CMBS Credit Focus

Releasing Holdbacks: RENT is Writing Up Bonds

Short-Order Holdback Release Leaves Many Open Questions

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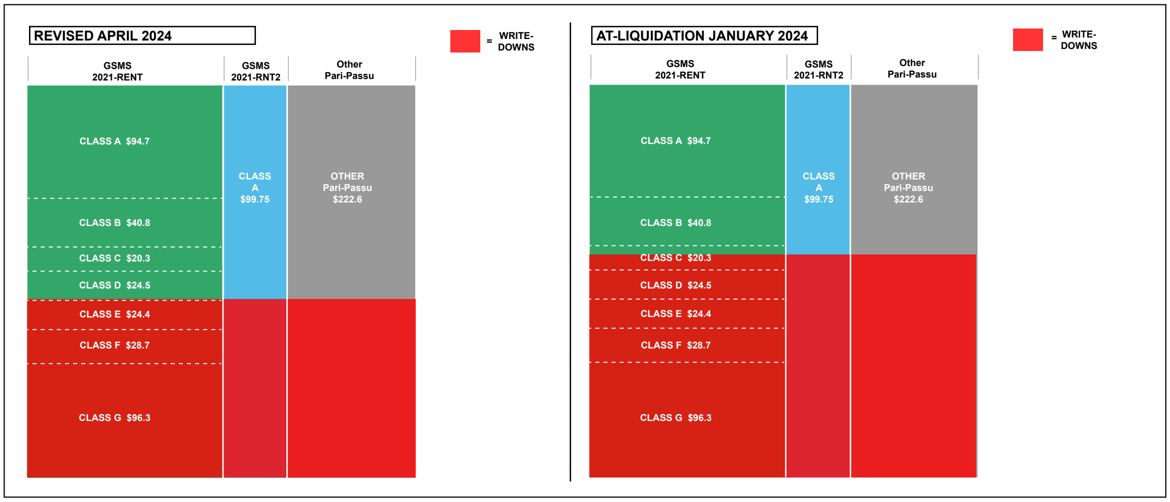
Three months after holding back an eye-popping $164 million of the liquidation proceeds on the $343 million Veritas Multifamily Portfolio Pool in GSMS 2021-RENT, the servicer is now starting to release some of those holdbacks. A revision to the January 2024 remittance that turned up on Friday shows the releases increased the net proceeds to the bondholders by nearly $40 million, to $188.5 million. This eliminated the realized losses on the deal's C and D classes, which were written down back in January (Figure 1).[1]

Figure 1. Veritas Multifamily Portfolio Pool Holdback Release



Source: Servicer Reports and Academy Securities

The development shows how ultimate bond losses can sharply swing when servicers hold back significant amounts of liquidation proceeds. Bondholders that were looking at full writedowns on their exposures just three months ago, are now fully paid off. Future holdback releases can potentially write-up more classes.

1 "Holdbacks: RENT in the Limelight, as Other Cases are Brewing," CMBS Credit Focus, Academy Securities, January 25, 2024

The holdback release happened based on what the remittance called the special servicer's "current assessment of the potential exposure." The servicer did not widely disclose back in January the rationale for the RENT holdbacks, and has not provided additional details in the months since. But deal notices and subsequent press reports suggested potential litigation risk on the heels of a dispute between certain investors in the deal and the special servicer.

The updated servicer assessment may reflect re-evaluation of the litigation risk, or actual developments behind-the-scenes that reduce the likelihood of the risk materializing. Without deal disclosures, market participants can't really know. Moreover, the difference between the revised holdback amount ($58.9 million, Figure 2) and the original $164 million holdback amount in January, is significantly higher than the overall write-up on RENT. The remittance mentions that registered investors can directly contact the servicer.

Figure 2. Veritas Multifamily Portfolio Pool Liquidation ($ millions), April 2024 Revision

	GSMS 2021-RENT	GSMS 2021-RNT2
Original Note Balance	$347.2	$105.0
Note Balance at Liquidation	**$343.6**	**$103.9**
Gross Sale Proceeds	$285.7	$75.0
Expenses	$35.2	$1.2
Holdbacks	$58.9	$0.0
Total Expenses/Holdbacks	**$94.1**	**$1.2**
Net Liquidation Proceeds	$188.5	$73.8
Realized Loss to Loan	**$155.1**	**$30.1**
Loss Severity	45.1%	29.0%

Source: Deal Documents and Academy Securities

Write-ups Timing and Scope Remains Elusive

As the market digests the fresh RENT write-ups, the development illustrates a few relevant aspects around holdback practices:

- **Release timing and scope remains uncertain.** The three-month time frame for initiating the holdback release in RENT echoes the one on Crossgates Mall (COMM 2012-CR1, CR2, and CR3). Crossgates was the first prominent case that unexpected, hard-to-project held back amounts created significant losses to the capital stack. In Crossgates, the servicer started to release holdbacks in November 2023, four months after initially holding them.[2] In RENT, the initial writeup percentage (~24% of the holdbacks) is also largely within the range of Crossgates. Still, it is probably too soon to draw firm conclusions about servicers' approach to the timing and scope of holdback releases based on just two cases, which are also quite different in their circumstances.

2 "Crossgates Liquidation: Holdbacks Complicate Severity Projections," CMBS Credit Focus, Academy Securities, September 11, 2023

- **Release disclosure.** The RENT deal reported the holdback release via a revision to the deal's final remittance report, that was originally published after the liquidation of the deal's only loan. RENT stopped producing regular remittance reports once all the deal's classes paid off or were written down back in January. In contrast, Crossgates reported its holdback releases in the CR1-C3 deals' monthly reporting cycles, because the conduit transactions still have bonds with outstanding balance. The RENT holdback release reporting underscores the difficulty in surveilling releases on paid-off deals. The timing of the remittance "revision" that discloses the release can be completely unexpected. Investors must be diligent in having various disclosure "alerts" once the regular reporting cycle ends. It remains to be seen if other trustees will also choose to report holdback releases via remittance revisions, or perhaps by using other disclosure formats.

- **CREFC best practices.** Holdback guidance that CREFC published earlier this month could help standardize holdback practices and reporting. To be sure, deals' pooling and servicing agreements (PSAs) already mention servicers can hold back liquidation proceeds for future trust expenses. In addition, a couple IRP data fields already aim at capturing such holdbacks and their adjustments (L116 and L121). But RENT and Crossgates clearly showed that holdback practices can catch investors by surprise, as well as the difficulty of tracking holdback accounts. The IRP holdback fields are buried deep in the csv-format loan periodic file. The fields are not readily available in most cashflow systems. Further, PSAs typically do not provide guidance on the servicer decision-making on the held back amounts, other than alluding to the general servicing standard. Reviewing a sample of PSAs, we did not see explicit provisions that limit holdback amounts. All told, CREFC's new best practices, which propose specific deal notices and quarterly updates on any holdbacks above $1 million, are a step in the right direction.

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