



Preferred Equity Facility Would Provide Much Needed Relief to Commercial Real Estate Market

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The commercial real estate finance industry continues to be significantly impacted by the ongoing COVID-19 pandemic. In a [letter](#) to Treasury Secretary Steven Mnuchin and Federal Reserve Chairman Jerome Powell, a group of 105 bipartisan congressional members urged the Department of the Treasury and Federal Reserve to provide additional assistance to the commercial real estate market, particularly borrowers in the commercial mortgage-backed securities ("CMBS") market who have been unable to obtain sufficient relief through many other state or federal aid facilities due to structural restrictions impacting CMBS loans.

Texas Congressman Van Taylor is discussing a bill that would provide additional aid to commercial real estate borrowers in the form of preferred equity with other members of Congress. The bill called the "Helping Open Properties Endeavor Act of 2020" (the "HOPE Act") would establish the "HOPE Preferred Equity Facility." The facility would infuse additional capital into distressed commercial properties by guaranteeing a financial institution's preferred equity investment in a borrower. This additional capital would enable borrowers to make debt service payments and pay operating expenses while property revenues continue to be impacted by the COVID-19 pandemic. The facility could be a lifeline for hospitality and retail properties which have been hardest hit by the COVID-19 pandemic and related governmental orders.

The HOPE Act is still being drafted and is only available in "Discussion Draft" form but seems likely to include:

- The preferred equity investment would be made by financial institutions and guaranteed by the federal government.
- Borrowers would need to satisfy certain criteria related to revenues during the COVID-19 pandemic, including but not limited to a debt service coverage ratio of at least 1.30 to 1.00 in 2019.

- The amount of the preferred equity investment would be up to 10% of the outstanding debt.
- The preferred equity instrument would be unsecured, subordinate to any existing financing on the property and provide for no voting rights or right of foreclosure.
- Payments would likely not begin until at least two years after the date of the preferred equity investment and the repayment period will likely be at least seven years after the date payments begin.
- The interest rate will potentially be as low as 2.5%.
- Borrowers could redeem the preferred equity at any time without penalty, subject to certain mandatory redemptions upon transfers of 50% or more of the ownership in the property.
- Borrowers would be required to redeem the preferred equity before any distributions could be made to other equity holders.
- Financial institutions would receive a servicing fee and could be entitled to reimbursement by the federal government for a portion of the preferred equity amount.

The HOPE Act could provide significant relief to borrowers with structured debt loans, such as CMBS, CLO, debt funds, mortgage REITS and life insurance company lenders who may not otherwise be able to take advantage of all of the other federal aid facilities during the COVID-19 pandemic due to loan restrictions.

The specifics of the bill will likely need to address some of the constraints on borrowers, including the general prohibitions on the creation of preferred equity and reductions in the loan guarantor's ownership interest. Commercial real estate market advocates are optimistic that the HOPE Act can provide significant relief to the commercial real estate market, particularly borrowers on hospitality and retail properties in need of critical support to address the COVID-19 pandemic's ongoing impact on revenues.

Frost Brown Todd will be continually monitoring the Helping Open Properties Endeavor Act of 2020 and will provide additional information as it becomes available. For more information, please

contact [John Gragg](#), [Geoff White](#), [Chandler Hodge](#), [Devon Callaghan](#), [Josh Brock](#) or any attorney in Frost Brown Todd's [Financial Services Industry Team](#).

To provide guidance and support to clients as this global public-health crisis unfolds, Frost Brown Todd has created a Coronavirus Response Team. Our attorneys are on hand to answer your questions and provide guidance on how to proactively prepare for and manage any coronavirus-related threats to your business operations and workforce.

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