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# CMBS Credit Focus

## Hotel Receiverships: Palmer House Hilton Spotlights Stabilization Efforts

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### Receivership Dynamics to Impact Loan Outcomes as Borrowers Pushed Aside

**The situation at Palmer House Hilton ($328.9 million, JPMCC 2018-PHH) could illustrate the value of receivership versus other workout approaches such as modifications or foreclosures.** The 1,641-room in Chicago, IL, is one of the most prominent cases of a receiver controlling a CMBS property. The loan defaulted back in April 2020 and transferred to special servicing ahead of its June 2020 maturity (Figure 1). The servicer opted for receivership in October 2020, as it evaluated resolution options. The receiver is now working with Hilton to stabilize the property's performance since the hotel re-opening in June 2021, following a pandemic-driven closure. The servicer is still negotiating with the original borrower, but is prepared to complete foreclosure within 60-day notice, according to fresh commentary released this week.

Figure 1. Palmer House Loan and Property Parameters

| Palmer House Hilton | | | |
|---|---|---|---|
| **Balance** | $328,933,823 | | |
| **Deal and Exposure** | JPMCC 2018-PHH | | |
| **Loan Type** | Floating-rate, interest only | | |
| **Maturity** | June 2020 | | |
| **Coupon** | 1ML + 2.4172% | | |
| **Loan Status** | Foreclosure (transferred to special servicing Apr-2020) | | |
| **Property Type / Size** | Full Service Hotel / 1,641 rooms | | |
| **Year Built / Renovated** | 1925 / 2014 | | |
| **Location** | Chicago, IL | | |
| **Financials** | YE 12/31/2019 (last reported) | Securitization (UW) | |
| **Net Operating Income** | $25,936,742 | $39,950,617 | |
| **DSCR** | 1.04 x | 1.46 x | |
| **Occupancy** | 76.0% | 82.0% | |
| **Debt Yield (Mortgage)** | 7.9% | 10.5% | |
| **Other Information** | **Appraisal History** | **Servicer Advancing** | **Additional Debt** |
| | $328.0 MM (Mar-2022) | P&I $26.3 MM | There is a $94.3 MM mezzanine loan outstanding, securitized in JPMCC 2018-PHMZ |
| | $310.0 MM (Jun-2021) | T&I $0.0 MM | |
| | $305.5 MM (Aug-2020) | Other $14.7 MM | |
| | $560.0 MM (Apr-2018) | Adv Int $2.3 MM | |

Source: MCIA and Academy Securities

**The market may see servicers increasingly employing receivership on troubled situations, especially with borrowers showing no interest or less commitment to their properties.** Servicers clearly have been inclined to cooperate with committed borrowers during the pandemic.[1] Forbearance agreements and modifications usually were the preferred workout approach. But as special servicing volume tick ups, and potentially becomes more adversely selected, servicers will likely need to deal with deeper distress cases. Keeping the borrower in control of the property in such cases, even if the borrower is interested in sticking around, may not be the ideal approach. The special servicing rate rose in October for the third-straight month, reaching 5.26% ($31.4 billion), according to DBRS Morningstar. Office saw the largest YoY increase in SS transfers among property types, rising 174bp to 3.95%. Shifting tenant demand, early termination options, and property obsolescence would clearly put a spotlight on workout alternatives.[2]

## Receivership More Appropriate for Hotels, Non-cooperative Situations

**The use of receiver may introduce a few aspects that could impact the ultimate recovery on troubled loans:**

- **Stabilizing operations.** Receivership may be especially appropriate for properties that require intensive day to day operation. As such, hotels often make good receiver candidates, according to market participants. A key aspect a receiver may need to manage is the hotel's franchise agreement, as is evident in Palmer House. The receiver reports in Palmer make repeated references to the relationship with Hilton. The 10-year management agreement expires in December 2025, and has two 10-year renewal options.

- **Control of the cashflow.** One concern with using receivers for property operations in lieu of the original borrower is that the receiver may not be as familiar with the property, or lack the management expertise of the existing operator. However, receivers may be particularly appropriate when the borrower is not motivated, and there is an urgent need to get the management of the property out of their hands. If the servicer is also interested in getting control of the cashflow as soon as possible (perhaps because there is a concern over misappropriating cash), it may add to the urgency of appointing a receiver. Conversely, if a hard lockbox is in place, or if the borrower is cooperative, it may alleviate the need for a receiver.

- **Receivership sale.** Receivership may delay the actual property foreclosure and any potential loss realization. Indeed, in some situations, servicers may not be interested in taking title of the property. Taking title crystalizes losses, and exposes the servicer/lender to potential liabilities. Further, a receiver sale may facilitate seller financing, which REMIC rules do not allow in case the trust takes title of the property. As such, servicers may prefer to recapitalize existing debt through receiverships, especially amid an elevated coupon environment. Still, until the trust executes a foreclosure, junior lenders with potentially competing interests, may continue to be part of the property's capital structure. Palmer House had a $94.3 million mezzanine position at issuance, that remained in place as of last month, according to the servicer.

1 Mall Foreclosures: What to Track as Servicers May Shift Away from Modifications, CMBS Credit Focus, Academy Securities, March 1, 2022

2 Office Modifications: 285 Madison Could Offer a Blueprint for More to Come, CMBS Credit Focus, Academy Securities, October 27, 2022

## Identifying Receivership Loans Requires a Bit of Sleuthing

**Consistently identifying CMBS properties in receivership unfortunately appears to be a challenge.** A dedicated IRP field that indicated a loan's receivership date (field #54 in the special servicer loan file) seems to have been phased out. In turn, "appointment of receiver" is one of the formal reasons for special servicing transfer (item "E" in IRP field L127). But we have found only a handful of small loans among the active specially serviced universe where appointment of receiver was the transfer reason (Figure 2). This may not be surprising. We would typically expect loans to transfer to special servicing for reasons such as imminent term default or balloon/maturity defaults; Receiver appointment would follow the transfer, rather than instigate it.

Figure 2. Sample of CMBS Loans in Receivership

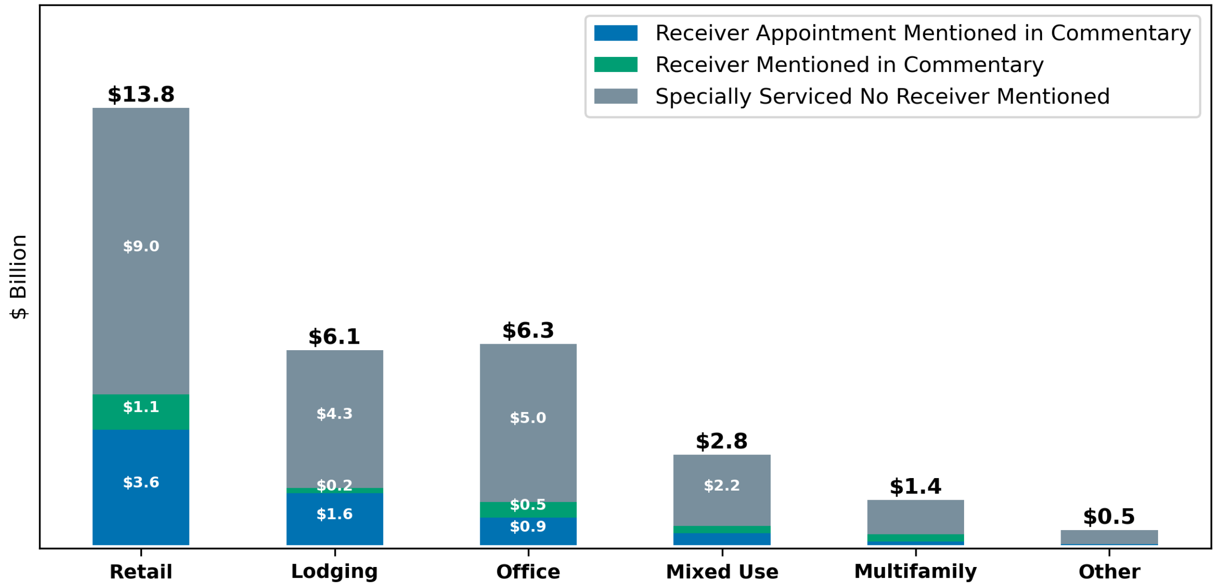
| Loan | Deal | Balance ($MM) | Maturity | Location | Property Type | DQ Status | SS Transfer | Reason for Transfer |
|---|---|---|---|---|---|---|---|---|
| Clinton Crossings Medical Office | CGCMT 2017-B1 | $9.1 | 8/1/2027 | Rochester, NY | Medical Office | Current | 9/20/2021 | Appointment of Receiver |
| 1049 5th Avenue | BANK 2021-BN31 | $4.5 | 1/1/2031 | New York, NY | Medical Office | Current | 8/4/2021 | Appointment of Receiver |
| Drexel Apartments | WFCM 2014-LC16 | $2.0 | 5/1/2024 | Chicago, IL | Garden Multi | 90+ Days | 9/14/2018 | Appointment of Receiver |
| The Shoppes at Buckland Hills | MSC 2012-C4 | $105.9 | 3/1/2022 | Manchester, CT | Regional Mall | Perf Mat | 10/29/2020 | Imminent Monetary Default |
| Harborplace | UBSBB 2013-C5 | $60.8 | 12/1/2022 | Baltimore, MD | Urban / Street Retail | 90+ Days | 2/15/2019 | Payment Default |

Source: MCIA and Academy Securities

**All told, it appears that investors are mostly left to identify receivership loans anecdotally via news feeds or servicer commentary.** A couple receivership situations that popped up include The Shoppes at Buckland Hills ($105.8 million, MSC 2012-C4) and Harborplace ($60.6 million, UBSBB 2013-C5). In Buckland Hills the special servicer and the borrower agreed in mid-2021 to a consensual receivership on the 535K sf mall in Manchester, CT, after they couldn't reach an agreement on other workout approaches. The mall just reported its value plummeting to $59.9 million, compared to $189.0 million appraisal at issuance. In Harborplace the receiver has been operating the lifestyle retail center in Baltimore, MD, since May 2019. Recent servicer commentary indicates that the receiver has now found a buyer for the property that will assume the loan, which matures next month.

**Beyond the anecdotal cases of receivership, we also attempted a more systematic search in servicer commentaries for indications of receiver appointment or consideration across 874 specially serviced loans.** We found 268 cases where servicers likely considered receivership as a workout approach, and 204 loans where there is a strong indication the servicer ended up appointing a receiver. About 36% of these specially serviced loans are retail, followed by 30% hotels (Figure 3). A full list of the receivership loans is available upon request.

Figure 3. Receivership in Servicer Commentary, by Property Type




Source: MCIA and Academy Securities

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