

# Workout Options



# Maturity Date Extension

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- **A maturity date extension is generally the most readily available type of modification**
- **Occurs when the impending default is due solely to the maturity of the loan and the borrower's inability to obtain replacement financing in the current capital market environment**
- **As a general rule, most Portfolio Loan lenders are not equipped and do not want to foreclose on and take back your property**
- **Accordingly, if the loan is otherwise performing and you are perceived to be a "good" borrower, many lenders are willing to grant maturity date extensions**
  - Up to 24 months for a Portfolio Loan
  - Up to 12 months for a CMBS Loan with extension options (6-12 months)
- **All (of course) subject to certain negotiated conditions**
- **The lender/servicer will request a fee for accommodating such an extension and/or option, in most cases**

# Additional Funding

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- **In some instances, the value of the lender's collateral can be significantly increased by an influx of additional capital**
- **While it is very unusual in today's environment for this to occur, in some instances a Portfolio Lender may be willing to advance additional funds to enhance the value of the property**
- **However, it is a virtual certainty that the lender will require the borrower also to infuse additional capital as the price for funding additional loan proceeds**
- **If the borrower is unable or unwilling to fund that additional capital, a more likely solution is sometimes achieved by convincing the lender to agree to allow a reallocation of reserves to other sources**
- **Since Special Servicers are not lenders, additional funding is not available in a CMBS Loan modification, although Special Servicers can, in appropriate situations, agree to allow a reallocation of reserves to other sources as previously described**

# Short Sale

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- **A so-called “short sale” is a scenario in which the lender allows the property to be sold for an amount less than the outstanding debt and releases its lien against the loan collateral**
  - Assuming the loan is no longer performing and the lender can be convinced that the market value has deteriorated to the amount sought in the short sale, both Portfolio Loan lenders and CMBS Loan lenders may consent to short sales
- **The incentive to the note holder is the generally accepted supposition that the property can be sold for more by the current borrower, than as REO by the lender**
  - The property will have been tainted by foreclosure and there will be significant associated sales costs to the selling lender
- **Typically the lender will not allow any sale proceeds to leak to the borrower**
  - However, we have seen Portfolio Loan situations where institutional borrowers with captive real estate brokers are allowed to retain a sales commission where the broker’s efforts are instrumental to facilitating the short sale

# Deed-in-Lieu

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- **A deed-in-lieu of foreclosure (a “Deed-in-Lieu”) is a deed to the property given to the lender (or to the lender’s affiliate) rather than (in lieu of) taking the property back through foreclosure**
- **In some instances the lender will work with the borrower to structure the Deed-in-Lieu to look more like a sale, which arguably may allow more favorable tax treatment and less perceived “taint” to the sponsor**
- **From both a Portfolio Loan lender and a CMBS Loan lender’s perspective, a Deed-in-Lieu is generally more expedient than foreclosure**
- **A Deed-in-Lieu does not eliminate liens and encumbrances that are subordinate to the senior loan**
  - Instances in which there are junior mortgages or mechanic’s liens, any lender is going to be less inclined to accept a deed-in-lieu
- **In some instances these concerns may be overcome by having the property conveyed to an affiliate of the lender**
  - Allows the lender the ability to foreclose the loan in the future, thereby eliminate junior liens and encumbrances
  - In this scenario, it is essential to include so-called “non-merger” language to make sure that the lender’s security interest and the owner’s fee interest have not merged by reason of the Deed-in-Lieu

# Interest Rate Reduction

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- **Your lender's own costs of funds are low and it is more palatable for Portfolio Loan lenders to grant**
  - Temporary interest rate reductions
  - Interest-only payments (where normally monthly principal (or amortization) payments would be payable monthly along with the applicable interest payments)
- **If the borrower can demonstrate that its property will cover operating expenses and debt service at a lower interest rate, Portfolio Loan lenders may agree to downward adjustments of the interest rate to as low as the "prime rate" on a temporary basis**
  - Generally for a period of up to 24 months
- **Interest rate reductions are very rare in CMBS Loan modifications**
- **However, in some instances, the Special Servicer may agree to temporarily allow monthly payments to be made on an interest-only basis**
- **There have been few instances when the Special Servicer allowed a reduction of the interest rate on a CMBS Loan *in exchange* for a partial principal reduction payment by the borrower**

# Principal Balance Reduction

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- **This is far and away the most difficult type of a modification to achieve**
- **However, if your Portfolio Loan lender can be convinced that the market value of the collateral has fallen significantly below the outstanding principal balance of your loan then it is possible to reduce the principal balance of their loan**
  - **To not less than the market value of the property**
- **In almost every instance however, the lender will require to see some equity or other benefit to the property infused by the borrower (or its principals)**
- **However, it should be noted that principal balance reduction is virtually unheard of in a CMBS Loan modification; especially since it is the Special Servicer who will typically absorb the principal reduction loss**
- **This alternative has tax implications resulting in cancellation of indebtedness Income**
- **The borrower may qualify for exclusion under IRS sec 108**
- **The rules are very complicated and require an analysis of each borrowers unique situation**

# White Knight

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- **A hybrid of the Principal Balance Reduction modification described above is a so-called “White Knight” transaction**
- **This is a transaction in which the lender agrees to substitute the original Portfolio Loan sponsor with a new sponsor (a “White Knight”)**
  - The White Knight is perceived by the lender to have superior financial and/or operational capacity to that of the original sponsor
  - In this scenario, the principal balance and/or interest rate of the Portfolio Loan is typically reduced to a current market level in exchange for the influx of new capital (or new capital commitment or partial recourse guaranty) by the White Knight
  - The original sponsor is released from liability, but may be allowed to retain passive participation
- **For the same reasons that principal balance reductions don’t generally take place on the CMBS Loan side of things, White Knight transactions are structured very differently in CMBS Loan modifications**
  - The White Knight contributes capital and takes a partial ownership in the Borrower typically in the form of preferred equity
  - In this scenario, the original Borrower/sponsor is not released from liability

# Equity Participation

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- **If a Portfolio Loan lender can be convinced that the borrower is the best operator for the property and has a realistic opportunity to reposition a property in the market**
  - We have seen Portfolio Loan lenders convert debt to preferred equity participation in the Portfolio Loan borrower
  - This is particularly true in connection with the resolution of mezzanine or subordinate debt held by Portfolio Loan lenders
- **Conversely, CMBS Loan lenders are precluded from taking equity participation interests, so this is not an option the CMBS Loan world**

# Relief from Personal Guaranty

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- **If the lender can be convinced that the borrower does not have meaningful financial resources or liquidity (or both, as they often go hand in hand)**
- **Both Portfolio Loan lenders and CMBS Loan lenders will often agree to reduce or eliminate personal guaranties**
  - In exchange for a borrower cooperation in a “friendly foreclosure” or deed-in-lieu transaction