

SINGLE ASSET REAL ESTATE BANKRUPTCIES UNDER BAPCA By Jeanne Wanlass

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Newspaper headlines shout out daily warnings of a downturn in the real estate market. Regardless of whether the real estate "bubble" actually bursts, with the changes in the bankruptcy law in 2005, an update of your familiarity with single asset real estate matters in bankruptcy cases can help you understand what could happen if such a case is filed.

What is a Single Asset Real Estate Case?

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) became effective on October 17, 2005. In an attempt to "fast track" certain types of cases, BAPCPA essentially redefined the term "single asset real estate" to mean a single piece of real property, other than residential real property with fewer than 4 residential units, which generates substantially all of the debtor's gross income, and on which no other substantial business is being conducted by the debtor. A single asset real estate case is a bankruptcy case filed for such an entity.

Why does it matter?

The Bankruptcy Code automatically stays certain actions, such as foreclosures, upon the filing of a bankruptcy petition. Under the prior law, the automatic stay was not limited to any specific period of time when the single asset real estate entity had secured debt of more than a certain amount (the automatic stay was limited to 90 days after the filing of a petition if the secured debt was less than \$4,000,000). Owners of valuable property could tie it up for months while they tried to resolve their financial difficulties.

Now, however, quick action by a single-asset debtor is required regardless of the amount of secured debt. A bankruptcy court will grant relief from the stay unless a single asset debtor has filed a plan of reorganization within 90 days of the date the petition is filed. Before the new law, a large single asset real estate chapter 11 debtor had at least 120 days after the petition filing date to file its plan of reorganization. Additionally, the plan of reorganization must now demonstrate a reasonable chance of being confirmed within a reasonable time. For example, the debtor must show in its plan that it has the ability to: (1) obtain new money to invest

in the enterprise; (2) refinance the current loans; or (3) sell the property entirely.

Debtors no longer have the option to hold off their secured lenders while they explore other options to save the property from foreclosure. The single-asset debtor must start making monthly payments on most secured debt in an amount equal to interest at the non-default contract rate, not just the interest on the current fair market rate as was authorized previously. If these monthly payments are not made, the secured creditor can obtain relief from the automatic stay to foreclose on the property. These debtors also do not have the chance to lower the payments on their secured debt due to a lower market value of the property. Creditors need no longer fear that an attempt to obtain relief from the automatic stay will bring a challenge to the value of the property, thus resulting in both denial of the stay and lower interest rate payments.

What Can A Debtor Do?

It is important for debtors to establish that they are not a single asset real estate entity if they wish to avoid having to file a plan on the fast track or make payments at the original contract rate.

A debtor can establish that it is not a "single asset real estate" case if it can show that the property is not being used only for rental purposes. One example of this is In re Kkemko, Inc., 181 B.R. 47 (Bankr.S.D.Ohio 1995), in which the business of a marina was more than the simple rental of moorings-the debtor also stored, repaired, and winterized boats, provided showers and a pool and other activities for boaters, sold gas, and provided concessions. In another example, In re CBJ Development, Inc., 202 B.R. 467 (9th Cir. BAP 1996), a Chapter 11 debtor's operation of a gift shop, restaurant and bar in its hotel constituted substantial other business and, thus, the debtor's hotel was not a "single asset real estate" for the purposes of the automatic stay.

If the debtor has no other substantial business at the property, it must do as much pre-bankruptcy planning as possible so as to be ready to file a plan of reorganization with a reasonable chance of success within 90 days of the petition filing. This is no easy task, as the debtor should recognize before it undertakes to accomplish it.

What Can a Creditor Do?

Creditors do not have to blindly accept a debtor's decision that the debtor is not a single asset real estate entity. Creditors may ask the bankruptcy court to review the debtor's status. If the bankruptcy court decides that the debtor is a single asset real estate entity, then the debtor must file its plan or begin making payments at the contract rate within 30 days. If the debtor does decide to make payments at the contract interest rate, the debtor may, at its sole discretion, make those payments from the rents or other income generated by the property.

The filing of a bankruptcy case always involves risks and rewards. With the amendments to the Bankruptcy Code, both creditors and debtors should be aware of how those risks and rewards have changed.

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