

# Operational Risk Assessments News Bulletin

## Berkadia Commercial Mortgage, LLC

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### **Morningstar Assigns 'MOR CS2' Commercial Primary and Master Servicer Rankings and 'MOR CS1' Special Servicer Ranking to Berkadia Commercial Mortgage, LLC**

Morningstar Credit Ratings, LLC ("Morningstar") has assigned Berkadia Commercial Mortgage, LLC (Berkadia) a 'MOR CS2' ranking as a commercial mortgage primary servicer, a 'MOR CS2' ranking as a commercial mortgage master servicer, and a 'MOR CS1' ranking as a commercial mortgage special servicer. The forecasts for the commercial mortgage primary and master servicer rankings are Favorable and the forecast for the special servicer ranking is Stable.

Each ranking is based on our assessment of Berkadia's operational infrastructure and portfolio administration capabilities. The primary and master servicer rankings largely reflect our view of the company's shift in organizational approach, which has generated a higher staff turnover within its U.S. operations while it concurrently moved a significantly greater portion of its primary and master servicing functions to operations in India and the Philippines. Berkadia stated that this organizational re-design, known as its Operational Excellence Program (OPEX), is steadily building process efficiencies, while lowering the costs of servicing. In recent months, Berkadia empowered its off-shore staff as the initial point of contact to address a range of portfolio management tasks for loans up to \$30 million, which we view as a high threshold. Berkadia reported that subject matter experts within its U.S. operations still directly handle larger and more complex assets, and provide quality control over any work conducted by offshore personnel. We also believe that Berkadia may benefit from the second shift operating hours provided by its offshore operations to address the large volume of information requests from borrowers, investors, and rating agencies. However, we will continue to monitor the effectiveness of this sharply changed organizational approach and Berkadia's concurrent ability to maintain servicing quality.

Our assessment is also based on our view of the following:

- Overall favorable investor feedback and comments within Morningstar CMBS surveillance DealView reports, which indicate Berkadia's responsiveness to information requests, information accuracy, and quality of its investor website.
- Our positive opinion of Berkadia's CMBS master servicing capabilities and expertise. In our view, Berkadia, as a master servicer, also has the capacity to meet its ongoing advancing responsibilities based on the company's representations regarding its financial resources and current funding vehicles including a new and substantial bank credit facility.

- The comparably fewer resources Berkadia has dedicated to sub-servicer auditing and compliance versus some other master servicers, although it did conduct a number of audits in recent months.
- Berkadia's overall effective technology tools, high level of automation, and centralized data management. However, Berkadia currently uses a much older version of its servicing system.
- An independent and intensive internal audit function that encompasses not only a Regulation AB attestation, but also includes an annual Statement of Auditing Standards No. 70 review, ongoing internally-managed audits, and other audits conducted by external parties.
- A proactive portfolio management process and procedures to monitor portfolio performance.
- Well-designed CMBS advancing procedures based on conservative thresholds and proactive special servicer oversight, particularly with respect to monitoring valuations.
- Very successful asset resolution activity within special servicing along with special servicing policies and practices that indicate expertise with CMBS structures and effective controls to manage conflicts of interest.

As of June 30, 2011, Berkadia's combined primary and master servicing portfolio had approximately \$182.7 in unpaid principal balances (UPB) and 24,648 loans, representing a 6% decrease in UPB and a 5% decrease in loans compared to the year ended December 31, 2010. Its active special servicing portfolio had approximately \$2.2 billion in UPB and 288 loans, representing a 19% decrease in UPB and 12% decrease in loan count from the year ended December 31, 2010. During the first half of 2011, Berkadia resolved approximately 32% of its inventory of specially serviced loans and REO assets that it had as of the beginning of the calendar year.

## Ranking Forecast

Our ranking forecasts for Berkadia are *Favorable* for primary and master servicing and *Stable* for special servicing. The ranking forecasts for primary and master servicing are based on our view that recent expansions in offshore operations may result in maintaining and possibly building even greater process and operational efficiencies.

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

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