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Servicer Evaluation: FinSolutia S.A.

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Table Of Contents

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Opinion

Standard & Poor's Ratings Services' overall ranking on FinSolutia S.A. is AVERAGE as a master servicer of residential mortgages in Spain.

The ranking reflects the following, in our view:

- FinSolutia has recruited staff selectively to create a mixture of industry-experienced people and younger, professionally qualified individuals.
- The company has, in our view, invested in the best IT proprietary systems that it feels it requires to optimize operations and to provide capacity for planned future growth.
- FinSolutia is a relatively young company but has achieved growth steadily. Staffing levels have increased to a level where the company now believes that it can both expand its master servicing activity and move into other areas such as special servicing.
- The number of portfolios for which FinSolutia currently provides master servicing is likely to constrains any future potential increase to the ranking to an extent, in our opinion. We note that the company is confident of increasing this number through conversion of current pipeline leads.
- The company has in our opinion reached a size where it would benefit from a dedicated and experienced HR function.
- Due to the volume of loans being master serviced since incorporation, FinSolutia has only recently deemed it necessary to establish an internal audit function. It has now appointed a suitably qualified person to establish an audit plan, which has received board approval. Implementation of the plan has started.

Outlook

The outlook is stable as a master servicer of residential mortgages in Spain.

Company Profile

FinSolutia was incorporated in 2007, promoted by the managing partner and funded as a joint venture between UBS AG (London branch), Espirito Santo Investment, and Ongoing Strategy Investments. The board of directors comprises a mixture of UBS and Espirito Santo Investment directors as well as the managing partner.

FinSolutia's initial target market was special servicing for nonperforming loan (NPL) positions in Portugal. The company believes that the changing economic environment and market created the opportunity for it to extend activity into other operational and geographic areas, in particular the master servicing arena. Currently, FinSolutia's strategic objective is to assist in facilitating loan portfolio transactions, in addition to the provision of advisory and servicing services for the acquisition and/or management of loan portfolios.

In 2007, FinSolutia opened its first office in Lisbon and last year it made a strategic decision to open a second office in Madrid with the aim of generating business in the much larger Spanish market. At present, FinSolutia thinks that there are new opportunities in the special servicing arena, particularly in Spain, and it is planning a strategy to position itself in such a manner that it can take advantage of these opportunities and develop new business.

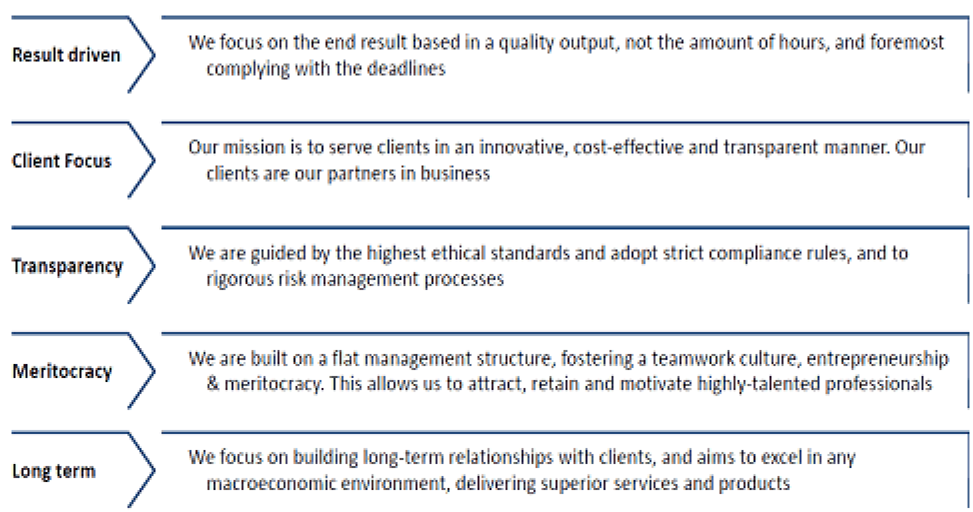
Management And Organization

Our subranking on FinSolutia for management and organization is AVERAGE for the master servicing of residential mortgages in Spain.

Company strategy and growth objectives

FinSolutia's core principles (see chart 1) are based, firstly, on the recruitment and retention of experienced employees who can then work together as a team to help the company in achieving its corporate objectives. Secondly, FinSolutia places great emphasis on developing a proprietary IT platform, with the aim of achieving highly automated, integrated, and standardized processes and services. These principles feed into what FinSolutia believes is an innovative business model, allowing it to help clients to react quickly to changing market conditions, with tailor-made solutions through full-scale value-added services. Infrastructure development is overviewed by the Business Intelligence and Support (BIS) team, which is responsible for coordinating and collating internal and external data.

Chart 1: FinSolutia Values And Principles



Source: FinSolutia.

We understand that the directors believe in ensuring that there are open and clear communication channels, so that all employees understand the company's objectives and can therefore contribute to helping achieve them.

FinSolutia regularly undertakes a review of its operation to identify and assess opportunities created by the flexibility and scalability of its business model. The company also looks to remain vigilant to threats to the business, such as new entrants to the market and fee erosion. Increased regulation also challenges the business model but

FinSolutia thinks that the flexibility that its operations allow leaves it well placed to respond to these threats, as well as regulatory changes as required.

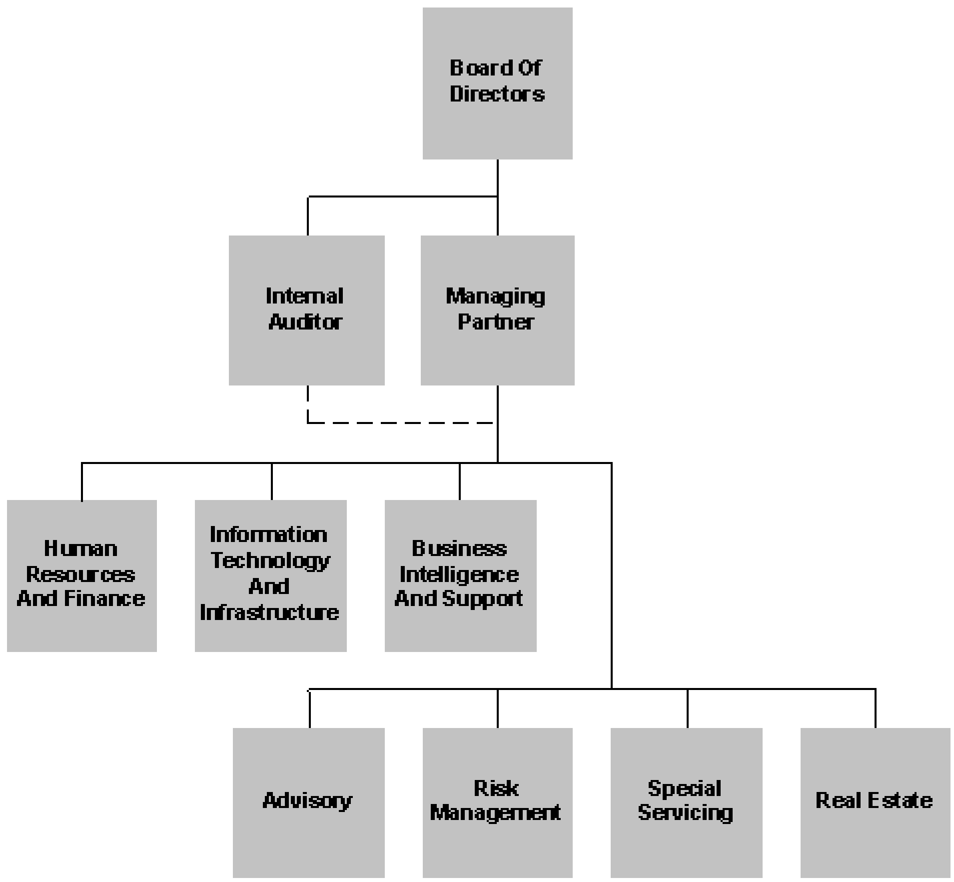
FinSolutia thinks that it is likely to restrict its operations to the residential mortgage market in the short term, on the basis that it believes this segment of the market is more sustainable, is familiar to it, and is aligned to skill sets and IT systems that the company has developed. It expects that there may be growth in the volume of asset-backed securities (ABS) loans, and whole-loan transactions which may require the oversight of a master servicer and of an independent servicer and is keeping a close watch on this segment of the market.

We understand that FinSolutia has a good pipeline of business, and while allowing for current market conditions, it is optimistic that it will be able to convert this into formal instructions, particularly as negotiations are fairly advanced in more than one instance. Part of this pipeline includes some possible special servicing contracts, and staffing levels in Lisbon and Madrid are being scaled up in anticipation of receiving formal instructions for some of these. At this stage, FinSolutia is not asking us to provide a ranking for special servicing.

Staff/structure

FinSolutia has a fairly flat but agile management structure which we believe enables it to react quickly to changing market conditions, and which the company has established to optimize its operational capacity (see chart 2). We are of the view that this structure is appropriate when considering the size of the company.

Chart 2: Management Structure



The number of employees at FinSolutia has increased to 30 as of April 2010, which is a significant increase from the 15 that they advised us were employed in April 2009. There have been 22 new arrivals and seven departures in this period. Currently, 17 employees work in Lisbon and 13 in Madrid, and we are of the view that there is a good level of interaction and support between the offices.

The company's recruitment policy is determined by the level at which vacancies are advertised. For example, FinSolutia generally looks to university graduates to fill trainee-type roles and may use the services of recruitment agencies for more senior or experienced positions. It has developed a recruitment template internally in order to standardize the process across the company. The seven departures were mainly people who did not meet the company's expectations and whose situation required to be resolved. The percentage of departures relative to the number of new employees at the company is higher than we would have anticipated and we have discussed this with FinSolutia. The company explained that it is refining its recruitment process with the aim of ensuring that a higher proportion of any new intake in future are suitable to remain in the company's employment.

Employees can give and receive regular feedback on their performance through one-to-one sessions with their line manager, using what FinSolutia describes as a 360-degree assessment feedback methodology. The company believes that this is a disciplined and effective method of performance management.

The company at present does not have a separate HR function. The responsibility for dealing with staff issues is currently fulfilled by the recently appointed head of financial operations, having previously been under the control of the managing partner. We understand that the company plans to recruit a qualified HR specialist at the earliest opportunity. In our opinion, this would be a sensible move, as the company has grown to a size that would warrant a permanent appointment to deal with recruitment, training, and other HR matters.

Table 1 shows staff's levels of industry experience, which we consider to be in line with the ranking assigned. Tenure at FinSolutia is low, as we may expect considering the recent expansion of the company.

Table 1

Average Years Industry Experience/Company Tenure In 2009

Experience			Tenure		
Senior managers	**Middle managers**	**Staff**	**Senior managers**	**Middle managers**	**Staff**
9.01	4.43	Not available	2.07	0.99	Not available

FinSolutia has internally developed a staff survey and intends to undertake this exercise every year, as an effective means of gauging the state of the company by assessing motivational levels, as well as being sensitive to employees' opinions and feedback. The first survey occurred in May 2010, with a response rate of 100%. We have received a summary of the results, which have been communicated to the participants, and generally they appear to be positive in terms of employees' views of the company. FinSolutia views communication with staff as important, particularly with the establishment of the Madrid office, to ensure that new staff feel included and are kept fully informed of all developments.

Training

FinSolutia's philosophy toward employee training is to view delivery as an investment rather than an overhead. The annual training target for staff is 40 hours, in addition to induction training for new starters. Trainees and analysts receive primarily technical servicing training but for managers there is also specific management training.

As staffing numbers have increased over the past 12 months, particularly with the opening of the Madrid office, induction training has had greater focus. The target average number of hours of induction training is between 40 and 60 hours. FinSolutia aims to develop business on the back of a strong corporate identity, and having staff "buy" into this is viewed as critical. About 20 of the induction hours are therefore devoted to communicating corporate strategy and aims. The amount of technical training included in the induction program is determined by the head of the relevant department and is dependent on the experience level of each individual.

Twice yearly, FinSolutia arranges an "offsite" team-building exercise over two days, with all staff attending from both offices. Work-related topics are delivered during the exercise; for example, in the last offsite there was a seminar on the Spanish real estate market. Activities that are not directly work-related have included cycling and surfing, with emphasis on developing teamwork.

In our opinion, the training arranged by FinSolutia is fairly comprehensive considering there is no dedicated training function. We would expect that there may be further enhancements to the company's training programs when the formal HR appointment is made.

Policies and procedures

Since 2007, FinSolutia has been working toward the formal documentation of its policies and procedures. Now that an internal auditor is in place, the appointee has been given the responsibility to review and update all processes, already in a centralized location on the company intranet. The policies and procedures cover master servicing, IT, real estate, and the support departments (which include HR and Financial).

The internal auditor has assumed the responsibility from one of the senior managers for updating documented policies and procedures. All amendments are formally documented for future reference.

Audit

At the time of our visit, FinSolutia had only recently appointed an internal auditor. The individual appears highly experienced and has structured a formal audit plan, which the board has approved. Initial focus has been on reviewing legislative compliance, as the company views this as the highest area of risk.

The audit function will report directly to the board, which in our view should ensure independence from operational areas. It will submit the first report in October 2010.

In 2009, prior to the appointment of the auditor, senior management undertook a gap analysis of various operational areas within the business. We understand that company followed up these findings but that these were minor. In our opinion, this exercise, while useful, was not undertaken with the thoroughness or independence that we would expect of full internal audit activity.

From our discussions with the directors of FinSolutia, we understand that the reason that they have held back from establishing the internal audit discipline was simply down to the size of the business. We propose to monitor the progress that the new internal auditor makes over the coming months.

KPMG undertakes the financial audit of FinSolutia.

Risk/Compliance

Similar to HR and internal audit, risk and compliance management is embedded into FinSolutia's policies and procedures, but due to the size of the company there has been no need to have a dedicated staff resource to deal with this. Part of the new internal auditor's role will be to consider and recommend any changes or enhancements to procedures. Our current ranking reflects our opinion of the current risk management structure.

IT systems

Since it was incorporated, FinSolutia informs us that it has promoted a robust attitude toward the IT systems it uses in support of its servicing activity, considering IT development a core activity, which it believes will give it an important competitive advantage. The core delivery goals of the IT function are: standardization, flexibility, scalability, and control. We understand that systems capacity would allow for growth of up to 200% from current levels.

The IT department now comprises five staff, all located in Lisbon. Four of the team are permanent FinSolutia employees and the fifth has been recruited on a contract basis. The head of the department has been with the company since 2007 and has significant industry experience.

In relation to the number of portfolios for which FinSolutia provides master servicing, the headcount in IT is proportionally higher than we have seen in the majority of other European servicers. FinSolutia has advised us that it proposes to continue its ongoing investment in IT. FinSolutia believes that one of the advantages of being a relatively new and growing company is that it can use the latest technologies, has no legacy, and can tailor IT to respond to operational demands in different geographic locations and asset types in a relatively short time to market.

FinSolutia's software systems are based on Microsoft technology. A "success case study" appears on Microsoft's website highlighting FinSolutia's "best use" of latest technology.

Portfolio Service Manager (PSM), the software which is used to undertake tasks required for master servicing, was introduced in 2009 as an upgrade of the previous system, Risk Manager. In addition to the management and reporting capabilities PSM provides for FinSolutia, it also facilitates external review of loan portfolios by stakeholders and investors.

PSM is supplemented by another software application, Property Manager (PM), which manages collateral at the property level, whether securing performing loans or repossessed assets. PM incorporates geographic detail, property photos, and market data. External interface with PM will be available in the second half of 2010 and will create accessibility for appraisal companies and brokers. FinSolutia believes that this will add value and efficiencies to the collateral management process, as well as mitigating operational risks.

In Spain, FinSolutia has licensed a real estate appraisal management tool (Gestasa), developed by Borsan, to integrate with its own systems. We understand that this system is used by a number of Spanish banks as well as the major appraisal companies. The company believes that the introduction and implementation of this system will leave it well placed to tender for servicing contracts and REO Management.

In addition to PSM and PM, the other key software products FinSolutia employs provide data warehousing/business intelligence and NPL management capabilities.

Systems produce key information on an automated basis, providing management with, for example, data to allow the monitoring of individual workloads, which assists with capacity management and individual employee performance.

FinSolutia uses "Scrum", an agile development methodology, consisting of an incremental process making use of agile software development, on which projects are divided into short work cadences, known as "sprints". At the end of each sprint, all parties involved meet to assess the progress of a project and plan its next steps with all managers represented. This allows a project's direction to be adjusted or reoriented based on completed work to date. All this work is performed upon a Microsoft collaborative platform—MS Team Foundation Server 2008—which manages workloads and communication between the teams. In order to monitor all of the requests, a list was created on the company intranet so that each employee could suggest improvements/new features on the existing applications, which FinSolutia believes promotes collaboration and is beneficial to business needs. We understand that more than 50% of all requests recorded have already been developed and implemented in the applications, and FinSolutia believes that the methodology has resulted in increased productivity in all areas and at all levels of the company.

The IT team holds a daily morning meeting, at which it undertakes a review of any issues arising as well as re-prioritizing/readjusting the tasks for each day of the sprint. The team provides weekly reports to senior management regarding the availability of IT infrastructure.

We understand that the IT system has been externally audited and that all third-party hardware, software, and operating systems remain supported by respective vendors.

Overall, we were able to form the view that the IT platforms that FinSolutia has developed and now uses are an operational asset and should provide it with a useful basis on which to grow the business in line with corporate objectives.

Business continuity/Disaster recovery

There is a formal business continuity (BC) and disaster recovery (DR) plan, which FinSolutia informs us is modeled on industry best-practice guidelines.

The DR plan was last updated in August 2009. We understand that data recovery is tested daily and that on average it takes between one and two hours to restore data. Critical data are backed up every 30 minutes to a backup system in a data center in Lisbon and replicated daily to a site in Madrid.

FinSolutia advises us that systems include antivirus software and that there are mechanisms in place to avoid external or internal intrusion into the systems. The company monitors critical elements of the systems for possible intrusion. There are firewalls in place at appropriate points within the system architecture. There is a defined password policy and access to systems is withdrawn if the user leaves.

FinSolutia stores legal documents as electronic images.

Chart 3 illustrates the data backup and DR plans at FinSolutia.

Chart 3: Data Backup And Disaster Recovery

Backup To Disk Instead Of Backup To Tape
—More efficient and cost-effective
—Easy backup and restore

Transfer To Multiple Locations Daily
—Data center
—Offsite to Madrid (ES)
—FS Office by Lan-Link

Backup Strategy
—Full backup each 12 hours
—Incremental each three hours
—Transaction log each 30 minutes

Recovery Site
—To FinSolutia office (approximately 24 hours)

Fault Tolerance And Security
—Security services delegated to DataCenter experts:
–Load-balancing
–Firewall

There is a formal BC site, which is 2km away from the main offices in Lisbon, providing seats for between eight and 12 employees. We understand that this site operates on a separate power grid. The site has not been tested since August 2008 and in our opinion would benefit from an up-to-date review. About 20 staff have the capacity to work from home. In addition, the establishment of the Madrid office allows for systems continuity, as each office could provide cover for the other if required.

There is no BC insurance.

Our opinion of the BC/DR capabilities of FinSolutia is that they are in line with an AVERAGE ranking.

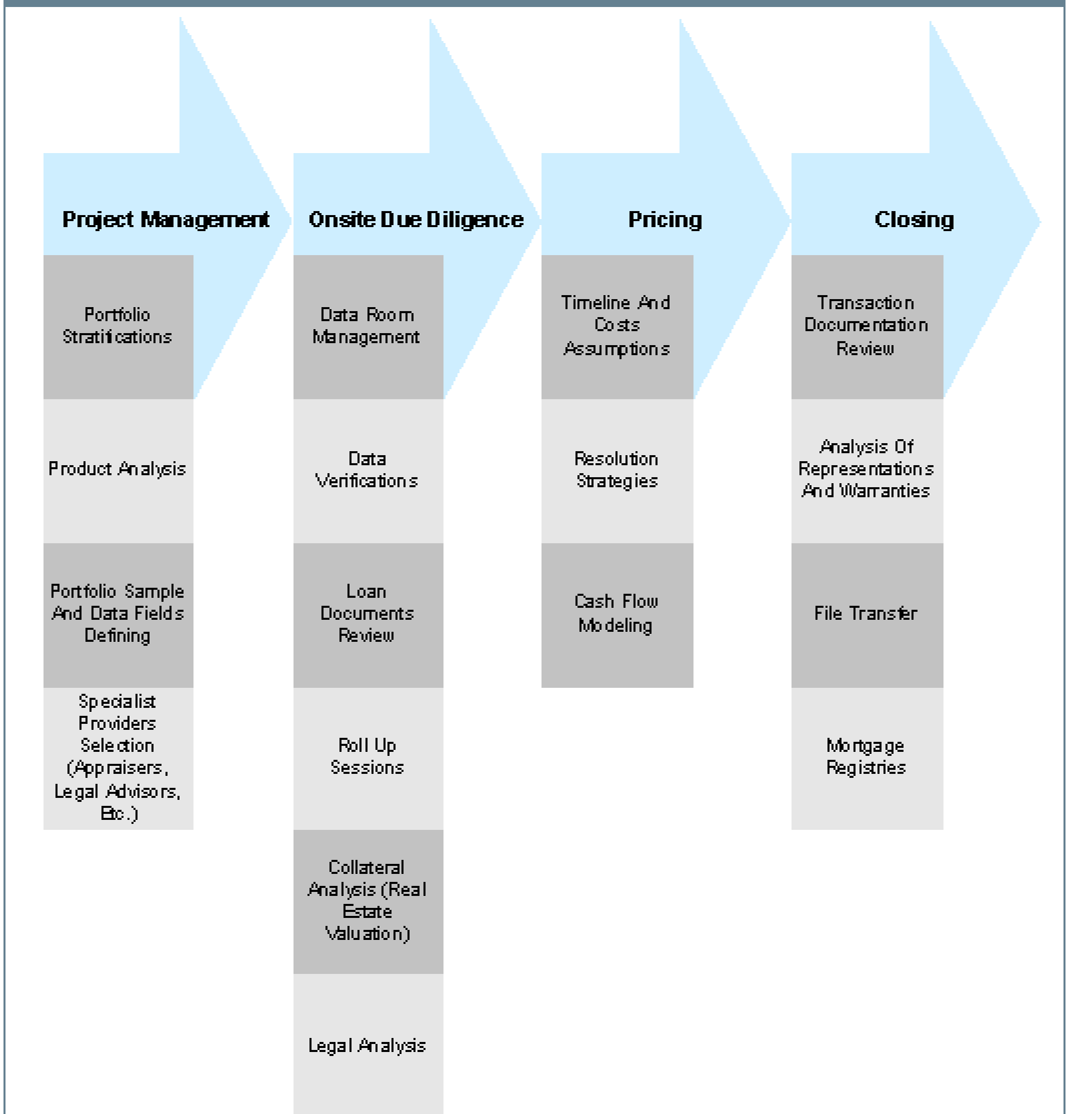
Loan Administration

Our subranking for loan administration on FinSolutia is AVERAGE for the master servicing of residential mortgages in Spain.

Loan boarding

FinSolutia has established a pre- and post-acquisition process through its Advisory Services team, enabling it to provide specialist guidance on portfolio purchase and servicing. Chart 4 illustrates the process. We understand that the data tape analysis stage of the process drives the indicative pricing and establishes the planning phase, leading to higher-level analytics and a better understanding of the portfolio as a whole.

Chart 4:
Pre- and Post-Acquisition Process



FinSolutia has recently boarded two new portfolios onto its systems and we understand that the whole process went smoothly and without any major issues arising.

Master servicing/Mortgage administration

The servicing platform is supported by PSM which, as indicated in the IT section above, FinSolutia developed in mid-2009 as an upgrade of the previous system, Risk Manager. We received a demonstration of PSM and it appears to have good automated workflows and robust controls. Tasks are prioritized depending on perceived risk and then automatically allocated to risk managers. Senior management is able to oversee performance and staff workloads using the management information which the system generates.

We understand that PSM also provides high levels of automation and standardizes the decision outputs for the user. The primary servicer sends detailed files daily which are then migrated to PSM to reconcile the data, highlighting missing or inaccurate information.

Activity is coordinated primarily through the risk management team. The aim of the team is to enhance the performance of portfolios by improving collections, maximizing resolutions, and minimizing losses and costs.

There are currently six staff in the master servicing area. Staff receive specialist training and attend seminars and conferences which are task-relevant. Employee costs have increased since the beginning of 2008 as a consequence of FinSolutia "staffing up", in anticipation of the conversion of some of the new business pipeline. FinSolutia expects these costs to reduce in proportion to income as new portfolios are boarded in future. Staff are being cross-trained so that they can become multi-skilled and we believe there is adequate coverage for workflow peaks, holidays, illness etc.

Table 2 shows the portfolios FinSolutia services and the capacities in which it acts. The company recognizes that further diversity in terms of the type of activity it undertakes would be beneficial and is looking to achieve this through business development.

Table 2

Portfolios

Portfolio	Bond type	Portfolio surveillance	Primary servicer oversight	Reporting	Remittance of funds to investors	Advisory	Proposals service
Portfolio A	RMBS	Yes	Yes	Yes	—	Yes	Yes
Portfolio B	RMBS	Yes	Yes	Yes	—	Yes	Yes
Portfolio C	RMBS	Yes	Yes	Yes	—	Yes	Yes
Portfolio D	RMBS	Yes	—	Yes	—	—	—
Portfolio E	RMBS	Yes	—	Yes	—	—	—

RMBS—Residential mortgage-backed securities.

Table 3 shows the performance of the first three portfolios. Portfolios A and B were boarded in September and December 2007, respectively. Portfolio C was boarded in May 2008. All three are Spanish portfolios. As can be noted, the number of loans and balances in the first three portfolios are showing signs of trending downward. Portfolios D and E (both U.K. portfolios) were boarded in August 2009. Activity on portfolios D and E (shown in table 2 above) is restricted to surveillance and reporting.

Table 3

Performance Of First Three Portfolios

Portfolio	Number of loans at cutoff	Number of active loans	Balance at cutoff (€)	Current balance (€)
A	1,715	1,383	178,803,095.36	157,708,379.52
B	416	354	68,781,932.33	58,138,624.51
C	2,597	2,492	457,706,311.92	430,353,280.40

About 98% of the loans in pools A, B, and C are floating-rate loans either linked to IRPH (Indeces de refencia de prestamos hipotecarios) or EURIBOR (European interbank offered rate). As both IRPH and EURIBOR are relatively low at present, an increase in rates could potentially bring about an uplift in the number of accounts in arrears. We discussed this with FinSolutia. Its systems allow it to simulate such scenarios and it is confident that it can deal with potential higher arrears volumes within current capacity.

In these portfolios, most of the loans which had a loan-to-value (LTV) ratio at origination in excess of 80% have mortgage indemnity guarantee (MIG) coverage and therefore FinSolutia is responsible for overseeing the claims submission by the relevant special servicer when applicable, as well as monitoring claim receivables.

The Spanish loans have performed as FinSolutia had initially anticipated and many loans have moved into the foreclosure process. The foreclosure process usually takes between 10 and 15 months and therefore there is a high proportion still in this phase. Unemployment has increased in Spain, currently reported to be between 20% and 25%, and this has been one of the major drivers of increasing delinquencies, in our view. The performance of the individual loans indicates that there are regional variations across Spain in terms of performance, but the portfolios that FinSolutia services do not show any significant geographical bias toward one particular area.

FinSolutia expects the role of the credit risk manager to be key in achieving resolution strategies for delinquent loans. Resolution strategies include loan restructuring, discounted payoffs, voluntary property sales, or if all else has failed, enforcement/foreclosure. The credit risk managers are required to adopt a hands-on and proactive approach and make rational and considered decisions. The other duties of the credit risk manager include: providing servicer information; reconciliation of weekly and monthly servicer statements, invoices, and bank accounts; reporting; loan oversight/monitoring; and validation of remittance of funds.

As part of its master servicing activity, we have discussed with FinSolutia the oversight that it applies to the primary servicers for the portfolios detailed in table 2 above. Initially, there were monthly site visits to all primary servicers by at least two FinSolutia staff, who undertook an audit of processes and procedures. As time has passed, this has moved to quarterly onsite meetings. Generally, this is more oversight than we normally see for a master servicer.

In addition to this, there is daily testing of data. FinSolutia's automated systems provide alerts if there are errors in data and then this triggers a discussion with the primary servicer. Data are prone to error, so these discussions can be regular. The key area of debate tends to revolve around mismatches on installments versus collections information. FinSolutia has brought this to the primary servicers' attention and advises that there has been some improvement, although the issue is not entirely resolved. FinSolutia will continue to monitor the position.

The continued audit of primary servicers has highlighted a number of issues over time. As an example, since 2008 FinSolutia reports that it has discovered and reported loan breaches of representations and warranties provided by the originator, leading to the successful repurchase of 6.15% of the original pools, representing a net inflow to the transactions of €26.7 million.

It is our view that the company has good systems and processes in place, which are underpinned by experienced staff. We will monitor the addition of further portfolios and will also have additional oversight on FinSolutia's performance, which may enable us to review the AVERAGE ranking.

Client/Investor reporting

Reporting is the responsibility of the risk management team, and the corporate goal is to provide bespoke reporting within a basic template that FinSolutia has devised. Reports are produced monthly or quarterly depending on investors' requirements. The reports are automated from systems and are checked for accuracy and timeliness.

FinSolutia has recently revamped the company website, with the intention of promoting better client communication.

Insurance

FinSolutia arranges its insurance with a broker, Chartis Europe, a subsidiary of a global brokerage entity. We have received copies of corporate insurance as well as administrator's insurance, which are both in force at this time.

Financial Position

We deem the financial position for FinSolutia SUFFICIENT.

Based on the audited 2009 financial statements and business plan provided in the project binder, we consider that there is sufficient financial strength for FinSolutia to continue its servicing operations in the medium term.

Related Criteria And Research

- Standard & Poor's Revises Criteria Methodology For Servicer Risk Assessment, May 28, 2009
- Servicer Evaluation Ranking Criteria: U.S., Sept. 21, 2004
- Structured Finance Sector Report Card: Low Lending Levels Continue To Constrain European Servicers' Portfolio Growth, Nov. 23, 2009
- Select Servicer List, published monthly
- Structured Finance Sector Report Card: European Loan Servicers, published half-yearly

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