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## Servicer Evaluation: Prelios Credit Servicing Spa

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### Table Of Contents

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Major Ranking Factors

Opinion

Outlook

Company Profile

Management And Organization

Loan Administration

Financial Position

Related Criteria And Research

# Servicer Evaluation: Prelios Credit Servicing Spa

## Ranking Overview

Servicing category	Ranking	Management and organization subranking	Loan administration subranking	Outlook
Residential mortgage master servicer	ABOVE AVERAGE	ABOVE AVERAGE	ABOVE AVERAGE	Stable
Residential mortgage special servicer	ABOVE AVERAGE	ABOVE AVERAGE	ABOVE AVERAGE	Stable
Commercial mortgage master servicer	ABOVE AVERAGE	ABOVE AVERAGE	ABOVE AVERAGE	Stable
Commercial mortgage special servicer	ABOVE AVERAGE	ABOVE AVERAGE	ABOVE AVERAGE	Stable
Unsecured credits master servicer	ABOVE AVERAGE	ABOVE AVERAGE	ABOVE AVERAGE	Stable
Financial position	Insufficient	N/A	N/A	N/A

N/A--Not applicable.

## Major Ranking Factors

- Since our last review, Prelios Credit Servicing SpA (PCS) has expanded its business development team and attracted new business. It was appointed as servicer of the first deal sponsored by the Italian government guarantee (GACS) and is currently involved in other GACS transactions. In addition, PCS signed a number of other mandates, including a servicing agreement to manage the first multiseller portfolio of nonperforming loans (NPLs) originated by a number of Italian banks. As a result, the servicer was able to replenish its portfolio and achieve positive portfolio growth, as well as raise its presence in the market. We will closely monitor the servicer's ability to maintain this trend.
- PCS' management team has extensive experience in the secure NPL market and the servicer has further strengthened its organization, recruiting senior-level resources with relevant backgrounds. The company's overall turnover rate for 2016 and 2015 had decreased since 2014. PCS' CEO was also appointed General Manager of the Prelios Group, which highlights the relevance of the servicing business within the group.
- In 2015 and 2016, PCS placed a great emphasis on training, focusing on leadership development and regulatory training, respectively. In addition, the company plans to expand the number of training courses provided in 2017 while creating a corporate academy.
- The company relies on an in-house servicing system, Phoenix, which has been used for many years. The servicer continuously updates the system in line with best practice among its peers. In 2015, PCS signed a strategic partnership with the provider of Syges, the NPL management system used by some Italian banks, to integrate the two platforms. This should guarantee a smoother loan set-up and lower the risk of data corruption when PCS manages loans from banks that use Syges.
- PCS recently reinforced its master servicing operations. It expanded the set of data required from subservicers, formalized the process of the onsite review, and introduced the assignment of subservicer rankings. We will closely monitor the effect of these changes.

## Opinion

S&P Global Ratings' affirmed its ABOVE AVERAGE ranking on PCS as a special servicer of residential and commercial mortgages in Italy and as a master servicer of residential, commercial, and unsecured credits in Italy. Our rankings (including our subrankings) reflect our assessment of the company's operations based on the major ranking factors in our criteria (see "Related Criteria").

## Outlook

The outlook on our rankings is stable. PCS provides a reliable service as master and special servicer. The company has worked on several initiatives to increase its business under management and maintain the standard of its operations. We will observe the consolidation of these changes.

## Company Profile

Company Overview	
Servicer name	Prelios Credit Servicing SpA
Date formed	2005
Parent company	Prelios SpA
Assets under management (overall)*	€9.548 billion
Assets under management (under assessment)**	€8.467 billion
Total staff	65 FTE***
Servicing centers	Two
Client types	Banks, investors, and special-purpose entities

\*Including special servicing of unsecured credits and excluding double counting of loans that are managed both in master and special servicing.

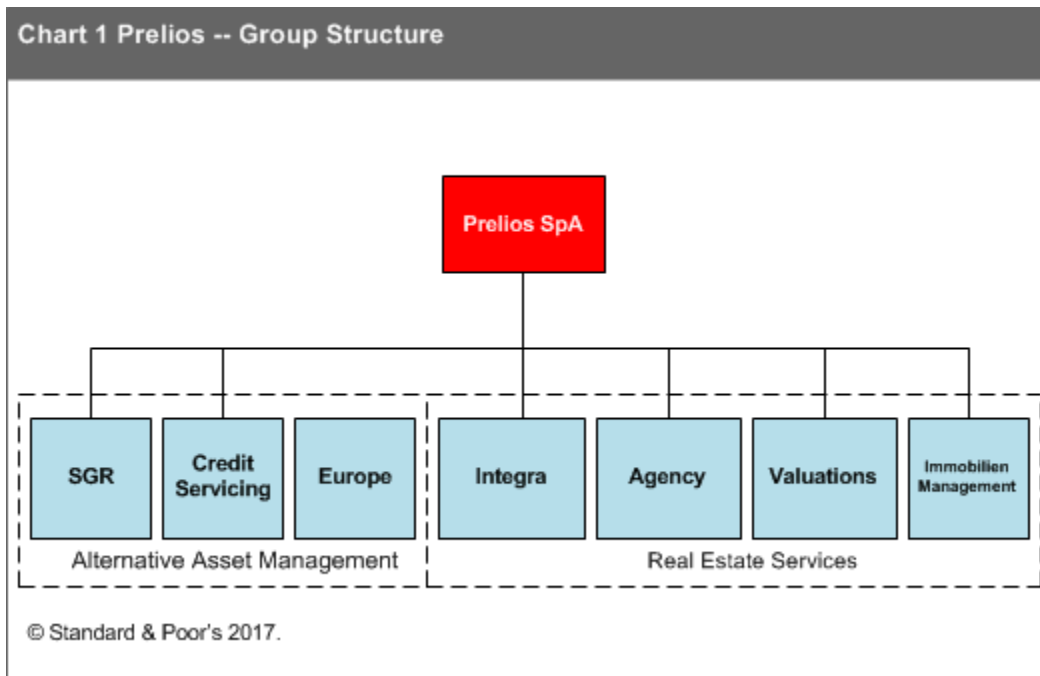
\*\*Excluding special servicing of unsecured credits and excluding double counting of loans that are managed both in master and special servicing.

FTE\*\*\*Full-time equivalents.

PCS is the servicing subsidiary of Prelios SpA and part of the Prelios Group, offering real estate services across Europe.

It is registered under Article 106 of the Italian Banking Act, allowing it to carry out a range of financial activities, including special and master servicing. PCS operates its servicing platform through the Milan head office and a second branch in Rome. The company serves banks, investors, and special purpose entities (SPEs).

PCS works in close collaboration with other companies of the group such as Integra, which offers property and facility management services, among others; Agency, the Prelios group's advisory company; and Valuations, which offers appraisal of real estate assets and portfolio (see chart 1).

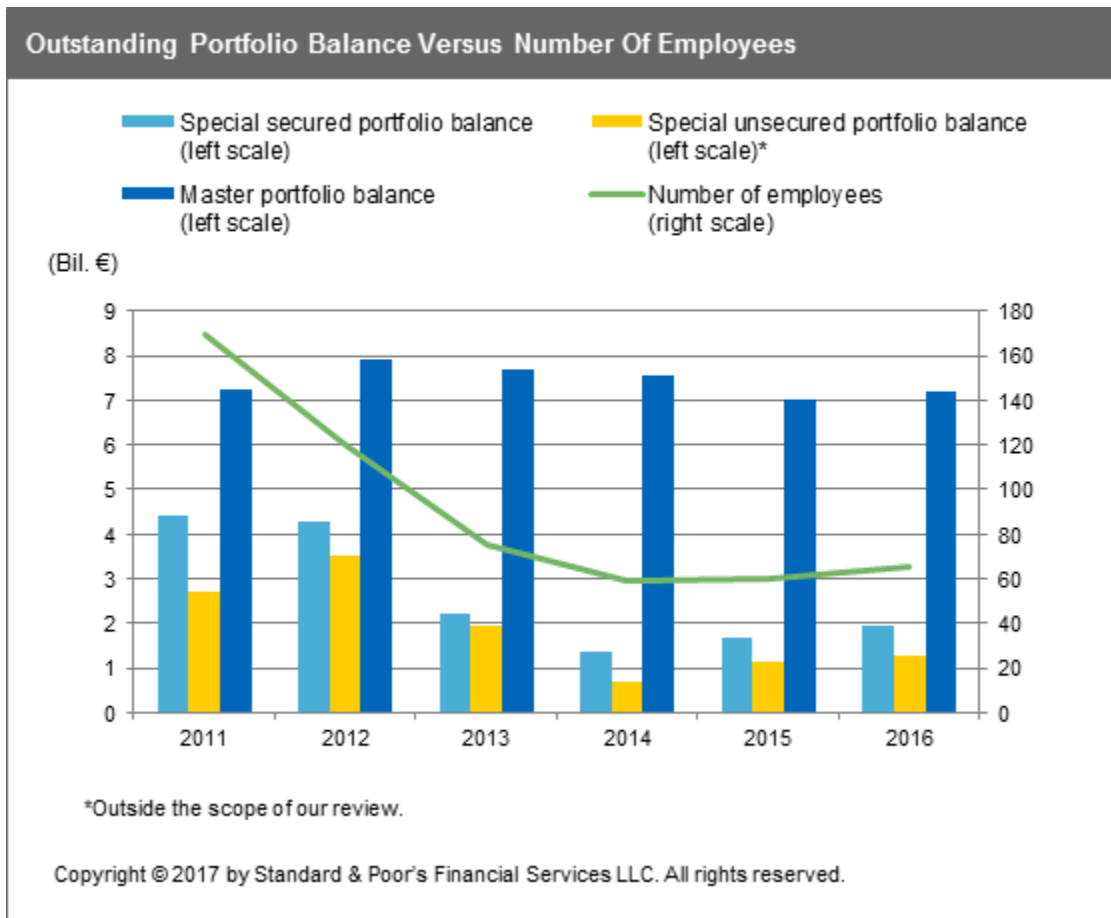


As of December 2016, PCS managed NPLs equivalent to a gross book value (GBV) of approximately €3.211 billion and 8,329 cases. Residential mortgages were 14% of this portfolio, commercial mortgages were 46%, and unsecured the remainder, which is out of the scope of our review because our rankings are limited to the special servicing operations of residential and commercial mortgages.

The master servicing portfolio was €7.198 billion and 35,843 cases over the same period. Residential mortgages were nearly 31% of this portfolio, commercial mortgages were 23.6%, and unsecured the remainder.

Since our previous review, the servicer has been involved in a number of new transactions. PCS was the first Italian servicer to take part in a public securitization embracing the GACS scheme on a portfolio originated by Gruppo Banca Popolare di Bari. The company is currently involved in other GACS deals. In addition, the servicer signed a number of other mandates, including the first multiseller portfolio of NPLs originated by a number of Italian banks.

Chart 2



## Management And Organization

We affirmed our ABOVE AVERAGE subranking on PCS for management and organization as a special servicer of residential and commercial mortgages, and master servicer of residential, commercial, and unsecured loans.

PCS has an experienced management team that successfully managed to attract new business, as well as raise the company's presence in the marketplace. Since our previous review, the servicer provided senior management training, and also focused on mandatory training related to new regulations for loan managers and for the external network. The servicer has effective internal controls in place, which support its servicing operations, and a reliable IT system, which is subject to continuous updates.

We based our subranking on our view of the following:

### Strategy and business plan

PCS registered a positive growth and improving results over the last three years. The company is going to approve its 2016 results and new three-year business plan by April 2017. Being a financial entity under Bank of Italy's supervision, PCS includes its business plan in its Internal Capital Adequacy Assessment Process (ICAAP), which it then submits to

the central authority.

During 2016, PCS boarded six new mandates equivalent to 2,098 special servicing cases and 911 master servicing cases. Over the same period, it undertook 11 due diligences and provided advisory services to banks. The company forecasts that these relationships will lead to new servicing opportunities.

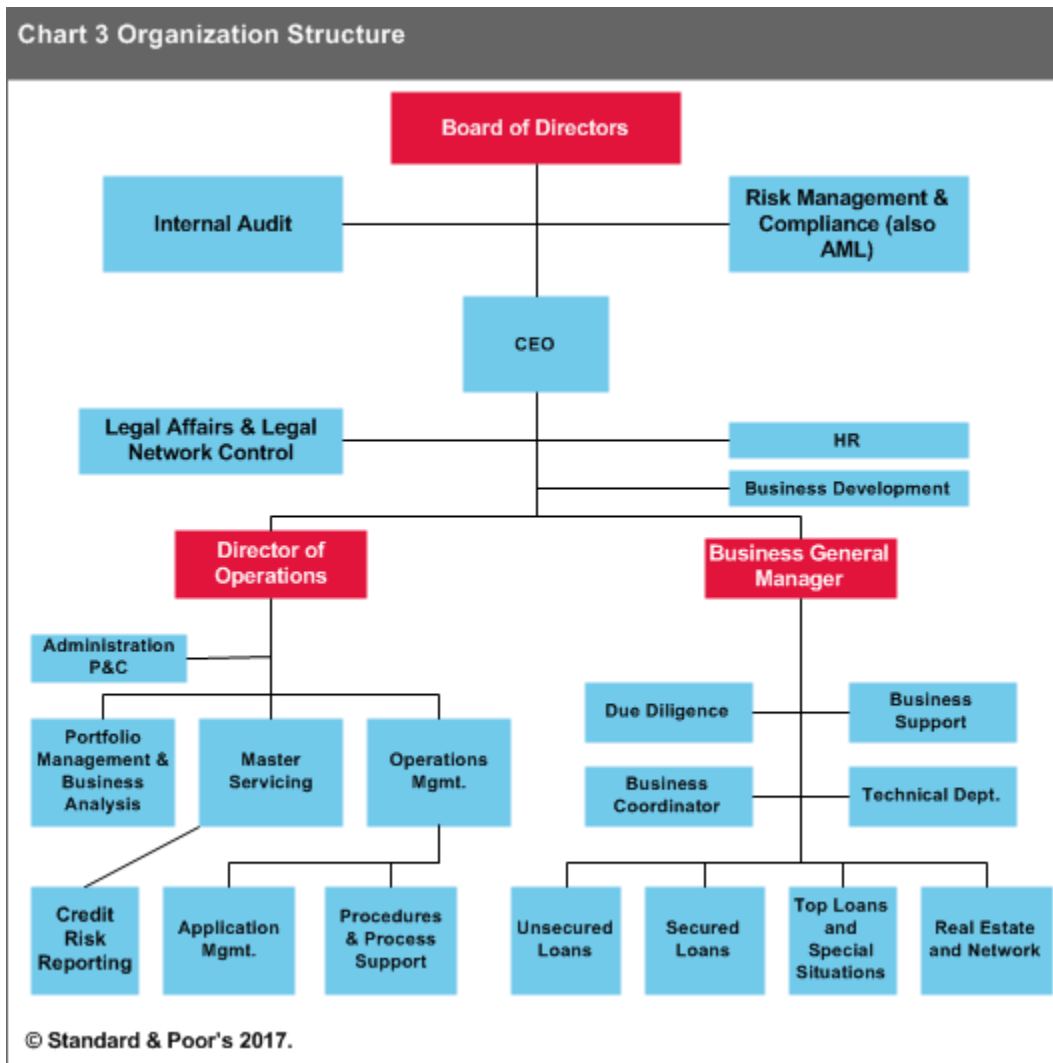
The servicer's outstanding pipeline includes several potential opportunities such as two new mandates as a special servicer and two as master servicer that the company expects will materialize by the first half of this year. As a result, PCS expects to keep on expanding across business lines and within each asset class.

### **Organizational structure, management, and staff**

As of December 2016, PCS had 65 employees (five more than since our last review) and four interns. The servicer's control functions--audit, risk management, compliance, and anti-money laundering (AML)--report directly to the board, which enhances their independency.

Since our previous review, Prelios Group has appointed PCS' CEO the additional role of Prelios Group general manager, which, in our opinion, highlights the relevance of the servicing branch within the group. Moreover, PCS internalized the internal audit function to align the structure to a conservative interpretation of new regulatory requirements. The company's business model and the corresponding organization structure have otherwise remained largely unchanged.

The servicer's structure guarantees the separation of the special and master servicing businesses as they report to two different departments: Business General Management, which includes the special servicing activity, and Operations, which includes administration, planning and control, IT, and the master servicing activity. There are internal managers or small teams in charge of other functions such as human resources (HR). Some of them can also receive support from the Prelios Group. The latter also provides external communication support.



PCS advised that the company recruited a number of senior resources with specific knowledge in the NPL market over 2015 and 2016. Overall staff turnover has decreased to 14% as of December 2016 from 18% as of end-2015 and 32% as of end-2014 (see table 1).

**Table 1**

Staff Turnover				
	2014	2015	2016	
Staff at beginning of period	75	60	59	
Number of joiners	9	10	14	
Number of staff leaving voluntarily	(21)	(8)	(7)	
Number of staff leaving involuntarily	(3)	(1)	0	
Number of expired contracts	0	0	0	
Number of staff redundant	0	(2)	(1)	
Staff at end of period	60	59	65	

Senior management and operations staff experience and tenure are at an appropriate level. The senior management team has over 20 years of experience in the NPL market and nine years of company tenure (see table 2).

**Table 2**

<b>Average Years Of Industry Experience/Company Tenure</b>	
<b>Experience</b>	
Senior managers	<b>20.3</b>
Middle managers	21.6
Master servicing staff	13.9
Special servicing staff	14.0
<b>Tenure in current position</b>	
Senior managers	9.3
Middle managers	13.6
Master servicing staff	13.9
Special servicing staff	7.8

PCS maintains a good level of communication with staff, organizing regular town hall and informal meetings and enhanced communication, using its intranet to increase staff engagement.

### **Training**

PCS' HR officer, supported by a member of the Prelios Group HR team, is in charge of recruitment, training, and the staff appraisal system.

PCS aligns its people's management in accordance with the Prelios group's policies and procedures. As a result, PCS has a performance management model that sets skills and abilities for each role, and defines ways to identify gaps of skills for every employee against those targets. The HR officer sets annual training and development programs for employees to fill potential skill gaps, and manages its performance and incentive program. PCS considers this model a transparent means of managing individual performance against pre-set objectives and to determine training needs.

### **Audit**

Internal audit is the third line in the company's three lines of defense model, established in its current format in 2007. The other two lines of defense are the risk management function (mapping and working to minimize risks) and operative staff (to reduce any operative failure). The internal audit function reports to the board of directors, which creates sufficient independence from operations and maintains the discipline's integrity, in our view. PCS internalized the audit function in 2016.

PCS' audit function methodology is risk-based so the risk associated to each function determines the frequency of the audit review. At the beginning of each year, the board approves the plan proposed by PCS' internal auditor and reviews progress semiannually. If remedy actions are required, the internal auditor and the head of the relevant department identify the action plan. PCS uses a software (GAIA) to process the plan as due and to record audit outcomes.

PCS' 2016 audit plan focused on ICAAP production process, reporting activity to Centrale dei Rischi, assessment of



conflict of interest policy, information security, discounted pay-off management process, and adherence to contractual obligations. The results of the above listed audit reviews were all satisfactory up until December 2016 and remediation plans were in progress as expected.

### **Risk management and compliance**

Two resources compose PCS' risk management, compliance and AML department--PCS' second line of defense. The head of the department has significant internal controls expertise while the second team member has legal expertise and several years of experience in the field of compliance and AML.

The risk management function identifies all relevant company's risks, evaluates them, and suggests solution to avoid, mitigate, or manage those risks. This requires:

- Analyzing risks embedded in new business acquisition;
- Drawing up the ICAAP report together with the CFO;
- Verifying the adequacy of the risk management process and map risks;
- Coordinate with internal audit, and compliance;
- Coordinate with Group risk;
- Producing a semiannual report to the board of directors and to the senior management;

Since our last review, the servicer introduced a new risk register for the identification and tracking of risks. We believe IT software helps automation and controls and the introduction of the risk map enhanced the effectiveness of this function. The risk management process is also supported by software tools monitoring operational performance against the risk framework.

The compliance function was established in 2008 and performs the following duties:

- Monitoring the effectiveness of the organizational structure, processes, and procedures in respect to potential non-compliance;
- Making recommendations to senior management in relation to potential non-compliance within each operational area;
- Verifying proper handling of complaints, focusing on those received from the BOI;
- Verifying supervisory authority disclosure obligations;
- Managing the company's Law 231/01 obligations; and
- Supporting employee compliance training, including Law 231/01.

The AML function reviews processes and procedures to minimize the risk of money laundering; one employee carries out all relevant tasks, helped by operating staff and business functions. PCS' AML vigilance covers all aspects of the business including:

- Identifying the AML-relevant regulation in force;
- Monitoring and regularly testing AML-related internal controls, proposing necessary changes and ensuring they are implemented;
- Checking servicing IT platforms to ensure they are AML compliant;
- Sending aggregate data monthly to the BOI's Financial Intelligence Unit;
- Working with HR to develop appropriate staff training on AML; and
- Advising and assisting corporate departments and senior management on AML.

The second line of defense prepares an annual plan of activities and tests, which it submits to the board of directors for approval. The statutory auditors and the board of directors also receive a semiannual report detailing the outcomes from all activities performed.

During 2016, PCS received 29 complaints regarding servicing, up from 15 (in line with the special servicing portfolio increase); 91% of these were resolved in the appropriate time frame (30 days). PCS says the majority of complaints received relate to debtors having been reported to Centrale dei Rischi.

### **Policies and procedures**

A single resource maintains the policies and procedures manual reviewing it at least annually--in line with industry best practice. The director of operations updates the board on related process changes with a similar frequency while the board has to approve changes to policies. Additionally, the compliance function can propose updates as a result of changes to the legal framework or to the group's directives. Similarly, process owners within the relevant organizational units can issue new ones. The new or updated procedures are published upon validation of the top management, legal department, and compliance.

Staff can access policies and procedures through the company intranet and changes are communicated via email. There is version tracking in place and the compliance department duly controls the storage of previous manuals in the company's central repository.

### **Systems and servicing platform**

PCS has two internal IT resources and three staff fully dedicated to the PCS part of the IT function, which remains centralized within the Prelios Group, supported by three external IT resources. Seven internal resources and 20 external professionals compose the corporate IT department looking after a group of almost 400 staff. This team is responsible for prioritizing and delivering IT requests. The team monitors ongoing projects on a monthly basis, updating a master plan. Employees can also recommend system upgrades passed to the IT team for development upon management approval.

PCS' core servicing platform, Phoenix, was built in-house and integrated with other components such as the accounting system (SAP) and the real estate management tool (PMS). Authorized external parties can access Phoenix and other internal applications. External brokers access PMS via a secure web link and external solicitors update Phoenix through a tailor-made user profile, which grants them access to the cases under their responsibilities. Phoenix backs up master and special servicing activities supporting:

- Management of NPL portfolios since the due diligence phase;
- Management of judicial and extrajudicial collections;
- Management of dynamic business plans;
- Management of collections and recovery expenses;
- Borrower management; and
- Management of Centrale Dei Rischi reporting.

A detailed user manual for Phoenix is available to all staff in electronic format.

Phoenix provides daily feeds to the Data Warehouse, which supports customized and standard data analysis. A basic

user can extract pre-defined reports with real-time data while advanced users can also produce customized reports. Similarly, users can access data based on their profile so team leaders can only access the data of loan managers assigned to them.

PCS continuously upgrades Phoenix to meet business needs. In 2015, the servicer signed a strategic partnership with the provider of Syges, an NPL management system used by some Italian banks, to integrate the two platforms. This should ensure a smoother loan boarding and lower risk of data corruption when PCS manages loans from banks that use Syges. Other IT developments since our previous review include:

- Quicker upload of higher volume of information from PCS to Prelios Valuations, which speeds up due diligence timing;
- Interface between Phoenix and PMS allowing loading of positions on PMS through Phoenix;
- Enhancement of the process to write off a credit, which guarantees a prompt update of Centrale dei Rischi; and
- Upgrade of the cash report application (Re.G.In.a).

PCS outsources infrastructure services such as the data center, network, and the service desk to Ingegneria Informatica SpA (Engineering), an external third party provider that is listed on the Milan Stock Exchange. Some applications are backed up by a third-party provider, SAP, which also supplies the general ledger software.

Data is backed up daily and retained for three weeks. There is also a daily and weekly full file back up. Data is stored in backup libraries at another site in Milan, and Oracle archive logs are stored on a backup disk held at a separate site in Bologna. The backup data is not encrypted.

The servicer has anti-virus software, and monitors physical or electronic system intrusion. PCS has a password policy in place requiring renewal every 90 days. If a user no longer has partial or full systems access, IT removes their permissions.

### **Disaster recovery/business continuity**

The application manager takes care of business continuity and the disaster recovery plan, which is based on business impact analysis and is updated and tested annually. The scope of the plan is to provide prompt recovery of fundamental business processes. Business continuity training is provided to all staff. Since our previous review, the Prelios Group decided to align its business continuity management with PCS' approach, confirming the servicer's solid policy.

The disaster recovery site is outsourced to a third-party provider and is located around 150km away from Milan. There is also an alternative disaster recovery site in close proximity to Milan. A specific procedure revised in 2016 defines roles and responsibilities for the disaster recovery activity. As part of the plan, the business director, operations director, a legal representative, an internal auditor, and risk, compliance and AML officer are in charge of leading the remedy action plan in the aftermath of a critical event. The last disaster recovery test was in November 2016. Critical data were restored in less than one hour. A generator provides power for up to 30 hours in the event of a power cut.

The company business continuity policy states that staff can move to another part of the building if an event affects only a certain office area, work from home if the whole office building is affected or move strategic staff to the other company branch in a different location in case of a major event. All employees can work securely from remote

locations via web access using either a corporate laptop or a personal PC. The distance between the two company offices that act as business continuity sites for one another is 600km. Although we would normally anticipate a business continuity site to be in closer proximity, this is mitigated by the staff's ability to work from home, if necessary.

## **Loan Administration**

We affirmed our ABOVE AVERAGE subranking on PCS for loan administration as a special servicer of residential and commercial mortgages, and master servicer of residential, commercial, and unsecured loans.

The servicer has a well-established loan boarding process. In our view, PCS has robust special servicing operations. The servicer has appropriate controls in place relating to the external network of professionals that support its servicing activity. As anticipated at the time of our previous review, the servicer has strengthened its controls on subservicer activity.

### **Loan boarding**

PCS has an established process for new portfolio boarding, whether it is acting as special or master servicer. The company uses Phoenix for new loan boarding. Clients provide Excel files that include predefined data automatically imported in Phoenix through the Oracle-based application.

Each loan is uploaded with a minimum set of mandatory data duly reviewed before the loan becomes live in the system.

PCS advised that all staff has been trained on the loan boarding process as a leveraged team of resources is formed for each boarding activity. For due diligence and/or boarding of a new portfolio, PCS appoints a project manager responsible for coordinating across all relevant departments within PCS and relevant providers, including Prelios Group. Generally, two functions— legal and commercial—support the project manager. During the boarding process, the business analysis function performs a daily check on loaded positions, summarizing the anomalies reported by the system and reporting them to the relevant loan manager through a control report.

In most cases, the loan originator sends the relevant documents electronically. If no electronic copies are available, external parties scan the documents using a checklist template that PCS created. Originators sometimes provide representations and warranties where documentation is not supplied.

PCS advised that the duration of the boarding process depends on the size of the portfolio and can take between 15 and 30 days.

### **Special servicing**

As of December 2016, PCS managed a total portfolio of loans in special servicing equivalent to €3.211 billion from €2.816 billion at the end of 2015 (see table 3). The special servicing portfolios consist of a mixture of secured and unsecured positions, with about 60% (€1.934 billion) of the total balance of loans being secured.

Table 3

Special Servicing Portfolio Evolution						
	--2015--		--H1, 2016--		2016	
	Amount (Mil. €)	No. of cases	Amount (Mil. €)	No. of cases	Amount (Mil. €)	No. of cases
<b>Type of credit</b>						
Residential mortgages	419	2,525	418	2,577	462	1,861
Commercial mortgages	1,248	1,464	1,274	1,464	1,472	1,215
Unsecured loans*	1,149	4,517	1,084	4,448	1,277	5,253
Special servicer	2,816	8,506	2,776	8,489	3,211	8,329
<b>Geographic distribution</b>						
North	1,046	3,134	774	3,248	1,021	3,083
South and the islands	958	3,612	1,056	3,535	1,079	3,448
Center	812	1,760	946	1,706	1,111	1,798
Total	2,816	8,506	2,776	8,489	3,211	8,329

\*Outside the scope of our review. H1--First half.

The special servicing team manages NPL from the initial due diligence till closing, taking care of the work out of the loan, the management of the real estate-owned companies (REOCOs)--if required--and marketing/sales of collateral. And through the process, PCS receive support from Prelios Valuations, Prelios Integra on REOCO, and from Prelios Agency on marketing/sales.

The PCS internal special servicing team currently comprises 25 staff. The special servicing team reports to the business general manager and is specialized by loan size and asset type and thus structured in three different units:

- The secured loans unit--in charge of collection of secured loans with an amount lower than €900,000. Each loan manager is responsible, on average, for 300 positions;
- The Top loans and special situations unit--responsible for recoveries on secured loans with an amount higher than €900,000 and for corporate unsecured loans. There are five experienced employees based in Milan (including the manager) who focus on larger, more complex loans that require a specific approach. PCS expects each team member to manage on average 80 loans.
- The unsecured loans unit (outside the scope of our review for the special servicing activity) is in charge of arrears and collection of credits not backed up by any collateral.

The business model for special servicing relies on a continuous interaction between internal loan managers and external network of professionals supporting the servicing activity. Loan managers define and execute the best recovery strategy coordinating and monitoring the work of external legal and real estate service providers, which include:

- 400 lawyers as of December 2016, which a PCS team, led by a qualified lawyer, coordinates. PCS uses a performance grid to measure the lawyers' effectiveness. It includes quality of IT, quality of invoicing, and the capacity to achieve discounted pay-offs. The panel of lawyers is also incentivized to try and extract monies from courts as quickly as possible. PCS has set up a test environment to enable invoices from lawyers to be processed through Phoenix to reduce time, errors, and costs. Some lawyers can directly update Phoenix, otherwise the internal loan manager does it. The servicer provides training to external lawyers at their head offices in Milan;

- Prelios Valuations, which is an independent entity within the Prelios Group that appraises and values portfolios and individual properties. Its network provides national coverage across Italy; Valuations developed Casaclick, a real estate trading portfolio website, which a number of external parties use, including real estate advisers;
- Prelios Integra, a property management company of the Prelios group, which has a long-standing track record in development and renovation projects. PCS uses Integra for REOCO transactions;
- Prelios Agency is an estate agency subsidiary that employs a network of about 450 local agents who provide coverage across Italy for both commercial and residential properties. Servicer operations works closely with the Agency team as and when required.

The allocation of the loan is based on specialization and each manager's current workload. The business general manager approves any diversion from general allocation criteria. PCS has a prescribed workflow for special servicing to create a consistent approach to loan management. The entire special servicing team follows the same workflow. Where possible (in common with other servicers we rank), the team's emphasis is biased toward negotiating nonjudicial (out of court) settlements with debtors. This generally speeds up resolutions because in Italy the legal process can be protracted. The team has a defined approval process for nonjudicial settlements so that it can efficiently deal with debtor proposals. A loan manager (or external lawyer) negotiates a proposal with a debtor and inputs the details into Phoenix. The system then undertakes an analysis using net present value and discounted cash flow calculations. The negotiated proposal is then submitted to and considered by the top management. Finally, the portfolio manager checks everything and sends a resolution to investors for their approval. A response confirming the decision is then sent to the debtor.

Upon loan allocation, the loan manager is responsible for achieving the recovery target for each loan and for maintaining the quality of the data input into the company's systems, even if the management of the loan is outsourced to external service providers. There is a bi-weekly call in place organized by the general business manager to monitor the performance of loan management. The business analysis team reports on special servicing results as well as does pre-appointment checks prior to the appointment of new lawyers.

### Master servicing

As of December 2016, PCS managed a master servicing portfolio accounting for €7.198 billion. The volume of assets under management by GBV is higher (+2.5%) than last year. PCS works as special servicer on 12.6% of the overall master serviced portfolio and other three servicers work on the remaining portion (see table 4).

**Table 4**

<b>Master Servicing Portfolio Evolution</b>						
	<b>--2015--</b>		<b>--H1, 2016--</b>		<b>--2016--</b>	
	<b>Amount (Mil. €)</b>	<b>No. of cases</b>	<b>Amount (Mil. €)</b>	<b>No. of cases</b>	<b>Amount (Mil. €)</b>	<b>No. of cases</b>
<b>Type of credit</b>						
Residential mortgages	1,990	11,508	2,180	12,382	2,237	12,686
Commercial mortgages	1,735	2,799	1,471	2,513	1,698	2,706
Unsecured loans	3,299	24,065	3,240	22,877	3,263	20,451
Master servicer	7,024	38,372	6,891	37,772	7,198	35,843
<b>Geographic distribution</b>						
South and the islands	3,252	12,882	3,979	17,363	4,275	17,705

**Table 4**

<b>Master Servicing Portfolio Evolution (cont.)</b>						
	<b>--2015--</b>		<b>--H1, 2016--</b>		<b>--2016--</b>	
	<b>Amount (Mil. €)</b>	<b>No. of cases</b>	<b>Amount (Mil. €)</b>	<b>No. of cases</b>	<b>Amount (Mil. €)</b>	<b>No. of cases</b>
North	1,954	12,484	1,445	10,096	1,500	10,103
Center	1,818	13,006	1,468	10,313	1,423	8,035
Total	7,024	38,372	6,891	37,772	7,198	35,843

H1--First half.

Seven staff members make up the master servicing department, which managed 10 portfolios as of December 2016. The head of the master servicing team also leads the portfolio management and business analysis department--including five more employees--and reports to the operations director. Being two relatively small teams that share synergies, PCS maintains them under the same leader, who reports to the director of operations.

The master servicing team uses Phoenix as well and performs the following functions:

- Master activities that involve bank account reconciliation, management of the SPE debt cycle e.g. expenses reporting and invoices payment, as well as total loan outstanding calculations;
- Credit risk management, which involves regulatory reporting to the BOI and all other relevant Italian authorities including monthly reporting to the Credit Risk Register, and complaints management;
- Subservicer monitoring; and
- Calculation and paying activities that comprise checking bank account movements, arrangement of the payment report, including instructions on how to allocate the SPE's available funds in line with payment waterfall.

Some of the functions are not limited to the master servicing activity and are therefore out of the scope of our review.

Since our last review, PCS introduced a ranking for each sub-servicer. The assessment range on a scale from 1 to 5--5 being the most positive result--reviewed on a quarterly basis. The ranking is based on a list of key performance indicators (KPIs) that PCS produces to monitor the sub-servicer's activity, internally called control panel. The director of operations, a representative of the legal department, the risk officer, and the internal auditor meet quarterly to discuss the control panel. As a result, they can plan further monitoring activity or review the actions and review the on-site visits calendar to the sub-servicers. For example, the master servicing team verifies cash collection performance on a monthly basis and a critical situation may trigger an earlier review of the sub-servicer ranking.

Similarly, PCS has formalized the on-site reviews process since our previous review. The company also revamped the checklist that sub-servicers need to complete on annual basis, covering information such as hardware, software, archive management, collection procedures, and internal controls. The checklist information is used as part of each subservicer ranking and desktop review.

### **Payment processing**

PCS is responsible for payment processing. There are two employees working on payment processing who are responsible for monitoring the payments work that S.A.R.E. does for PCS e.g. invoices payment. The payment process is automated across most areas, using Phoenix and the DWH, but there is some manual input. Because of the portfolio's nature (mostly NPLs), money is collected through credit transfers or checks/bank drafts, rather than

through direct debits. It is applied to debtors manually.

Bank accounts are reconciled bi-weekly, and payments that cannot be applied immediately are held on suspense to allow the staff the opportunity to resolve suspense items. It takes two-and-a-half days, on average, to resolve items in suspense.

We believe adequate controls and segregation of duties maintain the integrity of the process.

### **Client management and investor reporting**

There is a business development department in place that reports to the company's CEO. It increased to two employees in 2016. Its aim is to promote PCS services to third parties and share the responsibility to consolidate the relationship with outstanding clients with PCS senior managers. Indeed, PCS senior managers hold regular meetings with its clients to provide information on performance.

PCS has several reporting duties, based on the terms of the mandate and the role that the servicer is performing. As a master servicer, PCS produces SPV cash and expenses reports, monthly credit risk register reports, quarterly reporting to BOI, semi-annual reporting to BOI about securitizations, and KPIs reports. As a special servicer, the servicer delivers investor reports, business plan reports and ad hoc reports. The business analysis department provides regular reporting to the PCS management. Since our previous review, PCS has started producing a new loan by loan report as part of securitizations in accordance with the GACS laws.

PCS has trained staff in investor reporting; nine are now working on report production and related communication. Investor reports production takes eight to 10 days. PCS sends them by mail in PDF format. Moreover, PCS has launched a new website with a restricted user access area where the servicer can exchange restricted information with clients. Reporting is automated through Phoenix. PCS has not reported any errors or queries since our previous review.

## **Financial Position**

We consider PCS' financial position to be INSUFFICIENT based on our assessment of the audited 2013, 2014, 2015, and half-yearly 2016 financial statements of PCS and Prelios Group. PCS reported improved profitability results and registered a loss that was lower than it expected, but the servicer did not fully meet its 2015 targets. The group will approve its 2016 results and next three-year business plan by April, after which time we could reassess our view of PCS' financial position based on this wider set of information.

This opinion does not replace that of a senior debt or counterparty credit rating.

## **Related Criteria And Research**

### **Related Criteria**

- Revised Criteria For Including RMBS, CMBS, And ABS Servicers On Standard & Poor's Select Servicer List, April 16, 2009
- Servicer Evaluation Ranking Criteria: U.S., Sept. 21, 2004



**Related Research**

- EMEA Servicer Evaluation Industry Report 2016, Jan. 31, 2017
- Italian Servicers Could Be Part Of The Solution To The Nonperforming Loan Burden, Nov. 21, 2016
- ABOVE AVERAGE Ranking Affirmed On Prelios Credit Servicing As Residential And Commercial Special Servicer In Italy, Feb. 22, 2017
- Servicer Evaluation: Prelios Credit Servicing SpA, Oct. 26, 2015
- Select Servicer List, published monthly

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