# CMBS Credit Focus

## Mezz Loan Sales: A Potential Headache for CMBS Workouts

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### Track Reshuffling of Mezz Lenders on Troubled Loans

**Mezz loan sales may complicate workouts on troubled CMBS situations as new mezz holders join the property capital structure.** A few recent mezz sales underscore the issue. For example, a $4.7 million mezz loan on Parkway Center ($41.6 million, WFCM 2018-C45) is currently on the market. The borrower on the senior mortgage loan, the third largest exposure in the C45 deal, is in modification discussions with the servicer, according to recent commentary. The potential sale of the subordinate mezz loan on the 593K sf office complex in Pittsburgh, PA, may introduce a new motivated stakeholder, who may pursue various mezz rights, including a foreclosure. In turn, the just announced $275 million mezz loan sale on Parkmerced ($1.5 billion, MRCD 2019-PARK and eight other deals), to the tune of $167.5 million, showed that the economic incentives of mezz holders can change as buyers come in with a different cost basis.

**Several of the mezz loan sales we are now seeing are for performing loans.**[1] Sales of performing mezz are distinct from non-performing loan sales. The latter can sometimes represent UCC foreclosure sales, with the existing lender using a “credit bid” and almost always “winning” the auction sale. In such situations, the mezz lender essentially exercises one of the basic remedies of mezz lending – foreclosing on a defaulted borrower and acquiring ownership interest in the property.[2] In contrast, in performing mezz sales, the new owners may not be able to immediately exercise any rights, even when the property may be in trouble, at least until the mezz loan defaults.

### Recent Large Loan Defaults Have Mezz Positions in Place

**Many of the large office loans that recently defaulted or transferred to special servicing have mezz loans below the CMBS mortgage exposures.** Examples include the $484.7 million CXP 2022-CXP1 Portfolio, with $125 million mezz loan, and the $350 million Gas Company Tower and World Trade Center Garage (GCT 2021-GCT), which has two mezz positions totaling $115 million (Figure 1). Some CMBS borrowers may be defaulting “strategically”, looking to initiate loan modification discussions with special servicers, as we recently discussed. But mezz lender actions could upend some of the borrower or mortgage lender calculations. Interestingly, while the New York State Supreme Court determined last year that The Distrikt Hotel mezz lender cannot stop the mortgage lender from foreclosing on the troubled hotel ($33.0 million, MSBAM 2012-C5), the situation highlighted the nuances of mezz lender involvement, and potential legal delays.

1 Examples include a $57.4 million portfolio sale, with 12 performing mezz loans across different property types, and a $7 million performing mezz loan on a Midtown Manhattan office tower. We cannot identify all the underlying properties, and some of the senior mortgages on them may not be securitized.

2 See “Equity Pledges: Hotel Bossert Spotlights Dual Collateralized Loans,” CMBS Credit Focus, Academy Securities, February 23, 2023

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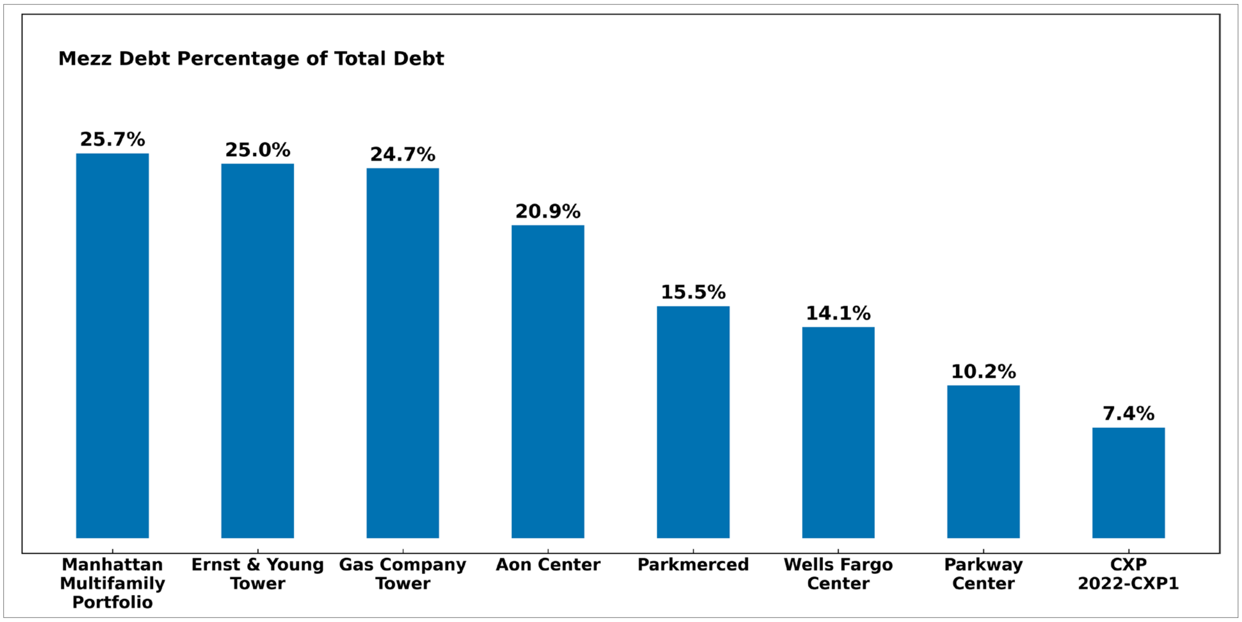
### Figure 1. Mezzanine Debt on Recently Delinquent or Specially Serviced Large CMBS Loans

| Loan Name | CXP 2022-CXP1 | Parkmerced | Aon Center | Gas Company Tower | Wells Fargo Center | Manhattan Multifamily Portfolio | Ernst & Young Tower | Parkway Center |
|---|---|---|---|---|---|---|---|---|
| Deal(s) | CXP 2022-CXP1 | MRCD 2019-PARK(1) | JPMCC 2018-AON(2) | GCT 2021-GCT | MSC 2019-NUGS | BX 2019-MMP | JPMCC 2019-FL12 | WFCM 2018-C45 |
| First Mortgage Amount ($MM) | 1,557.8 | 1,500.0 | 536.0 | 350.0 | 277.1 | 270.3 | 75.0 | 41.6 |
| Mezzanine Amount ($MM) | 125.0 | 275.0 | 141.5 | 115.0 | 45.3 | 93.3 | 25.0 | 4.7 |
| Special Servicer Transfer Date | Jan 2023 | NA | Feb 2023 | Feb 2023 | Dec 2022 | Jan 2023 | Dec 2022 | Nov 2022 |
| Current Maturity | Dec 2023 | Dec 2024 | Jul 2023 | Feb 2023 | Dec 2023 | Aug 2023 | Dec 2023 | Jun 2028 |
| Property Type | Office | Multifamily | Office | Office | Office | Multifamily | Office | Office |
| MSA | Various | San Francisco | Chicago | Los Angeles | Denver | New York | Cleveland | Pittsburgh |
| Most Recent Appraised Value ($MM) | 2,267.0 | 2,110.0 | 824.0 | 632.0 | 475.0 | 542.0 | 134.0 | 66.6 |
| Most Recent Appraisal Date | Oct 2021 | Sep 2019 | May 2018 | Nov 2020 | Oct 2019 | Jul 2019 | Sep 2018 | Mar 2018 |
| LTV Mortgage | 68.7% | 71.1% | 65.0% | 55.4% | 58.3% | 49.9% | 56.0% | 62.5% |
| LTV Mezzanine | 74.2% | 84.1% | 82.2% | 73.6% | 67.9% | 67.1% | 74.6% | 69.5% |

(1) Pari-passu loan components also included in MRCD 2019-PRKC, BBCMS 2020-C6, BBCMS 2020-C7, BMARK 2020-IG1, CF 2020-PG1, GSMS 2020-GC45, GSMS 2020-GC46, WFCM 2020-C56
(2) Pari-passu loan components also included in BMARK 2018-B4, BMARK 2018-B5 and BMARK 2018-B7

Source: MCIA and Academy Securities

### Figure 2. Mezz Debt Percentage on Recently Delinquent or Specially Serviced Large CMBS Loans




Source: MCIA, Bloomberg and Academy Securities

## Tracking Mezz Positions on CMBS Exposures

We suggest investors closely track mezz positions on CMBS exposures. The subordinate debt disclosures on deal documents can generally fall into three categories:

1. **Mezz debt in place at origination.** Investors will find the mezz positions in the prospectus, asset write-up, and Annex A. The challenge is typically collecting this information in a systematic manner. A dedicated IRP field (S89) would disclose if a loan has additional mezz financing (code “3”). But the field is part of the Loan Setup data file, which in our experience is not always readily available. Some cashflow systems do provide datasets or data feeds that appear to show mezz financing levels across all CMBS loans. To be sure, the mezz debt disclosures may not always reveal the identity of the mezz lender. Moreover, investors will usually find it difficult to track mezz positions over time. CMBS deal documents may not report the sale or payoff of the mezz positions, should any of those happen.
2. **Future mezz debt possible.** These are situations where the property capital structure does not have mezz position at the CMBS deal issuance, but the loan agreements permit future mezz debt. The sponsor will almost always need to satisfy a variety of conditions before taking on additional debt. This was the case for the $159 million 301 South College Street (WFRBS 2013-C13 and C14), that transferred to special servicing in January 2023 and matures in May 2023. The CMBS borrower on the 42-story office tower in Charlotte, NC, aka One Wells Fargo Center, requested a maturity extension, according to fresh servicer commentary. It is not clear if the sponsor incurred the permitted mezz debt since the loan origination in 2013, and the servicer comments are silent on this. Separately, a $16 million mezz position on The Distrikt Hotel that pulled the mortgage lender into court proceedings last year, apparently originated after the MSBAM 2012-C5 deal issuance. The deal documents noted that the borrower can obtain future mezz financing, but only a year after the mortgage closing, among other conditions.
3. **Mezz debt not permitted**. Many loans do not permit future mezz debt. The $120 million Charlotte Plaza (LNSTR 2017-4 and 5) is one example of recently defaulted large office loan that did not allow mezz debt. The loan on the 632k sf office property in Charlotte (a direct competitor of One Wells Fargo Center we mentioned above), defaulted at maturity in January 2023. The servicer is currently negotiating with the borrower, according to recent commentary.

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