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SARE

For the final chapter, we turn to a reexamination of a controversy and debate that has raged since the Code was enacted in 1978: the treatment of single asset real estate cases (SARE). The heart of the debate is how and why — if at all — single asset cases should be dealt with in chapter 11. The crux of the issue is that SARE cases are essentially nothing more than two-party disputes between the secured lender and the debtor. The debtor is typically invoking chapter 11 as a way to forestall foreclosure. Is that sufficient to merit the intervention of the federal bankruptcy laws? What bankruptcy policy dictates interfering with state foreclosure laws — when no "greater good" is to be found? In the first article in Chapter 7, "Time to Exclude SARE Cases from a Reformed Chapter 11," the author finds such justification wholly lacking and recommends excluding SARE cases from chapter 11. He notes that many of the difficult legal issues under chapter 11 involve SARE cases, and he sees no reason to keep trying to fit the square SARE peg into the round chapter 11 hole. The second article, "'Single Asset Real Estate': A Concept in Need of Redefinition," also looks at the reform of SARE cases. The authors in that article do not suggest excluding SARE cases from chapter 11, but they do recommend a variety of ways in which the SARE concept could and should be redefined to better serve the purposes of chapter 11. As ABI concludes its massive study of chapter 11, it is entirely appropriate to continue studying the usage and function of that chapter as a matter of first principles.

A. Time to Exclude SARE Cases from a Reformed Chapter 11

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Major bankruptcy reforms have occurred every 40 years — in 1898, 1938 and 1978 — and if this history is any guide, a new one may be expected soon. Any reform effort should ask basic questions, and this article focuses on whether single-asset real estate cases (SAREs) belong in chapter 11.

For this article, as in virtually all SARE cases, the SARE has (1) significant debt secured by the property, rents and profits (typically, the SARE's secured debt is greater than or close to the fair market value of the property), and (2) minimal unsecured debt (usually 1 percent or less of the secured debt). Substantially all of a SARE property's income comes from operating the property, but SARE property might be an apartment complex, office building or land held for sale. For this purpose, I exclude entities that have generally held to be outside of the SARE definition, such as hotels or golf courses.[1]

SAREs do not belong in chapter 11 because chapter 11 is intended to preserve going-concern value that would be lost in liquidation and to protect the rights of creditors. SARE is simply a contest between the secured lender and the property-owning debtor in which the debtor seeks to preserve its equity interest by using the tools of bankruptcy to reduce the lender's secured debt. Ultimately, such cases do not accomplish any significant social or policy benefit, unless reducing the lender's claims and transferring value to the debtor is considered such a benefit. Not surprisingly, many of the cases reaching the U.S. Supreme Court and courts of appeals dealing with chapter 11 plan issues are efforts by SARE debtors to use the tools of bankruptcy to preserve their equity interests.

These purposes are not applicable to a SARE. The value of a SARE property is essentially the economic value of the real estate, and little or no going concern value will be lost by an outright sale or transfer of the asset. The economic

1 *See* 2 *Collier on Bankruptcy* ¶ 101.51B (Alan N. Resnick and Henry J. Sommer eds., 16th ed.).

interests of unsecured creditors are minimal (and competing secured creditors have protections under state foreclosure law), so not surprisingly, a creditors' committee is rarely appointed in a SARE case. It is hard to justify the expense of chapter 11 and the work involved in that the debtor is dealing with nominal amounts of unsecured debt, as well as service providers and employees who are likely to follow the asset into new hands. In addition, the asset itself is not at risk, since no one is going to move the real estate. Chapter 11 has never been justified as a mechanism to transfer value from creditors to the debtors.[2]

How Is Chapter 11 Used in a SARE Case?

The typical SARE case is a dispute between the lender and debtor. The debtor cannot pay its secured debt under the terms and conditions of its loan and needs more time, lower payments, lower interest rate, reduced principal and/or different terms; put simply, it needs a loan modification. If the lender agrees to these terms, chapter 11 is not needed, so SARE cases are filed when a consensual arrangement cannot be reached.

If the debtor is required by bankruptcy law to pay the full value of the lender's entitlement, there will be no reason for the debtor to file. In SARE cases, the debtor seeks to use the tools of bankruptcy to accomplish a loan modification over the lender's objection. In simple terms, filing a SARE case reduces the lender's entitlement and transfers the value of that reduction to the debtor. Such a transfer inherently violates principles of absolute priority and lacks support in bankruptcy policy.

In a SARE case, the debtor seeks to accomplish the loan modification by confirming a plan in the face of various statutory obstacles. Historically, SAREs have become somewhat of a game, with debtors trying various possibilities and, rather consistently, being thwarted by the Supreme Court and courts of appeals — but not always, not quickly and not really ever. For one thing, the automatic stay stops the lender from exercising foreclosure remedies, and the Supreme Court has held that while the case is going forward, the undersecured debtor is

2 *See* Report of the National Review Commission, 661-63 (Oct. 20, 1997); *see also In re RYYZ LLC*, 490 B.R. 29, 34 (Bankr. E.D.N.Y. 2013) (SAREs are typically little more than a contest between debtor and secured lender, and trying to confirm is often "fool's errand"); *In re JER/Jameson Mezz Borrower II LLC*, 461 B.R. 293, 303 (Bankr. D. Del. 2011) (filing on eve of foreclosure; two-party dispute; case will not realize value not available outside of bankruptcy).

not required to pay interest to the lender (even on the "secured" portion of the debt).[3] The obstacles themselves are briefly discussed in this article, but there is just enough play in the joints to give the debtor a fighting chance of accomplishing its goal or, at least, coming close enough so that the lender decides to compromise. The transfer of value is thus accomplished.

As previously stated, a SARE case usually involves a lender whose debt exceeds the value of the collateral (the property), which bankruptcy law treats as a secured claim up to the value and an unsecured claim for the deficiency. To retain equity over the lender's objection, the debtor must (1) cram down the secured debt to the value of the property, on terms that it can service; (2) cram down the deficiency claim; and (3) obtain at least one accepting impaired class of creditors. How does it do these things?

Cramdown of Secured Debt

To cram down the secured debt, the debtor has three options: (1) a sale with the lender in which it is permitted to credit-bid; (2) payment of the secured claim with interest; or (3) the provision of the "indubitable equivalent."[4] Debtors have initially tried to satisfy the second option by proposing to cram down the debt at an appraised value and using their exclusivity period to prevent the lender from proposing an alternative. The Supreme Court ultimately stopped this tactic by holding that a debtor's exclusive right to propose a plan is value-protected by the absolute priority rule and that in such situations, a market test (not appraisals) is required.[5] Thereafter, debtors have tried to satisfy the first option by providing for a sale without credit-bidding.[6] Although such plans do not comply with the first two options, debtors allege that they are providing the "indubitable equivalent" of the secured claim, and several courts of appeals have agreed.[7] Ultimately, the Supreme Court held that when the debtor uses a cramdown method within the first or second option, it is required to comply with the conditions of those provisions, providing that the "indubitable equivalent" is not available as another option.[8]

3 *United Sav. Ass'n of Tex. v. Timbers of Inwood Forest Assocs.*, 484 U.S. 365, 378-79 (1988).

4 *See* 11 U.S.C. § 1129(b)(2)(A).

5 *Bank of Am. Nat'l Trust & Sav. Ass'n v. 203 N. LaSalle Street P'Ship*, 526 U.S. 434, 454-58 (1999).

6 *RadLAX Gateway Hotel LLC. v. Amalgamated Bank*, 132 S. Ct. 2065, 2070 (2012).

7 *See, e.g., In re Philadelphia Newspapers LLC*, 599 F.3d 298, 305-09 (3d Cir. 2010); *In re Pac. Lumber Co.*, 584 F.3d 229, 245-47 (5th Cir. 2009).

8 *In re River E. Plaza LLC*, 669 F.3d 826, 829-34 (7th Cir. 2012).

In most cases, the debtor will use the second option by proposing a plan with some combination of a "below-market" interest rate, maturity extension and sometimes a balloon payment of a substantial portion of the principal. Debtors have been aided in such efforts by the Supreme Court's decision in *Till v. SCS Credit Corp.* that where there is no "efficient market" for bankruptcy financing, the court should use a prime-plus risk factor for cramdown interest.[9] Although *Till* was a chapter 13 case, it has been widely applied in SARE cases to cram down secured loans at interest rates far below those in the credit agreement or market rates. In this way, the chapter 11 process transfers value to the debtor and enables the debtor to retain its equity interest.

Cramdown of a Deficiency Claim

In most cases, the lender has a deficiency claim that dwarfs other unsecured claims. If the lender does not agree to the treatment of its deficiency claim, the debtor must cram down the claim. However, in this instance, the debtor runs into the requirement that there must be at least one accepting impaired class to confirm a plan. Yet, if the lender's deficiency claim and other unsecured claims are in the same class, that class will not accept the plan. The debtor must (1) seek to classify the deficiency claim separately from other unsecured creditors, (2) have the class of general unsecured creditors accept the plan and (3) cram down the class of deficiency claims.

In a SARE case, the unsecured creditors other than the lender's deficiency claim are usually trade creditors, employees, contractors and utilities, but since these creditors are often timely paid, their claims are generally small. At present, the law on separate classification of similar claims with the same legal entitlement is, to say the least, neither well-defined nor consistent. Some courts have held that separate classification of legally similar claims is not permitted, and others have essentially held that any explanation is acceptable, while still others have only winked at the issue.[10] Courts have also split on whether, in

9 541 U.S. 465, 479-80 (2004); *see also, e.g., In re Tex. Grand Prairie Hotel Realty LLC*, 710 F.3d 324, 330-37 (5th Cir. 2013) (5 percent rate allowed under *Till*); *In re Marble Cliff Crossing Apartments LLC*, 486 B.R. 887, 895 (Bankr. S.D. Ohio 2013) (2.85 percent too low; almost no equity; 32-year payout); *In re GAC El Monte*, 489 B.R. 747, 761-64 (Bankr. N.D. Ill. 2013) (4.9 percent too low; 8.6 percent acceptable; 97 percent financing).

10 *See* 7 *Collier on Bankruptcy* ¶¶ 1122.03[1][a], 1122.03[3][a] (Alan N. Resnick and Henry J. Sommer eds., 16th ed.).

order to constitute an impaired class, there must be more than minimum impairment (*e.g.*, a delay of a few months or no interest) and whether the debtor must be unable to pay its creditors in full.[11] A third issue is whether, in the event of separate classification and different treatment, the treatment of the impaired class "discriminate[s] unfairly" and thereby violates § 1129(b). Some debtors try to satisfy this test by proposing minimum payments (*e.g.*, 5 percent) and arguing some version of necessity, or by paying the deficiency claim over a long period of time, but again, court treatment has been uneven.[12]

What one observes from such cases is that the fight is between the debtor and the lender, and the affected creditors have not appeared and do not care because the stakes are too small. Rather, the impairment and treatment of unsecured creditors only matter insofar as they enable the debtor to confirm a plan modifying the lender's rights and allowing the debtor to retain its equity interests. Thus, although those rules were designed to protect unsecured creditors, in a SARE case they become a mechanism to give the debtor leverage against the lender.

Once the classification and one accepting class's requirements are satisfied, it becomes necessary to cram down the remaining unsecured class containing the deficiency claim. This is tricky because under § 1129(b)(2)(B), equity may not retain any value on account of its equity interest. Debtors will sometimes try to use the so-called "new value" rule, which, although of somewhat dubious pedigree, permits the debtor to provide new value and argue that it is obtaining an equity interest by virtue of the new value and not its old equity interest. Legal issues abound, including whether the new-value rule applies under the Bankruptcy Code, and if so, what the conditions are for its application (*i.e.*, arguably, there must be a need for funds for future operations and not to pay claims in order to satisfy the absolute priority rule), how much is required, and whether, under *LaSalle*, there must be a competitive opportunity to provide the funds.[13] However, in a SARE case, the new-value rule is simply a construct to permit the debtor to retain equity. If the debtor truly has a need for funds for future operations and/or

11 *See In re Vill. at Camp Bowie I LP*, 710 F.3d 239, 244-48 (5th Cir. 2013) (artificial impairment allowed); *Fed. Nat. Mortg. Ass'n v. Vill. Green I GP*, 483 B.R. 807, 815-17 (W.D. Tenn. 2012) (reviewing authorities); *In re Swartville LLC*, No. 11-08676-8-SWH, 2012 WL 3564171 at *6 (Bankr. E.D.N.C. 2012) (artificial impairment is bad faith); *In re All Land Invs. LLC*, 468 B.R. 676, 689-92 (Bankr. D. Del. 2012) (no valid reason for impairing class; votes disqualified).

12 *See* 7 *Collier on Bankruptcy* ¶¶ 1129.03[3][a], 1129.03[b][1-3] (Alan N. Resnick and Henry J. Sommer eds., 16th ed.).

13 *See In re Castleton Plaza LP*, 707 F.3d 832, 822-24 (7th Cir. 2013) (new value provided by debtor's wife; competitive bidding required; case illustrates SARE issues raised in text).

to maintain value, it would look to the lender, but usually the debtor's approach is simple: How much can the debtor "get away with" to keep its equity?

Existing SARE Provisions

Many of these issues are not new, and various Bankruptcy Code provisions attempt to deal with some of them, but these provisions are imperfect and do not strike at the heart of the problem, which is that SARE cases do not belong in chapter 11. Instead, the Code provisions adopt a litigation approach to the most contentious issues. For example, under § 362(d)(3), the debtor has 90 days to begin making payments on the value of the collateral, which may be made from rents (here, disputed issue of valuation) or file a plan that has a "reasonable possibility of being confirmed within a reasonable time" (which might mean two confirmation hearings). The payment option often does no more than give the lender cash collateral to which it would be entitled under § 363, and then there is no deadline for confirming a plan. The plan-filing option adds a layer of litigation and permits the debtor to file a plan that raises the issues that were discussed earlier.[14]

In short, the SARE provisions almost encourage the debtor to take a stab at retaining value, while at the same time they impose costs on the lender that are not likely to be recovered. Indeed, the SARE provisions reinforce the notion that the contest is — and always has been — between the lender and the debtor over who is going to own the equity.

Conclusion

SARE cases inherently involve a contest between a lender and debtor. The policies and purposes of chapter 11 are not implicated because there is almost always no significant unsecured debt, no going-concern value and no other social purpose. In SARE cases, chapter 11 gives the debtor the full panoply of rules and procedures to extract value from the lender and retain all or some of its equity. Bankruptcy law was never intended for this purpose; therefore, SARE cases should not be covered by chapter 11.

14 *In re RYYZ*, 490 B.R. at 35-45 (illustrating lengthy and costly litigation over the tools of bankruptcy to take advantage of § 362(d)(3)); *In re RIM Development LLC*, 448 B.R. 280, 288-92 (Bankr. D. Kan. 2010) (same).

B. "Single Asset Real Estate": A Concept in Need of Redefinition

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Almost two decades ago, the Bankruptcy Code was amended to include special treatment for single asset real estate (SARE) debtors. In 2005, the Bankruptcy Code was once again amended to eliminate the $4 million debt limitation on SARE cases, so the special treatment thereafter applied to *all* SARE debtors who met the SARE test, not just small- and medium-sized property owners. In both instances, the purpose of the amendments was to make available expedited relief to secured creditors in SARE cases that are not likely to result in confirmed reorganization plans.[1]

When the current global economic downturn started in 2008, the SARE provisions of the Bankruptcy Code were somewhat untested by market participants, primarily because there had been many years of prosperity in various segments of the U.S. economy, especially in commercial real estate. What we did not know in 2008, we certainly know now: A key battleground in this downturn has been in the area of commercial real estate.

The Congressional Oversight Panel has estimated that more than *$1.4 trillion* in commercial real estate debt will mature between 2010 and 2014.[2] As a direct result of these maturities and declining real estate values, many areas of the country have been awash in commercial real estate workouts, restructurings and liquidations. While our experience suggests that most of these problems have been handled outside of the bankruptcy environment, hundreds of real estate projects of all kinds and sizes have ended up in chapter 11.

1 *See* H.R. Rep. No. 103-835, at 50 (1994), *reprinted in* 1994 U.S.C.C.A.N. 3340, 3359; H.R. Rep. No. 109-31, at 140-41 (2005), *reprinted in* 2005 U.S.C.C.A.N. 88, 199-200.

2 Congressional Oversight Panel, *February Oversight Report: Commercial Real Estate Losses and the Risk to Financial Stability* at 2 (2010) (Feb. 10, 2010), available at www.gpo.gov/fdsys/pkg/CPRT-111JPRT54785/pdf/CPRT-111JPRT54785.pdf.

Thus, we are several years into testing the SARE provisions in bankruptcy litigation. As discussed above, the clear policy goal of this legislation was to allow secured creditors in SARE cases to be able to obtain expedited stay relief pursuant to § 362(d)(3). It is clear that the SARE provisions have failed to meet this goal. Many SARE cases languish in court for months, merely because a debtor has filed a plan, irrespective of whether the plan stands a reasonable prospect of being confirmed. Debtors often do not come to the table with new money in underwater real estate deals, or months pass with promises, but not commitments, that new money will be obtained. We understand why the dynamic works as it does: A debtor or investor would not normally want to invest substantial sums on an underwater project until the issue of "who wins" in chapter 11 plays out. The fundamental problem in SARE cases, which relates back to the congressional goal of moving SARE cases along, is not significantly different from a problem that many pundits have identified in the residential real estate arena. The process of "clearing" underwater properties — whether they are residential or commercial — is slow and expensive, and uncertainty about where the market is going results in a transactional burden on American commerce. The faster that the chapter 11 "winner" can be determined (within reason) in a SARE case, the faster that the real estate can be made available to the market for development or improved management at a reset value.

We (the authors) represent both debtors and secured creditors on a regular basis — both in chapter 11, when this issue is directly relevant, and in out-of-court restructurings, when it is in the background. Therefore, we do not seek to push the Bankruptcy Code in favor of one side or the other; rather, we are simply trying to "build a better mousetrap" than the current SARE provisions provide. Although we recognize that other improvements are possible, the focus in this article is on the threshold question of whether the SARE requirements apply at all.

The Current Statute

Debtors have dual incentives to argue that the SARE provisions do not apply to their cases. As in most bankruptcies, time and money are critical. A SARE debtor would prefer not to pay interest or file a plan early in a chapter 11 case, but that is the practical and direct consequence of an admission or a judicial determination that a debtor's property is SARE.[3] This leads us to § 101(51B)

3 *See* 11 U.S.C. § 362(d)(3). The authors refer to the adequate-protection payments required by this section as "interest" for the sake of simplicity.

of the Bankruptcy Code, which contains the now-well-worn definition of what constitutes SARE:

> The term "single asset real estate" means real property constituting a single property or project, other than residential real property with fewer than [four] residential units, which generates substantially all of the gross income of a debtor who is not a family farmer and on which no substantial business is being conducted by a debtor other than the business of operating the real property and activities incidental thereto.

To meet their clients' goal of preserving cash and creating a longer breathing spell, debtors' counsel have regularly and justifiably tested this definition in bankruptcy court. Much litigation has turned on whether particular real estate holdings represent "a single property or project." For example, if a debtor has only a single property but is part of a corporate family with other operations, do the SARE provisions apply?[4] What if a debtor leases all of its properties to affiliates?[5] Is the result different if the debtor leases *most* of its properties to affiliates but has one or more unoccupied parcels?[6] Another fertile ground for controversy is whether a debtor's operations represent "substantial business … other than the business of operating the real property and activities incidental thereto."[7]

Litigation over the SARE definition can involve considerable expense and delay. In our experience, delay is related more to a debtor's hope that the market will rebound than to a true need for time to raise cash to implement a confirmable plan. It also has been our experience that a typical SARE case is straightforward enough that a debtor and its principals should not require several months to raise money — assuming that the project is viable — unlike cases that involve debtors with complex business operations and capital structures.

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4 *See In re Meruelo Maddux Properties Inc.*, 667 F.3d 1072, 1077 (9th Cir. 2012) (SARE).

5 *See In re JJMM International Corp.*, 467 B.R. 275, 278 (Bankr. E.D.N.Y. 2012) (SARE).

6 *See In re Hassen Imports Partnership*, 466 B.R. 492, 510 (Bankr. C.D. Cal. 2012) (not SARE). *See generally In re The McGreals*, 201 B.R. 736, 743 (Bankr. E.D. Pa. 1996) (not SARE where debtor had leased one parcel to third party and adjacent parcel was undeveloped).

7 *Compare In re Scotia Pacific Co. LLC*, 508 F.3d 214, 224-25 (5th Cir. 2007) (timberland owned by debtor that managed property and sold timber was not SARE), *with In re Kara Homes Inc.*, 363 B.R. 399, 405-06 (Bankr. D.N.J. 2007) (property of debtor that planned, constructed, marketed and sold homes was SARE).

Against this backdrop, we suggest revisions to the definition of what constitutes SARE that should help debtors and creditors avoid threshold disputes and move forward to the merits of their chapter 11 cases (in those cases that truly should be in chapter 11). A clear delineation of cases that may move forward on a normal chapter 11 path and those that will face early deadlines may also result in some debtors deciding not to file for bankruptcy protection at all, thereby potentially resolving matters without the additional expense and delay of the bankruptcy process.

Moving Away from "Single Asset"

As it is currently written, § 101(51B) imposes the burdens of SARE — principally the requirement to file a confirmable plan or begin paying interest to a secured creditor within 90 days post-petition — on many owners of real estate "on which no substantial business is being conducted." However, there are several exceptions, some of which make more sense than others. For example, because Congress has created a separate reorganization system in chapter 12 of the Bankruptcy Code, it would be anomalous for family farmers to be subject to the expedited procedures applicable to SARE. Congress might have also thought that small residential investment properties are less likely to produce abusive bankruptcy filings than larger properties or commercial investments.

The requirement that SARE be "a single property or project," however, does not readily correspond with the goals of the SARE provisions. The premise of those provisions is that debtors who have little or nothing more than ownership of real estate are not very likely to be able to compose confirmable plans, so that they should at least compensate their secured creditors with interest payments while they make the attempt. But those problems are equally present if a debtor's holdings consist of multiple properties or multiple projects, as well as if a debtor's passive holdings form only part of a larger project. Litigation about whether real estate is considered a single property or project is thus not a productive exercise.

We suggest that the Bankruptcy Code move away from the "single asset" concept and focus instead on whether a debtor's real property is part and parcel of a business that might be reorganized or instead merely produces an income stream (or no income at all) through the efforts of third parties, which may or may not be affiliates of the debtor. Our proposed revision of § 101(51B) thus replaces the "single asset real estate" terminology with a more descriptive phrase: "passive ownership real estate" (PORE). It also allows for the possibility that ownership of property and operation of a business on that property may be housed in separate affiliates, and the definition would exclude such an enterprise from the definition of PORE if both affiliates are debtors in bankruptcy. In other words, the new phrase would permit affiliates to qualify collectively as a business that may attempt to reorganize on a standard timetable if their owners are willing to place the collective enterprise under court supervision, thus minimizing or eliminating the contentious problem of a debtor's payment of management fees to a nondebtor affiliate.

Eliminating the Gross-Income Requirement

For similar reasons, the requirement that a SARE debtor produce substantially all of the gross income from its assets does not correlate well with the Bankruptcy Code's goal of protecting secured creditors of debtors that are not likely to be able to reorganize their real estate holdings. For example, there is little functional difference between a company that owns a retail store and an income-producing parking lot, and another company that organizes its retail and parking operations into separate subsidiaries. Under the current definition of SARE, the mortgagee of the parking lot in the former scenario can be dragged along with the restructuring of the operating business unless other grounds for relief from the automatic stay are present, while the mortgagee of a parking lot that produces all of the income of a separate subsidiary can take advantage of the SARE provisions.

We suggest that the gross-income requirement, and thus the anomaly described above, be eliminated. Under this formulation, a secured creditor of PORE would be entitled to stay relief, absent the filing of a confirmable plan or the payment of interest within 90 days post-petition, regardless of whether a debtor owns other income-producing businesses or properties. We acknowledge that in some situations — particularly if PORE is included in the same entity as complex operating businesses — it may not be realistic to expect a plan to be filed within 90 days. However, a debtor in such a situation always retains the option to commence interest payments under § 362(d)(3)(B) instead, and we would expect a debtor to do so if the PORE is essential to its business operations or valuable in its own right. A debtor that cannot afford to make interest payments on its PORE because of a negative cash flow in its other operations stands little chance of reorganizing successfully in any event.

Focusing Restructuring on Situations with Employment at Stake

Our revisions also align the SARE provisions with one of the policy goals that is the subject of much discussion nowadays: job preservation. When an operating company's reorganization fails, or if stay relief is granted and a lender forecloses, unemployment is a distinct possibility for the company's employees. This problem is significantly less in SARE situations, in which there often are few or no employees. SARE cases often (but not always) have little at stake beyond the interests of owners seeking to retain their interests, a secured lender pursuing foreclosure, and a relatively small amount of unsecured debt.

Our proposed language is consistent with these realities. If a piece of real estate involves a third-party business, such as a tenant or a management company, the likelihood of job losses following a change of ownership is not significant. If, on the other hand, the debtor conducts a business through its own employees or employees of an affiliated debtor, greater disruption is possible if a secured lender forecloses. The definition excludes such a property from the definition of PORE so that the debtor has an opportunity to propose a restructuring within a normal timeline.

A New Definition of SARE (PORE)

With these considerations in mind, we propose that § 101(51B) be rewritten as follows:

> The term "passive ownership real estate" —
>
> > (A) means real property —
> >
> > > (i) on which no substantial business is being conducted, other than the business of operating the real property and activities incidental thereto; or
> > >
> > > (ii) on which any substantial business is conducted primarily by persons other than the debtor, employees of the debtor, and employees of an affiliate of the debtor that also is a debtor in a case under this title; and

> (B) does not include residential real property with fewer than [four] residential units or real property owned by a family farmer.

Conclusion

The purpose of the SARE provisions is to allow simple real estate cases to work their way through the system, if at all, on an expedited basis. Section 101(51B) in its present form simply fails to align chapter 11 outcomes with this goal. Although there are other aspects of the SARE provisions that need fine-tuning, and SARE cases could be handled more effectively by the courts, amending § 101(51B) in the manner suggested in this article would result in a more efficient bankruptcy process in relatively simple real estate cases.

At least when jobs are not seriously at risk, a debtor should demonstrate its desire to retain ownership of its real estate by either making interest payments during its breathing spell or filing a facially confirmable plan. Our clearer definition of the PORE threshold should allow the parties (and the court) to focus on the real problem rather than debating whether the case qualifies for expedited treatment at all.