

Talmage, LLC

Servicer Report

Ratings^a

Commercial Loan-Level
Special Servicer CLLSS3+

^aThe ratings were affirmed on Jan. 13.

Servicer Summary

Talmage, LLC (Talmage, or the company) is an institutional commercial real estate (CRE) debt manager that has acquired more than \$10 billion of CRE investments since its inception in 2003. The company also provides CRE special servicing and advisory services, with expertise in large loan transactions and collateralized debt obligations (CDOs).

Talmage invests in subordinate debt with control rights that allow it to protect its investment by directing the workout of potentially distressed debt through restructure, modification or extension. The company also invests in CMBS positions throughout the capital stack. The company typically does not foreclose and manage owned CRE given their more active participation in large loan and single-borrower CMBS transactions, where this resolution strategy is less common. However, senior management does have prior REO experience. Third-party special servicing assignments are accepted on a selective basis. Talmage leverages its experience and expertise as a CRE investor in order to more effectively fulfill its duties as a special servicer.

Key Rating Drivers

Company/Management: The two senior managers average 30 years of industry experience and have worked out loans through the most recent and last major recession in the 1990s. Moreover, a large component of the management team has been with the company since its inception in 2003. However, Fitch Ratings notes considerable key man risk, as the company is indirectly owned by its CEO, who is integral to material decisions, including asset resolutions.

Staffing and Training: Servicing personnel are also responsible for other facets of Talmage's business, including investment management and acquisitions. The company historically has experienced minimal turnover; there was one middle management departure in 2016, resulting in 10% aggregate turnover. The company provides ongoing continuing education for its staff, including internally and externally hosted seminars and attendance at industry conferences and forums.

Potential for Conflicts of Interest: As Talmage holds control positions in B-notes, mezzanine debt and CMBS and the employees responsible for special servicing are also responsible for company investments, there is a potential for conflicts of interest in workout decisions. This is somewhat mitigated by the use of net present value (NPV) analyses to determine the highest recovery of alternative resolutions and the practice of hiring of an independent third party to perform an audit of its resolutions.

Procedures and Controls: Talmage uses a team approach, with extensive senior management involvement throughout the workout process. However, the ability to leverage technology to ensure compliance with servicing agreements and policies and procedures is limited. Following the resolution of each special servicing assignment, a senior manager performs an internal audit to ensure compliance with policies and procedures. Talmage also engages a third-party audit firm to perform an independent audit of workouts completed.

Related Research

Fitch Affirms Talmage, LLC's
Commercial Mortgage Servicer Rating
(January 2017)

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Additional Rating Drivers

Defaulted/Nonperforming Loan

Management: Talmage has historically had a small portfolio of loans to manage and workout; however, it has been named special servicer on 20 transactions since becoming a Fitch rated special servicer in 2010.

Company Overview

Talmage is an independently owned, Delaware-limited liability company formed in 2003 to manage, advise and invest in various private equity real estate funds, separate accounts and CRE debt obligations. The company is a CRE special servicer and advisor, with expertise in large loan transactions and CDOs. While Talmage's core business is investment management/advisory, the company's workout expertise and special servicing infrastructure enables it to effectively perform special servicing duties in select situations where it maintains a control position or is hired by a third party with a control position. The company partially mitigates potential conflicts in its role of investor and servicer through policies and procedures, business plans that consider alternate resolution strategies and an objective NPV analysis.

Talmage has over \$1 billion of assets under management through six investment vehicles, one of which is a commercial mortgage-backed CDO transaction. In addition to their legacy portfolio of funds, Talmage has recently deployed approximately \$180 million of capital, which it raised through its Talmage Total Return Partners Fund. Additionally, it successfully raised a second separate account fund for a private investor since Fitch's last review. Controlling interests in debt investments provide Talmage the right to restructure or work out these positions once distressed. Additionally, the company may be appointed as a special servicer for existing transactions on a third-party basis. Talmage was appointed as a third-party CDO manager for a legacy CDO transaction and also has served as third-party advisor for multiple CMBS transactions wherein it reviews the actions of other special servicers. RiverPark Commercial Real Estate Fund is Talmage's smallest investment vehicle to date with only \$50 million in assets under management; however, it is a potential growth area for the company going forward as it was recently converted from a private hedge fund vehicle into a public mutual fund with a focus on CMBS investments including large loan and single-borrower transactions.

Talmage views special servicing as a complementary component to its core asset management and investment services businesses. Since being rated by Fitch in 2010, the

Servicer Ratings

Fitch rates primary and master servicers, which protect the interests of the certificateholders in the trust, by servicing and administering the mortgage loans. The primary servicer is responsible for day-to-day servicing functions, while the master servicer is responsible for monitoring the activities of the primary servicers, investor reporting, and timely remittance of funds to trustees.

Fitch also rates special servicers, which are key to maintaining the credit quality of a pool containing nonperforming commercial mortgages and real estate-owned assets. The special servicer is responsible for working out loans, foreclosing, and liquidating assets.

In assessing and analyzing the capabilities of primary, master, and special servicers, Fitch reviews several key factors, including the management team, organizational structure and operating history, financial condition, information systems, and, with respect to the special servicer, workout and asset disposition experience and strategies.

Fitch rates commercial mortgage primary, master, and special servicers on a scale of 1 to 5, with 1 being the highest rating. Within each of these rating levels, Fitch further differentiates ratings by plus (+) and minus (-) as well as the flat rating.

Related Criteria

[Rating Criteria for U.S. Commercial Mortgage Servicers \(February 2014\)](#)

[Rating Criteria for Structured Finance Servicers \(July 2016\)](#)

Talmage is indirectly and wholly owned by the company's CEO, who leads all aspects of the business, including investing and special servicing. While a succession plan is in place, Fitch considers key man risk significant.

company has been appointed special servicer for 20 transactions, 10 of which have been resolved to date. As of Nov. 30, 2016, the company is named special servicer on 12 loans with a combined balance of \$3.4 billion. All servicing operations are performed from its New York City headquarters.

Servicing Portfolio Overview

	11/30/16	% Change	12/31/15	% Change	12/31/14
Special Servicing – Named					
UPB (\$ Mil.)	3,414	(2)	3,499	6	3,288
No. of Loans	12	20	10	43	7
Special Servicing – Active^a					
UPB (\$ Mil.)	0	(100)	477	32	362
No. of Loans	0	(100)	2	(33)	3

^aIncluding REO.

Financial

Fitch does not maintain a credit rating for Talmage but performed a financial assessment of the company and determined its short-term financial viability adequate to support the servicing platform while noting the small size of the firm and key man risk associated with the company's sole owner. The risks are offset by the company's stable base of assets under management, lack of debt, strong leadership and high degree of financial and operational flexibility.

Talmage has been investing in CRE debt since 2003. Investments include CMBS, whole loans, mezzanine loans, B-notes, CDOs, and bank debt. Special servicing operations are considered complementary to the company's core investment and asset management business.

Talmage is a small company of 10 people that is ultimately owned by Edward L. Shugrue III. Shugrue is a driving force behind most special servicing and asset management strategies employed by the company, and he is in a position to exercise a significant amount of discretion related to fund-raising, investment strategies, compensation, and profit distribution. In the event this individual is not able to oversee operations of the company, a succession plan is in place to enable operations to continue. If Mr. Shugrue were unable to perform his duties, a trustee would work with existing employees to either wind down the company or put in place a structure to enable operations to continue.

Employees

Talmage is one of the smaller Fitch-rated special servicers, with only 10 employees, all of whom are involved in some aspect of special servicing in conjunction with other responsibilities at Talmage. Senior managers have strong CRE, capital markets and asset management experience, averaging 29 years of industry experience, and 13 years of tenure (both senior managers have been with the company since its inception). The four middle managers average 24 years of industry experience and eight years of tenure. The team also has four support staff averaging seven years of experience and five years of tenure.

Employee Statistics

	2016				2015		
	No. of Employees	Average Years Industry Experience	Average Years Tenure	% Turnover	No. of Employees	Average Years Industry Experience	Average Years Tenure
Special Servicing							
Senior Management	2	29	13	0	2	29	12
Middle Management	4	24	8	25	4	30	9
Asset Managers	4	7	5	0	4	6	4
Total	10	—	—	10	10	—	—

N.A. – Not available.

One middle manager left the company voluntarily in the past year resulting in 25% turnover at the middle manager level and 10% aggregate company turnover. One middle manager also departed voluntarily the previous year. Prior to 2013, Talmage had not experienced any turnover since Fitch initiated special servicer ratings in 2010.

Four of the company's 10 employees are considered asset managers; however, workouts are performed using a team approach with all employees involved as needed. Overall, the asset managers average 10 years of industry experience and, given the low number of active specially serviced loans, maintain an assets to asset manager ratio of less than one to one.

Each specially serviced loan is assigned to team members based on working knowledge of the transaction, workload and asset type expertise. A managing director will be assigned to each special servicing team, as well as a mid-level and junior-level employee, to ensure adequate coverage. In addition, outside legal supervision and third-party providers will be engaged to assist in the process. While the senior managers have multiple years of experience in loan workouts during the current economic downturn as well as the earlier real estate recession, the relative small size of the group creates the potential for continuity risk. Fitch believes this risk is partially mitigated by employee cross-training to perform multiple job functions for redundancy, efficiency, and cross-coverage purposes.

Training

Talmage is actively engaged in continuing education opportunities and reported that its special servicing employees averaged 55 hours of instructor-led/web-based training in the past 12 months. Inclusive of conferences and informal training, which is outside of Fitch's criteria, Talmage employees averaged 60 hours of training. Employees attended and participated in CRE credit programs, industry conference calls, and other training opportunities, such as Trepp and Bloomberg proficiency classes as well as law firm-sponsored seminars. Recent seminars have focused on the required steps to a foreclosure, advanced workout strategies, and negotiating with an uncooperative borrower.

Additionally, Talmage hired an experienced chief compliance officer in 2016. Among her duties is to track both the number of hours of training per employee as well as the effectiveness of training efforts.

Operational Infrastructure

Outsourcing

Talmage does not outsource any core special servicing functions or any borrower contact to third parties outside of customary servicing functions such as property management, inspections, and legal counsel.

Vendor Management

Talmage does not maintain a dedicated vendor management group given the limited number of vendors utilized. Managers are responsible for monitoring the various vendors used by Talmage.

Talmage workouts are typically completed using a three-person team, including senior-, middle- and junior-level asset managers. All employees in special servicing have other responsibilities within Talmage, including on the investment side.

Talmage's business continuity plan does not consider an alternate place of operations if its offices cannot be occupied, instead relying on remote access to the network. Fitch considers having an alternate location for operations identified and contracted a best practice.

Talmage uses a proprietary Excel-based application to manage its special servicing portfolio.

Fitch reviewed the policies and procedures manual noting that they are relatively thorough, including sections for REMIC requirements.

Information Technology

Talmage created an internal Excel-based system called Talmage Asset Reporting System (TARS), for monitoring and reporting loan transactions. TARS includes electronic storage of legal documents, financial statements, and remittance reports as well as internal analyses and quarterly reporting. Talmage also uses ARGUS software to re-underwrite and analyze underlying loan collateral in special servicing assignments. The company uses Microsoft SharePoint products and technologies for internal documentation as well as Business Object XI and Crystal reports. Talmage's accounting system of record is Intuit MRI.

Talmage's in-house server environment was moved to a third-party cloud-based environment in 2013. The cloud environment is hosted in a co-location facility that offers a greater level of security against environmental disasters. The cloud environment removes server space and capacity limitations that Talmage could have experienced. Technical support for both the systems and employees is provided by the vendor as well as a 24-hour help desk. On-site issues can be addressed remotely or by an on-site engineer.

Disaster Recovery/Business Continuity Plan

Disaster recovery and business continuity is provided by Eze Castle Integration (ECI), which includes a semiannual disaster recovery test. The most recent test was successfully conducted in September 2016 in conjunction with ECI. The plan is reviewed annually by senior management for needed updates and available to all employees via a shared network.

ECI has redundant power for its disaster recovery facility, which is located on two separate power grids. There are also generators located on-site that can power the facility for five days in the event of an emergency, with scheduled fuel deliveries if any power outage lasts longer than five days.

In the event of an outage or disaster affecting Talmage, mission-critical information would be available within 24 hours and accessible to Talmage employees through their remote access capabilities. All data stored on the Talmage shared computer network are backed up daily to the disaster recovery site located in Massachusetts. All data changes are replicated in real time, so no more than five minutes of data would be lost in the event of a disaster. Additionally, an external hard drive is used to back up files from the on-site file server.

Internal Control Environment

Talmage's control environment is driven by its special servicing policies and procedures that specify all CRE loan resolution strategies be supported by a financial analysis demonstrating that the selected course of action will result in the highest NPV. All resolutions are subject to approval by a special servicing committee that includes the company's CEO, COO, and the asset manager. Upon the conclusion of each special servicing assignment, an internal and external independent third-party review of the resolution process are performed.

Policies and Procedures

Talmage's policies and procedures are formally reviewed annually and updated as necessary throughout the year. The review is performed and approved by members of the senior management team. Updates to the manual are discussed during Talmage's weekly staff meetings and copies of the manual are available to all staff through a shared network drive. The company's new compliance officer is reviewing compliance policies and procedures to make suggestions for enhancements in 2017.

Compliance and Controls

To maintain compliance with its special servicing policies and procedures, the Talmage transaction team reviews the pooling and servicing agreement (PSA) and other relevant loan documents, such as participation agreements and intercreditor agreements. Upon an asset's transfer from the master servicer to the special servicer, the transaction team will engage legal counsel who will prepare memos and detail intercreditor relationships and control rights and will further summarize steps to be taken regarding the PSA to ensure compliance with its terms.

Upon assumption of a special servicing assignment, the special servicing team logs all pertinent information regarding the loan into a manual deal tracker that is updated to reflect all activities related to special servicing an asset. As various resolution options are considered, the analysis and recommendations of the special servicing team are subject to review and approval by the special servicing committee.

Talmage's limited use of technology and other proactive measures to ensure full and timely compliance with applicable servicing agreements is a concern. While the control environment is less robust relative to other servicers, the team approach to asset resolution, with involvement of senior management in the workout process, appears sufficient relative to the limited number of assets being special serviced. Additionally, Talmage maintains a spreadsheet called deal tracker that tracks applicable PSA requirements along with the required timeframes as necessary.

Internal Audit

After each special servicing resolution, Talmage performs both an internal operational review and contracts a third-party firm to assess the actions taken during the workout and documentation against the company's policies and procedures. A senior staff member performs the internal operational review to ensure that the special servicing team complied with the loan documents and Talmage's policies and procedures manual when servicing the loan. Following the review, the senior staff member reviews the results of the assignment and the operational audit with the servicing team. Fitch reviewed several audit samples for recently resolved specially serviced loans and there were no materials findings.

As discussed, Talmage engaged a third-party auditor to perform an operational audit of the special servicing assignment for the two assets resolved in the past year. Fitch reviewed the audit, noting no findings.

External Audits

Talmage, as a registered investment advisor, is subject to the supervision of the SEC and was examined by it as part of its review process.

A Uniform Single Attestation Program (USAP) or Reg AB audit is performed each year by Janover LLC. The annual financial audit was performed by KPMG, which resulted in a clean opinion and no material findings.

Defaulted Loan Management — Special Servicing

Special Servicing Portfolio

As of Nov. 30, 2016, Talmage was the named special servicer on 12 CMBS loans in ten different transactions having an unpaid principal balance (UPB) of \$3.4 billion, of which no loans were in special servicing. Their portfolio of named assignments increased 30% by loan balance since

Fitch believes Talmage's operational review and audit of completed workouts and extensive involvement of senior management in the workout process provide sufficient internal controls given the small volume of loans serviced.

The size of Talmage's named special servicing portfolio relative to its four asset managers allows it to place a greater emphasis on surveillance than most Fitch-rated servicers.

year-end 2015. Talmage resolved two CMBS loan since Fitch's last review. In 2016, the company resolved two loans for third-party clients and is named special servicer for two third-party clients as of Nov. 30, 2016.

Special Servicing Portfolio Overview

	11/30/16	% Change	12/31/15	% Change	12/31/14
CMBS					
No. of Transactions – Special Servicer	10	43	7	40	5
UPB – Named Special Servicer (\$ Mil.)	3,414	6	3,218	9	2,950
No. of Loans – Named Special Servicer	12	33	9	80	5
UPB – Actively Special Servicer (Non-REO) (\$ Mil.)	0	(100)	196	(36)	305
No. of Loans – Actively Special Servicer (Non-REO)	0	(100)	1	(50)	2
UPB – REO Assets (\$ Mil.)	0	—	0	—	0
No. of REO Assets	0	—	0	—	0
Non-CMBS					
UPB – Named Special Servicer (\$ Mil.)	0	(100)	281	(17)	338
No. of Loans – Named Special Servicer	0	(100)	1	(50)	2
UPB – Actively Special Servicing (Non-REO) (\$ Mil.)	0	(100)	281	392	57
No. of Loans – Actively Special Servicing (Non-REO)	0	(100)	1	—	1
UPB – REO Assets (\$ Mil.)	0	—	0	—	—
No. of REO Assets	0	—	0	—	—

Loan Administration

Fitch found Talmage's approach to loan surveillance to be proactive. As part of Talmage's standard investment procedures, an asset summary report is prepared for each investment at the time the investment is made. Asset summary reports are reviewed and supplemented monthly and updated by the Talmage transaction team and submitted to senior management for review and approval. These reports provide a snapshot of any changes and operate as an early warning system.

Team members are assigned a specific list of transactions for which they have primary or secondary responsibility. The assigned asset manager is responsible for maintaining an updated loan file, which includes operating statements, rent rolls, and borrower/sponsor financials. Depending on the size, complexity and time demands of the transactions, an asset manager is expected to have the capacity to manage approximately five assets on average.

Talmage formally reviews all transactions quarterly, obtaining, and analyzing financial information on a monthly and/or quarterly basis. Through the review of this data as well as contact with the borrower/sponsor, servicers, and other interested parties, Talmage obtains a comprehensive picture of factors that may affect the transactions. The asset manager follows up with the master servicer and/or borrower if questions arise. All loans of concern are placed on the company's watchlist.

Loan Workout/Resolution

Once a special servicing transfer event has taken place, Talmage communicates with the master servicer for a smooth, effective transition. Before contacting the borrower, Talmage obtains the complete loan file, conducts a document inventory, and confirms the circumstances of the loan default. Upon transfer, the special servicing team is assigned and the loan is recorded in a deal tracker log to identify the events leading to the transfer as well as all other material events that occur until a resolution has been reached.

The special servicing committee, inclusive of the company CEO, COO and asset manager, meet no less than once per week and as often as necessary to review each loan in special servicing.

The asset manager prepares a business plan within 30 business days of a loan being transferred into special servicing. This plan is reviewed and approved by the special servicing committee. The business plan is the formal working document that dictates the process while the loan is in special servicing. Fitch reviewed the business plan for the loans resolved in the past year and noted that they included an overview of the status of the asset, including the cause precipitating the transfer, property description, the loans' financial performance to date, borrower and guarantor description, summary of third-party reports and the NPV analysis, proposed resolution strategy, and immediate actions that would need to be taken. A record of the steps taken in the workout is tracked in TARS with a reference to the PSA provision that supports the action.

Talmage performs market research using a variety of publications and commercially available market reports. Additionally, Talmage leverages its relationships with owners, lenders, brokers and appraisers to assist in the collection and evaluation of market- and property-level information. Talmage also reviews its existing transactions to gain an understanding of a particular market. A member of the special servicing team will arrange for a site visit accompanied by the property manager and obtain appropriate third-party reports.

Upon initial loan underwriting, Talmage vets the sponsor and any guarantors using Lexis/Nexis, credit checks and internet searches. Upon a loan being assigned to special servicing, a comprehensive new search is conducted. Where possible, updated financial statements of borrower parties are requested and reviewed.

Site inspections for CMBS loans are performed based on PSA requirements. Arrangements for the transaction team members to be accompanied by a property manager and leasing agent (if applicable) are made for a walk-through of the property. The inspector is responsible for verifying tenants in occupancy and inspection of the mechanicals, roof, among other property details, visiting comparables, compiling photos and meeting with owners, managers, brokers, and agents in the local market.

Talmage holds controlling class CMBS positions and invests in controlling B-note and mezzanine loans. With members of the special servicing committee also responsible for investment decisions, Talmage is subject to potential conflicts of interest. This potential for conflict is partially mitigated through the required use of an NPV analysis to determine the highest recovery of alternate resolutions and the engagement of a third-party audit firm to assess the actions taken during the workout.

REO Management

Talmage does not maintain a separate REO group given the small size of its named and active special servicing portfolio. If Talmage determines that a foreclosure would be the best course of action and a property becomes an REO asset, Talmage would hire third-party asset managers to manage the day-to-day property operations. Prior to acquisition, the asset manager would recommend a property manager to the special servicing committee for approval. The property manager would then prepare a 90-day budget typically within 10 days of acquisition and submit the annual budget typically within 90 days of acquisition. On a monthly basis, the property manager will prepare property operating reports and submit them to the asset manager. The goal of the asset manager would be to maximize the value of the property, manage operating expenses and, relative to the highest NPV, take all necessary actions to optimize the sale price.

Governance and Conflicts of Interest

Managing Conflicts of Interest

Potential conflicts of interest in special servicing arise through various forms, particularly as investors retaining controlling positions in securitizations or specific loans have influence on workout strategies and the ability to select the special servicer.

Talmage has not taken back any REO properties since Fitch initiated coverage of the company as a special servicer.

As a smaller investment manager and servicer, there is no separation between employees participating in investment activities and special servicing asset management. Talmage is an active investor and manager of CRE debt investments on behalf of its funds and separate accounts and is subject to the fiduciary responsibilities of an investment advisor. The company is an investor in CMBS loans, for which it may purchase whole loans or pieces of loans, granting Talmage the ability to appoint itself special servicer, which it has done on three occasions in the past year.

The company stated that it takes the perception of inherent potential conflicts in its role as special servicer very seriously and addresses them through policies and procedures, business plans that consider alternate resolution strategies and an NPV analysis. Fitch found the business plan for the loan resolved in the past year to be complete and contained a summary of the NPV analysis of alternate resolution strategies.

Talmage also has a documented code of ethics and conflicts of interest policies to mitigate the potential for conflicts. The company's code of ethics policy stipulates a code of conduct for all employees, including fiduciary responsibility to avoid actual and apparent conflicts of interest with clients of Talmage. The code of ethics is circulated at least annually to all Talmage employees and each employee must certify in writing that he or she has received and followed the code and any amendments thereto.

Affiliated Companies

Talmage does not provide real estate management or broker services.

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