

11 U.S.C. § 1126(a)  
Bankr. Rule 3017(e)  
Standing

In re Shilo Inn, Diamond Bar, LLC, Case No. 302-32435

10/18/02 ELP

Published

Debtors sought an order determining procedures for voting by beneficial holders of trust indebtedness. Debtors are obligors on loans that are held by trusts. The trusts hold pools of loans, including debtors' loans, in which investors have certificates of interest. Debtors proposed a plan of reorganization and sought a determination that the certificate holders, not the servicer of the loans on behalf of the trusts, must vote the trusts' claims.

The court first held that a third party to the dispute did not have standing to provide argument and evidence, because the third party is not directly affected by a determination of who can vote the trusts' claims.

The court also held that the certificate holders do not have a right to vote the trusts' claims. The opinion discusses the difference between REMIC trusts and certificate holders, on the one hand, and indenture trustees and bond holders, on the other. The court concluded that the claims belong to the trusts, not to the individual certificate holders, and therefore the servicer of the loans could vote the claims on the trusts' behalf. The fact that the pooling and servicing agreements under which the servicer operates may require the servicer to vote against the plan does not mean that the certificate holders should instead be allowed to vote on the plan.

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UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF OREGON

In Re: ) Bankruptcy Case No.  
)  
Shilo Inn, Diamond Bar, LLC, ) 302-32435-elp11 LEAD CASE  
Shilo Inn, Oakhurst, LLC, ) 302-32436-elp11  
Shilo Inn, Delano, LLC, ) 302-32437-elp11  
Shilo Inn, Salt Lake City, LLC, ) 302-32438-elp11  
Shilo Inn, Richland, LLC, ) 302-32681-elp11  
Shilo Inn, Portland/205, LLC, ) 302-32682-elp11  
Shilo Inn, Elko, LLC, ) 302-32982-elp11  
Shilo Inn, Seaside Oceanfront, LLC, ) 302-32987-elp11  
Shilo Inn, Spokane, LLC, ) 302-32988-elp11  
Shilo Inn, Beaverton, LLC, ) 302-33026-elp11 through  
Shilo Inn, Bend, LLC, ) 302-33043-elp11  
Shilo Inn, Boise Riverside, LLC, )  
Shilo Inn, Casper, LLC, ) (Jointly Administered under  
Shilo Inn, Coeur d'Alene, LLC, ) 302-32435-elp11)  
Shilo Inn, Grants Pass, LLC, )  
Shilo Inn, Idaho Falls, LLC, ) MEMORANDUM OPINION  
Shilo Inn, Lincoln City, LLC, )  
Shilo Inn, Nampa Blvd., LLC, )  
Shilo Inn, Nampa Suites, LLC, )  
Shilo Inn, Newport, LLC, )  
Shilo Inn, Salem, LLC, )  
Shilo Inn, Tacoma, LLC, )  
Shilo Inn, The Dalles, LLC, )  
Shilo Inn, Tillamook, LLC, )  
Shilo Inn, Warrenton, LLC, )  
Shilo Inn, Washington Square, LLC, )  
Shilo Inn, Yuma, LLC, )  
)  
Debtors. )  
)

1 Debtors have filed a Motion for Order Determining Procedures  
2 for Voting by Beneficial Holders of Trust Indebtedness. They seek,  
3 pursuant to Bankruptcy Rule 3017(e),<sup>1</sup> to have the court determine  
4 procedures for transmitting debtors' proposed plan, disclosure  
5 statement and ballots to the holders of certificates of interest in  
6 trusts holding loans that include loans to debtors. The issue is  
7 whether the special servicer of the loan pools may vote the trusts'  
8 claims, or whether those claims must be voted by the certificate  
9 holders. For the reasons explained below, I conclude that the  
10 special servicer may vote the claims, and therefore will deny the  
11 motion.

#### 12 FACTS

13 Debtors are 27 limited liability companies (LLCs), each of  
14 which owns real property on which a Shilo Inn hotel is operated.  
15 Prepetition, debtors obtained secured loans in an amount aggregating  
16 approximately \$159,000,000. Those loans are now included in pools  
17 of loans held in three trusts (Trusts 1-3). LaSalle Bank National  
18 Association is the trustee for Trusts 1 and 2; State Street Bank and  
19 Trust Company is the trustee for Trust 3. The trusts then sold the  
20 beneficial interests in the pools of loans, including loans to  
21 debtors and other entities, to investors who received certificates  
22 evidencing their interests. The certificates are divided into  
23 different classes, each of which has different rights with regard to  
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25 <sup>1</sup> Unless otherwise indicated, all chapter, section and rule  
26 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1330, and to  
the Federal Rules of Bankruptcy Procedure, Rules 1001-9036.

1 distributions from amounts collected on the pooled loans. This  
2 arrangement has been referred to by the parties as "securitized  
3 loans." Criimi Mae Services Limited Partnership (Criimi Mae) is the  
4 special servicer for the pools of loans held by all three trusts.

5 Debtors listed their debts to the trusts in their bankruptcy  
6 schedules. Criimi Mae asserts that, under the Pooling and Servicing  
7 Agreements (PSAs) that govern its actions as special servicer, it is  
8 entitled to vote on behalf of the trusts on debtors' proposed  
9 chapter 11 plan of reorganization.<sup>2</sup> Debtors assert that provisions  
10 of the PSAs restrict Criimi Mae's ability to vote in favor of the  
11 plan, and therefore the beneficial holders of the trust indebtedness  
12 must be able to vote on the plan.

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20 <sup>2</sup> There are three PSAs for the loans on which debtors are  
21 obligated, one PSA for each trust. At the trial in the adversary  
22 proceeding Shilo Inn, Diamond Bar, LLC v. LaSalle Bank National  
23 Assoc. et al., Adv. No. 02-3180 (Bankr. D. Or.), I admitted the  
24 three PSAs into evidence as Exhibits 681, 682 and 683. The three  
25 PSAs are substantially similar, although the specific section  
26 references are not identical. Both parties refer to and rely on the  
PSAs, therefore I will take judicial notice of them for purposes of  
this motion. See Fed. R. Evid. 201. In deciding this motion, I  
will primarily rely on and refer to Exhibit 681, which is the  
December 1, 1997 PSA for Commercial Mortgage Pass-Through  
Certificates Series 1997-ML1 (Trust 1).

1 DISCUSSION

2 1. Standing of Shilo Management Company

3 At the initial hearing on this motion, which was held at the  
4 same time as the disclosure statement hearing, I asked the parties  
5 to provide the court with further briefing with regard to the issues  
6 raised by the motion. Shilo Management Company (SMC) filed a letter  
7 and exhibits, providing argument and evidence for the position that  
8 the certificate holders are the appropriate parties to vote on  
9 debtors' plan.

10 The trusts object to my consideration of SMC's submissions,  
11 arguing that SMC is not a party to this motion and was not asked to  
12 provide briefing on the issues raised by the motion.

13 The parties to this motion are debtors and the trusts,  
14 represented by Criimi Mae. SMC is not a party.<sup>3</sup> It has no direct  
15 stake in the outcome of the motion. In order to have standing, a  
16 person must be "aggrieved" by the bankruptcy court's action. See In  
17 re CFLC, Inc., 89 F.3d 673, 675 (9th Cir. 1996); In re Commercial  
18 Western Finance Corp., 761 F.2d 1329, 1334 (9th Cir. 1985); In re  
19 Fondiller, 707 F.2d 441, 442-43 (9th Cir. 1983). A person is  
20 aggrieved if the person is "directly and adversely affected  
21 pecuniarily by an order of the bankruptcy court." Fondiller, 707

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23 <sup>3</sup> Counsel for SMC appeared telephonically at the disclosure  
24 statement hearing. In response to a comment offered by counsel for  
25 SMC on this motion, I suggested that counsel might be able to assist  
26 debtors in preparing their brief. However, I did not ask SMC to  
submit its own brief and did not intend to give SMC standing to  
argue this motion.

1 F.2d at 442. The party asserting standing must show that the  
2 bankruptcy court's order either diminishes its property, increases  
3 its burdens, or detrimentally affects its rights. Fondiller, 707  
4 F.2d at 442; In re Giordano, 212 B.R. 617 (9th Cir. BAP 1997).

5 SMC is a third party to the voting rights dispute. Its  
6 interests will not be directly affected by a determination of  
7 whether Criimi Mae or the certificate holders may vote the claims of  
8 the trusts against debtors. Therefore, I will sustain the trusts'  
9 objection and will not consider SMC's submissions.

10 2. Voting rights<sup>4</sup>

11 Bankruptcy Code § 1126(a) provides that "[t]he holder of a  
12 claim or interest allowed under section 502 of this title may accept  
13 or reject a plan." Claims are deemed allowed unless a party in  
14 interest objects. § 502(a). In this case, the trusts filed proofs

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16 <sup>4</sup> Debtors filed their motion pursuant to Rule 3017(e), which  
17 allows the court to enter an order that "provides for transmission  
18 of the plan and disclosure statement together with associated  
19 materials to creditors, equity security holders and, in a chapter 11  
20 case, the United States trustee." 9 Lawrence P. King, Collier on  
21 Bankruptcy ¶ 3017.02[1] (15th ed. Rev. 2001). The trusts argue that  
22 the rule does not apply because the creditors and equity security  
23 holders to which the rule refers are creditors and equity holders of  
24 the debtor, not creditors and equity security holders of creditors  
25 of the debtor. Debtors do not claim that Rule 3017(e) applies if  
26 the certificate holders are not entitled to vote on the plan; the  
purpose of providing them with the plan and disclosure statement and  
other associated materials is to inform their votes on the plan.  
The issue distills to whether the certificate holders rather than  
Criimi Mae are entitled to vote the trusts' claims. Debtors do not  
dispute Criimi Mae's authority to act on behalf of the trusts; they  
argue rather that the certificate holders are the proper entities to  
vote the claims, not the trustees or an agent of the trustees.  
Therefore, I will address the underlying issue of whether the  
certificate holders are entitled to vote on the plan.

1 of claim in each case and no objections have been filed. Therefore,  
2 pursuant to § 502(a), those claims are deemed allowed.

3         Only a holder of a claim may vote to accept or reject a plan.  
4 Debtors argue that the certificate holders are the beneficial owners  
5 of the loans to debtors, and therefore are the proper parties to  
6 vote. They compare the relationship between the certificate holders  
7 and the trusts to that between bondholders and an indenture trustee.  
8 According to debtors, because bondholders are entitled to vote on a  
9 plan in a reorganization of the entity that issued the bonds, the  
10 certificate holders in this case should be able to vote on debtors'  
11 proposed plan of reorganization. Debtors also argue that, as a  
12 practical matter, the PSAs require Criimi Mae to oppose the plan on  
13 behalf of the trusts.<sup>5</sup> Because Criimi Mae is contractually bound to  
14 vote to reject debtors' plan as proposed, debtors argue that the  
15 certificate holders should be able to vote, because they are not  
16 similarly constrained.

17         The trusts argue that indenture trustees and bond holders are  
18 very different from REMIC<sup>6</sup> trusts and certificate holders, and that  
19 the trusts, not the certificate holders, hold the claims against

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21         <sup>5</sup> As I explain in more detail below, the PSAs limit Criimi  
22 Mae's discretion in servicing and administering the loans. For  
23 example, Criimi Mae as special servicer may not grant an extension  
24 of the maturity of a loan for more than a year or modify a monetary  
term of a mortgage loan, or accept substitute or additional  
collateral, without the approval of the controlling class  
representative. See Exh. 681 at § 3.27.

25         <sup>6</sup> The trusts in this case are real estate mortgage  
26 investment conduits, or REMICs. See 26 U.S.C. § 860D (defining  
REMIC).

1 debtors. They point to provisions in the PSAs that limit the rights  
2 of certificate holders to control the actions of the special  
3 servicer in its actions on behalf of the trust.

4 I conclude that the claims belong to the trusts, not to the  
5 individual certificate holders, and therefore Criimi Mae as agent  
6 for the trusts may vote the trusts' claims. First and foremost, the  
7 certificate holders in this case hold certificates evidencing a  
8 beneficial interest in the trust funds. The trust assets include  
9 loans on which debtors are obligated. Debtors are not obligated to  
10 the certificate holders. Likewise, the certificate holders do not  
11 have any direct interest in the obligations of debtors. Their  
12 interest is in the assets of the trusts. The trusts are creditors  
13 of the Shilo Inn debtors.

14 Second, there are differences in structure between corporate  
15 bond issuance and the securitization of assets that results in  
16 issuance of certificates to investors.

17 Corporations, like other forms of business, frequently  
18 raise capital through debt financing. Debt represents  
19 borrowed capital which must be repaid. In essence, bonds or  
20 debentures are promissory notes but contain more elaborate  
21 provisions than ordinary commercial loans. . . . In order to  
22 borrow funds from a large number of investors, corporations  
23 and other public issuers contract with a third party to  
24 administer a bond issue. This third party acts as the  
25 indenture trustee.

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23 3 Thomas L. Hazen, The Law of Securities Regulation § 19.1 (4th ed.  
24 2002)(footnote omitted). Thus, the holders of the bonds or  
25 debentures are like holders of promissory notes evidencing debt of  
26 the issuer corporation.

1           Where the issuer of corporate bonds becomes a debtor in  
2 bankruptcy, Bankruptcy Rule 3003(c)(5) authorizes an indenture  
3 trustee to file a proof of claim on behalf of all the bond holders.  
4 However, "the indenture trustee is not the holder of the claim and,  
5 accordingly, is not entitled to accept or reject a plan." 4 William  
6 L. Norton, Jr., Norton Bankruptcy Law and Practice 2d § 91.19  
7 (1997). The bond holders are entitled to vote their own claim or  
8 interest. Lawrence P. King, Collier on Bankruptcy ¶ 1126.02[2]  
9 (15th ed. Rev. 2001).

10           A securitization of assets is a different financing  
11 structure.

12           A structured financing involving the issuance of asset-  
13 backed securities is a hybrid transaction; it is a cross  
14 between a traditional secured bank credit facility and a  
15 securities offering. Rather than borrowing money directly  
16 from a bank or issuing its own securities to investors, the  
17 company causes a separate entity to issue securities backed  
18 by the company's assets.

19           Although the details of structured financings vary  
20 greatly, the fundamentals of most transactions are the same.  
21 A company that generates receivables or loans (the originator  
22 or originating company) transfers a pool of these assets to a  
23 special purpose vehicle -- usually a corporation or a grantor  
24 trust. The special purpose vehicle then issues securities,  
25 either debt or equity, backed by the receivables or loans to  
26 investors. The monies that the vehicle receives from the  
investors are used by the special purpose vehicle to pay the  
originator for the assets. The cash generated by the assets  
is used to make principal and interest payments to the  
investors.

23 Stephen I. Glover, "Structured Finance Goes Chapter 11: Asset  
24 Securitization By Reorganization Companies," 47 Bus. Law. 611, 614  
25 (Feb. 1992). In an asset securitization, then, the special purpose  
26 vehicle, not the company that generates the receivables or loans,

1 issues the securities and has the relationship with the investors.  
2 The investors' right to payment comes from cash generated by the  
3 pooled assets, not from the general funds of the originator of the  
4 assets.

5 That the certificate holders do not have direct rights  
6 against the obligors on the pooled loans makes sense in light of the  
7 complications that would arise if they had such rights. Asset pools  
8 can contain a large number of assets. For example, the pool of  
9 loans underlying Trust 3 (Mortgage Pass-Through Certificates Series  
10 1996-C2) contains 300 loans, only four of which are debtors' loans.  
11 Exhibit 683 at p. 208. Because it would be unwieldy for each of the  
12 certificate holders to have individual rights against each of the  
13 obligors on the 300 loans, the PSA provides the mechanism for  
14 collection efforts, if needed, for the collective benefit of the  
15 certificate holders.<sup>7</sup>

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17 Thus, in a corporate bond issuance, the investor is a  
18 creditor of the corporation that issued the bonds or debentures, and  
19 has a right to payment from the corporation. In contrast, in an  
20 asset securitization, the investors' relationship is with the

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22 <sup>7</sup> Also, as the trusts point out in their brief, the  
23 different trust classes of certificate holders have widely disparate  
24 economic interests and would likely vote to protect those interests.  
25 Letter dated October 6, 2002 from Charles R. Gibbs at pp. 10-11. It  
26 is not clear how votes of certificate holders of the various trust  
classes would be calculated or weighed between trust classes in  
determining the vote of the single bankruptcy plan class for each  
mortgage.

1 special purpose vehicle to which the originator of the assets (here,  
2 the banks that took the assignments of debtors' loans from the  
3 original lenders) has transferred those assets, and the investors'  
4 right to payment comes from the cash generated by the transferred  
5 assets, not from the originator of the assets itself.

6 Finally, the PSAs in this case do not provide the certificate  
7 holders a right to vote on the reorganization plan of obligors on  
8 the loans that constitute the asset pool in which the certificate  
9 holders hold an interest. The certificate holders have certain  
10 limited voting rights, but only as specifically provided in the  
11 PSAs. Exh. 681 at § 10.2. Those rights include the right to vote  
12 to terminate the special servicer on default by the servicer, to  
13 waive defaults by the servicer, to remove the trustee for the trust  
14 and appoint a successor trustee, and to make certain limited  
15 modifications to the PSA. Id. at §§ 7.1; 7.5; 8.7; 10.7. A  
16 representative of the controlling class of certificate holders may  
17 advise the special servicer with regard to certain actions, and the  
18 special servicer may not take certain actions without the approval  
19 of the controlling class representative, including modifying a term  
20 of a mortgage loan other than the extension of the maturity date for  
21 less than one year, and selling a defaulted loan or accepting  
22 substitute or additional collateral for a mortgage loan. Id. at  
23 § 3.27. The PSAs give the certificate holders rights to advise the  
24 special servicer and to enforce their rights against the special  
25 servicer and the trustee. However, they do not give the certificate  
26 holders the right to enforce the pooled mortgage loans on their own

1 unless the trustee has been requested to do so and has refused. Id.  
2 at § 10.2. That has not happened in this case; here, the trustee is  
3 pursuing enforcement on behalf of the certificate holders. Thus,  
4 the certificate holders do not have any rights to vote with regard  
5 to any proposed modifications to the loans that are contained in  
6 debtors' proposed plan of reorganization.

7 Debtors argue that the certificate holders must be allowed to  
8 vote the trusts' claims because Criimi Mae as special servicer is  
9 obligated under the PSAs to reject debtors' proposed plan. The PSAs  
10 give Criimi Mae as special servicer broad authority "to do or cause  
11 to be done any and all things in connection with such servicing and  
12 administration of the Group 2 Mortgage Loans which they may deem  
13 necessary or desirable," subject to certain servicing standards.  
14 E.g., Exh. 681 at ¶ 3.2(a). The PSAs restrict that authority in  
15 certain respects. For example, after a default in the payment of a  
16 balloon payment on a Mortgage Loan, Criimi Mae is not permitted to  
17 grant an extension that would extend the maturity date of the loan  
18 beyond December 15, 2027. Id. at § 3.12(a). The special servicer  
19 is allowed to waive due on sale clauses and to enter into assumption  
20 agreements, but if it does so, it "shall not agree to modify, waive  
21 or amend, and no assumption or substitution agreement entered into  
22 pursuant to Section 3.11(a) shall contain any terms that are  
23 different from, any term of any Group 2 Mortgage Loan or the related  
24 Note or Mortgage." Id. at § 3.11(d). The special servicer can take  
25 certain actions only if the controlling class representative has  
26 approved such action in writing, including foreclosing on defaulted



