

Operational Risk Assessments News Bulletin

C-III Asset Management LLC

Morningstar Affirms C-III Asset Management LLC's 'MOR CS1' Commercial Mortgage Special Servicer Ranking; Ranking Forecast Remains Stable

Morningstar Credit Ratings, LLC (Morningstar) has affirmed its 'MOR CS1' ranking on C-III Asset Management LLC (C-III) as a commercial mortgage special servicer. The forecast for the ranking remains Stable. The affirmed ranking and Stable forecast reflect our assessment of C-III's operational infrastructure and portfolio administration capabilities as a special servicer.

In particular, Morningstar's ranking and forecast are based on these factors:

- Highly Experienced Management and Asset Management Teams - Morningstar's view that C-III's management and asset management teams are highly experienced in resolving complex distressed assets, and our favorable view of the company's recent hiring of a well respected special servicing industry veteran to head business development in the U.S. and in Europe.
- Accurate and Timely Reporting - Our view of C-III's capabilities to provide accurate and timely reporting, its responsiveness to information requests, the overall quality of its asset-level reporting content, and its website functionality. We also formed this opinion based on our review of selected Morningstar-published DealView® CMBS surveillance reports.
- Excellent Recovery Results with Challenging Assets - Over the past year, C-III resolved nearly 40% of the loans and more than one-third of the REO assets held in its inventory longer than 180 days, while achieving overall successful net recoveries on loan and REO liquidations. Morningstar calculated that C-III's net proceeds-to-value on REO liquidations averaged 97% and its net proceeds-to-value on loan liquidations averaged 94% in 2011 and 2012.
- Extensively-Controlled Asset Management and Effective Audit Function - Morningstar believes that C-III has diligent practices and procedures for highly controlled asset management to mitigate risk and minimize losses to investors. In our view, the company's audit practices also are extensive and encompass not only Regulation AB and USAP attestations, but also quarterly self-administered, yet independent, internal audits that test special servicing compliance with pooling and servicing agreements and C-III's own policies and procedures.
- Highly Transparent Asset Resolution Practices and Sound Conflicts of Interest Management - Our positive view of C-III's efforts to help create standardized templates for disclosing asset resolutions within the most recent version of the CREFC Investor Reporting Package. We believe that C-III adheres to a transparent process of disclosing potential conflicts of interests to outside parties as demonstrated by its continual presentations to the investor/research analyst community. C-III is affiliated with the controlling bondholder class on CMBS transactions for which it is the named special servicer. Although C-III, through its affiliate, has exercised its option on a few occasions to purchase loans out of the CMBS trust and continues to use affiliated entities for the workout and liquidation of some assets, we believe that C-III's recovery results indicate that it has minimized realized losses to affected trusts. Furthermore, we believe that C-III continues to make a strong effort to fully disclose its business cases substantiating such decisions to exercise asset purchase options and use affiliates to CMBS trustees, rating agencies, investors, research analysts, and other interested parties.
- Continued Outreach to Investors and Industry Participants - Our favorable opinion of C-III's continuing efforts to reach out to investors and research analysts to inform them about the company's asset management approach and to obtain feedback from the investor/analyst community concerning C-III's asset resolutions.
- Excellent Technology Platform, including Upgraded Asset Management System - Our positive view of the company's recently upgraded asset management system, LoanSStar Platinum, which CIII enhanced with added functionality and design features. LoanSStar Platinum is integrated with CIII's existing due diligence and surveillance system, which together provide a high degree of centralized data management and automated reporting.

- **Sufficient Capacity to Perform Special Servicing Functions** - Based on Morningstar's calculation of C-III's assets-to-asset manager ratio, the company appears to have sufficient staff resources to keep pace with its recent asset transfers. In fact, its overall ratio of assets-to-asset manager decreased from 12:1 as of June 30, 2012, to 9:1 as of December 31, 2012. The decrease in the overall ratio indicates that the company may have some excess capacity. However, we also observed an increase in the ratio of REO assets-to-asset manager between 2011 and 2012, as well as a corresponding increase in REO sale hold times during the same periods. The company reported that it recently segregated the REO department into two teams, asset management and REO sales, in order to manage higher REO volumes more effectively and liquidate the assets in a timely manner. The company also informed Morningstar that it will continue to reallocate internal resources to improve upon capacity metrics. As such, we will continue to monitor the company's REO asset management workloads and time to liquidate REO assets.

As of December 31, 2012, C-III's active special servicing portfolio was approximately \$11.8 billion consisting of 737 assets (compared to \$12.9 billion consisting of 932 assets as of June 30, 2012), which represented almost a 9% decrease in unpaid principal balance (UPB) and a 21% decrease in the number of assets from June 30, 2012. During the first half of 2012, C-III's asset resolutions were equivalent to approximately 45% of the specially serviced loans by loan count and 36% of the REO assets by property count that it held as of January 1, 2012. During the second half of 2012, its resolution volume was equivalent to approximately 57% of the specially serviced loans by loan count and 54% of the REO assets by property count that it held as of July 1, 2012.

Forecast

Stable. We expect C-III will continue to be a highly effective special servicer for its investor clients. Given the extent to which the company uses affiliates to purchase and sell assets, we will continue to monitor C-III's involvement of affiliates in its asset resolution activities and how its use of affiliates affects the company's overall asset recovery results.

Our full assessment report on C-III is forthcoming and will be made available on our website.

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