UCC Foreclosures: Overcoming Obstacles to the Sale and Evaluating Receivership and Bankruptcy Alternatives
Protecting Lender and Borrower Interests

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ENFORCING SECURITY INTERESTS IN EQUITY INTERESTS: 
FORECLOSURE BY SALE AND STRICT FORECLOSURE

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I. INTRODUCTION

A. Background. A mezzanine loan is a form of subordinate financing for commercial real property in which, in the typical case, the lender accepts a pledge of 100% of the equity interests in the entity that owns the real property rather than a junior lien on the real property itself.¹ Once a fairly obscure type of financing, in less than two decades mezzanine loans have become an integral part of the subordinated debt market for U.S. commercial real estate. The annual volume of originations in that market (including, for this purpose, the issuance of preferred equity interests) has recently been estimated as high as $20 billion.²

B. Increased Complexity. The rise in mezzanine lending has resulted in an increase in overall transactional complexity.

1. Transaction documents. In negotiating and documenting a mezzanine loan transaction, one must consider not only the mezzanine loan documents but also the senior loan documents and the intercreditor agreement between the senior lender and the mezzanine lender.

2. Relevant areas of law. In evaluating the rights of the various parties to a mezzanine loan, one must understand the impact of multiple areas of the law, including Article 8 (Investment Securities) and Article 9 (Secured Transactions) of the Uniform Commercial Code³ (the “UCC”), federal and state securities laws, and corporate, limited liability company and partnership law. Understanding these various areas of the law is critical not only when negotiating and documenting a mezzanine loan but also when enforcing a mezzanine loan.

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¹ For a depiction of a typical mezzanine loan structure, see Diagram 1 following page 16 of this outline.

² CRE FINANCE COUNCIL, INVESTING IN U.S. COMMERCIAL REAL ESTATE DEBT PRODUCTS 8 (2016).

³ In this outline, all references to the UCC are to the current official text of the UCC promulgated by the UCC’s sponsoring organizations, The American Law Institute and the Uniform Law Commission. Unless otherwise indicated, all “article” and “section” references in this outline are to articles and sections of the UCC.
C. **Focus of Outline.** The focus of this outline is on the often-complex process of enforcing a mezzanine loan by means of foreclosure. Before looking at the foreclosure process in greater detail, however, it is useful to understand the remedies generally available to a secured party under the UCC.

D. **Disclaimer.** This outline does not address issues relating to the creation of a security interest in equity interests, nor does it deal with issues relating to the perfection or priority of a security interest in equity interests. This outline also does not discuss any issues that relate to consumer transactions.

II. **SECURED PARTY REMEDIES GENERALLY**

A. **In General.** Under the UCC, a secured party has the following rights after a default by the debtor: (1) the rights provided by part 6 of Article 9 of the UCC\(^4\); and (2) subject to certain limitations,\(^5\) the rights provided by agreement of the parties.

B. **Part 6 Rights.** The rights of a secured party after default provided in part 6 of Article 9 include the following:

1. **Foreclosure by sale** – the right to sell the collateral pursuant to a public or private sale.\(^6\)

2. **Strict foreclosure** – subject to certain conditions, the right to “accept” (i.e., retain) the collateral in full or partial satisfaction of the secured obligation.

3. **Judicial enforcement** – the right to reduce a claim to judgment, foreclose or otherwise enforce a claim or security interest by any available judicial procedure.

4. **Collection** – subject to certain limitations, the right to collect from and otherwise enforce a debtor’s rights against certain persons obligated on collateral.

5. **Possession** – the right to take possession of collateral with judicial process or, so long as there is no breach of the peace, without judicial process.

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\(^4\) Part 6 of Article 9 comprises Sections 9-601 to 9-628.

\(^5\) These limitations are set forth in Section 9-602. Although these limitations are generally non-waivable, certain of them may be waived after default. For details, see Section 9-624.

\(^6\) Part 6 of Article 9 generally uses “dispose of” rather than “sell” and “disposition” rather than “sale.” For purposes of this outline, the terms may be regarded as interchangeable.
C. Rights by Agreement.

1. **General rule** – the rights of a secured party after default provided by agreement of the parties will vary from transaction to transaction. In a mezzanine loan transaction, such rights may include the following:

   a. **Voting rights.** The right to exercise management, voting and other consensual rights.

   b. **Removal rights.** The right to remove and replace certain personnel at the pledged entity (i.e., the project owner) level.

   c. **Collection rights.** Collection and enforcement rights broader than those provided by the UCC.

   d. **Rights to enter into agreements.** The right to enter into certain agreements with respect to the collateral.

2. **Limitations** – the rights provided to the secured party by agreement are limited by Section 9-602, which specifies various provisions of Article 9 that (with minor exceptions) cannot be waived or varied by agreement of the parties.7

D. **Cumulative Rights.** The rights provided by part 6 of Article 9 and, except as otherwise limited, the rights provided by agreement of the parties are cumulative and may be exercised simultaneously.

III. FORECLOSURE BY SALE

A. **In General.** After default, a secured party has the right to sell the equity interests pledged as collateral for a mezzanine loan in a public or private sale. Due to the special nature of that collateral, however, conducting an effective foreclosure sale requires more than compliance with Article 9 of the UCC and the provisions of the related security agreement; it also requires compliance with, among other things, (i) applicable securities laws, (ii) the organizational documents of the pledged entity and related provisions of law (e.g., Article 8 of the UCC and applicable corporate, limited liability company and partnership law) and (iii) any intercreditor agreement between the senior lender and the mezzanine lender. These requirements are discussed in turn.

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7 The parties are, however, generally permitted to determine by agreement the standards measuring the fulfillment of the debtor’s rights and the secured party’s duties under a rule set forth in Section 9-602 so long as the standards are not manifestly unreasonable. For details, see Section 9-603.
B. Complying with Article 9.

1. **Basic requirements** – Under Article 9, enforcing a security interest in pledged equity by means of a foreclosure sale requires a secured party to do two basic things: first, proper notice must be given to certain interested parties; and second, every aspect of the sale must be “commercially reasonable.”

   a. **Proper notice.** Following are the basic rules governing the giving of a notice of sale under Article 9:

   (i) **Persons to be notified** – As a general rule, a secured party conducting a foreclosure sale must send a reasonable authenticated\(^8\) notification of the sale to (A) the debtor (i.e., the pledgor), (B) any secondary obligor (e.g., a guarantor), (C) any person from which the secured party has received, before the notification date, an authenticated notification of a claim of an interest in the collateral, (D) any other secured party or lienholder that, ten days before the notification date, held a security interest in or other lien on the collateral perfected by the filing of a financing statement in the proper filing office, and (E) any other secured party that, ten days before the notification date, held a security interest in the collateral perfected by compliance with certain types of statutes, regulations or treaties. **Note:** Article 9 provides a “safe harbor” procedure for complying with the obligation to notify the persons specified in clause (D) above.\(^9\) It also provides relief to the secured party in the case of certain unknown persons.\(^10\)

   (ii) **Timeliness** – A notice of sale sent after default and at least ten days before the earliest time of sale set forth in the notice is sent within a reasonable time before the sale.

   (iii) **Content and form** – The contents of a notice of sale are sufficient if the notice does all of the following:

   (a) It describes the debtor and the secured party.

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\(^8\) Under Section 9-102(a), to “authenticate” a record (e.g., a writing) means either “to sign” the record or “with present intent to adopt or accept a record, to attach to or logically associate with the record an electronic sound, symbol, or process.” UCC § 9-102(a)(7).

\(^9\) See UCC § 9-611(e).

\(^10\) See UCC § 9-605.
(b) It describes the collateral that is the subject of the intended sale.

(c) It states the method of intended sale.

(d) It states that the debtor is entitled to an accounting of the unpaid indebtedness and states the charge, if any, for an accounting.

(e) It states (1) in the case of a public sale, the time and place of the sale or (2) in the case of a private sale, the time after which the sale is to be made.

In preparing a notice of sale, substantial compliance with the foregoing is sufficient and no particular phrasing is required. To make things even easier, Article 9 provides a sample form which, when completed, will provide sufficient information for a notice of sale.\(^{11}\)

b. **Commercially reasonable sale.** Under Article 9, “[e]very aspect of a disposition of collateral, including the method, manner, time, place, and other terms, must be commercially reasonable.”\(^ {12}\) A sale or other disposition of collateral may be public or private so long as it is commercially reasonable.\(^ {13}\) Whether a particular sale or disposition is commercially reasonable is a question of fact.\(^ {14}\) Following is some of the guidance on the issue of commercial reasonableness provided in Article 9:

(i) **Public sales**

(a) In general: “Although the term is not defined, as used in [Article 9], a ‘public disposition’ is one at which the price is determined after the public has had a meaningful opportunity for competitive bidding. ‘Meaningful opportunity’ is meant to imply that some form of advertisement or public notice must precede the sale (or other disposition)

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\(^{11}\) The sample form is provided in Section 9-613(5).

\(^{12}\) UCC § 9-610(b).

\(^{13}\) See id.

\(^{14}\) See, e.g., Ford & Vlahos v. ITT Commercial Finance Corp., 885 P.2d 877, 886 (Cal. 1994) (stating that whether a sale was commercially reasonable is an intensively factual question).
and that the public must have access to the sale (disposition).”\textsuperscript{15}

(b) Equity interests and similar property: “Dispositions of investment property may be regulated by the federal securities laws. Although a ‘public’ disposition of securities under [Article 9] may implicate the registration requirements of the Securities Act of 1933, it need not do so. A disposition that qualifies for a ‘private placement’ exemption under the Securities Act of 1933 nevertheless may constitute a ‘public’ disposition within the meaning of [Section 9-610]. Moreover, the ‘commercially reasonable’ requirements of [Section 9-610(b)] need not prevent a secured party from conducting a foreclosure sale without the issuer’s compliance with federal registration requirements.”\textsuperscript{16}

(ii) \textit{Private sales} – Although guidance on private sales is scant in Article 9, that should not be construed to mean that private sales are disfavored. Indeed, “[Section 9-610] encourages private dispositions on the assumption that they frequently will result in higher realization on collateral for the benefit of all concerned.”\textsuperscript{17}

(iii) \textit{Differences between public and private sales} – There are two key differences:

(a) Participating in the foreclosure sale: A secured party may purchase collateral at a public sale, but generally may not do so at a private sale.

(b) Time of sale: In its notice of sale, the secured party must set forth the \textit{time and place of} the sale in the case of a public sale, but must provide only the \textit{time after which} the sale is to be made in the case of a private sale.

(iv) \textit{Disclaimer of warranties} – Article 9 expressly provides that, in a foreclosure sale, a secured party may disclaim or

\textsuperscript{15} UCC § 9-610 cmt. 7.
\textsuperscript{16} UCC § 9-610 cmt. 8.
\textsuperscript{17} UCC § 9-610 cmt. 2.
modify the warranties that by operation of law would otherwise form part of the contract for sale (e.g., the warranties applicable to transfers of certificated and uncertificated securities under Article 8).

(v)  

Price – Article 9 provides that if the price yielded by a public or private sale is lower than the price that might have been achieved by a sale conducted in a different manner, that fact alone does not indicate that the sale was not commercially reasonable. “The fact that a greater amount could have been obtained by a [sale] at a different time or in a different method from that selected by the secured party is not of itself sufficient to preclude the secured party from establishing that the [sale] was made in a commercially reasonable manner.”18

2.  

Effect of sale – Under Article 9, a secured party’s sale of collateral after a default by the debtor does all of the following:

a. Transfer of rights. The sale transfers to a transferee for value acting in good faith all of the debtor’s rights in the collateral.

b. Discharge of secured party’s interest. The sale discharges the security interest under which the sale is made.

c. Discharge of subordinate interests. The sale discharges any subordinate security interest or other subordinate lien.

3.  

Certain post-sale matters – Once a secured party completes a sale, the secured party has the following obligations and liabilities:

a. Obligation to apply cash proceeds. As a general rule, the secured party is required to apply the cash proceeds of the sale as follows:

(i) Payment of certain expenses – First, toward the payment of the reasonable expenses of retaking, holding, preparing for disposition, processing and disposing, and, to the extent provided for by agreement and not prohibited by law, reasonable attorney’s fees and legal expenses incurred by the secured party.

(ii) Payment of secured obligation – Next, toward the satisfaction of obligations secured by the security interest under which the sale was made.

18 UCC § 9-627(a).
(iii) **Payment of subordinate obligations** – Thereafter, toward the satisfaction of obligations secured by any subordinate security interest in or other subordinate lien on the collateral provided that the secured party receives from the holder of the subordinate security interest or other lien an authenticated demand for proceeds before distribution of the proceeds is completed.

If there is any surplus after the secured party applies the cash proceeds of the sale as set forth above, the secured party is required to account for and pay the surplus to the debtor.

b. **Obligation with respect to noncash proceeds.** If the sale yields any noncash proceeds, the secured party is not required to apply the noncash proceeds unless the failure to do so would be commercially unreasonable. If the secured party nonetheless elects to apply the noncash proceeds even though it has no obligation to do so, the secured party is required to apply the noncash proceeds in a commercially reasonable manner. Any noncash proceeds of a sale that are not applied remain the secured party’s collateral.

c. **Liability for noncompliance.** If the secured party failed to comply with the provisions of Article 9 in conducting the sale, Article 9 provides that the secured party is liable for damages in the amount of any loss caused by the secured party’s failure (including, if applicable, the loss of any surplus). However, only a person that, at the time of the secured party’s failure, was a debtor or obligor or held a security interest in or other lien on the collateral sold may recover such damages.19

C. **Complying with Applicable Securities Laws.**

1. **Background** – Whether or not the equity interests pledged as security for a typical mezzanine loan constitute “securities” for purposes of Article 8 of the UCC, the equity interests will invariably constitute “securities” for purposes of the various federal and state laws governing (among other matters) the offer and sale of shares of stock, limited partnership interests, certificates of participation in a profit-sharing agreement and similar interests. Moreover, under these securities laws the equity interests will generally constitute “restricted securities” and the like which cannot be offered or sold to third party purchasers, even in a foreclosure sale under the UCC, unless either (a) the parties concerned comply with the rules related to the registration and other qualification of the equity interests or

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19 In the case of a debtor or obligor, the secured party’s liability for noncompliance may be eliminated by certain exculpatory provisions contained in part 6 of Article 9. For details, see Sections 9-605 and 9-628.
(b) applicable exemptions from such registration and qualification requirements are established.

2. **Article 9's recognition of issue** – Article 9 recognizes that compliance with applicable securities laws presents an issue for a secured party seeking to realize on collateral consisting of equity interests by means of a foreclosure sale, particularly a public foreclosure sale: “Dispositions of investment property may be regulated by the federal securities laws. Although a ‘public’ disposition of securities under [Article 9] may implicate the registration requirements of the Securities Act of 1933, it need not do so. A disposition that qualifies for a ‘private placement’ exemption under the Securities Act of 1933 nevertheless may constitute a ‘public’ disposition within the meaning of [Section 9-610]. Moreover, the ‘commercially reasonable’ requirements of [Section 9-610(b)] need not prevent a secured party from conducting a foreclosure sale without the issuer’s compliance with federal registration requirements.”

3. **No-action letters** – Fortunately, the Securities and Exchange Commission (the “SEC”) has addressed these issues in a series of “no-action letters” issued during the last 30 years or so. Under these letters, a foreclosure sale of pledged equity interests that follows certain guidelines and otherwise complies with Article 9 will generally be treated as exempt from the registration requirements imposed by the Securities Act of 1933 (the “Securities Act”). The guidelines established by the SEC in circumstances similar to those involving a defaulted mezzanine loan are as follows:

a. **Notice of sale.** A notice of sale should be sent to the debtor and all other known holders of interests in the pledged entity as well as to other persons that the secured party believes are interested and qualified to purchase the interests to be sold.

b. **Publication of notice of sale.** The notice of sale should be published and the sale should otherwise be advertised in a daily newspaper published in the county where the underlying real property is located.

c. **Content of notice of sale.** The notice of sale should state that any purchaser of the pledged equity interests at the sale will be required to represent to the secured party in writing that the equity interests are being acquired for that purchaser’s own account, are not being acquired with a view to the sale or distribution thereof in violation of the Securities Act and will not be sold by the purchaser except pursuant to an effective registration statement under the Securities Act or pursuant to a valid exemption from the

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20 UCC § 9-610 cmt. 8.
registration requirements of the Securities Act. If applicable, the notice of sale should also state that the secured party reserves the right to bid for and purchase the equity interests by credit bidding the amounts due on the secured obligation and all expenses of sale against the purchase price of the equity interests.

d. **Information regarding pledged entity.** Prospective purchasers at the sale should be furnished, upon request, such information concerning the financial position of the pledged entity as the secured party may have in its possession at the time.

e. **Investment letter.** Any purchaser of the equity interests at the sale should be required to represent to the secured party in writing that the equity interests are being acquired for that purchaser’s own account, are not being acquired with a view to the sale or distribution thereof in violation of the Securities Act and will not be sold by the purchaser except pursuant to an effective registration statement under the Securities Act or pursuant to a valid exemption from the registration requirements of the Securities Act.

f. **Sale in a single block.** The equity interests should be sold as a single unit and should not be subdivided or broken up.

g. **Legend on certificate or equivalent.** If the equity interests are certificated, the certificates should be imprinted with a legend that the equity interests are restricted securities and may not be sold or transferred except pursuant to an effective registration statement under the Securities Act or pursuant to a valid exemption from the registration requirements of the Securities Act. If the equity interests are not certificated, a notice similar to the above legend should be placed in the ownership records of the pledged entity.

The importance of the SEC’s guidance cannot be emphasized enough. A sale in which the secured party was unable to rely on a valid exemption from the registration requirements of the Securities Act would be expensive and time-consuming. If the only way that the secured party could avoid such time and expense was to sell the equity interests in a private sale, as noted above, the secured party would be precluded from purchasing the equity interests in the sale.

4. **State securities laws** – Whether following the federal guidelines outlined in the no-action letters issued by the SEC will also satisfy applicable state securities law requirements must be determined on a state-by-state basis. Such determination is beyond the scope of this outline.
D. **Complying with Organizational Documents.** Ideally, in a mezzanine loan transaction the issues related to the transfer of pledged equity interests in a foreclosure sale and the recognition of any purchaser of such interests as a partner, member or other owner of the pledged entity were addressed when the mezzanine loan was originated. To the extent that such issues have not been addressed, the secured party will need to review not only the applicable provisions of the pledged entity’s organizational documents but also the relevant provisions of state corporate, limited liability company and partnership law and, if applicable, Article 8 of the UCC.

E. **Complying with Intercreditor Agreement.** In most mezzanine loan transactions, the mezzanine lender is party to an intercreditor agreement with the senior lender. The intercreditor agreement will typically contain a number of provisions that the mezzanine lender must carefully review and strictly observe prior to commencing a foreclosure sale. Examples of such provisions, drawn from the CRE Finance Council’s standard form of intercreditor agreement,21 are as follows:

1. **Limitation on ability to foreclose** – The mezzanine lender may not exercise any rights it may have under the mezzanine loan documents or applicable law to foreclose or otherwise realize upon the pledged equity interests (including obtaining title to the pledged equity interests or selling or otherwise transferring the pledged equity interests) without first obtaining a so-called rating agency confirmation unless the transferee of title to the pledged equity interests is a so-called qualified transferee (which is generally defined to include the mezzanine lender or any entity controlled by the mezzanine lender) and certain other conditions are met.

2. **Notice of rating agency confirmation** – The mezzanine lender must notify the senior lender of any intended action relating to the mezzanine loan which would require a rating agency confirmation and must cooperate with the senior lender in obtaining such confirmation.

3. **Notice of equity collateral enforcement action** – The mezzanine lender may not take any enforcement action with respect to the pledged equity interests unless, prior to commencing such enforcement action, the mezzanine lender gives the senior lender written notice of the default which would permit the mezzanine lender to commence such enforcement action.

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21 A copy of this standard form of intercreditor agreement may be found on the CRE Finance Council’s website at [https://www.crefc.org/library](https://www.crefc.org/library) (search for “Intercreditor Agreement” using the “Search Our Library” tool).
IV. **STRICT FORECLOSURE**

A. **In General.** After default, a secured party also has the right, subject to certain conditions, to “accept” the collateral in full or partial satisfaction of the secured obligation. Under this procedure (generally referred to as “strict foreclosure” or “acceptance”), “the secured party acquires the debtor’s interest in the collateral without the need for a sale or other disposition under Section 9-610.” As a general rule, strict foreclosure will be a quicker and more efficient method of realizing on the secured party’s collateral than foreclosure by sale. As before, however, because of the special nature of equity interests as collateral, in carrying out a strict foreclosure a secured party will need to consider not only Article 9 of the UCC and the related security agreement but also applicable securities laws, the organizational documents of the pledged entity and related provisions of law (e.g., Article 8 of the UCC and applicable corporate, limited liability company and partnership law) and any intercreditor agreement between the senior lender and the mezzanine lender.

B. **Complying with Article 9.**

1. **Basic requirements** – The four basic requirements for an effective strict foreclosure or acceptance under Article 9 are as follows:
   
   a. **Preparation of proposal.** As an initial matter, the secured party will prepare a proposal to accept collateral in full or partial satisfaction of the secured obligation. “A proposal need not take any particular form as long as it sets forth the terms under which the secured party is willing to accept collateral in satisfaction. A proposal to accept collateral should specify the amount (or a means of calculating the amount, such as by including a per diem accrual figure) of the secured obligations to be satisfied, state the conditions (if any) under which the proposal may be revoked, and describe any other applicable conditions.” Although not required in all cases, as a practical matter the proposal will generally be prepared in written form.
   
   b. **Notification of proposal.** Once the secured party has completed preparation of the proposal, the secured party must send the proposal to the following persons:
   
   (i) **Debtor** – The debtor, but only if the secured party intends to rely on the debtor’s deemed acceptance of the proposal (in which event the proposal must also be unconditional

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22 UCC § 9-620 cmt. 2.

23 UCC § 9-620 cmt. 4.
and offer to accept the collateral in full satisfaction of the secured obligation).

(ii) Certain claimants – Any person from which the secured party has received, before the debtor consented to the acceptance, an authenticated notification of a claim of an interest in the collateral.

(iii) Holders of certain security interests and liens – Any other secured party or lienholder that, ten days before the debtor consented to the acceptance, held a security interest in or other lien on the collateral perfected by the filing of a financing statement satisfying certain conditions. Note that, for this purpose, there is no “safe harbor” excusing the secured party from notifying certain secured parties and other lienholders as there is under analogous circumstances in a foreclosure by sale.24

(iv) Holders of other security interests – Any other secured party that, ten days before the debtor consented to the acceptance, held a security interest in the collateral perfected by compliance with certain types of statutes, regulations or treaties.

(v) Secondary obligors – Any secondary obligor, but only if the secured party proposes to accept collateral in partial satisfaction of the secured obligation.

Each of the above persons (other than the debtor) is sometimes referred to as “a person to which the secured party was required to send a proposal under Section 9-621.”25

c. Debtor’s consent. The debtor must consent to the proposal. In an acceptance, there are two forms of consent:

(i) Actual consent – Actual consent occurs only when the debtor agrees to the terms of the acceptance in a writing or other record26 authenticated after default.

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24 See UCC § 9-621 cmt. 2.


26 In this context, a “record” means “information that is inscribed on a tangible medium or which is stored in an electronic or other medium and is retrievable in perceivable form.” UCC § 9-102(a)(70). Thus, the term “includes information that is in intangible form (e.g., electronically stored) as well as tangible form (e.g., written on paper).” UCC § 9-102 cmt. 9.a.
Deemed consent – Deemed consent occurs only when, in connection with a proposal that is unconditional and offers to accept the collateral in full satisfaction of the secured obligation, the secured party does not receive a notification of objection authenticated by the debtor within 20 days after the proposal is sent.

d. Lack of timely objection. The secured party must not receive a timely notification of objection to the proposal authenticated by any of the following persons:

(i) Persons described in Section 9-621 – Any person to which the secured party was required to send a proposal under Section 9-621. To be effective, a notification of objection from such a person must be received by the secured party within 20 days after notification was sent to that person.

(ii) Persons holding subordinate interests – Any other person, other than the debtor, holding an interest in the collateral subordinate to the security interest that is the subject of the proposal. To be effective, a notification of objection from such a person must be received by the secured party either (A) within 20 days after the last notification was sent pursuant to Section 9-621 or (B) if a notification pursuant to Section 9-621 was not sent, before the debtor consents to the acceptance.

2. Effect of acceptance – Under Article 9, a secured party’s acceptance of collateral in full or partial satisfaction of the secured obligation does all of the following:

a. Discharge of secured obligation. It discharges the secured obligation to the extent consented to by the debtor.

b. Transfer of rights. It transfers to the secured party all of the debtor’s rights in the collateral.

c. Discharge of various interests. It discharges the security interest that is the subject of the debtor’s consent and any subordinate security interest or other subordinate lien.

d. Termination of subordinate interests. It terminates any other subordinate interest.

3. Post-acceptance matters – If the secured party failed to comply with the provisions of Article 9 in undertaking the acceptance, Article 9 provides that the secured party is liable for damages in the amount of any loss caused by the secured party’s failure. Again, only a person that, at the
time of the secured party’s failure, was a debtor or obligor or held a security interest in or other lien on the collateral sold may recover such damages.\textsuperscript{27}

C. \textbf{Complying with Applicable Securities Laws.} In pursuing a strict foreclosure rather than a foreclosure by sale, a secured party will still be required to comply with applicable federal and state securities laws. Fortunately, compliance with such laws should be easier to achieve in a strict foreclosure than in a foreclosure by sale: the tension inherent in structuring a process that constitutes both a public sale under Article 9 and a private placement or other exempt transaction under applicable securities laws is simply not present in a strict foreclosure.

D. \textbf{Complying with Organizational Documents.} Generally, in a mezzanine loan transaction the issues related to the transfer of pledged equity interests in a strict foreclosure and the recognition of the transferee of the equity interests as a partner, member or other owner of the pledged entity were addressed when the mezzanine loan was originally documented. As before, to the extent that such issues have not been addressed, the secured party will need to review not only the applicable provisions of the pledged entity’s organizational documents but also the relevant provisions of state corporate, limited liability company and partnership law and, if applicable, Article 8 of the UCC.

E. \textbf{Complying with Intercreditor Agreement.} As previously noted, in most mezzanine loan transactions, the mezzanine lender is party to an intercreditor agreement with the senior lender. The intercreditor agreement will typically contain a number of provisions that the mezzanine lender must carefully review and strictly observe prior to undertaking a strict foreclosure. Examples of such provisions, drawn from the CRE Finance Council’s standard form of intercreditor agreement,\textsuperscript{28} are as follows:

1. \textit{Limitation on ability to enforce by strict foreclosure} – The mezzanine lender may not exercise any rights it may have under the mezzanine loan documents or applicable law to foreclose or otherwise realize upon the pledged equity interests (including obtaining title to the pledged equity interests) without first obtaining a so-called rating agency confirmation unless the transferee of title to the pledged equity interests is a so-called qualified transferee (which is generally defined to include the mezzanine lender or any entity controlled by the mezzanine lender) and certain other conditions are met.

2. \textit{Notice of rating agency confirmation} – The mezzanine lender must notify the senior lender of any intended action relating to the mezzanine loan

\textsuperscript{27} In the case of a debtor or obligor, the secured party’s liability for noncompliance may be eliminated by certain exculpatory provisions contained in part 6 of Article 9. For details, see Sections 9-605 and 9-628.

\textsuperscript{28} For information on how to obtain a copy of this form, see note 21 above.
which would require a rating agency confirmation and must cooperate with the senior lender in obtaining such confirmation.

3. **Notice of equity collateral enforcement action** – The mezzanine lender may not take any enforcement action with respect to the pledged equity interests unless, prior to commencing such enforcement action, the mezzanine lender gives the senior lender written notice of the default which would permit the mezzanine lender to commence such enforcement action.
DIAGRAM 1
TYPICAL MEZZ LOAN STRUCTURE

- Sponsor
- Mezz Borrower
- Mortgage Borrower (Project Owner)
- Commercial Real Estate Project

Sponsor → 100% → Mezz Borrower → 100% → Mortgage Borrower (Project Owner)

Mezz Borrower:
- Mezz Note Pledge
- Mezz Loan

Mortgage Borrower (Project Owner):
- Mortgage Note Mortgage
- Mortgage Loan

Mezz Lender
- Mezz Loan

Mortgage Lender
- Mortgage Loan