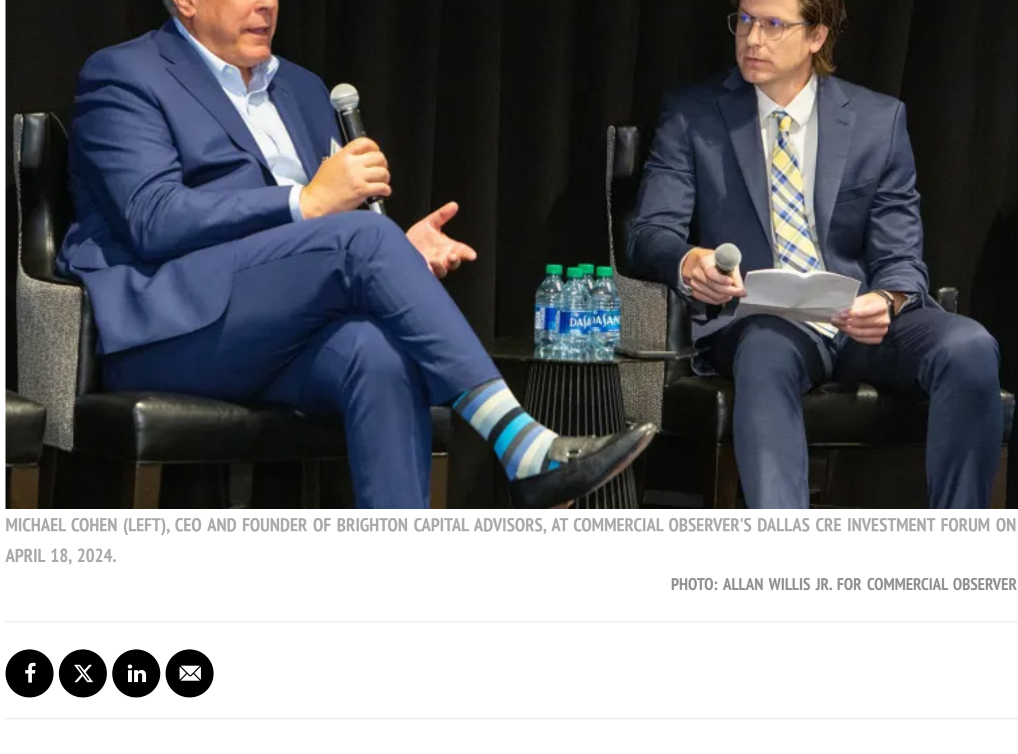
Michael Cohen's Brighton Capital Ushers CRE Borrowers Through Loan Servicing Era

'There's no dramatic interest rate change that's going to come that's going to save everybody'

BY GREG CORNFIELD APRIL 30, 2024 3:00 PM | REPRINTS



MICHAEL COHEN (LEFT), CEO AND FOUNDER OF BRIGHTON CAPITAL ADVISORS, AT COMMERCIAL OBSERVER'S DALLAS CRE INVESTMENT FORUM ON APRIL 18, 2024.
PHOTO: ALLAN NILLY JR FOR COMMERCIAL OBSERVER

As one can imagine, the relationship between borrowers and lenders — and subsequently special servicers — can be fraught with stress and anxiety in a new era of rising defaults, devaluations, and landlords giving back the keys to major assets.

Michael Cohen (not to be confused with that Michael Cohen, or with Colliers' Michael Cohen) launched **Brighton Capital Advisors** when he recognized the growing need for deal restructuring, workouts and recapitalization solutions. His firm helps borrowers navigate unfamiliar territory: distress.

Cohen, who is based in Charlotte, sat down with Commercial Observer at CO's commercial real estate investment forum in Dallas on April 18, and talked about the importance in understanding the sometimes tedious intricacies of CMBS loan servicing workouts, including modifications, extensions, discounted payoffs, and how to release cash trapped by the servicer.

This interview has been edited for length and clarity.

Commercial Observer: Tell us about yourself and about your team: What challenges are you dealing with as the market volatility continues?

Michael Cohen: Brighton Capital Advisors is comprised of people that just recently left the CMBS industry, from every facet of origination to loan closings and special servicing. We've all talked about the distress in the marketplace, and there are a lot of complications from the borrower's point of view to go through it, because there are a number of parties that they're not privy to speaking directly with. And there's a lot of tax and other fee implications that go with modifying loans.

Can you give us some examples of the deals you're seeing in the marketplace?
We're seeing a range of requests. We started this business three years ago during the COVID-19 pandemic, and we started getting requests for extensions. One example was an owner had a property in Midland, Texas, that was coming due and he needed an extension.

By going to the servicer, explaining to them why he was the best person and operator to continue to shepherd the property through, to show them where his fresh equity was coming in, and show a business plan, we were able to effectuate the change.

The key to servicing and special servicing of CMBS is communication. Lenders are creatures of consensus building, and in order to do that, you have to provide them with the information that they need to socialize the deal amongst the different parties — the master servicer and the special servicer.

Another example would be a deal we worked on in Houston. It was a two-story retail center, and the fitness center tenant left during COVID. The owner brought in a better fitness center tenant for a longer term, and brought in two restaurants, and leased it up to 100 percent. But, in order to do this, the investors wanted to make sure the lender wasn't going to take the property away while these tenants were getting in. So we had to do an extension.

Other extremes: We're doing a modification on 2 million square feet in two contiguous towers in Chicago. The value has dropped significantly, but we have a borrower that's strong that's willing to come with equity. So, we're in discussions with the servicer right now on different plans of creating an A-B note structure or some other structure that will entice the equity to come in.

There's nothing programmatic going on right now, so it requires people who are experienced in this. The people on my staff have been working 15 to 25 years in special servicing realms of Wells Fargo, to loan closings and workouts at Bank of America, to Fitch Ratings agencies and securitization at Citi and Barclays.

Why are you so focused on CMBS and CLOs vs. everything else?
I started in CMBS in 1991 at DLJ. We started First Financial, we were closing loans at the same time as securitizing them. I understand it very well. I moved to Charlotte to start the program at First Union in 1996, and then started to cover the Southeast for my clients. Since then, I've worked CMBS finance for Deutsche Bank, Allegiance, UBS and Citi.

The borrowers need a representative. And the way that we work with the borrowers is we work with them and their attorneys and their tax consultants. The borrower needs all three of those parties to opine on what to do.

And CMBS is effectively going to a pawn shop where it's stacked against you.

So, we tell everybody, "Don't wait to go in to talk to the servicer, don't try to rush yourself into special servicing, it will not benefit you."

The key is to communicate. And, when we talk to attorneys, they tell us, "These are the weaknesses of the recourse carveouts, these are your strengths." And your tax consultant tells you what you can and can't do with these certain strategies. Then we can communicate on your behalf and keep it on a business level.

There have been a lot of negative headlines around special servicing transfers and around the borrower perspective of CMBS. The other side of the table is rather opaque. What are you hearing from master and special servicers when it comes to their handling of workouts
The headlines are true: Borrowers do not have power with these special servicers. Once you get into special servicing, you're going to start to incur fees. And you're under their control. So, if it's a maturity default, they'll immediately start the foreclosure process and then start to talk to you to see what your action plans are.

There's no relationship at all. So, the relationship that you have to form is to establish that the borrower is the best representative to go through and take this asset to the next side.

CMBS servicers, the majority of them do not want the loan back. It doesn't benefit the trust at all. You're in a better situation if you extend and get this loan performing and paid off in a couple of years. In order to do so, you need equity.

What our job is, is to create transparency in the process so that we can identify who the parties are that are going to be spoken to. We don't speak to everybody. We'll speak to the master and special, but we're not going to speak to the controlling class holder who's the lowest member on that bond.

You have to realize that there's bond warfare. You'll get responses that are not logical because it's benefiting the lowest class holder because maybe they want to hold the loss and buy up the tranches.

So, our job is to replicate what's going on, create prepackaged workouts that have all the needs of the borrower in it that are beneficial to optimal results within their framework. And that's why they like us, because it's a collegial relationship. Servicers understand that we have the borrower's best interest, but they also understand that we've discussed with them and their attorneys what can and cannot be done. So there's a deal to be had.

You were recently at a servicer symposium in Charlotte. What were the major takeaways that you can share?
What's amazing is the servicers and special servicers have the same complaints that the borrowers have. And you're thinking, "Well, wait a second."

The first complaint the servicers will all say across the board is, "Why are borrowers coming to us so late with their action?" Servicers don't understand — they're not in real estate the same way as landlords. I'm a former lender; I have no idea how much this lightbulb costs, I don't understand how much it is to operate a building, and I don't understand for multifamily properties how much it is to cut a lawn. But you guys do.

So, borrowers who are waiting for the lender to create a loan modification or work out a deal for you: you're going to get the most draconian thing that you can possibly imagine. It's, "Pay me down and pay me down."

What lenders and servicers like is lead time. You're giving them a plan, and you're helping them to understand.

People complain about master servicers and how inefficient they are; and they are. They've admitted it. They said on the panel, "Look, we don't make a lot of money doing this, we're not investing in technology." So it's a very cumbersome process.

We try not to go to the top of the food chain to get the decision-making. We go through the process. We provide all the documentation, we provide all the support, we provide all the analytics, and most borrowers don't understand it.

If you get the lawyers on the phone, then the lender is going to get their attorney on the phone. As a former banker, you tend to stay away from those calls, so you lose the business people on the deal. Our goal is to keep the business people in the conversation.

Office defaults and transfers have comprised the bulk of the negative headlines and news. From your perspective, are those headlines misguided, or do you expect the doom loop to continue?
I expect it to continue based on what I've seen. I'm based in Charlotte, I was just in San Francisco, I was in New York last week, I was in Miami the week before. I'm heading to Chicago again in two weeks, and I'll be in L.A. The crisis is everywhere.

It is equivalent to the residential crisis in 2010: Just like before, if you have a beautiful mansion in Turtle Creek (neighborhood in Dallas County) you're thinking it's not going to be affected. But if the two houses on either side of you are getting devalued, you're going down in value.

These are great questions about where we think interest rates are going, but these are drops in the bucket. There's no dramatic interest rate change that's going to come that's going to save everybody.

When I talk to borrowers and they say, "Well, we're hoping that interest rates come down," or, "We're hoping the government's going to come in and save us and give us some TARP (Troubled Asset Relief Program) money." It ain't happening. The government could have done that during COVID. They didn't.

This is going to be a very slow wave. But it's going to come. As soon as somebody at a bank decides to capitulate, and starts to dump out loans, everybody will start doing it. The government tried not to have that happen, in my opinion. But at some point somebody's going to do it.

I think the office market is there. There are definitely buildings worth keeping. If you have a plan and you have money, you can do it. Some don't, though.

But my eyes are on the multifamily. Also, there's a number of assets that are just going to get caught up in this non-financing period. The regional banks are cold. The insurance companies are being very selective. Conduit lending is very strict.

It's the best time to buy CMBS bonds ever. Just like after 9/11 and after 2008: Whenever there's a crisis, you can get conservative again.

But the issue is that you've got good buildings that maybe have one year left on their loan terms or their lease terms, and they're just not going to find a home. So there's good opportunities everywhere to buy. There's good opportunities everywhere to invest.

Is multifamily the next issue that you're worried about after office?
Yes. Once the borrower decides that they don't want to buy the interest rate hedge, then game on, because now you have a problem. It's as simple as that.

It's not a question of operation; multifamily business is fine. It's just a leverage point that's too high for a value add that was predicated on having a 3 to 4 percent coupon as an exit with rent growth and not a lot of expense growth. It's just overleveraged. So somebody is going to have to take a loss.

And it's not like where an office loan can sit there for months, and you can just kind of kick around. I don't know what the CLO lender is going to do once they don't have a borrower who's not willing to put in a couple of million dollars of a sunk cost.

You've transacted through major crises before. What are some of the key differences you're seeing in borrower and lender behavior in this period?
There's not a liquidity crisis. So, unlike 2007 to 2010, where there was a liquidity crisis, banks are well capitalized today. This time around, it's going to be a transfer of assets.

If you recall, in 2010, when everything really started to get devalued, and there were really big problems, we really didn't see assets start to really trade until 2012. So, if last year was the pregame warmup, I think now we're getting into maybe the first batter walking up to the plate. This is going to take time.

There's no reason to rush it. But there's somebody who's going to have to take a loss. And it's just the question of who and when. And I have plenty of borrowers who have balance sheet loans — they're trying to give the keys back on $100 million deals in downtown Minneapolis, and the lender won't take it back, and they're going to try to force the recourse. So it's gamesmanship, and as a borrower you better be prepared for the worst.

It could be as simple as your loan getting sold to somebody else, and them calling you up and saying, "How do you want to handle this?" They're selling one by one right now.

Do you have any bold predictions for the rest of the year and moving forward?
Yes, it's going to get worse.

After this transfer of assets and the resetting of bases, then we can start to think about how cities are going to take the properties that aren't able to attract the tenants, and then repurpose them. And then use government incentives to bring in tenants that will create vibrancy in the marketplace.

It could be in the form of immersive AI and creative arts. It could be in the form of saying, "Hey, Armani, come wrap this building and we'll create a design center around you."

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