IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF KANSAS

In re:

JOHN Q. HAMMONS FALL 2006, LLC, et al.,	Case No. 16-21142
	Chapter 11
Debtors.	Jointly Administered

SUR-REPLY TO THE JOINT REPLY TO CMBS LENDERS' RESPONSE TO THE COURT'S ORDER OF JULY 5, 2018

The CMBS Lenders[1] hereby reply to the Joint Reply (the "Reply") [Docket No. 2442] filed by JD Holdings, LLC and the Debtors (jointly, the "Joint Parties") to the CMBS Lenders' Response (the "Response") [Docket No. 2442] to the Court's Order of July 5, 2018 [Docket No. 2396] regarding (1) the CMBS Lenders' Motion to Allow Oversecured CMBS Claims (the "CMBS Claims Motion")[2] and (2) the Joint Objections of the Debtors and JD Holdings, L.L.C. ("JDH") to Claims in Respect of the Chateau Lake and G7 Loans[3] as follows:

PRELIMINARY STATEMENT

The positions advanced by the Joint Parties' objections find no support in the law. First,

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[1] The "CMBS Lenders" include the following secured creditors: (a) U.S. Bank National Association, as Trustee for the Registered Holders of J.P. Morgan Chase Commercial Mortgage Securities Corp., Commercial Mortgage Pass-Through Certificates, Series 2006-LDP7, by and through LNR Partners, LLC, solely in its capacity as Special Servicer (holder of the loan known as the "Nomura Portfolio Loan"); (b) Wilmington Trust, National Association, as Trustee for the registered holders of Wells Fargo Commercial Mortgage Trust 2015-C26, Commercial Mortgage Pass-Through Certificates, Series 2015-C26 by and through Midland Loan Services, a division of PNC Bank, National Association, solely in its capacity as Special Servicer (holder of the loan known as the "Chateau Lake Loan"); (c) Deutsche Bank Trust Company Americas, as Trustee, on behalf of the Registered Holders of Citigroup Commercial Mortgage Securities, Inc., Commercial Mortgage Pass-Through Certificates, Series 2015-GC33, by and through LNR Partners, LLC, solely in its capacity as Special Servicer (holder of the loan known as the "Goldman Portfolio Loan" or the "G7 Loan"); and (d) Wells Fargo Bank, N.A., as successor to LaSalle Bank National Association, as Trustee for the registered holders of COMM 2006-C8 Commercial Mortgage Pass-Through Certificates, by and through LNR Partners, LLC, solely in its capacity as Special Servicer (holder of the loan known as the "Barclays Portfolio Loan").

[2] Docket No. 2038.

[3] Docket Nos. 2032; 2033.

as the Court knows, two of the CMBS loans have not matured. As to these two loans, JDH has requested that the lenders consent to either reinstatement pursuant to § 1124 of the Bankruptcy Code or assumption under the terms of the loan documents. It is black letter law that in the context of either an assumption or reinstatement scenario, JDH must cure existing defaults per the letter of the loan documents without change or alteration.[4] This is explicitly set forth in § 1124(2) of the Bankruptcy Code and has been affirmed by every circuit court to hear the issue. Any challenges to such assumption or reinstatement are governed by state law, not bankruptcy law. JDH does not challenge any of this and, importantly, concedes that under New York law the claims for default interest are fully enforceable.[5] A § 506(b) reasonableness analysis has no applicability to cure or reinstatement. These are state law issues.

The matured loans are also governed by New York law and their default interest provisions are similarly enforceable. Circuit court-level case law interpreting the issue states that default interest is presumptively enforceable at the contract rate, unless one of four equitable facts warrants otherwise, each of which is determined from the vantage point of the debtor:[6] (i) the creditor engaged in misconduct in the bankruptcy case, (ii) default interest will reduce distribution to other non-insider creditors, (iii) default interest will jeopardize a fresh start or reorganization, or (iv) the rate of default interest constitutes a penalty. None of these equitable factors exists here. There is a full-pay Chapter 11 plan in this case, so no unsecured creditors

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[4] See CMBS Claim Motion, pp. 17-19 [Docket No. 2038].

[5] See Reply, pp. 12, 13, note 14 ("…default interest in enforceable under New York law, something that the Joint Parties do not dispute.") The only loan not governed by New York law is the Chateau Lake Loan, which is governed by Missouri law. Default interest is enforceable under Missouri law, as has been previously briefed by the CMBS Lenders. See Response to Order of July 5, 2018 p. 14-16 [Docket No. 2428.]

[6] See CMBS Lender's Motion to Allowed Oversecured CMBS Claims, pp. 10-13. Additionally, at least one circuit court looks solely to the contract rate of default interest and does not allow for reduction for equitable considerations. See In re Dow Corning Corp., 456 F.3d 668, 679 (6th Cir. 2006).

will be paid less if the CMBS Lenders' default interest is paid. The CMBS Lenders are not even alleged to have engaged in misconduct and, in fact, are alleged in JDH's briefing to have been too passive in this case. The JDH plan has been confirmed, so there is no debtor "fresh start" at issue. Finally, there is no basis to contend that either a 4% or 5% default interest rate is penal. 33 cases affirm that a 4% or 5% default interest rate is reasonable and not a penalty.[7] In contrast, JDH has never identified a single commercial case reaching a different conclusion. Accordingly, none of the equitable factors analyzed by some courts in the context of post-bankruptcy default interest is present in this case.

Recognizing that the law does not support them, the Joint Parties' argue that default interest should be disallowed because the lender will use the default interest to pay for loan administrative services. This argument asks the Court to weigh allowability in a context that has never before occurred in a bankruptcy court. The determining factor being proposed is not whether the default interest rate will equitable as to the Debtor, but whether the Lenders' use of the money is equitable. In JDH's view, creditors who already have money or who would not use their money to their or a debtor's satisfaction should not be paid money that is contractually owed to them. If that were the case, Bill Gates would not be entitled to an allowed claim solely because he has enough money. And, a power company would not be entitled to repayment if it would use the money to build a power plant fueled by, in a debtor's opinion, the wrong kind of energy source. In other words, JDH wants to judge what a creditor would do with the creditor's own money before deciding whether the creditor should be paid. This is unheard of and it should come as no surprise that JDH cites no case law whatsoever for this proposition. No case law has ever evaluated the allowability of default interest by reviewing a lender's application of

[7] See Response, pp. 16-17.

payments ***after they are received by the lender***. No legal authority makes a lender's disposition of default interest a factor in evaluating its enforceability and none is cited by the Joint Parties.

Default interest under CMBS loan documents—the governing loan documents between the CMBS Lenders and the Debtors—***is not paid to special servicers. It is paid to the lenders – the securitization trusts that hold the loans.*** The only question before the Court is the CMBS Lenders' entitlement to default interest under the above equitable factors. It is irrelevant what the securitization trusts do with the funds that have been repaid to them.

The Joint Parties' arguments regarding guaranty liability are also misdirected. All of the four guaranties held by the CMBS Lenders provide for liability of the JQH Trust for the amounts owed by the underlying borrowers. The only partial exception to this is the Nomura Guarantee under which liability is capped at $25 million. As detailed in the Response, the JQH Trust is liable to the CMBS Lenders for the amounts owned by the relevant Borrower.[8]

Finally, the yield maintenance objections raised by the Joint Parties are not yet ripe for adjudication. JDH can either proceed to reinstate and assume the unmatured CMBS loans or it can prepay them. It cannot do both. JDH has pursued assumption of the unmatured loans with vigor both prior to and following plan confirmation. They have provided all requested documents needed to underwrite assumption of both the Chateau Lake Loan and the Goldman Portfolio Loan – they have gone so far as to pay one of the loan servicers a $40,000 deposit to cover the lender's out-of-pocket legal expenses related to the assumption. These efforts have required substantial efforts from the lender side of the transactions. The only issue apparently holding up the loan assumption process is JDH's unwillingness to pay default interest that they now admit is a legally enforceable obligation. By contrast, JDH has never at any time tendered early payment for the unmatured loans. Accordingly, although the yield maintenance provisions

[8] See Response, pp. 22-24.

of the relevant loan agreements are enforceable under controlling law, actual prepayment of the loans at this point in time is merely theoretical and thus not yet ripe for adjudication.

CMBS LENDERS' SUR-REPLY

1. Complete copies of the loan agreements ("Loan Agreements") out of which the CMBS Lenders' claims to (a) default interest, (b) fees, costs, and expenses, and (c) yield maintenance (collectively, "Disputed Claims") arise.

Response: The Joint Parties do not dispute the CMBS Lenders' response to question no. 1.

2. Citations to the particular sections of each Loan Agreement (including definitions, where applicable) that support each Disputed Claim.

Response: The Joint Parties do not dispute the CMBS Lenders' response to question no. 2.

3. Whether each Borrower's[9] bankruptcy filing constitutes an "Event of Default" (or the equivalent defined term) as to that Borrower under the applicable Loan Agreement.

Response: The Joint Parties do not dispute the CMBS Lenders' response to question no. 3.

4. Whether the JQH Trust's bankruptcy filing constitutes an "Event of Default" (or the equivalent defined term) as to each Borrower under the applicable Loan Agreement.

Response: The Joint Parties do not dispute the CMBS Lenders' response to question no. 4.

[9] The CMBS Lenders each hold one of four oversecured claims against certain debtors (the "Borrowers") in these jointly-administered cases.

5. Evidence of the *bankruptcy*-related risks and costs for which default interest on a CMBS loan compensates.

Response: As has been extensively briefed by the CMBS Lenders, default interest is a remedy that is enforceable under New York and Missouri law to compensate lenders for not only the ***costs*** of administering a defaulted loan, but also the increased ***risks*** of lending to a defaulted borrower. In re Bowles Sub Parcel A, LLC, 792 F.3d 897, 902-03 (8th Cir. 2015) (holding default interest enforceable with regard to CMBS loans: "[a] default on this type of loan has unique costs that are difficult to quantify, including *the increased risk of lending to a defaulted borrower*")(emphasis added.) The precise nature of the increased risks inherent to defaulted CMBS loans are described in the Reply in detail and are also articulated in detail in the Greenspan Declaration. Despite this evidence, the Joint Parties have categorically failed to specifically respond to or refute these bankruptcy-related risks and costs. The following table demonstrates this failure:

Risks and Costs Detailed in CMBS Lenders' Response	Joint Parties' Reply
Delay in recovery in principal upon maturity	No reply
Payment of non-market rate interest prior to maturity	No reply
Inability to control timing of reinvestment of repaid principal	No reply
Lost opportunity to reinvest repaid principal	No reply
Negative effect on CMBS bond pricing due to uncertainty	No reply
Unfavorable changes in CMBS re-investment rates due to inability to timely re-invest repaid principal	No reply
Risk of non-recoupment of costs and expenses	No reply
Disruption in monthly CMBS bond interest payments due to cash collateral orders	No reply

Accrual of interest on amounts advanced to CMBS bondholders due to interruptions in monthly debt service payments	No reply
Inability of CMBS Lenders to promptly exercise remedies	No reply
Inability to control market timing of collateral disposition	No reply
Risk of changes to loan maturity	No reply
Risk of change to interest rates	No reply
Risk of reduction in principal	No reply
Risk of discharge of debt	No reply
Risk of change to terms of loan documents	No reply
Risk of non-consensual 363(f) sale of collateral	No reply
Risk of imposition of new borrower credit risk imposed upon non-consensual collateral sales	No reply
Confirmation of Chapter 11 plans over creditor objection	No reply
Non-consensual changes in borrower and guarantor	No reply
Non-consensual release of collateral in non-recourse loan	No reply

In addition to failing to respond to the elements of bankruptcy-related risk detailed in the Response, the Joint Parties rely on fallacious reasoning in maintaining that the default interest owed to the CMBS Lenders, which they themselves admit is enforceable under New York law, should not be a part of the CMBS Lender's oversecured bankruptcy claims. The first fallacy is that default interest is not payable to the CMBS Lenders, but rather only to the special servicers who service the loans. The second fallacy is that default interest can only be enforced in bankruptcy if the CMBS Lenders can show what the Joint Parties refer to as "actual harm." The final fallacy is that *ipso facto* clauses are unenforceable in bankruptcy as a matter of law.

A. <u>Default interest is not solely for the benefit of servicers</u>. The case law cited by the CMBS Lenders conclusively shows that default interest at the rates of 4% or 5% provided for under the CMBS Lenders' loan documents is enforceable under state law, regardless of what type of lender is at issue – commercial banks, insurance companies, CMBS lenders or other, non-bank lenders, or how it is utilized by the lenders. <u>See</u> Response, 16-17. In point of fact, in the Reply, the Joint Parties state more than once that the default interest sought by the CMBS Lenders is enforceable under New York law.[10]

The Joint Parties nonetheless maintain that default interest should be denied because it will be used by the CMBS Lenders to pay the special servicers for loan servicing. This is patently false. Under the terms of all of the loan agreements produced to the Court in connection with the Response, default interest is paid to the CMBS Lenders – the securitization trusts which hold the promissory notes. Under no provision of any of those documents are the Borrowers obligated to pay default interest to loan servicers. To support their point, the Joint Parties sew confusion by conflating the ***CMBS bondholders***, who ultimately receive their principal and interest payments from the CMBS mortgage payments, ***with the actual lenders – the CMBS trusts themselves***.

The Joint Parties also seek to have the Court believe – without the support of a single reported case or statute – that a lender's disposition of default interest ***after it is paid to the lender*** can determine the enforceability of the default interest provision in bankruptcy. Under this thinking, a 4% or 5% default interest rate could be enforceable for a commercial bank that lends on a portfolio basis and holds and services loans for its own income, but would not be enforceable for a CMBS loan of similar amount and with

[10] <u>See</u> Reply, pp. 12, 13 n. 14;

similar terms and collateral because the default interest may be paid as a part of CMBS special servicer compensation. Such reasoning stands logic on its head. The Joint Parties cite no case law whatsoever that allows courts to look behind a lender's receipt of default interest and hold that interest charge to be either allowable or not based up the post-payment disposition of the default interest received.

Even if courts were authorized to look behind the loan documents to determine the reasonableness of default interest, the Joint Parties' assertion that default interest is paid to servicers is inaccurate and a gross oversimplification. Before any default interest monies are paid to a special servicer, the securitization trust must first be reimbursed for amounts advanced for debt service or to protect its collateral. By way of example, the document which determines distribution of default interest for the Goldman Portfolio Loan provides a distribution waterfall for default interest and other charges such as late fees. That document is the Pooling and Servicing Agreement Dated as of September 1, 2015 (the "Goldman PSA"). Under § 3.14 of the Goldman PSA, modification fees, default interest and certain other charges (defined as under the term "Penalty Charges") flow over a four-level distribution waterfall. The first priority in payment is reimbursement of amounts "advanced" by either the special servicer, master servicer or the trustee of the securitization trust, along with interest payable on those advances. "Advances" include (i) "P&I Advances" – amounts advanced by the master servicer or securitization trust trustee for principal and interest due on CMBS bonds to make up for shortfalls in the amount due to bondholders, and (ii) "Property Advances" – amounts advanced by the master or special servicer needed to protect the securitization trust's interest in collateral, including costs such as legal and appraisal fees.

The second priority in the waterfall is reimbursement to the securitization trust of Advances that have been determined to be non-recoverable from late payments, insurance or condemnation proceeds or liquidation proceeds. The third priority is reimbursement to the securitization trust of certain other securitization trust expenses not provided for in the two higher levels of distribution priority. The forth, final and lowest priority in the distribution of default interest is compensation to the special servicer, provided that the default interest accrued while the underlying loan was specially serviced and provided that the default interest has not become exhausted in making the trust whole. A copy of the relevant portion of the Goldman PSA, including controlling definitions, is attached hereto as Exhibit A.

Contrary to the assertions of the Joint Parties, default interest results in lower base interest rates for borrowers than if no default interest were embedded in the loan documents. This obvious conclusion was reached years ago in the Ruskin case from the Second Circuit. See Ruskin v. Griffiths, 269 F.2d 827, 832 (2d Cir. 1959)("It [default interest] can be beneficial to a debtor in that it may enable him to obtain money at a lower rate of interest.") The same conclusion was reached in the context of CMBS loans in the Greenspan Declaration, p.9, ¶ 12(b). The Joint Parties' conclusory arguments to the contrary are made of whole cloth and based upon their misguided argument that default interest serves as some sort of disguised servicing fee. The Joint Parties' argument that CMBS base interest rates would not be higher absent default interest is completely without support in either the reported case law or evidence, be it expert testimony or otherwise.

As is clear from the Goldman PSA and the Greenspan Declaration, any default interest that does get paid to special servicers is not duplicative[11] of the normal special servicing fee, but rather is a negotiated component of total servicer compensation for the securitization trust overall which may contain hundreds of individual CMBS loans. As stated in the Greenspan Declaration:

> "[a]lthough the special servicer cannot know exactly which loans will ultimately default and provide it with this additional default interest compensation, the expectation of earning these amounts is a material consideration for their agreement to specially service defaulted loans and the consideration of what is an acceptable base-level monthly special servicing fee to which it is entitled when a defaulted loan is transferred to special servicing. Greenspan Declaration, ¶ 12(c).

Further, the Greenspan Declaration points out the logical extension of these facts – absent the availability of default interest, the base rate of compensation paid to special servicers would have to be higher than its present level. Greenspan Declaration, pp. 9-10, ¶ 12(c). Again, the Joint Parties offer only conclusory arguments to the contrary – they offer no evidence or case law to support their arguments of double compensation to servicers or to counter the market disruption that would be caused in CMBS lending if default interest were not enforceable and available as a component of servicer compensation. The Joint Parties also fail to cite a single case holding that default interest is unenforceable because some of it may be paid to CMBS special servicers or that CMBS servicer compensation

[11] The Joint Parties also incorrectly argue that the special servicers are receiving some sort of double payment because "expense reimbursement provisions in the Loan Agreements (which include special serving fees) cover all of these incremental costs.") See Reply, p. 7, n.8. While more recent CMBS loans, such as the Goldman Portfolio Loan and Chateau Lake Loan, contain provisions that allow for the special servicing fee to be recovered from the borrower, older legacy CMBS loan agreements such as those that document the Barclays Portfolio Loan and the Nomura Portfolio Loan do not have such provisions.

is in any way subject to a reasonableness analysis under § 506(b) of the Bankruptcy Code.[12]

B. The fallacy of "Actual Harm." The Joint Parties also maintain that "actual harm" in an easily quantifiable amount must be shown in order for post-bankruptcy default interest to be allowable. This position is contrary to the case law which holds that default interest is presumptively allowable in an over-secured bankruptcy case, subject only to reduction for narrowly prescribed equitable considerations, none of which are present here. See Bowles Sub Parcel A, LLC, 792 F.3d 897, 902-03 (8th Cir. 2015); Southland Corporation v. Toronto Dominion (In re Southland), 160 F.3d 1054, 1059 (5th Cir. 1998); see also In re Terry Ltd. Partnership, 27 F.3d 241, 243 (7th Cir. 1994) ("What emerges from the post-Ron Pair decisions is a presumption in favor of the [default] contract rate subject to rebuttal based upon equitable considerations.") Other courts at the circuit court level do not even consider equitable considerations in a solvent debtor, full payment case. See, e.g., In re: Dow Corning Corp., 456 F. 3d 668, 679 (6th Cir. 2006) (holding that "courts generally confined themselves to determining and enforcing whatever pre-petition rights a given creditor has against the debtor" rather than considering "equitable considerations.")

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[12] The cases relied upon by the Joint Parties regarding reasonableness analysis under § 506(b) do not apply to the facts of this case. In In re Nicfur-Cruz Realty Corp., the amounts challenged for reasonableness under § 506(b) of the Bankruptcy Code were attorneys' fees, not default interest. See also In re Market Center E. Retail Prop., Inc., 433 B.R. 335, 357-58 (Bankr. D.N.M. 2010) (the "prepetition default interest claim and late fees are presumably enforceable under New Mexico law and should be allowed under section 502" and allowing postpetition default interest under the general presumption of validity where "the Court also finds no equitable reason not to allow this charge" because "allowance of the default rate will only impact the equity interests"). The Joint Parties' reliance on In re Vest, 217 B.R. 969 (Bankr. S.D.N.Y. 1998) is also misplaced. In that case, the court noted that the 5% default interest rate fell "within the range of reasonableness," but declined to enforce post-petition default interest because there was no record in the case of the debtor's solvency. Id. at 703-04. These bankruptcy estates are solvent, the secured creditors oversecured and all creditors promised payment in full under JDH's confirmed Chapter 11 plan.

None of the equitable considerations taken into account by the minority of bankruptcy courts in determining the allowability of post-petition default interest are present here: (i) creditor misconduct, (ii) adverse impact on unsecured creditors; (iii) the default rate constituting a penalty; and (iv) default interest jeopardizing the debtor's "fresh start". See, e.g., P.G. Realty, 220 B. R. 773, 780 (Bankr. E.D.N.Y. 1998). The CMBS Lenders engaged in no misconduct and none is alleged.[13] Payment of default interest cannot adversely impact other creditors in a "full-pay" case. The 33 cases cited by the CMBS Lenders in the Response and the Greenspan Declaration amply demonstrate that the 4% and 5% default interest rates at issue are not penalties. Finally, the default interest sought by the CMBS Lenders did not interfere with confirmation of the JDH Chapter 11 plan or the sale to JDH, so no "fresh start" was jeopardized by the CMBS Lenders' claims.

The Joint Parties go further and maintain that because the CMBS Lenders were oversecured during the pendency of these bankruptcy cases, full payment at some point in time was never really at risk and therefore the lenders were never "harmed." Under this line of thinking, default interest would never be payable to any oversecured mortgage lender in any bankruptcy case. Under § 506(b) of the Bankruptcy Code, in order to be paid post-bankruptcy interest, a secured creditor ***must*** be over-secured. By the Joint Parties' logic, oversecured creditors bear no risk of ultimate non-payment of their claims because of the equity cushion and therefore the oversecured creditors cannot be harmed.

[13] The Joint Parties assert that the CMBS Lenders "did nothing to expedite resolution of these cases" by failing to seek relief from stay or support a plan. This position is particularly unconvincing and ironic. JDH forced confirmation of its plan on a "full-pay," "unimpairment" basis that stripped creditors of plan voting rights. Accordingly, the plan did not need creditor support. Also, JDH's motion to dismiss and stay relief litigation, both of which were rejected by this Court, unnecessarily prolonged this case. Creditor support of these unsuccessful tactics would have added nothing to these cases. Had JDH not engaged in its misdirected and unsuccessful motion practice, this case would have moved to a sale or plan confirmation much sooner than it actually did.

Oversecured lenders therefore would never be entitled to default interest ever, under any circumstances. This rationale defies reason and is contrary to the controlling circuit court level case law cited above.

Further, though difficult to quantify in exact dollar terms, the harms visited upon the CMBS Lenders by the Debtors' bankruptcy filings are articulated in detail in the CMBS Lenders' Response to the Court's question no. 5 and in the Greenspan Declaration. See Greenspan Declaration, pp. 4-7, ¶¶ 9, 10. Without recounting all of these risks and harms in detail here, one of the most obvious examples is the lack of timely repayment of principal on the matured Nomura Portfolio Loan and Barclays Portfolio Loan. Principal was due on the Nomura Portfolio Loan in April of 2016 and on the Barclays Portfolio Loan in November of 2016. The underlying investors were harmed because, among other things, for about two years they were denied the ability to re-invest the returned principal due when the loans matured. They were only compensated during that period with payment of interest that was not market rate not upon maturity in 2016, but rather reflected the market in 2006 when the loans originated. That the nominal principal amount of the loans will ultimately be repaid at some future time through a bankruptcy plan does not negate the harms and losses visited upon the CMBS Lenders by the alteration of their rights caused by the Debtors' bankruptcies and detailed in the Response to question no. 5 and the Greenspan Declaration.

The Joint Parties also argue that these bankruptcy cases somehow benefitted the CMBS Lenders. Without citing legal authority, the Joint Parties state that somehow JDH's right of first refusal ("ROFR") agreement with some of the Debtors constitutes an interest in real property which primes the CMBS Lenders' consensual mortgage liens.

Again without benefit of legal authority or even a cursory factual explanation, the Joint Parties then maintain that bankruptcy cases somehow made the JDH's priming rights go away. These far-fetched assertion should be disregarded. JDH and the Debtors fought hammer and tong for a year and a half in these bankruptcy cases, deploying substantial legal resources in their attempts to dismiss the cases, obtain stay relief, move the disputes back to the Delaware courts, sell the hotels and confirm a plan. If JDH had the legal right to prime the CMBS Lenders' liens, it would have used its legal arsenal to assert those claims long, long ago. That they did not speaks volumes.

In contrast and as highlighted in the CMBS Lenders' Response to question no. 5 and the Greenspan Declaration, these bankruptcy cases have imposed very real costs, risks and uncertainties upon the CMBS Lenders. It is perhaps possible to imagine a bankruptcy that might benefit a secured creditor, but the Joint Parties can point to no specific or real benefits that these cases have brought to the CMBS Lenders.

C. <u>Ipso facto defaults are enforceable defaults</u>. The CMBS Lenders' claims are based upon real property mortgages which are not executory contracts under § 365 of the Bankruptcy Code and are therefore not subject to the *ipso facto* prohibitions contained in that code section. The plain language of § 365 of the Bankruptcy Code excludes non-executory contracts from the limitation on *ipso facto* clauses.[14] Courts, including those in the Tenth Circuit, view real property mortgages as non-executory under the Countryman definition of executory contracts. <u>See, e.g.</u>, <u>Thomas Am. Stone & Bldg., Inc. v. White</u>, 142 B.R. 449, 453 (D. Utah 1992) (seller of real property by purchase money loan secured by a deed of trust "fully performed its obligations under the

[14] This issue has already been extensively briefed by the CMBS Lenders. <u>See</u> <u>CMBS Lenders' Motion to Allow Oversecured CMBS Claims</u> p. 13-15 [Docket No. 2038.]

contract when it deeded the property to [buyer"]); see also In re N. Am. Dealer Grp., Inc., 16 B.R. 996, 1000 (Bankr. E.D.N.Y. 1982) (a "mortgage is not an executory contract which required an assumption or rejection by the trustee pursuant to Section 365(d) (1)"); In re EES Lambert Assocs., 62 B.R. 328, 336 (Bankr. N.D. Ill. 1986); In re Kash & Karry Wholesale, Inc., 28 B.R. 66, 69 (Bankr. D.S.C. 1982); H.R. Rep. No. 95–595, 95th Cong., 2d Sess. 347, reprinted in 1978 U.S. Code Cong. & Admin. News, pp. 5963, 6303–04 (a "note is not usually an executory contract if the only performance that remains is repayment").

In addition to the defaults caused by the filing of the Borrowers' Chapter 11 cases and the bankruptcy of the guarantor, the JQH Trust, two of the four CMBS Loans have gone into maturity default – the Nomura Portfolio Loan matured before bankruptcy on April 11, 2016 and the Barclays Portfolio Loan matured on November 1, 2016, about four months after these bankruptcies commenced. The Joint Parties do not appear to contest that these maturity defaults trigger liability for default interest.

6. Whether any other provision of each Loan Agreement already compensates for such bankruptcy-related risks and costs.

Response: The Joint Parties do not dispute the CMBS Lenders' response to question no. 6. As detailed in the response to question no. 5 above, the Joint Parties fallaciously state that default interest is solely compensation paid to CMBS special servicers, even though, as detailed above, such special servicer compensation is actually the last items paid under the distribution waterfall imposed by the controlling agreements.

7. Evidence of the *maturity*-related risks and costs for which default interest on a CMBS loan compensates.

Response: The only response provided by the Joint Parties in the Reply to question no. 7 is that default interest serves solely as compensation paid to CMBS Special Servicers. As recounted above in the response to question no. 5, default interest is actually first applied to make the securitization trust whole, with servicer compensation being the last item paid under the governing distribution waterfall. The Joint Parties further absurdly state that payment of default interest somehow prejudices *the Debtors* and would serve to discourage them from filing for bankruptcy. That argument does not apply in his case. The confirmed JDH Chapter 11 plan is a liquidating sale plan that leaves the Debtors with no post-confirmation operations, business or assets. Allowance of default interest has no bearing on the Debtors' fate under the confirmed plan.

The only party who will be benefitted by disallowance of the CMBS Lenders' default interest claims will be JDH who has already purchased the entire Hammons empire solely for the payment of debt – with no consideration paid for equity, enterprise value or goodwill. Payment of post-petition default interest, which JDH concedes is enforceable under state law, is the only way to prevent JDH, a sophisticated, big money East Coast hospitality investment group, from receiving an unearned, multi-million dollar windfall. If the Court were to rule to the contrary, all solvent borrowers would flock to bankruptcy court to rid themselves of default interest obligations rather than pay their lenders the contracted and legally-enforceable amount due. And, once again, no bankruptcy court has denied the payment of default interest in the 4%-5% range provided for here.

8. Whether any other provision of the Chateau Lake and Goldman Portfolio Loan Agreements already compensates for such maturity-related risks and costs.

Response: The only response provided by the Joint Parties in the Reply is that default interest serves solely compensation paid to CMBS special servicers which is incorrect. As recounted above in the response to question no. 5, default interest is not paid to loan servicers, but rather is paid to the lenders – the CMBS trusts which hold the loans and promissory notes. Additionally as stated above in the response to question no. 5, any default interest received is first applied to make the lender whole under the governing PSA. Special servicer compensation is actually the last items paid under the PSA's governing distribution waterfall to the extent that default interest is not exhausted making the trust whole.

9. Evidence of actual loss to the CMBS Lenders caused by the alleged ipso facto defaults by the Borrower and the JQH Trust on the Chateau Lake Loan.

Response: The Joint Parties state nothing beyond their reply to the CMBS Lenders' reply to question no. 5 above. Accordingly, the CMBS Lenders incorporate by reference their sur-reply to question no. 5 contained above.

10. Whether each of the fees, costs, and expenses claimed by the CMBS Lenders and disputed by JD Holdings is (a) supported by a Loan Agreement and (b) reasonable.

Response: In the Reply, the Joint Parties have requested detail regarding legal fees incurred by the CMBS Lenders since February 28, 2018 – the end of the period for which legal fees statements have been already been filed with the Court. Detail regarding post-petition Venable's legal fees incurred by the CMBS Lenders for the period from March 1, 2018 through July 31, 2018, in a format similar to that submitted in support of court-approved professional fee

applications, is attached hereto on a loan-by-loan basis as Exhibits B -E. The attached exhibits reflect only the amounts billed to the CMBS Lenders. Venable made material voluntary discounts to its legal fees for the time period covered by the exhibits in the following amounts – expressed as a percentage, the discounts average just below 12%: (i) Goldman Portfolio Loan discount -- $23,048.00; (ii) Chateau Lake Loan discount -- $23,163.50; (iii) Barclays Portfolio Loan discount -- $20,998.00; and (iv) Nomura Portfolio Loan discount -- $20,863.00. The CMBS Lenders submit that such fees are reasonable in light of the services rendered, the nature and scope of the issues in the case and the amounts at issue for the CMBS Lenders.[15]

11. Whether the JQH Trust is liable for the Disputed Claims as a guarantor for each Borrower under each Loan Agreement.

Response: The Joint Parties reading of the Chateau Lake Guaranty is simply incorrect – the document is clearly a full recourse guaranty under the clear language of the document. The Nomura Guaranty is similarly a recourse guaranty, however one that is subject to a $25 million liability cap. The following paragraphs analyze the specific language of the guaranties in question.

A. The Chateau Lake Guaranty. The language of the Chateau Lake Guaranty is quite clear and broad in its application, stating that the JQH Trust is liable for all "Full Recourse Liabilities":

1. Indemnity and Guaranty.

> (a) **Guarantor hereby assumes liability for**, hereby absolutely and unconditionally guarantees payment to Lender of, hereby agrees to pay, protect, defend and save Lender harmless from and against, and hereby indemnifies Lender from and against (i) **the Full Recourse Liabilities (as defined in the Loan Agreement)** and any and all Guaranteed Costs (as defined in the Loan Agreement) incurred, suffered or sustained by Lender

[15] The CMBS Lenders reserve the right to file a further supplemental pleading documenting the legal fees of their Kansas City counsel, Lathrop & Gage, LLP.

> pursuant to Article V of the Loan Agreement, and (ii) any and all Guaranteed Costs incurred, suffered or sustained by Lender due to a violation of this Agreement. (*Emphasis added*. Chateau Lake Guaranty, p. 2).

The Loan Agreement for its part states that the filing of a voluntary bankruptcy is an event that renders the entire loan a "Full Recourse Liability" for which the JQH Trust guarantor is liable:

> 5.2 Full Recourse Liability.
>
> (b) Notwithstanding anything to the contrary in Section 5.1 above or otherwise in the Loan Documents, **in the event that:…(E) any petition for bankruptcy, insolvency, dissolution, liquidation, reorganization or arrangement pursuant to the Bankruptcy Code**, any other federal or state bankruptcy or insolvency law, or any similar federal or state law**, shall be filed, consented to or acquiesced in by Borrower or any Guarantor** or any SPC Entity, or Borrower or any Guarantor or any SPC Entity seeks (or consents to, or acquiesces in) the appointment of a receiver, liquidator or trustee, or any proceeding for the dissolution or liquidation of Borrower or any Guarantor or any SPC Entity shall be instituted or consented to, or acquiesced in by Borrower or any Guarantor or any SPC Entity (in each case, other than at the direction or request of Lender);… **((A) through (0) collectively being the "Full Recourse Liabilities")**, **then the Loan shall be fully recourse to Borrower**. (*Emphasis added*. Chateau Lake Loan Agreement, p. 92-93).

The Joint Parties mis-read these industry-standard documents. The Joint Parties assert that § 5.2 of the Chateau Lake Loan Agreement does not state that the recourse triggers found in that provision cause "full recourse of the entire loan." Quite to the contrary, the provisions from the loan agreement in bold above clearly state that: (i) the filing of a voluntary petition in bankruptcy by either the Chateau Lake Borrower or the JQH Trust guarantor trigger the "Full Recourse Liability" defined term used in the Chateau Lake Guaranty, and (ii) occurrence of such a Full Recourse Liability

trigger ***renders the entire loan a full recourse obligation.*** Under the language of the Chateau Lake Guaranty quoted above, the JQH Trust has guaranteed all such "Full Recourse Liabilities." Further, the guarantor is not a party to the Chateau Lake Loan Agreement – only the lender and borrower are. The failure of Section 5.2 of the Chateau Lake Loan Agreement to include the words "and the Guarantor" at the end of the operative sentence does not re-write or negate the clear language of the Chateau Lake Guarantee that obligates the JQH Trust to pay all amounts due under the loan in the event of a voluntary bankruptcy.

B. The Nomura Guaranty. As described in the Response, the Nomura Guaranty is not a full recourse guaranty, but rather is a limited guaranty document that requires the JQH Trust to pay certain "Guaranteed Obligations" to the lender when they come due.[16] Nomura Guaranty, § 1.1. The document defines "Guaranteed Obligations" to be

(i) prompt payment by the Nomura Borrower of the loan, (ii) prompt payment of all accrued and unpaid interest on the loan, and (iii) the reasonable legal fees and expenses incurred by the lender in enforcing the Nomura Borrower's obligations or the obligations of the JQH Trust guarantor. Nomura Guaranty, § 1.2. Under § 1.3 of the Nomura Guaranty, the JQH Trust's guaranty obligations are not triggered by any so-called "bad-boy" events, but rather are expressly exempted from any non-recourse exculpation provisions of the governing loan agreement ("No exculpatory language contained in any of the other Loan Documents shall in any event or under any

[16] The governing Limited Payment Guaranty dated March 30, 2016 (the "Nomura Guaranty"), was correctly described in the Response. However, a different, companion guaranty that addressed specific issues at a hotel in New Mexico was inadvertently exhibited to the Response instead of the correct Nomura Guaranty. A copy of the Nomura Guaranty is attached hereto as Exhibit F.

circumstances modify, qualify or affect the personal resource obligations and liabilities of Guarantor hereunder.")[17] The Nomura Guaranty also imposes a cap of $25 million on the guaranty liability of the JQH Trust. See Nomura Guaranty § 6.19.

12. Whether post-petition interest is an allowable unsecured claim against the JQH Trust as an alleged guarantor of the Loans.

Response: As stated in the Response, the JQH Trust is obligated to pay all guaranteed obligations of the Borrowers, including post-petition interest owed by the Borrowers under the unambiguous language of the guaranty documents. The only exception to this is the Nomura Guaranty, which as described above is subject to a $25 million liability cap. The Joint Parties cite no case law to the contrary in their Reply to question no. 12. Guarantors remain fully liable regardless of the collectability or discharge of the underlying borrower's obligations. In re Gentry, 807 F.3d 1222, 1227 (10th Cir. 2015).

The Joint Parties maintain that § 506(b) of the Bankruptcy Code bars collection on account of the guaranty claims because the JQH Trust is not a "surplus" estate. This is certainly different from the promise of full payment upon which the JDH Chapter 11 plan is premised. It is also contrary to JDH's agreement to subordinate its $500 million claim to all other creditors – the guaranty claims held by the CMBS Lenders certainly belong to the group of creditors who are superior in distribution priority to JDH's claim. The

[17] JDH's own citations belie their argument. Courts do not recognize any specific language necessary to render an obligation recourse, and instead simply look to the plain language of the agreement. Blue Hills Office Park LLC v. JP Morgan Chase Bank, 477 F.Supp.2d 366, 380-81 (D. Mass. 2007) (explaining that "the plain language of the contract governs" interpretation and finding that guarantor liability was triggered upon "[t]he occurrences of the events described, by the express terms of the guaranty"). Contrary to JDH's claim, the broad exemption from non-recourse exculpations in the Nomura Guaranty are typical of modern commercial guarantees. See John C. Murray & Randall L. Scott, Enforceability of Carve Outs to Nonrecourse Loans: An Evolution, 48 Real Prop. Trust & Estate L. J. 2013, at 218 (recognizing that "[u]nder the most recent case law . . . the exceptions [to nonrecourse provisions] have virtually swallowed the rule; that is the clause is drafted so that the borrower has liability for virtually all defaults except the failure to pay principal and interest due on the loan").

record built in this case at plan confirmation shows that ample resources exist to fully pay all amounts due on the CMBS Lenders' claims whether they are paid on account of the claims against the Borrowers or the JQH Trust. Furthermore, although the default interest provisions of the CMBS lenders' claims are enforceable under state law and bankruptcy law, guarantor liability survives disallowance of the underlying claim against the primary obligor. In re Modern Textile, Inc., 900 F.2d 1184, 1191 (8th Cir. 1990) (holding that the cap on lease damages claims imposed by § 502(b)(6) does not serve as a cap on lease guarantees); see also Things Remembered, Inc. v. BGTV, Inc., 151 B.R. 827, 831 (Bankr. N.D. Ohio 1993.)

Additionally, the cases cited by the Joint Parties that stand for the proposition that simultaneously filed bankruptcy cases are "protected" against *ipso facto* defaults triggered by the other debtor's bankruptcy case does not apply to the CMBS Lenders' claims. The cases relied upon by the Joint Parties involve executory contracts that are governed by the anti-*ipso facto* provisions of § 365(e) of the Bankruptcy Code. See, e.g., In re Lehman Brothers Holdings, Inc., 422 B.R. 407 (Bankr. S.D.N.Y. 2010). As described above in the sur-reply to question no. 5, the mortgages held by the CMBS Lenders and the accompanying guaranties are not executory contracts and are therefore not subject to the *ipso facto* prohibitions of § 365(e). As detailed in the Response,[18] the filing of the JQH Trust Chapter 11 case was as much a default under the CMBS loan documents as the filings of the Borrowers themselves.

13. Whether the CMBS Lenders' claims for yield maintenance (and the joint objections thereto) are ripe for decision, given that the Borrowers and JD Holdings

[18] See Response to question 4, pp. 6-7.

currently intend to cure, reinstate, and assume the unmatured loans rather than prepay them.

Response: The loan assumption process has gone far enough with both the Goldman Portfolio Loan and the Chateau Lake loan that the major stumbling block to forward progress is JDH's unwillingness to pay the default interest due on the loans due to the default caused by the bankruptcies. Whether JDH first proceeds with reinstatement under § 1124 of the Bankruptcy Code or assumption under the terms of the operative loan agreements, the loan must be reinstated or assumed in conformity with all of the terms of the governing documents – not a single comma can be moved without the lenders' agreement. With regard to a Bankruptcy Code reinstatement, the law is clear that default interest – which the Joint Parties agree is enforceable – must be paid. See In re K & J Props., Inc., 338 B.R. 450, 461 (Bankr. D. Colo. 2005) (noting that "Section 1123(a)(5)(G) and section 1124(2) provide no basis to nullify the post-petition default interest claimed by [creditor] to the extent it is otherwise allowable under [creditor]'s loan documents and applicable nonbankruptcy law"); In re Sweet, 369 B.R. 644, 650-51 (Bankr. D. Colo. 2007) (requiring payment of interest at the contract default rate to effect cure under section 1124(2)); accord In re Consolidated Operating Partners L.P., 91 B.R. 113, 117 (Bankr. D. Colo. 1988). The same result is required if the loans are assumed, not under the Bankruptcy Code, but pursuant to the loan assumption provisions of the controlling documents. See, e.g. 131 Heartland Blvd. Corp. v. C.J. Jon Corp., 82 A.D. 3d 1188, 1189 (N.Y. Sup. Ct., App. Div. 2011) (recognizing, as a fundamental principle of commercial contract interpretation under New York law, that "[t]he court's role is limited to interpretation and enforcement of the terms agreed to by the parties, and the court may

not rewrite the contract or impose additional terms which the parties failed to insert"); BACM 2001-1 San Felipe Road Ltd. P'ship v. Trafalgar Hldgs. I, Ltd., 218 S.W.3d 137, 147 (Tex. Ct. App. 2007) (borrowers' liability for late fees and default interest on a commercial loan were not altered where "these past and future penalties are part of the original Loan Documents").

JDH has provided virtually all of the materials needed by the CMBS Lenders to complete their underwriting and assumption analysis. JDH has also paid one of the servicers the required $40,000 deposit intended to cover the lender's assumption-related expenses including legal fees. Obviously, abundant resources have been committed to the assumption process.

In contrast to the work that has been done with regard to assumption, JDH has done almost nothing to attempt to pre-pay the unmatured CMBS loans. At no time has JDH ever tendered payment on the unmatured loans. Accordingly, any pre-payment is at this point merely a theoretical possibility. Under Tenth Circuit precedent, claims must be ripe prior to judicial determination in order to avoid entangling courts in fruitless "abstract disagreements." Morgan v. McCotter, 365 F.3d 882, 890 (10th Cir. 2004.) To determine if a dispute is ripe for consideration, a court must determine if the dispute involves "uncertain events" that "may never happen at all." Skull Valley Band of Goshute Indians v. Nielson, 376 F.3d 1223, 1237 (10th Cir. 2004.) JDH's plan was confirmed over three months ago. Since that time, they have not attempted to tender early payment of the unmatured CMBS Loans. Given this lack of effort, prepayment is clearly an "event that may never happen at all" which is not ripe for adjudication at this time. The cases cited by JDH are inapposite – the cases address unique harms in the

context of federal preemption and do not justify a departure from the typical ripeness analysis in this case. See U.S. v. Supreme Court of N.M., 839 F.3d 888, 903-04 (10th Cir. 2016) (finding a "cognizable issue" ripe for determination "in the absence of a pending state enforcement action" where "that federal prosecutors need not risk disbarment by violating the [Ethics] Rules in order to challenge those rules in federal court"); Skull Valley Band of Goshute Indians, 367 F.3d at 1239 (noting that "[t]he preemptive effect of federal law may be apparent from the text of the statute" and recognizing specific "hardship that would be imposed if a judicial decision were delayed" in nuclear regulatory cases).

If the yield maintenance issue were ripe for adjudication, however, make-whole premiums are enforceable under state law.[19] See In re Madison 92nd St. Assocs. LLC, 472 B.R. 189, 195 (Bankr. S.D.N.Y. 2012) ("Prepayment premiums are generally enforceable under the New York common law 'rule of perfect tender in time.' This rule prohibits the prepayment of the loan under the rationale that the lender has the absolute right to receive the bargained for income stream over the life of the loan."); Dubinsky v. Chem. Bank, 748 S.W.2d 957 (Mo. Ct. App. 1988) (enforcing prepayment premium pursuant to plain terms of loan agreement); Arend v. Great Southern Sav. & Loan Ass'n, 611 S.W.2d 381 (Mo. Ct. App. 1981) (enforcing prepayment premium provision in commercial loan). Also, Courts routinely enforce yield maintenance provisions in the context of CMBS lending. See LaSalle Bank Nat'l Ass'n v. Sleutel, 289 F.3d 837, 843 (5th Cir. 2002) (concluding that "prepayment consideration by [guarantor] is due under the terms of the [CMBS] Note"); Norwest Bank Minn. V. Blair Road Assocs., L.P., 252

[19] This issue has been fully briefed by the CMBS Lenders. See CMBS Lenders' Response to Joint Objections to Proofs of Claim Related to Chateau Lake Loan and Goldman Portfolio Loan [Docket No. 2179.]

F. Supp. 2d 86, 96 (D.N.J. 2003) (recognizing in a CMBS lending context under New Jersey law that "a prepayment premium is enforceable…so long as the loan documents clearly provide for the premium"); U.S. Bank Nat'l Assoc. v. Kontogiannis, No. 13-1090, 2013 WL 12108071, at *3 (E.D.N.Y. 2013) (finding "clear and unambiguous" prepayment penalty in CMBS loan enforceable under New York law); Bear Creek Partners II, LLC v. Deutsche Bank Trust Co. Americas, No. 14-309, 2016 WL 7626239 (W.D. Mich. 2016) at *6 (finding yield maintenance provisions to be enforceable under New York law) (citing In re United Merch. & Mfrs., Inc., 674 F.2d 134, 143 (2d Cir. 1982)).

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Respectfully Submitted,

/s/Frederick W. H. Carter

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