbearance terms
- Prepackaged bankruptcy



Bankruptcy mitigation

- How to discourage bankruptcy filing?
- Springing recourse
- Stay relief waivers
 - Absence of equity
 - Single asset real estate
 - Two party dispute: no other creditors
- Absolute assignment of rents
- Collateral assignment of equity
- “Don’t come crying to me”