



FARELLA BRAUN + MARTEL LLP

Working Out Problem Loans

For Hotels and Other Commercial Real Estate Projects

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big firm know how + small firm know you

Agenda

- Context: It's More than the Economy
- Goals and Realistic Outcomes
- Know Your Lender/Borrower
- The Bankruptcy and Walk Alternatives
- Managing the Process
- Junior Debt, Guaranties, and Tax Issues
- Deal Alternatives, and When they Work Best

It's More than the Economy

- Worldwide Credit Crunch—Underwriting Standards, Loan to Value Ratios
- Hundreds of Billions in Real Estate Debts in Default or Maturing
- In an Economic Recovery Interest Rates Rise
- “New Normal”
- No Quick Turnaround

Realistic Analysis I

- Beginning with the End in Mind
- Can/Should this Asset Be Saved?
- Who Is in the Money and Who Will Be, in 2013 and Beyond?
- Fire Sale Liquidation and Its Cost
- Denial and Its Cost

Lender Motivations

- Lending Is a Low Margin Business and They Don't Care About Borrower's Lost Upside
- Lenders Typically Don't Have the Resources to Deal With Difficult Operational Problems
- Most Hotels and Commercial Real Estate Projects Are Not Difficult Operations

Know Your Lender

- Banks: Regulatory and Accounting. Get Paid, Have a Performing Loan, Get Cash by End of Quarter (or Take Hit Now.)
- Insurance Companies: Not Afraid of Owning the Asset
- CMBS Special Servicer: Maximize Fees, Don't Get Sued by Bondholders
- Mezzanine Lender: Cash or Carry

Lenders' View of Owner

- Honest? Usually.
- Competent? Often.
- Better Informed About Asset? Probably.
- In Denial? Always.
- Does the Owner Have a Better, Cheaper, Faster Plan for the Lender's Benefit? The Real Question

Lender Alternatives to Workout

- Sell the Loan
- Foreclose on the Asset
- Get a Deed in Lieu of Foreclosure

If the Lender Forecloses

- Some Delay
- (Expensive) Appointment of a Receiver, Pre-Foreclosure
- May Be Able to Sue on Guaranties
- Can Hold the Asset (Bid in the Debt) to Resell it Later
- Can Sell the Asset to Buyer at the Foreclosure Sale

Owner Alternative to Workout

- Walk Away (Unless There's a Guaranty)
- File Bankruptcy (If Practical)
- Short Sale/Refinancing

Bankruptcy Won't Always Work

- Bankruptcy Won't Improve Operating Income
- Retainer for Bankruptcy Counsel is Necessary
- At Least One Class of Impaired Non-Insiders Must Approve Plan to Confirm It
- Guaranties or Bad Boy Guaranties
- Absolute Priority Rule May Wipe Out Owner

When Bankruptcy Can Work

- Extend Loan Maturities, Change Interest and Pay Rates and Other Loan Terms (e.g., Due on Sale)
- Permit New Junior Borrowing
- Pay Unsecured or Junior Creditors at a Deep Discount or Convert to Equity
- Sell Assets
- Get Breathing Room

Managing Your Lender

- Owner is honest, competent and gets it
- Full information about the property and prospects
- Plan A and a Plan B
- Why It Is in Lender's Interest to Work With You

Why Work With Owner?

- Owner/Manager is Cheaper than Receiver
- Owner Can Sell at Higher Price
- Owner Motivated to Turn Property Around (Unless No Guaranty and Junior Lender Captures Appreciation)
- Owner Often Has Other Motivation to Make Property a Success (Tax, Guaranty, Management Fees, Reputation)
- Less Trouble/Delay

Managing the Process

- Moving to Special Assets
- The Pre Workout Negotiation Agreement
- Forbearance
- Information
- Speed and Realism
- Get Credit for Contributions Before Making Them

Doable Deals

- Extension and Forbearance: For How Long?
- Recapitalizing With a Lender Haircut: Debt Relief Plus Interest Reserve
- New Money in for Releasing Guarantor and Changing Pay Terms
- Cash Flow Mortgage Plus
- Deed in Lieu or Short Sale With a Sop to Ownership

Undoable Deals

- Unrealistic Owners
- Lender Takes a Haircut Now for Nothing in Return
- Deals that Are Worse for Lenders than Foreclosure
- Deals that Leave Nothing for Ownership or Guarantors Except Tax Problems
- Deals on CMBS Loans Without Appalling Fees for the Special Servicer

When Bankruptcy Can Help

- Extend Loan Maturities, Change Interest and Pay Rates and Other Loan Terms (e.g., Due on Sale)
- Permit New Junior Borrowing
- Pay Unsecured or Junior Creditors at a Deep Discount or Convert to Equity
- Sell Assets
- Get Breathing Room

Useful Structures

- New Money vs. Old Debt Negotiation
- “Hope Certificate”
- Management/Consulting Fees
- Cash Flow Mortgage
- Interest Reserve/Capital Reserve
- Trading Something for Relief on the Guaranty or Relief from Tax Consequences

Past Webinars

- Buying Hotels (and Other Commercial Real Estate Assets) Out of Bankruptcy
- Guaranties of Debt in Default: What to do Now (for Guarantors and Creditors)

Future Webinars

- Understanding Tax Impacts of Foreclosure and Debt Restructuring: Better Deals (with Uncle Sam's Money)

Presenters

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