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ResCap Rescued

Complex DIP Facility Paves Way for Successful Sale

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When Residential Capital, LLC (or ResCap) filed for Chapter 11 protection in May 2012, the company and its affiliates constituted the fifth largest servicer of residential mortgage loans and the tenth largest originator of residential mortgage loans in the United States. As of March 2012, ResCap and its affiliates were responsible for servicing approximately $374 billion of domestic residential mortgage loans and working with more than 2.4 million homeowners across the United States, according to James Whitlinger, ResCap's Chief Financial Officer. Only Bank of America, J.P. Morgan Chase Bank, Wells Fargo Bank, and CitiMortgage serviced more mortgage loans than ResCap at that time.

ResCap filed for bankruptcy with ambitious goals. The company intended to use the Chapter 11 process to complete two separate asset sales – the first for the company's mortgage loan origination and servicing businesses and the second for ResCap's legacy portfolio consisting mainly of mortgage loans and other residual financial assets. Those sales were expected to generate several billion dollars in proceeds.

While asset sales during the course of a Chapter 11 case are common, ResCap's asset sales presented unique challenges. In order to preserve the value of the assets, ResCap needed to continue operating as a going concern until the sales could be completed. There was no precedent that would suggest that ResCap could remain a going concern after filing, however. "No mortgage originator and servicer had ever been able to remain in business through a bankruptcy," says Todd Goren, one of the partners at Morrison & Foerster responsible for leading the ResCap engagement.

One of the primary issues for ResCap was the amount of funding that the company would need early in the Chapter 11 cases, combined with the filing's impact on its existing sources of funding. Marc Puntus, a partner and co-head of the Restructuring Group at Centerview Partners LLC, which was retained as ResCap's investment bankers in the bankruptcy cases, stated in court filings that ResCap would owe approximately $350 million for servicing advance obligations during the first week of its bankruptcy. However, the primary facility used by ResCap to finance and fund servicing advances prior to the bankruptcy filing was structured as an off-shore, bankruptcy-remote, special purpose financing. The Chapter 11 filing would cause the facility to go into "rapid amortization" if it was not "refinanced" by a debtor-in-possession (DIP) financing facility, according to Puntus.

Against this backdrop and months in advance of the filing, ResCap's advisors began a marketing process to seek out the DIP financing that would be required in a Chapter 11 case. ResCap ultimately secured two DIP facilities – a $1.45 billion super-priority secured facility from Barclays Bank PLC as lead lender, as well as an additional $200 million facility from Ally Financial, ResCap's parent company, which was not a debtor in the bankruptcy cases. The $200 million of additional lending from Ally Financial was provided in the form of post-petition draws on an existing facility and was provided to cover ResCap's second largest expense – repurchases of certain whole loans that were sold into securitization trusts guaranteed by Ginnie Mae. The Ally financing was arranged once ResCap determined that the Barclays DIP facility would not be sufficient to cover these expenses, Puntus noted in court filings.

The Barclays DIP facility consisted of a $1.06 billion A-1 term loan, a $200 million A-2 term loan, and a $190 million revolver. While ResCap conducted an extensive marketing process, Barclays represented an ideal lead lender because Barclays was already the sole lender under ResCap's existing $800 million servicing facility. Therefore, Barclays was "comfortable lending against the assets, which are repaid on a priority basis, making loans against the stream – up to a percentage – relatively safe," says Goren.

Despite that familiarity, the financing was still "extraordinarily complex because it also refinanced an existing loan repo facility and took a second lien on numerous

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other assets," according to Goren. "Thus, the deal had to include aspects of a traditional servicing advance, loan repo, and syndicated DIP credit agreement, but, in this case, all merged into one facility."

"These are somewhat esoteric assets," says Mark Shapiro, Barclays' head of global restructuring and finance. "This was not your traditional inventory receivables ABL-type lending." To complete the loan, Barclays drew on the resources of its leveraged finance team, its syndicate desk, its securitized product group, and its financial institutions group.

The competitive pressure resulting from the advisor-led marketing process for the DIP mandate, combined with Barclays' familiarity with ResCap's business and the assets securing the borrowings allowed for ResCap to receive very favorable terms, despite the facility's complexity. "Barclays was able to provide ResCap a liquidity lifeline at a funding cost of roughly six percent, which was 300 basis points better than other deals the company had considered," says Goren. In court filings, Puntus also noted that, when measured by all in yield, which accounts for original issue discount, interest rate, and aggregate fees, "the Barclays DIP facility was more favorably priced than any other…similarly sized DIP facility" entered into during the same time frame. The Barclays facility also provided the added benefit of not encumbering ResCap's existing unencumbered assets, according to Goren, thus directly benefiting ResCap's unsecured creditors. Those unencumbered assets, totaling $775 million in book value, included $250 million in cash.

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Ultimately, the Barclays and Ally facilities provided the financing ResCap needed to continue its operations and bridge to a sale of its mortgage loan origination and servicing businesses, as well as the sale of its legacy portfolio. Those sales, led by Morrison & Foerster and Centerview, proved to be even more successful than the company had originally anticipated. After competitive auctions, the mortgage loan origination and servicing assets were sold to Ocwen Loan Servicing and Walter Investment Management Corporation for approximately $800 million more than the stalking horse bid, while the legacy whole loan portfolio was sold to Berkshire Hathaway for approximately $175 million more than the stalking horse bid. In the aggregate, "the sales yielded approximately $4.5 billion in gross proceeds to ResCap," according to Puntus and "will result in almost $1 billion more for distribution to ResCap's creditors than was originally anticipated," notes Goren. Both the Ally and Barclays DIP facilities were repaid in full after the closing of both sales in February of this year.

The uniqueness and success of ResCap's DIP financing has drawn attention. The Barclays DIP facility was recognized as International Financing Review's 2012 Americas Restructuring of the Year. It was also one of only six deals short listed for International Financial Law Review's Americas 2013 Restructuring Deal of the Year. ¤