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Commercial Real Estate Workouts

Single Asset Real Estate Bankruptcy Cases

As commercial real estate values continue to fall, real estate owners and their lenders need to be aware of bankruptcy laws related to single asset real estate entities.

In 1994, the Single Asset Real Estate (SARE) law was added to the Bankruptcy Code. Bankruptcy courts and Congress recognized the need to have specific laws that address a common scenario in all economic downturns.

WHY DOES QUALIFYING AS A SARE DEBTOR MATTER UNDER U.S. BANKRUPTCY LAW?

Because it can mean a much more streamlined—and lender friendly—bankruptcy process.

WHAT KINDS OF COMMERCIAL REAL ESTATE QUALIFY UNDER SARE?

- Single, commercial real estate properties such as office buildings, shopping, and strip malls—including a project spread between several parcels of real estate, as long as the project is unified by a common plan or usage.
- Property whose income is generated as a result of passive ownership—not workers' labor and management services.

Property that generates no income can qualify under the SARE definition according to most courts.

- Real property that, for the generation of revenue, requires active, day-to-day employment of workers and managers and that would not generate substantial revenue without such labor.

For example, a boat marina that generates income from storing boats or selling gas or a golf course that sells memberships or provides golf lessons are considered outside of the SARE definition.

WHAT MAKES SARE BANKRUPTCIES DIFFERENT FROM OTHER BANKRUPTCIES?

Within 90 days of filing bankruptcy, a SARE debtor needs to either file a plan of reorganization that has a reasonable possibility of being confirmed within a reasonable time, or provide its secured lender with payments equal to the non-default interest due under the applicable loan documentation on the value of the creditor's interest in the real estate.

This is a marked exception to the general automatic stay privilege that most debtors are entitled to upon filing bankruptcy. The general automatic stay can only be lifted in most instances upon "cause" or a showing of a lack of equity in the property. The SARE exception provides a secured lender either clarity as to the debtor's intentions with respect to the property or a payment stream equal to some amount of interest, all within 90 days of the bankruptcy filing.



Commercial real estate debtors fight the SARE label—and their secured lenders fight to apply it. Case law is littered with disputes as to whether a debtor qualifies as a SARE debtor or whether the interest payments made by the debtor after 90 days are congruent with the secured creditor's interest in the real estate.

Getting the bankruptcy court to recognize the bankruptcy as an attempt to avoid a rightful foreclosure and applying the streamlined SARE bankruptcy provisions can provide a secured lender helpful leverage in the debtor's bankruptcy case.

A secured lender that receives notice of a bankruptcy on the eve of foreclosing on a SARE debtor's commercial property needs to engage experienced bankruptcy counsel. Please contact us should you face a Single Asset Real Estate bankruptcy issue.

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