

Southeast Bankruptcy Workshop

Senior Living

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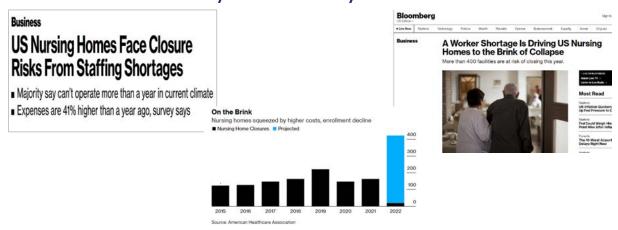
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Senior Housing Panel

- Suzanne A. Koenig SAK Healthcare Chicago
- Hon. Scott M. Grossman U.S. Bankruptcy Court S.D. Fla.
- John H. Rowland Baker Donelson Nashville
- Alexandra Shipley McGuireWoods Chicago
- David Gordon Polsinelli Atlanta



Why So Many Cases?



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Staffing and Labor Issues

- Short Term/Long Term/Permanent
 - Pre-Covid issues now more pronounced and sped up the inevitable
 - · Lack of automation and low use of technology/AI
 - · Very labor dependent delivery model
 - · Many low skilled positions
 - · Costly and inefficient delivery model
 - Talent shortages for various reasons
 - · Competition for some positions is not in industry

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Staffing and Labor Issues

- Short Term/Long Term/Permanent (cont'd)
 - Health care providers are being forced to limit capacity and cancel elective procedures because of issues with respect to availability and capacity of hospital staff, including:
 - Nurses and other clinical positions waiting to take a shift for more money, leaving for contract labor or higher paying positions
 - In some markets, lower paid clinical and back office are leaving to join restaurant or manufacturing industry for higher total rewards and less risk
 - · No per diem talent available
 - Drawing unemployment benefits \$\$\$
 - · Child care issues
 - · Burnout and earlier retirements/exits
 - Fear/Risks from COVID
 - Employer vaccination requirements

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Risks and Stressors

- SNFs & Assisted-Living Facilities
 - Current Status
 - Although serving the most vulnerable population in the COVID outbreak, skilled nursing and assisted-living facilities have been the forgotten stepchildren.
 - Industry census has fallen roughly 10% from late 2019 to early May 2020.
 - Census & Revenue
 - · Fair stimulus packages have helped temporarily
 - · Cessation of hospital elective procedures have hurt census in downstream referrals
 - Virus has devastated facilities in reputational, financial, and human terms
 - COVID residents convert to Medicare eligible
 - Expenses
 - · The race for Personal Protective Equipment expensive, hard-to-find, consumption grows
 - · Employee hazard pay for those having direct COVID exposure

Risks and Stressors (cont'd)

- Pipeline of talent coming into the Health care industry is down
 - CNA candidate pool behaviorally unstable and poor quality
 - CNA credentialing/testing failure rate very high
 - Concern about risks from COVID and vaccine adverse
 - Field is too demanding
 - Skilled workers make 2X plus in bio pharma
- Vaccine requirements
 - Not all health systems mandating united front?
 - When presented with deadlines, most employees have complied or moved to another system/industry
 - Unions fighting requirement

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Unique Chapter 11 Issues in Senior Housing

- A significant amount of senior housing facilities are operated by tenants who lease the facilities from healthcare REITs using long term, triple net leases.
- Are these leases "residential" within the meaning of Section 365 of the Bankruptcy Code?

Senior Housing Facility Leases

- When debtor is a lessee of real property where it operates a senior housing facility, important issue arises as to whether the lease is a "residential" lease or a "non-residential" lease
- Different treatment under Bankruptcy Code

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Section 365

365(d)(2):

In a case under chapter 9, 11, 12, or 13 of this title, the trustee may assume or reject an executory contract or *unexpired lease of residential real property* or of personal property of the debtor at any time before the confirmation of a plan but the court, on the request of any party to such contract or lease, may order the trustee to determine within a specified period of time whether to assume or reject such contract or lease.

Section 365

365(d)(3)(A):

The trustee shall <u>timely perform all the obligations of the debtor</u> . . . arising from and after the order for relief under <u>any unexpired lease</u> <u>of nonresidential real property</u>, until such lease is assumed or rejected, notwithstanding section 503(b)(1) of this title.



Section 365

365(d)(4):

(A) Subject to subparagraph (B), an <u>unexpired lease of nonresidential real property under which the debtor is the</u>
<u>lessee</u> shall be <u>deemed rejected</u>, and the trustee shall immediately surrender that nonresidential real property to the lessor, <u>if the trustee does not assume</u> or reject the unexpired lease <u>by the earlier of</u>—

- (i) the date that is 210 days after the date of the order for relief; or
- (ii) the date of the entry of an order confirming a plan.

(B)

- (i) The court may extend the period determined under subparagraph (A), prior to the expiration of the 210-day period, for 90 days on the motion of the trustee or lessor for cause.
- (ii) If the court grants an extension under clause (i), the court may grant a subsequent extension only upon prior written consent of the lessor in each instance.

"Residential"

- May assume or reject at any time before confirmation
- Not required to timely perform post-petition obligations (i.e., pay rent)

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"Nonresidential"

- DIP must continue post-petition performance (i.e., pay rent)
- 210 days to assume/reject (subject to one 90-day extension)

Split of authority

- "Property Test" looks at nature of the property (majority view)
- "Lease Test" looks at nature of the lease (minority view)

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"Property Test"

- Statutory analysis of "unexpired lease of nonresidential real property"
- The term "nonresidential" modifies "real property" and not "lease"
- Nature of the property not of the lease –determines whether § 365 (d) (3) and (4) apply

"Property Test"

In re PNW Healthcare Holdings LLC, 617 B.R. 354, 362 (Bankr. W.D. Wash. 2020)

- Property test "is most consistent with the language of § 365 (d), its usage in the broader context of § 365, and the legislative history of the 1984 and 2005 Amendments"
- The terms "residential" and "nonresidential" modified the real property, not the lease
- To rule otherwise would make all commercial leases nonresidential, and such a result "would produce 'unsensible and unintended circumstance by requiring immediate surrender of real property where people live and depend on a licensed operator'"
- Concluded leases were of residential real property, so § 365(d)(2) and not § 365(d)(3) and (d)(4) applied

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"Property Test" cases

- In re Michael H. Clement Corp., 446 B.R. 394 (N.D. Cal. 2011)
- In re Memory Lane of Bremen LLC, 535 B.R. 901 (Bankr. N.D. Ga. 2015)
- In re Tex. Health Enters., 255 B.R. 181 (Bankr. E.D. Tex. 2000)
- In re Bonita Glenn II, 152 B.R. 751 (Bankr. S.D. Cal. 1993)
- In re Care Givers Inc., 113 B.R. 263 (Bankr. N.D. Tex. 1989)
- In re Indep. Vill. Inc., 52 B.R. 715 (Bankr. E.D. Mich. 1985)

"Property Test" issues

What makes a property "nonresidential real property"?

- Residential apartment building with commercial businesses and offices?
- Transient or short-term patients?
- Extended stay hotels?
- Mobile home affixed to real property in manufactured housing community?
- RV park?
- Janitor or caretaker living on otherwise commercial property?

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"Lease Test"

Examines relationship between lessor and lessee and nature of lease, to determine whether the lease is intended to produce income for the lessee.

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"Lease Test"

In re Passage Midland Meadows Operations LLC, 578 B.R. 367 (Bankr. S.D. W.Va. 2017)

- Isolating the word "nonresidential" in § 365(d) (4) "isolate[s] one portion of the statute from its balance"
- Rather, the analysis must include references to other Bankruptcy Code provisions, including §§ 362, 365 and 541, which "indicate together that one cannot so easily dispense with the actual use to which the debtor will put the demised premises personally"
- Criticized the property test, because it "focus[es] . . . on the use to which unnamed, unknown, nondebtor sublessees, perhaps far down the leasing chain, will put the property"
- Believed the focus should be on "[t]he substance of the lease, namely the precise purpose the lessee has for the property"
- Concluded lease was nonresidential; therefore § 365(d)(3) and (d)(4) applied

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"Lease Test"

- In re Clinton Care Ctr. LLC, 436 B.R. 390 (Bankr. N.D. Miss. 2010)
- In re Summit Ventures, 1991 WL 133412 (Bankr. D. Vt. 1991)
- In re Emory Props. Ltd., 106 B.R. 318 (Bankr. N.D. Ga. 1989)
- In re Sonora Convalescent Hosp. Inc., 69 B.R. 134 (Bankr. E.D. Cal. 1986)
- In re Condo Admin. Servs. Inc., 55 B.R. 792 (Bankr. M.D. Fla. 1985)

"Lease Test" issues

- Does this test conflate the terms "lease of nonresidential real property" with commercial income-producing leases, without a clear congressional intent to do so?
- Will patients and residents be put out on the street?

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Secured Lender's Perspective Why is Healthcare Lending a Challenging Risk Environment?

- 1. Regulatory Risks highly regulated industry
- 2. Operating Risks labor/staffing, management, resident care
- Event Risks people-intensive industry, occupancy rates affected by macro issues
- **4. Liquidity Risks** cashflows depend on government reimbursement/3rd parties
- Asset Valuation Risks certifications (CON/Medicare/Medicaid programs)
- 6. Litigation Risks patients, governmental



- a. Compositions and Extensions
- b. Standstill Agreements
 - i. cash conservation and management (tied to professionals) to ensure standard of care is key
- d. Engagement of Professionals (Borrower/Lender)
- e. Use of CROs and Turnaround Management
- f. Deal Drivers (MAD/Who Runs the Process)

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Pre-Bankruptcy Options, Opportunities & Threats Forbearance / Workouts / Out of Court Restructurings

- g. Potential Pitfalls for the Lender
 - i. excessive control/lender liability
 - ii. organizing the enemy
 - iii. herding cats
 - iv. lack of an organizational framework
 - v. weird & uninvited guests (government agencies)
 - vi. borrower resistance and trust issues
 - vii. public health crisis affecting ability to comply with covenants
- h. Exit Strategies



Receiverships

- It's Litigation Not Free
 - b. Capitulation or Counterclaims
 - c. The Receiver Who Pays? We Do
 - i. where to file (federal common law vs. state law)
 - ii. who(m) (& who chooses)
 - iii. how much
 - iv. how long
 - v. other professionals the Lender may have to pay for
 - d. Court Oversight, Control & Expertise (or not)
 - e. Think about the End before You Begin
 - i. management and operation
 - ii. sale (targets/process/timing)
 - iii. closure/liquidation/compliance

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Know Before You Go

- a. Your Collateral
- b. Value (including liquidation value)
- c. State of Perfection/Competing Claims
- d. Borrower's Operational Integrity Short Term/Long Term
- e. Exit Strategies and Escape Options



It's a Bankruptcy – Now What? What Cause the Filing / Is it Fixable?

- a. Reimbursement Issues (Patient Mix)
- b. External Factors competition, referral sources, litigation
- c. Quality of Care paramount consideration
- d. Staffing
- e. Facilities deferred maintenance, infrastructure, capital needs

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Initial Assessment

- a. Review Loan Documents
 - i. entity/transaction structure
 - ii. collateral pool and perfection
 - iii. status of government receivables ("perfection" and payment threats)
 - iv. assess competing interests in assets
 - v. operating covenants, occupancy, liquidity

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Use of Cash Collateral / DIP Financing

- i. immediate need/budgeting
- ii. valuation and available collateral
- iii. risk assessment and competing lenders
- iv. does funding provide measure of control/direction (milestones)
- v. leverage funding to sanitize pre-bankruptcy actions
- vi. does funding preserve/enhance collateral value
- vii. does funding buy time for exit/soft landing

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Exit Strategies – How Long Should I Stick Around?

- a. Note Sale
- b. Restructuring
- c. 363 Sale
 - i. timing
 - ii. process
 - iii. targets
- d. Stay Relief and Foredosure Seriously?
 - i. post-foredosure issues
 - ii. dosure plans and shutdown
- e. Conversion/Dismissal

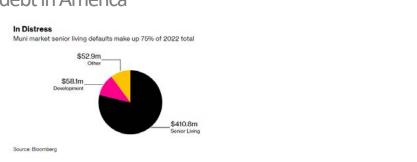
Tax Exempt Municipal Bond Financing & Senior Housing

- The past 10 years have seen a significant rise in the number of senior housing facilities financed with tax exempt municipal bond debt
- Most of the deals put together in the years leading up to the COVID-19 pandemic are extremely tight.

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Tax Exempt Municipal Bond Financing & Senior Housing

 Senior Housing defaults are now the number one driver of distressed municipal bond debt in America



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Tax Exempt Municipal Bond Financing & Senior Housing

- Role of the Trustee & Restrictions on What It Can Do
- Difficulties in Finding a Negotiating Party
- Material Non-Public Information, EMMA, and "Cleansing" the Holders
- Use of RSAs and Pre-negotiated Chapter 11s

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Looking Forward

- Operational Solutions
- Private Equity & Consolidation
- The Silver Tsunami
- Role of Government in Healthcare

Faculty

David E. Gordon is a shareholder with Polsinelli PC in Atlanta and leads Polsinelli's national distressed health care practice. He counsels on business bankruptcies and insolvencies with a distinct focus on health care industry restructuring. Mr. Gordon has represented health care providers, REITs, hospitals, lenders, landlords, health care systems, skilled-nursing and assisted-living facilities, purchasers of distressed assets, secured and unsecured creditors, committees, trustees and other parties-in-interest in chapter 11 reorganization proceedings, receiverships and workouts throughout the U.S. His transactional experience includes representing purchasers in § 363 sales and representing various parties in problem loan workouts, bridge loans and other financings, forbearance agreements and other distressed transactions. Prior to joining Polsinelli, Mr. Gordon taught as an adjunct professor of law at the Emory University School of Law for more than seven years. He received his B.A. in 2003 from Georgetown University and his J.D. with honors in 2006 from Emory University School of Law.

Hon. Scott M. Grossman is a U.S. Bankruptcy Judge for the Southern District of Florida in Fort Lauderdale, sworn in on Oct. 2, 2019. He previously was a shareholder with a large international law firm in its global restructuring and bankruptcy practice, and he represented distressed companies, debtors, secured and unsecured creditors, official committees, trustees, landlords and purchasers of distressed assets, and worked on bankruptcy cases across various industries, including real estate, hospitality, health care, entertainment, banking, technology, energy and financial fraud. While primarily involved in chapter 11 reorganizations, he also represented clients in out-of-court workouts and restructurings, chapter 7 liquidations, receiverships, assignments for the benefit of creditors and insolvency-related litigation. Judge Grossman was active in local bar activities, including having served as president of the Bankruptcy Bar Association of the Southern District of Florida. When in private practice, he was listed in Chambers USA, The Best Lawyers in America and Super Lawyers magazine, and was a member of the winning teams for the Global M&A Network's Turnaround Atlas Awards for both "Cross Border Special Situation M&A Deal (Small-Mid Markets)" in 2019, as well as "Turnaround of the Year — Small Markets" in 2015. Judge Grossman began his legal career in the Attorney General's Honors Program at the U.S. Department of Justice, where he was a trial attorney in the Tax Division, Civil Trial Southern Section, from 1999-2004. He received his B.S. in 1996 from the University of Florida and his J.D. in 1999 from George Washington University Law School.

Suzanne A. Koenig, CTP is the founder and CEO of SAK Management Services, LLC in Riverwoods, Ill., a health care management firm and consultancy. She is experienced across several segments of the health care industry, including post-acute, senior housing and long-term care, with expertise in the areas of operations improvement, staff education, quality assurance, marketing and census-development. Ms. Koenig is one of the most frequently appointed patient care ombudsmans by courts across America. Her experience includes court-appointed service as an examiner, receiver, chapter 11 trustee and patient care ombudsman; health care bankruptcy filings under chapters 11 and 7, particularly since the enactment of BAPCPA in 2005; leadership of more than 500 facilities to cultivate teams that restore quality care and fiscal soundness; consulting and advising clients involved with bankruptcy proceedings, restructurings and workouts, as well as turnaround management scenarios; and executive positions in marketing, development and operational efficiencies and management for numerous regional and national health care providers. Ms. Koenig testified before the Illinois House of Representatives as

an industry expert in funding issues facing the long-term care industry, was a member of the Negotiating Team Task Force in Arizona who designed and negotiated the contract between the State and counties for delivery of indigent health services, was the only non-lawyer and non-Attorney General invited by the National Association of Attorneys General to participate on the "Patient Care Ombudsman" panel addressing the PCO's interaction with the States in their role as patient care monitor, served as a member of the board of directors of both ABI and the Summit Healthcare REIT, Inc., and co-chaired ABI's Health Care Insolvency Committee. In addition, she was elected to the Global Turnaround Management Association's board of trustees, co-chaired the Steering Committee of the Midwest Chapter of the Turnaround Management Association (TMA), served on the board of directors for the School of Social Work at the University of Illinois at Urbana - Champaign, and was elected officer and director for several long-term care provider associations. Ms. Koenig is a Licensed Nursing Home Administrator and a Licensed Social Worker in multiple states. She is a frequent speaker for leading health care industry associations and business affiliates, where she conducts continuing education and training programs. Ms. Koenig received her Bachelor of Social Work degree from the University of Illinois at Urbana-Champaign and her M.S. from Spertus College.

John H. Rowland is a shareholder in the Nashville, Tenn., office of Baker, Donelson, Bearman, Caldwell & Berkowitz, PC and is the immediate past chair of its Corporate Restructuring and Bankruptcy Group. He represents a variety of clients in complex business reorganizations, restructurings and financing transactions. Mr. Rowland regularly counsels companies facing financial challenges, and he is experienced in representing various constituencies, creditors and individuals in bankruptcy cases and adversary proceedings. He also represents buyers and sellers of distressed assets, parties who wish to proceed outside of bankruptcy, and lenders seeking to provide chapter 11 debtor-inpossession and exit financing. Mr. Rowland is a frequent presenter on bankruptcy-related topics. He has been listed in *The Best Lawyers in America* since 2005 for Bankruptcy and Creditor/Debtor Rights/Insolvency and Reorganization Law and Bankruptcy Litigation, named the Best Lawyers' 2017 Nashville Litigation - Bankruptcy "Lawyer of the Year," listed since 2008 in Mid-South Super Lawyers and selected as "Best of the Bar" in the Nashville Business Journal in 2005. Mr. Rowland was president of the Midsouth Commercial Law Institute from 2010-11 and chair of the Bankruptcy Court Committee of the Nashville Bar Association in 2004, and he is a member of the American, Tennessee (Executive Committee Member, Commercial, Bankruptcy, and Banking Law Section) and Nashville Bar Associations. He received his B.A. with honors in 1986 from Alma College and his J.D. in 1989 from the University of Kentucky College of Law.

Alexandra Shipley is an associate with McGuireWoods in Chicago and focuses her practice in the areas of insolvency and restructuring. She represents a wide range of clients in all stages of bank-ruptcy, restructuring and workout matters. She also serves as a restructuring and insolvency resource for the firm's CBD team. Prior to joining McGuireWoods, Ms. Shipley practiced with the Tulsa office of an Oklahoma law firm, where she gained experience in various areas of civil litigation and bankruptcy. She is a board member of the Chicago Chapter of the International Women's Insolvency & Restructuring Confederation, and she is admitted to practice in Illinois, Oklahoma, the U.S. Bankruptcy Court for the Northern District of Illinois, and the U.S. District Courts for the Northern District of Illinois and the Eastern and Northern Districts of Oklahoma. Ms. Shipley received her B.S. in ballet with high distinction in 2011 from Indiana University and her J.D. in 2015 with highest honors from the University of Oklahoma College of Law, where she was admitted to the Order of the Coif and was assistant managing editor of the *Oklahoma Law Review*.