

Operational Risk Assessments News Bulletin

Wells Fargo Commercial Mortgage Servicing

Morningstar Raises Wells Fargo's Commercial Mortgage Primary and Master Servicing Rankings to 'MOR CS1' from 'MOR CS2' and Affirms Its 'MOR CS2' Commercial Mortgage Special Servicing Ranking; Forecast for All Rankings is Stable

Morningstar Credit Ratings, LLC (Morningstar) has raised its commercial mortgage primary servicer and commercial mortgage master servicer rankings on Wells Fargo Commercial Mortgage Servicing (WFCMS) to 'MOR CS1' from 'MOR CS2' and has affirmed its 'MOR CS2' ranking on WFCMS as a commercial mortgage special servicer. The raised primary and master servicer rankings and the affirmed 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 Conversion of Technology Platform - The company successfully converted two large legacy portfolios and separate servicing systems, and upgraded to the latest version of a singular application (McCracken version 17) in January 2013. As a result of the conversion, WFCMS retired and consolidated several of its supplemental applications to achieve greater efficiencies. We observed that the company continued to provide accurate, timely reporting, and high quality servicing as it streamlined its technology applications. WFCMS also added a consolidated investor web portal, which has received favorable user reviews.
- Highly Effective Use of Off Shore Facilities and Fully Integrated Organizational Structure - Our opinion that WFCMS operates very effectively through a fully integrated organizational structure, consisting of East and West Coast-based office hubs, including an off-shore support staff provided through Wells Fargo India Solutions (WFIS), a subsidiary of the company's parent bank. During 2013, the servicer continued to increase its WFIS staff and expand their involvement to assist with more primary and master servicing-related tasks. However, these tasks generally remain non-credit decision-oriented and permit only very limited and scripted email communication with borrowers. Morningstar traveled to WFIS earlier this year to observe WFCMS's ability to provide quality servicing as it continues to increasingly use WFIS staff for primary and master servicing tasks, and the degree to which WFIS staff have become further acclimated and trained in their respective duties, workflows, and use of the new servicing system.
- Strong Management and Professional Depth - Our belief that the company continues to operate with highly experienced management and professional staff. It recently hired an industry veteran, whose background includes senior management experience at the former Wachovia Bank, to head servicing operations.
- Investor Reporting Expertise - Our favorable view of the company's responsiveness to information requests, 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. The company also recently added WFIS staff to perform quality control activities over investor reporting functions to monitor accuracy.
- Extensive Sub-servicer Oversight, and Proactive and Controlled Asset Administration - Our positive opinion of the company's CMBS asset administration capabilities and expertise for a broad range of large and complex transactions. In addition, we believe that WFCMS has a high degree of experience and a very solid performance record as a CMBS master servicer with respect to pooling and servicing agreement (PSA) compliance, cash management and monthly reporting, advance determination procedures, sub-servicer oversight and audit practices, and meeting its specific service level agreements. During 2012, the company conducted sub-servicer audits corresponding to approximately 92% of all sub-serviced loans by loan count, which we believe is quite high compared to other master servicers we rank.

- Sound Internal Audit Program - Our view that WFCMS has a sound internal audit program conducted by the parent bank's audit division, an annual Regulation AB attestation process, various client-led examinations, and a self-administered quality control program, which examines approximately 400 control processes on a rolling basis. The latest audit results provided to Morningstar were overall satisfactory. While the recent parent bank audit cited a few exceptions, none was deemed high risk and WFCMS expects to have all remaining open items cleared before year end. WFCMS also received Fannie Mae's first ever "Exceptional" rating of a servicing operation.
- Effective Portfolio Management - Our view that the company's practices and procedures provide proactive asset-level management and portfolio oversight to monitor collateral performance, track loan covenant compliance and trigger events, and manage borrower requests. In addition, the company proactively addresses the timely and accurate re-boarding of loan modifications received from external special servicers, and it continues to hold annual summit meetings with special servicers to expedite the cash management and modification process resulting in a steady reduction in WFCMS' loan modification boarding turnaround times.
- Expanded Training Program - WFCMS expanded its training program by consolidating it under the control of a senior asset manager, adding curriculum specifically for analysts, and by providing career path guidance for U.S. and WFIS personnel.

Special Servicing

- Sound Asset Resolution Record - Our view that the company has a sound track record of asset management and well controlled procedures covering asset resolutions involving a number of large and complex structures. We believe that WFCMS asset managers are well-experienced, although their average years of experience continue to be somewhat lower than some other higher volume CMBS special servicers. In our view, its special servicing technology is less extensive than other CMBS special servicers, but it accommodates the company's tracking and reporting requirements for a moderate volume of specially serviced assets.
- No Discernible Conflict of Interest - WFCMS reported that it usually serves as a CMBS special servicer for portfolios in which it serves as master or primary servicer. Furthermore, neither WFCMS nor its parent has any affiliated investment interests in the controlling classes of the bonds, and WFCMS rarely has involved an affiliated brokerage entity to market specially serviced assets. Overall, we view WFCMS 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.

As of June 30, 2013, WFCMS' total primary and master serviced portfolio was approximately \$431.0 billion by unpaid principal balance (UPB) and 33,843 by loan count, and it was the primary and/or master servicer on 408 CMBS transactions. As of June 30, 2013, CMBS loans accounted for approximately 80% and 70% of its total primary and master serviced portfolio based on UPB and loan count, respectively. As of June 30, 2013, the company's total active special servicing portfolio was approximately \$2.1 billion by UPB and 86 by asset count (78 loans and 8 real estate owned properties). The CMBS component comprised 24 active assets with a UPB of approximately \$2.0 billion (19 loans and 5 REO). WFCMS was the named special servicer on 84 CMBS transactions (approximately \$54.0 billion by UPB and consisting of 1,811 loans).

Forecast

Stable for all rankings. We expect WFCMS 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 WFCMS is forthcoming and will be made available on our website.

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