

## Negotiating Reserve Provisions in Real Estate Loan Transactions

Determining Funding and Disbursement Conditions for Tax and Insurance,  
Tenant Rollover, Repair, FF&E, Environmental and Earnout Reserves

WEDNESDAY, FEBRUARY 8, 2017

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

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# Reserve Provisions in Real Estate Loan Transactions

Strafford Webinars

**February 8, 2017**

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# Reserve Roadmap

- Required Repairs / Deferred Maintenance
- Taxes & Insurance Premiums
- Replacements / Capital Expenditures
- Tenant Improvement and Leasing Commissions aka “TI/LC”
- Fixtures, Furniture & Equipment aka “FF&E”
- Ground Rent
- Seasonality
- Earn-out
- Environmental Remediation
- Litigation
- Excess Cash Flow
- Letters of Credit

# Required Repairs / Deferred Maintenance Sample Term Sheet Language

- **Upfront Reserves:**

Borrower shall be required at closing to deposit [\_\_\_\_]% of any immediate and year-one deferred maintenance or environmental remediation costs into a sub-account of the Cash Management Agreement (the “**Upfront Reserves Account**”), unless waived by Lender based upon review and approval of property condition report for the Property.

# Required Repairs / Deferred Maintenance

## Sample Loan Agreement Language

### ■ Immediate Repair Funds.

- Borrower shall perform the repairs at the Property as set forth on Schedule I hereto (all such repairs are hereinafter referred to as “**Immediate Repairs**”) and shall complete each of the Immediate Repairs on or before the respective deadline for each repair as set forth on Schedule I hereto (as such deadlines may be extended by Lender in its sole discretion). On the Closing Date, Borrower shall deposit into an Eligible Account held by Lender or Servicer (the “**Immediate Repair Account**”) an amount equal to \$[\_\_\_\_\_], such amount representing [125]% of the estimated costs of the Immediate Repairs. Amounts deposited pursuant to this Section [\_\_] are referred to herein as the “**Immediate Repair Funds**”.
- Lender shall disburse to Borrower the Immediate Repair Funds upon satisfaction by Borrower of each of the following conditions: (i) Borrower shall submit a request for payment to Lender at least ten (10) days prior to the date on which Borrower requests such payment be made and specifies the Immediate Repairs to be paid; (ii) on the date such request is received by Lender and on the date such payment is to be made, no Event of Default shall exist and remain uncured; (iii) Lender shall have received a certificate from Borrower (A) stating that all Immediate Repairs to be funded by the requested disbursement have been completed in a good and workmanlike manner and in accordance with all applicable Legal Requirements, such certificate to be accompanied by a copy of any license, permit or other approval by any Governmental Authority required in connection with the Immediate Repairs, (B) identifying each Person that supplied materials or labor in connection with the Immediate Repairs to be funded by the requested disbursement, and (C) stating that each such Person has been paid in full or will be paid in full upon such disbursement, such certificate to be accompanied by lien waivers, invoices and/or other evidence of payment satisfactory to Lender; (iv) at Lender’s option, if the cost of the Immediate Repairs exceeds \$25,000, a title search for the Property indicating that the Property is free from all liens, claims and other encumbrances other than Permitted Encumbrances; (v) at Lender’s option, if the cost of the Immediate Repairs exceeds \$25,000, Lender shall have received a report satisfactory to Lender in its reasonable discretion from an architect or engineer approved by Lender in respect of such architect or engineer’s inspection of the required repairs; and (vi) Lender shall have received such other evidence as Lender shall reasonably request that the Immediate Repairs to be funded by the requested disbursement have been completed and are paid for or will be paid upon such disbursement to Borrower. Lender shall not be required to disburse Immediate Repair Funds more frequently than once each calendar month nor in an amount less than the Minimum Disbursement Amount (or a lesser amount if the total Immediate Repair Funds is less than the Minimum Disbursement Amount, in which case only one disbursement of the amount remaining in the account shall be made).

# Taxes & Insurance Premiums

## Sample Term Sheet Language

- **Tax and Insurance Reserve:**

Borrower shall be required make monthly deposits into a sub-account of the Cash Management Account (the “**Tax and Insurance Reserve Account**”) in an amount equal to 1/12<sup>th</sup> of the annual taxes and insurance premiums as Lender reasonably estimates will be payable during the ensuing twelve-month period. Lender shall make disbursements from the Tax and Insurance Reserve Account to pay for such real estate taxes and insurance premiums in accordance with the loan documents.

# Taxes & Insurance Premiums

## Sample Loan Agreement Language

- **Deposits to Taxes & Insurance Reserve Fund:**

On each Payment Date after the Closing Date, Borrower shall pay to Lender one-twelfth (1/12) of the real estate taxes and insurance premiums Lender estimates will be payable during the ensuing twelve-month period in order to accumulate with Lender sufficient funds to pay such taxes and insurance premiums as they become due. Amounts so deposited shall hereinafter be referred to as the “**Taxes & Insurance Reserve Funds**” and the account in which such amounts are held shall hereinafter be referred to as the “**Taxes & Insurance Reserve Account**”.

- **Release of Taxes & Insurance Reserve Funds:**

Lender shall apply the Taxes & Insurance Reserve Funds to the payment of real estate taxes and insurance premiums. In making any payment relating to real estate taxes and insurance premiums, Lender may do so according to any bill, statement or estimate it procures from the appropriate public office or insurer or agent, without inquiry into the accuracy of such bill, statement or estimate. If the amount of Taxes & Insurance Reserve Funds exceeds the amounts due for the real estate taxes and insurance premiums for the immediately succeeding twelve (12) months as determined by Lender, Lender shall return any excess to Borrower. If at any time Lender reasonably determines that the Taxes & Insurance Reserve Funds are not or will not be sufficient to pay the real estate taxes and insurance as they become due, Lender shall provide written notice to Borrower of such determination and Borrower, commencing with the first Payment Date following receipt of such notice, shall increase its monthly payments to Lender by the amount that Lender estimates is sufficient to make up the deficiency at least thirty (30) days prior to the due date of the real estate taxes and insurance premiums.

# Replacements / CapEx

## Sample Term Sheet Language

- **Replacement Reserve:**

Borrower shall be required to deposit at closing \$[\_\_\_\_\_] into a sub-account of the Cash Management Account (the “**Replacement Reserve Account**”). In addition, Borrower shall make monthly deposits into the Replacement Reserve Account in an amount equal to \$[\_\_\_\_\_] / [\$\_\_ [psf] / [per unit] per annum (subject to adjustment based on Lender’s review of the property condition report for the Property). Lender shall make disbursements from the Replacement Reserve Account for replacements incurred by Borrower in accordance with the loan documents.

# Replacements / CapEx

## Sample Loan Agreement Language

- a) Borrower shall deposit into an Eligible Account held by Lender or Servicer (the “**Replacement Reserve Account**”) on each Monthly Payment Date an amount equal to \$[\_\_\_\_\_] (the “**Replacement Reserve Monthly Deposit**”) for the Replacements. Amounts deposited pursuant to this Section [ ] are referred to herein as the “**Replacement Reserve Funds**”. Lender may reassess its estimate of the amount necessary for Replacements from time to time and, and may require Borrower to increase the monthly deposits required pursuant to this Section [ ] upon thirty (30) days notice to Borrower if Lender determines in its reasonable discretion that an increase is necessary to maintain proper operation of the Property.
- b) Lender shall disburse Replacement Reserve Funds only for Replacements. Lender shall disburse to Borrower the Replacement Reserve Funds upon satisfaction by Borrower of each of the following conditions: (i) Borrower shall submit a request for payment to Lender at least ten (10) days prior to the date on which Borrower requests such payment be made and specifies the Replacements to be paid; (ii) on the date such request is received by Lender and on the date such payment is to be made, no Event of Default shall exist and remain uncured, (iii) Lender shall have received a certificate from Borrower (A) stating that the items to be funded by the requested disbursement are Replacements, (B) stating that all Replacements at the Property to be funded by the requested disbursement have been completed in a good and workmanlike manner and in accordance with all applicable Legal Requirements, such certificate to be accompanied by a copy of any license, permit or other approval required by any Governmental Authority in connection with the Replacements, (C) identifying each Person that supplied materials or labor in connection with the Replacements to be funded by the requested disbursement and (D) stating that each such Person has been paid in full or will be paid in full upon such disbursement, such certificate to be accompanied by lien waivers, invoices and/or other evidence of payment satisfactory to Lender; (iv) at Lender’s option, if the cost of any individual Replacement exceeds \$25,000, a title search for the Property indicating that the Property is free from all liens, claims and other encumbrances other than Permitted Encumbrances; (v) at Lender’s option, if the cost of any individual Replacement exceeds \$25,000, Lender shall have received a report satisfactory to Lender in its reasonable discretion from an architect or engineer approved by Lender in respect of such architect or engineer’s inspection of the required repairs; and (vi) Lender shall have received such other evidence as Lender shall reasonably request that the Replacements at the Property to be funded by the requested disbursement have been completed and are paid for or will be paid upon such disbursement to Borrower. Lender shall not be required to disburse Replacement Reserve Funds more frequently than once each calendar month nor in an amount less than the Minimum Disbursement Amount (or a lesser amount if the total amount of Replacement Reserve Funds is less than the Minimum Disbursement Amount, in which case only one disbursement of the amount remaining in the account shall be made).

# TI/LC

## Sample Term Sheet Language

- **TI/LC Reserve:**

Borrower shall be required to deposit at closing \$[\_\_\_\_\_] into a sub-account of the Cash Management Account (the “**TI/LC Reserve Account**”). In addition, Borrower shall make monthly deposits into the TI/LC Reserve Account in an amount equal to \$[\_\_\_\_\_]. Lender shall make disbursements from the TI/LC Reserve Account for approved tenant improvements and leasing commissions at the Property in accordance with the loan documents.

# TI/LC

## Sample Loan Agreement Language

- **Deposits to TI/LC Account:**

At Closing, Borrower shall deposit \$[AMOUNT] (“**TI/LC Funds**”) into an account with Lender (“**TI/LC Account**”). The TI/LC Funds will be used to reimburse Borrower and/or to pay for the reasonable costs and expenses incurred by Borrower in completing the tenant improvements and/or paying the tenants under the applicable leases’ allowances for tenant improvements and/or paying leasing commissions under the applicable Leases, in each case in the amounts allocated to, and as described for each applicable lease (“**TI/LC Lease**”).

- **Release of TI/LC Funds:**

Provided that no Event of Default has occurred and is continuing, Lender shall disburse TI/LC Funds held in the TI/LC Account to Borrower, within 15 days after the delivery by Borrower to Lender of a disbursement request (“**TI/LC Request**”). Borrower shall not make TI/LC Requests more than once a month. Lender shall disburse TI/LC Funds pursuant to a TI/LC Request, provided: (i) Borrower shall have provided Lender with either (1) as to any leasing commission relating to a TI/LC Lease, reasonable evidence that such commissions have been paid, or are then due and will be paid with proceeds of the requested disbursement, or (2) as to tenant improvement work or allowances therefor, reasonable evidence indicating, as applicable, (A) that the tenant improvements or allowances therefor have been completed in accordance with the applicable TI/LC Lease, (B) that the tenant is then owed and entitled to payment upon the applicable tenant allowance pursuant to the terms of a TI/LC Lease, or (C) if the time period upon which the applicable tenant may draw upon the TI/LC Lease has elapsed, that such tenant is no longer entitled to obtain or require the payment of the tenant allowance under the terms of the TI/LC Lease; and (ii) the TI/LC Request is accompanied by (A) an Officer’s Certificate certifying that TI/LC Funds will be used only to pay (or reimburse Borrower for) the relevant expenditures set forth above, and that the same have not been the subject of a previous disbursement, and (B) reasonably detailed supporting documentation as to the amount, necessity, and purpose therefor. Any disbursement of TI/LC Funds of more than \$50,000 to pay (rather than reimburse) tenant improvements under this Section may, at Lender’s option, be made by joint check payable to Borrower and the payee of such tenant improvements.

# FF&E

## Sample Term Sheet Language

- **FF&E Reserve:**

Borrower shall be required to deposit at closing \$[\_\_\_\_\_] into a sub-account of the Cash Management Account (the “**FF&E Reserve Account**”). In addition, Borrower shall make monthly deposits into the FF&E Reserve Account in an amount equal to 1/12<sup>th</sup> of the greater of (i) [\_\_\_\_]% of total gross revenues of the Property or (ii) that amount required pursuant to the franchise agreement. Lender shall make disbursements from the FF&E Reserve Account for FF&E expenses incurred by Borrower in accordance with the loan documents. **[INSERT FOR HOSPITALITY ONLY, IN LIEU OF REPLACEMENT RESERVE, WHICH IS TO BE DELETED.]**

# FF&E

## Sample Loan Agreement Language

- **Deposits to FF&E Reserve Fund:**

On each Payment Date after the Closing Date, Borrower shall pay to Lender one-twelfth (1/12) of the greater of (i) [\_\_]% of the Projected Gross Revenues of the Property; or (ii) that amount required pursuant to the Franchise Agreement in order to accumulate with Lender sufficient funds to pay FF&E Expenditures as such may arise. Amounts so deposited shall hereinafter be referred to as the “**FF&E Reserve Funds**” and the account in which such amounts are held shall hereinafter be referred to as the “**FF&E Reserve Account**”.

- **Release of FF&E Reserve Funds:**

So long as no uncured Event of Default exists, Lender shall disburse FF&E Reserve Funds for Approved FF&E Expenses actually due and payable, pursuant to draw requests made by the Borrower in the form of Exhibit [\_\_]. Each draw request shall (i) specify the Approved FF&E Expenses for which such disbursement is requested, (ii) include a certification from Borrower that no Event of Default has occurred and is continuing, (iii) include a certification from Borrower that the repair or work that is the subject of such request has been performed substantially in accordance with the terms of the agreements for the performance of such repair or other work, (iv) include a certification from Borrower that such Approved FF&E Expenses are due and payable to the applicable payees, and (iv) include a certification from Borrower that the costs and expenses that are the subject of such request have not been the subject of a previous request for disbursement.

Each draw request for Approved FF&E Expenses must be accompanied by (i) invoices, receipts, or other evidence satisfactory to Lender verifying costs for which FF&E Reserve Funds are being requested, and (ii) if required by Lender, affidavits, lien waivers, and/or releases from all parties who furnished materials and/or services in connection with the requested disbursement. Lender shall make disbursements from the FF&E Reserve Account within 10 days of the date Lender receives a request meeting the above requirements.

# FF&E

## Sample Loan Agreement Language (cont'd)

- If there are FF&E Reserve Funds remaining in the FF&E Reserve Account after the Maturity Date, Lender shall return any excess to Borrower. If at any time Lender determines that the FF&E Reserve Funds are not or will not be sufficient to pay FF&E Expenditures, Lender shall provide written notice to Borrower of such determination and Borrower, commencing with the first Payment Date following receipt of such notice, shall increase its monthly payments to Lender by the amount that Lender estimates is sufficient to make up the deficiency.
- **“Projected Gross Revenues”** shall mean all revenue the Borrower anticipates it will receive in the following twelve month period from the ownership and operation of the Property from whatever source, including, without limitation, any rents.
- **“Approved FF&E Expenses”** shall mean FF&E Expenditures incurred by Borrower or an operating lessee and either (i) included in the Borrower’s annual budget, as approved by Lender, or (ii) approved by Lender, which approval shall not be unreasonably withheld or delayed.

# Ground Rent

## Sample Loan Agreement Language

- **Deposits to Ground Rent Reserve Fund:**

On each Payment Date after the Closing Date, Borrower shall pay to Lender one-twelfth (1/12) of the rents (including both base rent and additional rents (excluding any real estate taxes or similar charges otherwise reserved for hereunder)) (collectively, the "**Ground Rent**") due under the Ground Lease during the next ensuing twelve (12) months in order to accumulate with Lender sufficient funds to pay all such Ground Rent at least thirty (30) days prior to the due date. In addition, on the Closing Date, Borrower shall pay to Lender an amount equal to any Ground Rent payable under the Ground Lease within thirty (30) days of the first Payment Date. Amounts so deposited shall hereinafter be referred to as the "**Ground Rent Reserve Funds**" and the account in which such amounts are held shall hereinafter be referred to as the "**Ground Lease Reserve Account**".

- **Release of Ground Rent Reserve Funds:**

Lender shall apply the Ground Rent Reserve Funds to the payment of the Ground Rent. In making any payment relating to the Ground Rent, Lender may do so according to any bill, statement or estimate procured from Ground Lessor, without inquiry into the accuracy of such bill, statement or estimate. If the amount of Ground Rent Reserve Funds exceeds the amounts due for the Ground Rent under the Ground Lease for the immediately succeeding twelve (12) months as determined by Lender, Lender shall return any excess to Borrower. If at any time Lender reasonably determines that the Ground Rent Reserve Funds are not or will not be sufficient to pay the Ground Rent by the dates set forth above, Lender shall provide written notice to Borrower of such determination and Borrower, commencing with the first Payment Date following receipt of such notice, shall increase its monthly payments to Lender by the amount that Lender estimates is sufficient to make up the deficiency at least thirty (30) days prior to the due date of the Ground Rent.

# Seasonality

## Sample Term Sheet Language

- Additional on-going deposits for seasonality shall be as set forth below. The year-one deposits for seasonality are estimated at approximately \$[\_\_\_] million, (sized to achieve 1.10x actual DSCR after actual capex reserves, for anticipated shortfalls during July, August, September and October) and for all periods thereafter shall be sized to achieve 1.10x actual DSCR after actual capex reserves, for anticipated shortfalls during July, August, September and October. The seasonality reserve shall be funded from operating cash flows and cash contributed at closing or a letter of credit (at Borrower's choice).

# Seasonality

## Sample Loan Agreement Language

- Borrower shall deposit with Lender (i) on the Closing Date, an amount equal to \$[\_\_\_\_\_] and (ii) on the Payment Dates occurring in each of the months of December, January, February, March, April and May thereafter (the “**Seasonality Payment Period**”) during the term of the Loan, the applicable Seasonality Monthly Deposit to create a seasonality reserve to be available for use by Borrower to pay for shortfalls in Debt Service and Operating Expenses set forth on the Annual Budget as more particularly described in Section 9.3(b) below. Amounts so deposited shall hereinafter be referred to as the “**Seasonality Reserve Fund**” and the account in which such amounts are held shall hereinafter be referred to as the “**Seasonality Reserve Account**”.

# Seasonality

## Sample Loan Agreement Language (cont.)

- No later than ten (10) Business Days prior to each of the Payment Dates occurring in each of the months of July, August, September, October and November, Borrower may, at its option, deliver to Lender an Officer's Certificate requesting a disbursement from the Seasonality Reserve Account, and setting forth in reasonable detail the amount of funds necessary for the payment of Debt Service due and payable on such Payment Date and/or Operating Expenses set forth on the Annual Budget to be incurred in such calendar month, in either case, together with such other information necessary and sufficient to fairly represent the financial position and results of operation of the Property during such calendar month; provided, however, that, notwithstanding the foregoing, Borrower shall be permitted to request (1) Debt Service shortfalls with respect to the Payment Dates occurring in August, September, October and November only (and no other calendar months), and (2) Operating Expense shortfalls with respect to the Payment Dates occurring in July, August, September and October only (and no other calendar months). Provided no Event of Default is then continuing, on the Payment Date in each of July, August, September, October and November of each calendar year, Lender shall disburse to the Deposit Account or other account designated in writing by Borrower such amount so requested by Borrower pursuant to the terms and conditions of the immediately preceding sentence (if and to the extent sufficient funds are on then on deposit and available for disbursement from the Seasonality Reserve Account). Upon the written request of Borrower, provided no Event of Default is then continuing, Lender agrees to disburse to Borrower on the Payment Date occurring in December of each calendar year, any funds in excess of the amount Borrower is required to deposit with Lender for the next Seasonality Shortfall Period (if and to the extent excess funds are then on deposit and available for disbursement from the Seasonality Reserve Account).

# Earn-out

## Sample Loan Agreement Language (additional loan or release of loan funds)

- Lender shall [loan to Borrower the following amounts (each, a “**Milestone Loan**”)] [release the following additional funds of the Loan (each, a “**Milestone Release**”)], up to, but not including, the Maturity Date and up to an aggregate outstanding principal amount of \$[AMOUNT], upon the achievement by Borrower of the following events (each, a “**Milestone Event**”):
  - (i) \$[AMOUNT] upon [DESCRIPTION OF MILESTONE]
  - (ii) \$[AMOUNT] upon [DESCRIPTION OF MILESTONE]
  - (iii) \$[AMOUNT] upon [DESCRIPTION OF MILESTONE]

Borrower shall promptly notify Lender after a Milestone Event has been achieved by providing evidence of such achievement as required by Lender. Within [\_\_] business days of notification by Borrower to Lender of the realization of a Milestone Event, Lender shall make the corresponding [Milestone Loan] [Milestone Release] in cash by wire transfer of immediately available funds to the bank account provided by Borrower. All amounts loaned to Borrower under this section will be added to the aggregate outstanding principal balance under the Loan.

# Earn-out

## Sample Loan Agreement Language (borrowing base)

- Lender shall increase the Borrowing Base by [\_\_]% of the book value of Eligible Accounts (each, a “**Milestone Increase**”), up to, but not including, the Maturity Date and up to a total percentage of [\_\_]%, upon the achievement by Borrower of the following events (each, a “**Milestone Event**”):
  - (i) [DESCRIPTION OF MILESTONE]
  - (ii) [DESCRIPTION OF MILESTONE]
  - (iii) [DESCRIPTION OF MILESTONE]

Borrower shall promptly notify Lender after a Milestone Event has been achieved by providing evidence of such achievement as required by Lender. Within [\_\_] business days of notification by Borrower to Lender of the realization of a Milestone Event, Lender shall make the corresponding Milestone Increase.

# Environmental Remediation

## Sample Loan Agreement Language

- At Closing, Borrower shall establish a reserve account with Lender in an amount equal to \$[AMOUNT] (“**Environmental Remediation Reserve**”) to cover costs necessary to remediate environmental issues identified [during the Environmental Due Diligence/by [GOVERNMENT AGENCY]] (“**Environmental Remediation Work**”). Upon the occurrence and during the continuance of an Event of Default, Lender, at its option, may withdraw all funds from the Environmental Remediation Reserve and Lender may apply such funds either to completion of the Environmental Remediation Work or toward reduction of the Indebtedness. Lender’s right to withdraw from and apply the Environmental Remediation Reserve is in addition to all other rights and remedies provided to Lender under this Agreement and the other Loan Documents.

# Litigation

## Sample Loan Agreement Language

- On the Closing Date, Borrower shall deposit with Lender an amount equal to \$[\_\_\_\_\_] to pay for certain costs and expenses incurred by Borrower in connection with a final settlement or other final disposition of the Castle Blue Litigation. Amounts so deposited shall hereinafter be referred to as the “**Castle Blue Reserve Funds**” and the account in which such amount is held shall hereinafter be referred to as the “**Castle Blue Reserve Account.**”
- Notwithstanding anything herein to the contrary, no deposit of Castle Blue Reserve Funds by Borrower shall be required hereunder so long as an amount equal to \$[\_\_\_\_\_] is being held in escrow by Stone LLC for application to settlement of the Castle Blue Litigation in accordance with the terms of the Settlement Agreement. If such amounts are being held in escrow as set forth in the foregoing sentence, then upon reasonable request of Lender, Borrower will provide evidence reasonably satisfactory to Lender that such amounts are being so held.

# Litigation

## Sample Loan Agreement Language (cont.)

- Lender shall disburse to Borrower the Castle Blue Reserve Funds from the Castle Blue Reserve Account from time to time, but not more frequently than once in any thirty (30) day period, upon satisfaction by Borrower of each of the following conditions: (a) Borrower shall submit a written request for disbursement to Lender at least fifteen (15) days prior to the date on which Borrower requests such payment be made which request shall specify the costs and expenses incurred by Borrower in connection with a final settlement or other final disposition to be paid with the requested disbursement, (b) on the date such request is received by Lender and on the date such payment is to be made, no Default or Event of Default shall exist and remain uncured, and (c) Lender shall have received an Officer's Certificate (i) stating that all costs and expenses to be funded by the requested disbursement relate to a final settlement or other final disposition of the Castle Blue Litigation, such Officer's Certificate to be accompanied by a copy of the relevant settlement agreement, final judgment or other evidence reasonably satisfactory to Lender evidencing such final settlement or disposition, (ii) identifying each Person to be paid or reimbursed by the requested disbursement, and (iii) stating that each such Person has been paid in full or will be paid in full upon such disbursement. Lender shall not be required to make disbursements from the Castle Blue Litigation Reserve Account unless such requested disbursement is in an amount greater than \$5,000 (or a lesser amount if the total amount in the Litigation Reserve Account is less than \$5,000, in which case only one disbursement of the amount remaining in the account shall be made) and such disbursement shall be made only upon satisfaction of each condition contained in this Section.

# Excess Cash Flow

## Sample Term Sheet Language

- **Cash Flow Sweep:**

[All revenues of the Property remaining after the payment of debt service and required reserve and escrow deposits and monthly disbursements to Borrower for budgeted operating and capital expenditures in accordance with the Lender-approved budget and payment of any other amounts due and payable to Lender (such remaining revenues, “**Excess Cash Flow**”) shall be retained by Lender as additional cash collateral for the Loan if the Property fails to maintain a DSCR of at least [\_\_\_\_]x / [the debt yield on the Loan is less than [\_\_\_\_]%] for two consecutive calendar quarters. Such Excess Cash Flow shall continue to be collected until, and all such retained Excess Cash Flow then on deposit with Lender, shall be released to Borrower when the Property achieves a DSCR of at least [\_\_\_\_]x / [the debt yield on the Loan is at least [\_\_\_\_]%] for two consecutive calendar quarters and no event of default then exists. Debt yield shall be determined by Lender quarterly on a trailing 12 month basis by dividing net operating income (determined by Lender) by the outstanding amount of the Loan.]

# Excess Cash Flow

## Sample Loan Agreement Language

- **Retention of Excess Cash Flow:**

Lender shall retain all Excess Cash Flow in a reserve account (“**Excess Cash Flow Reserve**”) if the Borrower fails to maintain a Debt Service Coverage Ratio of at least  $[[\_\_\_\_]x]$  / [the debt yield on the Loan is less than  $[\_\_\_\_]\%$ ] for two consecutive calendar quarters. Amounts held in the Excess Cash Flow Reserve are hereinafter referred to as the “**Excess Cash Flow Funds.**” Lender shall continue to retain all Excess Cash Flow until the Borrower achieves a DSCR of at least  $[[\_\_\_\_]x]$  / [the debt yield on the Loan is at least  $[\_\_\_\_]\%$ ] for two consecutive calendar quarters and no Event of Default then exists (“**Excess Cash Flow Cure**”). Upon the occurrence of an Excess Cash Flow Cure, the Lender shall return all Excess Cash Flow Funds to the Borrower.

Lender shall calculate debt yield quarterly on a trailing 12 month basis by dividing Net Operating Income by the outstanding amount of the Loan.

# Letters of Credit

## Sample Loan Agreement Language

- Borrower may deliver to Lender a Letter of Credit in accordance with the provisions of this Section 7.10 in lieu of the deposits required to be made or previously made in accordance with Sections 7.1(a), 7.2(a), 7.3(a), 7.4(a), 7.5(a), 7.6(a), 7.7(a) and 7.8 (the “**Applicable Accounts**”); provided that any such Letter of Credit shall be accompanied by an instrument reasonably acceptable to Lender whereby the applicant/obligor under such Letter of Credit shall have waived all rights of subrogation against Borrower thereunder until the Debt has been paid in full. The aggregate amount of any Letter of Credit and cash on deposit with respect to the Applicable Accounts shall at all times be as provided pursuant to Sections 7.1(b), 7.2(b), 7.3(u), 7.4(c), 7.5(b), 7.6(a), 7.7(b) and 7.8. Borrower shall provide Lender no less than thirty (30) days prior notice of Borrower’s election to deliver a Letter of Credit to Lender and Borrower shall pay to Lender upon demand all of Lender’s costs and expenses in connection therewith, including, without limitation, reasonable attorneys’ fees. If Borrower delivers to Lender a Letter of Credit in accordance with the provisions of this Section 7.10 in lieu of the deposits required to be made or previously made in any Applicable Account, Borrower shall deliver to Lender a New Insolvency Opinion if any of the repayment obligations under such Letter of Credit are borne by any Affiliate of Borrower. Neither Borrower nor the applicant/obligor under any Letter of Credit shall be entitled to draw upon any such Letter of Credit. Upon thirty (30) days notice to Lender, Borrower may replace a Letter of Credit with a cash deposit to any Applicable Account in the amount required pursuant to the applicable Section hereof only if the applicable Letter of Credit has been outstanding for more than six (6) months. In addition, if Borrower shall, at any time, receive notice that the bank issuing any Letter of Credit has ceased to be an Approved Bank, before being required to replace such Letter of Credit with a cash deposit as provided in the immediately preceding sentence, Borrower shall have ten (10) Business Days after receipt of notice to replace such Letter of Credit with another Letter of Credit in the same face amount as the replaced Letter of Credit, which new Letter of Credit shall be issued by an Approved Bank. If Borrower elects to replace a Letter of Credit with a cash deposit in accordance with the terms and conditions hereof, Borrower shall deposit with Lender an amount equal to the amount that would have accumulated in any Applicable Account if such Letter of Credit had not been delivered.

# Letters of Credit

## Loan Agreement Language (continued)

- **“Letter of Credit”** shall mean an irrevocable, unconditional, transferable, clean sight draft letter of credit which is either (a) an “evergreen” letter of credit (meaning, for the purposes of this definition, a Letter of Credit which is automatically renewed unless the issuer thereof provides not less than thirty (30) days notice to Lender that said Letter of Credit will not be automatically renewed) or (b) one which does not expire until at least two Business Days after the Maturity Date and which Letter of Credit is in form and substance reasonably satisfactory to Lender, and entitles Lender as beneficiary thereunder to draw thereon based solely on a statement executed by an officer of Lender stating that it has the right to draw thereon, and issued by a domestic Approved Bank or the U.S. agency or branch of a foreign Approved Bank, provided that if there are no domestic Approved Banks or U.S. agencies or branches of a foreign Approved Bank then issuing letters of credit, then such letter of credit may be issued by a domestic bank, the long term unsecured debt rating of which is the highest such rating then given by the Rating Agency or Rating Agencies, as applicable, to a domestic commercial bank.
- **“Approved Bank”** shall mean (i) with regard to a Letter of Credit having a term in excess of one (1) month, either (A) a bank or other financial institution which has a minimum long term unsecured debt rating of at least “AA” by S&P and its equivalent by the other Rating Agency or Rating Agencies, as applicable, or (B) [\_\_\_\_\_]; provided that at the time in question, (x) [\_\_\_\_\_] is an Eligible Institution and (y) the issuance by [\_\_\_\_\_] of such Letter of Credit shall not cause or give rise to a Material Adverse Effect on any Secondary Market Transaction and (ii) with regard to a Letter of Credit having a term not in excess of one (1) month, a bank or other financial institution which has a minimum short term unsecured debt rating by S&P of at least A 1+ and its equivalent by the other Rating Agency or Rating Agencies, as applicable.

# Letters of Credit

## Loan Agreement Language (continued)

- Each Letter of Credit delivered under this Agreement shall be additional security for the payment of the Debt. Upon the occurrence and during the continuance of an Event of Default, Lender shall have the right, at its option, to draw on any Letter of Credit and to apply all or any part thereof to the payment of the items for which such Letter of Credit was established or to apply each such Letter of Credit to the payment of the Debt in such order, proportion or priority as Lender may determine. Any such application to the Debt after an Event of Default that remains uncured shall be subject to the payment by Borrower of an amount equal to the Yield Maintenance Premium that would be required if a Total Defeasance Event had occurred in an amount equal to the outstanding principal amount of the Loan to be satisfied or prepaid. On the Maturity Date, any such Letter of Credit may be applied to reduce the Debt.

# Letters of Credit

## Loan Agreement Language (continued)

- In addition to any other right Lender may have to draw upon a Letter of Credit pursuant to the terms and conditions of this Agreement, Lender shall have the following additional rights to draw in full any Letter of Credit: (i) with respect to any evergreen Letter of Credit, if Lender has received a notice from the issuing bank thereof that such Letter of Credit will not be renewed and a substitute Letter of Credit (or appropriate cash collateral pursuant to Section 7.10(a)) is not provided at least thirty (30) days prior to the date on which such Letter of Credit is scheduled to expire, notwithstanding any Property Substitution elected by Borrower but not completed pursuant to Section 7.8 by such date; (ii) with respect to any Letter of Credit with a stated expiration date, if Lender has not received a substitute Letter of Credit (or appropriate cash collateral pursuant to Section 7.10(a)) at least thirty (30) days prior to the date on which such Letter of Credit is scheduled to expire, notwithstanding any Property Substitution elected by Borrower but not completed pursuant to Section 7.8 by such date; (iii) upon receipt of a notice from the issuing bank that such Letter of Credit will be terminated (except if the termination of such Letter of Credit is permitted pursuant to the terms and conditions of this Agreement or a substitute Letter of Credit or appropriate cash collateral pursuant to Section 7.10(a) is provided), notwithstanding any Property Substitution elected by Borrower but not completed pursuant to Section 7.8; or (iv) if Lender has received notice that the bank issuing such Letter of Credit shall cease to be an Approved Bank and Borrower shall have not replaced such Letter of Credit with a Letter of Credit issued by an Approved Bank (or appropriate cash collateral pursuant to Section 7.10(a)) within ten (10) Business Days after notice thereof, notwithstanding any Property Substitution elected by Borrower but not completed pursuant to Section 7.8 by such date. Notwithstanding anything to the contrary contained above in this Section 7.10(c), Lender is not obligated to draw on any Letter of Credit upon the happening of an event specified in clauses (i), (ii), (iii) or (iv) above and shall not be liable for any losses incurred by Borrower due to the insolvency of the bank issuing any Letter of Credit if Lender has not drawn on such Letter of Credit.

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