

Bankruptcy Court Maintains the *Status Quo*, Allaying Fears of CMBS Industry

When General Growth Properties, Inc. (GGP) filed for bankruptcy on April 16, 2009, the commercial mortgage backed securities market (CMBS) paid attention. Not only is GGP the second-largest operator of shopping centers in the United States, but it is also reported to be, through its affiliates and subsidiaries, the largest borrower in the United States CMBS market, accounting for \$15 billion of the approximately \$800 billion outstanding in U.S. CMBS loans. CMBS market participants have been especially concerned about the simultaneous bankruptcy filings by numerous bankruptcy-remote special purpose subsidiaries (SPEs) that hold title to GGP's real estate assets.

GGP's Original Proposed DIP Financing and Cash Management Plan

In order to continue operating during reorganization, the GGP debtors, as a group, sought to incur debtor-in-possession (DIP) financing, to continue to process cash received from tenant rents through GGP's existing centralized cash management system, and to use that cash to support the debtors' collective operations. As originally conceived, the DIP loan would have been guaranteed by the SPE debtors and the DIP lender's collateral would have included second mortgages on the SPE debtors' real property and first priority liens on the cash in the centralized cash management system.

Objections to GGP's Original Proposal

Lenders and industry groups objected vociferously to the voluntary bankruptcy filings of the SPE debtors and the originally proposed DIP financing and cash management plan.

First, they argued that the SPE bankruptcy filings were made in bad faith since the SPE debtors were not in need of bankruptcy protection and filed solely for the benefit of GGP in contravention of their own organizational documents (which would have required unanimous consent of the SPEs' directors/managers, including the affirmative vote of the SPEs' independent directors/managers).

Second, they contended that the proposed DIP collateral package and cash management order did not provide adequate protection for the use of the lenders' cash collateral and would result in de facto substantive consolidation.

Approved DIP Financing and Cash Collateral Plan

The bankruptcy court approved a revised DIP financing and cash management plan that was responsive to the CMBS lenders' most significant concerns by providing for the following:

- Maintaining the pre-bankruptcy status quo with respect to the SPE debtors' shopping center properties by providing for the ongoing payment of real estate taxes, maintenance and operating expenses and current interest on the loans
- Removing the SPE debtors' assets securing the CMBS loans from the DIP lender's collateral package

- Providing the CMBS lenders with a first priority adequate protection lien on cash collateral in the centralized cash management system and a second priority adequate protection lien on a separate portfolio of real property
- Requiring compliance with CMBS loan covenants with respect to periodic financial reporting and to lenders' approval rights over leasing and other encumbrances on the real property collateral

While making the above concessions to the CMBS lenders, the approved DIP financing and cash management order retained the following features:

- No property specific cash escrows for insurance, taxes or property expenses, whether or not lender controlled
- No lender controlled lockboxes
- No amortization payments

Fears Allayed

Because the final DIP financing and cash management order eliminated any liens on the SPE Debtors' collateral to secure the DIP financing and provided the CMBS lenders with significantly improved priority on the cash collateral and other assets of GGP, the worst fears of the CMBS industry were allayed.

Open Questions

While the cash management order maintains the status quo for now, there remain many uncertainties as to how various stakeholders, including the mezzanine lenders, may fare as the bankruptcy case progresses. In particular, the court is scheduled to hear motions seeking the dismissal of certain of the SPE bankruptcy cases on June 17, 2009. The court's decisions on those motions could have significant ramifications for holders of CMBS and other asset-backed securities issued by bankruptcy remote, special purpose subsidiaries of real estate and other operating companies.

Impact

It seems certain that CMBS lenders will use the GGP bankruptcy as an opportunity to tighten up the terms of future loans in order to make SPE borrowers even more "bankruptcy-remote." Terms will likely include the routine imposition of "hard" lockboxes on property level cash flow, tighter restrictions on affiliated entities providing services to SPE borrowers, stricter monitoring and reporting requirements and stronger credit enhancement and recourse guarantees.

Ropes & Gray's Real Estate, Debt Finance and Bankruptcy and Business Restructuring groups have significant experience in advising on CMBS and other securitized financing arrangements. Ropes & Gray represents clients ranging from borrowers to purchasers of participations in mortgage and mezzanine loans and CMBS and other asset-backed securities. If you have any questions about the GGP bankruptcy or CMBS and other securitized financings, please do not hesitate to contact your regular Ropes & Gray attorney.

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