

Operational Risk Assessments News Bulletin

KeyBank Real Estate Capital

Morningstar Affirms KeyBank Real Estate Capital's 'MOR CS1/Stable' Commercial Mortgage Primary and Master Servicer Rankings; Raises Commercial Mortgage Special Servicer Ranking to 'MOR CS1/Stable'

Morningstar Credit Ratings, LLC (Morningstar) has affirmed its 'MOR CS1' commercial mortgage primary servicer and commercial mortgage master servicer rankings on KeyBank Real Estate Capital (KBREC), a subsidiary business unit of KeyBank, N.A. Concurrently, Morningstar has raised its commercial mortgage special servicer ranking on KBREC to 'MOR CS1' from 'MOR CS2'. The affirmed primary and master servicer rankings and the raised special servicer ranking reflect our assessment of KBREC's operational infrastructure and portfolio administration capabilities for its respective duties as a primary, master, and special servicer. The forecast for each ranking is Stable.

Our assessment and assigned rankings are based on the following composite factors:

Primary and Master Servicing

- Investor Reporting Expertise - Our view of KBREC'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, which addresses both CMBS and non-CMBS client requirements. Based on our review of selected Morningstar published DealView® CMBS surveillance reports, we found KBREC's reporting content to be quite sound.
- Proactive and Controlled Asset Administration - Our positive opinion of KBREC's CMBS primary and master servicing asset administration capabilities and expertise for a broad range of large and complex transactions. In addition, we believe that KBREC has a high degree of experience and an overall successful performance record as a CMBS master servicer with respect to pooling and servicing agreement (PSA) compliance, cash management and monthly reporting, diligent advance determination procedures, enhanced sub-servicer oversight and audit practices, and meeting its specific service level agreements.
- Excellent Technology - KBREC's excellent technology tools, sound data security and disaster preparedness protocols, high level of automation, and centralized data management to accommodate a diverse and large servicing portfolio while also yielding a high degree of operating efficiency. In particular, we believe the company's proprietary, integrated asset management and reporting application, called RECWeb, is highly effective for workflow management, tracking loan-level covenants and trigger events, and handling many other core functions with customized features to address CMBS and other investor reporting requirements in tandem with its main servicing system, which KBREC plans to upgrade this year.
- Strong Management and Professional Depth - KBREC's overall operational stability and its retention of a highly experienced management and professional staff. While KBREC incurred a sharply higher staff turnover rate in the first half of 2012, almost all of it involved lower-level staff and was associated with the shared servicing agreement that KBREC entered into with Berkadia Commercial Mortgage, LLC (Berkadia) in March 2012. Through this agreement, KBREC transferred nearly all primary servicing duties on approximately \$40 billion (about 4,500 loans) of its CMBS servicing portfolio to Berkadia. KBREC does not outsource servicing functions and it centralizes nearly all primary, master and special servicing operations in one location. We also believe that KBREC operates with a well-designed organizational structure that addresses its myriad servicing requirements efficiently.
- Robust Internal Audit Program - KBREC's multi-faceted internal audit program that encompasses annual Regulation AB and USAP attestations, annual operational audits conducted by the parent bank, and an annual Service Organization Control 1 Report (SOC 1) that collectively examine a broad range of loan administration and portfolio management processes. KBREC supplements its audit function with various performance tracking activities embedded in the company's technology applications and daily workflow practices. KBREC's dedicated compliance unit monitors these

tracking activities. The 2012 Regulation AB and USAP attestations did not cite any exceptions. In our view, neither the parent bank's December 2012 audit report, which assigned KBREC its highest rating, nor the 2012 SOC 1 cited any major exceptions.

- Effective Portfolio Management - KBREC's practices and procedures for proactive asset-level management and portfolio oversight, which include a number of reporting tools managed through the proprietary technology application, to monitor collateral performance, track loan covenant compliance and trigger events, and manage borrower requests.

Special Servicing

- Excellent Asset Resolution Record - Our belief that KBREC is an effective special servicer having a diligent and pragmatic approach, sound analytics, and a corresponding successful asset resolution record based on recovery proceeds and overall timeframes. While much of KBREC's special servicing work has involved smaller balance and multifamily assets, and its volume may be viewed as moderate compared to some other special servicers, our raised ranking recognizes KBREC's extended asset resolution track record, which has included many larger-scale loans of varying complexity and property types and problematic FDIC assets. Additionally, Morningstar recognizes KBREC's proactive and successful efforts in completing a number of large scale CMBS loan workouts with excellent outcomes that also obviated the need for formal special servicing transfers.
- Expanding Client Base - Our view that the FDIC's recent renewal of its asset resolution flow contract with KBREC and KBREC's procurement in late 2012 of a separate servicing and asset management assignment with another government sector client are both testaments to KBREC's special servicing capabilities. We also acknowledge KBREC's five new special servicer appointments from Freddie Mac and KBREC's appointment as the replacement third party special servicer on a 2007-vintage CMBS as further indications of investor confidence in KBREC during 2012.
- Effective, Well-Designed Technology - In our view, KBREC's RECWeb application also serves as a highly effective and thorough asset management and reporting tool for specially serviced assets.
- No Discernible Conflict of Interest - Our belief that KBREC has effective policies and procedures to manage conflicts of interest. Overall, we generally view KBREC as a special servicer that operates without the potential conflicts of interest inherent in transactions in which the special servicer has a close affiliation with the CMBS B-piece investor. KBREC's business model is to act as an independent, third party special servicer without any investment in subordinate CMBS. In addition, KBREC does not have or use affiliates to purchase or sell assets within securitization trusts.

As of December 31, 2012, KBREC's total primary and master serviced portfolio was approximately \$101.6 billion by unpaid principal balance (UPB) and 10,972 by loan count, and it was the primary and/or master servicer on 146 CMBS transactions. CMBS loans accounted for approximately 62% and 63% of KBREC's total primary and master serviced portfolio based on UPB and loan count, respectively.

As of December 31, 2012, KBREC's total active special servicing portfolio was approximately \$1.17 billion by UPB and 610 by asset count (606 loans and 4 real estate owned properties). The CMBS component comprised 97 active assets with a UPB of \$394.7 million (93 loans and 4 REO). KBREC was the named special servicer on 25 CMBS transactions (\$9.5 billion by UPB consisting of 1,737 loans).

Forecast

Stable. We expect KBREC to continue serving as a highly effective primary, master, and special servicer and expect all three rankings to remain unchanged during the next 12 months.

Our full assessment report on KBREC is forthcoming and will be made available on our website.

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