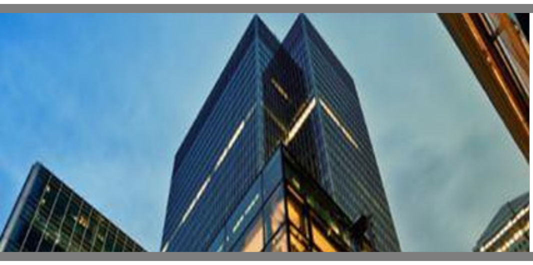
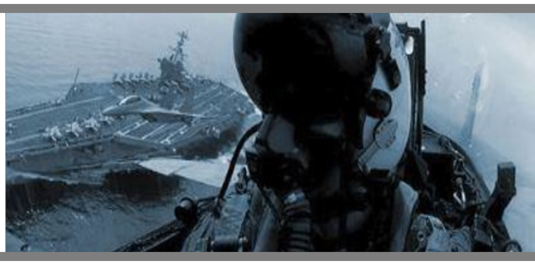
CMBS Credit Focus

Special Servicer Replacements: 1740 Broadway Crystalizes Implications





Frequent Special Replacements Could Shift Workout Directions

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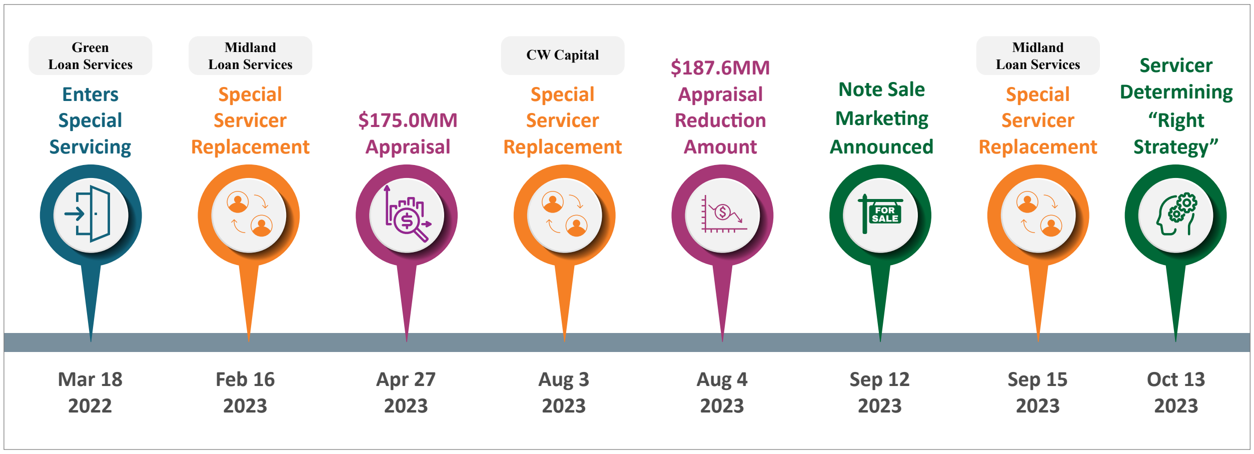
We expect a rising frequency of special servicer replacements, as the rights to terminate servicers and appoint new ones shift across the capital structure. Such replacements could have significant consequences on loan workouts and bond cashflows. The closely-watched $308 million 1740 Broadway (BWAY 2015-1740) just crystalized the implications of special servicer replacement. As Midland succeeded CWCapital as special last month following bondholders vote, the imminent note sale on the beleaguered Manhattan office building is apparently no longer in motion.

To be sure, the complexity of the 1740 Broadway workout, and limited availability of public documents on the note sale, make it hard to conclusively tie the special replacement to the note sale cancelation. But the rapid replacements of the specials on 1740 Broadway in recent months (three in total), and the varying classes that directed those replacements, underscore that investors should not expect continuity (or clarity) on handling troubled loans as specials changeover (Figure 1).

Figure 1. 1740 Broadway Special Servicer Replacements



Source: Deal Documents and Academy Securities

Special Servicer Appointment Rights Shift to Senior Bondholders

As highly distressed new appraisals increasingly "appraise out" subordinate bonds, senior bondholders will be gaining special servicer appointment rights. Deal documents typically give directing holders the right to terminate and appoint special servicers as long as the directing holder's class balance remains above 25% of the initial balance. In addition to actual writedowns, appraisal reduction amounts ("ARA") also reduce the class balance for control calculations. In BWAY 2015-1740, class E originally had special servicer appointment rights. The class so-called "subordinate control period" ended once a large ARA hit the deal in August 2023 (Figure 2). This shifted the appointment rights to a voting-based mechanism, according to deal documents.

Figure 2. 1740 Broadway Loan and Property Parameters

Asset	**1740 Broadway**			
Deal	BWAY 2015-1740			
Loan Balance ($psf)	$308,000,000 ($510 psf)			
Maturity	January 2025			
Coupon / Amortization	3.84% fixed / Interest-only	Appraisal History	Total Advancing (as of 9/2023)	
Loan Status	90+ Days Delinquent & Specially Serviced	$175.0 MM (Apr-2023)	Principal & Interest:	$9.7 MM
Property Type	Office	$605.0 MM (Dec-2014)	Taxes & Insurance:	$5.4 MM
Property Size / Occupancy	603,928 sq. ft. / 7.4% occupied (Sep-2023)		Other:	$19.7 MM
Location	New York, NY		Unpaid Advance Interest:	$1.7 MM
	Corner of Broadway and 56th Street		Total Advances & Interest:	$36.5 MM

Source: MCIA and Academy Securities

After the subordinate control period ends, >75% of the bondholders or >50% of each class can direct special servicer replacement.[1] This exactly played out in BWAY 2015-1740. In July 2023 the directing holder appointed CWCapital as special, terminating Midland's appointment (just five months earlier, in February 2023, Midland had replaced the deal's original special, Green Loan Services). Then, in mid-September 2023, after a $187.6 million new ARA appraised out the directing holder, senior bondholder vote directed the trust to terminate CWCapital, a little over a month after its appointment.

Midland is now working to determine the correct approach to managing the property and the loan's workout approach, according to just-released servicer commentary. The fresh commentary no longer mentions "wide marketing" of the note, a significant development that popped up last month. The 1740 Broadway's note sale, posted on R Marketplace auction website a few weeks ago, is no longer there. Morningstar commentary also indicated that the servicer scrapped the planned note sale. 1740 Broadway may now be heading towards REO status, according to the rating agency.

1 We greatly simplified the description of the voting-based special servicer replacement mechanism. Deal documents describe in great detail this mechanism, which depends on elaborate definitions of "voting rights", "certificateholder quorum" and other nuances.

Tracking Special Servicer Replacements

Recent special servicer replacements we identified have been directed by controlling holders, unlike the latest one in 1740 Broadway. Examples include replacements in BX 2021-MFM1, ONYP 2020-1NYP, and COMM 2013-CCRE7. The market may widely expect special replacements as control shifts from one subordinate class to another, or across controlling holders on the same class. But projecting the timing or tracking such replacements appears to be a challenge. We continue to see cases of delayed appraisals and ARAs on troubled loans, which may trigger control shifts.[2] Even when a new appraisal is imminent (perhaps based on servicer commentary), it is not clear if control will shift, and to which class.

When replacements do happen, investors may need to do some sleuthing to identify their occurrence, and the identity of the new special. To be sure, the IRP package provides extensive guidance on special servicer transfers. A whole slew of documentation should accompany special replacements, including replacement notices, rating agency opinions (so-called "RACs"), "Goodbye" and "Hello" letters, and so on. But we found it challenging to consistently track special replacements via IRP fields and data feeds. Additionally, it may not always be clear what drove the replacement – ARA-driven change of control, controlling holder changeover unrelated to an ARA event, or something else.

2 "Triple-A Shortfalls: Destiny Spotlights Delayed ASERs Impact," CMBS Credit Focus, Academy Securities, September 20, 2022

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