Operational Risk Assessments

Torchlight Loan Services, LLC

April 2020

Operational Classification: Commercial Mortgage Special Servicer

Ranking: MOR CS1 (Affirmed)

Forecast: Stable

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Rationale

Morningstar Credit Ratings, LLC (DBRS Morningstar) affirmed its MOR CS1 commercial mortgage special-servicer ranking for Torchlight Loan Services, LLC, a wholly owned subsidiary of Torchlight Investors, LLC. Morningstar affirmed its ranking based on the following factors:

- Asset-Recovery Performance: Torchlight has been an active special servicer with legacy commercial mortgage-backed securities (CMBS) transactions. Because of asset resolutions and slowing incoming transfers, its active volume declined to a modest level at year-end 2019 and has shifted toward real estate owned (REO) assets. In 2019, the company posted another year of successful recovery results, including the resolution of some large assets. The affirmed ranking also considers Torchlight's handling of some especially problematic retail assets and Torchlight Investors' management of a few troubled non-CMBS assets in its debt funds.
- Organizational Stability and Professional Depth: Torchlight has a well-experienced executive and professional team operating in a cohesive organizational framework. Asset managers' average industry experience is solid and trending higher. The company had no turnover in its special-servicing team in 2019, and total turnover involved only two positions in Torchlight Investors' financial control group, which is well-integrated with the special-servicing team to support client reporting, asset accounting, and vendor oversight. Torchlight Investors assists the special-servicing unit with compliance, portfolio surveillance, and legal oversight as well. It also has portfolio managers with real estate loan workout expertise, including some who have worked at other special servicers.
- Staffing Workloads and Capacity: Considering Torchlight's much reduced specially serviced asset volume at year-end, corresponding low asset manager workload ratio, ability to deploy investment fund managers and analysts, and its overall exposure as a named CMBS special servicer, the company should have enough capacity in the coming months to address an uptick in new transfers associated with the Coronavirus Disease (COVID-19) pandemic. DBRS Morningstar will continue to monitor Torchlight's staffing.
- Technology and Disaster-Recovery Readiness: Torchlight uses the Backshop asset-management application, which has strong asset-tracking, investor-reporting, and workflow-control capabilities geared to CMBS requirements. Through the application provider, Torchlight continues to implement functionality enhancements. Another vendor manages Torchlight's network support, user needs, and disaster-recovery management. This approach is acceptable based on the vendor's 24-hour helpdesk, testing protocols, and satisfactory security audits and Service Organization Control (SOC 1 and 2) examinations of its data centers. Torchlight's business-continuity plan includes a third-party contingency agreement for office space. Most recently, Torchlight has demonstrated its ability to

readily and effectively activate its remote-access work plan for the entire operation. An automated and integrated vendor-invoice approval/processing application also facilitates special-servicing controls and efficiency.

- Asset Analytics and Management: Supported through the asset-management application, Torchlight has diligent asset-analysis practices and well-delineated policies and procedures for effective and controlled special servicing, including borrower consents on performing loans. With growing REO activity in the past few years, Torchlight has a sound property-manager audit program as well.
- Internal Audit and Compliance: Torchlight has sound auditing and control practices. The company engages a nationally known firm to conduct audits that examine a range of processes, including cash controls, investor reporting, and asset-level approvals. Torchlight follows a 24-month audit cycle, which is acceptable based on lower active-asset volume, annual Regulation AB attestations, and other compliance-monitoring practices. The latest available audit report issued in May 2019 did not identify any high-risk control weaknesses, and Torchlight has addressed the few recommendations raised in the audit. Additionally, Torchlight's Regulation AB attestations have not contained any exceptions for the past several years. The asset-management system, a vendor invoice-processing application, and solid and strengthened vendor oversight also support Torchlight's focus on controls and compliance.
- Conflicts of Interest Management: For many CMBS transactions in which Torchlight is the named special servicer, Torchlight Investors holds first-loss bond positions and is the controlling classholder. Torchlight does not use affiliates for its special-servicing work, but its parent has acquired a few assets using permitted purchase options on legacy CMBS. As an SEC registered investment advisor, Torchlight Investors has a compliance department to protect against information sharing and other potential conflicts with its special-servicing work. Torchlight's asset-management practices, asset-recovery results, and handling of fees indicate that the company is cognizant of upholding the servicing standard.

As of December 31, 2019, Torchlight was the named special servicer for 26 CMBS securitizations (including one Freddie Mac) with a combined remaining unpaid principal balance (UPB) of $11.88 billion consisting of 690 loans and 1,386 properties. Eleven of these transactions were issued before 2011. It also was the special servicer for a 2005-vintage commercial real estate collateralized debt obligation with a remaining $64.5 million UPB containing three assets. As a named special servicer, 29.9% by property count were retail assets, 21.5% were lodging assets (approximately 25% were in one single asset single borrower (SASB) transaction), and 16.0% were multifamily assets.

As of December 31, 2019, excluding a few non-CMBS workouts in affiliated debt funds, the active special-servicing portfolio contained 16 assets (nine loans and seven REO properties) with a combined UPB of approximately $397.5 million, including an REO asset with two properties in the above-referenced commercial real estate collateralized debt obligation (CRE CDO).

As of March 31, 2020, the active portfolio increased to 20 assets with a $568.7 million UPB (13 loans with a $439.5 UPB and seven REO with a $129.2 million UPB). Torchlight received four loan transfers since late February, including a two-property hotel loan associated with the COVID-19 pandemic. By property count, the active portfolio was 22% lodging, 30% retail, 30% office, 9% multifamily, and 9% industrial.

During 2019, Torchlight resolved six nonperforming loans through one loan restructure, two full payoffs, and three note sales that generated aggregate net proceeds equal to nearly 99% of value. It also sold eight REO properties, including two retail malls, that generated aggregate net proceeds equal to approximately 91% of value. All resolved assets were in CMBS transactions.

Forecast

DBRS Morningstar's forecast for the ranking remains Stable. The forecast considers Torchlight's record of excellent resolution results, professional depth, solid control practices, robust technology, and contingency personnel resources to address volume increases.

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Company Profile and Business Overview

New York City-based Torchlight is a wholly owned subsidiary of Torchlight Investors, which began in 1995 as Jones Lang Wootton Realty Advisors. In 2002, ING Group purchased a minority equity stake in Jones Lang Wootton Realty Advisors and changed the name to ING Clarion Capital. In 2010, the management team acquired ING Group's investment position, and the company assumed its current name. Torchlight Investors is 100% management-owned.

Torchlight Investors' core businesses are investment advisory, which encompasses special servicing and commercial real estate debt investment and asset management. To support its acquisitions and investment-management businesses, the company may provide senior or subordinated financing or preferred equity. Since 1995, the company has acquired investment positions in assets valued at more than $20 billion and launched several opportunistic or value-add investment funds. Its most recent closed fund launched in 2017 with a capital commitment of almost $1.7 billion for a three-year investment period following the transaction's final closing date. Earlier this year, the company began marketing another fund with an initial capital-raising target of $1.5 billion. As of December 31, 2019, Torchlight Investors had approximately $3.7 billion in assets under management, including investments in CMBS. It manages assets on behalf of third-party institutional clients, largely comprising retirement and pension funds, principally through its closed-end debt funds.

Torchlight Investors was one of the most active CMBS B-piece investors in the years immediately preceding the 2008 financial crisis. As a result, Torchlight became one of the larger-volume special servicers for legacy CMBS. Torchlight Investors also has acquired subordinate bond positions in newer-issue CMBS and appointed Torchlight as the special servicer. Additionally, Torchlight Investors has acquired first-loss positions in several Freddie Mac K-Series securitizations and has been a selective buyer of these bonds. Cumulatively, across all transactions, it has acquired approximately 59 B-pieces with an approximate $1.5 billion acquisition value. Its most recent purchases, through its funds, were B-pieces in three 2018-issued CMBS and a B-piece in a 2011-vintage transaction acquired in early 2019.

Torchlight is an approved Freddie Mac special servicer and, as of December 2019, it was the named special servicer for one Freddie Mac securitization that was issued in 2014. As of December 31, 2019, that transaction did not contain any specially serviced assets. Additionally, Torchlight is a consultant for its affiliate's position as the directing certificateholder for one Freddie Mac transaction.

Since inception through September 2019, Torchlight has resolved 690 specially serviced loans with an aggregate balance of approximately $10.8 billion and managed 230 real estate assets valued at approximately $2.3 billion.

As of December 2019, Torchlight Investors had 57 total employees across its business lines of real estate investment and asset management, special servicing, and securitization structuring. It had a core four-person special-servicing team for CMBS loan and REO workouts. Including its investment-management team, senior credit officers, portfolio managers, and accounting/reporting, legal, and compliance staff, Torchlight's broader special-servicing platform consisted of approximately 16 employees in addition to several debt-fund asset managers available for CMBS special servicing if needed.

Table 1 – Historical Active Special-Servicing Volume

	December 31, 2019		December 31, 2018		December 31, 2017	
	UPB ($000s)	Loans	UPB ($000s)	Loans	UPB ($000s)	Loans
Loan Portfolio	268,159	9	174,281	10	549,524	22
REO Portfolio	129,369	7	463,352	28	340,133	21
Total Active Portfolio	397,528	16	637,633	38	889,657	43
Active CMBS Portfolio Only*	397,528	16	637,633	38	889,657	43
Named CMBS Special Servicer**	11,880,426	690	16,225,793	951	16,687,316	1,028
Number of Transactions**		26		34		35

*Loans and REO assets. **As of December 2019, included one Freddie Mac securitization (FREMF 2014-K39) and one 2005-vintage CRE CDO.

Operational Infrastructure

Organizational Structure

Torchlight Investors' executive team consists of six partners: the CEO (and co-chief investment officer), the co-chief investment officer, the head of asset management, the investment-management head, the chief credit officer, and the chief operation officer. They oversee the company's principal business of real estate debt investment and asset management, which involves its debt funds, the funds' related CMBS bond positions, and the operations of Torchlight, the special-servicer subsidiary.

Torchlight Investors' chief operating officer oversees the 13-person financial-control department, which has teams for corporate-level, fund-level and special-servicer accounting, finance, and operations work. Among its duties for special servicing, the financial-control staff manages REO property bank accounts and reconciliations, special-purpose entity management in conjunction with internal legal counsel, vendor invoice approvals and processing, master-servicer 1099 reporting, and external auditor management.

The organization also has dedicated staff for legal, compliance, portfolio surveillance, investment underwriting, and client services, which handles marketing and investor relations for the debt funds.

Torchlight, as the special-servicing subsidiary operation for publicly rated CMBS, is part of Torchlight Investors' asset-management division, which handles the underwriting and assets in the private-placement debt funds.

Including other support staff from the parent, Torchlight's special-servicing platform consists of the following:

- The asset-management division head;
- A four-person asset-recovery team consisting of the head of special servicing, who is especially involved in the REO assets, a senior-level loan asset manager, a supporting analyst, and a senior associate with CMBS investor reporting and asset management experience to assist with those functions (the senior associate coordinates CMBS reporting content and distribution to master servicers, with the financial-control team involved in the review and approval process);
- Accounting personnel from Torchlight Investors' financial-control department for portfolio- and asset-level accounting, including property-level accounting oversight on REO assets;
- Torchlight Investors' chief compliance officer, who serves the company on a contract basis to provide counsel regarding servicing-agreement issues and regulatory compliance, including conflicts-of-interest risk mitigation;
- Shared resources from the parent: an in-house attorney, a five-person client services team, and a four-person portfolio surveillance team;
- The 11-person Torchlight Investors' investment due-diligence and asset-management team, which has three designated people (two senior-level and one associate-level) with loan workout experience available to assist with special servicing; and,
- A founding member of a Torchlight Investors' predecessor company who serves as a special advisor and member of Torchlight's special-servicing credit committee.

Management and Staff Experience

Asset managers' average experience has increased year-over-year since 2017. As of December 2019, the CMBS special-servicing team averaged 13 years of experience, including the asset-management division head who had 22 years of experience. The two most-senior managers averaged nearly 16 years of experience. Additionally, several members of Torchlight Investors' asset-management and analytics team for its debt funds have solid loan workout experience and are available to support CMBS work if needed. The company's in-house legal counsel and former special-servicing department head, who principally now supports funds management, has 25 years of industry experience.

Table 2 – Management and Staff: Average Years of Experience

	December 2019		December 2018		December 2017	
	Industry	Tenure	Industry	Tenure	Industry	Tenure
Senior Management	22	9	20	8	23	5
Middle Management	13	8	15	9	10	5
CMBS Asset Managers*	13	5	12	4	10	4
Other Asset Managers**	10	3	10	5	11	6

*Includes head of asset-management division, head of special servicing, loan-management vice president, senior associate, and an asset analyst. **Available on a contingency basis, designated staff in Torchlight Investors' debt fund team.

Management and Staff Turnover

Torchlight had no turnover in its CMBS asset-management team in 2019. The noted employee departures in 2019 both involved positions in the financial control team, and those vacancies were subsequently filled. Much of the turnover in 2018 involved an operations unit, which principally handled CMBS investor reporting and rating-agency communications. As noted, a senior associate now manages that function, which entails reduced volume, in conjunction with the special-servicing department head and the financial-control team.

Table 3 – CMBS Special Servicing: Management and Staff Turnover Rates*

	2019		2018	
	Personnel (#)	Rate (%)	Personnel (#)	Rate (%)
Total Staff - Beginning of Period (# of Positions)	16		12	
Total Turnover	2	12.5	4	33.3
Involuntary	1	6.25	1	8.3
Voluntary	1	6.25	3	25.0
Management Only	1	6.25	1	8.3
Staff Only	1	6.25	2	25.0
Including Torchlight Investors' Financial Controls Team**	--		5	
New Hires (# of Positions)	2		3	
Total Staff- End of Period (# of Positions)	16		16	

*Based on number of people at the period beginning. All 2019 turnover was in the financial control department. **To reflect 2018 centralization of all accounting and finance functions under one department.

Workload Ratios

As of March 31, 2020, Torchlight had a 5:1 ratio of assets per asset manager excluding the asset-management division head, although he is involved in some asset deliberations. By comparison, Torchlight's assets/asset manager ratios (excluding the division head), were 10:1 as of December 31, 2018 and 14:1 as of December 31, 2017.

> **Assessment:** Torchlight has the requisite organizational depth and capabilities to effectively address its CMBS-oriented special-servicing work. The average experience of Torchlight's asset managers is solid and increased again during 2019. The company noted that its consolidation of certain special-servicing operational tasks to the corporate financial-control team in 2018 also has facilitated organizational synergies and efficiency. Most special servicers find it more efficient to have dedicated staff apart from asset managers for CMBS investor reporting. However, Torchlight's inclusion of its financial-control team in the review and approval process, which has been tempered by easing portfolio volume, indicates that the company is handling this function effectively with sound control procedures.

Considering Torchlight's much reduced specially serviced asset volume at year-end 2019, low workload ratio, ability to enlist personnel from its parent's investment-management business, and its overall exposure as a named CMBS special servicer, the company should have enough staff in the coming months to address a moderate increase in new transfers before it may need to hire additional personnel.

Training

Torchlight provides formalized training for all staff, with scheduled sessions from invited guest speakers covering a range of CMBS-centric and other special-servicing topics as well technology application usage. Senior management, with administrative support, coordinates training-event logistics and tracks employee-participation hours. The special-servicing manager also oversees asset-management system training and serves as liaison to the vendor supporting the system. Torchlight managers also conduct weekly asset-review meetings that cover every specially serviced asset and serve as a training forum for case studies and procedural issues. The company expects all personnel to complete 30-40 hours of training annually, excluding participation at conferences. During 2019, employees averaged about 42 training hours. Between March 2019 and January 2020, Torchlight's sponsored training sessions covered 20 topics and totaled about 40 hours. The company noted that it expanded these sessions with added topics in the past year.

Assessment: Based on the substance and frequency of Torchlight's activities, it has maintained a sound employee training function. The company's required minimum and actual annual training hours are solid and appear to be in line with and even higher than some other Morningstar-ranked special servicers. Torchlight may benefit from developing an intranet portal, integrated with specialized software or leveraging the asset-management system, as feasible, to serve as a centralized tool for staff to access training materials and recorded sessions, register for sessions, and track hours.

Audit, Compliance, and Procedural Completeness

The financial-control department certifies portfolio transfers and serves as liaison with firms engaged to perform internal audits. The department also monitors compliance with servicing agreements in conjunction with a corporate-level chief compliance and legal officer.

Torchlight uses a nationally recognized accounting firm to conduct operational audits examining cash management and accounting; special servicing approvals, processes, and asset transfers; investor/master servicer reporting; and technology application workflows. In 2017, Torchlight shifted to a two-year from a one-year cycle for these audits based on its reduced special-servicing portfolio projections. The most recent audit report, dated May 2019, contained some recommendations that Torchlight remedied but did not identify any high risk or material control weaknesses. Additionally, Torchlight provides an annual Regulation AB attestation that has not contained any exceptions for the past eight calendar years through 2019.

The reporting, task-tickler, and workflow-management features of the asset-management system support Torchlight's quality-control and compliance efforts. In particular, the system has compliance checklists for asset transfers to and from master servicers and other special servicers and for loan-to-REO transitions. As a special servicer focused on CMBS, Torchlight also may benefit by integrating its abstractions of PSA requirements into the system's workflow and user-dashboard programming.

Torchlight formally updated and enhanced its documented policies and procedures in 2018, and again this year. They include added references to the asset-management system and focus on proactive and controlled special-servicing practices and especially CMBS requirements. The policies and procedures encompass vendor-oversight protocols and authority delegations, including required committee approvals, for asset-level expenses and various asset management/recovery recommendations. The financial-control department, in conjunction with other senior management, manages updates to the company's policies and procedures. Additionally, employees must adhere to Torchlight Investors' separately documented policies and procedures covering corporate compliance and governance.

> **Assessment:** Torchlight has a sound internal-audit function supplemented with solid internal practices, resources, and supporting technology to monitor operational risk and servicing-agreement compliance. The 24-month audit cycle, excluding the annual Regulation AB attestation, is reasonable for the company's special-servicing volume. The updated policies and procedures, along with the workflow processes embedded in its asset-management system, denote proactive and controlled practices to address Torchlight's focus on CMBS special servicing.

Legal Liability and Corporate Insurance

Torchlight reported that it was not involved in any litigation directly related to its special-servicing operations. It also reported that it has directors and officers, errors and omissions, and fidelity bond insurance policies. Torchlight's corporate insurance program includes a data-security policy providing a $5 million coverage limit. The company reported that, as a special servicer, it has not received any notices of PSA default or citations related to performance.

> **Assessment:** Torchlight's insurance coverage limits are reasonable based on the company's asset volume and relative to other special servicers. DBRS Morningstar views Torchlight Investors' procurement of cybersecurity insurance as a best practice that has become more common among servicers. Based on Torchlight's representations, DBRS Morningstar is not aware of any material lawsuits related to, or which could potentially impair, the special servicer's operations.

Technology, Disaster Recovery, and Cybersecurity

Torchlight uses CMBS.com, Inc.'s Backshop special-servicing/asset-management system. Torchlight, as a licensee since 2015, uses the system in a hosted environment on Backshop's servers through a cloud-computing structure. The vendor, with Torchlight's input, continues to roll out functional enhancements for surveillance, consent approvals, and nonperforming asset management. Additionally, Backshop provides Torchlight with its programming source codes, associated technology requirements for the entire application, and monthly updates, which Iron Mountain Inc. as custodian holds in escrow. Iron Mountain conducts usability testing, with the most recent test report issued in 2019, for Torchlight verifying the integrity of the intellectual property and deposit agreement. This year, Torchlight, as an added control test, plans to use the report results and source coding to recreate the Backshop technology environment for itself.

Torchlight stated that Backshop can produce the latest CMBS investor-reporting package requirements established by the Commercial Real Estate Finance Council. The system has modules to prepare and store asset business plans, perform property cash flow modeling/valuation analysis and net present value recovery projections based on different scenarios, compare current performance with original underwriting, track property-level line item budgeted-to-actual income and expenses, produce asset-status reports, and shadow loan-administration activity such as payment histories, real estate tax payments, and insurance policy renewals using file downloads from master servicers. The system can provide business-volume forecasting/revenue tracking tied to expected losses and controlling classholder changes. The application provides cloud-based document storage, a menu of standard reports, and ad hoc reports based on database queries. To facilitate surveillance and asset transfers, the application's database includes every loan for which Torchlight is the named special servicer.

Through the system's functionality enhancements, Torchlight can initiate and track work orders from vendors and track vendors' performance; conduct all essential loan-level tickler management; obtain automated realized loss, fee, and advancing calculations; populate information into form documents and notification-letter templates; and track internal workflows and approvals. The system also has links to each asset's corresponding pooling and servicing agreement (PSA) and PSA abstraction, but, as previously noted, there is not a direct feed of the PSA requirements for each asset-management task to the system's workflow features of credit-management action alerts and procedural checklists. Torchlight also uses SAP Concur Technologies' automated vendor-invoice processing application, which is integrated with Torchlight Investors' corporate accounting system and was already used for its other business lines.

Torchlight Investors uses Eze Castle Integration, Inc. to provide information-technology support for all business lines. The IT vendor, which has offices in seven U.S. cities, London, and Asia, has a 24-hour help desk manned seven days per week and an on-site engineer available every workday at Torchlight's New York headquarters. Torchlight stated that the vendor provides a dedicated network with ample storage capacity through a cloud-based server structure, handles network access, and performs real-time data backups to an alternate data center. Employees' network access at the folder level also requires Torchlight management approval. The vendor, which also provides Torchlight with disaster-recovery services, completed its most recent recovery tests in February and July 2019 with successful results. Eze Castle's data centers (through other vendors) also are represented to be SOC 1 and 2 compliant.

Last year, Torchlight's financial-control department, in conjunction with the network vendor, expanded data-security protocols and awareness with required annual training modules for all employees and by conducting periodic phishing exercises.

Torchlight's business-continuity plan is predicated on staff working remotely with access to all network applications through a virtual private network. The business-continuity plan includes a formalized third-party agreement that provides some office space in Atlanta. Through its technology vendors, Torchlight indicated that it should have access to all business-critical systems and data and resume all special-servicing functions within four hours of a declared disaster event or business interruption.

> **Assessment:** Torchlight's technology platform provides workflow and data-management efficiency for detailed asset-level tracking and reporting for CMBS transactions and real estate fund investors. The company's information-technology outsourcing and cloud-based approach for file network maintenance is acceptable because of the vendor's represented capabilities and audits of its infrastructure, data centers, and security protocols. Torchlight's vendor-invoice management application, office space contingency plan, and focus on cybersecurity further support operational soundness and resiliency.

Special-Servicing Administration

As one of the larger-volume special servicers in the years following the 2008-09 financial crisis, Torchlight has managed many large, complex assets collateralized by a range of property types throughout the United States. Although the company has managed a few assets transferred from later-vintage CMBS pools, most of its resolutions have consisted of loans originated between 2004 and 2007. During 2019, its special-servicing activity continued to focus on the remaining troubled assets in its legacy CMBS transactions, with a substantial portion involving highly distressed larger-scale retail properties often compounded with legal impediments and collateral deficiencies. Torchlight's work includes a moderate amount of borrower consent reviews, which it expects to increase as Torchlight Investors looks to add new CMBS investments.

Chart 1 – Active Portfolio by UPB*

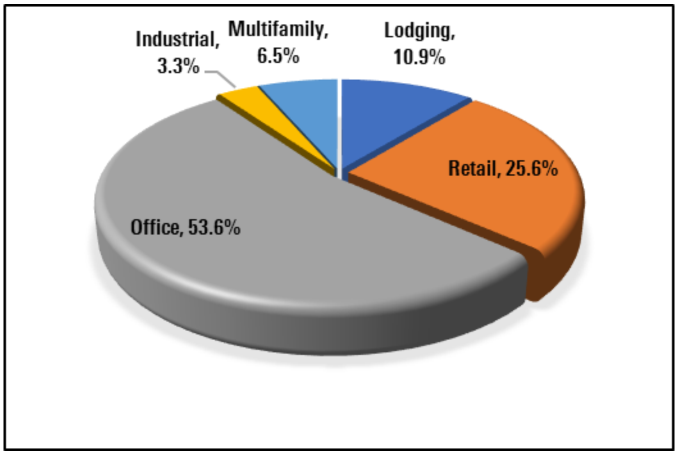


Chart 2 – Active Portfolio by Asset Count*

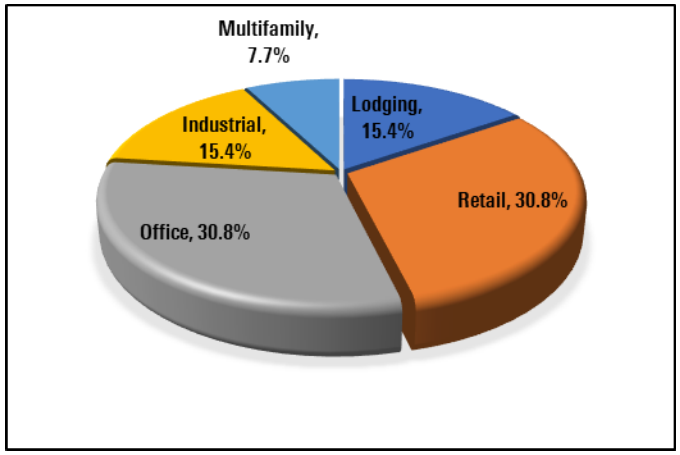


Chart 3 – Active Portfolio by State - UPB*

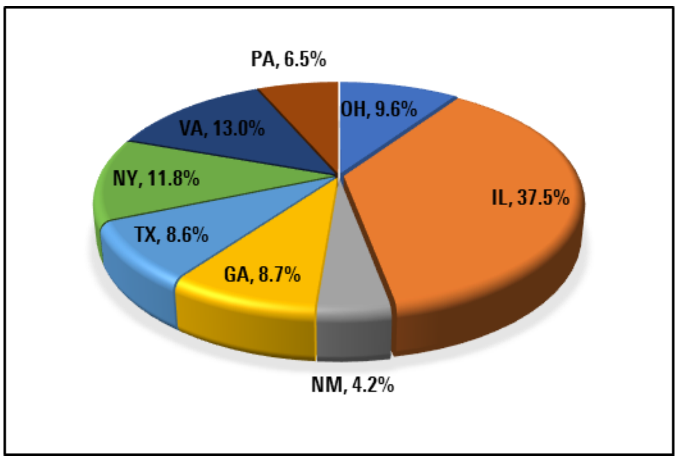
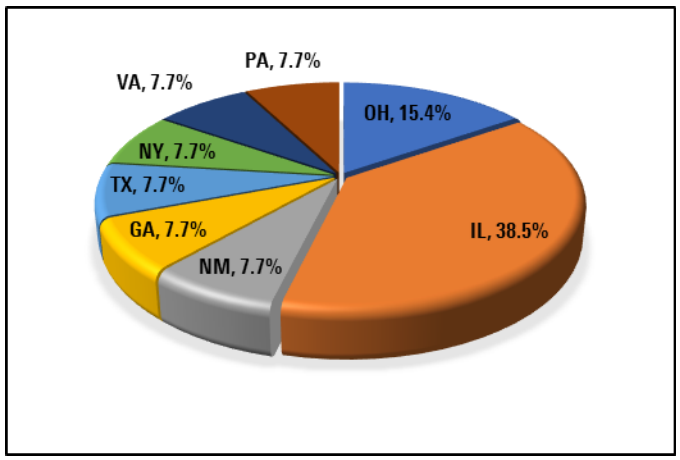


Chart 4 – Active Portfolio by State - Asset Count*



*As of December 31, 2019. Includes loans and REO assets. Percentages may not equal 100% because they are rounded.

Asset-Review Process

Once an asset transfers to special servicing, the asset manager reviews the file records, examines PSA-related requirements and loan-level covenants, and orders a property inspection. If needed, the manager also may visit the property. Through the file review, the asset manager formulates recovery options and strategies. Before engaging in workout discussions, Torchlight requires borrowers to sign prenegotiation agreements and pursues updated financial statements. As noted, the asset-management system houses data for all CMBS transactions in which Torchlight is the special servicer. This enables the company to have access to core information if a loan requires special servicing.

Asset managers generally prepare and obtain approval of an initial business plan within 60 days of an asset transferring to Torchlight for special servicing. For CMBS loans, asset managers also prepare an initial asset status report for investor reports as required by PSAs. Asset managers must update their asset-status comments twice a month. They must submit action-approval cases to initiate foreclosure, when they have negotiated specific resolution terms or before committing to other major asset decisions. Business plans and updated cases include a net present value analysis of each alternative resolution scenario. Asset managers prepare their business plans and approval cases directly in the asset-management system. As noted, the system also serves as the central tracking, compliance, and asset-analysis tool for the entire lifecycle of each specially serviced asset; its functionality includes cash flow modeling and workout scenario analysis.

The company has delegations of authority that require senior management sign-off and a committee-type approval structure for asset business plans and most resolution cases. Torchlight's special-servicing approval committee includes Torchlight Investors' head of asset management, a co-chief investment officer, and a former special-servicing department manager who now serves as in-house counsel.

The asset-management system tracks pending and approved asset plans and cases, issues alerts based on critical dates and trigger events, and provides for electronic signatures. As a recent enhancement, the system can initiate email requests to third-party vendors for updated appraisals and inspections based on tickler dates. Torchlight also holds weekly asset-review meetings. Torchlight stated that it formally monitors outstanding advances against property values and expected recovery amounts through the asset-management system, and it consults with master servicers on their advancing decisions. Through the asset-management system, Torchlight uses checklists to manage loan transfers from master/primary servicers and portfolio transfers to and from other special servicers.

> **Assessment:** Based on its stated policies and procedures, Torchlight has proactive and controlled loan-transfer, asset-analysis, and resolution-management practices especially geared for CMBS special servicing. The asset-management system's tracking and workflow features strengthen the company's asset analytics and data-management controls.

REO Property Management

Torchlight uses a property-takeover checklist when transitioning an asset to REO status. The REO asset manager addresses any immediate property issues and engages a property-management company and listing broker. The selected companies must qualify for or already be on Torchlight's approved-vendor lists. Once a loan becomes an REO asset, the REO asset manager generally prepares and obtains approval of a business plan within 60 days, with subsequent business cases submitted to obtain approval of specific sales offer terms or other major decisions. In preparation for taking title, the manager must ensure that the property is added to Torchlight's blanket insurance program.

Torchlight's property-management agreement contains specific monthly reporting requirements and procedures. The company retains the property-management company reports on its shared drive and uploads the information into the asset-management system to track budget-to-actual property performance and to prepare operating statement analysis reports. Torchlight controls property-level cash management through dual operating accounts: one for rent collections and one to fund expenses based on approved budgets. Torchlight requires multiple levels of approval authorizations involving accounting and management personnel to establish REO property bank accounts, fund expenses, and move excess cash to investor-level custodial accounts. Although REO asset managers review monthly property manager reporting packages and the property manager's bank account reconciliations, they do not have online access rights to the bank accounts. Torchlight's accounting staff independently reconciles property manager bank account activity. For periods of higher activity, the company also has used a third-party accounting firm to assist with bank reconciliations.

Using an external auditing firm, Torchlight annually targets approximately 15%-20% of its REO portfolio for property manager audits. Torchlight obtained three property-manager audits in 2019 and four in 2018.

Assessment: Torchlight has maintained diligent practices for transitioning loans to REO status, overseeing property managers and brokers, and formulating and executing property resolution plans. Torchlight demonstrates sound control procedures for monitoring property performance and reconciling monthly property manager receipts and expenditures. Torchlight's property-manager audit program also is a best practice that further mitigates risk.

Legal and Vendor Oversight

Torchlight controls vendor selection through a centralized list of approved vendors for appraisals, environmental and engineering assessments, legal counsel, property management, and brokerage services. It also conducts a request-for-proposal bidding process to engage most vendors. Torchlight uses a designated external law firm to review environmental assessments. For most engagements, Torchlight requires vendors to use its own standardized agreements. The asset-management system tracks all pending and completed vendor work orders; the system's vendor-tracking features also enable Torchlight to revise its approved lists based on vendors' delivery performance and work quality.

During 2019, Torchlight enhanced its vetting, onboarding requirements, and monitoring practices for all third-party service providers. The expanded vendor compliance program includes: confirming the vendor's legal, tax, and state business record, confirming new and changed electronic remittance instructions through a call-back procedure, and multilevel approvals from the financial-control and special-servicing departments for new engagements. Additionally, Torchlight assesses every new vendor with a risk rating and reviews available servicer organization controls (SOC) reports from its largest and more critical vendors. Torchlight reviews vendors' risk ratings and SOC reports annually as well. As previously noted, Torchlight uses SAP Concur Technologies' vendor invoice management application, which automates invoice tracking, approvals, and payment processing, and provides vendor performance metrics.

For legal oversight, a former special-servicing department head serves as Torchlight Investors' in-house counsel. Although principally supporting the company's investment-management business, she also can advise on CMBS special-servicing matters. Torchlight uses an external general counsel to assist with CMBS servicing-agreement issues and to obtain legal opinions as needed on transactions. The senior loan-recovery manager approves law firm selections in consultation with the special-servicing department head. The asset manager and special-servicing department head, along with accounting staff, review and approve legal and all other vendor invoices before issuing payment.

Assessment: Torchlight has soundly controlled engagement and oversight practices for legal counsel and other vendors, as delineated in the company's policies and procedures. Along with the existing features of the asset-management system, the company's vendor invoice processing software and enhanced compliance requirements further strengthen this function. For Torchlight's consideration, some special servicers have realized operational benefits by centralizing law firm engagements and fee arrangements through their in-house counsel.

Managing Conflicts of Interest

Torchlight is a special servicer for several CMBS transactions in which Torchlight Investors holds the first-loss bond positions and is the controlling classholder. Torchlight does not use affiliates for its special-servicing work, but its parent has acquired a few assets from CMBS trusts using permitted purchase options. Torchlight also stated that it does not seek an additional fee from the CMBS trust if it has already obtained an equivalent fee from the borrower and collecting such a fee from the trust would create or increase a loss to a trust. Torchlight's internal compliance policies require borrowers' loan-modification fees to be at or below market rates, which Torchlight tracks. Should Torchlight execute a loan-forbearance agreement, it stated that it generally will not recognize its fee until the loan pays off.

As an added control, Torchlight Investors' chief compliance officer monitors investment-fund activities and data access for potential conflicts between business lines. The compliance officer also must approve any special-servicer fee not specified in the governing PSA.

> **Assessment:** Based on its stated compliance procedures and practices, Torchlight effectively manages its conflicts of interest. Its asset-resolution results during the past two years are consistent with the company's stated commitment to the servicing standard of working for the entirety of the CMBS trust and minimizing realized losses whenever possible.

Borrower Consent Requests

The special-servicing team also underwrites consent requests and obtains approvals through delegations of management authority, which usually require sign-off from the special-servicing division head and, for larger transactions, committee approval. Some legacy CMBS portfolios that Torchlight received because of controlling classholder changes require Torchlight to coordinate the entire process directly with the borrower and underwrite the request as though it were the primary servicer. Supported through the asset-management system, Torchlight uses underwriting and transaction-closing checklists and approval case templates.

> **Assessment:** The company demonstrates suitable controls and procedures for effective consent management. With moderating special-servicing activity, Torchlight should have enough staff in the near term for consent management. However, as it acquires special-servicing rights on new-issue CMBS transactions, and especially if the transactions empower the special servicer to manage the entire process with the borrower, the company could experience increased consent-request volume and may need to evaluate its resources for this function. Torchlight's average processing times for lease reviews and assumption requests increased in 2019, based on similar volume as in 2018. Given the variables involved, Torchlight demonstrates overall timeliness with consent reviews.

Table 4 – Torchlight Borrower-Consent Request Volume and Average Processing Times (Days)

	2019				2018			
	Total Volume (#)	Special Servicer Role Only (#)	Internal Time - All Consents	Internal Time - As Special Servicer Only	Total Volume (#)	Special Servicer Role Only (#)	Internal Time - All Consents	Internal Time - As Special Servicer Only
Assumptions	11	11	25	25	8	8	11	11
Leasing	40	40	26	26	43	38	20	19
Total	51	51			51	46		

Asset Resolution and Recovery Performance

Asset-Resolution Volume and Disposition Methods

During 2019, Torchlight fully resolved 14 assets (one modification, three note sales, two full payoffs, and eight REO sales) with total resolution proceeds or UPB of approximately $237.9 million. All resolutions involved CMBS assets. By comparison, during 2018, Torchlight fully resolved 19 assets (two discounted payoffs, four modifications, two full payoffs, and 11 REO sales) with total resolution proceeds (or UPB) of approximately $143.2 million. During 2014-17, when it managed a much larger portfolio, it fully resolved 269 assets (32 discounted payoffs, 18 note sales, 31 modified or corrected loans, 77 full payoffs, and 111 REO sales) with total resolution proceeds or UPB of approximately $2.85 billion.

Chart 5 – Resolutions by Disposition Methods (2019)*

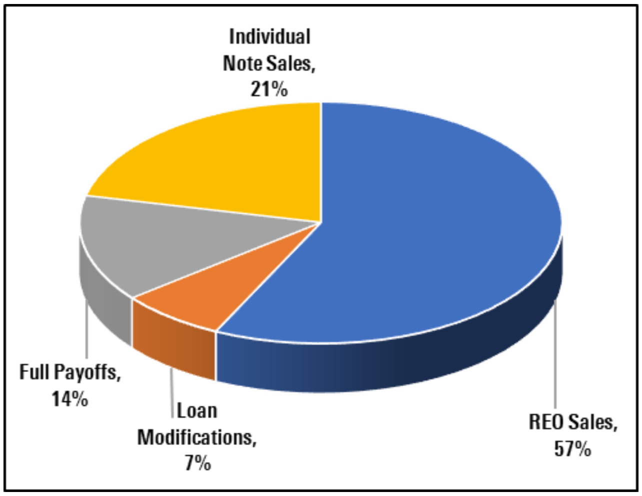
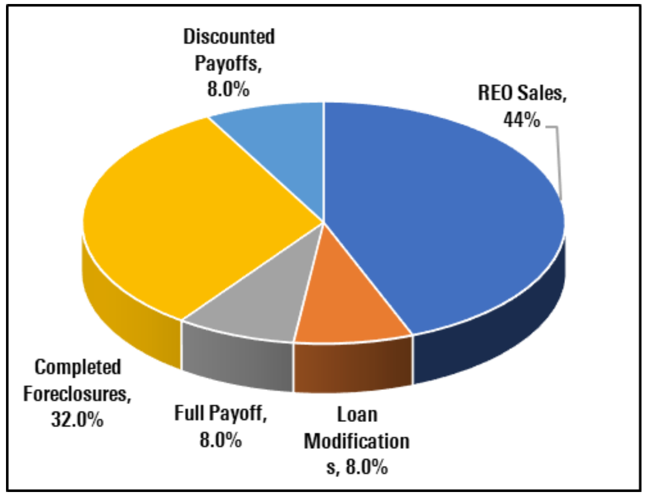


Chart 6 – Resolutions by Disposition Methods (2018)*



*Percentages are by asset count. Percentages may not equal 100% because they are rounded.

Asset-Resolution Hold Times

Accounting for the concentration of 2004-07 vintage assets and several large assets with protracted legal and collateral issues, the company's average resolution times have generally been in line with other special servicers contending with similar assets. Some especially problematic retail and office properties have caused Torchlight's average REO holding period to lengthen in the past two years.

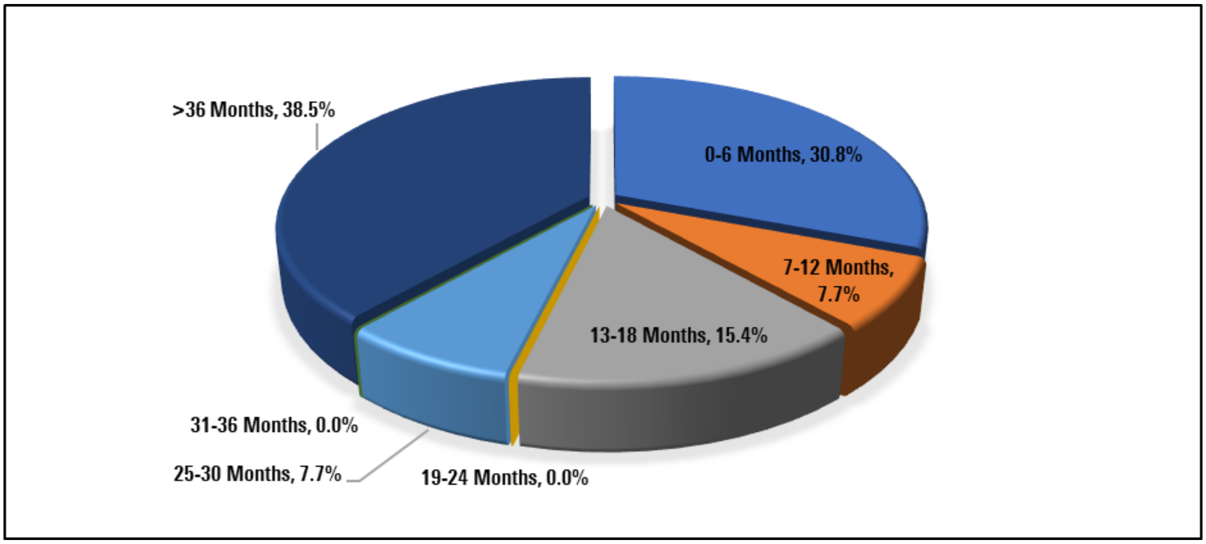
As of December 31, 2019, Torchlight held approximately 54% of its unresolved assets for two years or less, and approximately 39% for more than three years. Skewed by three assets (including a retail mall REO and an industrial park REO), the average age of assets was approximately 36 months and the median age was 14 months. The average age of the remaining active assets was approximately 18 months.

Table 5 – Special-Servicing Average Resolution Times (Months)*

Resolution Type	2019	2018	2017	Three-Year Average (Unweighted)
Corrected/Restructured	8	6	17	10
Note Sales	40	n/a	5	22
Discounted Payoffs	n/a	11	13	12
Full Payoffs	4	10	8	7
REO Sales**	27	30	21	26
Completed Foreclosures	n/a	22	8	15

*Rounded to nearest whole month. **Based on the time Torchlight held the asset as an REO. n/a - not applicable.

Chart 7 – Active Special-Servicing Portfolio Aging by Asset Count (Dec. 31, 2019)*



*Aging is based only on the time Torchlight held the asset. Percentages may not equal 100% because they are rounded.

Asset-Resolution Recovery Proceeds

Torchlight's recovery proceeds relative to loan balances and/or values have been high for most liquidations. Recoveries from most REO sales for the past three years were near or above 90% of estimated value. The company noted that the net proceeds/value percentages for some REO sales reflect the last available appraisals or broker opinions that did not include subsequent collateral or other valuation considerations.

Table 6 – Asset Recoveries Relative to Collateral Value and UPB (%)*

	2019	2018	2017
Net Recovery Proceeds-to-Value			
Note Sales	98.6 (3)	N/A	64.0 (1)
Discounted Payoffs	N/A	129.1 (2)	103.2 (7)
REO Sales	91.4 (8)	88.7 (11)**	90.7 (21)
Net Recovery Proceeds-to-UPB			
Note Sales	53.9	N/A	100.9
Discounted Payoffs	N/A	87.5	74.8
Full Payoffs	100.0 (2)	111.2 (2)	105.2 (10)

*Number of assets shown in parentheses. **99.3% based on gross proceeds.

Table 7 – Special-Servicing Loan Portfolio Activity (Full-Year 2019)

	Total Portfolio			CMBS-Only Portfolio		
	Vol ($ Mil)	Loans (#)	Properties (#)	Vol ($ Mil)	Loans(#)	Properties (#)
Loan Portfolio at Beginning of Period	174.3	10	11	174.3	10	11
Loans Transferred Into Portfolio:						
Retransferred/Redefaulted Loans	127.4	1	1	127	1	1
New Nonmonetary/Imminent Default	69.3	4	4	69.3	4	4
New Monetary Default	25.4	4	4	25.4	4	4
Total Transfers Into Special Servicing	222.2	9	9	222.2	9	9
Loans Fully Resolved:						
Modified or Corrected Loans	(4.4)	(1)	(1)	(4.4)	(1)	(1)
Individual Note Sales	(100.1)	(3)	(3)	(100.1)	(3)	(3)
Full Payoffs	(26.2)	(2)	(2)	(26.2)	(2)	(2)
Total Loan Resolutions	(130.8)	(6)	(6)	(130.8)	(6)	(6)
Adjustments or Other Loans Transferred Out	(2.5)	(4)	(5)	(2.5)	(4)	(5)
Loan Portfolio at End of Period	268.2	9	9	268.2	9	9

Table 8 – Special-Servicing REO Portfolio Activity (Full-Year 2019)

	Total Portfolio		CMBS-Only Portfolio	
	Vol ($ Mil)	Properties (#)	Vol ($ Mil)	Properties (#)
REO Portfolio at Beginning of Period	463.4	28	463.4	28
REO Sold During Period	(107.1)	(8)	(107.1)	(8)
Other REO Transferred Out	(94.6)	(16)	(94.6)	(16)
Other Adjustments	(132.3)	3	(132.3)	3
REO Portfolio at End of Period	129.4	7	129.4	7
Average REO Size	18.5		18.5	

Table 9 – Special-Servicing Loan Portfolio Activity (Full-Year 2018)

	Total Portfolio			CMBS-Only Portfolio		
	Vol ($ Mil)	Loans (#)	Properties (#)	Vol ($ Mil)	Loans(#)	Properties (#)
Loan Portfolio at Beginning of Period	549.5	22	43	549.5	22	43
Loans Transferred Into Portfolio:						
New Nonmonetary/Imminent Default	79.6	7	9	79.6	7	9
New Monetary Default	0.0	0	0	0.0	0	0
Total Transfers Into Special Servicing	79.6	7	9	79.6	7	9
Loans Fully Resolved:						
Modified or Corrected Loans	(49.8)	(4)	(5)	(49.8)	(4)	(5)
Discounted Payoffs (Excludes Note Sales)	(6.8)	(2)	(2)	(6.8)	(2)	(2)
Full Payoffs	(6.5)	(2)	(2)	(6.5)	(2)	(2)
Loan Paid Off at Foreclosure	0.0	0	0	0.0	0	0
Total Loan Resolutions	(63.1)	(8)	(9)	(63.1)	(8)	(9)
Other Cash Recoveries	(21.4)	0	0	(21.4)	0	0
Completed Foreclosures	(386.1)	(8)	(29)	(386.1)	(8)	(29)
Adjustments or Other Loans Transferred Out	15.8	(3)	(3)	15.8	(3)	(3)
Loan Portfolio at End of Period	174.3	10	11	174.3	10	11

Table 10 – Special-Servicing REO Portfolio Activity (Full-Year 2018)

	Total Portfolio		CMBS-Only Portfolio	
	Vol ($ Mil)	Properties (#)	Vol ($ Mil)	Properties (#)
REO Portfolio at Beginning of Period	340.1	21	340.1	21
Completed Foreclosures	386.1	29	386.1	29
REO Sold During Period	(80.1)	(11)	(80.1)	(11)
Other REO Transferred Out	(69.9)	(11)	(69.9)	(11)
Other Adjustments	(112.8)	0	(112.8)	0
REO Portfolio at End of Period	463.4	28	463.4	28

Table 11 – Torchlight Investors: Select Non-CMBS Distressed Asset Management and Workout Activity (2016-19)

Property Type	State	Original Balance ($ Mil)	Original Investment Type	Outcome/Status
Industrial Portfolio	Various	149.1	Distressed First Mortgage Note	A performing asset through a third-party refinancing with Torchlight Investors retaining a mezzanine loan and preferred equity. Both positions have been realized, with Torchlight retaining warrants for potential further recovery.
Office Portfolio	Various	36.0	Mezzanine Loan	Loan modification and subsequent deed-in-lieu and sale of a remaining property.
Student Housing	Michigan	18.0	Preferred Equity	Became REO property in 2018 through foreclosure. Torchlight Investors is working toward stabilization.
Hotel	Maryland	27.5	Senior/Mezzanine Loans	Became REO through foreclosure in 2018. Working toward stabilization.
Hotel	Florida	41.6	Senior/Mezzanine Loans	Equity real estate through a deed-in-lieu. Renovated and reflagged the hotel (brand upgrade). Working toward stabilization.
Office	Ohio	24.6	Distressed First Mortgage Note	Negotiated a full payoff of the loan while pursuing foreclosure.
Office	Delaware	42.6	Distressed First Mortgage Note	Became equity real estate through foreclosure in 2019. Obtained new senior loan and working toward stabilization.
Total		339.4		

Fees Collected From CMBS Trusts Versus Borrowers

Torchlight stated that it does not charge the CMBS trust a modification (or liquidation) fee if it has already obtained such fee from the borrower. Morningstar found that the company's collected and retained asset-resolution fees in recent years match with that policy. Moreover, as noted, Torchlight Investors' chief compliance officer must approve any special-servicer fee not specified in the governing PSA.

Torchlight Investors' Asset Purchases from CMBS Trusts

Torchlight Investors has exercised its permitted fair market value purchase option on a few occasions to buy assets out of legacy CMBS deals in which Torchlight was the special servicer. Torchlight Investors acquired one loan through option rights in 2017, but none in 2016, 2018, and 2019. During 2014-15, Torchlight Investors purchased six loans using its FMV option rights and purchased five REO properties out of CMBS trusts in 2014. Torchlight's stated recovery results for the trusts, based on net proceeds-to-value and realized losses, for these total CMBS asset purchases exceeded its results for asset liquidations to third parties. Torchlight noted that it obtained independent validations of the values for the assets purchased by its affiliate, as required by its servicing agreements.

Assessment: Torchlight continued to demonstrate solid recovery results through 2019. DBRS Morningstar's favorable view of the company's performance also considers that it has principally managed older vintage CMBS assets with challenging workout issues and that it has resolved many loans with minimal or sometimes zero realized losses. Although the company has had large realized losses for some REO sales, and especially large-scale retail, the corresponding sales proceeds were generally high relative to the collateral values and Torchlight's estimates for recoverability. The company especially demonstrates expertise and success resolving large and highly distressed office and retail assets, including a demonstrated ability to re-lease and repurpose space for REO assets. Torchlight has a few assets that continue to be in special servicing for an extended time. However, the company's command of the issues and its action plans indicate that it is working as proactively as practicable to liquidate these assets.

Investor and Master-Servicer Reporting

Torchlight's CMBS investor-reporting practices involve oversight from the financial-control team resulting in three levels of review. The special-servicing team's senior associate, who was hired in 2018 and has reporting experience, prepares the reports and verifies content before the special-servicing head reviews them. The financial-control team then reviews the reports and all calculations before signing off on each pool. As a last step, the special-servicing head reviews and formally approves the final reports. A separate sign-off sheet tracks the reviews and approvals.

Surveillance practices and reporting procedures address CREFC-compliant content including asset status reports, property protection advances, appraisal subordination entitlement reductions, and realized loss calculations. Torchlight noted that it routinely communicates with master servicers on loan watchlist activity, trigger events and covenant-compliance, advancing, transfers, and resolution decisions. Torchlight has all its deals as a named special servicer loaded on the Backshop system, and it reviews monthly portfolio performance reports downloaded from a CMBS data provider. The special-servicing senior associate, in conjunction with the special-servicing department head and financial-control team, coordinates portfolio transfers arising from CMBS directing classholder changes.

Assessment: Torchlight has reporting expertise with legacy CMBS transactions as well as with newer-issue transactions. Its experienced staff, sound review and approval procedures, and technology indicate that the company remains soundly positioned to provide effective asset surveillance and special-servicer reporting for CMBS trusts and investors in its affiliated debt funds.

Ranking Definitions

The numerical scale of MOR CS1 to MOR CS4 is defined as follows:

1	Exceeds prudent loan servicing standards in key areas of risk
2	Demonstrates proficiency in key areas of risk
3	Demonstrates compliance in key areas of risk
4	Demonstrates lack of compliance in one or more key areas of risk

A servicer assigned a ranking of at least MOR CS3 is deemed to comply with what we view as the minimum prudent loan servicing standards and requirements for the servicer's operational category and role. Morningstar's operational risk assessments methodology and all published reports are available at www.morningstarcreditratings.com.

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