

Operational Risk Assessments News Bulletin

Ocwen Loan Servicing, LLC

Morningstar Assigns 'MOR CV2/Stable' Ranking/Forecast to Ocwen Loan Servicing, LLC as a Commercial Vendor for REO Asset Management; Concurrently, 'MOR CS3/Stable' Commercial Mortgage Special Servicer Ranking is Withdrawn

Morningstar Credit Ratings, LLC (Morningstar) has assigned its 'MOR CV2' ranking to Ocwen Loan Servicing, LLC (Ocwen) as a commercial vendor for REO asset management. Ocwen Loan Servicing is a wholly owned subsidiary of Ocwen Financial Corporation. The assigned ranking reflects our assessment of Ocwen's operational infrastructure and portfolio administration capabilities specifically for its duties as a commercial asset manager for REO properties, which currently principally involve multifamily asset management, liquidation, and related assignments for a government sponsored entity (GSE) client.

The assigned 'MOR CV2' ranking replaces our 'MOR CS3' ranking assigned to Ocwen as a commercial mortgage special servicer in 2012. Accordingly, concurrent with our newly assigned 'MOR CV2' ranking, Morningstar has withdrawn its 'MOR CS3' ranking on Ocwen. Morningstar's rationale for assessing Ocwen as a commercial vendor for REO asset management rather than continuing to assess the company as a commercial mortgage special servicer is twofold: (i) Ocwen's commercial real estate portfolio and related resolutions of larger balance assets have principally comprised GSE multifamily REO asset management and related assignments as a result of the company's client assignments and business pursuits in recent years; and (ii) our corresponding acknowledgment of Ocwen's successful track record as a multifamily REO asset manager and resolution specialist. (For additional information on Ocwen's commercial operations, please refer to Morningstar's operational risk assessment report covering Ocwen as a small balance commercial mortgage primary and special servicer).

Our assessment and assigned ranking reflects the following composite factors:

- Management and Professional Depth - Ocwen's overall operational stability and its retention of a highly experienced management and professional staff within a very scalable organizational structure suitably designed for its current portfolio and client assignments. We view Ocwen as being quite adept with REO asset management, especially with multifamily properties. The team also is experienced in managing a low income housing tax credit (LIHTC) portfolio. Based on Ocwen's proactive hiring practices, ability to leverage its offshore platform, and ongoing staff redeployments, we believe that Ocwen, as an REO asset manager, demonstrates effective mobilization skills and the capacity to address new asset transfers and portfolio assignments.
- Well Established Client Reporting Capabilities - Ocwen's well established capabilities to provide complete and timely reporting to its current GSE and other investor clients. We believe that Ocwen's expanded relationship with its GSE client in the past year through an additional assignment involving loan underwriting compliance, along with the continuation of its existing assignments, including some added reporting work, are a testament to Ocwen's solid performance and its ability to satisfy client requirements.
- Soundly Controlled Procedures and Internal Audit Program - Our view that Ocwen has soundly controlled operating practices governing commercial REO asset management, including asset analysis, business plan documentation and internal approvals, cash accounting, and external vendor engagement.
- Overall Sound Internal Audit Program - The company's soundly designed internal audit function that covers compliance across a range of operational areas. The audit program includes annual, GSE-client commissioned operational and security examinations, an annual USAP attestation, and internal audits conducted approximately

every 18 to 24 months by Ocwen's own independent internal audit department. Based on Morningstar's review of the latest available audit reports and Ocwen's representations regarding those still in process, none of these audits cited any material or high risk exceptions.

- Effective Technology - Ocwen's technology tools that provide a high level of automated reporting and overall operating efficiency. We also believe that Ocwen has sound data security and disaster preparedness protocols. Overall, we believe the company's proprietary servicing and integrated asset management applications provide for effective workflow management and centralized data management, along with the ability to address CMBS and other investor reporting requirements, if needed. However, Ocwen could benefit from the migration of certain property accounting and activity tracking reports, which it currently handles through separate spreadsheets, into its asset management application or an integrated REO accounting system.
- Solid Record of Multifamily REO Resolutions- Ocwen's steadily expanding track record of successful REO asset dispositions for third party investors, especially for its current GSE client, as a result of its ability to find effective solutions to challenging real estate issues, and its overall net recovery results and resolution timeframes. We also acknowledge Ocwen's ability to enhance asset values and increase net recovery amounts through effective hold/sell analyses and successfully administering a number of sizable capital expenditure and renovation projects.
- Effective Property Management and Accounting Oversight - Our belief that Ocwen has effective oversight controls covering property management company engagements and monthly reporting, including an ongoing property manager audit program.
- Portfolio and Client Diversity - The assigned ranking, while reflecting Ocwen's well developed expertise with multifamily REO and related GSE reporting, also reflects the company's limited activity in recent years with managing and liquidating larger-scale real estate assets involving other property types and for other clients. Ocwen has resolved commercial REO assets in all regions of the U.S., although its work has principally involved properties located in the Southeast, Southwest, and Midwest.
- No Discernible Conflict of Interest - Our belief that Ocwen has effective policies and procedures to manage any potential conflicts of interest. Ocwen's business model is to act as an independent, fee-for-service asset manager. It does not have any investment in commercial real estate securitizations and does not maintain or use affiliates to purchase or sell assets that it manages for third party investors. Accordingly, we view Ocwen as a company that operates without the potential conflicts of interest arising from using affiliates in managed transactions.

Ocwen conducts its commercial REO asset management from its West Palm Beach, Florida office. As of June 30, 2013, Ocwen's large asset commercial portfolio comprised 89 multifamily REO properties having a total unpaid principal balance (UPB) of approximately \$451.6 million. During 2012, it sold 130 REO properties yielding total net sales proceeds that represented 90.3% of its established property values. Through the first half of 2013, Ocwen sold another 24 REO properties yielding total net sales proceeds that represented 115.7% of its established property values. The company's average hold time of REO sold during the first half of 2013, inclusive of the additional time held to complete capital improvement projects on certain assets, was approximately 13 months. Its average resolution time was slightly more than one year for all REO sold between January 2012 and June 2013. Ocwen's LIHTC portfolio comprised seven assets as of June 2013. Additionally, the company is the named special servicer for one commercial real estate collateralized debt obligation, which had 14 performing loans with a total UPB of approximately \$242.7 million as of June 30, 2013.

Forecast

Stable. Based on the company's successful asset resolution history, well designed technology and reporting capabilities, solid professional experience, sound operational practices, and overall satisfactory audit results, Morningstar expects Ocwen to continue serving as an effective REO asset manager with particular expertise in multifamily assets and related GSE reporting.

Our full commercial vendor assessment report on Ocwen as an REO asset manager is forthcoming and will be made available on our website.

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