

Operational Risk Assessments News Bulletin

Berkadia Commercial Mortgage, LLC

Morningstar Affirms Berkadia Commercial Mortgage Primary and Master Servicing Rankings at 'MOR CS1' and Lowers Its Commercial Mortgage Special Servicing Ranking from 'MOR CS1' to 'MOR CS2'; Forecast for All Rankings is Stable

Morningstar Credit Ratings, LLC (Morningstar) has affirmed its commercial mortgage primary servicer and commercial mortgage master servicer rankings on Berkadia Commercial Mortgage, LLC (Berkadia) at 'MOR CS1' and has lowered its ranking on Berkadia as a commercial mortgage special servicer from 'MOR CS1' to 'MOR CS2'. The affirmed primary and master servicer rankings and the lowered special servicer ranking reflect our assessment of the company's operational infrastructure and portfolio administration capabilities for its respective duties as a primary, master, and special servicer. Our assessment and rankings are based on the following composite factors:

Primary and Master Servicing

- Successful Systems Integration and Transfer of Assets - In its role as subservicer to KeyBank, Berkadia successfully converted the former Bank of America commercial mortgage portfolio to its servicing platform. The transfer of assets involved migrating data from Bank of America's *Enterprise!*-supported servicing system to Berkadia's servicing system which uses McCracken's Strategy servicing technology. In our view, the conversion was complex as it involved two unique servicing systems with significantly different architecture. However, Berkadia was able to complete this large-scale conversion in 45 days. We believe that Berkadia completed the conversion without any significant operation disruption, and that the company continued to provide accurate, timely reporting, and high quality servicing during the conversion period. The company reported that it achieved a 99% accuracy/timeliness score in accordance with its Servicing Level Agreement with KeyBank in connection with the conversion.
- A Long History and Highly Effective Use of Offshore Operations for Balance Sheet and Third Party Servicing - Our opinion that Berkadia operates very effectively through a fully integrated organizational structure, consisting primarily of its servicing headquarters in Horsham, PA and an offshore facility provided through its subsidiary, Berkadia Services India Private Limited (BSIPL), based in Hyderabad, India. During 2013, the servicer continued to increase its BSIPL staff, expanding their primary and master servicing involvement to support an increase in portfolio volume. BSIPL tasks are generally non-credit decision-oriented with very limited and scripted email communication with borrowers. Morningstar continues to monitor both Berkadia's ability to provide quality servicing as it increasingly uses BSIPL staff for servicing tasks, and the degree to which BSIPL staff have become increasingly acclimated and trained in their respective duties and workflows.
- Strong Management and Professional Depth – We believe that the company continues to operate with highly experienced management and professional staff.
- Expertise as a Third Party Servicer - Our positive opinion of Berkadia's CMBS primary and master servicing capabilities and expertise as a third party servicer. Berkadia effectively uses its BSIPL platform to provide extensive servicing functions for other servicers.
- High Degree of Experience and Successful Performance as a CMBS Master Servicer - We believe that Berkadia has a high degree of experience and an overall successful performance record as a CMBS master servicer with respect to its trustee reporting; controlled advance determination procedures; proactive sub-servicer oversight and audit practices; pooling and servicing agreement (PSA) compliance; and the handling of master servicing duties for a range of large and complex transactions. The company incurred no material reporting errors or restatements during 2012 or first half of 2013.
- Overall Operational Stability and Effective Use of Resources to Address Increased Servicing Volume - In our view, Berkadia demonstrates sound operational stability as a primary servicer, and, as a master servicer, has the capacity to meet its

ongoing advancing responsibilities based on the company's representations regarding its financial resources. Servicing headcount increased this year to accommodate the additional servicing volume attributed to KeyBank's acquisition of the Bank of America portfolio. The company relies on its offshore personnel in India for a significant portion of administrative servicing functions while subject matter experts in its U.S. operations directly handle larger and more complex assets. The company is in the process of relocating its Hyderabad operation to a larger highly secured location to accommodate the increase in staffing. In our view, the company continues to benefit from having a second and swing shift in its offshore operation to enhance operating efficiencies across the servicing platform.

- Investor Reporting Expertise - Our favorable view of Berkadia's responsiveness to information requests, as well as its capabilities to provide accurate and timely reporting, the overall quality of its asset-level reporting content, and its website functionality, which addresses both CMBS and non-CMBS client requirements.
- Robust Internal Audit Program - Berkadia has an independent and highly proactive internal audit function that quarterly examines a broad range of loan administration and portfolio management processes, and is supplemented with a number of performance monitoring activities and compliance routines embedded in the company's daily workflow practices. Audits encompass annual Regulation AB and USAP attestations, a Service Organization Controls (SOC1) Report, and a self-administered quality control program. The latest audit results provided to Morningstar were overall satisfactory. While the internal audits cited a few exceptions, none was deemed high risk and all have been cleared.
- Overall Effective Technology Tools and High Level of Automation - In our view, Berkadia effectively uses its servicing infrastructure to interface with other servicing systems so that it may provide specific functional support for other servicers in addition to primary and master servicing for other third parties. We also believe that Berkadia's servicing operation is highly automated with technology that centrally manages data. Berkadia is in the process of implementing version 17.3 of McCracken Financial Solutions Corp.'s Strategy application, which will be completed by the second quarter of 2014. Berkadia currently uses a highly customized version 12b of the system.
- Enhanced Insurance Administration - We believe that Berkadia's partnership with Marsh US Consumer to manage and monitor insurance coverage through a shared technology platform developed by Marsh has greatly enhanced Berkadia's ability to administer insurance compliance.
- Expanded Training Program - Berkadia expanded its training program within BSIPL to address the increase in servicing staff handling the legacy Bank of America assets.

Special Servicing

- Stability within Special Servicing - Although Berkadia sold its legacy CMBS special servicing portfolio to KeyBank and transferred the assets in July 2013, we believe that it has retained appropriate resources and experienced personnel to provide effective asset management for its own balance sheet and third parties. However, the lowered ranking is attributed to an overall reduction in management and professional depth resulting from the KeyBank transaction which substantially reduced Berkadia's actively managed portfolio.
- Sound Special Servicing Practices/History of Successful Asset Resolution Performance - In our view, Berkadia has retained well controlled procedures and robust technology tools to support effective special servicing and related reporting requirements for CMBS and other investors. Our assessment also considers the company's extensive history of very successful asset resolution performance results with many large and complex assets.
- No Discernible Conflict of Interest - We believe that Berkadia has effective policies and procedures to manage conflicts of interest. Overall, we generally view Berkadia 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. Berkadia's business model is to act as an independent, third party special servicer without any investment in subordinate CMBS.

As of June 30, 2013 Berkadia's total primary and master serviced portfolio was approximately \$234.6 billion by unpaid principal balance (UPB) and 25,867 by loan count, and it was the primary and/or master servicer on 349 CMBS transactions. After the KeyBank integration, Berkadia's total primary and master serviced portfolio increased to \$253.4 billion by UPB and 29,660 by loan

count. As of June 30, 2013 CMBS loans accounted for approximately 34% and 37% of Berkadia's total primary and master serviced portfolio based on UPB and loan count, respectively. CMBS represented 69% of the portfolio by UPB and 61% by loan count post integration.

As of June 30, 2013, Berkadia's total active special servicing portfolio was approximately \$1.41 billion by UPB and 87 by asset count (73 loans and 14 real estate owned properties). The CMBS component comprised 80 active assets with a UPB of \$1.25 billion (69 loans and 11 REO). Berkadia was the named special servicer on 57 CMBS transactions (\$10.6 billion by UPB consisting of 2,891 loans). After KeyBank acquired Berkadia's legacy CMBS special servicing portfolio on July 31, 2013, Berkadia retained seven special servicing assignments, which comprised 1,349 assets with a total UPB of \$240.5 million and included 20 active assets with a total UPB of \$1.6 million.

Forecast

Stable for all rankings. We expect Berkadia to continue serving as a highly effective primary and master servicer, and fully competent special servicer, and expect all three rankings to remain unchanged during the next 12 months. We will continue to monitor Berkadia's overall servicing performance and its substantial use of off-shore personnel as the company's portfolio continues to grow.

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

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