

The Beyond Agency Series: A Guide to Private Credit and CMBS Lockbox and Cash Management Account Provisions

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If you are an experienced agency borrower exploring a CMBS or private credit loan, one often-overlooked part of the negotiation process is cash management. It may not jump off the page, but failure to comply with cash management procedures will result in default and could trigger recourse to the guarantor.

Agency borrowers who are used to full control of their funds for most (if not all) of the loan term can sometimes be caught off guard during closing procedures when they are informed that they need to open new accounts at a bank they're not familiar with and shift the direction of their cash flow.

Welcome back to our *Beyond Agency* series, a collaboration between FBT Gibbons' Multifamily and Commercial Real Estate Finance teams that is geared toward multifamily owners whose next loan will not be an agency loan, and who could use a translator to help them decode cash management. This is cash management, part one. In what follows, we walk you through the three primary structures of lockbox and cash management provisions most commonly seen in CMBS and private credit term sheets, moving from least to most restrictive. We also translate the customary term sheet language into plain English, while flagging what each structure actually requires a borrower to do at — and after — closing.

What Accounts Are Involved in Cash Management? A Shared Vocabulary

Different lenders and different banks use a variety of terms to describe the same types of accounts. Before getting into the three most common cash management structures, one must first understand the two accounts that are in play for these deals:

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- **Deposit Account:** Sometimes called a Lockbox Account, Deposit Account, Blocked Account, Restricted Account, or Clearing Account, a Deposit Account is set up for the sole purpose of accepting rents from the tenants and directing them on to their next destination. It's the water valve that a lender pulls on when there's a cash management trigger event, directing funds either back to the borrower or over to the lender.
- **Cash Management Account:** This account is set up as an impound for funds after a Cash Management Trigger Event (see below). When funds arrive here from the Deposit Account, the lender applies the funds in an order set up in the loan documents known as the "waterfall" — typically debt service first, then reserves and escrows, then approved operating expenses, and finally excess cash flow, which is either released to the borrower or held by the lender as additional collateral (depending on the type of Cash Management Trigger Event).

When looking at different cash management structures, the basic questions to ask are: When does this account open? And what happens to the funds?

There are a few more terms worth having on hand:

- **Deposit Account Control Agreement (DACA) and Cash Management Agreement (CMA)**: Each of these is a tri-party agreement among the borrower, the lender, and the bank through which the lender opens and "controls" the Deposit Account or Cash Management Account. These agreements spell out the mechanics of each account and are specific to whichever bank opens the account. For this article, we will be calling the agreements the "DACA" and the "CMA" — which many also use to refer to the accounts themselves.
- **Cash Management Trigger Event** (sometimes called a Cash Sweep Event or Trigger Event): The trigger event — often an event of default, a debt service coverage ratio or debt yield falling below a specified threshold, or a "lease sweep" event tied to a major tenant's lease expiration, termination or going

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dark — is what flips the switch from business as usual to active cash management.

1. What Is a Springing Lockbox and Springing Cash Management? — The Least Restrictive Option

This is the structure you'll see in the strongest-performing deals with the most borrower-friendly leverage and sponsorship. The term sheet language usually requires the borrower to enter into a DACA and CMA for closing and not to open any accounts — yet.

Term sheet language typically looks like this:

*"**At closing**, Borrower shall enter into **an agreement** with lockbox bank…"*; or

*"**After the occurrence of a trigger event**, Borrower **will be required** to establish an account…"*

Prior to closing, the only work that needs to be done is to simply make an introduction with the bank and come to an acceptable springing DACA and CMA — that's it. Under this structure, the borrower keeps collecting rent the way it always has into its ordinary operating account, and the accounts may never open for the life of the loan. However, upon the occurrence of a Cash Management Trigger Event, the borrower must immediately open both accounts and start depositing rents directly into the Deposit Account, which then flows to the Cash Management Account impound and waterfall.

What this means practically: This is the most permissive and cost-effective of the cash management structures because it means business as usual and no setup or transfer fees with a third-party bank. But it is important to work with legal counsel to define when and how these obligations spring: what exactly constitutes a Cash Management Trigger Event, how much time there is to comply once one occurs, and whether it can be cured.

2. What Is an In-Place ("Soft") Lockbox with Springing Cash Management? — The Middle

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Ground

Here, unlike the springing structure above, the Deposit Account itself is actually established at closing — that's the "in-place" part. From day one, every dollar of rent physically lands directly into the Deposit Account and is subject to a DACA in favor of the lender. But because the cash management waterfall is still springing, the lockbox bank automatically sweeps the funds right back into the borrower's own operating account on a daily basis — that's the "soft" part. Functionally, this is the same as a Springing Lockbox, but now the water valve is already installed for the lender to easily and timely redirect funds to the Cash Management Account in case of a trigger. Lenders typically prefer this over a fully springing arrangement, as they can switch the flow of funds on their own and don't need to wait for the borrower to open up the account. However, this comes at a cost in the form of service and transaction fees for the funds passing through the Deposit Account.

Term sheet language typically looks like this:

*"**At closing**, Borrower will be required to **establish an account**, and all rents shall be deposited directly into such account and transferred daily into Borrower's operating account."*

What this means practically: Now that an account is being opened, there is real work to do — the borrower needs to onboard and run know-your-customer (KYC) procedures with a bank that meets the lender's (and often the rating agencies') eligibility criteria, needs to execute the DACA, and needs to work with the management company (or directly with any commercial tenants) to ensure that all rents go directly into the Deposit Account before a single expense is paid. There are also real costs *during* the loan term — a Deposit Account that is open and operating with funds passing through regularly will incur transfer and maintenance fees each and every month.

3. What Is an In-Place ("Hard") Lockbox with Hard Cash Management? — The Most Restrictive

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Option

This structure assumes, from day one, that the Cash Management Trigger Event has already occurred — because in practical terms, it has: it's baked into the loan structure itself rather than tied to a future event. Term sheet language here tends to be shorter, precisely because there's no springing mechanism to describe:

*"Borrower shall establish a lockbox account **and** cash management account with the lockbox bank at closing, and all rents shall be deposited directly into such accounts and applied in accordance with the cash management waterfall described herein from the Closing Date."*

There's no "absent a trigger" carve-out, because the pipeline from the Deposit Account straight into the Cash Management Account waterfall is already built and operating as of closing. The first month's rent is subject to the same waterfall — debt service, reserves, approved operating expenses, excess cash flow — that would otherwise only apply after a trigger in the two structures above. That's where the "hard" comes in: both accounts are operating with the maximum of lender protections.

What this means practically: This structure carries with it the greatest restriction and the highest costs — now there are two open and active accounts, and one of them is heavily managed by the Cash Management bank as it follows lender instructions. The borrower has essentially no free cash flow, and no distributions, outside of what the lender-approved operating budget permits from the very first month of the loan. Because there's no springing period to negotiate here, the borrower's counsel's leverage shifts almost entirely to (1) how generous and how quickly approved the operating expense budget process is, since that becomes the borrower's only real source of working capital; (2) the conditions under which excess cash is released rather than held as reserve; and (3) whether the loan documents include a "flip" mechanism — some deals allow a hard structure to convert to a springing one if the property achieves a specified debt service coverage ratio for a set number of consecutive quarters.

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Quick Reference: Which Accounts Do I Need to Open for a Lockbox, and When?

Structure	Accounts Needed at Closing	Waterfall Active at Closing?	What a Trigger I
Springing Lockbox / Springing CM	None — ordinary operating account only	No	Borrower must o Cash Manageme Deposit Account Management Ac
In-Place ("Soft") Lockbox / Springing CM	Deposit Account	No — funds from Deposit Account auto-sweep to Borrower	Lender switches from Borrower's Management Ac
Hard Lockbox / Hard CM	Deposit Account (Lockbox) and Cash Management Account	Yes, from the closing date	Trigger is already

Closing Thoughts

The labels "springing," "soft" and "hard" are useful shorthand, but they aren't defined terms with universally consistent meanings across every lender's documents or with every bank. The only way to know for certain what a given term sheet requires is to read past the label to the actual mechanics: what account has to be opened, when, who controls it, and what has to happen before money starts flowing somewhere other than the borrower's own account. Getting a quick understanding will allow you and your counsel to get at the heart of these provisions and have meaningful negotiations with your lender before you exit the term sheet stage.

If you have questions regarding multifamily financing, including CMBS and private credit options, or need help evaluating the terms and structure of a loan, please contact the authors or any member of the firm's **Commercial Real Estate Finance** and **Multifamily** teams. And be on the lookout for cash management, part two, in our *Beyond Agency* series, where we will discuss working with lockbox banks and navigating the pitfalls of cash management triggers and cures.

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Beyond Agency Series

- Part 1 – Multifamily Loans in a Higher for Longer World
- Part 2 – A Guide to Private Credit and CMBS Lockbox and Cash Management Account Provisions
- Part 3 – What Should a Borrower Pay Attention to When Negotiating CMBS or Private Credit Cash Management Terms?
- Part 4 – What Should a Borrower Focus on When Negotiating Transfer Provisions in Private Capital and CMBS Loan Documents?

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