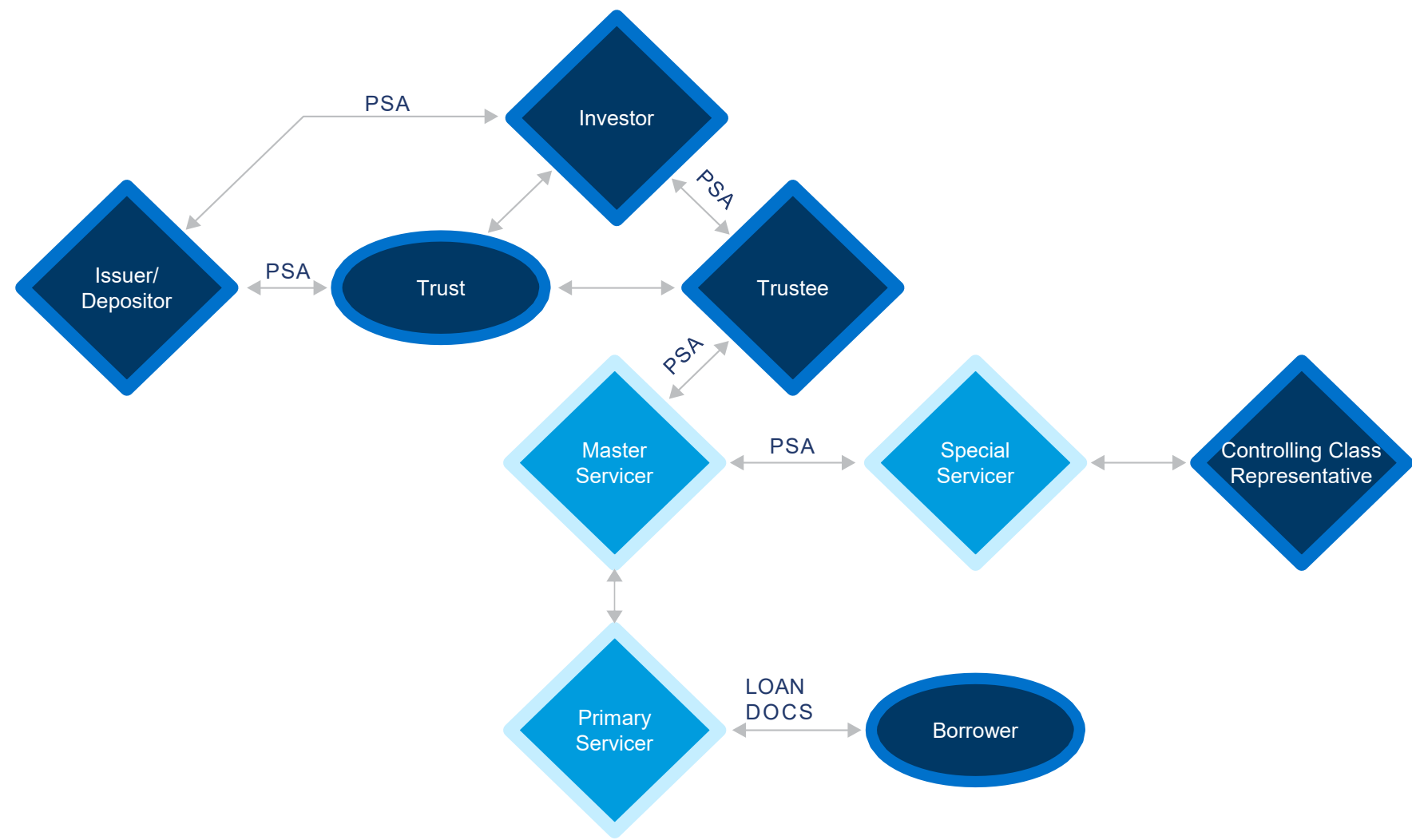




From Distressed to Opportunity

Proskauer»

CMBS Loan Parties



Master vs. Special Servicer Duties

- A Borrower will interact with a servicer for the life of the loan.
 - The responsibilities of the various parties servicing the loan are described in the Pooling and Servicing Agreement (“PSA”).

Master Servicer

- Master servicer duties are typically administrative (tracking/analyzing loan reserves, remitting taxes and property insurance, lease reviews, etc.).
- The master servicer handles Borrower requests such as performing loan consents, waivers, and reserve disbursements.

Special Servicer

- Special servicer requests may include modifications, loan maturity and other major decisions as defined in the PSA.
- The special servicer is typically responsible for making recommendations to the CCR for all major decisions.

Master Servicer Role

Typical Responsibilities would include:

- Cash management, including escrow reserve account adequacy and reserve disbursements.
- Insurance claims and disbursements.
- Property inspections.
- Lease review and approval.
- Rent roll/tenancy monitoring and triggers.
- Property related approvals, i.e., easements and release of collateral.
- Loan assumption and ownership equity transfer approvals.
- Financial and legal covenant monitoring, i.e., Debt Service/Yield testing and compliance with Special Purpose Entity provisions.
- Rating agency interactions.
- Reporting.
- Loan prepayments; Yield maintenance or Defeasance.
- Payoff statements.
- Coordinate the transfer of loan to special servicing.

Special Servicer Role

Typical responsibilities include making recommendations to the CCR for all major decisions.

- Loan is transferred to the special servicer (“SS”) if Borrower defaults on loan, or a default is imminent.
- The SS has substantial experience in dealing with non-performing loans.
- The SS determines the terms of a potential loan workout, such as a forbearance or modification, a discounted payoff, or if a foreclosure/deed-in-lieu is the best recovery option.
- The special servicer represents and acts on behalf of the B-Piece Buyer/Controlling Class Representative (“CCR”) and may be an affiliate of these parties.
- The CCR is the controlling bondholder class at the time of modification. The CCR may change from time-to-time if there is a loss in the bond pool and they are “appraised out”.

Controlling Class Representative

The Ultimate Decision Maker:

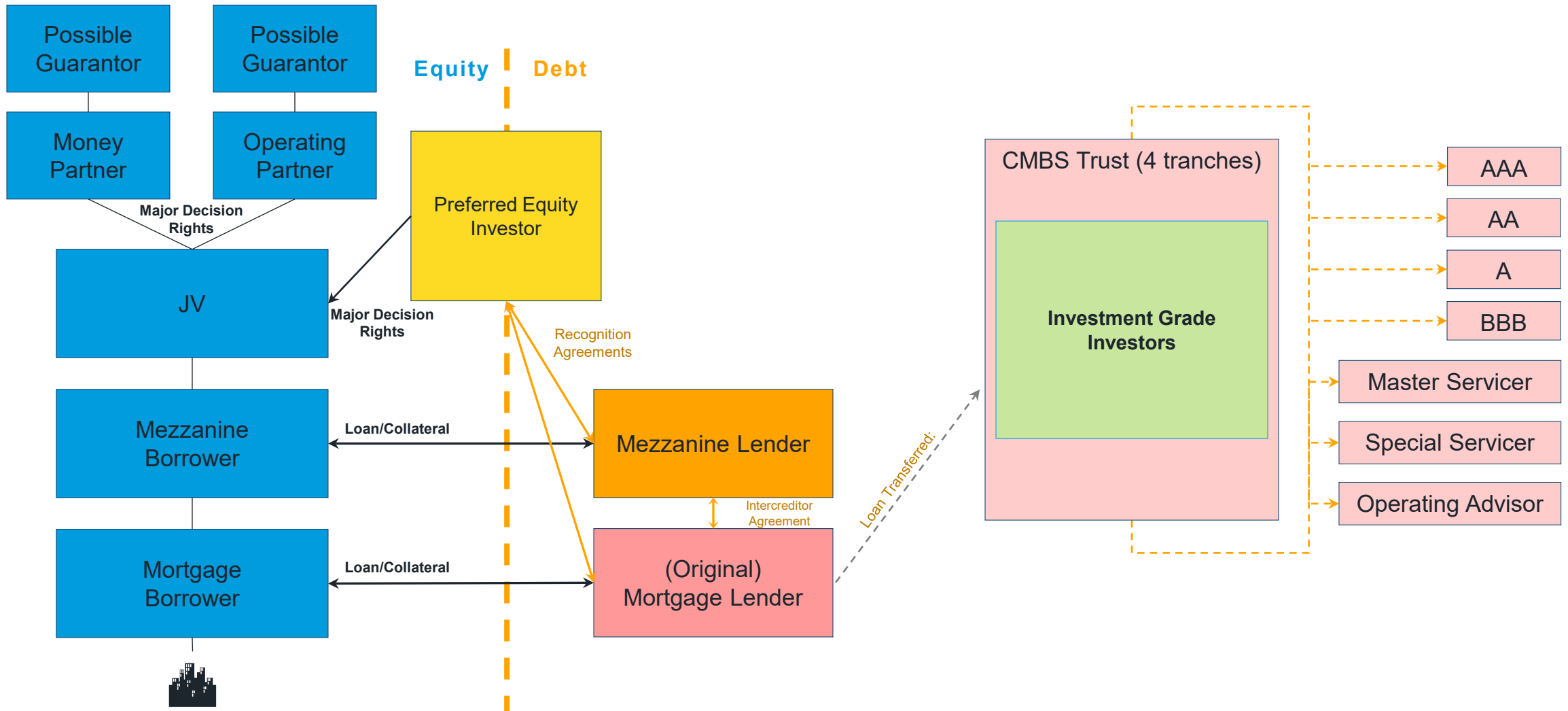
- The holder of the most subordinate CMBS bond/unrated bond class is typically referred to as the B-piece Buyer.
- The B-piece Buyer plays an active role in the decision-making process on issues that can affect the value of individual loans and the overall CMBS pool.
- Formally, the B-piece Buyer is referred to as the CCR.
- The CCR has ultimate approval rights/responsibilities for the first mortgage.
- Rights of other subordinate holders (mezz lenders) are also factored into the modification negotiations.

CMBS Servicing Rights

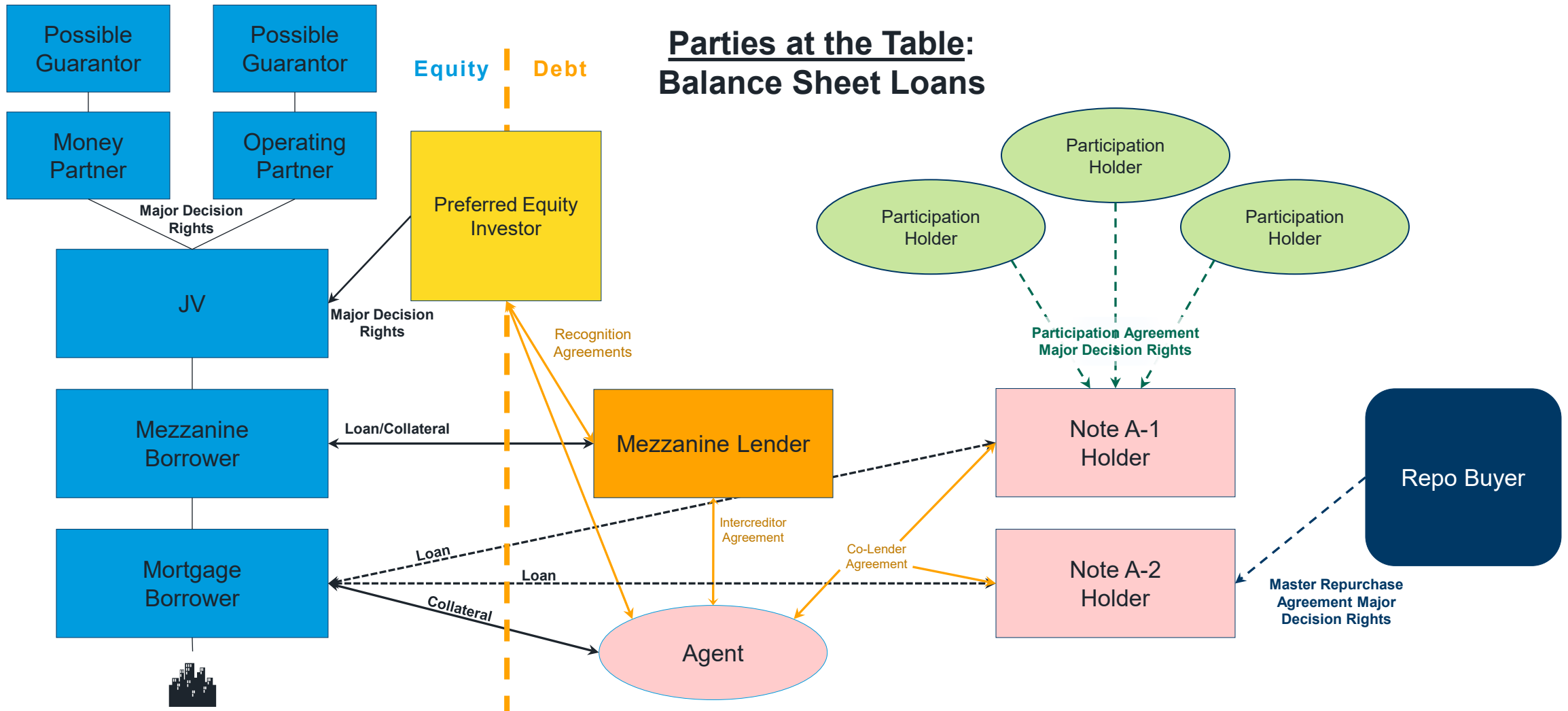
Pooling and Servicing Agreements dictate how the **CMBS Servicers** are to govern the loan.

- Describe in detail how the loans within the CMBS pool are serviced.
- While there are similarities amongst PSA's, individual CMBS pools have their own PSA with specific terms.
- Includes servicing standards by which the servicer is required to perform their functions.
- Identifies which class of bondholder controls the special servicer decision making process.
- Requires the servicers to meet REMIC requirements and to protect the bondholders.

Parties at the Table – CMBS Loans



Parties at the Table – Balance Sheet Loans



Distressed Office Case Study

- The subject Property is a mixed-use class B+ office building with ground floor retail located in Atlanta.
- At origination (January 2014/10-year term/interest only), the Property was valued at \$180MM and the loan amount was \$108MM (60% LTV). The office space was 90% occupied and the retail was 100% occupied by a Trader Joe's, Bed Bath and Beyond, and a fast casual restaurant.
- As of May 2023, the office space was 65% leased and 50% occupied, BB&B was in bankruptcy/liquidation and the restaurant is struggling. A cash flow sweep period had been triggered as a result of the BB&B BK and a low Debt Service Coverage Ratio test. All excess cash flow from the Property is being retained in a reserve. Sponsor anticipates having to come out-of-pocket for shortfall in principal and interest payments when an office tenant vacates in February 2024. Sponsor estimates the value of the Property as-is at \$80MM +/- \$10MM. LTV ranges between 154% and 120%.
- Sponsor has determined that the Property will require a \$25M equity infusion to re-tenant the BB&B space and for amenities improvements to the office space to remain competitive in the market. Rents will continue to deteriorate even with the improvements.
- With the performance of the Property, and loan maturity within 12 months (and inability to refinance the current loan), Sponsor is reluctant/not willing to invest additional equity (CapX, TI/LC and out-of-pocket principal and interest shortfalls).

Variables in Loan Structure:

- CMBS loan-four tiered tranches in a single-borrower, single loan pool.
- We will also assume that at securitization the following rated tranches were created
 - \$20M “BBB”
 - \$18M “A”
 - \$35M “AA”
 - \$35M “AAA”
- Balance sheet loan with three pari passu A-Note participations owned by different lenders/investors with a participation agreement.
 - We will also assume that after origination this loan was split into an \$88M mortgage and \$20M mezzanine loan.

Borrower/ Sponsor Options:

- Loan Modification with new equity from either Sponsor or a new financial partner providing preferred equity.
- Discounted payoff or DPO.

Appraisal Reduction Amount Calculation

- Appraisal Reduction Amount = Property Debt and Liabilities – (Appraisal Value x 90%) + Reserves
- Property Debt and Liabilities include:
 - the outstanding principal amount of the Mortgage Loan
 - accrued and unpaid interest on the Mortgage Loan (at the non-default rates)
 - unpaid property protective advances made by the Servicer with respect to the Mortgage Loan
 - unpaid interest (typically accruing at a rate equal to the prime rate) on such property protection advances and on any outstanding debt service advances made by the Master Servicer with respect to the Mortgage Loan
 - unpaid real estate taxes, ground rents and insurance premiums currently due with respect to the mortgaged property (net of any escrows or letters of credit held by the Servicer for such items)
- any liens against the mortgaged property which are senior to the mortgage securing the Loan
 - To the extent Property debt and liabilities exceed 90% of the appraisal value of the Property plus reserves the resulting excess is the Appraisal Reduction Amount
 - Under the PSA the most junior bond tranche is the controlling holder until the Appraisal Reduction Amount exceeds 75% of the outstanding principal amount of those bonds. So in our example let's assume the appraisal value of the Property is \$80.0 million and reserves are \$4 million. Also let's assume Property debt and Liabilities are \$110.0 million. Finally let's assume the outstanding principal amount of the BBB bonds is \$20M, the outstanding principal amount of the A bonds is \$18M, the outstanding principal amount of the AA bonds is \$35M and the outstanding principal amount of the AAA bonds is \$35M.

In this case, the Appraisal Reduction Amount is \$34.0M ($(\$110M - (80M \times .9) + \$4M)$). For controlling holder purposes the following analysis takes place:

BBB Bondholders:

$\$34M > .75 \times \$20M$ so the control shifts to the A bondholders

Then turning to the next tranche Appraisal Reduction Amount is \$14M ($\$34M - \$20M$).

A Bondholders:

$\$14M > .75 \times \18 so control shifts to the AA bondholders

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